

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:)	Chapter 11
CONEXANT SYSTEMS, INC., <i>et al.</i> , ¹)	Case No. 13-10367 (MFW)
Debtors.)	Jointly Administered
)	Hearing Date: April 10, 2013 at 11:30 a.m. (ET)
)	Objection Deadline: April 3, 2013 at 4:00 p.m. (ET)

**DEBTORS' MOTION FOR ENTRY OF AN
ORDER AUTHORIZING, BUT NOT DIRECTING,
THE DEBTORS TO (I) CONTINUE PREPETITION INSURANCE
COVERAGE, (II) MAINTAIN FINANCING OF INSURANCE
PREMIUMS AND (III) ENTER INTO A NEW PREMIUM FINANCING AGREEMENT**

Conexant Systems, Inc. and its debtor affiliates, as debtors and debtors in possession in the above-captioned chapter 11 cases (collectively, the "*Debtors*"),² respectfully represent:

Jurisdiction

1. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2).
2. Venue in this Court is proper pursuant to 28 U.S.C. §§ 1408 and 1409.
3. The bases for the relief requested herein are sections 105(a), 363, 364, 1107 and 1108 of the Bankruptcy Code, Rule 6004(h) of the Federal Rules of Bankruptcy Procedure

¹ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal taxpayer-identification number, are: Conexant Systems, Inc. (9439); Conexant CF, LLC (6434); Brooktree Broadband Holding, Inc. (5436); Conexant, Inc. (8218); and Conexant Systems Worldwide, Inc. (0601). The Debtors' main corporate address is 4000 MacArthur Blvd., Newport Beach, California 92660.

² A detailed description of the Debtors and their businesses, and the facts and circumstances supporting this motion and the Debtors' chapter 11 cases, are set forth in greater detail in the Declaration of Sailesh Chittipeddi, President and CEO of Conexant Systems, Inc., in Support of First Day Pleadings (the "*First Day Declaration*"), filed contemporaneously with the Debtors' voluntary petitions for relief filed under chapter 11 of title 11 of the United States Code (the "*Bankruptcy Code*"), on February 28, 2013 (the "*Petition Date*").

(the “*Bankruptcy Rules*”) and Rule 9013-1(m) of the Local Rules of Bankruptcy Practice and Procedure of the United States Bankruptcy Court for the District of Delaware (the “*Local Rules*”).

Relief Requested

4. By this motion, the Debtors request entry of an order, substantially in the form attached hereto as **Exhibit A** (the “*Order*”), (a) authorizing, but not directing, the Debtors to (i) continue prepetition insurance policies (collectively, and as discussed herein, the “*Insurance Policies*”) uninterrupted and renew and/or modify the Insurance Policies; (ii) pay unpaid prepetition premiums associated with the Insurance Policies, and (b) authorizing financial institutions to receive, process, honor and pay all related checks and electronic payment requests for payment of the related Insurance Policies.

5. In addition, out of an abundance of caution and consistent with the Debtors’ prepetition practice of financing certain of the Debtors’ Insurance Policies, the Debtors are seeking authority to (a) enter into a new financing agreement (the “*New Financing Agreement*”) with Premium Assignment Corporation (“*PAC*”), attached hereto as **Exhibit B**; (b) grant PAC or its successor or assigns a first priority lien on and security interest in unearned premiums as described in the New Financing Agreement; and (c) pay PAC or its successor or assigns all sums due under the New Financing Agreement.³

Basis for Relief

A. The Debtors’ Insurance Policies

6. The Debtors maintain 13 insurance policies that are administered by several third-

³ The Debtors are currently in the process of negotiating a consensual form of order with PAC and their debtor-in-possession lender.

party insurance carriers (collectively, the “*Insurance Carriers*”).⁴ These Insurance Policies collectively provide coverage for, among other things: (a) general commercial liability; (b) commercial excess liability; (c) umbrella excess liability; (d) professional liability (errors and omissions); (e) director and officer fiduciary and crime liability; (f) director and officer excess liability; (g) property; (h) cargo; (i) business automobile; (j) foreign credit insurance and (k) foreign liability (collectively, the “*Insurance Policies*”). A schedule of the Insurance Policies is attached hereto as **Exhibit C** and incorporated herein by reference. Continuation of the Insurance Policies is essential to the preservation of the value of the Debtors’ businesses, properties and assets. Moreover, in many cases, coverage provided by the Insurance Policies is required by the regulations, laws and contracts that govern the Debtors’ commercial activities.

