

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

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| IN RE: |) | Chapter 11 |
| |) | |
| UAL CORPORATION, <i>et al.</i> , |) | Case No. 02-B-48191 |
| |) | (Jointly Administered) |
| |) | |
| Debtors. |) | Honorable Eugene R. Wedoff |
| |) | |
| |) | |
| |) | Hearing Date: January 18, 2006 |
| |) | Hearing Time: 10:30 am |
| |) | Objection Deadline: December 12, 2005 |

**TRUSTEES' REPLY IN SUPPORT OF (A) TRUSTEES OBJECTION TO CONFIRMATION
OF DEBTORS' PLAN OF REORGANIZATION BASED ON MATERIAL POST-BALLOTING
CHANGES TO THE PLAN AND (B) EMERGENCY PROVISIONAL
MOTION OF TRUSTEES PURSUANT TO RULE 3018 TO ALLOW HOLDERS
OF CLASS 2E-5 CLAIMS TO CHANGE VOTES RELATING TO DEBTORS'
FIRST AMENDED PLAN OF REORGANIZATION¹**

(Relates to Dkt. Nos. 13277, 14635, 14684, 14699, 14701, 14758 and 14774)

INTRODUCTION

The Trustees submit that the Debtors' Response [Dkt. No. 14758] confuses the limited discretion Debtors had to provide a portion of the Unassigned UBL Claim to one or more stakeholders on a rational basis for the benefit of all unsecured creditors with an unfettered right to arbitrarily discriminate against one disfavored group of creditors -- the Public Debt Holders -- for the sake of getting their Plan confirmed. Unless Debtors had the right to arbitrarily

¹ The Trustees were served with the Committee's Response [Dkt. No. 14774] at approximately 9:30 p.m., January 17, 2006. As it is substantially duplicative with the Debtors' Response, it is not separately addressed herein. Nor does this Reply attempt to address every argument made by the Debtors. The Trustees respectfully reserve the right to address any argument made by the Debtors or the Committee at oral argument, whether or not addressed herein, to the extent deemed necessary or appropriate by the Court. Unless expressly indicated otherwise herein, capitalized terms shall have the same meaning as provided in the Trustees' Objection [Dkt. No. 14699] and the Trustees' Motion to ReVote [Docket No. 14701].

discriminate -- *i.e.*, absolute discretion -- with respect to the Unassigned UBL Claim, and such right was adequately disclosed in the Disclosure Statement and First Amended Plan of Reorganization, Debtors' entire argument falls apart.²

The Debtors' Response attempts to justify an arbitrary and discriminatory allocation of estate assets, which even Debtors concede is attributable to the Committee's displeasure with the Public Debt Group. (Resp. at 6 n.9 (noting the Committee's "oft-expressed displeasure with the Debtors' negotiations with the Public Debt Group").) The Response is flawed in at least the following critical particulars:

1. Contrary to Debtors' argument in Response, distribution of the UBL Claim is a "Plan Issue";
2. As more fully set forth below, the First Amended Disclosure Statement did not provide adequate notice that the allowed, general unsecured claims of the Public Debt Group would not be treated *pari passu* with all other allowed, general unsecured claims;
3. The proposed distribution to all unsecured creditors except the Public Debt Holders is discriminatory:

The treatment is disparate. Debtors' argument that increasing the size of all other unsecured claimants claims and then providing recovery on those enlarged claims is "the same recovery" as provided to the Public Debt Group because the same "percentage of recovery" is then applied to the enlarged claims as to the Public Debt unenlarged claims is simply disingenuous.

4. The discriminatory treatment is arbitrary and unjustified:

The Debtors response argues that disparate treatment is not discriminatory because the Public Debt Holders have the "different attribute" of having received an assignment from the UBL Claim. This argument conveniently ignores the following facts well known to Debtors:

² Tellingly, Debtors complain that "It is inappropriate for the Trustees to 'wait and see what they would get'" under the Plan, and then complain about their treatment under the Plan. (Resp. at 20.) But, this is what adequate disclosure under § 1125 is all about. The Trustees should not have had to "wait and see," what they would get under the Plan. It should have been adequately disclosed in the Disclosure Statement for the First Amended Plan. As discussed below, it was not. Accordingly, if the Court somehow finds that the Debtors have the unfettered right to arbitrarily discriminate against the Public Debt Holders -- or other creditors -- resolicitation is required. If Debtors do not have such a right, the Plan cannot be confirmed. 11 U.S.C. § 1123(a).

