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ENTERED

TO: Dave Cobrain, Program Manager, Permits Management Program

FROM: Vanessa Colón, Environmental Scientist & Specialist

SUBJECT: **SPARTON TECHNOLOGY, INC.**
CERBERUS ACQUISITION & FINANCIAL ASSURANCE ANALYSES

DATE: **August 26, 2019**

Cerberus Capital Management is a private equity/buyout/investment firm which has a history of acquiring companies in financial peril. They are not industry specific and have a wide assortment acquisition portfolio. The company specializes in distressed debt, lending to companies ready to file bankruptcy and/or purchasing the company and then filing for bankruptcy, for significantly high lending fees while taking a percentage of ownership, and in some instances stripping companies of assets and laying off their workforces.

An example includes the Cerberus acquisition of Aegis Mortgage Corp. in 1998 assuming a controlling foothold in Aegis, and in 2007 Aegis filed for Chapter 11 bankruptcy. One of the lenders in that purchase, fighting over Aegis' assets, was Cerberus' lending subsidiary Madeleine, LLP. As a result, Cerberus fired 738 people and left them without benefits. Other examples can be seen in their 2004 Guilford Mills (GM) acquisition. Whilst GM was emerging from a bankruptcy in 2002, Cerberus acquired the company in 2004 and proceeded to close the Hornaday Road facility letting go 101 employees just 14 months later. Similar results involving the purchasing and lending of/to distressed companies for large sums of money, stripping them of their assets and leaving them to perish can also be seen in acquisitions like Mervyns (2004), Hocking Glass Company (2004), Bushmaster Firearms International (2006), Remington (2007), Marlin (2008), Chrysler Group (2007), and many other companies.

Cerberus' strategy in such acquisitions is via the "leveraged buyout" which requires the acquired successor company to borrow the funds for its own purchase and then pay back the loan at extremely high interest rates. The approach used by Cerberus often causes their successors to lose equity in their acquisition deal while saddling the company with debt. This is by design. The new parent company of Sparton, Cerberus, should provide an Independent Financial Assurance mechanism in the form of a RCRA Performance Surety Bond which requires a standby trust and the standby trust will require a letter of credit.

2007-2009: Chrysler Under Cerberus

by David Zatz

On May 14, 2007, Cerberus announced that it would buy 80% of Chrysler Group, including the highly profitable Chrysler Financial division. In 2009, Cerberus gave up Chrysler — except for Chrysler Financial. It was an era that started with great hopes, only to have them quickly dashed, ending in bankruptcy, followed by a slow recovery.

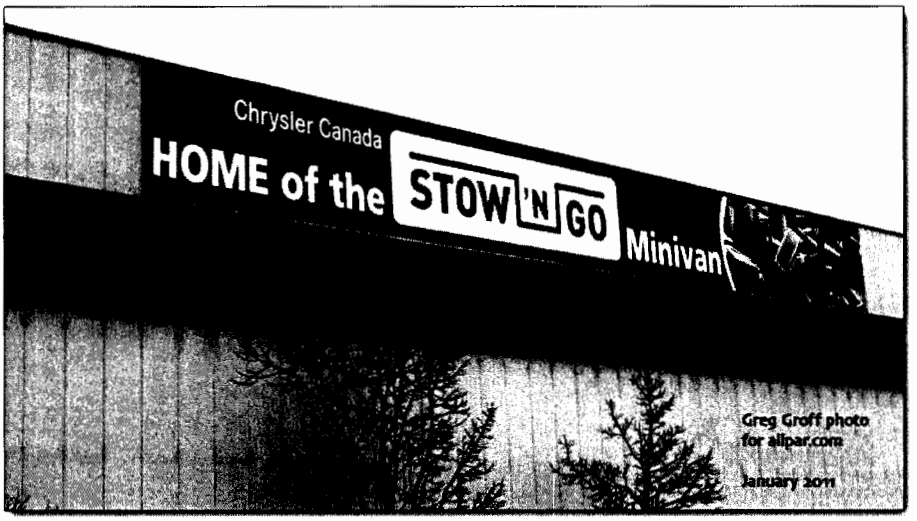
The private-equity firm signed on reputable ex-Chrysler people as advisors, including designer Tom Gale, former sales chief Gary Dilts, past Chrysler Financial president Jerry Farrell, and past Chrysler Financial CFO Thomas Gillman. They also hired Mercedes ex-pat Wolfgang Bernhard, who ended up returning to Daimler AG.

Just before the transfer took place (on August 3, 2007), another 13,000 jobs were eliminated.

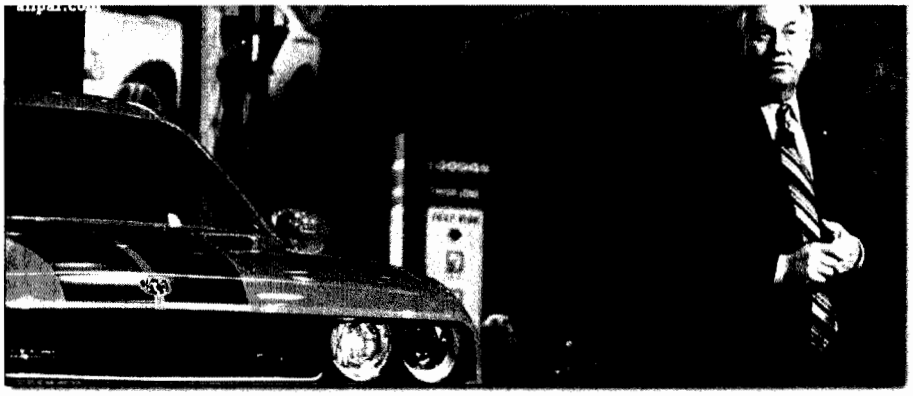
CLOSED FACILITIES

- Newark, Delaware
- Sterling Heights (planned)
- St. Louis minivan and truck
- Marysville Axle
- Conner Avenue
- Plymouth Road Office Complex

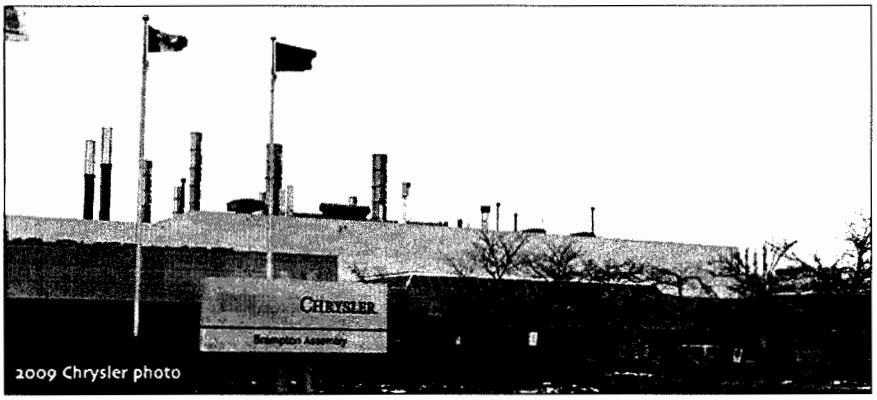
The plant signs were changed, slowly, starting on August 1, 2007; most often, Cerberus did not pay for the change, and local employees or managers simply covered up the "Daimler." Labels (including on parts and boxes), brochures, and stationery were updated as they ran out, so that cars and parts had DaimlerChrysler labels until Fiat took over.



On August 4, the new Chrysler web site declared "Get ready for the next hundred years" (the CTC gained a banner with the slogan). Tom LaSorda, Eric Ridenour, and Tom Sidlik left the Daimler Board of Management, and DaimlerChrysler quickly renamed itself Daimler AG. The new company was called Chrysler Holdings LLC and consisted of Chrysler Financial and Chrysler Corporation, LLC.



In an *Automotive News* interview, Frank Klegon said that Daimler and Chrysler would stil share electrical architectures (with a new, jointly engineered architecture due around 2011) and SUV chassis components. Mr. Klegon seemed happy that Chrysler would have more freedom to work with other automakers and suppliers.



The options

There were three major competitors for Chrysler. Cerberus had political pull, and may have promised continuing joint projects with Mercedes; and they were unlikely to bring Chrysler into competition with Mercedes, or bring the company back, so that Daimler's line of "we rescued Chrysler" would be proven a lie. The deal also allegedly let Daimler use the Viper design and the next-generation "Pentastar" V6 engines as the basis for Mercedes engines and cars.

Kirk Kerkorian, who had spurred the Daimler takeover in the first place, supported plant workers in Toledo who wanted to take Chrysler over in an employee buyout.

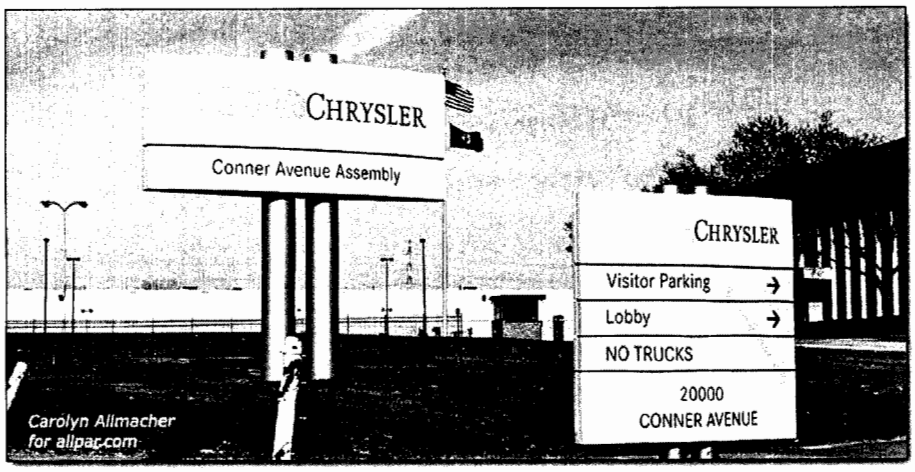
Canadian parts-maker **Magna** had experience in automotive assembly in Europe. They were working with a private equity firm with a less controversial background.

The DaimlerChrysler era

Other private equity firms in the running, according to *Detroit News*, were Apollo Management, Blackstone Group, and Carlyle Group.

Initial Reactions and Reality

Employees, dealers, customers, and potential buyers were excited. Allpar saw a favorable response, with many being happy that the Daimler nightmare was nearly over. Reactions were overwhelmingly positive, with autoextremist.com dissenting, as it did when Fiat took over.



Under Daimler, Chrysler had been cut to a third of its size, its cars altered to provide Mercedes with increased purchasing volumes (or royalties), its advertising changed to emphasize "German Engineering" — which cut Chrysler sales but benefited Mercedes (and Volkswagen). Large cars were changed to share more with Mercedes, other cars with Mitsubishi, four cylinder engines with Hyundai and Mitsubishi.

In May 2007, it *appeared* that Cerberus would run Chrysler to make money, not transfer profits to another division's budget line. That idea died when Robert Nardelli was hired as CEO, replacing Tom LaSorda on August 6, 2007. It seemed that few people within Chrysler were not dismayed, and for good reason: Mr. Nardelli and his team shared a common desire to outsource manufacturing to China.

> Nardelli was bought out of Home Depot with $210 million, after cheapening products with replacing full time people with part-timers for temporary profit increases, both causing plummeted customer satisfaction.

Well-respected executive Eric Ridenour left just after Bob Nardelli came in; though bringing in Toyota's Jim Press as co-President and co-Vice Chair helped to counter the gloom.

Cerberus often portrayed itself as patriotically rescuing a great American automaker, but their CEO, multi-billionaire Steve Feinberg, allegedly did not invest his own money, oversaw the outsourcing of manufacturing to China, and then tried to sell Chrysler to numerous Chinese companies.

Cerberus also borrowed $10 billion, using Chrysler assets as collateral, to avoid investing their own money. In February 2008, Steven Feinberg, CEO of Cerbgerus, said, "We do not need to transition the car industry or even to return Chrysler to a much stronger relative position in the U.S. car market in order to be successful."

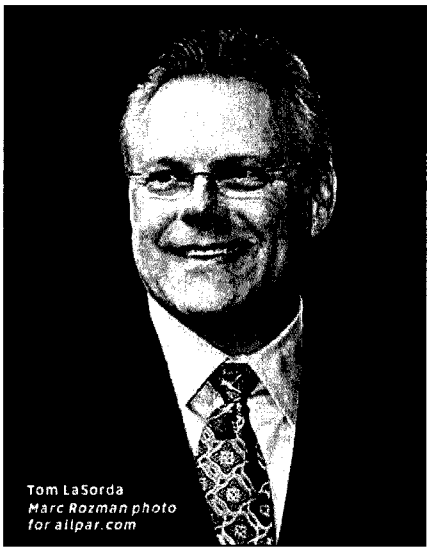
Talks with Nissan started in 2007; the companies exchanged term sheets, but Nissan could not get the needed financing. Indeed, Allpar was told that Chrysler executives nearly closed down the Pentastar V6 project in favor of buying Nissan V6 engines.


Kolka, LaSorda, and Nardelli

One source wrote, "Nissan was taking Ram, Volkswagen the vans, one of Chinese companies was taking Jeep. Chrysler, Dodge, and Jeep would be divided up and dumped." Tom LaSorda wrote in a court statement:

> Chrysler sent letters to parties, primarily in China, whom we thought would be potentially interested in purchasing our assets [*not* say purchasing the company.] ... Beijing Automotive Industry Holding Co., Tempo International Group, Hawtai Automobiles, and Chery Automotive Co., expressed interest in purchasing specific vehicles, powertrains, intellectual property rights, distribution channels and automotive brands.

Mr. LaSorda said that Chrysler also tried to form alliances with Volkswagen, Tata, Magna, GAZ, Hyundai, Honda, and Toyota. The alliance with Toyota suggested by LaSorda and Jim Press would have had Toyota using Chrysler factories to build new products. Toyota quickly rejected the proposal, as did Honda, both preferring to build on farmland in remote areas.


