Hearing Date and Time: March 20, 2013 at 10:00 a.m. (ET)

COOLEY LLP
1114 Avenue of the Americas
New York, New York 10036
Tel.: 212-479-6000
Cathy Hershcopf
Jeffrey L. Cohen
Alex R. Velinsky
Robert B. Winning

Counsel for the Official Committee
Of Unsecured Creditors

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: ATARI, INC., et al., Debtors,[1]	Chapter 11 Case No. 13-10176 (JMP)

OMNIBUS REPLY OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS IN SUPPORT OF THE APPLICATION TO RETAIN AND EMPLOY DUFF & PHELPS SECURITIES, LLC AS FINANCIAL ADVISOR TO THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF ATARI, INC., *ET AL.*, *NUNC PRO TUNC* TO FEBRUARY 11, 2013

The Official Committee of Unsecured Creditors (the "Committee") of Atari, Inc., *et al.*, as debtors and debtors-in-possession in these proceedings (the "Debtors"), by its undersigned counsel, hereby replies (the "Reply") to (i) the limited objection (the "Objection") of Alden Global Value Recovery Master Fund, L.P. ("Alden") to the Committee's application (the "Application") to retain Duff & Phelps Securities, LLC ("D&P") as its financial advisor, *nunc pro*

[1] The Debtors are Atari, Inc., Atari Interactive, Inc., Humongous, Inc., and California U.S. Holdings, Inc.

tunc to February 11, 2013, pursuant to section 1103 of chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"), Rule 2014 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules") and Rule 2014-1 of the Local Rules of Bankruptcy Procedure for the Southern District of New York (the "Local Rules"); and (ii) the statement and reservation of rights (collectively, the "Reservation") filed by the Debtors with respect to the Application, and respectfully represents as follows:

PRELIMINARY STATEMENT

Importantly, neither the Debtors nor Alden objects to the retention of D&P by the Committee. Rather, Alden asserts specific objections to D&P's proposed fee structure and passively raises a potential conflict issue, while the Debtors fail to assert any specific objection at all.

As described more fully below, the compensation structure that the Committee proposes to pay D&P is comprised of a below-market monthly fee of $50,000 per month (the "Monthly Fee") which will be partially credited towards a restructuring fee payable as the product of (i) $700,000 times (ii) the percentage recovery paid to general unsecured creditors (the "Restructuring Fee," together with the Monthly Fee, the "Fee Structure"), which Restructuring Fee is earned and payable only in the event general unsecured creditors receive distributions on account of their claims. The Committee negotiated the proposed Fee Structure with D&P in good faith and at arms' length and believes that D&P will provide the Committee with critical services geared exclusively towards maximizing the value of these estates and ensuring a meaningful recovery to general unsecured creditors.

Curiously, Alden objects to the Fee Structure solely in its capacity as DIP lender in these cases. Given that the Committee designed the Restructuring Fee to only be earned and payable

if, and when, general unsecured creditors get paid, all DIP borrowings will be paid in full well before the Restructuring Fee becomes relevant in these cases. While Alden, as DIP lender, is clearly a party in interest in these cases, the Committee respectfully submits that it has no interest in the Fee Structure proposed in the Application.

In addition to serving as DIP Lenders, Alden is now also the holder of certain prepetition claims and interests against the Debtors and the Debtors' parent company that it acquired in connection with providing the DIP financing in these cases. The Committee is currently investigating the claims Alden purchased, with the assistance of its counsel and D&P, and the outcome of that investigation will directly impact whether, and to what extent, general unsecured creditors receive recoveries in these cases. Much like full repayment of the DIP borrowings, if the Committee's investigation comes up empty, and secured claims of Alden are found to be valid, the Restructuring Fee would not be relevant until Alden is repaid in full. Again, even in its capacity as the holder of prepetition secured claims, Alden has no interest in the Restructuring Fee proposed in the Application. As the target of the Committee's investigation, Alden objected to D&P's retention in a thinly veiled attempt to determine who the Committee could retain as its financial advisor and how that advisor should be compensated. Respectfully, the Committee submits that it has chosen D&P as its financial advisor on reasonable financial terms designed by the Committee and D&P to fully align D&P's compensation with the recoveries of general unsecured creditors in these cases.

