

**IN THE UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA**

District Court Case No.

In re:

Bankruptcy Court Case No.

Polaroid Corporation, et al.,

08-46617 (GFK)

Chapter 11 Case

Debtors.

(includes:

Polaroid Holding Company;

Polaroid Consumer Electronics, LLC;

Polaroid Capital, LLC;

Polaroid Latin America I Corporation;

Polaroid Asia Pacific LLC;

Polaroid International Holding LLC;

Polaroid New Bedford Real Estate, LLC;

Polaroid Norwood Real Estate, LLC;

Polaroid Waltham Real Estate, LLC)

**ACORN'S MEMORANDUM IN SUPPORT OF EMERGENCY MOTION FOR
STAY PENDING APPEAL**

Acorn Capital Group, LLC (“Acorn”) respectfully moves the District Court for a stay of the Order Authorizing: (I) Sale of Certain of the Debtors’ Assets, Free and Clear of Liens, Claims, Encumbrances, and Interests; and (II) the Granting of Related Relief entered in the above-captioned bankruptcy case on April 17, 2009, (“Order”), pending completion of Acorn’s appeal of the Order.

Introduction

Acorn timely filed its Notice of Appeal of the Order to the District Court on April 20, 2009, and filed its Motion for Stay Pending Appeal to the Bankruptcy Court on April 21, 2009, pursuant to Bankruptcy Rule 8005. The Bankruptcy Court heard and denied Acorn's Motion for Stay Pending Appeal on April 22, 2009, and entered its Order to that effect on April 23, 2009.

Accordingly, Acorn may now request the District Court to stay the Order approving the sale of Polaroid Corporation and its affiliates' (collectively, "Debtors" or "Polaroid") assets free and clear of Acorn's liens under 11 U.S.C. § 363 pending Acorn's appeal. Fed. R. Bankr. P 8005. Acorn, who is owed \$281 million and who holds first priority liens against Polaroid's U.S. Inventory, Accounts and North American Trademarks, has raised two critically important statutory issues on appeal from the Bankruptcy Court's Order approving the Debtors' motion for the sale of Polaroid's assets free and clear of Acorn's liens.

First, Acorn's appeal raises the important question of the proper standard that should apply to determine whether there is a bona fide dispute that would enable the Debtors to sell Polaroid's assets free and clear of liens under 11 U.S.C. § 363(f)(4). Acorn contends that the Debtors were required to make some evidentiary showing in order to meet their burden of establishing a bona fide dispute. In connection with perhaps the most bizarre sale proceeding ever to occur in any modern bankruptcy proceeding, the Court allowed the Debtors to meet their statutory burden based solely upon frivolous

pleadings and baseless allegations, which had been thoroughly refuted by unrebutted evidence placed in the record by Acorn.

Second, Acorn's appeal from the Order challenges the Court's approval of the sale of Polaroid's assets free and clear of PAC Funding LLC's ("PAC") liens and claims in which Acorn has a significant and controlling interest. The Debtors failed to establish any basis for selling assets free and clear of PAC's liens and claims under 11 U.S.C. § 363(f)(2). In particular, the Debtors have failed to establish that PAC has consented to this sale. On the contrary, the unrebutted and irrefutable record establishes that PAC cannot consent to the sale free and clear of its liens and interests, *inter alia*, without Acorn's consent—and Acorn has not consented.

In addition, Acorn was denied due process of law by the Bankruptcy Court, which abruptly deprived Acorn of any meaningful opportunity to present evidence or arguments in support of its objections. From the time of the initial February 18, 2009 bidding procedures hearing, the Bankruptcy Court repeatedly refused to address the merits of Acorn's arguments under 11 U.S.C. §§ 363(f)(4) & (2), asserting these issues were "not ripe until a sale is actually presented to the Court for approval." (*See* Affidavit of Thomas H. Boyd ("Boyd Aff.") Ex. B at 86.) At the March 26, 2009, protective order hearing the Bankruptcy Court again refused to address the merits of Acorn's objections and, in connection with its ruling on the Debtors' Motions for a Protective Order, the Court stated for the first time that, in evaluating whether to permit the sale of Polaroid's assets free and clear of Acorn's liens, its focus would be to determine whether the

Complaint against Acorn would withstand a motion to dismiss under Rule 12(b)(6). (*Id.* Ex. E at 89-92.)

Finally, at the April 16, 2009, Sale Hearing (the “Sale Hearing”), Acorn was deprived of any meaningful opportunity to make its 11 U.S.C. §§ 363(f)(4) & (2) arguments. The Bankruptcy Court repeatedly cut Acorn’s counsel off during oral argument, warned counsel to “get on with [it]” and stated – in direct contravention of its decision on March 26 –that Acorn’s counsel was “not arguing a motion for dismissal under [Rule] 12(b)(6)” and would not permit Acorn to put on evidence. (*See* Boyd Aff. Ex. C at 304-305.) When Acorn’s counsel attempted to argue that no bona fide dispute as to Acorn’s liens on Polaroid’s assets exists, even when applying the Court’s previously articulated 12(b)(6) standard, the Court stated “Stop wasting time haggling with me over whether I’m going to cut you off or I will right now and just rule on the basis of your written submissions. It has been a long day. . . . Get on with your argument right now.” (*Id.*) At the April 22, 2009 hearing on Acorn’s Motion to Stay Pending Appeal in the Bankruptcy Court, the Court went so far as to acknowledge that it cut Acorn’s counsel short on his argument at the April 16, 2009 hearing. (*See* Boyd Aff. Ex. D at 68.)

Acorn has appealed the Bankruptcy Court’s Order as to each of these separate and independent grounds upon which Acorn is entitled to relief from the terms of the sale of Polaroid’s assets free and clear of Acorn’s and PAC’s liens and claims. Needless to say, Acorn would suffer substantial harm if its direct lien and its indirect lien (through PAC) are stripped from these assets. Moreover, the attachment of Acorn’s interests to the sale proceeds is wholly inadequate because, *inter alia*, the sale of the assets has failed to

maximize the value of these assets, in and of themselves, as well as in connection with the operation of the business as a going concern.

In contrast, the Debtors will not suffer irreparable harm if the sale of these assets is stayed pending Acorn's appeal. In fact, the Debtors' argument that Acorn's liens against Polaroid's assets is the subject of a bona fide dispute was based exclusively on the frivolous and unsubstantiated allegations contained in their Complaint, which constitutes a shameless and reprehensible attempt to portray Acorn, an innocent fraud victim, as a perpetrator of fraud. The Debtors should not have been permitted to rest on the irresponsible and baseless speculation contained in their Complaint without coming forward any evidence to validate their assertions. Finally, the public interest will be served if the Court were to grant the stay pending appeal.

Accordingly, Acorn respectfully requests the District Court to grant its motion for a stay of the sale of the assets pending its appeal of the Order.

Background Facts

A. The PAC Funding Loan.

On November 1, 2004, PAC Funding, LLC ("PAC") and Acorn entered into a credit agreement, as subsequently amended on December 14, 2005, September 6, 2006, January 19, 2007, October 29, 2007, and May 12, 2008, whereby Acorn agreed to make revolving loans to PAC up to a \$300 million commitment (the "PAC Credit Agreement"). Under the PAC Credit Agreement, the proceeds of each loan from Acorn would be used to purchase specifically identified goods (e.g. consumer electronics) from retailers, distributors or manufacturers, and each loan would be collateralized by accounts

receivable generated from the resale of those same goods to recognized retailers at a mark-up or profit of no less than 10%. Upon each advance from Acorn, PAC was required to deposit cash equal to 10% of the requested financing into a blocked account which served as additional cash collateral for each loan. In effect, the net financing amount approximated 80% of the expected account receivable to be generated upon resale of the goods in question, a reasonably conservative loan arrangement.

Also on November 1, 2004, PAC and Acorn entered into a security agreement (the “PAC Security Agreement”) pursuant to which PAC granted Acorn a first priority security interest in PAC’s assets, which secured the full amount of PAC’s debt to Acorn. Specifically, PAC’s assets include all: Accounts Receivable; Investment Property; Contract Rights, Commercial Tort Claims, cash, Chattel Paper, Deposit Accounts, Equipment, General Intangibles, Goods, Health-Care-Insurance Receivables, Instruments, Inventory, Letter of Credit Rights and Supporting Obligations; Documents; and Proceeds or products of the foregoing.

