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

In re MPM Silicones, LLC, et al.,¹ Debtors.))))))	Chapter 11 Case No. 14-22503 (RDD) Jointly Administered
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TRIAL BRIEF OF BOKF, N.A., AS INDENTURE TRUSTEE

¹ The last four digits of the taxpayer identification numbers of the Debtors follow in parentheses: (i) Juniper Bond Holdings I LLC (9631); (ii) Juniper Bond Holdings II LLC (9692); (iii) Juniper Bond Holdings III LLC (9765); (iv) Juniper Bond Holdings IV LLC (9836); (v) Momentive Performance Materials China SPV Inc. (8469); (vi) Momentive Performance Materials Holdings Inc. (8246); (vii) Momentive Performance Materials Inc. (8297); (viii) Momentive Performance Materials Quartz, Inc. (9929); (ix) Momentive Performance Materials South America Inc. (4895); (x) Momentive Performance Materials USA Inc. (8388); (xi) Momentive Performance Materials Worldwide Inc. (8357); and (xii) MPM Silicones, LLC (5481). The Debtors' executive headquarters are located at 260 Hudson River Road, Waterford, NY 12188.

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PRELIMINARY STATEMENT

The Second Circuit's opinion remanding this case identified two issues for determination: (1) whether the market for exit financing available to Momentive on October 24, 2014, the date Momentive's plan (the "Plan") went effective (the "Effective Date"), was efficient and, if so, (2) what the market rate of interest for the first lien notes ("Replacement First Lien Notes" or "Notes") and 1.5 lien notes (the "Replacement 1.5 Lien Notes"; together with the Replacement First Lien Notes, the "Replacement Notes") issued under the Plan was. *In re MPM Silicones, L.L.C.*, 874 F.3d 787, 800-801 (2d Cir. 2017).

As BOKF, N.A. ("BOKF" or "First Lien Trustee") will show at trial, the market for exit financing on the Effective Date was efficient, and the market rate of interest for the Notes was at least between 6.47% and 6.99% per annum. In addition, BOKF will show that the "catch-up" payment that is due to the holders of the Replacement First Lien Notes (the "Noteholders") at those rates (as of August 22, 2018) is \$121.7 million and \$147.5 million, respectively.

First, the market was efficient. As discussed more fully in BOKF's motion in limine (ECF 1644), the Second Circuit explained that "markets for financing are 'efficient'" where they "offer a loan with a term, size, and collateral comparable to the forced loan contemplated under the cramdown plan," which "generates an interest rate that is apparently acceptable to sophisticated parties dealing at arms-length." *MPM Silicones*, 874 F.3d at 800-01. That test is met here because (1) Momentive secured commitments for exit financing (the "Exit Term Loan"), in an arm's length transaction with three of the leveraged loan market's largest competitors, that had a term, size and collateral comparable to the Replacement First Lien Notes, and (2) even if Momentive had not obtained such commitments, the markets for this type of financing were highly active when Momentive emerged from bankruptcy.

Even if the Court does not exclude Momentive's expert, Professor David Smith, for applying the incorrect legal standard of market efficiency, BOKF will show that his opinion is fundamentally flawed and unreliable. Professor Smith's opinion boils down to the remarkable proposition that, because Momentive gratuitously crammed down the Notes with an "off-market" term (no call protection) that increased the risk to the Noteholders, the market was inefficient and therefore the formula rate of 3.88% should apply, resulting in a *lower*, not higher, interest rate.

Second, as BOKF's expert, Professor Bradford Cornell, will show, the market rate for the Replacement First Lien Notes was at least between 6.47% and 6.99%. By contrast, the opinion of Momentive's expert, William Q. Derrough, that the market rate was between 5.5% and 5.7% (or even lower if the Court were to require a floating rate, notwithstanding that the Plan specified a fixed rate, as is standard in the high-yield bond market) is deeply flawed and unreliable.

The principal difference between the parties derives from their starting point. In ascertaining the interest rate that the market would require for making a loan comparable to the Replacement First Lien Notes, Professor Cornell determined that the best indication of that rate was the actual market transaction that Momentive itself entered into with independent lenders for exit financing—the Exit Term Loan. Given this record, Professor Cornell's approach was straightforward: he simply converted the floating rate on the Exit Term Loan to a fixed rate under the standard methodology for doing so to arrive at his concluded range of between 6.47% and 6.99%. Moreover, Professor Cornell was conservative. For example, while he noted that the Replacement First Lien Notes lacked several of the lender-protective terms of the Exit Term Loan—such as call protection, amortization, and a default rate of interest—that made the Notes riskier for the Noteholders, he did not increase his range of 6.47% to 6.99%, instead noting only that, if anything, the market rate was *at least* between 6.47% to 6.99%.

Mr. Derrough, on the other hand, gave little, if any, weight to the Exit Term Loan. Instead, he derived an interest rate primarily by looking at the interest rates implied by the trading prices of debt issued by other purportedly “comparable” companies; although, as he admits, none were truly “comparable” to Momentive and the Replacement First Lien Notes. Even if the trading prices of debt securities could properly be afforded such great weight—and this Court appeared to question that proposition at the March 9, 2018 status conference—Mr. Derrough disregards the market evidence that is most assuredly the best “comparable” of all: *Momentive and its own first-lien debt*. Mr. Derrough ignores not only the Exit Term Loan, but in looking to bond trading prices, he also ignores the trading prices of Momentive’s first-lien bonds around the Effective Date—both the Original First Lien Notes, which continued to trade after this Court announced its decision confirming the Plan on August 26, 2014, and the Replacement First Lien Notes. Both evidence that the market rate was significantly higher than Mr. Derrough’s range (and, instead, was consistent with Professor Cornell’s range, although he did not give primary weight to trading prices in his analysis). Instead, Mr. Derrough gave primary weight to a handful of “comparable” companies that, by his own admission, are anything but, including investment-grade debt that bears no resemblance to the high-yield Replacement Notes.

Third, the catch-up payment that Momentive owes the Noteholders if the Court determines that the market rate is between 6.47% and 6.99% is \$121.7 million and \$147.5 million, respectively (as of August 22, 2018). The only disagreement between the parties (other than the underlying market rate) is whether that calculation should include compound interest (as BOKF’s calculation does, but Momentive’s does not). As discussed below, both the indenture and basic economic principles require the payment of compound interest to make the Noteholders whole.

This brief addresses each point in greater detail below. Rather than set out a separate statement of facts, the brief discusses the facts and evidence as they are relevant to each issue.

ARGUMENT

The weight of authority provides that the burden of proof on § 1129(b) issues, like all confirmation issues, rests on Momentive, as the proponent of the Plan. *See, e.g., In re 20 Bayard Views, LLC*, 445 B.R. 83, 93 (Bankr. E.D.N.Y. 2011) (“[T]he proponent of the Plan ... must establish by a preponderance of the evidence each of the [§ 1129] confirmation requirements ... has been met.”); *id.* at 105-11 (holding no efficient market existed where “the Debtor ... established by a preponderance of the evidence that there is not a market for the loan proposed in the Plan”).² Indeed, that is consistent with the words of the statute. Section 1129(b)(2)(A) permits a debtor to cram down a secured creditor only if the plan provides the creditor its collateral, payment of equivalent value, or some other “indubitable” equivalent—language strongly suggesting the debtor has the burden to show the plan will undoubtedly provide the creditor the full value of its secured claim.

² *See also, e.g., In re LightSquared*, 534 B.R. 522, 533-534 (S.D.N.Y. 2015) (“The Plan Proponents bear the burden of proving by a preponderance of the evidence that the plan complies with the absolute priority rule.”), *aff’d*, 644 F. App’x 24 (2d Cir. 2016); *In re Briscoe Enters.*, 994 F.2d 1160, 1163-1165, 1168-69 (5th Cir. 1993) (“Supreme Court holdings[] and the structure of the Code lead[] this Court to conclude that preponderance of the evidence is the debtor’s appropriate standard of proof both under § 1129 and in a cramdown.”); *In re Ambanc La Mesa Limited P’ship*, 115 F.3d 650, 653-54 (9th Cir. 1997); *In re Danny Thomas Props.*, 241 F.3d 959, 963 (8th Cir. 2001); *In re Quigley Co.*, 437 B.R. 102, 125 (Bankr. S.D.N.Y. 2010); *In re Delphi Corp.*, 2009 WL 2482146, at *20 (Bankr. S.D.N.Y. 2009); *In re WorldCom*, 2003 WL 23861928, at *46, *59-62 (Bankr. S.D.N.Y. 2003).