unlike the proposed assignment, the prior agreed assignment of a portion of the UBL Claim to the Public Debt Group was in satisfaction of administrative claims;

the compromise and resolution of those administrative claims inured to the benefit of all unsecured creditors and the estates; there is no similar trickle down benefit from the Debtors' discriminatory distribution;

there is not an identity of claimants between those Public Debt Holders who received benefit from the prior assignment in satisfaction of administrative claims and those who hold the allowed, general unsecured claims that are to be discriminated against (e.g., the EETC Transactions received no benefit of the UBL Claim assignment and compromised their claims in these cases for allowed, general unsecured claims);

United asked the Public Debt Holders to compromise their right to cash in satisfaction of their administrative claims, so that United might conserve its cash;

The Chicago Municipal Bond holders also received a prior UBL Claim assignment, but are not to be discriminated against in the Debtors' proposed amendment

5. The First Amended Disclosure Statement did not provide adequate notice that the Debtors and the Committee might seek to arbitrarily discriminate against the Public Debt Group; and even if it did, the Plan was materially changed when the Debtors and Committee actually took steps to do so;

The protocols and safeguards built into the PBGC Settlement, and as set forth in the First Amended Disclosure Statement, entitled the unsecured creditors to vote with the understanding that their interests would be protected by the safeguards and the Committee's fiduciary role to all unsecured creditors as gatekeeper of further distributions;

The Debtors and the Committee ignored or attempted an end run around the safeguards built into the PBGC Settlement.

6. Debtors ignore their duty to preserve and maximize the contractual right to assign the UBL Claim -- an estate asset -- for the benefit of all unsecured creditors.

ARGUMENT

Debtors argue that this is not a “Plan Issue.”³ (Resp. at *passim*.) This is patently false. The Debtors’ agreement with the Committee leading to withdrawal of the Committee’s objection to confirmation (the “*Confirmation Agreement*”) expressly required that the Plan be modified to reflect the unfairly discriminatory spread of the Unassigned UBL Claims. (See Dkt. No. 14635.) Indeed, it was expressly labeled as a “Plan Issue” in the Confirmation Agreement. (See *Id.* at Ex. A.) The Second Amended Plan of Reorganization incorporated the UBL Claim assignment provision in keeping with the Confirmation Agreement. (Dkt. No. 14715 at 90-91.) The question of Debtors’ right to arbitrarily discriminate against the Public Debt Holders is nothing if not a “Plan Issue.” Indeed, even if Debtors and the Committee had attempted to implement the UBL-assignment provision outside of the Plan, it would be a “Plan Issue.” See, e.g., *In re CGE Shattuck, LLC*, 254 B.R. 5, 11 (Bankr. N.H. 2000):

While NCC claims that the NCC Commitment is not a plan, as was noted above, the economic substance and effect of the NCC Commitment would be to sanction a distribution scheme that discriminates between creditors in the same class. Such discrimination would not be allowed under a plan of reorganization by virtue of the provisions of 11 U.S.C. § 1123(a)(4) and the holding of *Granada Wines* [748 F.2d 42 (1st Cir. 1984)].

Debtors argue that the Confirmation Agreement did not change the Plan, or did not materially change the Plan, because Disclosure Statement adequately disclosed the Debtors’ purported right to “selective parceling out of value.” (Resp. *passim*.) This cannot be reconciled with the language of the Disclosure Statement or the PBGC Settlement. In the Disclosure Statement and in the PBGC Settlement, Debtors “right” to make “selective assignment” of the

³ Debtors argue “Because the Trustees’ objection is based on the false premise that the PBGC assignment is a Plan issue, every argument flowing from this premise is tainted.” (Resp. at 2.) Yet, as Debtors note themselves, in the Confirmation Agreement, the UBL Claim assignment provision is found under the heading “Plan Issues.” (See Dkt. No. 14635 at Ex. A; see also Resp. at 4 n.6.) It appears that Debtors’ view that assignment of the Unassigned UBL Claim is not a “Plan Issue” is of recent construct.