In connection with the PAC Credit Agreement and PAC Security Agreement, PAC and Acorn entered into two separate blocked account agreements with Crown Bank and Associated Bank to perfect Acorn’s security interest in those accounts (the “Blocked Account Agreements”). Between 2004 and 2007, PAC borrowed from and repaid Acorn more than \$3 billion under the PAC Credit Agreement.

B. The February Polaroid Loan.

Sometime between December 2007 and February 2008, Polaroid approached Acorn and requested working capital financing. Specifically, Polaroid’s current Chief

Executive Officer, Mary Jeffries, requested that Acorn make available to Polaroid a revolving loan facility and purchase order financing of up to \$200 million. Jeffries, with the assistance of Polaroid's then-President and Chief Financial Officer, Thomas Beaudoin, represented that Polaroid required such financing to build its inventory of branded electronics, implement new product lines and expand into foreign markets. Jeffries and Beaudoin also represented that Polaroid was negotiating the terms of potential financing with other lenders, including Accord Financial and Gordon Brothers.

Given the size of the requested loan and the time necessary to undertake diligence and documentation, Acorn was unwilling to open a permanent working capital loan facility at that time. Acorn was willing, however, to make certain short-term secured loans to fund Polaroid's immediate working capital needs in the interim.

In response to various diligence requests, Polaroid furnished certain business information to Acorn, including financial statements, inventory and accounts receivable reports and financial projections illustrating the use of loan proceeds by Polaroid. Polaroid also furnished Acorn with a draft of its 2007 unaudited financial statements. The diligence information provided to Acorn by Polaroid purported to reflect that Polaroid maintained substantial shareholder equity.

During separate conference calls on February 22 and 25, 2008, Jeffries and David Baer (who, in addition to Polaroid, was also General Counsel to all other Petters related entities) negotiated the terms of Polaroid's initial loans from Acorn. On February 29, 2008, Polaroid's first loan from Acorn, in the principal sum of \$15 million, was memorialized in the following agreements, among others:

- Promissory Note in the principal sum of \$15 million with a term of 45 days.
- Security Agreement whereby Polaroid granted Acorn a security interest in its U.S. Inventory and Accounts to secure (i) amounts owed under the Promissory Note and (ii) the Blocked Account Obligation,” i.e., the obligation of PAC to replenish the Blocked Account with cash of up to \$28 million.
- Subordination Agreement whereby Petters Company, Inc., Petters Company, LLC, Petters Capital, LLC, Thomas Petters, Inc. agreed to subordinate their rights and claims in and to Polaroid’s assets (the “Subordination Agreement”).
- PAC and Acorn also entered into a limited forbearance agreement (the “Forbearance Agreement”), pursuant to which Acorn agreed to forbear from exercising its remedies under the PAC Credit Agreement and the PAC Security Agreement. Pursuant to the terms of the Forbearance Agreement, Acorn released to PAC more than \$20 million being held in the Blocked Accounts. Upon information and belief, some portion or all of the funds released from the Blocked Accounts was advanced by PAC to or for the benefit of Polaroid.

Under the February loan documents, Polaroid pledged its U.S. Inventory and Accounts to secure its obligations to repay the \$15 million loan and its limited guaranty of PAC’s obligation to maintain cash of at least \$28 million in the Blocked Account (which PAC failed to do).

C. The April Polaroid Loan.

After receiving the initial \$15 million loan from Acorn, Polaroid continued to solicit additional financing from Acorn. Polaroid insisted that either a permanent financing or a strategic transaction would facilitate repayment of any additional loans from Acorn. More specifically and in addition to its other highly touted financing prospects: (a) Petters represented that Polaroid was on the verge of a major brand licensing deal in India; (b) Jeffries represented that Polaroid was in the process of

negotiating several intellectual property licensing agreements that would generate cash with which Polaroid could repay any loan from Acorn; and (c) Baer represented that he was negotiating terms for sale of various licensing agreements which would provide the cashflow to repay Acorn loans.

Showcasing the value of its intellectual property, on March 11, 2008, Polaroid furnished Acorn with a valuation by the investment advisory firm Duff & Phelps which ascribed a value of at least \$350 million to Polaroid's intellectual property, which, internally, Acorn discounted heavily for purposes of calculated underwriting adequacy, given Polaroid's illiquidity and market niche of branding. Polaroid produced additional and updated diligence and financial information, which reinforced the value of its assets (and, therefore, its solvency), while Jeffries and others maintained the idea that a sale or license of Polaroid intellectual property was near.

As with the February loan, Jeffries and Baer were the lead negotiators for Polaroid. On April 18, 2008, Polaroid's second loan from Acorn, in the principal sum of \$10 million, was memorialized in the following agreements, among others:

- Promissory Note in the principal sum of \$10 million with a term of 120 days.
- Amended and Restated Security Agreement whereby Acorn was granted a security interest in Polaroid's U.S. Inventory and Accounts. Polaroid granted Acorn collateral to secure (i) amounts owed under the Promissory Note and (ii) the Blocked Account Obligation," i.e., the obligation of PAC to replenish the Blocked Account with cash of up to \$28 million.
- On April 18, 2008, Acorn advanced \$10 million to Polaroid.

Under the documents memorializing the February and April loan transaction, Polaroid's U.S. Inventory and Accounts were pledged to secure (i) two loans totaling \$25 million and (ii) the Blocked Account Obligation totaling \$28 million.

D. The May Polaroid Transaction.

In late April and early May 2008, Acorn engaged in further negotiations with Jeffries and Baer regarding Polaroid's continued need for financing. Unfortunately, by this time PAC had again defaulted on its loan obligations. In view of this default and the general economic decline at that time, Acorn decided to convert its revolving loan to a fully amortizing term loan facility. After further negotiations, on May 12, 2008, a Fifth Amendment to the PAC Credit Agreement was entered into whereby Polaroid and PAC were afforded an additional 18 months to repay their loan obligations (including the Polaroid loan) which then totaled more than \$281 million.

Under the Fifth Amendment, PAC was given the flexibility of remitting only 50% (rather than 100%) of the proceeds received on its alleged receivables and Polaroid would be given the right to prime Acorn's first lien against U.S. Inventory, Accounts and U.S., Canadian and Mexican Trademarks (collectively, "North American Trademarks") with a new working capital loan facility from another lender up to \$75 million. There was extensive correspondence required to negotiate the Fifth Amendment, with conference calls throughout the period May 5-12, 2008. In exchange for substantial direct and indirect financial benefits from Acorn, Polaroid agreed to guaranty PAC's obligations to Acorn and to secure that guaranty with additional collateral, namely a first priority lien against Polaroid's North American Trademarks. In connection with the Fifth

Amendment to the PAC Credit Agreement, Polaroid and Acorn entered into a Second Amended and Restated Security Agreement (the “Polaroid Security Agreement”).

E. Events Preceding Polaroid’s Bankruptcy Filing.

PAC made its regularly scheduled payment to Acorn in June and July of 2008 under the terms of the Fifth Amendment. Throughout the summer of 2008, Polaroid, through Jeffries, Beaudoin and others, continued to request that Acorn establish a permanent working capital loan facility for Polaroid and represent to Acorn that Polaroid was negotiating the terms of potential financing with other lenders, including Accord Financial and Gordon Brothers. Acorn evaluated additional diligence information furnished by Polaroid, including financial statements, reports and projections.

On August 1, 2008, PAC failed to make its regularly scheduled payment to Acorn pursuant to the Fifth Amendment, and on August 13, 2008, Acorn notified PAC of its default. On August 14, 2008, Acorn filed a complaint for breach of contract against Thomas J. Petters in the Southern District of New York captioned *Acorn Capital Group, LLC, v. Thomas J. Petters*, No. 08-CIV-7236 (S.D.N.Y. Aug. 14, 2008).

Subsequent to August 14, Petters introduced to Acorn an affiliate of the Fortress Investment Group (a publicly traded hedge fund) (“Fortress”). The affiliate, Drawbridge Special Opportunities Advisors, LLC (“Drawbridge”), made a written proposal to purchase 100% of the debt owed to Acorn by PAC (and Polaroid), Petters Aviation and Petters Aircraft Leasing for a purchase price of 90% of \$310 million outstanding in Petters related debt. The proposal, however, was subject to a brief period of diligence and an agreement by Acorn to forbear from exercising its rights against PAC and others

while the parties formalized and consummated the purchase and sale. Acorn and Drawbridge memorialized their intentions in a letter agreement on August 25, 2008.