Tom LaSorda
Marc Rozman photo for allpar.com

Newspapers wrote that Cerberus also tried to join Chrysler to GM, whose conditions would have involved the loss of nearly all jobs at Chrysler; Tom LaSorda refused to go along with this, according to the reporting.

Around a week after the Cerberus takever, Chrysler announced it will open engineering centers in China, Poland, and India, and would explore expanding relationships with Hyundai and Mitsubishi. Chrysler product chief Frank Klegon said the company would bolster its collaboration.

The same day, the company said it would sell a diesel Ram 1500 in 2009. Dodge was already working with Cummins to package a new V6 diesel engine, and according to an insider, they finished the project but didn't continue.

By the end of the month, there were reports in the *Wall Street Journal* that Chrysler was seeking to sell Mopar.

An economic crash in 2008, combined with high fuel prices, slashed demand, and rumors of bankruptcy became self-fulfilling. George W. Bush set up loans to Chrysler and GM to keep them alive until Barack Obama was inaugurated. (Mr. Bush had initially put off a meeting with industry leaders to attend a tee-ball game, and to meet with an *American Idol* winner and Tom DeLay — who was later booked on conspiracy and money laundering charges.

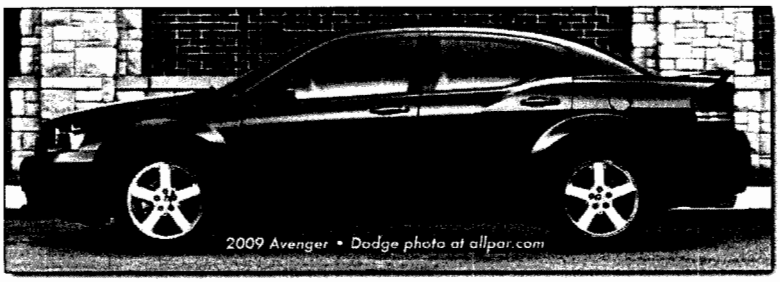
Bob Nardelli reportedly called Rick Wagoner in January 2009, but GM was not interested. Talks with Fiat, which started in March 2008, had seemed promising; by the time the deal actually came, Cerberus only wanted to hold onto Chrysler Financial, a predictable moneymaker.


Presidential visit
November 2010

President Obama quickly set up a team of people to deal with the problem of GM, Ford, and Chrysler. Ford survived with several billion dollars in low-interest loans from the Department of Energy; GM and Chrysler were put into bankruptcy, shedding billions in debt. Both paid off their high-interest new loans (though not the Bush loans) ahead of schedule, and the government profited well from its post-Bush investments in Chrysler.

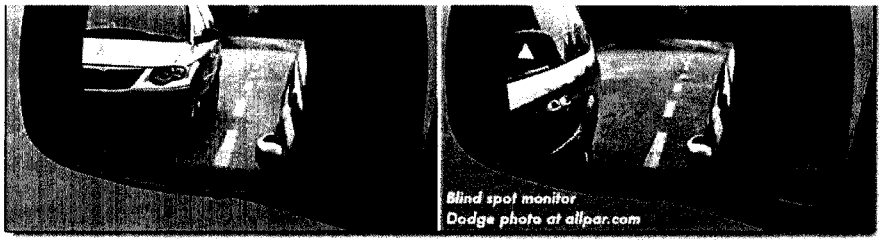
The brighter side

In addition to keeping Pentastar V6 engineering on track (albeit after threatening to close it for Nissan engines), and hiring Jim Press to try to increase quality, executives reportedly allowed designers to put another $150 per car into the interiors, helping reduce the excessive cost-cutting of Daimler — though laying off engineers and other employees could not have helped. We can disregard most 2007-2008 model year launches, since these were essentially in the works when Daimler was in charge.


2009 Avenger • Dodge photo at allpar.com

For 2009, the Chrysler Sebring and Dodge Avenger lineups were dramatically simplified, cutting costs, while extras and upgrades (including better sound insulation) were included in both to increase value. 300's base model was upgraded. Chrysler adjusted the badge placement of many vehicles, for what we believe to be a more sensible and pleasing appearance. Compass and Patriot got a far better interior with more padding, better materials, and more graceful lines and curves.

Dodge Charger and other cars and trucks got the revised Hemi V8 with variable cam timing, good for roughly 370 horsepower and 398 lb-ft of torque; Dodge Charger SRT8 got the Dodge Challenger suspension tuning for a nicer ride, and the Super Bee was brought back.



Dodge Grand Caravan and Chrysler Town & Country got optional blind spot monitoring, rain-sensitive wipers, and rear cross path systems. Gas mileage on the 4-liter models shot up 8% over 2008s while power was boosted. Viper ACR was lightened, with aero works to increase downforce; numerous other improvements were made. For far more, see our 2009 updates page.

Cerberus and its people

Intensely tied to politics, paying their dues by hiring on Dan Quayle, former Treasurer John Snow, and other politicians with dead careers, Cerberus was allegedly in the "pay to play" contracts game; they owned a company accused of mistreating wounded veterans at Walter Reed. A timely $110,000 donation to congressman Jerry Lewis was quickly rewarded with the renewal of a controversial $1 billion contract; US Attorney Carol Lam, who was investigating Lewis' contributors (presumably including Cerebrus), was fired. Bob Nardelli was a major fundraiser, and some said this may have been the reason he was given Chrysler's top job despite his record at Home Depot.

Cerebrus did sometimes turn companies around. They also owned 51% of GMAC Financial Services (now Ally Bank) and several large parts suppliers. However, their behavior during Chrysler ownership did not provide any evidence of any regard for American jobs or actual patriotism; they refused to invest in the company after buying it, with personal or company funds, and sought to sell whatever they could, other than the loan company.

And what happened to Chrysler Financial? In late 2010, Cerberus sold it to Toronto Dominion (TD) Bank for $6.3 billion, recovering 90% of their initial investment in Chrysler. As one Allpar contributor wrote,

> A private equity firm that buys a company, doesn't want to invest any of its own money after purchase, mortgages it to the hilt, whose owner openly states they do not have to return Chrysler to a much stronger position when it is losing billions a year, and exits while keeping the only profitable part of the company while dumping the rest, was never in it for the long haul. If they were in it for the long haul, they would have taken Chrysler through a traditional bankruptcy themselves.

Cerberus certainly had the cash to take Chrysler through bankruptcy and into the future, and most likely would have made a large profit doing so — assuming they had removed Mr. Nardelli and his ex-Home Depot crew first.

Perspective

Cerberus came in as knights in shining armor, but their behavior tended to be more like stereotypical used-car salesmen. Under their rule, Chrysler had some notable successes and invested in making their product line better, but always with an eye towards selling the company, preferably to a Chinese company, but to anyone who would pay. The Cerberus goal seems to have always been Chrysler Financial, not the car-making group; and any thought that they were in for the long haul, should have been dispelled by the first engineer layoffs and by the hiring of Bob Nardelli. It is also telling that multi-billionaire Steven Feinberg, head of Cerberus, reportedly refused to invest his *own* money once he had Chrysler Financial.

The time and energy spent on selling the company, rather than fixing it, was also a "tell." When Fiat took over, Chrysler was doing even worse, and the economy was equally bad, but they still turned it around fairly quickly.

The success of the company under Fiat, *before Fiat designs were used to launch new vehicles,* shows that Chrysler could have recovered given investment, leadership, and favorable publicity. Cerberus did make some investments — they started much of what Fiat was able to take credit for, including numerous refreshes — but reportedly, Sergio Marchionne ordered further investment in vehicles from the start. The results were positive, with overall sales rising, retail sales booming, and incentives falling.

One can speculate endlessly about the past, but it seems most likely that, had one of the other buyers been put in charge, Chrysler may have been rescued without government help — even by the same mechanism Ford used, that is, a private line of credit (advised by Chrysler's own economists) before the crisis.

Likewise, without the Daimler merger, Chrysler would never have been weak enough for Cerberus to pretend to be its saviors in the first place.

Tom LaSorda's letter to employees on the Cerberus sale • *2008 Recovery Plan* • *Plant closings*

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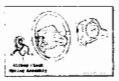

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For Private Equity, a Very Public Disaster

By LOUISE STORYAUG. 8, 2009

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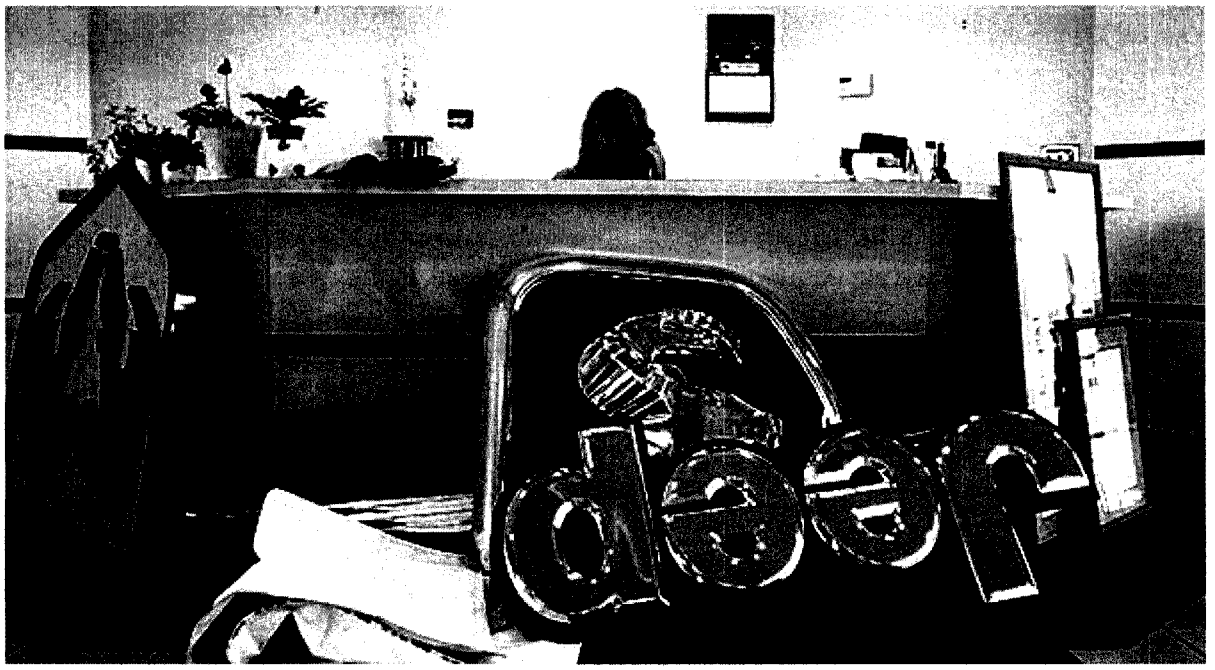

Cerberus Capital Management had high hopes for Chrysler. But by this spring the automaker ended franchise agreements with hundreds of dealers, like this one in Phoenix, and was sold to Fiat. Credit Joshua Lott/Reuters

FOR Steve Feinberg, the onetime owner of Chrysler, the past year has been a crawl toward defeat. He lost billions of dollars. He lost prestige. He lost his privacy. And he ended up a ward and supplicant of the federal government.

But, even now, Mr. Feinberg, a man who can play a decent game of chess while blindfolded, is hard-pressed to pinpoint many mistakes. Sitting in his office on Park Avenue, far away from the detritus that surrounds Detroit, he grows pensive when asked what he has learned from his audacious — and failed — effort to privatize and resurrect the legendary and deeply troubled auto giant. "I don't know what we could have done differently," he says, crossing his arms on his chest. "From the day we bought it, we worked hard to improve it."

He pauses, pondering, as the clock ticks away. Then he shakes his head. "We were too optimistic on timing," he says. "Maybe what we should have done was not bought it."

Mr. Feinberg took over Chrysler almost exactly two years ago, promising to revive the company. Chrysler filed for bankruptcy protection at the end of April. So how he and his private equity firm, Cerberus Capital Management, choose to describe their journey with Chrysler is a delicate matter.

If he says he should have shelled out more money to help Chrysler, he could face the ire of investors who have already suffered heavy losses on his gambit. If he says he should have simply dumped Chrysler's auto arm, while clinging to its more promising finance unit, he could be accused of caring more about his wallet than he did about Chrysler's workers and the automaker's role in the economy.

Continue reading the main story

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Mr. Feinberg's education at the hands of Chrysler, the government and economic reality is emblematic of the limits private equity players have encountered as they've sought to reap outsize returns while also contending that they had the smarts and managerial prowess to repair companies of any size. Not too long ago, some pundits and analysts wondered whether private equity firms — backed with a rising tide of easy bank loans — could gain enough traction to make runs at seemingly untouchable behemoths like General Electric.

When Cerberus began poking around Detroit, some at the firm said they thought that the American automobile industry was going to be the biggest turnaround story in history. In sessions with potential investors in the last few years, the Cerberus team came across as passionate, skilled and incredibly confident that they could succeed where others had failed.

"I thought, wow, this really signals a real change in the landscape here," recalls a person who attended a Cerberus session who asked to remain anonymous because of agreements he signed. "I guess it gave me hope. The auto companies needed an enormous amount of capital, and where else was it going to come from?"

John W. Snow, a former Treasury secretary in the Bush administration and Cerberus's chairman, also heralded Cerberus as Chrysler's savior, likening the firm's investment to the government rescue of Chrysler in 1979.

"Over 25 years ago, when Chrysler faced bankruptcy, it turned to the United States government for assistance," Mr. Snow said at a National Press Club meeting in 2007. "Today, Chrysler again faces new financial challenges. But it is private investment stepping in to inject much-needed support."