Unassigned UBL Claim was expressly subject to compliance with the Bankruptcy Code, for the good of the unsecured creditor body after notice and consultation with the Unsecured Creditors Committee -- the fiduciary for all general unsecured creditors, and notice and hearing: substantial due process.⁴ It is tortured sophistry to suggest that the foregoing conditions on further distributions of the Unassigned UBL Claim provided adequate disclosure to the general unsecured creditors with allowed claims, including the Public Debt Holders, that Debtors had, or claimed, the right to arbitrarily exclude one or more groups of similarly situated creditors.⁵ Nor is the idea that the Debtors and the Committee could conspire to deprive the Public Debt Holders of what they had truly bargained for, *pari passu* treatment with all other allowed, general unsecured claims for their general unsecured claims anywhere expressed or even suggested in the language of the PBGC Settlement or the Disclosure Statement. Nor does the concept that the Debtors and the Committee acting together had unfettered discretion to assign the Unassigned UBL Claim appear. Rather, the PBGC Settlement and the Disclosure Statement expressly provided that any distribution would be for the good of the creditor body -- with the implication that it would be for the good of the creditor body as a whole, particularly in light of the safeguard provisions and the Committee's role in safeguarding the distributions for all unsecured creditors, consistent with its fiduciary duty to all unsecured creditors. If Debtors, or Debtors and the Committee acting together, have the right to arbitrarily discriminate against one or more creditor groups, it is inadequately disclosed in the Disclosure Statement and resolicitation is required.⁶

⁴ Among other things, Debtors and the Committee did not comply with the 10 business day-notice requirement. Debtors seek to measure 10 business days to the Effective Date. (Resp. at 4 n.7.) But, if the Plan is confirmed on January 18 or 19, the issue will be a *fait accompli* on that date, less than the 10 business days notice required by the PBGC Settlement. Debtors also argue that the hearing required by the PBGC safeguard provision is satisfied by "discussion" at the confirmation hearing. (*Id.*) This is inconsistent with the plain language of the PBGC provision.

⁵ Debtors' argument that the exclusion of the Public Debt Holders is not arbitrary or discriminatory because the Public Debt Holders otherwise received a distribution of the UBL Claim in satisfaction of certain administrative claims is debunked below.

⁶ Nor, does the "Committee's Disclosure" which noted that the Committee requested additional distributions to some, but not all, other creditors, provide adequate disclosure that Debtors and the Committee might seek to arbitrarily assign the Unassigned UBL Claim in an unfairly discriminatory manner. (*See* Resp. at 5-

Footnote continued.

Debtors argument that the Confirmation Agreement is good for the creditor body as a whole because it will advance the goal of confirmation (*see* Resp. at 12) proves too much. By this standard Debtors could justify any settlement favoring one group of creditors over another because it advances confirmation. Section 1123(a)(4) prohibits a plan that provides for discrimination in treatment of claims or interest in a particular class -- absent that class' consent.

Debtors argue “first” that discrimination only becomes an issue in a § 1129(b) cramdown. (Resp. at 15.) Debtors inexplicably ignore § 1123(a)(4) (. . . “a plan shall . . . provide the same treatment for each claim or interest of a particular class, unless the holder of a particular interest agrees to less favorable treatment of such particular claim or interest”); *see also In re CGE Shattuck, supra*. Moreover, this has little to do with the Public Debt Holders’ right to resolicitation based on the inadequate disclosure of Debtors’ unfair, discriminatory allocation of the UBL Claim -- even if Debtors had such a right to discriminate.

Even the cram down context, Debtors’ argument must fail. *See, e.g., In re 203 N. LaSalle Street Limited Partnership*, 190 B.R. 567 (Bankr. N.D. Ill. 1995); *aff’d* 195 B.R. 692 (N.D.Ill. 1996); *aff’d* 126 F.3d 955 (7th Cir. 1997); *rev’d on other grounds sub nom Bank of America Nat’l Trust and Sav. Ass’n v. 203 North LaSalle St. P’ship*, 119 S.Ct. 1411 (1999):

First, any discrimination must be supported by a legally acceptable rationale. . . Second, the extent of the discrimination must be necessary in light of the rationale.

Debtors do not attempt to meet this test. Instead, Debtors argue that there is no discrimination because “[s]imilarly situated creditors are receiving the exact same percentage recovery for the claims they hold, either directly or by assignment of a portion of the PBGC

6.) The “Committee’s Disclosure” suggested the Committee might request that a large number of general unsecured creditors be excluded (e.g., Classes 1D, 1E-1, 1E-2, 2D-1, 2D-2, 2E-1, 2E-2, 2E-4, 3E-1, 3E-2 and Employee Distributions) -- not just one. The creditors, however, including the Public Debt Holders, were entitled to expect that any such request would only be made by the Committee to the extent it was consistent with the Committee’s fiduciary duty to all unsecured creditors and complied with the safeguard provisions of the PBGC Settlement, as set forth in the Disclosure Statement.