On September 9, 2008, Acorn and Petters agreed to extend the time for Petters to respond to Acorn's Complaint to October 1, 2008. Acorn only so stipulated in view of its ongoing negotiations with Drawbridge. On September 24, 2008, the Federal Bureau of Investigation together with the Internal Revenue Service-Criminal Investigation Divisions and the United States Postal Inspection Service, executed a search warrant and seized records related to certain entities owned by Petters. Also on September 24, 2008, Acorn received a letter from Drawbridge terminating its proposal to purchase the Petters related debt from Acorn. At no time prior to September 24, 2008, was Acorn aware of anything that would suggest any fraud or impropriety involving Petters, PAC, Polaroid or any affiliate thereof.

On October 3, 2008, Petters was arrested on charges of mail and wire fraud, money laundering and conspiracy. On October 6, 2008, the District of Minnesota placed the various affiliated Petters entities into receivership and appointed Kelley to serve as their receiver. By Order dated October 14, 2008, the District Court amended the receivership to place Kelley as receiver for Petters and other individuals. In an Order dated December 12, 2008, the District Court clarified that it intended Polaroid to be included within the group of entities subject to the receivership.

On December 1, 2008, Petters was indicted by a federal grand jury on charges of mail fraud, wire fraud, money laundering and conspiracy in violation of 18 U.S.C. §§ 371, 1343, 1956 and 1957.

F. Polaroid's Bankruptcy Filing.

On December 18, 2008, Polaroid and its affiliated companies filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code. As of the petition date, Acorn was owed more than \$281 million by Polaroid, and Acorn's claim is secured by a first priority lien against Polaroid's U.S. Inventory, Accounts and its North American Trademarks.

G. The Sale Motion, Bidding Procedures And Procedural Posture.

On January 24, 2009, the Debtors and PHC Acquisitions, LLC (the "Proposed Purchaser") entered into an Asset Purchase Agreement (the "Purchase Agreement"). Under the Purchase Agreement, the Proposed Purchaser agreed to purchase substantially all of the Debtors' assets, free and clear of all liens, claims and encumbrances for a purchase price of \$42 million.

On January 28, 2009, the Debtors filed their motion seeking, among other things, approval for the Purchase Agreement as well as bidding and auction procedures (the "Bidding Procedures") for the proposed sale (the "Sale Motion"). (*See* Docket No. 71.) At paragraph 23 of the Sale Motion, the Debtors represented that, *inter alia*, PAC has not objected to the relief requested in the motion. As further discussed below, PAC cannot consent to the proposed sale without Acorn's consent, which Acorn did not provide. (*Id.*) At paragraph 24 of the Sale Motion, the Debtors stated their intention to commence adversary proceedings against Acorn to "(i) set aside, avoid and recover certain fraudulent and preferential transfers made and obligations incurred to or for the benefit of those creditors; (ii) obtain declaratory relief and a determination relative to the validity,

extent, nature and proprietary of liens and agreements delivered in favor of Acorn;” and “(iii) disallow, subordinate and/or recharacterize claims that have been or may be asserted against the bankruptcy estates by Acorn[.]” (*Id.*)

On February 12, 2009, the Debtors commenced an adversary proceeding against Acorn with the Adversary Complaint (the “Complaint”). The Complaint alleges that the pre-petition loan transactions between Polaroid and Acorn were fraudulent and, therefore, avoidable. 11 U.S.C. §§ 544(b), 548, 550(a), 551, 1107 and Minn. Stat. § 513.41 et seq. In a shocking and patently frivolous effort to cast a fraud victim as the perpetrator of fraud, the Debtors repeatedly asserted that Acorn knew of and was complicit in the massive fraud perpetrated by Petters. (*See* Docket No. 99.)

On February 13, 2009, Acorn objected to the Bidding Procedures asserting that the Sale Motion could not be allowed to proceed with a sale free and clear of Acorn’s and PAC’s liens because the Debtors failed to meet their burden to produce facts demonstrating either consent from Acorn or the existence of a bona fide dispute under 11 U.S.C. § 363(f)(4) and (2). As a result, those assets should not be sold free and clear of those liens unless Polaroid could establish a legal basis upon which to do so. (*See* Docket No. 106.)

On February 18, 2009, the Court heard arguments concerning the Bidding Procedures. Acorn argued that, under *In re Gaylord Grain L.L.C.*, 306 B.R. 624, 627 (8th Cir. B.A.P. 2004), the Debtors have an obligation to produce *some evidence* demonstrating a factual basis for the existence of a bona fide dispute to sell Polaroid’s assets free and clear of Acorn’s liens. (*See* T.39.) The Court would not address the merits of its

arguments under 11 U.S.C. §§ 363(f)(4) & (2), stating that it “need not reach the very specific discreet statutory issue on [the] merits of whether there is a bona fide dispute over Acorn Capital’s claim within the meaning of 363(f)(4) [because] it is technically not ripe until a sale is actually presented to the Court for approval.” (Transcript of Hearing (“T”) 86.) (For Order *see* Docket No. 118.)

H. Polaroid’s Refusal To Engage In Discovery Or To Divulge The Basis For Facts Alleged In Its Complaint.

Following the Court’s approval of the Bidding Procedures, Acorn repeatedly sought discovery to ascertain the basis for the allegations contained in the Complaint. Polaroid avoided any such discovery and withheld information that would (presumably) be relevant to their allegations. (*See* Docket No. 183, Affidavit of Michael A. Rosow in Support of Acorn’s Objection to 363 Sale ¶2.) Specifically, Acorn’s counsel endeavored to meet with Polaroid’s counsel to discuss these matters on numerous occasions. Despite Acorn’s efforts, Polaroid refused to cooperate or produce relevant information. (*Id.* ¶3.)

Accordingly, on March 16, 2009, the same date Acorn filed its Answer and Counterclaim to the Adversary Complaint, Acorn’s counsel served notices of taking depositions of Jeffries and Baer for March 23 and 24, 2009, respectively, and arranged for service of a subpoena on Baer on March 16, 2009. (*Id.* ¶4.) Acorn sought to depose Jeffries in her capacity as Chief Executive Officer for Polaroid, the individual who must have authorized the filing of the Complaint. Acorn also sought to depose Baer as Polaroid’s former General Counsel, who along with Jeffries, was intimately involved in soliciting financing from Acorn and negotiating the agreements the parties entered into to

secure that financing. (*Id.* ¶5.) Rather than produce these witnesses who have first hand knowledge of the pre-petition transactions, Polaroid refused and moved the Court for a protective order to prevent the depositions from going forward. (*Id.* ¶6.)

On March 26, 2009, the Court granted the Motions for Protective Order, thereby preventing Acorn from deposing Jeffries and Baer in connection with Acorn's objection. Notably, in connection with the Court's ruling, the Court stated for the very first time that, in evaluating whether to permit the sale of Polaroid's assets free and clear of Acorn's lien, its focus would be to determine whether the Complaint against Acorn would withstand a motion to dismiss under Rule 12(b)(6). (Boyd Aff. Ex. E at 86.)

After securing a protective order for Jeffries, the Debtor attempted to offer her testimony by a "verified" omnibus response, which did not address the facts contained in the Affidavit of Marlon Quan filed in connection with Acorn's Objection to the 363 Sale. When it became clear that the Debtors were having significant difficulty executing their sale process, Polaroid filed a motion to offer Jeffries as a witness at the Sale Hearing, but that motion sought to strictly confine the scope of Jeffries' testimony and deprive parties from utilizing cross examination.

I. Acorn's Supplemental And Continuing Objections To Polaroid's 363 Sale Proposal.

Acorn filed supplemental and continuing Objections to 363 Sale on March 26, 2009, and April 3, 2009, reaffirming its objections to the Debtors' proposed sale of Polaroid's assets free and clear of Acorn's and PAC Funding's liens. Following the Sale Hearing on April 16, 2009, the Court overruled Acorn's Objections and approved the

sale. In overruling Acorn's Objection, the Court concluded that it did not need to consider evidence and that it did not need to evaluate the Complaint under a 12(b)(6) standard.