Momentive cites a few cases placing the burden on the creditor to establish an efficient market, *see* Response Mot. Limine [ECF No. 1653] at 19, but those cases either cite no authority, *In re Cantwell*, 336 B.R. 688, 693 n.1 (Bankr. D.N.J. 2006), or cite to *Till*’s explication of the formula approach. *See In re Riverbend Leasing LLC*, 458 B.R. 520, 537 (Bankr. S.D. Iowa 2011) (citing *Till*, 541 U.S. at 479); *accord In re S. Canaan Cellular Invs.*, 427 B.R. 44, 78 (Bankr. E.D. Pa. 2010); *In re Seaspan Dev. Corp.*, 2006 U.S. Dist. LEXIS 66827, at *7 (E.D. Tenn. 2006).

I. THE FINANCING MARKET FOR MOMENTIVE WAS EFFICIENT

A. Momentive Secured Exit Financing In An Arm's Length Transaction That Had a Term, Size and Collateral Comparable to the Replacement Notes

The record in this case unequivocally establishes that the “markets for financing” offered “a loan with a term, size, and collateral comparable to the forced loan contemplated under the cramdown plan.” *MPM Silicones*, 874 F.3d at 800. Shortly before it filed for bankruptcy, Momentive went into the market and secured exit financing that it would have used to cash out the Original First Lien Notes if the Noteholders had accepted the Plan. That financing had terms virtually identical to the Replacement First Lien Notes: the Exit Term Loan had the same tenor (7 years), approximately the same size (\$1.0 billion versus \$1.1 billion), and the same collateral.³ None of this is disputed. Momentive’s expert on market efficiency expert has conceded the point: “I would say the size, the term, the collateral in that exit term loan were comparable to what’s discussed in the replacement notes.”⁴

There is also no question that the resulting interest rate was negotiated among “sophisticated parties dealing at arms-length.” *MPM Silicones*, 874 F.3d at 801. Momentive retained Moelis, a leading restructuring firm, as an investment banker in November 2013 to “evaluate strategic alternatives and financing options” and authorized Moelis to “initiate the process of securing DIP financing to fund a potential chapter 11 filing” in February 2014.⁵

Moelis structured a “competitive process” that was “designed to attract multiple financing proposals,” “promote competition and obtain financing on the best terms available.”⁶

³ See Tr. Dep. Jamal (May 22, 2018) (“Jamal 2018 Tr.”) 169:19-170:24, 179:12-184:16; Statement of Stipulated Facts (ECF 1663) (“Stip. Facts”) ¶¶ 14, 45, 69.

⁴ See Anker Decl. (8/13/14) Ex. A, Tr. Dep. Smith (July 20, 2018) (“Smith Tr.”) 77:15-21.

⁵ JX 9 (Decl. Derrough Supp. DIP Financing, ECF 14) (“Derrough Decl.”) ¶ 11; Jamal 2018 Tr. 22:20-23:10, 24:18-25:12, 26:2-13, 26:20-30:8, 30:22-33:6, 33:23-34-7, 34:10-38:4.

⁶ Derrough Decl. ¶ 12; Jamal 2018 Tr. 57:11-58:22, 59:6-17.

Moelis requested DIP and exit financing proposals from each of J.P. Morgan, Citibank and Credit Suisse.⁷ These banks were not “insiders,” but three of the largest lenders in the leveraged loan market, who were selected because they were “sophisticated and highly skilled in providing financing in distressed situations” and were already familiar with Momentive, having participated in prior loans to the company.⁸ Each of these banks engaged in due diligence; met with management; and conducted its own internal credit-committee approval processes.⁹

In late February and early March 2014, J.P. Morgan, Citibank and Credit Suisse each submitted detailed proposals for DIP and exit financing.¹⁰ After comparing the proposals, Moelis separately sent each bank a draft of the Commitment and Fee Letters for the DIP and Exit Financing setting forth Momentive’s counterproposals—its “ask”—and requesting mark-ups as Momentive was “planning to select roles.”¹¹

Until the Commitment and Fee Letters for the DIP/Exit Financing were executed on April 3, 2014, Momentive and Moelis engaged in “extensive,” “virtually non-stop,” “multi-track

⁷ Derrough Decl. ¶ 12; Stip. Facts ¶ 10. Moelis also reached out to Apollo, GE Capital, and the ad-hoc group of second-lien lenders, but none offered better terms. Jamal Tr. 55:7-16, 71:8-25, 74:15-75:2, 75:22-76:4, 76:12-20, 77:7-16.

⁸ Stip. Facts ¶ 27; Derrough Decl. ¶ 12; Tr. Dep. Derrough (May 24, 2018) (“Derrough May 2018 Tr.”) 64:13-65:3, 68:11-16; JX77 at MPM1C_WFG_00031815 (J.P. Morgan, Citibank and Credit Suisse held minority positions in pre-petition ABL facility).

⁹ Derrough Decl. ¶ 13; Jamal 2018 Tr. at 105:11-23; JX113 (Credit Suisse due diligence questions for management call); JX121 (Credit Suisse diligence questions); JX122 (Momentive responses to diligence questions); JX124 (Credit Suisse credit approval memo); JX211 (Citibank credit approval memo); JX214 (J.P. Morgan credit approval memo).

¹⁰ Stip. Facts ¶ 10; JX75 (Citi Feb. 28, 2014 DIP); JX110 (J.P. Morgan Feb. 28, 2014 DIP); JX76 (Citi Mar. 6, 2014 DIP/Exit); JX77 (J.P. Morgan Mar. 12, 2014 DIP/Exit); JX111 (Credit Suisse Mar. 15, 2014 DIP); JX85 (Credit Suisse Mar. 17, 2014 Exit).

¹¹ Stip. Facts ¶ 11; Jamal 2018 Tr. 121:2-15, 122:18-124:4, 127:21-135:2; JX78 (Moelis Mar. 20, 2014 comparison); JX79 (Moelis Mar. 20, 2014 draft of Commitment/Fee Letters sent to Credit Suisse); JX80 (same sent to J.P. Morgan); JX81 (same sent to Citibank).

negotiations” with each of J.P. Morgan, Citibank and Credit Suisse.¹² More than 20 drafts of the Commitment and Fee Letters for the DIP/Exit Financing (and many additional e-mails and term sheets) went back and forth; those documents were “heavily negotiated.”¹³ The “negotiations were arms’ length at all times and were characterized by good-faith, hard bargaining by all interested parties.”¹⁴ The banks competed intensely with each other to be the lead arranger for the financing, as Moelis “played the three off against each other.”¹⁵ JX116 (Citibank email to Jamal of Moelis asking “where we stand”; Jamal responds the “biggest economic issues versus competition” included “flexing into a covenant in exit financing” and “initial pricing on exit”).

“As a result of this competitive process, the terms of each of the DIP Lenders’ initial standalone proposals were substantially improved.”¹⁶ Momentive ultimately determined that J.P. Morgan offered the “most cost-effective” terms and selected it to lead the financing, after which Citibank and Credit Suisse (collectively with J.P. Morgan, and the three other banks noted below, the “Arrangers”) each agreed to commit to provide one-third of the DIP and Exit Financing on the same terms.¹⁷ As Momentive’s and Moelis’s witnesses have testified, the result of this “competitive process” was the “best financing possible” on the “best terms” available for the company.¹⁸ Indeed, with respect to the Exit Term Loan’s interest rate, the final commitments

¹² Derrough Decl. ¶ 15; Jamal 2018 Tr. 65:21-66:7, 69:4-16, 70:4-71:3.

¹³ Jamal 2018 Tr. 135:3-136:7, 136:21-141:3; JX82, JX114 – JX115, JX117 – JX120, JX123, JX125 – JX137, JX139 (Commitment/Fee Letter drafts, term sheets).

¹⁴ Derrough Decl. ¶ 18; Derrough May 2018 Tr. 29:8-31:8; Jamal 2018 Tr. 66:8-16; Tr. Dep. Tramontozzi (June 7, 2018) (“Tramontozzi Tr.”) 42:13-19.