Claim.” (Resp. at 15.) “Equal “recovery” after some special, discriminatory treatment that enlarges some claimants’ claims then provides for “equal” recovery on those enlarged claims -- as proposed by Debtors’ Plan -- is not equal or non-discriminatory treatment. To suggest that such mathematical legerdemain is equal treatment of holders of similarly situated claim because of “equal recovery percentages” on differently treated claims is simply disingenuous.⁷

The Debtors next suggest that the exclusion solely of the Public Debt Group is not unfairly discriminatory because the Public Debt Group “got theirs” (Resp. at 9 n.16 and 17-18) and/or that the Public Debt Group somehow agreed to an “implicit cap” on distributions from the UBL Claim. (Resp. at 7 n. 12 and 9.) These arguments do not hold up well under scrutiny.

The Public Debt Group cannot be discriminated against on this basis. The discretion of the proponent of plan of reorganization to classify claims and interests according to facts and circumstances of case is not unlimited; thus, if the plan unfairly creates too many or too few classes, if classifications are designed to manipulate class voting, or if classification scheme violates basic priority rights, the plan cannot be confirmed. *In re Holywell Corp.*, 913 F.2d 873 (11th Cir. 1990). Among factors that bankruptcy courts consider in deciding whether a debtor should be allowed to separately classify similar claims are whether discrimination is reasonably based, whether debtor can reorganize without such discrimination, whether discrimination is fair and proposed in good faith or necessary only to create impaired consenting class, and whether degree of discrimination is directly related to rationale for disparate treatment. *In re Tucson Properties Corp.*, 193 B.R. 292 (Bankr. D.Ariz. 1995). Plan proponents cannot create separate

⁷ Debtors weakly argue that “Even if Debtors had to cram down the Trustees’ class, there is no discrimination here, let alone unfair discrimination, because by the Assignment United is merely taking an action that it was allowed to do by the PBGC Agreement.” (Resp. at 20.) It is axiomatic that just because one has a right to do something does not make the discriminatory exercise of that right non-discriminatory. An employer in an “at will” state may hire or fire a person “for any reason or no reason at all,” but not for discriminatory reasons based on race, creed, color or other protected classes. The right to do something does not by itself make the doing non-discriminatory. Debtors in bankruptcy are required to manage existing estate assets for the benefit of all unsecured creditors. If the Debtors sold or used the UBL Claim to pay secured or administrative claims, the value of not paying cash inures to all unsecured creditors. That is the “best interest” of all unsecured creditors.

“classes” of similarly situated creditors. *In re Roswell-Hannover Joint Venture*, 149 B.R. 1014 (Bankr. N.D. Ga.1992). *In re Barnes*, 13 B.R. 997 (D.D.C.1981) (existence of co-borrower was not valid reason to create separate “class”); *In re Boston Post Road Ltd. Partnership*, 21 F.3d 477 (2d Cir. 1994) (Separate classification of unsecured claims solely to create impaired assenting class for purposes of cramdown will not be permitted; instead, debtor must adduce credible proof of legitimate reason for separate classification of similar claims).

The Debtors argue that the Public Debt Holders have the “different attribute” of having received an assignment from the UBL Claim. (Resp. at 9 n.16 (claiming “Mikado Dilemma”)and 17-18 (claiming distinguishing characteristic of Class 2E-5 is “that it is already the beneficiary of an assignment from the PBGC Claim”).) As Debtors are well aware, but fail to address, the UBL Claim was assigned not to resolve general, unsecured claims, but to resolve certain administrative claims. (*See* Resp. at 7 n.12 (“In consideration for the settlement and release of all PDG administrative claims, the Debtors agreed to direct assignment of a portion of [the UBL Claim]”; *see also* Term Sheets at II.B. and V.C. “Aggregate Supplemental Payment” which consisted of \$65 million cash and “Conveyance Claims” (assignment of UBL Claim) was in resolution of administrative claims for rejected aircraft and certain other aircraft).)