7. As of the Petition Date, approximately \$100,000 in prepetition premiums associated with the Debtors’ Insurance Policies (the “*Unpaid Premiums*”) remain due and owing. The Debtors seek the authority to pay the Unpaid Premiums.

8. From time to time, and to avoid paying all premiums in full up front, the Debtors set up installment payment programs with their insurance carriers, or finance the premiums associated with certain of their Insurance Policies (collectively, the “*Financed Insurance Policies*”). More specifically, the Debtors have financed the premiums for the Financed Insurance Policies⁵ under financing agreements with PAC, which expired on March 1, 2013 (the

⁴ Equity Risk Partners, a third-party insurance broker (the “*Insurance Broker*”), assists the Debtors in obtaining comprehensive insurance coverage in the most cost-effective manner. The Debtors are liable for certain fees associated with obtaining such coverage. Specifically, the Insurance Broker earns a commission of approximately fifteen (15) percent of all premium payments under the Insurance Policies. The Broker commission is included in the premium payments.

⁵ The Financed Policies include: employer liability; general liability; director and officer fiduciary and crime liability; and excess director and officer liability.

“*Prepetition Financing Agreements*”). As a result of the recent expiration of the Prepetition Financing Agreements, the Debtors are seeking authority to enter into the New Financing Agreement with PAC, which is attached hereto as Exhibit B. The Financed Insurance Policies, and the accompanying monthly installment payments, are summarized in Exhibit C.

Supporting Authority

A. Payment of the Obligations Related to the Insurance Policies is Required by the Bankruptcy Code and the U.S. Trustee

9. The Insurance Policies are essential to the preservation of the value of the Debtors’ businesses, properties and assets. Not only are some of the Insurance Policies required by the various regulations, laws and contracts that govern the Debtors’ commercial activities, but section 1112(b)(4)(C) of the Bankruptcy Code provides that “failure to maintain appropriate insurance that poses a risk to the estate or to the public,” is “cause” for mandatory conversion or dismissal of a chapter 11 case. 11 U.S.C. § 1112(b)(4)(C). Moreover, the Operating Guidelines for Chapter 11 Cases of the Office of the United States Trustee for the District of Delaware also require debtors to maintain insurance coverage throughout their chapter 11 cases.

10. Courts in this jurisdiction have approved relief similar to the relief requested in this motion. *See, e.g., In re Vertis Holdings, Inc.*, No. 12-12821 (CSS) (Bankr. D. Del. Nov. 1, 2012) (authorizing debtors to maintain, extend and renew existing insurance programs and pay all insurance obligations including premiums, deductibles, retrospective adjustments, expenses, taxes, fees, etc.); *In re Bicent Holdings LLC*, No. 12-11304 (KG) (Bankr. D. Del. Apr. 24, 2012) (same); *In re Friendly Ice Cream Corp.*, No. 11-13167 (KG) (Bankr. D. Del. Oct. 5, 2011) (same); *In re Appleseed’s Intermediate Holdings, LLC*, No. 11-10160 (KG) (Bankr. D. Del.

Feb. 18, 2011) (same); *In re The Majestic Star Casino*, No. 09-14136 (KG) (Nov. 23, 2009) (same).⁶

B. Financing Under Section 364 of the Bankruptcy Code

11. Section 364(c) of the Bankruptcy Code permits a debtor to incur secured debt if the debtor has been unable to obtain unsecured credit. *See* 11 U.S.C. § 364. Courts have permitted debtors in existing or future insurance premium financing agreements to grant a postpetition security interest in insurance policies and unearned premiums under section 364. *See, e.g., In re Nat'l Reserve Corp.*, 199 B.R. 241, 244 (Bankr. D. Mass 1996) (section 364 approval required for “all secured debt incurred postpetition” under insurance premium financing agreements); *In re Braniff Int'l Airlines, Inc.*, 164 B.R. 820, 828 (Bankr. E.D.N.Y. 1994) (requiring section 364 approval for entry of postpetition financing agreements).