¹⁵ Jamal 2018 Tr. 92:12-94:5, 108:18-112:21; Derrough May 2018 Tr. 27:20-28:11; Anker Decl. (8/13/14) Ex. B, Tr. Dep. Derrough (July 26, 2018) (“Derrough 7/2018 Tr.”) 31:2-16.

¹⁶ Derrough Decl. ¶ 18; Jamal 2018 Tr. 116:16-24.

¹⁷ Derrough Decl. ¶ 15.

¹⁸ Tr. Dep. Jamal (July 22, 2014) 214:4-10; Tr. Dep. Carter (July 24, 2014 Tr.) 313:17-315:2; Derrough Decl. ¶¶ 12-18; Jamal 2018 Tr. 91:10-92:11, 102:7-17; Derrough May 2018 Tr. 24:21-26:22.

gave Momentive everything it requested in its “ask”: (1) LIBOR plus 400 basis points (“bps”) (or 4.00%), with a 1% LIBOR floor (not LIBOR plus 425 bps as Citibank proposed); (2) an upfront fee paid to every lender in the form of original issue discount (“OID”) of 50 bps (not 100 bps as Citibank proposed); (3) and market “flex” of 125 bps, permitting the Arrangers to increase the interest rate by up to 125 bps if necessary for a “successful syndication” of the Exit Term Loan in which the Arrangers were left holding none of the debt (not 175 bps of flex as J.P. Morgan proposed, or 150 bps of flex with a “step up” over time, as Credit Suisse proposed).¹⁹

After signing the commitments for the DIP/Exit Financing, Moelis reached out to three additional lenders—Goldman Sachs, Deutsche Bank, and UBS—inviting them to join as additional Arrangers.²⁰ When asked why Moelis did not reach out to them from the beginning, Mr. Jamal explained that the process was already “sufficiently competitive.”²¹ Ultimately, Goldman Sachs, Deutsche Bank and UBS each agreed to join as additional Arrangers for the Exit Term Loan on the same terms Moelis negotiated with J.P. Morgan, Citibank and Credit Suisse.²²

Although Momentive obtained commitments for the Exit Term Loan from the Arrangers in April 2014, the commitments extended through October 2014, the month in which Momentive emerged from bankruptcy.²³ The Arrangers protected themselves against the possibility that spreads above LIBOR might widen in the market between April and October 2014 with the 125 bps of flex that they negotiated for use, if necessary, for a successful syndication.²⁴

B. The Markets For Financing Were Very Active Around The Effective Date

¹⁹ Stip. Facts ¶¶ 12, 14-17; Jamal 2018 Tr. 116:25-121:15, 122:18-128:12; JX76 – JX79, JX85.

²⁰ Stip. Facts ¶19; Jamal 2018 Tr. 85:14-17, 85:22-86:5.

²¹ Jamal 2018 Tr. 86:11-89:10.

²² Stip. Facts ¶ 19; Jamal 2018 Tr. 141:4-142:10.

²³ JX4 (DIP/Exit Commitment Letter) ¶ 15.

²⁴ JX5 (DIP/Exit Fee Letter) ¶ 9.

Even if Momentive had not secured commitments for the Exit Term Loan, the debt financing markets were highly active at the time that Momentive emerged from bankruptcy, providing further evidence that Momentive could have obtained exit financing with a similar term, amount, and collateral as the Replacement First Lien Notes. The markets for leveraged loans and high-yield corporate bonds were both at very high levels in 2014. More than 2,400 leveraged loans providing nearly \$1 trillion in financing were issued in 2014 (one of the highest years on record between 2000 and 2015), with more than 100 issuances of \$1 billion or more.²⁵ Similarly, 763 high-yield corporate bonds providing \$369.5 billion in financing were issued in 2014 (again one of the highest years on record between 2000 and 2015).²⁶ Of this amount, 178 leveraged loans providing \$65 billion in financing and 68 high-yield bonds providing \$31.2 billion were issued in the “materials” industry in which Momentive operates.²⁷ Furthermore, 109 high-yield issuances totaling \$53.2 billion were issued with a “B” credit rating from Standard & Poor’s—the same rating assigned to the Replacement First Lien Notes—and 11 of these issuances had a principal amount of \$1 billion or more.²⁸

Momentive’s market-rate expert, Mr. Derrough, has acknowledged that the “leveraged loan market remained robust” around the Effective Date.²⁹ Consistent with this strong market activity, Mr. Tramontozzi of J.P. Morgan testified that if Momentive had issued \$1.1 billion of seven-year notes secured by the same collateral as the Replacement First Lien Notes with market terms, J.P. Morgan would have underwritten those notes and they would have cleared the market

²⁵ Cornell Expert Report ¶ 30 & Ex. 1.

²⁶ Cornell Expert Report ¶ 31 & Ex. 3. A few months after the Effective Date, the Replacement First Lien Notes were assigned credit ratings by Standard & Poor’s and Moody’s of B and B3, respectively, both of which are non-investment grade ratings. Stip. Facts ¶¶ 74-75.

²⁷ Cornell Expert Report ¶¶ 30-31 & Exs. 2, 4.

²⁸ Cornell Expert Report ¶ 31 & Ex. 5; Stip. Facts ¶ 74.

²⁹ Derrough Expert Report ¶ 63.

(i.e., been purchased by investors).³⁰ And Mr. Derrough conceded at his deposition that Momentive could have sold the Replacement First Lien Notes into the market (assuming the interest rate were higher).³¹

C. Momentive’s Expert on Market Efficiency Applies the Incorrect Legal Standard and a Novel Three-Step Test That Is Fundamentally Flawed

As set forth in BOKF’s motion in limine (ECF 1644), Professor Smith’s opinions are not based on the correct legal standard of market efficiency explicated by the Second Circuit, but rather an irrelevant “efficient market theory” that examines whether securities trading prices reflect all available information. If the Court does not exclude Professor Smith, BOKF is prepared to show at trial that his opinions are, in any event, deeply flawed and unreliable.

Not only does Professor Smith ask the wrong question—he incorrectly asks whether the trading prices of the Replacement Notes would have reflected all available information, rather than whether the lending markets offered financing comparable to the Replacement Notes—but he constructs a novel “three-step” test that, conveniently, is almost certain to lead to one and only one answer: the market is always inefficient.

To test whether the trading price of the Replacement Notes reflected all available information, Professor Smith does not examine how their prices reacted to new information (or how the prices of the original First Lien Notes reacted to new information between this Court’s ruling on August 26, 2014 approving the Plan and the Effective Date).³² Rather, Professor Smith develops a three-step test (without citing any literature recognizing his test) in which he (1) selects the “key” features of the Replacement Notes that purportedly capture their risk exposure, (2) looks for securities issued by *other* companies that contained all the same “key” features, and

³⁰ Tramontozzi Tr. 138:7-140:3.

³¹ Derrough 7/2018 Tr. 68:22-70:12, 71:7-18.

³² Smith Expert Report ¶¶ 13, 102-04.

(3) if he finds any such securities (a “reference market”), tests whether the prices of those *other* securities reflected all available information.³³ Although Professor Smith found securities containing six of the seven “key” features he identified, he found none containing the seventh—a long-term fixed-rate high-yield bond with no call protection.³⁴ Remarkably, instead of concluding that his test simply failed to answer the question—because he found no “reference market” whose efficiency he could test—Professor Smith concludes that his inability to *test* efficiency means that the *answer* to the test is that the market was *not efficient*.³⁵

In short, Professor Smith’s opinion is that no efficient market existed simply because the Replacement Notes included a term—no call protection—that was, in the words of Mr. Derrough, “highly unusual” and “off-market.”³⁶ Of course, Momentive could have included call protection; there was no economic reason or legal reason it could not have. It simply elected not to do so. Nonetheless, as Mr. Derrough and Mr. Tramontozzi of J.P. Morgan have testified, Momentive could have sold the Replacement Notes into the market even without call protection—the interest rate simply would have needed to be *higher* to compensate the Noteholders for the additional risk.³⁷ But because the lack of call protection was so unusual, Professor Smith opines that no efficient market existed. As a result, in Momentive’s view, the *Till* formula rate of 3.88% should still apply—notwithstanding that its market-rate expert admits that the market rate for those Notes would be materially *higher* even with call protection, and

³³ Smith Expert Report ¶¶ 10, 46, 52, 65, 105-106; BOKF Mot. Limine (ECF 1644) 8-11.