At that hearing, after two months of waiting based on the Court's instruction that they were "not ripe" until the Sale Hearing, Acorn was again deprived of any meaningful opportunity to make its 11 U.S.C. §§ 363(f)(4) & (2) arguments or present evidence. After 7:00 p.m., when Acorn was finally permitted to present limited argument, the Court repeatedly cut Acorn's counsel off his argument, demanded that he "get on with [it]" and "warn[ed]" Acorn's counsel that he would be "on sudden death overtime." (Boyd Aff. Ex. C at 304-05.) The Court went on to chastise Acorn's counsel for attempting to argue "a motion for dismissal under [Rule] 12(b)(6)" even though this is the very standard the Court had stated would be applied to determine whether the Debtors had met their burden to establish a bona fide dispute. (*Id.*)

Thus, after a sale process that started on March 30 and consumed approximately five full days, Acorn was afforded only a few limited minutes to present a case in defense of its nearly \$300 million claim. The Court subsequently entered its formal written Order in this regard on April 17, 2009.

Acorn promptly filed its Notice of Appeal of the Order on April 20, 2009, and filed its Motion for Stay Pending Appeal to the Bankruptcy Court on April 21, 2009. The Bankruptcy Court denied Acorn's Motion for Stay Pending Appeal on April 22, 2009.

Legal Argument

In determining whether a stay is proper, the District Court shall consider the following factors: “1) the likelihood of success on the merits of the appeal; 2) the injury suffered by the applicant in denying the stay; 3) the injury to the appellee by granting a stay; and 4) the harm to the public interest.” *In re Howley*, 38 B.R. at 315 (citations omitted). “These factors are *not applied in a vacuum* but instead *must be viewed in light of the importance of the right to appeal and preservation of the status quo during the appeal.*” *Id.* (emphasis added). Thus, “[i]n most situations, . . . the Court will treat these factors as interests to be considered and balanced in deciding whether to grant a stay rather than as absolute prerequisites for a stay.” *In re Dakota Rail, Inc.*, 111 B.R. at 820 (citation omitted).

I. ACORN IS LIKELY TO SUCCEED ON THE MERITS OF THE APPEAL.

In their effort to sell substantially all of their assets, the Debtors asked the Bankruptcy Court to ignore the statutorily and constitutionally protected property rights that Acorn has in the Debtors’ assets. Rather than making any effort to obtain Acorn’s consent to the proposed transactions or complying with the plain language of 11 U.S.C. § 363(f), the Debtors made a series of baseless accusations in an attempt to conjure up a bona fide dispute over the validity and extent of Acorn’s liens and claims. Based only on these false accusations, the Debtors successfully prevailed upon the Bankruptcy Court to disregard Acorn’s security interest in the Debtors’ assets and its right to be repaid more than \$281 million by Polaroid. This constituted error as these unsupported accusations did not provide any basis to sell the Debtors’ assets free and clear of Acorn’s liens.

Acorn has raised two significant issues in its appeal of the Order granting the Debtors' motion for approval of the sale of Polaroid's assets: (1) whether Polaroid has met its burden to establish a bona fide dispute as to Acorn's lien, and (2) whether Polaroid has met its burden to establish consent to the sale free and clear of PAC's lien. Both of the issues primarily involve questions of law that will be reviewed *de novo*. To the extent either of these issues might involve questions of fact, the unrebutted record favors Acorn. Acorn believes there is a high likelihood that it will succeed in its appeal of the Order approving the sale of Polaroid's assets free and clear of Acorn's and PAC's liens.

Moreover, in addition to Acorn's contention that the Bankruptcy Court clearly erred in its findings of fact and conclusions of law on these issues under 11 U.S.C. § 363(f), Acorn also was deprived of due process because the Bankruptcy Court at no time provided Acorn with a sufficient opportunity to present its arguments on these important issues, and the Court did not provide these issues with sufficient time and attention.

In order to establish a likelihood of success on appeal, the moving party need only show it has a "substantial case" or a "strong case on appeal." *In re Miraj & Sons*, 201 B.R. 23, 26-27 (Bankr. D. Mass. 1996); *see also In re Texas Equip. Co.*, 283 B.R. 222, 227 (Bankr. N.D. Tex. 2002)(moving party "need not always show a 'probability' of success on the merits; instead, the movant need only present a substantial case on the merits when a serious legal question is involved and show that the balance of equities weigh heavily in favor of granting the stay")(citations & quotations omitted).

Particularly “[w]ith respect to questions of law, . . . especially questions involving the application of law, or when the law has not been definitively addressed by a higher court, the movant more easily satisfies the first element” of establishing a likelihood of success on appeal. *In re Texas Equip. co.*, 283 B.R. at 227. Applying these standards and principles, this is a “substantial case” and Acorn meets its burden of showing the requisite likelihood of success on appeal.

Pursuant to 11 U.S.C. § 363(f), the Debtors may sell their assets outside of the ordinary course of business:

free and clear of any interest in such property of an entity other than the estate, only if –

- (1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;
- (2) *such entity consents*;
- (3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
- (4) *such interest is in bona fide dispute*; or
- (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

In the Sale Motion, the Debtors acknowledged that they had the burden to establish that at least one of these subsections was satisfied with respect to each “interest” affected by the Sale Motion. (*See* Docket No. 71 ¶ 24.) The Debtors argued that Acorn’s claims and liens were subject to a bona fide dispute, and, therefore, the Debtors claimed they could sell these assets free and clear of Acorn’s liens under subsection (f)(2). The Bankruptcy Court ruled in favor of the Debtors on this issue. Acorn’s appeal will focus

on the proper standard that should have been applied to determine whether bona fide dispute exists. Acorn has argued that the Debtors must make some evidentiary showing in order to meet their burden of establishing a bona fide dispute. The Bankruptcy Court disagreed and allowed the Debtors to meet their burden solely based upon untested pleadings, even though these pleadings and the allegations contained therein were thoroughly refuted by unrebutted evidence in the record. Courts in various jurisdictions have disagreed as to the proper standard that should be applied. The District of Minnesota and the Eighth Circuit have yet to rule on the issue. Given that the Debtors bear the burden to establish the existence of a bona fide dispute, and given that the Debtors chose to rest solely and exclusively on their pleadings—even in the face of the unrebutted evidence supplied by Acorn demonstrating defects and deficiencies in the Debtors' pleading—there is essentially a near certainty that Acorn will prevail on appeal if the reviewing court holds that Polaroid was required to make any type of evidentiary showing to establish a bona fide dispute.

In addition to seeking to sell the assets free and clear of Acorn's direct lien, the Debtors sought the Bankruptcy Court's approval to sell these assets free and clear of PAC's liens in Polaroid's assets. However, the Debtors did not offer any argument with respect to any of the subsections to support this relief. In the Sale Motion, the Debtors simply stated that PAC has not objected to the sale of the assets. This was disingenuous to say the least. PAC has not provided its consent. Indeed, PAC cannot unilaterally provide its consent to the sale of these assets free and clear of PAC's liens under subsection (f)(4). The unrebutted and irrefutable record establishes that PAC cannot

consent to the sale free and clear of its liens and interests, *inter alia*, without Acorn's consent—and Acorn has not consented. Accordingly, Acorn believes there is a high likelihood that it will prevail on this issue on appeal.

A. Acorn Is Likely To Prevail In Its Appeal Because The Debtors Failed To Establish That Acorn's Lien In The Assets Is The Subject Of A Bona Fide Dispute.

Acorn has a constitutionally protected property right as a secured creditor, which is being impaired by the sale. As such, the sale must comply with the Fifth Amendment's prohibition against deprivation of property without due process and just compensation. The sale violated the constitution as well as the applicable statute by stripping Acorn's liens in the assets without requiring the Debtors to make any evidentiary showing to establish the alleged bona fide dispute.

Acorn's security interest in Polaroid's assets and its rights to liquidate and recover the value of its collateral constitute property rights protected by the Fifth Amendment. *See In re Townley*, 256 B.R. 697, 700 (Bankr. D.N.J. 2000) ("The right of a secured creditor to the value of its collateral is a property right protected by the Fifth Amendment."); *In re Briggs Transp. Co.*, 780 F.2d 1339, 1342 (8th Cir. 1985) (protecting secured creditor's Fifth Amendment property rights); *In re Holly's, Inc.*, 140 B.R. 643, 686 (Bankr. W.D. Mich. 1992) (same).