12. The Debtors request authority to enter into the New Financing Agreement with PAC and to grant PAC or its successors and assigns a first priority lien on and security interest in unearned premiums as described in the New Financing Agreement. The Debtors believe that providing PAC or its successors and assigns security interests to secure premium financing is imminently reasonable. The New Financing Agreement will enable the Debtors to spread the cost of their insurance coverage over a longer period of time, thereby permitting the Debtors to use cash most efficiently. Without the New Financing Agreement, the Debtors would be forced to seek alternative means by which to finance their insurance premiums on an expedited basis and at greater cost to the Debtors and their estates. Therefore, to allow the Debtors the greatest opportunity to continue to restructure efficiently, the Debtors respectfully request that the Court

⁶ Because of the voluminous nature of the orders cited herein, such orders are not attached to this motion. Copies of these orders are available upon request to the Debtors' counsel.

grant authority to grant necessary security interests to PAC or its successors and assigns in addition to authority to enter into the New Financing Agreement.⁷

13. In light of the demonstrable benefits of financing insurance premiums and spreading costs over a longer period of time, courts in this district have regularly approved entry into premium financing agreements on a prospective basis, in other recent chapter 11 cases. *See, e.g., In re U.S. Concrete, Inc.*, Case No. 10-11407 (PJW) (Bankr. D. Del. Apr. 30, 2010); *In re Flying J Inc.*, Case No. 08-13384 (MFW) (Bankr. D. Del. Feb. 18, 2010); *In re Muzak Holdings LLC*, Case No. 09-10422 (KJC) (Bankr. D. Del. Feb. 12, 2010). Consistent with the orders in these other chapter 11 cases, the Debtors believe that granting the relief requested herein is appropriate and in the best interests of their estates and their creditors.

C. Payment of the Insurance Obligations is Warranted Under the Doctrine of Necessity

14. Courts generally acknowledge that, under appropriate circumstances, they may authorize special treatment for, or a Debtor to pay for, certain prepetition obligations. *See, e.g., In re Just for Feet, Inc.*, 242 B.R. 821, 824-45 (Bankr. D. Del. 1999) (noting that, in the Third Circuit, debtors may pay prepetition claims that are essential to the continued operation of the debtor's business); *In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989) (granting the debtor the authority to pay prepetition wages); *Armstrong World Indus., Inc. v. James A. Phillips, Inc.*, (*In re James A. Phillips, Inc.*), 29 B.R. 391, 398 (Bankr. S.D.N.Y.

⁷ Section 362(d) allows the Court to grant relief from the automatic stay if "cause" is shown. *See* 11 U.S.C. § 362(d). In determining whether "cause" exists, courts in this and other circuits have developed a balancing test, which primarily considers the balancing of harms to the parties. *See, e.g., United States v. Nicolet*, 857 F.2d 202, 206 (3d Cir. 1988); *In re Rexene Prod. Co.*, 141 B.R. 574, 577 (Bankr. D. Del. 1992). Even though the Debtors intend to enter into new premium financing agreements postpetition and the automatic stay may not apply, the Debtors, out of an abundance of caution, seek relief from the stay and assert that cause exists for such relief. Relief from the automatic stay would allow the Debtors to enter into new premium financing agreements and thereby finance their insurance premiums on terms that are most cost-effective and beneficial to the Debtors and their estates.

1983) (granting the debtor the authority to pay prepetition claims of suppliers who were potential lien claimants). When authorizing payments of certain prepetition obligations, courts have relied upon several legal theories rooted in sections 105(a), 363(b), 1107(a) and 1108 of the Bankruptcy Code.

15. Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, debtors in possession are fiduciaries charged with “holding the bankruptcy estate[s] and operating the business[es] for the benefit of [their] creditors and (if the value justifies) equity owners.” *In re CoServ, L.L.C.*, 273 B.R. 487, 497 (Bankr. N.D. Tex. 2002). Inherent in a debtor in possession’s fiduciary duties is the obligation to “protect and preserve the estate, including an operating business’s going-concern value,” which, in certain instances, can be fulfilled “only . . . by the preplan satisfaction of a prepetition claim.” *Id.* Indeed, the *CoServ* court specifically noted that the preplan satisfaction of prepetition claims would be a valid exercise of the debtor’s fiduciary duty when the payment “is the only means to effect a substantial enhancement of the estate” *Id.*