³⁴ Smith Expert Report ¶ 67; Smith Tr. 156:12-158:19.

³⁵ Smith Expert Report ¶ 110.

³⁶ Derrough Expert Report ¶¶ 34-43.

³⁷ Derrough 7/2018 Tr. 68:22-70:12, 71:7-18; Tramontozzi Tr. 125:15-129:14, 148:20-150:4.

higher still without it.³⁸ Thus, by including an off-market term that made the Notes *riskier*, Momentive claims that it can cram down the Notes at a *lower*, not higher, interest rate.

That is contrary to basic economic principles, common sense, and the law.³⁹ Professor Smith's test would allow every debtor to evade a market rate of interest by simply including "off-market" terms in the cramdown notes, nullifying the Second Circuit's and Supreme Court's command that, in Chapter 11 cases, "the best way to determine value is exposure to a market," at least "when some form of market valuation may be available." *MPM Silicones*, 874 F.3d at 800 (quoting *Bank of Am. v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 457 (1999)).

II. THE MARKET RATE WAS AT LEAST BETWEEN 6.47% TO 6.99%

A. The Best Evidence of the Market Rate for the Replacement First Lien Notes Is the Interest Rate for the Exit Term Loan

To ascertain the market rate of interest for the Replacement First Lien Notes, BOKF's expert Professor Cornell principally referred to the terms of the Exit Term Loan. He concluded the Exit Term Loan provided the best evidence of the market rate because it was an actual market transaction with these very Debtors for first lien financing. As discussed above, the loan resulted from competition among three of the largest lenders in the market and involved extensive, arm's length negotiations among highly sophisticated parties, producing the "best terms" available for Momentive.⁴⁰ This competitive process provided reasonable assurance that

³⁸ Derrough Expert Report ¶ 75; Derrough Rebuttal Report ¶¶ 8, 25; Derrough 7/2018 Tr. 64:3-10; Smith Tr. 190:12-18 (all things being equal, no call protection leads to higher interest rate).

³⁹ Cornell Rebuttal Report ¶¶ 20-22.

⁴⁰ Although Momentive obtained commitments for the Exit Term Loan from the six Arrangers, it retained the right to obtain exit financing from another lender if it received a better offer. JX5 (DIP/Exit Fee Letter) ¶ 10; Derrough May 2018 Tr. 43:12-20. On the first day of its bankruptcy, Momentive's counsel stated in open court that "everybody knows Bill Derrough"; "[i]f they think they have a competitive proposal, we're happy to hear it." JX74 at 134:16-20. Yet no one came forward with a better proposal for exit financing. Derrough May 2018 Tr. 43:21-45:25, 47:23-48:15, 49:10-50:7, 53:16-54:12; Jamal 2018 Tr. 78:17-82:21, 91:10-92:11.

the resulting interest rate was a competitive market rate. Moreover, the Exit Term Loan was an actual commitment to provide essentially the same financing (a seven-year \$1 billion loan secured by the same basic collateral) as the Replacement First Lien Notes. Accordingly, Professor Cornell concluded that the Exit Term Loan provided the best evidence of the market rate of interest that Momentive would have been required to pay for the Replacement First Lien Notes if it had sought to obtain that financing from independent lenders in the open market.⁴¹

Professor Cornell's analysis is consistent with the case law, in which courts have similarly relied on the rates the debtor negotiated for its exit financing. For example, in *In re Winn-Dixie Stores, Inc.*, 356 B.R. 239 (Bankr. M.D. Fla. 2006), the court determined the market rate for a Chapter 11 cramdown loan by looking to the interest rate for the debtors' \$720 million exit facility. It explained that the debtors "went out into an efficient market and shopped" for exit financing, "result[ing] in fourteen proposals among competing lending institutions." *Id.* at 255-56. The "process leading to the exit facility was an efficient test of the market" and provided an appropriate basis for determining the market rate. *See id.* The same is true here.

B. The Fixed-Rate Equivalent of the Exit Term Loan Floating Rate (Assuming No Flex) Is 6.47%

The Exit Term Loan provided for a floating rate of interest tied to LIBOR. However, the Replacement First Lien Notes bear a fixed rate of interest. Accordingly, to determine the market rate of interest for the Replacement First Lien Notes, Professor Cornell converted the Exit Term Loan's floating rate to the equivalent fixed rate of interest.

1. The Market Rate Should Be A Fixed Rate

⁴¹ Cornell Expert Report ¶¶ 20, 34.

As a threshold matter, Momentive’s expert opines that the market rate for the Replacement Notes should be a floating rate.⁴² That is incorrect. The Plan expressly provided that the Replacement First Lien Notes would “bear[] interest at a fixed rate.”⁴³ This is consistent with standard market practice.⁴⁴ Whereas leveraged loans typically bear a floating rate of interest, high-yield bonds typically bear a fixed rate of interest, as Mr. Derrough and his Moelis colleague Mr. Jamal both admit.⁴⁵

Applying a fixed rate of interest is also consistent with the law. *See, e.g., United States v. Neal Pharmacal Co.*, 789 F.2d 1283, 1286 (8th Cir. 1986) (applying §1129(b)(2)(A) cramdown standard for determining market rate for note issued to tax creditor under §1129(a)(9)(C), and rejecting use of floating rate because §1129 “contemplates the use of a fixed interest rate”). In *Winn Dixie*, the debtors similarly negotiated exit financing bearing a *floating rate* of interest. But consistent with Professor Cornell’s approach here, the court held that the market rate for the cramdown notes there was the equivalent *fixed rate* of interest. 356 B.R. at 255-56 (“Debtors expect the exit financing interest rate to be LIBOR plus 150 basis points, currently equivalent to a 7% interest rate”; “the Court ... conclude[s] that the appropriate interest rate ... is 7%”).

The sole reason Mr. Derrough asserts the market rate should be a floating rate is because the Replacement Notes “lack call protection and thus investors do not receive the benefit of interest rate increases as partial compensation for the lack of any call premium upon an early redemption.”⁴⁶ But the fact that Momentive crammed down the Replacement Notes with an off-market term—no call protection—does not mean that the market rate for those Replacement

⁴² Derrough Expert Report ¶ 12, 75.

⁴³ JX55 (Plan) § 1.153; Stip. Facts ¶ 45.

⁴⁴ Cornell Expert Report ¶ 36; Cornell Rebuttal Report ¶24.

⁴⁵ Derrough 7/2018 Tr. 57:21-58:8; Jamal 2018 Tr. 192:18-193:2.

⁴⁶ Derrough Expert Report ¶ 75.

Notes must be a floating rate; it simply means that the market rate for the Replacement Notes may need to be a *higher* fixed rate of interest than the market would otherwise have required if the Notes had call protection.⁴⁷ As the lead Arranger J.P. Morgan's witness (Mr. Tramontozzi) testified, J.P. Morgan would have underwritten the Replacement Notes, even with no call protection and a *fixed rate* of interest, so long as it had flex to increase the interest rate.⁴⁸ Indeed, Mr. Derrough admits that investors expect a higher interest rate if there is no call protection, and he has conceded that the Replacement First Lien Notes could have been sold into the market even without call protection at a *fixed rate* of interest, provided the interest rate were higher.⁴⁹

Moreover, retroactively requiring a floating rate for the Replacement Notes would be an improper use of hindsight and provide a windfall to the Debtors. When Momentive's Plan went effective, LIBOR was expected to increase. Market expectations of future LIBOR rates are reflected in the "forward LIBOR curve," a standard market data source that is commonly used to estimate future interest payments for floating-rate LIBOR-based loans as of a particular date.⁵⁰ As of the Effective Date, the forward LIBOR curve projected that LIBOR would be higher than has actually been the case over the past four years.⁵¹ Momentive would therefore benefit from

⁴⁷ Cornell Rebuttal Report ¶ 41.

⁴⁸ Tramontozzi Tr. 125:15-129:14, 148:20-150:4 ("Q. [J]ust assume these things with me. One, that the replacement first lien notes were issued at a fixed rate of 3.88 percent; two, that there was no call protection; and ... three, that they had a tenor of seven years; and four, that they did not have a rating as of the effective date. [] Q. Okay. Based on your knowledge of J.P. Morgan's underwriting requirements, do you know whether J.P. Morgan would have underwritten a debt instrument with those four characteristics as of the effective date? ... A. I don't believe we would have without flex. ... A. We would look for pricing flex to increase the interest rate.").