Cerberus and its co-investors ultimately invested $7.4 billion in Chrysler, a sum now worth an estimated $1.4 billion. Ideally, Cerberus hoped to wed Chrysler's finance arm to another finance company it controlled, GMAC. To that end, the risks in Chrysler's auto business were something that the Cerberus team thought it could manage and that wouldn't stand in the way of making billions of dollars for investors.

"This will go down as one of the investments made at the very top of the credit bubble," Josh Lerner, a professor who studies private equity at the Harvard Business School. "They don't look good. This will be a black eye on their record." Indeed, GMAC and Chrysler became so weak that they needed $22.6 billion in government aid in the last year to stay afloat. For Chrysler and its workers, investors, business partners and customers, was all of that worth it?

Mr. Feinberg defends his actions, saying he did everything possible to help the company. Known for avoiding publicity, he says that he was naïve not to anticipate the public attention that would surround him once he bought Chrysler and that he would have avoided the investment had he known.

Photo

Stephen A. Feinberg, a co-founder of Cerberus. Credit Haraz N. Ghanbari/Associated Press

"I always view the press as something for guys who were trying to do big things," he says, perhaps overlooking that Chrysler was, indeed, a very big thing.

DON JOHNSON, a former Chrysler employee, says he worked on initial production of the Jeep Liberty at a plant in Toledo, Ohio, in summer 2007, when Cerberus won the right to buy Chrysler from Daimler of Germany.

To the surprise of some, Mr. Feinberg managed to woo the support of the United Automobile Workers for the deal. But Mr. Johnson says he was always skeptical about the carmaker's new owners. "Cerberus did not have a clue about the automotive industry," he says. "I don't think anything could have been worse."

Still, if you peel back Mr. Johnson's argument, you quickly find a story of an automaker that was already in peril by the time Cerberus came on the scene. For example, he says the body shop at his plant couldn't produce Jeep frames fast enough to keep up with the paint and assembly lines. Instead of fixing the problem, he says, the factory paid the body shop workers overtime to come in Sundays to keep up.

Cerberus took the helm about a week after Mr. Johnson's team ran into problems with the Jeep. When Mr. Feinberg addressed workers at a town hall meeting at Chrysler's headquarters in Auburn Hills, Mich., shortly after the deal, he spoke of his long love of American manufacturing, according to workers who attended the speech. In particular, he said he was proud to repatriate Chrysler's ownership from Germany.

"Steve saw this as a huge patriotic opportunity, in addition to a great investment," says Robert L. Nardelli, the former Home Depot chief executive whom Cerberus installed at Chrysler's helm.

Although some investors doubt that anything other than profits drove Mr. Feinberg's investment, many say they believe that he was authentically excited by the prospect of reviving an American corporate icon — a theme that Mr. Feinberg is happy to support.

Surrounded by rifles, a motorcycle and model cars in his office, Mr. Feinberg mentions family members who have served in Iraq and a brother-in-law who worked at G.M. He apologizes for rambling and explains his motivation for investing in Chrysler: "I love this country," he says. "I feel it's been great to me. I had a great chance."

Still, Mr. Feinberg, 49, has spent years as a dealmaker. The son of a steel salesman, he graduated from Princeton in 1982, where he studied politics. He went into finance so he could pay off his student loans. He worked at Drexel Burnham, the investment bank made famous by Michael R. Milken before it collapsed, and then, after a brief stop at a smaller firm, he was a co-founder of Cerberus in 1992.

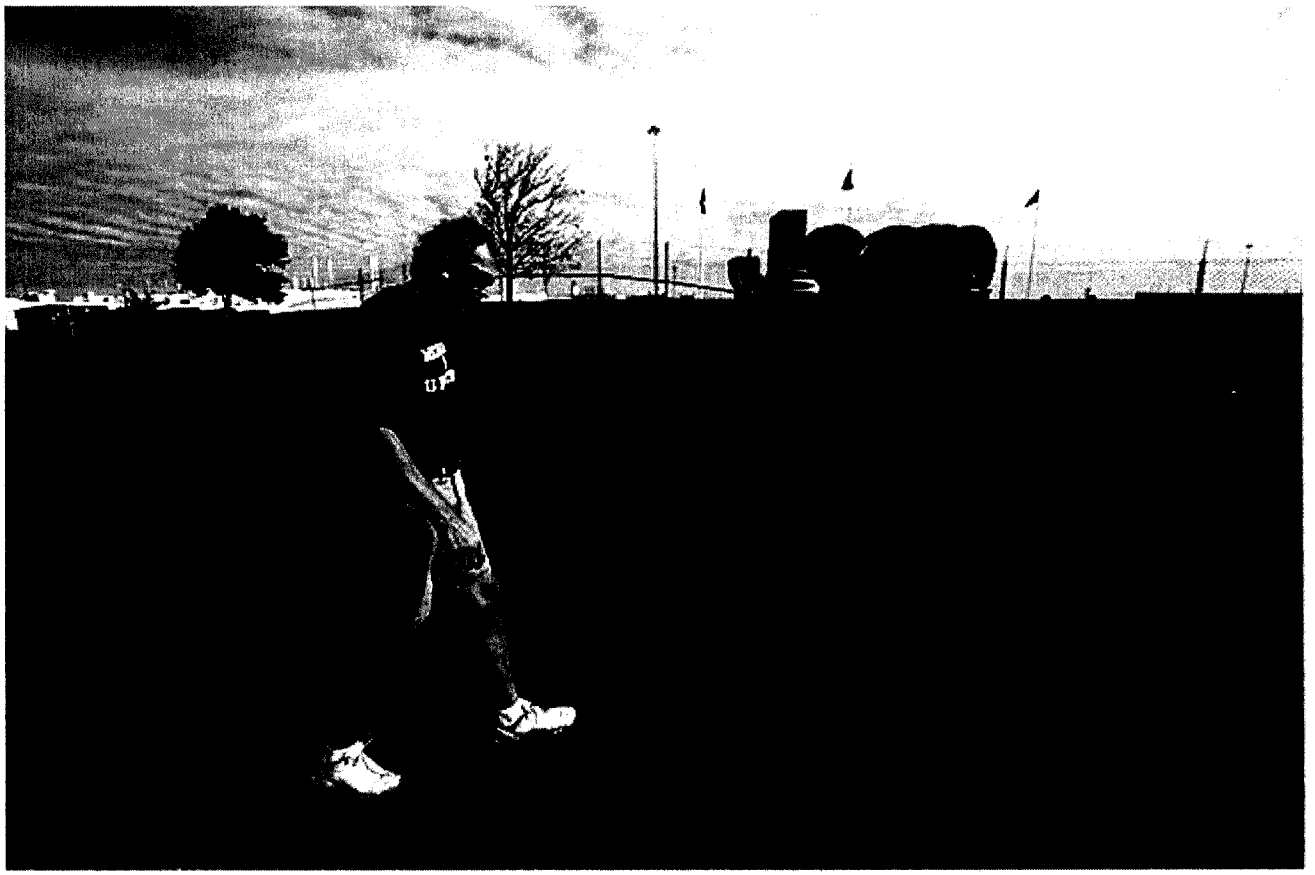
For years, Cerberus was largely a trading shop specializing in distressed debt. But by the mid-1990s, Mr. Feinberg expanded into buying and selling distressed companies and hired dozens of seasoned corporate executives to run them. Chrysler was the biggest prize he had ever bagged, and many co-investors say they always believed Cerberus's stake in Chrysler's auto operation was never the main reason the firm was interested in the company.

According to five people who heard Cerberus's Chrysler pitch, all of whom requested anonymity because of confidentiality agreements, Mr. Feinberg's deputies valued the financing unit more than the auto operation. In fact, the deputies believed, the finance unit's value covered the cost of buying Chrysler, making the car company something of a bonus — if that part of the investment worked out, great; if not, Cerberus could still profit on the finance unit.

Mr. Feinberg says he believed the automobile operation had great potential value, perhaps even more than the finance arm if Cerberus could put the automaker on the right track. But that meant he and Mr. Nardelli (who had never overseen a car company) had to effectively manage the auto operation — no small feat.

By October, only three months into Cerberus's tenure, Mr. Johnson says it was becoming obvious to him and other workers that trouble was ahead. "We went from three shifts to two shifts to one shift within a year," Mr. Johnson recalls. "Then there was just down week after down week."

Photo



"Cerberus did not have a clue about the automotive industry," said Don Johnson, a former Chrysler employee in Ohio. "I don't think anything could have been worse." Credit Fabrizio Costantini for The New York Times

To reduce expenses, Mr. Nardelli cut excess factory capacity and billions of dollars in fixed costs. He improved the interiors of several models, which bolstered some of its approval ratings.

But there still wasn't a strong demand for Chrysler's product line, which was packed with large vehicles like minivans and S.U.V.'s at a time when skyrocketing gas prices were making consumers interested in more fuel-efficient cars.

The company was aware that its lineup was far too limited. And Cerberus sent Chrysler executives around the world to seek partnerships with foreign automakers like Nissan. The hope was that those companies would help provide a broader product line for dealers.

Continue reading the main story

But there was not time for any of the efforts to bear fruit. Chrysler was burning through cash.

"Once the car market stalled, the cash in the auto market evaporated," says Maryann Keller, a longtime auto analyst and consultant, of Chrysler's predicament. "The cash was leaving their balance sheet, and they weren't selling cars to make money they could invest."

That situation was made worse by hefty interest payments on more than $10 billion in debt that Cerberus arranged for Chrysler as part of the takeover, which left the automaker carrying piles of debt just as auto sales were about to plummet. While many private equity deals involved saddling companies with debt to pay off investors, Chrysler needed to take on more debt because it had so little cash on hand to finance its operations, some analysts say. The company paid back some of the debt in November 2007.

Ms. Keller says that the company that Mr. Feinberg took over was already suffering from myriad problems: a bad cost structure, a limited product line and no pipeline of more diverse offerings. In short, she says, Cerberus had simply bought "a basket case."

At the beginning of 2008, Mr. Feinberg sized up his investment in a private letter to his investors. "We do not need to be heroes to earn a good return on the investment in Chrysler," he wrote. "We do not need to transition the car industry or even to return Chrysler to a much stronger relative position in the U.S. car market in order to be successful."

His letter sent a chill around New York, where dozens of hedge funds had joined in his Chrysler bet. Although these firms had agreed to let Cerberus control decisions involving their investments, there was fear about how his harsh words might affect the industry's image. After all, such a steely, hard-headed look at Chrysler didn't mesh with the patriotic tone of Cerberus's other statements about the company. Nor did it comport with the private equity industry's broader arguments that its investments were good not only for its firms, but also for America.

Cerberus, meanwhile, was unable to stop Chrysler's downward spiral. Last fall, Chrysler and General Motors tried to merge their operations, a scenario Mr. Feinberg supported, but a deal

could not be struck. And in November, Chrysler announced a huge employee buyout. Mr. Johnson, the worker at the Toledo plant, joined thousands of others who signed up.

"There was absolutely no hope" among employees accepting the buyouts, he says.

Mr. Feinberg says that he sympathizes with Mr. Johnson, but that he also believes business restructurings are, unfortunately, often brutal affairs. "It's demoralizing when things go down," he says. "But that's a turnaround, you know. Some guys make it; some guys don't want to deal with it. This was the most difficult environment. You couldn't think of a worse storm for an employee to have to live through."

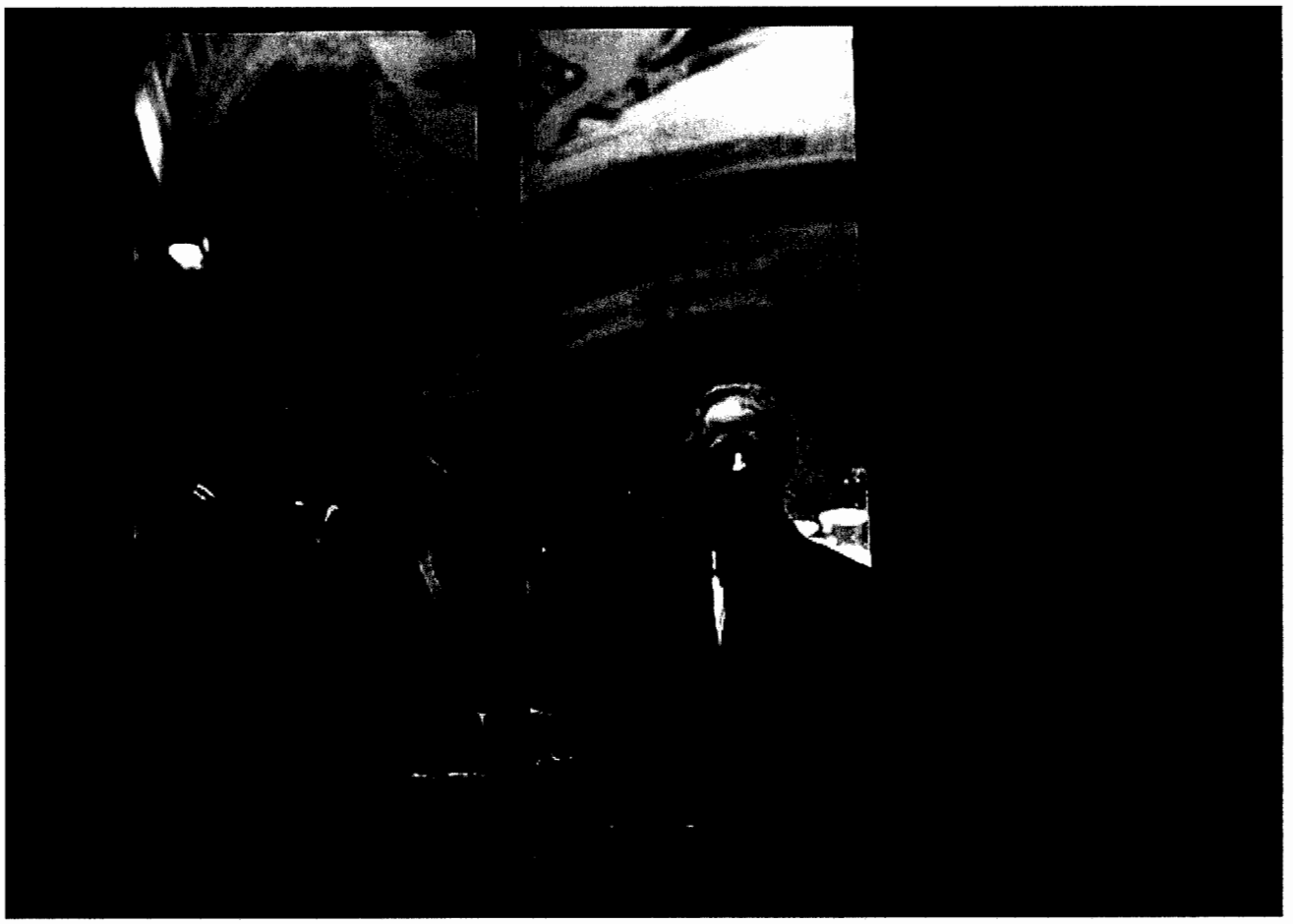
It was also, as it turns out, a bad storm for Chrysler's owners.