16. Consistent with a debtor’s fiduciary duties, where there is a sound business purpose for the payment of prepetition obligations and where the debtor is able to “articulate some business justification, other than the mere appeasement of major creditors,” courts have authorized debtors to make such payments under section 363(b) of the Bankruptcy Code. *See, e.g., In re Ionosphere Clubs, Inc.*, 98 B.R. at 175 (finding that a sound business justification existed to pay prepetition wages); *In re James A. Phillips, Inc.*, 29 B.R. at 397 (relying upon section 363 as a basis to allow a contractor to pay the prepetition claims of suppliers who were

potential lien claimants).⁸

17. In addition to the authority granted a debtor in possession under sections 105(a), 363(b), 1107(a) and 1108 of the Bankruptcy Code, courts have developed the “doctrine of necessity” or the “necessity of payment” rule, which originated in the landmark case of *Miltenberger v. Logansport, C. & S.W.R. Co.*, 106 U.S. 286 (1882). Since *Miltenberger*, courts have expanded their application of the doctrine of necessity to cover instances of a debtor’s reorganization, see *Dudley v. Mealey*, 147 F.2d 268, 271 (2d Cir. 1945) (holding, in a hotel reorganization matter, that the court was not “helpless” to apply the rule to supply creditors where the alternative was the cessation of operations), including the United States Court of Appeals for the Third Circuit, which recognized the doctrine in *In re Lehigh & New England Ry. Co.*, 657 F.2d 570, 581 (3d Cir. 1981).

18. In *Lehigh*, the Third Circuit held that a court could authorize the payment of prepetition claims if such payment was essential to the continued operation of the debtor. *Id.* (stating that a court may authorize payment of prepetition claims when there “is the possibility that the creditor will employ an immediate economic sanction, failing such payment”); see also *In re Penn Cent. Transp. Co.*, 467 F.2d 100, 102 n.1 (3d Cir. 1972) (holding that the necessity of payment doctrine permits “immediate payment of claims of creditors where those creditors will

⁸ Courts have also authorized payment of prepetition claims in appropriate circumstances pursuant to section 105(a) of the Bankruptcy Code. Section 105(a) of the Bankruptcy Code, which codifies the inherent equitable powers of the bankruptcy court, empowers the bankruptcy court to “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.” 11 U.S.C. § 105(a). Under section 105(a), courts may permit preplan payments of prepetition obligations when such payments are essential to the continued operation of the debtor’s business and, in particular, where nonpayment of a prepetition obligation would trigger a withholding of goods or services essential to the debtors’ business reorganization plan. See *In re UNR Indus.*, 143 B.R. 506, 520 (Bankr. N.D. Ill. 1992) (permitting the debtor to pay prepetition claims of suppliers or employees whose continued cooperation is essential to the debtors’ successful reorganization); *Ionosphere Clubs*, 98 B.R. at 177 (finding that section 105 empowers bankruptcy courts to authorize payment of prepetition debt when such payment is needed to facilitate the rehabilitation of the debtor).

not supply services or material essential to the conduct of the business until their pre-reorganization claims have been paid”); *In re Just for Feet, Inc.*, 242 B.R. at 824-45 (noting that debtors may pay prepetition claims that are essential to continued operation of the business); *In re Columbia Gas Sys., Inc.*, 171 B.R. 189, 191-92 (Bankr. D. Del. 1994) (same).

19. Today, the rationale for the necessity of payment rule – the rehabilitation of a debtor in reorganization cases – is “the paramount policy and goal of Chapter 11.” *In re Ionosphere Clubs, Inc.*, 98 B.R. at 176; *Just For Feet*, 242 B.R. at 826 (finding that payment of prepetition claims to certain trade vendors was “essential to the survival of the debtor during the chapter 11 reorganization.”); see also *In re Quality Interiors, Inc.*, 127 B.R. 391, 396 (Bankr. N.D. Ohio 1991) (“[P]ayment by a debtor-in-possession of pre-petition claims outside of a confirmed plan of reorganization is generally prohibited by the Bankruptcy Code”, but “[a] general practice has developed . . . where bankruptcy courts permit the payment of certain pre-petition claims, pursuant to 11 U.S.C. § 105, where the debtor will be unable to reorganize without such payment.”); *In re Eagle-Picher Indus., Inc.*, 124 B.R. 1021, 1023 (Bankr. S.D. Ohio 1991) (approving payment of prepetition unsecured claims of tool makers as “necessary to avert a serious threat to the Chapter 11 process”); *Burchinal v. Cent. Wash. Bank (In re Adams Apple, Inc.)*, 829 F.2d 1484, 1490 (9th Cir. 1987) (finding that it is appropriate to provide for the “unequal treatment of pre-petition debts when [such treatment is] necessary for rehabilitation . . .”); Collier on Bankruptcy n 105.02[4][a] (Alan N. Resnick & Henry J. Sommer eds., 16th ed. rev.) (discussing cases in which courts have relied upon the “doctrine of necessity” or the “necessity of payment” rule to pay prepetition claims immediately).