⁴⁹ Derrough 7/2018 Tr. 64:3-10, 68:22-70:12, 71:6-18 ("Q. There is an implied yield at which the replacement first lien notes and the replacement 1-and-a-half lien notes would have cleared the market with a fixed rate of interest even without any call protection as of October 24, 2014, true or false? A. I would ... I would assume true. We just don't know what that is.").

⁵⁰ Cornell Expert Report ¶¶ 38, 42.

⁵¹ Cornell Rebuttal Report ¶¶ 32, 44 & Ex. 5; Stip. Facts ¶ 73.

imposing a floating rate because, as Mr. Derrough admits, calculating interest payments based on actual LIBOR over the post-Effective Date period would result in a lower “catch up” payment than a catch-up payment based on the fixed rate equivalent of expected LIBOR as of the Effective Date.⁵²

That would be improper. Momentive chose to issue the Replacement Notes as bonds bearing a fixed rate of interest. It should not be permitted to revisit that decision now just because, with the benefit of hindsight, it would have been better off with a floating rate over the past four years than with a fixed rate set precisely where the market was when the Plan went effective. Cramdown notes must have a value “as of the effective date of the plan” equal to the secured creditors’ allowed claim. 11 U.S.C. § 1129(b)(2)(A)(i)(II). The market rate must therefore be based on expectations as of the Effective Date, without the benefit of hindsight, consistent with general principles of valuation that must be made at a point in time. *See In re Iridium Operating LLC*, 373 B.R. 283, 345-46 (Bankr. S.D.N.Y. 2007) (rejecting “use of improper hindsight analysis” in valuation of debtors and recognizing “the advantage of contemporaneous market evidence as being untainted by hindsight or post-hoc litigation interests” (internal quotation marks omitted)). Indeed, the real difference between Professor Cornell’s approach and Mr. Derrough’s is that Professor Cornell performed an “ex ante” analysis, while Mr. Derrough performed an “ex post” analysis⁵³—precisely what the law forbids.

Moreover, Mr. Derrough’s analysis (like Professor Smith’s) would reward Momentive for cramming down the Replacement Notes with an “off market” term—purportedly requiring a

⁵² Cornell Rebuttal Report ¶¶ 32, 44; Derrough Rebuttal Report ¶¶ 8, 25 (catch-up payment of \$61.9 million if floating rate and \$70.3 million if fixed); Derrough 7/2018 Tr. 50:24-56:24.

⁵³ Anker Decl. (8/13/14) Ex. C, Tr. Dep. Cornell (July 31, 2018) 168:7-169:24.

floating rate and *lower* catch-up payment—notwithstanding his admission that imposing “off market” terms like no call protection will, in the real world, require a *higher* market rate.⁵⁴

2. Under the Standard Market Methodology For Converting A Floating Rate To A Fixed Rate, The Fixed-Rate Equivalent Of The Exit Term Loan Is 6.47%

There is a standard methodology commonly applied in financial markets for converting a floating rate of interest to an equivalent fixed rate as of a given date.⁵⁵ In fact, an entire market—the interest-rate swap market—is premised on the recognition that floating rates can be exchanged for equivalent fixed rates.⁵⁶ To convert the Exit Term Loan’s floating rate to its fixed-rate equivalent here, Professor Cornell determined the expected future principal and floating-rate interest payments over the seven-year term of the Exit Term Loan and calculated the fixed rate of interest that would set the present value of those future cash flows (discounted at such fixed rate) equal to the net amount the Arrangers committed to lend on the Effective Date (i.e., \$1 billion principal, net of the offsetting value the lenders would receive from the \$5 million upfront fee/OID and from the 1% LIBOR floor, as valued using the standard methodology for valuing options called the Black-Scholes model).⁵⁷

As noted, the commitments for the Exit Term Loan provided for a floating rate of LIBOR plus 400 basis points (with a 1% LIBOR floor) and 125 basis points of flex. Taking the lower bound of this range (i.e., LIBOR plus 400 bps) and assuming that the Arrangers would not have needed to use any flex to syndicate the Exit Term Loan, Professor Cornell determined the expected future floating-rate interest payments on the Exit Term Loan using the forward LIBOR

⁵⁴ Derrough 7/2018 Tr. 64:3-10.

⁵⁵ Cornell Expert Report ¶ 38.

⁵⁶ Cornell Expert Report ¶ 55.

⁵⁷ Cornell Expert Report ¶¶ 38-49 & Exs. 6-8.

curve provided by the standard industry source, Bloomberg, as of the Effective Date.⁵⁸ Then, applying the foregoing methodology, Professor Cornell determined that the fixed-rate equivalent of the Exit Term Loan's floating rate of LIBOR plus 400 bps (assuming no flex) was 6.47%.⁵⁹

C. The Fixed-Rate Equivalent of the Exit Term Loan Floating Rate (Assuming 50 Basis Points of Flex) Is 6.99%

The Exit Term Loan commitments granted the Arrangers flex to increase the interest rate by up to 125 bps if needed for a "successful syndication" in which the Arrangers were left holding none of the debt.⁶⁰ Because the Exit Term Loan was never syndicated, it is impossible to know with certainty whether, and to what extent, the Arrangers would have needed to use flex to syndicate the loan. Accordingly, Professor Cornell did not simply assume that the Arrangers might have used the full 125 bps of flex in setting the upper bound of his range for the market rate. Rather, he examined the contemporaneous market environment and the record in this case and, based thereon, set the upper bound of his range based on the premise that the Arrangers might have needed to use 50 bps of flex, to increase the interest rate to LIBOR plus 450 bps.

Average spreads above LIBOR for leveraged loans increased by more than 50 bps between April 2014, when the Exit Term Loan was committed, and October 2014 when the Plan went Effective.⁶¹ Mr. Derrough has himself acknowledged this, specifying that they increased by 87 bps over that period.⁶²

⁵⁸ Cornell Expert Report ¶¶ 40-43 & Exs. 6, 8; *see also* Derrough 7/2018 Tr. 54:19 ("Bloomberg is a great source.").

⁵⁹ Cornell Expert Report ¶¶ 46-49 & Exs. 6, 8.

⁶⁰ JX5 (DIP/Exit Fee Letter) ¶ 9; Tramontozzi Tr. 44:14-45:22.

⁶¹ Cornell Expert Report ¶ 51 & Ex. 9 (average spreads increased 62 bps between second and fourth quarters of 2014, increasing from LIBOR plus 396 bps to LIBOR plus 458 bps).

⁶² Derrough Expert Report ¶ 63 & Ex. 5 (weighted average spreads increased by 87 bps between April and October 2014, increasing from LIBOR plus 418 bps to LIBOR plus 505 bps).

All of this is consistent with the record in this case. Mr. Tramontozzi confirmed the obvious—that it was more likely that the Arrangers would have needed to use flex if, as was the case, spreads above LIBOR were increasing.⁶³ In fact, in August 2014, Momenive and J.P. Morgan drafted offering materials in anticipation of seeking to syndicate the Exit Term Loan in September 2014. In late August—only three days before this Court’s confirmation ruling—J.P. Morgan advised Momenive and Moelis that its “current interest rate assumptions” for the Exit Term Loan was LIBOR plus 450 bps (with a 1% LIBOR floor).⁶⁴ The last draft of the offering materials—dated only one day before this Court’s confirmation ruling—similarly used an interest rate of LIBOR plus 450 bps for the Exit Term Loan.⁶⁵ That was the last “guidance” J.P. Morgan provided Momenive on the interest rate for the Exit Term Loan before Momenive abandoned the Exit Term Loan in favor of issuing the Replacement Notes.⁶⁶

To be sure, as Mr. Tramontozzi noted, it is possible that demand for the Exit Term Loan would have been so substantial on the Effective Date that no flex would have been required (or even, in theory, that the loan might have syndicated at a rate lower than LIBOR plus 400 bps). But spreads above LIBOR continued to widen, not narrow, between late August and late October 2014.⁶⁷ And, in any event, because of the uncertainty, Professor Cornell did not simply calculate a single fixed interest rate based on the floating rate of LIBOR plus 450 bps. Rather, he used

⁶³ Tramontozzi Tr. 88:19-23 (“Q. If spreads above LIBOR are increasing, it’s more likely that J.P. Morgan as the arranger is going to need to use the flex? ... A. Yes.”). As noted, Professor Cornell and Mr. Derrough both observed that spreads were increasing.