Lastly, with respect to the Debtors' Reservation, while it appears harmless enough—seeking to preserve their right to be heard at a hearing in their own chapter 11 cases, which the Committee acknowledges is always their prerogative—their failure to assert any specific objections by the objection deadline nevertheless deprives the Committee and D&P of an

opportunity to consider and respond to any such objection in writing, in advance of the hearing, and adequately prepare for the hearing itself. For the reasons stated in the Application and herein, as supported by the original and supplemental declarations, the Committee requests the Objection and Reservation be overruled and the Application be granted.

REPLY

I. The Committee has a Fiduciary Duty to Unsecured Creditors and has the Right to Retain the Professionals That it Believes Will Help Fulfill That Duty

1. A creditors' committee, as the fiduciary representative of unsecured creditors, has the primary duty of advising unsecured creditors of their rights and the proper course of action in the debtor's bankruptcy case. *See In re Caldor, Inc. N.Y.*, 193 B.R. 165, 169-170 (Bankr. S.D.N.Y. 1996) (citations omitted); *In re Baldwin-United Corp.*, 45 B.R. 375, 376 (Bankr. Ohio 1983) ("those who serve on a creditors' committee owe a fiduciary duty to all creditors which they fulfill by advising creditors of their rights and of the proper course of action in the bankruptcy proceeding.") (internal citations omitted).

2. "To that end, an official committee may 'select and authorize the employment…of one or more attorneys, accountants, or other agents, to represent or perform services for such committee. Public policy favors permitting parties to retain professionals of their choice." *Caldor*, 193 B.R. at 170; *In re Advisory Comm. of Major Funding Corp.*, 109 F.3d 219, 224 (5th Cir. 1997) (holding that a "creditors' committee not only has, with the court's approval, the power to employ attorneys, accountants and other agents to represent or perform services for the committee, it has the duty to determine what assistance it requires in order to perform its duties, when such assistance is required, and to select those best qualified to render such assistance."); *In re Brennan*, 187 B.R. 135, 150 (Bankr. D.N.J. 1995), *rev'd on other*

grounds, 180 F.3d 504 (holding that there is a presumption in favor of party's right to choose the accountant of its choice); *see also In re Codesco, Inc.*, 18 B.R. 997, 999 (Bankr. S.D.N.Y. 1982) (holding that "[o]nly in the rarest cases should the trustee be deprived of the privilege" of selecting its own professional) (internal citations omitted).

3. After interviewing multiple financial advisory firms, and considering their qualifications and proposed fee structures, the Committee selected D&P to assist the Committee in fulfilling its fiduciary duty in these cases. The Committee selected D&P for, among other reasons, D&P's skill and experience in both investment banking and forensic accounting. From the time of its formation, the Committee anticipated that it would have a need for financial advisory assistance in connection with any sale of the Debtors' assets, and in connection with any investigation (and subsequent litigation) related to the prepetition claims asserted by the Debtors' prepetition lenders and non-debtor affiliates. The Fee Structure was negotiated at arms-length between the Committee and D&P, as is more fully set forth in the *Supplemental Declaration of Thomas Clark Carlson* (the "Supplemental Carlson Declaration") filed contemporaneously herewith. This negotiation resulted in a substantial discount from D&P on its requested monthly fees, along with a restructuring fee component that is directly correlated with the interests of unsecured creditors. As a result, the Committee elected to retain D&P on the terms set forth in the Application, which terms the Committee believes are fair and reasonable under the circumstances of these cases.