There are constitutional limitations on any court's ability to prevent a secured party from exercising its Article 9 rights and remedies to recover the value of its collateral. The Bankruptcy Code was drafted in a manner that recognizes the constitutional property rights of secured creditors. *See Louisville Joint Stock Land Bank*

v. Radford, 295 U.S. 555, 589 (1935) (“The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment.”); *see also United States v. Security Indus. Bank*, 459 U.S. 70, 75 (1982) (“[T]he bankruptcy power is subject to the Fifth Amendment’s prohibition against taking private property without compensation.”).

Acorn holds an Article 9 security interest in the collateral of Polaroid, which constitute property rights protected by the Fifth Amendment. As of the date of the February Polaroid loan, Polaroid’s collateral secured approximately \$43 million in Polaroid and PAC obligations to Acorn. As of the date of the April Polaroid loan, Polaroid’s collateral secured approximately \$53 million in Polaroid and PAC obligations to Acorn. As of the date of the May Polaroid Transaction, Polaroid’s collateral secured Polaroid’s and PAC’s obligations to Acorn in their entirety, or approximately \$281 million. By permitting the Debtors to sell their assets free and clear of Acorn’s liens based on nothing more than mere allegations, Acorn will be deprived of its constitutionally protected property rights with no means of protecting its interests.

The Debtors’ argument that Acorn’s liens against Polaroid’s assets is the subject of a bona fide dispute was based exclusively on the unsubstantiated allegations contained in their Complaint. As Acorn pointed out in its Objection to the Sale, the Adversary Complaint filed against Acorn by the Debtors on February 12, 2009, constitutes a shameless and reprehensible attempt to portray an innocent fraud victim as a perpetrator of fraud and to disparage Acorn with false and unfounded allegations. Indeed, the Debtors’ constant reference to allegations and claims “upon information and belief” is, in

essence, an admission that they do not have any specific evidence to support their assertions. In view of the fact that one of the three people directly responsible for Acorn's loans to Polaroid is now its CEO, the Debtors should not have been permitted to rest on the baseless speculation contained in their Complaint. Jeffries, who actively solicited loans from Acorn and renegotiated the terms of those loans when Polaroid was unable to meet initial lending terms, knows full well that Acorn had absolutely nothing to do with the fraud being perpetrated by Petters and several affiliates, including Petters Group Worldwide, a company of which Jeffries was a director. Ultimately, the Complaint is nothing more than an illegitimate vehicle the Debtors have been able to successfully employ to steamroll the sale of their prime assets free and clear of Acorn's liens.

When Acorn has sought to depose Jeffries and others, such as Polaroid's former General Counsel Baer, the Debtors refused to produce those individuals. Polaroid was not prepared to deal with specific facts and admissible evidence. Rather, the Debtors successfully prevailed upon the Bankruptcy Court to grant them a protective order that barred Acorn from gaining access to these witnesses and the exculpatory evidence they would most certainly be able to provide.

Thus unburdened by true facts and actual evidence, the Debtors were free to rest on their strident claims of fraud and other intentional acts, while failing to meet their burden to plead such claims with the requisite specificity. Rather, the Debtors pleaded their claims by selectively and conspicuously ignoring the material, undisputed facts that are well known to them and based upon evidence that is well within their possession that

conclusively refutes the very claims they have asserted against Acorn. For example, it is beyond dispute that in February and April 2008, Acorn loaned \$25 million directly to Polaroid. These funds were requested by Polaroid senior management, including Jeffries, Chief Financial Officer Beaudoin, and General Counsel Baer, who represented to Acorn the funds would be used for ongoing operations. The Debtors' obligations to repay these funds and other benefits provided are lawfully secured by Acorn's legitimate liens against the Debtors' assets. At all times, Acorn acted in good faith and without knowledge of any fraudulent or improper activities on part of the Debtors or their owner, Petters. Polaroid appeared to act honestly and in good faith at the time it sought multi-million dollar loans and other financial accommodations from Acorn, and Acorn responded in kind.

In short, there is nothing *bona fide* about the dispute conjured up in the Debtors' Complaint against Acorn. Thus, the Debtors were not entitled to sell assets free and clear of Acorn's liens.

The Debtors have the burden of demonstrating that a bona fide dispute exists. *See In re Terrace Chalet Apartments, Ltd.*, 159 B.R. 821, 828 (N.D. Ill. 1993); *In re Taylor*, 198 B.R. 142, 162 (Bankr. D.S.C. 1996). The phrase "bona fide dispute" is not defined in the Bankruptcy Code. Nevertheless, courts applying § 363(f)(4) have ruled that a "bona fide dispute" exists when there is "an *objective* basis for either a factual or legal dispute as to the validity of the debt." *In re Gaylord Grain L.L.C.*, 306 B.R. at 627 (emphasis added).

Under *In re Gaylord Grain L.L.C.*, 306 B.R. at 627, the Debtors have an obligation to produce some evidence demonstrating a factual basis for a bona fide dispute. This burden of production cannot be satisfied by the unsupported, conclusory statements and allegations contained in the Complaint. While reported cases reveal a range of evidentiary requirements, it is quite clear that, at a minimum, the Debtors must produce at least some evidence illustrating the factual grounds that would be sufficient for an objective party to conclude that a good faith dispute exists. *In re Gaylord Grain L.L.C.*, 306 B.R. at 627 (“Courts utilizing this definition have held the parties to an evidentiary standard and evidence must be provided to show factual grounds that there is an ‘objective basis’ for the dispute.”).

Mere allegations unsupported by evidence are not sufficient. *In re Octagon Roofing*, 123 B.R. 583, 589-90 (Bankr. N.D. Ill. 1991) (giving detailed consideration to underlying claims in trustee’s avoidance action; which, ultimately determining theories were viable on evidence presented, court also held that mere allegations of insider preference claim did not constitute bona fide dispute); *see also In re Southwest Fla. Heart Group, P.A.*, 342 B.R. 639, 643-44 (Bankr. M.D. Fla. 2006) (holding trustee failed to establish existence of bona fide dispute and there was insufficient basis for selling property free and clear of interest). “[N]ot any alleged dispute satisfies [§ 363(f)(4)] . . . [i]t clearly entails some sort of meritorious, existing conflict.” *In re Taylor*, 198 B.R. 142, 162 (Bankr. D.S.C. 1996) (holding that “[u]nder the specific conditions of this case involving leasehold interests . . . , the Debtor has failed to meet his burden of *persuading*

the Court that the issues constituted a bona fide dispute within the meaning of § 363(f)(4)”) (emphasis added).

The mere existence of an adversary proceeding does not meet this standard *per se*; rather, “a party must articulate in [the adversary] pleading or in an argument an objective basis sufficient under the facts and circumstances of the case for the court to determine that a bona fide dispute exists.” *In re Robotic Vision Sys., Inc.*, 322 B.R. 502, 506 (Bankr. D.N.H. 2005)(finding sufficient allegations and evidence to create a bona fide dispute through: adversary proceeding complaint; motion for determination of a bona fide dispute; unsecured creditors’ joinder motion; and arguments by movant at the hearing). Thus, the Complaint, standing alone, does not establish a good faith dispute that will support a sale of the Debtors’ assets free and clear of Acorn’s liens under section 363(f)(4). *See In re Robotic Vision Sys., Inc.*, 322 B.R. at 506.

Moreover, each material allegation of Polaroid’s Complaint has been refuted, under oath, by the Affidavit of Acorn’s principal Marlon Quan which was filed in support of Acorn’s Objection. Unlike the Complaint, which largely rests “upon information and belief” of some unknown source, the Quan Affidavit unconditionally refutes any suggestion of impropriety by Acorn. Moreover, the Quan Affidavit clearly established that Acorn advanced at least \$25 million to Polaroid in February and April and that it also provided substantial indirect financial benefits at a time when Polaroid was solvent. The un rebutted testimony from Mr. Quan, vitiates both the allegations made in the Complaint and the integrity of whomever made such allegations.