MR. FEINBERG, a longtime free-market enthusiast and a Republican who never envisioned himself needing the government for help, suddenly found himself running a company that needed federal support to stay alive.

By early last December, with Chrysler bleeding cash, he had become a vocal presence in Washington, circulating around Congressional offices to get his story out. He even offered to put tens of millions of his own money into Chrysler, a move that would have been largely symbolic.

"He said his dad was a blue-collar manufacturing type," says Senator Bob Corker, Republican of Tennessee, who often spoke with Mr. Feinberg. "You sit there and you talk to Steve, and you can tell he's from a background that greatly understands what the American worker is all about."

Photo



Steve Feinberg on Capitol Hill in December, as lawmakers worked on a bailout for automakers. "From the day we bought it," he recently said of Chrysler, "we worked hard to improve it." Credit Brendan Smialowski for The New York Times

But Mr. Feinberg soon found himself negotiating with government officials who understood what Wall Street was all about.

When Congress did not pass a rescue bill for the automakers, the Treasury Department stepped in, using financial authority it had already assumed from its bailout of the banking system. Cerberus's fate moved into the hands of Steven Shafran, a Goldman Sachs alumnus who represented the government and was regarded inside Treasury as a tough negotiator.

Mr. Shafran forced Cerberus to accept a painfully low valuation of its GMAC stake. He also quashed arguments by Cerberus that Chrysler's financial arm shouldn't be responsible for paying back bailout funds provided to Chrysler's auto operation.

At some point in December, Mr. Feinberg began to realize that Cerberus's investment in Chrysler's auto operations was largely unsalvageable. In a phone call with Mr. Shafran about 2 a.m. on Dec. 19, he offered to simply give the car company to the government, according to five people briefed on the call.

Mr. Feinberg says he was offering Cerberus's stake in the auto company to the government as a bargaining chit for negotiating with bankers, the union and others. But some Treasury officials were worried that he was simply trying to avoid leaving the finance unit on the hook for $2 billion of the $4 billion the auto operation received in federal aid.

Treasury officials declined Mr. Feinberg's offer and also were so wary of his motives that they put in a rule requiring that federal bailout money provided to Chrysler's financial arm could be used only to help Chrysler's auto unit. Despite all of that back and forth, Mr. Shafran says he believes that Cerberus behaved professionally. "They were prepared to work closely with us to ensure a smooth landing for the car company," he says.

When the Obama administration took over this year, Mr. Feinberg got a second chance to negotiate. He faced yet another Wall Street refugee trying to save the auto industry, Steven Rattner, as well as Ron Bloom, a former banker who worked more recently for the United Steelworkers union.

Mr. Feinberg was particularly focused on decreasing the $2 billion guarantee the previous administration had wrung out of Chrysler's financial arm. He eventually knocked that amount down by hundreds of millions of dollars after agreeing to give up some other things the government wanted — something Mr. Feinberg regards as a fair outcome.

"Basically," Mr. Bloom says, "they realized they made a poor investment and wanted to end it in a decent way." Chrysler filed for bankruptcy protection on April 30 to help clear the way for a merger with the Italian automaker Fiat.

Cerberus now values its Chrysler stake at 19 cents on the dollar. It is a humbling and embarrassing figure for Mr. Feinberg. But it's better than zero cents on the dollar, which is what his stake might have been worth had the government not bailed him out.

Mr. Feinberg and his colleagues at Cerberus maintain to this day that their time at Chrysler was, in part, a reflection of their patriotism — a view that some analysts find hard to swallow.

"It's hard to believe that any of these firms — including Cerberus — will be viewed as patriots in 10 years," said John Rogers, a private equity analyst at Moody's Investors Service, "because I don't think their impact on any of these companies will be seen as so positive for the overall economy."

Mr. Feinberg still begs to differ, saying his experience at Chrysler has left him feeling like a good citizen.

"There were times we could have been tougher and pushed harder and gotten more," he says, "but it wasn't the right thing for the country."

Acquisitions

Number of Acquisitions 21

Cerberus Capital Management has acquired 21 organizations. Their most recent acquisition was Sparton on Dec 12, 2018.

Which types of acquisition does this organization make most frequently? pro Show

Acquired Organization Name	Announced Date	Price	Transaction Name
Sparton	Dec 12, 2018	—	Sparton acquired by Cerberus Capital Management
SGI Frontier Capital	Nov 1, 2018	—	SGI Frontier Capital acquired by Cerberus Capital Management
Subsea Communications Created Subcom LLC to acquire Subsea Comm. bus. of TE Connectivity	Sep 17, 2018	Created Holding CO. 10/2018 —	Subsea Communications acquired by Cerberus Capital Management
Officine CST SpA	Jul 6, 2018	—	Officine CST SpA acquired by Cerberus Capital Management
WFS	Jun 19, 2018	—	WFS acquired by Cerberus Capital Management
Electrical Components International	Apr 26, 2018	—	Electrical Components International acquired by Cerberus Capital Management
Cyanco	Feb 7, 2018	—	Cyanco acquired by Cerberus Capital Management
Bushkill Group	May 19, 2017	—	Bushkill Group acquired by Cerberus Capital Management
Staples Europe	Dec 7, 2016	$1.8B	Staples Europe acquired by Cerberus Capital Management
ABC Group	Jul 1, 2016	—	ABC Group acquired by

crunchbase

Cerberus Capital Management > Acquisitions

WOLF STREET
The Stories behind Business, Finance & Money

PE Firm Cerberus Capital's "Rollup" Collapses into Bankruptcy

by Wolf Richter • Mar 26, 2018 • 67 Comments • Email to a friend

Bankruptcy becomes an increasingly common "exit." And the pension obligations?

On Sunday, storied gun maker Remington Outdoor Co. filed for Chapter 11 bankruptcy, buckling under its debts. Its intention to file for bankruptcy has been known at least since February, but sources told The Wall Street Journal that the filing was delayed after the school shooting in Parkland Florida on February 14 that re-awakened the national debate on gun regulations.

As part of the deal negotiated beforehand, shareholders will hand over the company to *secured* creditors, which include Franklin Resources and JPMorgan Chase's asset-management division. In turn, these creditors will forgive part of the company's debt. When it's possible to do so, the new owners will unload the reorganized company.

Among the largest *unsecured* creditors listed in the petition are the Pension Benefit Guaranty Corp., which is the US government's insurer for failed private-sector pension plans, and the Marlin Firearms Company Employees Pension Plan. Remington had acquired Marlin Firearms in 2008. So the idea is that the restructured

OUR BRILLIANT CATEGORIES

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company will walk away from its pension obligations.

Who are the shareholders that are surrendering control?

Fund investors of PE firm Cerberus Capital Management. Cerberus acquired Bushmaster Firearms International in a leveraged buyout in 2006. In 2007, it acquired Remington, and later put them under a holding company, Freedom Group Inc., that also acquired other firearms makers, such as Marlin in 2008. Cerberus was doing a classic "rollup" in the firearms industry.

Those were the heady days of the fabulous leveraged buyout boom with its "Merger Mondays," as CNBC used to call it – as many of the mergers were announced early Monday, similarly to bankruptcy filings.

In a leveraged buyout the acquired company is made to borrow the money for its own acquisition and pay those funds to the acquirer, which uses those funds to pay off the bridge loan originally taken out to fund the initial deal. In other words, the acquirer has little or no equity in the deal, and the acquired company has been loaded up with debt. Hence "leveraged buyout."

The plan was to sell this structure at a big profit to the unsuspecting public via an IPO. But months after the Marlin acquisition closed, the Financial Crisis blew into the open. Then came December 2012, when a gunman used a Bushmaster rifle to kill 20 kids at Sandy Hook Elementary School in Newtown, Conn. Nine families of victims brought a wrongful-death lawsuit against Remington, alleging it was liable for selling a weapon unfit for

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by Wolf Richter • Jun 23, 2019 • Email to a friend
The Fed has already accomplished more with its

civilian use. The case is before the Connecticut Supreme Court, and with this decision hanging over the company, potential buyers completely disappeared.

Knowing that trouble was brewing, Cerberus separated Remington Outdoor — the name Freedom Group had already been scuttled — from its funds in May 2015 and opened a door for its fund investors to get out. At the time, the Wall Street Journal reported:

> Cerberus sent a letter to its investors, which include pension funds and endowments, telling them that it has separated Remington Outdoor Co., the maker of Remington and Bushmaster rifles formerly known as Freedom Group Inc., from its funds and will allow any investor wishing to cash out of the company to do so, according to a person familiar with the letter.

The letter claimed that the company's value, including debt, was about $880 million.

The deal to allow fund investors to cash out had a typical private-equity structure that has doomed so many companies: Remington used the proceeds from a 2013 debt sale to pay off equity investors. So the money the company had borrowed for operating capital was suddenly gone. And Sunday's bankruptcy had moved a step closer.

This scenario of pre-Financial Crisis LBOs now going bankrupt is playing out in other stressed industries, such as the brick-and-mortar retail meltdown, including the liquidation of Toys 'R' Us, or in the radio broadcasting sector with the $20 billion bankruptcy of iHeartMedia.

Here's the thing: If a PE firm cannot exit the LBO profitably, either by selling it to a deep-pocket

verbiage this year than it had last time when it cut rates all the way to zero and did trillions of dollars of QE.

corporation, or by selling it via an IPO, it is stuck with the company.

What causes a company to file for bankruptcy protection isn't declining sales or thin profits but debt (and sometimes other obligations) that it can no longer handle. A PE firm could invest equity in the company to pay down this debt burden, and it could invest equity to improve the company's operations. But that's a not its job. Its job is to load up the company with debt, extract cash, and then "exit" via a profitable sale either to another company with deep pockets or to the public via an IPO.

When those two potential exits are blocked, the company is left to bleed out. And once the last drop of liquidity is gone, the company files for bankruptcy protection. This is the increasingly common third exit for PE firms from their LBOs.

What are zombie retail locations worth? Some of them "little or nothing." See Toys "R" Us and its commercial mortgage backed securities. Read… What Are Zombie Retail Stores Really Worth: Answers Emerge

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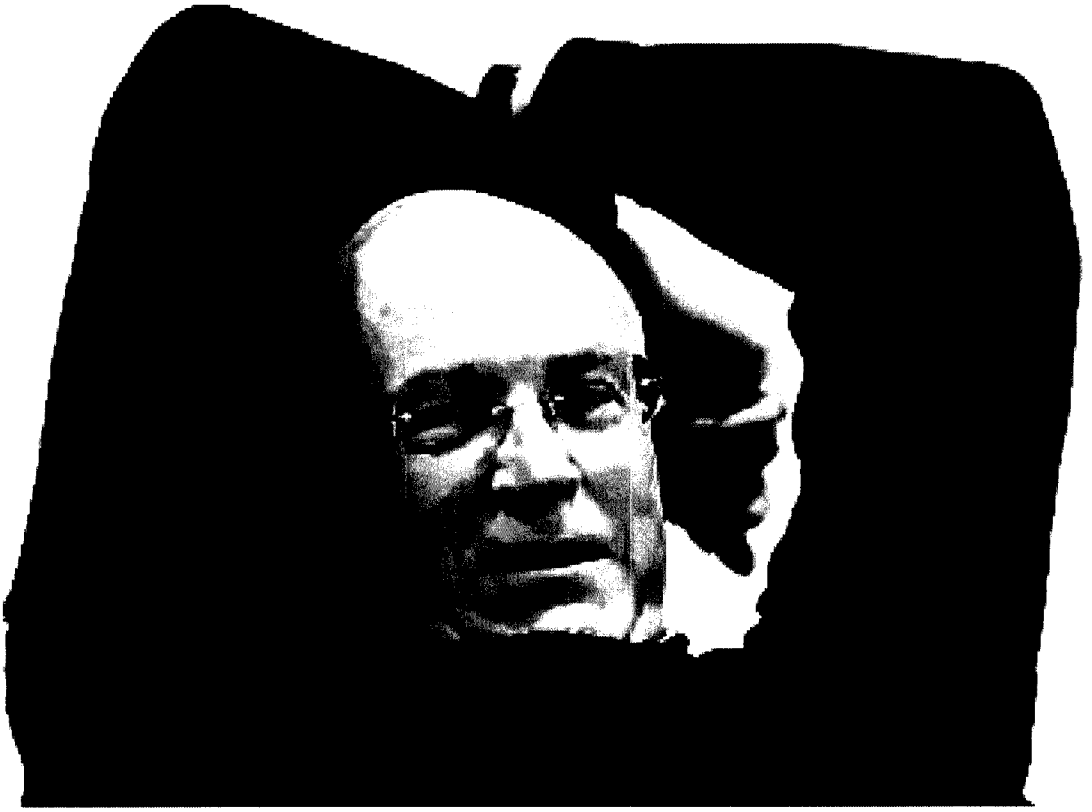
The Guardian

Meet the bankruptcy barons who turn bust into boom

In the third part of our series looking at the stories behind the slump, we turn the spotlight on the dealers in debt who make a profit from the failures of others



Private equity boss Jon Moulton. Photograph: David Levene

Elena Moya

Mon 26 Jan 2009 19.01 EST

The staff and owners of Manchester tea-bag maker JR Crompton thought a sympathetic bank manager would rescue them in times of trouble; after all, the company had been around since 1856. What they didn't know was their future was in the hands of young, aggressive traders in a well-known investment bank in London. The traders had bought parts of the company's debt, gaining enough control to block a proposed restructuring. The company was pushed into administration and the assets sold. Crompton ceased to exist.