Debtors cannot realistically compare the UBL Claim distribution to the Public Debt Group in satisfaction of administrative claims to the proposed arbitrary, discriminatory distribution to all holders of allowed, general unsecured claims except the Public Debt Group because:

the compromise and resolution of the Public Debt Group’s administrative claims inured to the benefit of all unsecured creditors and the estates generally; there is no similar “trickle down” benefit from the Confirmation Agreement;⁸

⁸ Indeed, if the proposed distribution were in the interest of resolving some other claims -- other than the same class of allowed, general unsecured claims held by the Class 2E-5 claimants -- it would be consistent with the purpose of the PBGC Settlement safeguard provisions, so long as it was shown to be in the best interest of the unsecured creditor body. This is what sets the prior-agreed distribution to the Public Debt Holders apart from the proposed distribution to all general unsecured creditors except the Public Debt Holders.

United asked the Public Debt Group to take the UBL Claims in lieu of cash, because United wanted to conserve cash;

the allowed, general unsecured claims accepted by the Public Debt Holders were for separate and distinguishable claims from the administrative claims resolved by the prior acceptance of a distribution from the UBL Claim; and

the unsecured Chicago Municipal Bond Claim (Class 2E-4) is designated to receive an assignment of the Unassigned UBL Claim under the Confirmation Agreement, even though it also received a prior assignment of upto \$35 million of the UBL Claim in settlement of certain of its claims.

Accordingly, the Public Debt Holders' prior acceptance of a distribution from the UBL Claim in satisfaction of administrative claims cannot color or bar the Public Debt Holders' right to fair and equal treatment of their allowed, general unsecured claims.

Finally, the Debtors attempt to suggest that in accepting the UBL Claim distribution in satisfaction of their administrative claims, the Public Debt Group somehow "implicitly" agreed to a cap on their distribution from the UBL Claim for all other purposes, including on their general, unsecured claim. (Resp. at 7 n.9 and 9.) There is no rational basis for this suggestion. As noted above, there is not an identity of interests between the administrative claims and the general unsecured claims. Moreover, the PBGC Settlement and the Disclosure Statement each were written in a manner to lead the rational reader to believe that any further distributions would be for the benefit of the unsecured creditor body as whole -- particularly in light of the requirements of § 1123(a)(4) and the Committee's fiduciary role as gatekeeper of further distributions (or, more likely than not, that the UBL Claim would go to the unsecured creditor body, as provided for in the default provision). Accordingly, there was no reason for the Public Debt Holders to believe by accepting a limitation on the UBL Claim recovery for their administrative claims they had somehow agreed to a "cap" on any further distribution in satisfaction or compromise of their allowed, general unsecured claims. There is no evidence or rational basis for the Court to conclude that the Trustees agreed expressly or implicitly to any cap on UBL Claim distributions in satisfaction of their allowed, general unsecured claim -- other than to agree that some part of the UBL Claim might be distributed to others for the general benefit of the general unsecured creditor body.

To the extent that Debtors or the Committee dispute the foregoing, an evidentiary hearing should be required to resolve any relevant factual questions, but the Trustees believe the foregoing is factually undisputed.

Finally, like the change in distribution scheme, Debtors' argue that the disclosure of "flexibility" in naming of Board Members allowed Debtors to significantly expand the role of the Committee in post-confirmation operations without requiring resolicitation. In view of the recent events, the Public Debt Holders have the right to resolicitation or to change their votes based on the materially expanded role of the Committee in the post-confirmation management of the Debtors. *See e.g. In re Frontier Airlines, Inc.*, 93 B.R. 1014, 1023 (Bankr.D.Colo. 1988); *In re MCorp Financial, Inc.*, 137 B.R. 237, 238 (Bankr.S.D.Tex. 1992).

Because the Disclosure Statement did not adequately disclose Debtors' plan or claim of right to discriminate against the Public Debt Holders in the treatment of the Public Debt Holders' allowed, general unsecured claims, or the Committee's expanded role in Debtors' post-confirmation operations, resolicitation is required, or at the very least, good cause is shown for allowing the Trustees leave to resolicit the Public Debt Holders, and as appropriate change their votes under Rule 3018. In addition, if the Plan is confirmed over the Public Debt Holders' objection, it should be confirmed without binding the Public Debt Holders to any release of the Committee.

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**THE BANK OF NEW YORK AS TRUSTEE AND
COLLATERAL AGENT**

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