The Bankruptcy Code and the Minnesota Fraudulent Transfer Act provide for two scenarios under which a transfer will be considered fraudulent: the first is where the transfer is made with actual intent to hinder, delay or defraud creditors, and the second is where the transfer is constructively fraudulent. A constructively fraudulent transfer is avoidable if all four of the following conditions are met:

- (1) there was a transfer of an interest of the debtor in property;
- (2) the transfer was made within two years of the filing of the petition, or within six years under Minnesota state law;
- (3) the debtor received less than a reasonably equivalent value in exchange for the transfer or it was made without fair consideration; and
- (4) the debtor was insolvent on the date the transfer was made.

In re Minn. Utility Contracting, Inc., 110 B.R. 414, 417 (D. Minn. 1990). The trustee or debtor in possession has the burden of proving each of these four elements by a preponderance of the evidence. *Id.*

The Debtors have not supported their claim to avoid the transfers as actually fraudulent because they have produced no evidence demonstrating the intent of Polaroid to hinder, delay or defraud any of its creditors in exchange for loans from Acorn totaling \$25 million. While Petters is alleged to have perpetrated a ponzi scheme against investors in his other businesses, Acorn is aware of no allegations that implicate Polaroid in that fraud or which suggest that Polaroid was anything other than a legitimate business that was owned (indirectly) by a dishonest person.

Likewise, the Debtors have not supported their claim to avoid the transfers as constructively fraudulent because they have produced no evidence demonstrating the

Debtors' insolvency at the time of the transfers and have produced no evidence that the pledge of collateral to Acorn was given for less than reasonably equivalent value. On the contrary, numerous allegations in the Complaint are based "upon information and belief," which is a thinly veiled attempt to legitimize and give credence to otherwise unsupportable theories advanced by apparently overzealous lawyers. The Quan Affidavit makes clear that in two separate transactions in February and April 2008, Acorn loaned \$25 million to Polaroid and gave substantial financial accommodations to its sister corporation, PAC. It is highly likely that at least one of those accommodations, the release of more than \$20 million from the Blocked Account, produced a substantial direct benefit for Polaroid. In exchange for these (and other) direct and indirect forms of consideration, Polaroid granted Acorn a first lien against its U.S. Inventory and Accounts; an arm's length bargain supported by substantial consideration (i.e., value). In a separate transaction in May, Acorn again gave Polaroid and its sister corporation substantial value when it extended and restructured payment terms which afforded both entities maximum flexibility in their stated pursuit of strategic alternatives. In exchange, Polaroid granted Acorn additional collateral (i.e., the North American Trademarks) and provided a guaranty of PAC's other obligations to Acorn. As with the prior loan transactions, the agreements reached in May 2008 were supported by ample direct and indirect value and were the result of arm's length negotiations between the parties.

Moreover, each of the transactions in question occurred at a time when Polaroid was unquestionably solvent as illustrated by its own financial statements. Importantly, any evidence demonstrating a factual basis for insolvency, lack of reasonably equivalent

value, and/or actual intent to hinder, delay or defraud, supporting the existence of a bona fide dispute, is within the Debtors' possession, custody or control. Notwithstanding this fact, the Debtors have done everything in their power to avoid discovery and to withhold whatever information they have that would support the allegations in the Complaint.

In cases such as this one, where the Court is faced with mere tangential, or unsupported allegations of a bona fide dispute, confirming a sale free and clear of liens would be inequitable. *See, e.g., In re K.C. Mach. & Tool Co.*, 816 F.2d 238, 241 (6th Cir. 1987); *In re Restaurant Assocs., L.L.C.*, No. 1:06CV53, 2007 WL 951849, at *9 (N.D. W.Va. March 28, 2007); *In re Taylor*, 75 B.R. 682, 684 (Bankr. N.D. Ill. 1987) (citing 11 U.S.C. § 303(h)(1)).

Moreover, at the time Acorn took a security interest in Polaroid's assets, it had no knowledge of Petters' illegal conduct and no reason to believe that Polaroid was insolvent. As a result, Acorn acted in good faith as that term is used in Section 548(c) and should, at the very least, be able to maintain its liens to the extent of the value it conferred upon Polaroid.

B. Acorn Is Likely To Prevail In Its Appeal Because The Debtors Failed To Meet Their Burden To Establish That Either Acorn Or PAC Consented To The Sale Of These Assets.

The Debtors lacked the consent of both Acorn and PAC to the sale of Polaroid's assets free and clear of all liens, claims and encumbrances. Acorn expressly notified the Debtors and the Bankruptcy Court that it *does not* consent to the sale of Polaroid's assets free and clear of Acorn's direct security interest on those assets. Acorn also expressly notified the Debtors and the Bankruptcy Court that it *does not* consent to the sale of the

Debtors' assets (i.e., the liens in favor of PAC), free and clear of Acorn's indirect security interest on those assets.

In the Sale Motion, the Debtors asserted that PAC does not object to the relief sought in the Debtors' Motion. *See* Motion at p. 9, ¶ 23. In fact, PAC cannot consent to the relief sought by the Debtors. PAC cannot consent to the sale of the Debtors' assets free and clear of Acorn's security interest because: (i) Article 9 and the PAC Security Agreement provide that Acorn, not PAC, has the right to consent; (ii) the Subordination Agreement specifically prohibits PAC from consenting without Acorn's written consent; (iii) doing so is a breach of PAC's duty to protect and conserve its assets for the benefit of its creditors, such as Acorn; (iv) providing such consent is outside the ordinary course of PAC's business operations and thus requires prior Bankruptcy Court approval; (v) PAC has not sought or received court approval to do so as it would be required to do under Fed. R. Bankr. P. 9019(a); and (vi) taking such an action is precluded by PAC's obligation to adequately protect Acorn's security interest in its assets.

As explained above, Acorn has a security interest in PAC's assets. PAC's assets include a \$10 million note from Polaroid, which is secured by Polaroid's assets. Pursuant to Article 9 of the U.C.C. and section 6(e) of the PAC Security Agreement, Acorn is entitled to enforce Polaroid's obligations to PAC under the \$10 million note secured by Polaroid's assets. Upon an event of default under the PAC Credit Agreement, Acorn, *inter alia*:

may enforce the obligations of an account debtor or other person obligated on collateral and exercise the rights of the debtor with respect to the obligation of the account debtor or other person obligated on collateral to

make payment or otherwise render performance to the debtor, and with respect to any property that secures the obligations of the account debtor or other person obligated on the collateral[.]

U.C.C. § 9-607(a)(3). The comments to Section 9-607 state that the section “explicitly provides for the secured party’s enforcement of the debtor’s rights in respect of . . . (other third parties’) obligations” U.C.C. § 9-607 comment 3. Thus, for example, when a debtor defaults, “the security interest in an account receivable operates as an assignment by the debtor to the secured party of the right to receive payment from the account debtor.” *Mooney v. Univ. Sym.*, 943 A.2d 108, 111 (Md. Ct. App. 2008) (citing generally § 9-607(a)(1)). In short, “[t]he assignee stands exactly in the shoes of his assignor.” *Bank of Waunakee v. Rochester Cheese Sales, Inc.* 906 F.2d 1185, 1189 (7th Cir. 1990).

Pursuant to the PAC Security Agreement, Acorn has a first priority security interest in PAC’s assets, which includes the \$10 million note secured by Polaroid’s assets. When PAC defaulted under the Forbearance Agreement, Acorn became entitled to pursue its remedies under the PAC Security Agreement. Acorn’s remedies under Article 9 of the U.C.C. and the PAC Security Agreement include the right to enforce Polaroid’s obligations to make payments or otherwise render performance to PAC under the \$10 million note. By virtue of those rights, Acorn stands in the shoes of PAC to refuse to consent to the Debtors’ sale of their property free and clear of PAC’s security interest.

Additionally, pursuant to the Subordination Agreement, PAC is not permitted to exercise any of its rights as a secured party without first obtaining Acorn’s written consent. Consenting or refusing to consent to the sale of assets in which it has a security interest is one of the rights a secured creditor, such as PAC, has in a bankruptcy

proceeding. Because Acorn has not consented in writing to the proposed sale of Polaroid, PAC lacks the authority and ability to consent. Indeed, PAC has never sought authority from Acorn to consent.