Vulture funds are at the extreme end of a booming market in distressed debt - pushing companies into administration for profit even when other investors feel the company is worth saving.

The funds circle struggling firms and buy their debt at a discount to gain control of the business. Usually hedge funds or proprietary desks at large investment banks, the funds may turn their debt into equity in a restructuring, gaining a stake or full control of the firm, or sell the assets in a liquidation, receiving a higher price for the debt than they paid for it.

"When debt has been acquired at a substantial discount to par, the fund may still make a profit notwithstanding the liquidation of a company," says Mark Hyde, global head of restructuring at law firm Clifford Chance. "If you buy at 20 and recover at 30, you've made a good profit."

Administration will also relieve the company of its pension deficit, making a sale of the assets more attractive - which was the case at Crompton.

The deals are struck behind the scenes. The secondary market where loans trade is not public, with investors buying and selling large amounts of a company's debt in bilateral transactions.

Usually based in offices in upmarket areas, vulture funds also tend to act together. Last summer, debtholders of Martinsa Fadesa, Spain's largest construction company, imposed stringent conditions on a restructuring deal, which led to the company's failure. The funds, which bought the debt at a discount after Morgan Stanley sold some of its loans, negotiated favourable terms for themselves: as soon as the sale of assets started, they would receive payments within one year, whereas some Spanish savings banks will have to wait as much as seven years.

Other funds have become professionally noisy. By imposing conditions or threatening a restructuring, they encourage other creditors to buy them out just to see the deal through. Most restructurings need the agreement of all creditors.

Not all distressed funds are run by aggressive players who put companies into insolvency deliberately. "Debtholders are entitled to get as much as they can but you want to save jobs as well," says distressed-debt investor Jon Moulton. "But if somebody deliberately blocks a restructuring, or does nothing about a problem, that's being an asset stripper. All we're trying to do is to find value, help a company. More often than not we preserve jobs, but sometimes a hopeless business needs to close down."

Vulture funds are only one of many players to profit from a company's misfortune. Those at the top of the tree include private equity directors, who bought firms with as much debt as possible - sometimes putting in no equity or cash at all - and used the company's profits to repay debt instead of making operational improvements. Private equity firms also borrowed even more money to pay themselves substantial dividends, credit rating agencies such as Standard & Poor's warned.

"Undoubtedly people have benefited during the good years from financial engineering,"

says Buchan Scott, head of investor relations at Duke Street Capital, the private-equity firm behind Focus, the DIY chain which had to be restructured. "Ultimately, the debt was too high and the sector fell off the cliff. We didn't call the administrators, we ended selling it to Cerberus, but it still was one of our most successful investments [after growing it from seven to 450 stores]."

Primary lenders, such as Barclays, RBS or Deutsche Bank, sold billions of pounds worth of loans for leveraged buy-outs (LBOs) in the market, allowing hedge funds and other investors to take positions in a company's debt.

Young and financially savvy, distressed-debt players study companies - sometimes beyond the belief of bankers and company directors. A US hedge fund once produced an 800-page report on Drax, Britain's largest power station, whose failure turned into multimillion-pound profits for funds such as BlueBay when its debt was converted into equity. Through similar transactions, BlueBay holds - or has recently held - stakes in Polestar, a printing business, and Danoptra, a gaming company.

Vulture funds swoop after a company is about to or has breached its banking covenants - a move than can give them the right as creditors to call in the administrators. The creditors usually appoint banking advisers, such as Rothschild, Close Brothers or Houlihan, and specialist law firms, including Clifford Chance, Freshfields or Allen & Overy. The company appoints its advisers as well. Each stage of the process generates fees for all the professionals involved.

"Round-table meetings between all the stakeholders can get quite heated - you see people getting very angry, shouting," Hyde says. "This is not surprising given that somebody who has to accept that they're going to lose all their investment is likely to get emotional."

Alfred Schefenacker, a German industrialist, was absent from the meeting that had to decide the fate of the car parts maker he had devoted his life to. Company advisers Alix Partners moved the firm's headquarters to from Germany to Britain's more creditor-friendly administration and restructuring system. Schefenacker creditors turned some of their debt into equity, rescuing the company but leaving the founder and owner with a substantially reduced stake. It wasn't his company any more.

Some companies are trying to ring-fence their loan syndicate, closing the doors to vulture funds. "We don't tend to have vulture funds in our company portfolio - we like to have control of the banking syndicate to ensure a proper alignment of interest in case things go wrong," said Duke Street's Scott. Vulture funds "have other agendas - they are much more short-termist and less relationship driven".

Hedge fund managers have found their niche in the market. Wealthy and flexible, they will pick up the distressed assets of insolvent companies and recycle them, said Matthew Prest, head of European special situations group at Close Brothers.

Vulture funds may also help a business survive by assuming a level of risk that high-street banks would not tolerate - and charge accordingly for it.

"We don't see hedge funds as being difficult," says Alistair Dick, restructuring director at Rothschild in London. "They can often provide more flexible capital than the original lenders - typically banks and CLOs [collateralised loan obligations] - so they can help in the process."

The vultures risk becoming distressed themselves if their trades go wrong. "Buying distressed debt is always a gamble," says Hyde.

Some hedge funds are stuck in deals because buyers are hard to find. Others have bought debt at 60p to the pound only to see it fall further. They are under pressure as the $1.2tn (£860m) hedge-fund industry is expected to see an outflow of $450bn in assets this year through losses and withdrawals, on top of the $600bn lost last year, according to Bloomberg News.

"People are scared now to invest in turnaround opportunities - they don't think we've reached the bottom," Prest says. "Things will turn when people start believing they have some visibility about the future, some confidence about the forecast in the company, or when prices have gone to a certain level.

"We still have a very illiquid secondary-debt market. Buyers are looking at things from a very bearish point of view, while sellers think tomorrow will be brighter."

At this point, only the administrators have their fees guaranteed.

Cerberus, and its reputation

By Michael Flaherty
December 4, 2007

Will Cerberus' reputation be damaged, as the firm has now had two deals fall apart in the past month alone? The answer is, probably, no.

Certainly a company's board will raise the issue of loyalty at future meetings. But will they slam the door shut when Cerberus shows up offering a 20 % plus premium to an undervalued company? Unlikely.

On Tuesday, Cerberus' Option One deal with H&R Block was officially called off, to the surprise of very few. Unlike United Rentals, a deal that Cerberus pulled last month to the shock of the market (and frankly, a lot of top folks at the company), the Option One agreement had been unraveling since the subprime mortgage meltdown took hold this summer. The original majority buyout was toast as of a few months ago, and all that was left was the possibility of Cerberus scooping up some servicing units. So much for that idea.

Oh and by the way, Cerberus' portfolio company Aegis Mortgage Corp. filed for bankruptcy in August.

A blow to their image? Maybe. But Cerberus will still be getting plenty of business, bankers and investors say.

Folks on Wall Street say that Cerberus' behavior in the United Rentals deal is hardly exemplary in terms of painting buyout firms as the friendly, faithful-to-the-end buyer–or, if you will, the "white knight" swooping in to fend off angry shareholders and tired management teams. Buyout firms typically seal deals with a "you can count on us," kind of handshake.

The buyout industry has tried very hard in the last year to boost its image from the "asset stripper and flipper" reputation that has clung to it. Cerberus' decision to walk from United Rentals without even citing a material adverse change in the business certainly hasn't painted a pretty picture of the industry.

But there is one thing that so many on Wall Street point out. Under the leadership of the legendary Stephen Feinberg, Cerberus is seen more as a trading shop, as opposed to a nuts and bolts buyout firm.

Indeed, they are the only major buyout player with such a sophisticated hedge fund operation. To be fair, Cerberus is very much concerned about its image after the United Rentals dust up, and has ramped its public relations effort since the mud-slinging began.

So with a United Rentals decision yet to be determined, and with Option One deal behind it, Cerberus will keep treading through the market searching for targets in need of capital and industry insight. And they'll find them, and will likely keep minting money and raising loads more of it.

(Image credit. Cerberus, three-headed dog. Alison Smith. http://www.amosink.com)

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Cerberus Forms SubCom, Acquires Business

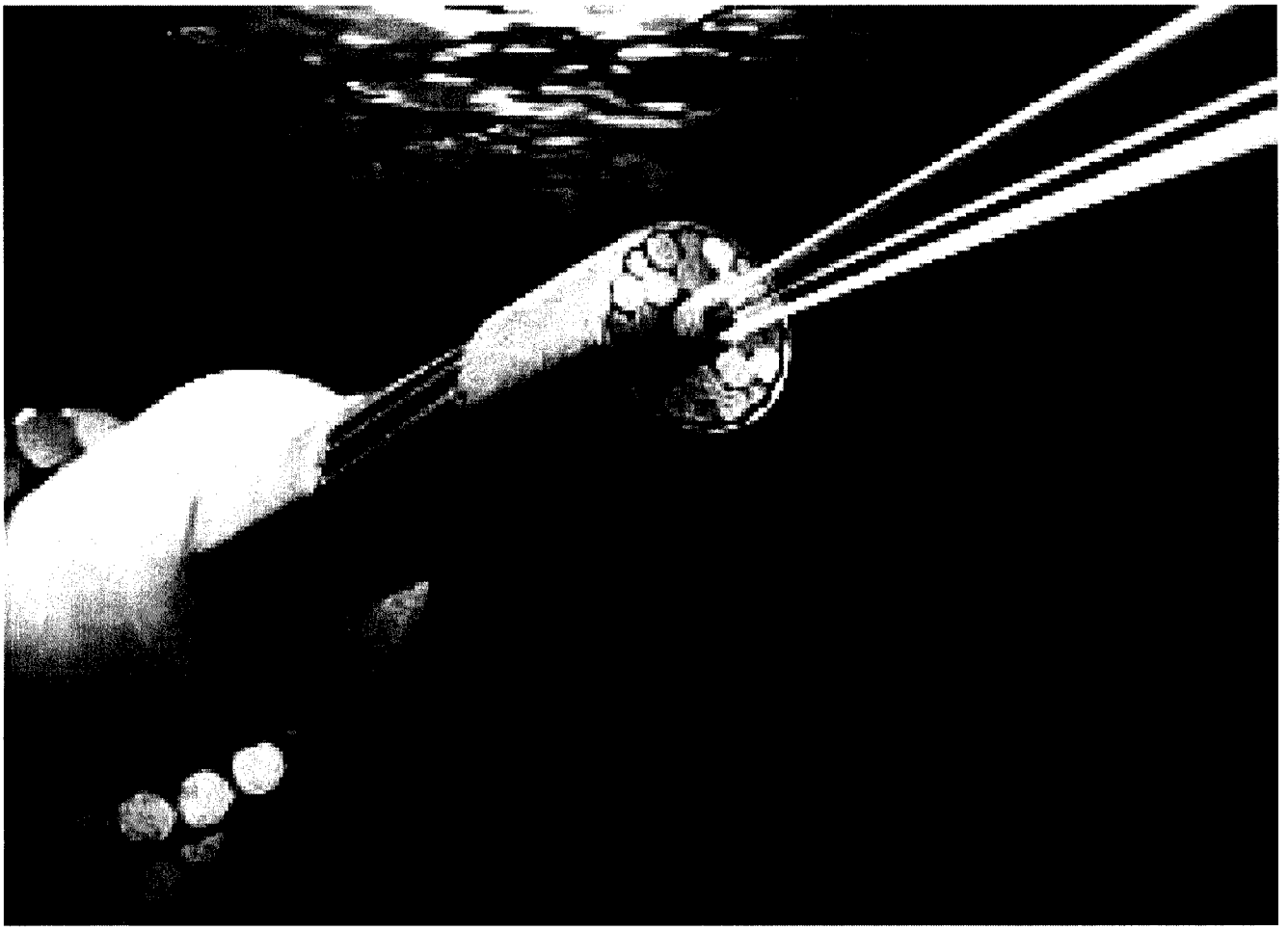
peprofessional.com/2018/11/cerberus-forms-subcom-acquires-business

November 5, 2018

Cerberus Capital Management has formed **SubCom LLC** to acquire the subsea communications business of **TE Connectivity**.

SUBCOM

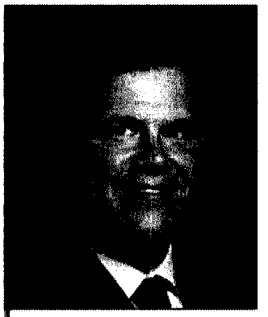
SubCom designs, manufactures, deploys, and services fiber optic cable systems that are used to transmit data and communications. The company has completed more than 200 networks (with enough undersea cable to circle the Earth more than 17 times at the equator) for many of the world's leading technology companies and entrepreneurs.



SubCom is headquartered near New York in Eatontown, NJ and has more than 1,400 employees on four continents (www.subcom.com).

At closing of the acquisition, Cerberus named **David Coughlan** as the new CEO of SubCom. Mr. Coughlan was previously the General Manager of the business from 2001 to 2014. From 2014 to 2016, Mr. Coughlan was the General Manager of TE's Sensor Solutions business unit and, most recently, he was the Vice President of Business Development at publicly-traded Littelfuse.