II. The Proposed Fee Structure is Reasonable and is Completely Aligned With the Interests of General Unsecured Creditors

4. Section 328 authorizes the retention of a professional person "on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or

percentage fee basis, or on a contingent fee basis[,]" 11 U.S.C. § 328(a), and a Court may authorize the retention of a "professional person on any terms and conditions that [it] finds necessary to satisfy the requirements of reasonableness." *In re Federal Mogul Global Inc.*, 348 F.3d 390, 397 (3d Cir. 2003). Fee structures for financial advisors consisting of monthly fees with a back-end transaction fee have become commonplace in this and other districts. *See generally*, Diana G. Adams and Roberta A. DeAngelis, *Does "Improvident" Mean "Immutable"? The Standard of Review for Advisors' Professional Fees*, *available at*, http://www.justice.gov/ust/eo/public_affairs/articles/docs/2009/abi_200906.pdf. These fee structures are often approved under section 328 upon a consideration of what is to be accomplished before the transaction fee is earned, the degree of difficulty of the task, and the skill of the professional to be retained. As explained by Judge Gonzalez:

> When the parties to an engagement negotiate the restructuring fee, they assess the value of future services to be provided by the financial advisor. They take into consideration what is to be accomplished, the degree of difficulty of the task and the skill of the professional retained. Each side assumes the attendant risk of setting the reasonableness at this prospective stage. If it turns out that the financial advisor had no real impact on the transaction, the retaining entity may have overpaid for the services rendered. In the same way, if the financial advisor expends far more of its resources than initially anticipated in bringing about the desired result, the financial advisor may have been under-compensated for the services it provided.
>
> Once in bankruptcy, the same prospective analysis usually applies if the financial advisor's compensation is sought to be approved under 11 U.S.C. § 328 at the outset of its actual engagement. A determination of reasonableness is made at the time of retention based upon the available information. Pursuant to section 328, a court is asked to approve the reasonableness of a transaction fee arrangement based upon the financial advisor accomplishing a certain goal . . . .
>
> The section 328 retention is similar to the pre-petition prospective approach to setting compensation, in that the court reviews the terms and conditions of compensation to see if they are reasonable from a prospective viewpoint. Thus, whether retained outside of bankruptcy or under a section 328 prospective analysis, the typical engagement would preclude an examination of, among other things, the impact the financial advisor had in

> bringing about the transaction; and the parties agree to assume the attendant risks involved as to the potential for underpayment or overpayment for the services rendered.

In re XO Communications, Inc., 398 BR 106, 111-23 (Bankr. S.D.N.Y. 2008).

PROPOSED D&P FEE STRUCTURE

5. As is more fully set forth in the Application, the Committee requests that D&P be entitled to receive the following compensation for professional services rendered to the Committee: a Monthly Fee of $50,000 per month, plus a Restructuring Fee based upon the percentage recovery received by general unsecured creditors on account of their allowed general unsecured claims in these cases. The Restructuring Fee will be calculated by applying the pro rata percentage recovery to be received by general unsecured creditors on account of their allowed general unsecured claims to a maximum of $700,000. Fifty percent of any Monthly Fees actually paid to D&P following the second Monthly Fee, will be credited toward any Restructuring Fee payable to D&P.

6. The Monthly Fee is below-market and does not, on its own, fairly compensate D&P for the services that it will provide to the Committee. As such, the Monthly Fee is clearly reasonable. In addition, the Restructuring Fee, which is payable only in direct proportion to the recoveries received by holders of unsecured claims, is also reasonable in light of the crucial services D&P proposes to provide and the fact that the Restructuring Fee is directly aligned with unsecured creditor recoveries. Moreover, fee structures that include both monthly and success fee components are commonly approved in this district and elsewhere. A list of comparable cases where financial advisors were compensated with both monthly and success fees in connection with their retention by creditors' committees in bankruptcy cases is attached as Exhibit A to the Supplemental Carlson Declaration.

MONTHLY FEE

7. The Debtors do not object to the Monthly Fee in the Reservation, but Alden suggests that the already below-market Monthly Fee should be reduced by half. In a clear attempt to define the scope of retention of the financial advisor that the Committee proposes to retain to investigate the merits of Alden's claims against the Debtors and the Parent, Alden argues that the Monthly Fee "bears no reasonable relationship to the services that are necessary and required for these cases." *See* Objection at ¶12.