⁶⁴ JX84 (Aug. 23, 2014 e-mail from J.P. Morgan to Moelis); Stip. Facts ¶ 21; JX43 (Aug. 23, 2014 internal J.P. Morgan e-mail noting “new guidance Tram [Tramontozzi] gave to Apollo” of “50 bps (guidance now L+450 vs. L+400) on \$1,000[MM]” Exit Term Loan); Tramontozzi Tr. 52:24-53:6, 54:2-5, 54:9-56:9, 59:12-66:23, 67:7-68:5, 68:16-71:13, 72:3-73:25.

⁶⁵ JX44 (Aug. 25, 2014 draft of Lender Presentation for Exit Term Loan) p.7 n.2 (MPMR_AGSHF_0009346); Tramontozzi Tr. 74:4-11, 74:24-75:24, 77:14-78:21, 80:8-81:12.

⁶⁶ Tramontozzi Tr. 82:18-84:10.

⁶⁷ Stip. Facts ¶ 22 (spreads above LIBOR increased from 4.58% to 5.05%).

that merely as the upper bound of his range, with the lower bound remaining at LIBOR plus 400 bps (i.e., assuming that no flex would be needed, notwithstanding the evidence to the contrary).

For the upper bound of his range, Professor Cornell proceeded as he did for the lower bound. He converted the floating rate of LIBOR plus 450 bps to the equivalent fixed rate using the same methodology described above, resulting in a fixed rate of 6.99% per annum.

D. Because the Replacement Notes Had Less Favorable Terms Than the Exit Term Loan, the Market Rate Was At Least Between 6.47% and 6.99%

Professor Cornell's opinion that the market rate of interest for the Replacement First Lien Notes was at least between 6.47% and 6.99% is, if anything, understated, and not merely because of the cautious assumptions he made on both ends of his range regarding the amount of flex that would have been required to syndicate the Exit Term Loan. The terms of the Replacement First Lien Notes were less favorable to the Noteholders as compared to the Exit Term Loan and exposed them to greater risk. For example, the Replacement First Lien Notes had a slightly larger size (\$1.1 billion versus \$1.0 billion); provided for no amortization of principal (the Exit Term Loan did); had no default rate of interest (the Exit Term Loan did); and had no call protection (the Exit Term Loan did).⁶⁸ Momentive's own experts have emphasized that "[c]all protection is a fundamental price term that cannot be ignored in evaluating the market rate of interest for the Replacement Notes" (Mr. Derrough) and that, all things being equal, the lack of call protection—which places "the Investor ... at risk of significant economic loss" (Mr. Derrough) and "expose[d] the Replacement Notes to additional risk" (Mr. Smith)—should (as Messrs. Derrough and Smith have each testified) lead to a higher rate of interest.⁶⁹ Yet Professor

⁶⁸ Cornell Expert Report ¶ 34; JX4 (DIP/Exit Commitment Letter) Ex. C 11, 15, 17; JX57 (Replacement First Lien Notes Indenture) §§ 2.01, 3.09, 4.01 & Ex. A-2, A-5, A-6.

⁶⁹ Derrough Rebuttal Report ¶ 7; Derrough Expert Report ¶¶ 37-39; Smith Expert Report ¶¶ 57-58; Derrough 7/2018 Tr. 63:3-18, 64:3-10, 66:19-24; Smith Tr. 161:4-8, 190:12-18.

Cornell did not increase his range of 6.47% to 6.99% to account for that or any of the other increased risks. He simply observed that the market rate of interest for the Replacement First Lien Notes was, if anything, *at least* between 6.47% to 6.99%.

E. Other Market Evidence Confirms That The Market Rate Was At Least Between 6.47% And 6.99%

To check the reasonableness of his conclusions, Professor Cornell also examined several other market data points and observed that this additional market evidence confirms that the market rate for the Replacement First Lien Notes was between 6.47% and 6.99%.

First, as of the Effective Date, the market for interest-rate swaps priced a floating interest rate of LIBOR plus 400 bps (with a 1% LIBOR floor and 50 bps of OID) at a fixed rate of 6.45%. Assuming 50 bps of flex, the swap price was a fixed interest rate of 6.96%.⁷⁰

Second, while Professor Cornell did not place primary weight on trading prices, he observed that the trading prices of the Original First Lien Notes and the Replacement First Lien Notes around the Effective Date—approximately 87% of face value—implied a market rate of interest (or “yield”) of approximately 6.2%.⁷¹ Under basic principles of finance, when a bond’s interest rate is below the prevailing market rate for bonds of comparable risk, investors will pay less than face value for the bond and will discount the bond’s price to the level—here 87% of face value—required to earn the market rate.⁷² Moreover, the implied rate of 6.2% almost surely understates the market interest rate on the Replacement First Lien Notes because, as Momentive’s experts acknowledge, investors who paid 87 cents on the dollar received, in addition to the future stream of principal and 3.88% interest payments, a potential recovery from BOKF’s then-pending confirmation appeal on its claims for the make-whole and a market rate of

⁷⁰ Cornell Expert Report ¶¶ 55-58 & Exs. 7-8, 12A-B, 13.

⁷¹ Cornell Expert Report ¶¶ 59-60.

⁷² Cornell Expert Report ¶ 59.

interest.⁷³ Without that potential recovery, common sense dictates that investors would have paid less than 87 cents on the dollar, producing a market interest rate even higher than 6.2%.

Finally, bond indices for bonds with the same credit rating as the Replacement First Lien Notes, i.e., a “B” credit rating from Standard & Poor’s, reflected yields as of the Effective Date of 6.58% (for bonds with 5-7 years to maturity) and 6.15% (for bonds with 7-10 years to maturity).⁷⁴ Moreover, a substantial portion of the bonds in these indices had yields of at least 6.99% as of the Effective Date (38% and 24%, respectively).⁷⁵

F. Momentive’s Expert’s Opinion That the Market Rate Was Between 5.5% to 5.7% (or a Lower Floating Rate) Is Fundamentally Flawed and Unreliable

Mr. Derrough opines that the market rate for the Replacement First Lien Notes should be a floating rate ranging between LIBOR plus 400 bps to LIBOR plus 425 bps (each with a LIBOR floor of 1%) or, if the Court declines to require a floating rate, a fixed rate ranging between 5.5% and 5.7%.⁷⁶ Mr. Derrough’s opinions are fundamentally flawed for numerous reasons.

To begin with, Mr. Derrough’s opinion that the market rate must be a floating rate is unfounded for the reasons discussed above. Moreover, the upper bound of his floating-rate range—LIBOR plus 425 bps—has no basis in the record. Mr. Derrough admits that even this upper bound assumes that the Arrangers would not have had to use any of the 125 bps of flex (and, instead, simply takes account of the OID/upfront fee the lenders would have received under the Exit Term Loan).⁷⁷ An analysis that, even on the higher end of the range, assumes that no flex would have been needed to syndicate the Loan, notwithstanding the substantial widening in

⁷³ Cornell Expert Report ¶¶ 61-64; Smith Expert Report ¶¶ 102-103; Derrough 7/2018 Tr. 151:5-25; Stip. Facts ¶¶ 76-77.

⁷⁴ Cornell Expert Report ¶ 65; Stip. Facts ¶ 74.

⁷⁵ Cornell Expert Report ¶ 65.

⁷⁶ Derrough Expert Report ¶ 75; Derrough Rebuttal Report ¶¶ 8, 25.