Moreover, PAC cannot consent to the sale of the Debtors' assets free and clear because doing so would be a breach of PAC's duty to protect and conserve its assets for its creditors' benefit. An insolvent debtor has a duty to protect and conserve the property in its possession for the benefit of the creditors. *In re Halux, Inc.*, 665 F.2d 213, 216 (8th Cir. 1981); *In re Schwen's, Inc.*, 20 B.R. 638, 641 (D. Minn. 1982). This duty includes administering the bankruptcy estate for the creditors' benefit. *In re Schwen's, Inc.*, 20 B.R. at 641. In doing so, the administrator may not have an adverse interest, or be in active competition between two interests where one interest can only be served at the expense of the other. *In re J & M Dev. of Cass Co., Inc.*, 2004 WL 1146451, at *3 (Bankr W.D. Mo., May 19, 2004).

According to PAC's schedules, PAC has only approximately \$12 million in assets and over \$300 million in liabilities, making PAC insolvent. Acorn is PAC's largest creditor with approximately \$281 million in claims for unpaid and outstanding loans to PAC. The remaining two creditors are affiliates of PAC. PAC owes Acorn a duty to act in Acorn's interests by protecting and conserving its assets for the benefit of Acorn and other creditors.

As Chapter 11 Trustee of PAC, Kelley (represented by Lindquist & Vennum, which is also counsel for Polaroid) is obligated to act in both the best interests of PAC and its creditors in connection with evaluating the proposed sale. Kelley has also been

involved in an uncertain capacity with the Debtors in evaluating the sale. These interests are in active competition with one another. Each creditor has a unique interest in certain assets of a particular company or companies comprising the Debtors and benefit from a maximization of the value of those particular assets. This interest is in tension with the Debtors' interest in obtaining value for the Debtors' assets as an unallocated whole.

The sale of the Debtors' assets free and clear of PAC's interest in those assets is not in Acorn's best interests because it will deprive Acorn of the value of its secure claim against PAC. Sale of the Debtors' assets as an unallocated and undervalued whole fails to maximize Acorn's individual interest in Polaroid's U.S. Inventory, Accounts and North American Trademarks. PAC, therefore, cannot consent to the Debtors' sale because such consent would be a breach of PAC's duty to protect and conserve its assets for the benefit of Acorn and other PAC creditors.

Apart from its duty to protect and conserve its assets for the benefit of its own creditors, PAC cannot consent to the sale of the Debtors' assets free and clear of Acorn's security interest because PAC has not sought or received Court approval to do so. Pursuant to § 363(b), a debtor may only take actions other than in the ordinary course of business after providing notice to the relevant parties and obtaining a Bankruptcy Court order permitting the debtor to take such action.

Here, the Debtors have asked the Bankruptcy Court to find that PAC has consented to the Bidding Procedures and the sale of the Debtors' assets. PAC consenting to the sale of assets that constitute collateral for a loan made to the Debtors is not, however, an action made in the ordinary course of PAC's business. Accordingly, PAC

must, under § 363(b), obtain Bankruptcy Court approval before it can be deemed to have consented.

Because PAC has not obtained Bankruptcy Court approval to consent to the sale of the Debtors' assets, the District Court must determine that PAC has not consented to the sale. Under Rule 9019(a) of the Federal Rules of Bankruptcy Procedure, PAC may only compromise its security interest in Polaroid's assets with Court approval "[o]n motion by the trustee and after notice and a hearing." Fed. R. Bankr. P. 9019(a). PAC has neither provided notice, nor has it sought approval, as required by Rule 9019(a) for compromise or settlement of its security interest.

Courts will only approve a compromise or settlement under Rule 9019(a) if it is fair and equitable, and in the best interest of the bankruptcy estate. *See In re Jackson Brewing Co.*, 624 F.2d 599, 602 (5th Cir. 1980) (citing *Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson* ("TMT Trailer"), 390 U.S. 414, 425 (1968)). It is "the interests of the creditors not the debtors [that] are paramount." *In re Texas Extrusion Corp.*, 844 F.2d 1142, 1159 (5th Cir. 1986), *cert. denied*, 488 U.S. 926 (1988).

As noted, according to PAC's schedules, PAC has approximately \$12 million in assets and over \$300 million in liabilities, making PAC insolvent. Also as noted, Acorn is PAC's largest creditor with approximately \$281 million in claims for unpaid and outstanding loans to PAC. PAC's consent to the Debtors' sale free and clear of PAC's security interest in those assets would be a compromise of those rights and would

therefore be subject to Court approval requirements imposed under Fed. R. Bankr. P. 9019 and the notice requirements of Fed. R. Bankr. P. 2002.

PAC has not sought or received court approval for compromising its claim to Polaroid's assets, nor has PAC given the requisite 20 days' notice. Moreover, PAC is obligated to adequately protect Acorn's collateral, namely the secured obligation from Polaroid. By consenting to the sale of the Debtors' assets free and clear of PAC's lien on those assets, however, PAC would be failing to protect Acorn's collateral. Without Court approval, PAC is prohibited from consenting to the Debtors' sale of assets free and clear of its security interest.

Accordingly, Polaroid did not meet their burden to establish that PAC had consented to the Sale of the assets in question, or any other grounds for that matter, that would permit the sale of these assets free and clear of PAC's liens.

C. The Bankruptcy Court Violated Acorn's Right To Due Process By Refusing To Allow Acorn A Full And Fair Opportunity To Present Evidence And Arguments On Its Objections.

In addition to Acorn's contention that the Bankruptcy Court erred in its finding of fact and conclusions of law on the bona fide dispute issues, the Bankruptcy Court refused to provide Acorn with a sufficient opportunity to present evidence and arguments and did not give these issues sufficient time and attention, thereby depriving and violating Acorn's right to a full and fair hearing as required by the Due Process Clause. Due process of law requires adequate notice, hearing and procedures to contest the deprivation of property. *See Board of Regents v. Roth*, 408 U.S. 564, 569 (1972). Acorn's security interest in Polaroid's assets and its rights to liquidate and recover the value of the

collateral constitute property rights protected by the Fifth Amendment. *See In re Townley*, 256 B.R. 697, 700 (Bankr. D.N.J. 2000) (“The right of a secured creditor to the value of its collateral is a property right protected by the Fifth Amendment.”); *In re Briggs Transp. Co.*, 780 F.2d 1339, 1342 (8th Cir. 1985) (protecting secured creditor’s Fifth Amendment property rights); *In re Holly’s, Inc.*, 140 B.R. 643, 686 (Bankr. W.D. Mich. 1992) (same).

The Bankruptcy Court repeatedly refused to address the merits of and take evidence on Acorn’s objections under 11 U.S.C. §§ 363(f)(4) & (2)—from as far back as the initial February 18, 2009 bidding procedures hearing, up to and including the April 16, 2009 Sale Hearing that resulted in the Order from which Acorn takes this appeal. At the February 18, 2009 hearing, Acorn argued that under *In re Gaylord Grain L.L.C.*, 306 B.R. 624, 627 (8th Cir. B.A.P. 2004), the Debtors have an obligation to produce *some evidence* demonstrating a factual basis for the existence of a bona fide dispute to sell Polaroid’s assets free and clear of Acorn’s liens. (Boyd Aff. Ex. B at 39.) In refusing to hear Acorn’s objection at that time, the Bankruptcy Court ignored the merits of its arguments under 11 U.S.C. §§ 363(f)(4) & (2) and stated that it “need not reach the very specific discreet statutory issue on [the] merits of whether there is a bona fide dispute over Acorn Capital’s claim within the meaning of 363(f)(4) [because] it is technically not ripe until a sale is actually presented to the Court for approval.” (*Id.* at 86.)

The Bankruptcy Court purported to distinguish *In re Gaylord Grain, L.L.C.*, 306 B.R. at 627, by narrowly focusing on the fact that, in that case, “the Trustee did not file an adversary proceeding to seek to avoid the creditor’s liens before he sought to sell the

property free and clear of interests.” The Bankruptcy Court emphasized the *Gaylord Grain* court’s statement that “the issue [then] *becomes* whether there’s a bona fide dispute for the purposes of Section 363(f)(4).” (Emphasis added). (Boyd Aff. Ex. B at 87.)