8. Respectfully, Alden is not D&P's client and is not in any position to opine as to what services are necessary and reasonable for the Committee to fulfill its fiduciary duty in these cases. Alden lists certain categories of services enumerated in the Application that may or may not be applicable to these cases, and draws the conclusion that the Monthly Fee should be cut in half—a reduction of equal proportion to the number of categories of services that Alden identified as unnecessary. This absurd suggestion fails to recognize the substantial amount of work that the Committee anticipates will be required of D&P in order to assist the Committee in fulfilling its fiduciary duties in these cases.

9. The Committee, with the assistance of its counsel and D&P, is actively investigating various claims asserted against the Debtors' estates. This investigation is likely to entail substantial financial analysis, including with respect to multiple intercompany transactions, for which the Committee will require the assistance of D&P. The result of this investigation, and any subsequent litigation, will directly impact the recovery received by general unsecured creditors on account of their claims.

10. In connection with the DIP financing, the Debtors waived any right to challenge or contest in any way various purported secured and unsecured debt obligations owed to Atari

Europe SAS, the Debtors' French affiliate company ("Atari Europe") and Atari, S.A. (the "Parent") as well as security interests in certain of the Debtors' assets granted to Blue Bay Value Recovery (Master) Fund Limited ("Blue Bay") in order to secure outstanding secured indebtedness owed to Blue Bay by Atari Europe and guaranteed by the Parent (the "Blue Bay Debt"). Alden is the assignee of the obligations owed to Blue Bay as well as the majority owner of the Parent.[2] The Committee requires D&P's assistance to analyze the complex relationships among the Atari entities and their related debt obligations.

11. At the same time, D&P is well-positioned to assist the Debtors' professionals in maximizing the proceeds received in connection with the sale of substantially all of the Debtors' assets. D&P has extensive experience selling assets in and out of bankruptcy, as is more fully set forth in the Declaration of Thomas Clark Carlson (the "Original Carlson Declaration"), which was filed with the Application. While admittedly, D&P is not running the sale process, D&P is poised to assist the Debtors, their professionals and the Committee in ensuring the sale process is robust, fair and value-maximizing. Among other things, D&P will facilitate bidder interest, analyze prospective bids, test the assumptions in the Debtors' management presentations, and analyze the Debtors' intellectual property portfolio on behalf of the Committee.

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[2] In addition to the Blue Bay Debt, the right to investigate the following intercompany claims were waived in the final order approving the DIP financing [D.I. 125] include: (i) $255 million of net obligations due to the Parent from Atari Interactive Inc.; (ii) $18.9 million in net obligations due to the Parent from Atari, Inc.; (iii) $25.3 million of net obligations due to Atari Europe from Atari, Inc. Along with the security interest in certain of the Debtors' assets, the Blue Bay Debt is purportedly also secured by a lien on receivables due to the Parent from the Debtors. Accordingly, Alden (as assignee of the Blue Bay Debt) would receive proceeds of such receivables.

12. In addition, D&P serves a vital function for the Committee in connection with the sale process. The Committee does not receive reporting on the sale process directly from the Debtors' investment bankers, but rather, D&P receives information from the Debtors' investment bankers (often, on a professionals' eyes only basis), and then D&P reports to the Committee with appropriately filtered and analyzed information. The results of the sale process will impact recoveries to general unsecured creditors, and therefore it is vital that the Committee's financial advisors closely monitor the process, report to the Committee, and be fairly compensated for their work. Consequently, the Monthly Fee as proposed by the Committee, is reasonable.

RESTRUCTURING FEE

13. The Debtors do not object to the Restructuring Fee in the Reservation. For a variety of reasons, Alden claims the Restructuring Fee is not justified in these cases. In doing so, Alden ignores that: (i) the Restructuring Fee is not payable from DIP borrowings, since it only becomes payable when creditors recover on their unsecured claims — *after* the DIP borrowings are fully repaid, (ii) the Restructuring Fee is directly proportional to the recovery of general unsecured creditors, such that the interests of D&P and the unsecured creditors are squarely aligned, and (iii) the fees incurred by D&P, including the Restructuring Fee, are subject to review by the Office of the United States Trustee (the "U.S. Trustee") under Section 330 of the Bankruptcy Code.