"I am excited to be back at SubCom and working with our team members as we begin this new chapter," said Mr. Coughlan. "SubCom is already the largest subsea fiber optic cable solutions provider with #1 share in the long-haul market. Through this partnership with Cerberus, we will be able to execute on strategic opportunities to position us for long-term success, while continuing to deliver the highest lifetime value network solutions to our global customers."



David Coughlan

TE Connectivity (formerly **Tyco Electronics**) designs and manufactures connectivity and sensor products for harsh environments in a variety of industries, such as automotive, industrial equipment, data communication systems, aerospace, defense, medical, oil and gas, consumer electronics, energy and subsea communications. The company has more than $13 billion in revenue and nearly 90,000 employees in over 50 countries. TE Connectivity (NYSE: TEL) is headquartered near Philadelphia in Berwyn, PA (www.te.com).

"We look forward to working with Dave and the SubCom team to build upon the business' leadership position," said **Michael Sanford**, Co-Head of Private Equity and Senior Managing Director of Cerberus. "We believe that need for reliable, high-performing undersea networks will continue to be exceptionally robust as demand for data and connectivity continues to increase around the world. With its industry-leading capabilities and reputation for operational excellence, we are confident that SubCom will continue to be the partner of choice to deliver and maintain these critical undersea networks for years to come."

Michael Sanford

Cerberus has approximately $35 billion of capital under management and invests in three strategies: global credit opportunities (which includes non-performing loans, corporate credit & distressed debt, mortgage securities & assets, and direct lending); private equity; and real estate. The firm was founded in 1992 and is headquartered in New York (www.cerberuscapital.com).

Acquirer

Cerberus Capital Management

PE FIRM

New York, New York
United States
www.cerberuscapital.com

PE ASSETS

30.0B USD

SIZE

Mega

INVESTOR TYPE

Sector Agnostic

DESCRIPTION

Cerberus Capital Management is a private investment firm that targets a wide range of global investments. Cerberus primarily looks for undervalued or distressed situations. Industry sectors of interes include aerospace and defense, apparel, automotive and industrial, building products, commercial services, consumer and retail, financial services, healthcare, manufacturing an distribution, paper, packaging, and printing, real estate, technology, telecommunications, transportation, and travel. Cerberus was formed in 1992 by Steve Feinberg and is based in New York. Cerberus also has offices/affiliates in Chicago, Illinois; Los Angeles, California; Atlant Georgia; London, United Kingdom; Baarn, Netherlands; Frankfurt, Germany; Tokyo and Osaka, Japan; and Taipei, Taiwan.

DEAL STATS	#
Acquisition	46 of 63
Sector (Renewable Energy)	1 of 1
Type (Secondary Buyout)	6 of 9
Country (Spain)	2 of 3
Year (2016)	1 of 3

ADVISORS

LEGAL

Ashurst LLP

Watson, Farley & Williams LLP

Acquirer

DESCRIPTION

PREVIOUS DEAL

DATE	TARGET	DEAL TYPE	VALUE
2015-12-17	Avon Products, Inc.	Buy	-

FOLLOWING DEAL

DATE	TARGET	DEAL TYPE	VALUE
2016-05-27	Blue Bird Corp.	Sell	-

SELLER

1

SELLER	DESCRIPTION
JHP Enterprises LLC PE FIRM Norwalk, Connecticut United States www.jhpenter.net	JHP Enterprises is a merchant bank and advisory firm. JHP provides management consulting and investment banking advisory services to private equity investors, companies and entrepreneurs in the United States, Latin America and Europe. JHP also sponsors and participates as principals in buyouts, restructurings and development capital transactions. JHP Enterprises was formed in 1988 and has offices in New Canaan, Connecticut and Barcelona, Spain.

DEAL STATS	#
Exit	1 of 1
Type (Secondary Buyout)	1 of 1
Year (2016)	1 of 1

FOLLOWING DEAL

DATE	TARGET	DEAL TYPE	VALUE
2017-01-02	Simplewater, Inc.	Buy	-

creditrisk monitor

Crown Subsea Communications Holding, Inc.

United States

This is a **Subsidiary**, click **here** for the Parent Company

Business Summary

Crown Subsea Communications Holding, Inc. was formed by Cerberus Capital Management, L.P. to facilitate its acquisition of the subsea communications business ("SubCom" or the "Company") of Tyco Electronics Group S.A. ("TE") for an aggregate purchase price of $325 million. TE's SubCom business, a part of the company's Communications Solutions segment, is a leading global supplier of undersea communications technology and marine services. The Company provides planning, engineering, manufacturing, installation and maintenance services for the construction of subsea fiber optic cable systems worldwide. SubCom's customers include telecom providers, operators, internet content providers, network consortiums and government entities.

Scores and Ratings

FRISK® Score	Z" Score	PAYCE® Score	DBT Index	IRA CQ Score	Moody's Rating	Fitch Rating	DBRS Rating	Morningstar Rating
-	-	-	-	-	Yes	-	-	-

Financials, News and Filings

Latest Statement	Last Audit	News	SEC Filings	Bankruptcy Filings	Suit & Judgment Filings	Tax Lien Filings

-	-	-	-	-	-	-

Monday, June 17, 2019

DEALS OCTOBER 31, 2018 / 10:12 PM / 8 MONTHS AGO

Buyout firm Cerberus to buy SGI for foothold in frontier markets

Couldn't find any Ch 11 bankruptcy on SGI Frontier Capital

Joshua Franklin

3 MIN RE

NEW YORK (Reuters) - Private equity firm Cerberus Capital Management LP said on Thursday it has agreed to buy SGI Frontier Capital Pte Ltd, giving it a foothold to invest in frontier markets in Asia and Africa.

Singapore-based SGI, which does not disclose its assets under management, invests in countries such as Ethiopia, Georgia, and Mongolia. These are considered earlier in their economic development than emerging markets like China and India.

Cerberus' new frontier markets platform will be run by SGI Founding Partner Gabriel Schulze and SGI Managing Partner Alexander Benard, and will initially invest out of SGI's existing assets and Cerberus' funds.

"The main attraction of the deal was the people. Gabriel knew Steve, our Co-CEO," Cerberus Chief Operating Officer Mark Neporent said in a telephone interview.

"We felt there was a tremendous intellectual and cultural fit. Our philosophy is if you go into a new market you have to live in it and be imbedded. Historically, we've had no presence in these markets where Gabriel and his team have been imbedded for many years."

Cerberus may eventually raise a dedicated frontier markets fund but currently feels it already has ample resources to make investments in these markets, Neporent added.

The deal comes as private equity investor confidence in frontier markets is being tested by concerns over the size of opportunities in some markets, particularly in Africa, as well as the strong performance of Western economies.

Africa-focused private equity fundraising fell from $4.5 billion in 2015 to $700 million in 2017, according to industry tracker Preqin. Emerging Asia-focused private equity fundraising, which excludes Hong Kong, Japan and Singapore, rose over the same period from $80 billion to $101 billion.

A Preqin survey last month found 53 percent of alternative assets investors plan to increase investments in emerging Asia and 30 percent plan to increase allocations to Africa.

New York-based Cerberus, whose co-founder and co-CEO Stephen Feinberg earlier this year was appointed chair of U.S. President Donald Trump's intelligence advisory board, has over $35 billion in assets.

Schulze, whose great-great-grandfather William Boyce Thomson founded gold mining conglomerate Newmont Mining Corp in 1916, used his family wealth to set up SGI in 2006.

In June, The New York Times reported that Schulze's early contacts with Jared Kushner, President Donald Trump's son-in-law and a senior White House adviser, facilitated a dialogue which led to a summit between Trump and North Korean leader Kim Jong Un. Schulze has declined to comment on that report.

Reporting by Joshua Franklin in New York; Editing by Christopher Cushing

Our Standards: The Thomson Reuters Trust Principles.

Cerberus Capital Management Acquires SGI Frontier Capital

cerberus

NEWS PROVIDED BY
Cerberus →
Nov 01, 2018, 07:00 ET

NEW YORK and SINGAPORE, Nov. 1, 2018 /PRNewswire/ -- Cerberus Capital Management, L.P. ("Cerberus"), a global leader in alternative investing, today announced the strategic acquisition of SGI Frontier Capital ("SGI"), a leading private equity firm focused on frontier markets in Asia and Africa.

Headquartered in Singapore with over 20 professionals across six locations, SGI has an extensive track record of direct investment in dynamic frontier markets, including Ethiopia, Georgia, and Mongolia. Since its founding over ten years ago, SGI has completed more than 30 transactions and currently manages a diversified portfolio of investments in a variety of key sectors, including consumer goods, clean energy, real estate, healthcare, and building materials.

"The rapid growth in frontier-market countries can offer attractive opportunities to investors with the right experience and on-the-ground presence," said Steve Feinberg, co-Founder and co-Chief Executive Officer of Cerberus. "SGI is an established leader with a proven track record in some of the world's fastest growing economies. We look forward to partnering with their talented team and advancing Cerberus' investment activities in emerging and frontier markets."

Gabriel Schulze, Founding Partner of SGI, commented, "With Cerberus, we are joining a global leader in alternative investing with deep resources and highly complementary platforms. We look forward to leveraging our combined investment expertise and operating experience to drive value in existing and future investments. Further, as part of Cerberus, we remain aligned and committed to ensuring our investments have a positive impact beyond achieving successful financial results, an approach core to SGI since our inception."

Mr. Schulze and Alexander Benard, Managing Partner of SGI, will lead Cerberus' frontier markets investment platform as Senior Managing Directors and Co-Heads.

Mark Neporent, Chief Operating Officer of Cerberus, added, "We are excited to welcome the SGI team to the Cerberus family. Not only are our capabilities and footprints complementary, we are aligned culturally and philosophically. Cerberus and SGI firmly believe in the power of business, economics, and investment to create social value. Together, we can direct even greater resources to areas of the world where the scarcity of private capital creates opportunities to generate attractive risk-adjusted returns and make valuable contributions to development."

About Cerberus

Founded in 1992, Cerberus is a global leader in alternative investing with more than $35 billion in assets across complementary credit, private equity, and real estate strategies. We invest across the capital structure where our integrated investment platforms and proprietary operating capabilities create an edge to improve performance and drive long-term value. Our tenured teams have experience working collaboratively across asset classes, sectors, and geographies to seek strong risk-adjusted returns for our investors. For more information about our people and platforms, visit us at www.cerberus.com.

About SGI Frontier Capital

SGI Frontier Capital is a private equity firm focused on the world's most dynamic frontier markets. Over the past decade, SGI has pioneered a unique approach to successfully investing in frontier markets. That approach combines rigorous financial analysis, a deep understanding of the local culture and business community, and strong in-country relationships. SGI looks for frontier markets that are undervalued because the global investment community either overestimates the risks related to the market, or underappreciates the market's growth potential. The scarcity of capital in these markets means that SGI is able to generate high risk-adjusted rates of returns while at the same time making valuable contributions to a country's development. → hmmm....

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SOURCE Cerberus

Related Links

http://www.cerberus.com

"Killer Acquisition"
- Protection of Market power

Cerberus Completes Acquisition of Sparton Corporation

SCHAUMBURG, Ill. – March 4, 2019 – Sparton Corporation ("Sparton" or the "Company") (NYSE:SPA) today announced the completion of its acquisition by Sparton Parent, Inc. (formerly known as Striker Parent 2018, LLC) ("Parent"), an affiliate of Cerberus Capital Management, L.P. ("Cerberus").

Pursuant to the terms of the transaction, Sparton has become a wholly

owned subsidiary of Parent and the holders of Sparton shares (other than shares held by (i) the parties to the transaction or any of their respective wholly owned subsidiaries and (ii) shareholders who have properlyexercised dissenters' rights) are entitled to receive an amount in cash equal to $18.50 per share of Sparton common stock. As a result of the completion of the acquisition, Sparton will operate as a privately held company and shares of Sparton common stock will cease trading on the New York Stock Exchange (the "NYSE") prior to the opening of trading on the NYSE on March 5, 2019, and will be delisted from the NYSE.

"This transaction represents an important milestone for our company," said Joseph Hartnett, Interim President and Chief Executive Officer of Sparton. "Cerberus is an exceptional financial and operating partner that will help drive Sparton's long-term growth and continue our track record of delivering industry-leading solutions to our customers around the world."

"We are excited to partner with Sparton as it looks to the future," said Dev Kapadia, Co-Chief Investment Officer of Private Equity and Senior Managing Director of Cerberus. "Building on the Company's foundation of market-leading capabilities and strong customer relationships, we look forward to supporting the Sparton team as they drive new innovations and capitalize on dynamic global opportunities."

About Sparton Corporation

Sparton Corporation, now in its 119th year, is a provider of complex and sophisticated electromechanical devices with capabilities that include concept development, industrial design, design and manufacturing engineering, production, distribution, field service, and refurbishment. The primary markets served are Medical & Biotechnology, Military & Aerospace, and Industrial & Commercial. Headquartered in Schaumburg, IL, Sparton currently has thirteen manufacturing locations and engineering design centers worldwide. Sparton's website may be accessed at http://www.sparton.com/ (http://www.sparton.com/).

About Cerberus

Founded in 1992, Cerberus is a global leader in alternative investing with

over $35 billion in assets across complementary credit, private equity, and real estate strategies. Cerberus invests across the capital structure where its integrated investment platforms and proprietary operating capabilities create an edge to improve performance and drive long-term value. Cerberus's tenured teams have experience working collaboratively across asset classes, sectors, and geographies to seek strong risk-adjusted returns for Cerberus's investors. For more information about Cerberus's people and platforms, visit Cerberus at www.cerberus.com (http://www.cerberus.com/).

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Sparton announced the issuance of two patents to the Company by the United States Patent and Trademark Office. One for an invention that protects electronic circuits from electromagnetic fields and one for the invention of a high efficiency power amplifier.