The Bankruptcy Court noted that the use of the word *becomes*, “seems premised upon a bed rock assumption that if an adversary proceeding were pending there is a bona fide dispute, [which] is reinforced by the fact that the commencement of an adversary proceeding . . . triggers Rule 11 considerations and any attorney . . . should be doing a *very comprehensive factual investigation* before launching litigation or there’s a violation of Rule 11.” (*Id.* at 88.) (emphasis added.) Thus, the Bankruptcy Court stated, “I don’t think [*Gaylord Grain*] can be read for the prospect that under the current procedural posture here with an adversary proceeding Complaint filed with all the implications that [it] has and with the deemed certification of merit based upon an adequate investigation of facts and law that Rule 11 applies to the mere fact of subscribing and filing that adversary proceeding. I don’t think the analysis that’s made here requiring the production or the providing of evidence . . . is applicable at all.” (*Id.* at 89.)

At the March 26, 2009, protective order hearing, the Bankruptcy Court again refused to address the merits of Acorn’s arguments and, in connection with its ruling on the Debtors’ Motions for a Protective Order, the Court stated that, in evaluating whether to permit the sale of Polaroid’s assets free and clear of Acorn’s lien, its focus would be to determine whether the Complaint against Acorn would withstand a motion to dismiss under Rule 12(b)(6). With no case law precedent for this standard, this was the first time

Acorn was put on notice that the Bankruptcy Court intended to apply a 12(b)(6) standard to a determination of whether a bona fide dispute existed as to Acorn's liens. (*Id.* Ex. E at 89-92.)

Again at the April 16, 2009 Sale Hearing, Acorn was deprived of any meaningful opportunity to make its 11 U.S.C. §§ 363(f)(4) & (2) arguments. When Acorn's counsel sought to argue that the Debtors had failed to meet the narrowly created Rule 12(b)(6) pleading standard for showing a bona fide dispute, the District Court repeatedly cut Acorn's counsel off during argument, warning him to "get on with [it]" and then stated, inconsistent with its previously articulated standard, that Acorn's counsel was "not [be] arguing a motion for dismissal under 12(b)(6)." (Boyd Aff. Ex. C at 304-05.) The Court also continued to refuse to hear evidence.

When Acorn's counsel attempted to argue that no bona fide dispute exists, even when applying the Bankruptcy Court's previously articulated 12(b)(6) standard, the Court stated "Stop wasting time haggling with me over whether I'm going to cut you off or I will right now and just rule on the basis of your written submissions. It has been a long day. . . . Get on with your argument right now." (*Id.*) In overruling Acorn's objections, the Court improperly stated as a basis the fact that Acorn responded to the Adversary Complaint with an Answer and Counterclaim, rather than filing a Motion to Dismiss pursuant to Rule 12(b)(6), and this demonstrated the existence of a bona fide dispute. Acorn's Answer and Counterclaim, however, was filed March 16, 2009, ten days before the Court announced the never-before articulated 12(b)(6) standard at the March 26, 2009

protective order hearing for a determination of whether a bona fide dispute exists and the Debtors can sell Polaroid's assets free and clear of Acorn's claims.

As the transcripts of these hearings demonstrate, over the course of two months' time, Acorn was deprived of a fair opportunity to present evidence and arguments on its objection to the sale of Polaroid's assets free and clear of Acorn's liens. Even when Acorn's counsel was permitted to speak on these objections, those arguments were brushed over in haste, in the late evening of what was in the Court's words "a long day" of hearings. As a result, it is clear that the Bankruptcy Court did not provide these issues with sufficient time and attention and Acorn has been deprived due process of law.

II. ACORN WILL SUFFER IRREPARABLE HARM IF THE STAY PENDING APPEAL IS NOT GRANTED.

Acorn will suffer substantial and irreparable harm if its direct lien and indirect lien (through PAC) are stripped and Polaroid's assets are sold free and clear of these liens.

Acorn is entitled to constitutional protections of these property rights. Acorn negotiated to acquire these liens in these assets in consideration and reliance for the financing Acorn provided to Polaroid. Stripping Acorn of its liens would, by definition, deprive Acorn its contract and property rights and the benefit of its bargain. It is not adequate for Acorn to have a claim in the sale proceeds because the sale of the assets at issue has failed to maximize the value of those assets, in and of themselves.

Further, this sale has also failed to maximize the value of these assets in connection with their value as components of the business as a going concern. The balance of hardships favors the granting of a stay pending appeal where the order for sale

would strip off a party's lien and reduce the value of that right. *See, e.g., In re Hoekstra*, 268 B.R. 904, 907 (Bankr. E.D. Va. 2000) (balance of hardship favored stay of order that would “strip off” government's lien because, in absence of stay, other liens might attach to property and reduce whatever further value federal tax lien might have). Ordinarily, risk of mere monetary loss would not constitute irreparable injury because a prevailing appellant would usually be able to be adequately compensated by legal damages. However, where, as here, there is no other meaningful source for recovery, creditors like Acorn are threatened with irreparable harm sufficient to justify granting the stay pending appeal. *In re Moreau*, 135 B.R. 209, 215 (Bankr. N.D.N.Y. 1992); *In re Miraj & Sons, Inc.*, 201 B.R. 23, 27 (Bankr. D. Mass. 1996).

Clearly, Acorn would suffer irreparable harm through the diminution and loss of the value of its direct and indirect liens if these liens are stripped from the assets at issue and attached to the sale proceeds, which reflect a different type of asset that constitute a mere fraction of the assets that were sold.

III. THE DEBTORS AND PLR HOLDINGS, LLC WILL NOT SUFFER INJURY IF THE COURT GRANTS A STAY OF THE SALE PENDING APPEAL.

The Debtors have failed to make any showing that they will suffer harm—much less irreparable harm—if the sale of the assets in question is stayed pending Acorn's appeal. Having succeeded in its bid to purchase the assets in question, PLR Holdings, LLC (“Hilco/Gordan”) is bound to complete the transaction to acquire these assets from Polaroid. Accordingly, a stay of the closing on the sale of those assets will not jeopardize Hilco/Gordan's obligations to purchase the assets in accordance with the terms of its bid.

Any argument that Polaroid will be harmed by a stay pending appeal because Polaroid “will run out of cash” is meritless because it is a self-inflicted wound. At no time did Polaroid attempt to obtain Acorn’s consent to the sale as required under 11 U.S.C. § 363(f) for undersecured creditors. The District Court should not tolerate cries of irreparable harm made by the Debtors who had six months to secure Acorn’s consent and failed to do so.

Moreover, the issues Acorn is raising on appeal are discrete and determinable before Polaroid runs out of cash. The Hilco/Gordon APA contains a May 14 drop-dead date, which can be extended by mutual agreement of the parties under Section 8.1. At that point, Hilco/Gordon can terminate its agreement and the Debtor will be in a position to sell the assets to Patriarch for an amount of money greater than the Hilco/Gordon bid. Under those circumstances, Patriarch, as the “back-up bidder,” will have a moot appeal and only Acorn’s issues will remain to be resolved, making the process streamlined. In the meantime, Polaroid can continue to operate as a going concern during the limited timeframe necessary for Acorn to pursue its appeal of the Order.

Finally, and most importantly, Polaroid will not suffer any harm if Acorn is correct in its legal position that the Debtors are not entitled to sell these assets free and clear of Acorn’s and PAC’s liens.

IV. A STAY PENDING APPEAL WILL NOT CAUSE ANY HARM TO THE PUBLIC INTEREST.

Acorn is not aware of any harm or threat of harm that would occur to the public interest if the Court were to stay the closing on the sale of Polaroid’s assets pending

Acorn's appeal of the Order. On the contrary, the harm to the public interest would occur if the stay pending appeal were not granted. The threat to Acorn's liens and claims as to the Debtor's assets implicate fundamental constitutional protections and property rights. If these protections and rights are sacrificed in this instance, this would create adverse precedent that would, indeed, pose substantial harm to the public interest.

In the meantime, the Court must be concerned with the interests of third parties who act in reliance on the bankruptcy court's ruling, only to perhaps learn that the ruling was incorrect. This situation militates granting the stay in the public interest. *In re Moreau*, 135 B.R. 209, 215 (Bankr. N.D.N.Y. 1992).

Conclusion

For the foregoing reasons, Acorn respectfully requests the District Court to grant its motion for stay of the closing of the sale of Polaroid's assets free and clear of Acorn's liens under 11 U.S.C. § 363 pending Acorn's appeal of the Order.

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