⁷⁷ Derrough Expert Report ¶ 75; Derrough 7/2018 Tr. 81:10-82:10, 334:9-338:4.

spreads between April and October 2014 and J.P. Morgan's guidance in August 2014 of 50 bps in flex, is simply not credible. As even Mr. Derrough admits, he cannot point to anything in the record that supports his cap of LIBOR plus only 425 bps.⁷⁸

In any event, when shifting to his rebuttal opinion that the market fixed rate of interest was between 5.5% and 5.7%, Mr. Derrough appears to disregard the Exit Term Loan altogether. Instead, he derives his fixed rate by looking at (1) the yields implied by the trading prices of debt issued by other purportedly "comparable" companies, and (2) new debt issuances by other companies in the leveraged loan and high-yield bond markets around the Effective Date (although he placed "a limited amount of weight" on this second category).⁷⁹

It is striking that the crux of Mr. Derrough's analysis, like Professor Smith's, thus relies on the trading prices of debt securities.⁸⁰ This Court questioned the significance of such trading prices at the March 9, 2018 scheduling conference.⁸¹ In any event, Mr. Derrough's analysis ignores the elephant in the room: the trading prices of the First Lien Notes themselves. The Replacement First Lien Notes traded in the market shortly after the Effective Date, at a price of 87 cents on the dollar, just as the Original First Lien Notes did shortly before the Effective Date, implying a market rate of interest of at least 6.2% (really higher since, as discussed, the potential

⁷⁸ Derrough 7/2018 Tr. 82:11-85:10. While Mr. Derrough suggests that Momentive's "company-specific" factors improved after April 2014, Derrough Rebuttal Report ¶ 12 (citing its financial results in the Disclosure Statement, the \$600 million equity investment, and certainty around the Plan), the company's financial performance in bankruptcy and the terms of the Plan were known when J.P. Morgan provided its "interest rate assumptions" of LIBOR plus 450 bps in Aug. 2014.

⁷⁹ Derrough Rebuttal Report ¶¶ 25-28; Derrough Expert Report ¶¶ 65-74 & Exs. 6-8.

⁸⁰ Derrough 7/2018 Tr. 137:4-140:12 ("Q. What you are looking at is what the trading price was for that debt as of the effective date and thereby compute the yield, either yield to worst or yield to maturity; right? A. Trading price and all the other elements, coupon and things like that, yes.").

⁸¹ Mar. 9, 2018 Hr'g Tr. (ECF 1633) 9-10, 17-19, 24-25.

litigation recoveries presumably pushed up the trading price). Yet, as Mr. Derrough admits, he gave zero weight to the trading prices of the Replacement First Lien Notes and the Original First Lien Notes.⁸² Instead, he looked solely at the debt of *other* companies to arrive at a substantially lower market rate of 5.5% to 5.7%.

It is also striking that, while Mr. Derrough asserts that the “preferred market approach” to determine a market rate for a bond is to examine the prevailing interest rates for the bonds or loans of companies that are as “similar” and “comparable” to Momentive and the Replacement First Lien Notes as possible, he concludes that “none of the[] issuances” that he examined truly “are comparable to the Replacement Notes.”⁸³ Yet, he disregards the two market transactions that are unquestionably the most “comparable” to Momentive and the Replacement First Lien Notes: (1) the commitments that *Momentive itself* obtained for the Exit Term Loan, and, as noted, (2) the trading of *the very bond in question*, the Replacement First Lien Notes (and the Original First Lien Notes) around the Effective Date.

Mr. Derrough also disregards Momentive’s own, contemporaneous assessment of the market rate for the Replacement First Lien Notes—which was likewise substantially higher than the rate Momentive now urges in this litigation four years later. When Momentive emerged from bankruptcy, it recorded the “fair value” of the Replacement First Lien Notes in its financial statements filed with the Securities and Exchange Commission at 87% of their \$1.1 billion face value (or \$957 million).⁸⁴ It explained in its 10-K that it valued the Replacement First Lien Notes as of the Effective Date at “approximately 87% of par value” “based on a market approach

⁸² Derrough 7/2018 Tr. 154:16-23, 158:18-159:9.

⁸³ Derrough Expert Report ¶¶ 43, 65; Derrough Rebuttal Report ¶¶ 25-27; Derrough 7/2018 Tr. 144:6-147:6.

⁸⁴ Stip. Facts ¶ 79; JX61 (10-Q) 21; JX65 (10-K) 51, 64, 66, 68; Tr. Dep. Knight Tr. (May 23, 2018) (“Knight Tr.”) 107:11-112:7.

utilizing current market yields.”⁸⁵ In reaching that conclusion, Momentive relied on the analysis of a third-party valuation firm it had hired, Valuation Research Corporation (“VRC”).⁸⁶ VRC determined that the Notes’ 3.88% interest rate was “below market” and performed a market analysis to conclude that the market rate of interest for the Replacement First Lien Notes was approximately 6.25%.⁸⁷ At that market rate, VRC concluded that the value of the Replacement First Lien Notes was 87% of face value—the value Momentive adopted in its SEC filings and the approximate trading price of the Original First Lien Notes and Replacement First Lien Notes around the Effective Date.⁸⁸ Momentive’s auditors, PricewaterhouseCoopers, reviewed the VRC analysis, raised no issues, and gave Momentive a “clean audit” opinion.⁸⁹ Yet, Mr. Derrough admits that he did not consider VRC’s work, instead performing a new “market” analysis to advance a materially *lower* rate (5.5% to 5.7%) than what Momentive accepted and reported at the time (6.25%).⁹⁰

As for Mr. Derrough’s own analysis, he primarily examined (1) new debt issuances around the Effective Date and (2) the trading prices of “comparable” companies. As for the former, Mr. Derrough considers seven secured high-yield bond issuances and fourteen leveraged loan issuances around the Effective Date.⁹¹ Notably, the interest rates for these issuances were

⁸⁵ JX65 (10-K for year ended Dec. 31, 2014) 51, 68; Knight Tr. 115:4-120:14.

⁸⁶ Stip. Facts ¶79; JX60 (VRC valuation report) at MPMR_AGSHF_0032185; Knight Tr. 78:25-79:24, 112:23-114:3.

⁸⁷ JX60 (VRC valuation report) at MPMR_AGSHF_0032189, 0032191-92; Tr. Dep. Newell (May 29, 2018) (“Newell Tr.”) 52:16-53:10, 58:2-63:16, 69:16-23, 77:4-79:3; Knight Tr. 89:18-90:6, 96:20-97:11.

⁸⁸ JX60 (VRC valuation report) at MPMR_AGSHF_0032185, 0032189; Newell Tr. 50:4-52:10, 54:16-24, 63:22-64:17; Knight Tr. 94:15-21, 110:17-112:16.

⁸⁹ JX204 (Pricewaterhouse Report) at MPMR_AGSHF_0054954; Knight Tr. 80:5-81:2.

⁹⁰ Derrough 7/2018 Tr. 307:15-308:7.

⁹¹ Derrough Rebuttal Report ¶ 28; Derrough Expert Report ¶¶ 71-74 & Exs. 7-8.

within Professor Cornell's range. As Mr. Derrough acknowledges, the mean "yield," or market rate, for the bond issuances was 6.23%, with a median of 6.75%.⁹² The mean interest rate for the leveraged loan issuances was LIBOR plus 473 bps, with a median of LIBOR plus 450 bps.⁹³ Moreover, all of those bond and loan issuances had call protection, suggesting the market rate would be, if anything, higher for a bond like the Replacement Notes that did not.⁹⁴ Similarly, all of the leveraged loan issuances were issued with OID (ranging from 50 to 500 bps), which Mr. Derrough notes "has the effect of increasing the overall yield to the Investors," suggesting again that the market rate would be higher for debt like the Replacement Notes that had no OID.⁹⁵

Evidently recognizing this, Mr. Derrough suggests the median rate for the bond issuances should be adjusted downward (to 5.86%, still above his range) by excluding the single issuance that had a *lower* credit rating than the Replacement First Lien Notes (Albertsons, which also had the highest interest rate, 8.00%).⁹⁶ But he cherry picks; he does not exclude the five issuances that had *higher* credit ratings (and interest rates as low as 4.25%).⁹⁷ Indeed, the bond issuance with the credit rating most similar to Momentive's (Schaeffler) had a yield of 6.75% (and call protection).⁹⁸ Likewise, Mr. Derrough seeks to adjust the mean for leveraged loan issuances downward (to LIBOR plus 435, still above his range) by, again, excluding the single issuance with the *highest* interest rate (Toys 'R' Us), while including the five issuances with *lower* interest

⁹² Derrough Expert Report Ex. 8; Cornell Rebuttal Report ¶ 48; TTX214 (chart analyzing Derrough Expert Report Ex. 8).

⁹³ Derrough Expert Report Ex. 7.

⁹⁴ Derrough Expert Report Ex. 8; TTX215 (chart analyzing Derrough Expert Report Ex. 7); Derrough 7/2018 Tr. 89:2-17.