(https://sparton.com/news/sparton-announces-issuance-of-

two-us-patents-on-electronics/)

(http://www.linkedin.com
/company/29190)

BUSINESS

The Ghost Bosses

Private-equity firms have been rapidly buying and selling off companies for decades, and workers in Lancaster, Ohio, are living with the consequences.

BRIAN ALEXANDER MAR 13, 2017

LUCAS JACKSON / REUTERS

Men started making glassware along Pierce Avenue in Lancaster, Ohio, in 1905. That was when Ike Collins and his business partners fired up a small furnace to melt silica and other minerals inside The Hocking Glass Company near the banks of the Hocking River. Locals were soon calling the outfit "The Hockin'."

There were other glass companies in Lancaster, drawn there by cheap

natural gas. But following a 1937 merger with the New York-based Anchor Cap and Closure, The Hockin', now Anchor Hocking, grew into the world's largest manufacturer of glass tableware and the second-largest maker of glass containers such as beer bottles and peanut-butter jars. It even played a role in the invention of late-night TV, in 1950, by sponsoring the pioneering NBC show Broadway Open House. Anchor Hocking became Lancaster's largest employer by far, the rare Fortune 500 company based in a small town. At its peak, it employed roughly 5,000 people there, including executives in the headquarters, and many more in plants around the country.

But then came the 1980s. Since the start of the Reagan administration, Anchor Hocking has undergone a series of staggering transformations as a result of the financial manipulation that has come to define the American economy in the late 20th and early 21st centuries. Carl Icahn bought up shares and demanded a board seat and other changes, then agreed to leave the company alone after being allowed to sell back his ownership stake at a premium—a practice commonly referred to as "greenmailing." Then, Anchor Hocking was purchased in a leveraged hostile takeover by Newell Corporation. After Newell's own near-disastrous merger with Rubbermaid, Anchor Hocking was sold off in a debt-financed buyout to the huge private-equity firm Cerberus Capital Management. The company promptly fell into bankruptcy, out of which it was sold in another debt-financed buyout to a much smaller private-equity firm called Monomoy Capital Partners. There was a forced marriage with the silverware company Oneida, then an initial public offering after which the stock soon tanked. In quick succession came a shutdown, a notice (in accordance with the Worker Adjustment and Retraining Notification Act) that the place might close for good, a second bankruptcy during which the former creditors became the equity

owners, and countless leadership rotations. During the past 15 years, it's had three different corporate owners. In January the company's name was changed from EveryWare Global to The Oneida Group.

Even after all this, they still make glass in Plant 1, the plant Ike Collins started, and roughly 900 people still have jobs in Lancaster. But the factory has been poorly maintained and the people who work there have seen their wages and benefits walked back so that now some make just about what they made, or less, adjusted for inflation, than they did back when the saga began. In 1985, that was roughly $10 per hour for a 20-year, high-level employee, or about $22.50 in today's dollars.

The poor maintenance, the wages and benefits, and the drastic job cuts are only the most obvious costs. The spiritual damage may be more profound. Recently I sat in the small living room of a Lancaster glassman who works in Plant 1 and asked him if he knew which company currently owned Anchor Hocking. The last I knew, after the 2015 bankruptcy the ownership group consisted of former lenders that aren't in the business of running a glass manufacturer. The company was for sale. I wondered if there'd been some ownership consolidation, and my query to the company went unanswered.

"I think it's Monomoy," the glassman said. It wasn't Monomoy. I wasn't surprised by his reply, though. Keeping track of who owned what, or even the name of the parent company, is exhausting. Many employees have mentally disconnected from their employer in an effort to tune out the turmoil. None had any idea, for example, of the dividend recapitalizations the company had performed that benefited the private-equity sponsors and increased the company's debt burden. They had no idea what a dividend recap was. Some didn't

know a CEO had been fired until weeks after the fact. Better, they thought, to put their heads down, do their work, go home, collect a check. If the furnaces were blazing when workers showed up for their shift, they had a job.

"Stability has been replaced by chaos," Shannon Monnat, a sociologist and demographer at Penn State University who researches the interplay between economics and health, says of such situations. The longer the stress lasts, whether it involves family, community, or work, the more disheartened people become and the more faith they lose in the system, until, finally, they disconnect to survive.

Monnat has recently been studying "diseases of despair"—the plague of opioid addiction, alcoholism, and suicide afflicting places like Lancaster. She's found that instability at work is strongly correlated with the prevalence of these problems as well as with social and family breakdown. Drug abuse is not solely due to the cheap availability of heroin or meth, nor some imagined weakness of the working class. Monnat believes it's also caused by people's loss of faith that they each occupy an important place in the American system.

In Lancaster, the transition from stability to chaos seemed to happen fast, in about three decades, so many can still recall when the city was prosperous and predictable for people like the Plant 1 workers. In those days, the biggest criticism of the town was how boring it was. Lancaster was a cohesive community—a trait not lost entirely, thanks to the devotion many local people still feel—where social classes mixed and executives, from the founders to middle management, all lived in town. Their kids went to school with the factory workers' kids.

Workers didn't work only to earn a check. Anchor Hocking's

employees believed they were part of Lancaster's social web, and the nation's. But the respect workers once felt emanating from the world around them has largely disappeared. One day in the summer of 2015, I sat in on a meeting between labor and management where a woman spoke up to ask about the 401(k) plan. (Anchor Hocking's defined-benefit pension plan was switched to a 401(k) long ago.) The company had stopped making contributions to workers' 401(k) accounts in 2014 when the plant shut down during a fiscal crisis prompted in part by all the private-equity financial engineering.

The worker said she'd heard or read somewhere that, now that the Great Recession was over, employees at banks had once again begun receiving 401(k) matches from their employers. Referring to the lenders-turned-equity-holders, she asked, weren't she and her fellow workers now bank employees, too? Shouldn't they get their 401(k) matches back? She didn't know which employees of which banks were receiving matching contributions, but it didn't matter anyway, because EveryWare was not owned by banks, but other finance firms like Nationwide and Voya Financial. There was a giant, gray system hovering somewhere, out there, and she had no idea where, how, or even if, she fit into it.

"New hires can get a 401(k) at McDonald's," one man piped up. Was it any wonder Plant 1 couldn't attract skilled millwrights? (A new contract signed last fall re-instituted 401(k) contributions for some employees.)

As the publication date of my book about Lancaster and Anchor Hocking, *Glass House: The 1% Economy and the Shattering of the All-American Town*, approached, the company's employees had been warned via a company memo not to speak to me, or any journalists, so

their identities have been kept anonymous here. (Some of the workers' statements in this article also appeared in *Glass House*.) When asked about the company's current status and plans for the future, Erika Schoenberger, The Oneida Group's general counsel, declined to provide any details, "many of which," she said, "remain confidential." She only offered that Oneida is "proud of our heritage and our people" and "concentrated on strategic initiatives to build a successful future for our company and our communities."

Weighed down by the powerful feeling that they aren't valued, many workers are left to mark the passing of time. "These are the working-class people more likely than everybody else to have retirement countdown clocks on cell phones," Monnat says of laborers like those at Anchor Hocking. "There's no sense of meaning." The American Flint Glass Workers Union, which represents some of Anchor Hocking's factory workers, was forced to fold itself into the United Steelworkers in an attempt to maintain at least some bargaining power. But there's precious little of that left because the workers know that at any time the plant could shut down. Production could be moved, possibly to another country.

In late February, employees were informed that The Oneida Group was contracting with the India-based outsourcer Infosys to handle customer-service functions currently based in Lancaster. The word "layoffs" did not come up in the announcement, but the implication was clear enough: They were disposable workers. "It's tough for those people in customer service," one salaried employee told me. Speaking of the community spirit that extended from the company into the town itself, the employee said, "It's really heartbreaking. A lot of them have known each other for 30 years, grew up with each other."

I asked this employee what might have been if Anchor Hocking had not been subject to the whims of the financial engineers. "I can't help but think if things had been different, if some money had been put into machinery, product development, training, that we'd be in better shape." Counterfactuals are hard to prove, of course. But Anchor Hocking's longtime rival, Libbey, based in Toledo, Ohio, is still in business as a public company and still making money, despite having spent years under the ownership of the private-equity giant Kohlberg Kravis Roberts when KKR owned the container company Owens-Illinois; Libbey had been spun out from Owens-Illinois in 1993 and a former Anchor Hocking executive now runs it.

Lancaster's decline, then, wasn't the result of some sort of natural and inevitable evolution of technology, like the demise of the buggy-whip industry, nor of the pressures of free trade and offshoring, as intense as those have been. It is the culmination of a series of decisions over a period of roughly 35 years. As one former CEO of EveryWare Global told me, "It's not about making the product. It's about making money appear and the 99 percent doesn't understand that." The Plant 1 employees certainly don't. They only know that the old social contract has disintegrated and that nothing has come to take its place.

Back in 1984, A. Bartlett Giammatti, who was then the president of Yale University, and who would later become the commissioner of Major League Baseball, warned that the tide of deal-making and the financialization of the economy could lead to disillusionment and drift as "the impulse to private gain has nothing to connect itself to except itself." As Chris Nagle, a union leader in Plant 1, said to me in answer to my question about which presidential candidate his fellow union members seemed to prefer, "We don't like anybody."

Those who voted for Donald Trump, the salaried employee suggested, did so not out of enthusiasm, but out of this very disconnect. "People are grasping for anything," he said. What many didn't know, and may still not, was that two of the men who played such a large role in shaping Anchor Hocking's history—Carl Icahn and Stephen Feinberg, the founder of Cerberus—have been confidants of Trump and helped get him elected.

We want to hear what you think about this article. Submit a letter to the editor or write to letters@theatlantic.com.

ANCHOR HOCKING

TIMELINE

A COMPANY IS BORN

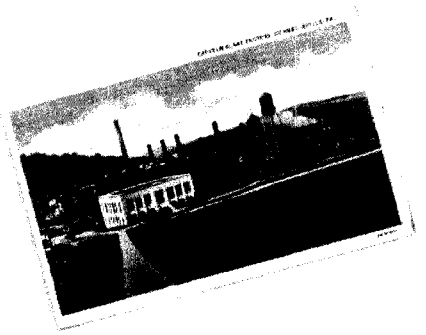
The Hocking Glass Company was incorporated under the laws of Ohion on November 2, 1905 for the purpose of manufacturing plain and decorated, pressed, blown, machine, hotel, bar and kitchen tableware, tumblers, stemware, illuminating glassware, packers ware, glass novelties and specialities. Its plant and headquarters were located in Lancaster, Ohio.

1905 | The Hocking Glass Company was founded by I.J. Collins and E.B. Good, in Lancaster, Ohio.

1923 | First I.S. machine installed in Salem Glass Works.

1924 | Plant No. 1 of The Hocking Glass Company destroyed by fire.

The history of Anchor Hocking is a story of a company that started small, but grew through initiative and desire on the part of its founders and employees. Isaac J. Collins founded the Hocking Glass Company in 1905 in Lancaster, Ohio. The company name comes from the Hocking River which flows nearby.



The Hocking Glass Company got its start with $25,000 that was raised by Mr. Collins. The company started small with just 50 employees housed in an old carbon plant, called the "Black Cat", so named because its walls were blackened with carbon dust.

The first year, $20,000 worth of glassware was sold.

Fire destroyed the "Black Cat" in March of 1924, throwing some 650 employees out of work. The employees, townspeople, fireman all worked together to battle the fire, but by morning all that remained were five acres of ashes and rumble.

The dusty old carbon plant was destroyed, but not the spirit of Hocking Glass, by the end of the following day, the Company had set up temporary offices in a vacant grocery store.

Hocking Glass purchased controlling interest in the Lancaster Glass Company in April 1924 and used its facilities to meet shipping requirements. At the time of its purchase by Hocking, Lancaster Glass had one continuous tank and one day-tank. While Plant 1 was being rebuilt over the ashes of the "Black Cat", Hocking was producing and shipping from Lancaster Glass. This purchase later became known as Plant 2.

Plant 1 was in production by October, 1924, just six months after the fire. This time the plant was more conducive to glass manufacturing. Today,

in the year, 2012 the Anchor Hocking Company stands in the original sight.

The company became the Anchor Hocking Corporation on December 21, 1937, with the merger of the Hocking Glass Company and subsidiaries and Anchor Cap Corporation and its subsidiaries. The "Anchor" came from the phrase that caps "were anchored for safety.

The depression Era saw another revolution in machine-made glassware. The Company knew that it had to produce tumblers as cheaply and quickly as possible if they wanted to sell in volume. Wilbur Secoy and William Fisher, both company employees designed and built a rotary 15-mold machine that could make 90 pieces of blown glassware a minute. With that machine (called the FS for Fisher and Secoy) the Company could sell tumblers "two-for-a –nickel," which was less than half of what it formerly cost.

During the next 50 years The Anchor Hocking Corporation grew through acquisitions and mergers to become a diversified manufacturer making consumer and industrial products sold around the world.

1905

The history of Anchor Hocking is a story of a company that started small, but grew through initiative and desire on the part of its founders and employees. Isaac J. Collins founded the Hocking

Glass Company in 1905 in Lancaster, Ohio. The company name comes from the Hocking River which flows nearby.

1924

Fire destroyed the manufacturing facility in March of 1924, throwing some 650 employees out of work. The employees, townspeople, fireman all worked together to battle the fire, but by morning all that remained were five acres of ashes and rumble.

Hocking Glass purchased controlling interest in the Lancaster Glass Company in April 1924 and used its facilities to meet shipping requirements. At the time of its purchase by Hocking, Lancaster Glass had one continuous tank and one day-tank.

1937

The company became the Anchor Hocking Corporation on December 21, 1937, with the merger of the Hocking Glass Company and subsidiaries and Anchor Cap Corporation and its subsidiaries. The "Anchor" came from the phrase that caps "we're anchored for safety".

1987

During the next 50 years The Anchor Hocking Corporation grew through acquisitions and mergers to become a diversified manufacturer making consumer and industrial products sold around the world.