20. Failure to pay amounts related to the Insurance Policies as and when they come due may harm the Debtors’ estates in several ways. More specifically, there is the potential for

an insurance company to terminate coverage, which would likely place additional strain on the Debtors' relationships with key employees who benefit from the Debtors' insurance coverage, and would also eviscerate the Debtors' ability to prevent loss in value caused by casualty, natural disaster or another unforeseen event. In the event of termination of insurance coverage, the Debtors would need to obtain replacement insurance, at a likely higher price. Additionally, any interruption of payment would have a severe, adverse effect on the Debtors' ability to finance premiums on future policies. Accordingly, continued payment of insurance premiums is necessary to a successful reorganization. In light of the importance of maintaining insurance coverage with respect to their business activities, the Debtors submit it is in the best interest of their estates to maintain the Insurance Policies and to pay related amounts as described herein under the Bankruptcy Code.

D. Cause Exists to Authorize the Debtors' Financial Institutions to Honor Checks and Electronic Fund Transfers

21. The Debtors represent that they have sufficient availability of funds to pay the amounts described herein in the ordinary course of business by virtue of cash reserves, expected cash flows from ongoing business operations and anticipated access to debtor in possession financing. Also, under the Debtors' existing cash management system, the Debtors represent that checks or wire transfer requests can be readily identified as relating to an authorized payment made with respect to the Insurance Policies. Accordingly, the Debtors believe that checks or wire transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized, when requested by the Debtors, to receive, process, honor and pay any and all checks or wire transfer requests with respect to the Insurance Policies.

Waiver of Bankruptcy Rules Regarding Notice and Stay of an Order

22. To implement the foregoing successfully, the debtors seek a waiver of the notice requirements under Bankruptcy Rule 6004(a) and any stay of an order granting the relief requested herein pursuant to Bankruptcy Rule 6004(h), 7062, 9014 or otherwise.

The Debtors' Reservation of Rights

23. Nothing contained herein is intended or should be construed as an admission as to the validity of any claim against the Debtors, a waiver of the Debtors' rights to dispute any claim or an approval or assumption of any agreement, agreement, contract or lease under section 365 of the Bankruptcy Code. Additionally, nothing contained herein is intended or should be construed as an admission as to the validity of any claim against the Debtors or a waiver of the Debtors' rights to dispute any claims regarding escheatment. The Debtors expressly reserve their rights to contest any claim or billing dispute. Likewise, if this Court grants the relief sought herein, any payment made pursuant to the Court's order is not intended and should not be construed as an admission as to the validity of any claim or a waiver of the Debtors' rights to subsequently dispute such claim.

Notice

24. The Debtors have provided notice of this Application to: (a) the Office of the United States Trustee for the District of Delaware; (b) proposed counsel to the Official Committee of Unsecured Creditors; (c) counsel to the Debtors' prepetition secured lender and debtor in possession lender; (d) the agent for the Debtors' prepetition secured notes; (e) counsel to each of the prepetition equity holders; (f) the Delaware Secretary of State; (g) the Delaware Secretary of Treasury; (h) the Delaware State Attorney General; (i) the Office of the United States Attorney General for the State of Delaware; (j) the Internal Revenue Service; (k) the

Securities and Exchange Commission; and (l) each of the insurers on the list attached hereto as **Exhibit C**. In light of the nature of the relief requested in this Application, the Debtors respectfully submit that no further notice is necessary.

No Prior Request

25. No prior motion for the relief requested herein has been made to this or any other court.

WHEREFORE, for the reasons set forth herein and in the First Day Declaration, the Debtors respectfully request that the Court enter the Order, substantially in the form attached hereto as **Exhibit A**, (a) authorizing the Debtors, in their discretion, to (i) continue the Insurance Policies uninterrupted and renew and/or modify the Insurance Policies; (ii) pay unpaid prepetition premiums associated with the Insurance Policies, and (b) authorizing financial institutions to receive, process, honor and pay all related checks and electronic payment requests for payment of the related Insurance Policies.

In addition, out of an abundance of caution and consistent with the Debtors' prepetition practice of financing certain of the Debtors' Insurance Policies, the Debtors seek authority to (a) enter into a the New Financing Agreement; (b) grant PAC or its successor or assigns a first priority lien on and security interest in unearned premiums as described in the New Financing Agreement; and (c) pay PAC or its successor or assigns all sums due under the New Financing Agreement.

Dated: March 15, 2013
Wilmington, Delaware

/s/ Michael W. Yurkewicz

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