14. First, Alden suggests that D&P would receive a "windfall" in the event of a sale of the Debtors' assets or even as a result of a plan that is opposed by the Committee, because D&P is not running the sale process. *See* Objection at 9-10. This "windfall" argument completely ignores the structure of the Restructuring Fee. The Restructuring Fee is **not** triggered solely by the occurrence of a sale or confirmation of a chapter 11 plan. The Committee cannot

emphasize enough that the Restructuring Fee is **only** earned and payable if and when general unsecured creditors receive a recovery. Contrary to Alden's blind assertion, unless a sale or confirmed plan results in a return to general unsecured creditors, D&P will not receive the Restructuring Fee.

15. Second, and quite interestingly, in an attempt to argue that the Restructuring Fee is inappropriate because it is "not clearly linked to the services that D&P seeks to provide," Objection at ¶8, Alden accidentally acknowledges the importance of D&P's services to unsecured creditors and, consequently, the propriety of the Restructuring Fee. As Alden itself notes in its Objection, a successful sale does not necessarily result in significant distributions to the unsecured creditors. *See* Objection at Fn. 4. In fact, Alden admits that a meaningful recovery will likely depend on the results of the Committee's investigation and complex litigation to avoid and/or recharacterize various secured claims (which are held by Alden). *Id.* As detailed above, D&P will play a vital role in this investigation and potential litigation, including, *inter alia*, providing forensic accounting and valuation services. At the same time, while perhaps not sufficient on its own to result in meaningful recoveries to unsecured creditors, a successful sale process is nevertheless of critical importance to the Committee's interests in these cases. As such, as described in the Application, D&P's proposed services, which supplement those of the Debtors' investment banker, are directly linked to creditor recoveries.

16. As the target of the Committee's investigation, Alden is grasping at straws in an attempt to constrain D&P in its investigatory efforts. The Committee respectfully submits that the Fee Structure, including a below market Monthly Fee and a Restructuring Fee that is fully contingent on the recovery received by general unsecured creditors, is reasonable.

III. D&P Does not Represent any Holder of an Adverse Interest in Connection With These Cases

17. Although Alden states that it does not object to the Committee's retention of D&P, in a footnote to its Objection, Alden qualifies this statement by pointing to the disclosure in the Original Carlson Declaration that D&P has represented in the past and currently represents "Alden Global Entities" in connection with ongoing portfolio valuation services. *See* Objection at Fn. 3. In relevant part, Section 1103(b) of the Bankruptcy Code provides:

> An attorney or accountant employed to represent a committee appointed under section 1102 of this title may not, while employed by such committee, represent any other entity having an adverse interest in connection with the case.

11 U.S.C. § 1103(b). Generally an "adverse interest" takes the form of a competing economic interest tending to diminish estate values or to create a potential or actual dispute in which the estate is a rival claimant. *See Caldor*, 193 B.R. 171. As is set forth in the Original Clark Declaration and more specifically described and disclosed in the Supplemental Carlson Declaration, D&P does not represent any such adverse interest in connection with these cases.[3]

[3] Given the breadth of the past and current representations disclosed by Akin Gump Strauss Hauer & Feld LLP, Debtors' counsel, of Alden and its affiliates (to which Alden did not object), it is disingenuous for Alden to now raise this issue with respect to D&P.

WHEREFORE, the Committee hereby requests that the Court overrule the Objection and Reservation and that it be authorized to retain and employ D&P as its counsel *nunc pro tunc* to February 11, 2013 and that said firm be paid such compensation as may be allowed by this Court, and that this court grant such further relief as is deemed just and proper.

Dated: March 18, 2013
New York, New York

/s/ Jeffrey L. Cohen
COOLEY LLP
1114 Avenue of the Americas
New York, New York 10036
Tel.: 212-479-6000
Cathy Hershcopf
Jeffrey L. Cohen
Alex R. Velinsky
Robert B. Winning

Counsel for the Official Committee of Unsecured Creditors