⁹⁵ Derrough Expert Report ¶ 55; TTX215 (chart analyzing Derrough Expert Report Ex. 7); Derrough 7/2018 Tr. 94:14-95:25, 122:14-123:4.

⁹⁶ Derrough Expert Report ¶ 73 & Ex. 8; Derrough Rebuttal Report ¶ 28.

⁹⁷ Derrough Expert Report Ex. 8.

⁹⁸ Derrough Expert Report Ex. 8; Derrough 7/2018 Tr. 96:19-102:4.

rates than the committed Exit Term Loan rate of LIBOR plus 400, including an issuance with an *investment-grade* credit rating (Sensata, which had the lowest interest rate of LIBOR plus 275 bps).⁹⁹ Moreover, the only two loans to other chemical companies, which each had the same or higher credit ratings than Momentive, were issued at LIBOR plus 500 bps (Novolox) and 550 bps (Syrolution), respectively.¹⁰⁰ Indeed, although Mr. Derrough suggests that the Exit Term Loan would have been issued with no flex, eight of the 14 loan issuances he examines “flexed up” (while only one “flexed down”), including both of the other chemical-company issuances.¹⁰¹

Ultimately, Mr. Derrough asserts that he gives little weight to these new debt issuances (with higher interest rates) and instead places primary weight on the second category of “comparables” he examines, the yields implied by the trading prices for the outstanding debt of ten other chemical companies as of the Effective Date.¹⁰² Of these ten companies, he suggests that one should be excluded (Hexion), which—yet again—is the single company whose debt has a *lower* credit rating than the Replacement First Lien Notes (and the highest interest rates); at the same time, he includes six other companies whose debt had *higher* credit ratings (and lower interest rates).¹⁰³ Indeed, two of the ten companies (Avery Dennison and Eastman) had *investment-grade* ratings, with interest rates that were even *lower* than the existing 3.88% rate for the high-yield Replacement First Lien Notes (3.35% and 3.08%, respectively).¹⁰⁴

⁹⁹ Derrough Expert Report ¶ 73 & Ex. 7; Derrough 7/2018 Tr. 123:7-124:18.

¹⁰⁰ Derrough Expert Report Ex. 7; Derrough 7/2018 Tr. 116:18-118:21.

¹⁰¹ TTX215 (chart analyzing Derrough Expert Report Ex. 7).

¹⁰² Derrough Expert Report ¶¶ 65-70 & Ex. 6; Derrough Rebuttal Report ¶¶ 25-28; Derrough 7/2018 Tr. 113:23-115:3, 137:4-141:12.

¹⁰³ Derrough Expert Report ¶¶ 66-68 & Ex. 6; Derrough Rebuttal Report ¶¶ 26; Derrough 7/2018 Tr. 144:6-22, 250:13-251:4, 253:7-18.

¹⁰⁴ Derrough Expert Report ¶¶ 66-68 & Ex. 6; Derrough Rebuttal Report ¶ 27; Derrough 7/2018 Tr. 242:12-243:11, 245:8-246:23.

Of the nine companies he considered (after excluding Hexion), Mr. Derrough acknowledges that “some had credit statistics superior to MPM,” and therefore he “relied most heavily” on four (Kraton, Minerals Technology, Chemtura, and Huntsman) that “had smaller scale and somewhat higher leverage.”¹⁰⁵ There are a host of problems with these purported “comparables.” For example, only one of those companies (Kraton) had debt with the same (or slightly higher) credit rating as the Replacement First Lien Notes, while the other three (Chemtura, Huntsman, Minerals Technology) had significantly higher credit ratings.¹⁰⁶ Furthermore, although Mr. Derrough criticizes Professor Cornell for looking at the *floating-rate* Exit Term Loan, asserting that the “preferred market approach” is to look at “companies similar to the Company that have *fixed rate* debt,” one of the four companies Mr. Derrough “relied most heavily” on (Minerals Technology) had only *floating-rate* debt (a \$1.5 billion LIBOR-based term loan), not fixed-rate debt.¹⁰⁷ In addition, while Mr. Derrough asserts that he focused on these four companies because they had “smaller scale,” one of Mr. Derrough’s four primary “comparables” (Huntsman) had revenue and EBITDA approximately *four to seven* times higher than Momentive’s.¹⁰⁸ As BOKF will show at trial, there are many more flaws in this analysis.

¹⁰⁵ Derrough Rebuttal Report ¶ 27; Derrough 7/2018 Tr. 160:2-161:17.

¹⁰⁶ Derrough Expert Report Ex. 6. Mr. Derrough’s report incorrectly states that Minerals Technologies’ debt was unrated; in fact, it was rated BB and Ba3 by Standard & Poor’s and Moody’s, respectively. TTX218 (Bloomberg screenshot of Minerals credit rating); Derrough 7/2018 Tr. 167:14-171:17, 172:17-173:24, 178:18-181:24.

¹⁰⁷ Derrough Rebuttal Report ¶¶ 15, 25 (emphasis added); JX243 at 14; Derrough 7/2018 Tr. 161:23-167:13. Mr. Derrough also lists floating-rate debt for Chemtura and Huntsman. Derrough Expert Report Ex. 6; Derrough 7/2018 Tr. 177:15-24, 180:20-181:3.

¹⁰⁸ Derrough Expert Report Ex. 6; Derrough Rebuttal Report ¶¶ 21, 27; Derrough 7/2018 Tr. 181:25-184:7.

In the end, Mr. Derrough could not explain how he weighed the various factors he considered to arrive at his ultimate conclusion that the market rate for the Replacement First Lien Notes was between 5.5% to 5.7%, nor how anyone else could replicate his analysis.¹⁰⁹

III. A CATCH-UP PAYMENT IS DUE IF THE MARKET RATE IS APPLIED

If the Court determines that a market rate of 6.47% or 6.99% should apply, the catch-up payment as of August 22, 2018 is \$121.7 million or \$147.5 million, respectively.¹¹⁰ The parties' only disagreement is whether the calculation should include compound interest. Professor Cornell compounded interest at the market rate; Mr. Derrough included no compound interest.¹¹¹

Compounding at the market rate is necessary to make the Noteholders whole. If the Replacement Notes had borne the market rate as of the Effective Date, the Noteholders would have received the incremental interest payments twice a year during the past four years and could have reinvested those payments. The failure to receive those incremental interest payments on a timely basis was a forced loan by the Noteholders as of the Effective Date, and thus Momentive's borrowing costs—i.e., the market rate—is appropriate.¹¹² Moreover, the indenture requires Momentive to pay interest on late interest payments at the Notes' contract rate.¹¹³ Even without such a contractual provision, New York law provides for prejudgment interest on missed contractual payments at 9%.¹¹⁴ Finally, the Bankruptcy Code itself requires that, in a cram

¹⁰⁹ Derrough 7/2018 Tr. 78:3-81:9, 247:7-249:9.

¹¹⁰ Cornell Expert Report ¶¶ 66-69 & Exs. 16A-16B.

¹¹¹ Cornell Expert Report ¶¶ 67-68 & Exs. 16A-16B; Derrough Rebuttal Report ¶¶ 8, 25, 29 & Ex. 1; Derrough 7/2018 Tr. 31:23-35:14, 36:24-42:4, 44:7-45:17.

¹¹² Cornell Expert Report ¶ 68.

¹¹³ Cornell Expert Report ¶ 68; JX57 (Indenture) Ex. A-5; N.Y. Gen. Oblig. Law § 5-527; *NML Capital v. Republic of Argentina*, 952 N.E.2d 482, 488-89, 494-95 (N.Y. 2011); *Themis Capital, LLC v. Democratic Republic of Congo*, 626 F. App'x 346, 349 (2d Cir. 2015); *4 B's Realty 1530 CR39, LLC v. Toscano*, 818 F. Supp. 2d 654, 660-61 (E.D.N.Y. 2011).

¹¹⁴ N.Y. C.P.L.R. 5001(a), 5004; *NML*, 952 N.E.2d at 488-89, 494-95.

down, a secured creditor receive payments over time that, have a value, “as of the effective date of the plan,” equal to the secured claim. 11 U.S.C. § 1129(b)(2)(A)(i)(II). Given the delay in payment of the market rate of interest in this case, that can only happen if the catch-up payment includes compounding.

CONCLUSION

The Court should grant judgment in favor of the Trustee and grant such other and further relief as the Court deems just and proper.

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New York, New York

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