On July 1, 1987, Anchor Hocking became a member of the Newell Group. Since then the manufacturing operations of the consumer glass division have been consolidated into this facility and a second manufacturing plant in Monaca, Pennsylvania. The primary focus tableware, ovenware and various other household glass products for the high volume retail, specialty and foodservice businesses.

2004

Newell Rubbermaid sold Anchor Hocking to Cerberus Investment Group; Global Home Products is formed comprising Anchor Hocking, WearEver Cookware and Burns of Boston Picture Frames.

2007

April, 2007 Monomoy Capital Partners, LLC purchases Anchor Hocking.

2008

November 19, 2008 Monomoy Capital Partners acquired Indiana Glass Company and E.O. Brody Company from Lancaster Colony Corporation. March 2008 E.O. Brody sold to Syndicate Sales. Sapulpa, OK plant closed. Processes moved to Lancaster, Ohio.

2011

November 1, 2011 Monomoy Capital Partners acquired Oneida ltd.

2012

April 2012 –EveryWare, Inc. becomes the corporate parent of the newly-merged Anchor Hocking and Oneida Companies.

2013

May 2013-EveryWare Global, Inc. goes public.

ECONOMY HOWL DECEMBER 29, 2008 ISSUE

How Hedge Funds and Private Equity Hurt Us

College endowments and workers bear the brunt of hedge fund managers' gambles and private equity takeovers.

By Nicholas von Hoffman

DECEMBER 11, 2008

Harvard University's endowment is down at least $8 billion. The slump, slowdown, recession or depression–or whatever you want to call it–is taking its toll on higher education's piggy banks.

The *Wall Street Journal* reports that, "The University of Virginia Investment Management Co. said it lost nearly $1 billion, or 18 percent, of its endowment over the four-month period, reducing it to $4.2 billion. In Vermont, Middlebury College says its endowment fell 14.4 percent, to $724 million. In Iowa, Grinnell College's endowment dropped 25 percent, to $1.2 billion. In Massachusetts, Amherst College says its endowment, $1.7 billion as of June 30, also fell by 25 percent."

Since cost containment is an idea foreign to American higher education, these losses are going to translate into many a bitter moment for countless thousands of college students. At

Harvard, which is an extreme case, more than one-third of operating funds come from the now-depleted endowment. In the good old days, higher education might have shrugged its shoulders and told its students to go take out larger loans, something which is hardly possible at this gloomy moment in American history.

Had colleges and universities now looking at large losses kept their money in safe, low-interest, government securities, they would be in much better shape–but they would also have been attacked by their alumni for such conservative, low-yield use of their endowments. The *Journal* reports that for many years places like Harvard and Yale "pioneered an investment approach that de-emphasized US stocks and bonds and placed large sums in more exotic and illiquid investments, including timberland, real estate and private-equity funds."

Illiquid is the word for it. Harvard has been trying to sell $1.5 billion in private equity funds and has been unable to get more than fifty cents on the dollar on its original investment. Private equity funds use their money to execute corporate takeovers, and to call them lucrative is something of an understatement; given the university's past profits, it would be hard to shed a tear for Harvard–except that it will be innocent students and faculty who will get it in the neck.

The rationale for private equity funds, known as buyout shops, is that they take over poorly run companies and spin them off into higher levels of productivity and profitability. Though sometimes that actually happens, we have also seen private equity funds put a little money down, borrow much more to pay for the company, strip it of its assets and leave it

dead or dying.

The ever-enterprising *Wall Street Journal* reports that "Of the 109 US companies that have filed for bankruptcy this year with assets of $1 million or more, 67 have been owned by buyout shops or been spun off by them, according to data provider Capital IQ. Among the more prominent casualties are retailers Linens 'n Things Inc. and Mervyn's LLC."

Mervyn's was seized and looted by Cerberus Capital Management, the same group of billionaires who now own Chrysler; having exhausted other avenues for unearned profit, they are begging the federal government for a handout. How Cerberus destroyed Mervyn's is instructive. According to the *Journal*, they and some others "bought Mervyn's from Target Corp. in 2004 for $1.25 billion. The investor group, which structured the buyout as two separate purchases–one for the retail operations, and one for the chain's valuable real-estate holdings–has earned Cerberus more than $250 million in profits, say people familiar with the deal."

The stores were stuck paying off the debt Cerberus contracted to buy Mervyn's. This debt was not money borrowed to make Mervyn's more competitive or productive. The stores got nothing from the debt but an added burden and, as is often the case with such private equity takeovers, the victim company collapsed under the weight of the obligations dumped on it and perished along with thousands of jobs.

Another example, this one involving a historic name, is that of Sears. It has fallen into the hands of a hedge fund operator who is milking the company by using its cash to buy back its

own stock.

One element in the disaster that has overtaken the American economy is the vast misallocation of capital by entities such as the private equity funds. They are not venture capital enterprises that made bad bets on what seemed like good ideas but free-market vampires. They have been able to take over healthy business organizations and ruin them for their own profit and the larger society's loss.

One of the not-yet-investigated stories is how so much capital fell into hands that wasted it on destructive games of profit, pointless mergers and acquisitions or insane derivative speculations. In the largest sense, capital is the fruit of the labor and the savings of the whole society. To see university endowments and to witness nothing less than productive companies destroyed by debt and bankruptcy is a crime.

Nicholas von Hoffman Nicholas von Hoffman, a veteran newspaper, radio and TV reporter and columnist, is the author, most recently, of *Radical: A Portrait of Saul Alinsky*, due out this month from Nation Books.

Bankruptcy No. 08-11586(KG)
United States Bankruptcy Court, D. Delaware

Mervyn's LLC v. Lubert-Adler Group IV, LLC (In re Mervyn's Holdings, LLC)

426 B.R. 488
Decided Mar 17, 2010

Bank of America Corporation, pro se

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491 *491 Ashley B. Stitzer, Daniel A. O'Brien, Justin R. Alberto, Neil B. Glassman, Bayard, P.A., Christopher M. Samis, Richards, Layton & Finger, P.A., Mary E. Augustine, Ciardi Ciardi & Astin, Wilmington, DE, Jennifer L. Stewart, Cooley Godward Kronish LLP, Boston, MA, Nicholas Smithberg, Ronald R. Sussman, Cooley Godward Kronish LLP, New York, NY, for Plaintiff.

492 *492 Adam G. Landis, Matthew B. McGuire, Landis Rath & Cobb LLP, Kimberly Ellen Connolly Lawson, Reed Smith LLP, Sharon M. Zieg, Young, Conaway, Stargatt & Taylor, Domenic E. Pacitti, Klehr Harrison Harvey Branzburg LLP, Gabriel R. MacConaill, Laurie Selber Silverstein, Potter Anderson & Corroon LLP, Francis A. Monaco Jr., Womble Carlyle Sandridge & Rice, John H. Strock, III, Fox Rothschild LLP, Natalie D. Ramsey, Montgomery, McCracken, Walker & Rhoads, Stuart M. Brown, Edwards Angell Palmer & Dodge LLP, Wilmington, DE, Aaron Rubinstein, Lee M. Cortes, Jr., Jr., Phillip A. Geraci, Kaye Scholer LLP, Richard G. Haddad, Otterbourg Steindler Houston Rosen, P.C., New York, NY, Dennis M. Ryan, Michael F. Doty, Wendy J. Wildung, Faegre & Benson LLP, Minneapolis, MN, Laurie A. Krepto, Montgomery, McCracken, Walker & Rhoads, Philadelphia, PA, for Defendants.

Bank of America Corporation, pro se.

MEMORANDUM OPINION

1 [1] This Opinion constitutes the findings of fact and conclusions of law pursuant to Federal Rule of Bankruptcy Procedure 7052. To the extent any of the following findings of fact are determined to be conclusions of law, they are adopted, and shall be construed and deemed, conclusions of law. To the extent any of the following conclusions of law are determined to be findings of fact, they are adopted, and shall be construed and deemed, as findings of fact.

KEVIN GROSS, Bankruptcy Judge.

INTRODUCTION

The matter before the Court is Defendant Target Corporation's Motion to Dismiss (the "Motion") the adversary proceeding brought against it by Mervyn's LLC ("Debtor") acting through the Official Committee of Unsecured Creditors (the "Committee").

2 [2] The Committee has brought this adversary proceeding on behalf of the Debtor pursuant to an Order which the Court entered on December 30, 2008 (D.I. 1330), granting it standing.

STATEMENT OF FACTS

3 [3] The operative complaint is the First Amended Complaint which the Committee filed on December 22, 2008 (Adv.Dkt.7). The Court denied leave to the Committee to file a Second Amended Complaint (Adv. Dkt. 178 and 179), which does not impact

the Motion. The well-pleaded facts are deemed true for purposes of the Motion. *See* Standard of Review, *infra*.

I. *Background*

Debtor, a California limited liability company, was a nationwide retailer of affordable fashion and home décor products which at one time operated 177 retail stores in the Midwest, South and Pacific Northwest. (Am.Compl.s 42). In 1978, the Dayton Hudson Corporation ("DHC") acquired Mervyn's which became a wholly-owned subsidiary of DHC. DHC also owned several "higher end" department stores, including Target Stores which became such a successful chain of discount retail stores that DHC changed its corporate name to "Target Corporation" ("Target"). By 2003, Target owned and operated three department store chains: Marshall Field's, Mervyn's and Target Stores. Target's board of directors had decided to focus solely upon the Target chain and therefore decided to sell both Marshall Field's and Mervyn's.

II. *Private Equity Sale*

After a competitive auction process, Target entered into an Equity Purchase Agreement (the "Agreement") on July 29, 2004 with a group of private equity firms that formed one of the Debtor entities *493 "Mervyn's Holdings LLC," ("Mervyn's Holdings"). Mervyn's Holdings is a Delaware limited liability company that was formed by three private equity groups (collectively, "PE Sponsors.") In order to spin-off Debtor's valuable real estate assets from Debtor, the PE Sponsors formed defendant "MDS Companies," bankruptcy remote entities. (Am.Compl.ss 62-63). The Agreement itself called for Target to convey 100% of its ownership interest in Debtor to Mervyn's Holdings for $1.175 billion. (Agreement, s 1). Mervyn's Holdings represented to Target that it had equity and debt commitment letters from external funding sources indicating that it had arranged loans and letters of credit from outside sources. *Id.*, s 6(d). The Agreement did not require the sale of Debtor's real estate either by Target or anyone else. *Id.*, s 5(b). Instead, the Agreement expressly prohibited Target from selling or transferring any of Debtor's real estate and also required Target to convert Debtor from a corporation to a limited liability company ("LLC"). *Id.*

III. *The Sale Transaction*

On September 2, 2004 the sale closed (the "2004 Sale"). Am Compl. ss 56-57. The parties satisfied or waived the Agreement's conditions. Mervyn's Holdings and PE Sponsors borrowed using Debtor's real estate as collateral and incurred substantial obligations in order to fund the 2004 Sale. (Am.Compl.s 46). Debtor received no residual interest in its own real estate and "all or substantially all of the loan proceeds were paid over to Target." (Am. Compl.ss 46, 59).[4] Mervyn's Holdings also leased the real estate back to Debtor at a "substantially increased rate to both service the acquisition debt and to continue to extract over time the significant excess value of the real estate assets over the debt piled onto those assets." (Am. Compl.s 49). Debtor claims that Mervyn's Holdings' actions destroyed the Debtor's value and led to filing of the Chapter 11 petition with the Court on July 29, 2008.

[4] According to Mervyn's Amended Complaint, the 2004 Sale was funded by three sources:

1. Pursuant to that certain Loan Agreement dated September 2, 2004, Greenwich and Archon, as lenders (the "Senior Real Estate Secured Lenders"), advanced $675,000,000 to Realty I, Realty II, Texas Realty I and Texas Realty II. Repayment of these loans was secured by the Unitary Leases held by the listed borrowers, mortgages, liens, assignments of rents and deeds of trust with respect to the real estate assets that had been transferred to the borrowers by Debtor. Mervyn's Holdings used all or substantially all of the loan proceeds to pay the purchase price of the 2004 Sale.

2. Pursuant to the Mezzazine Loan Agreement dated September 2, 2004, Greenwich and GS Mortgage (the "Mezzanine Real Estate Secured Lenders"), advanced $125,000,000 to

Holdings I, Holdings II, Texas Properties I and Texas Properties II. Repayment of these loans was secured by certain pledges and security interests provided by such borrowers. Mervyn's Holdings used all or substantially all of the loan proceeds to pay the purchase price.

3. Pursuant to the Securities Purchase Agreement, dated September 2, 2004, Mervyn's Holdings purchased 100% of the interests in Holdings I and Holdings II for $429,746,414,84. At the closing, Mervyn's Holdings used these funds to pay the purchase price.

(Am.Compl.s 58).

CAUSES OF ACTION

On September 2, 2008, Mervyn's brought this adversary proceeding against Target and 38 other defendants by filing a complaint alleging that Target and the other defendants engaged in a fraudulent transaction and that Target, among others, breached their fiduciary duty to Debtor and its creditors. Thereafter, Debtor filed its Amended Complaint on December 22, *494 2008, containing the following claims against Target:

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Count I: Mervyn's Holdings caused Debtor's real estate assets to be transferred with the actual intent to hinder, delay, or defraud creditors or without adequate consideration, in violation of the applicable provisions of the Uniform Fraudulent Transfer Act (UFTA) or Uniform Fraudulent Conveyance Act (UFCA), and Bankruptcy Code Sections 544(b) and 550. Target is liable as a transferee of the proceeds.

Count II: Mervyn's Holdings caused Debtor's to pledge its real estate assets with the actual intent to hinder, delay, or defraud creditors or without adequate consideration, in violation of the applicable provisions of the UFTA or the UFCA, and Sections 544(b) and 550. Target is liable as a transferee of the proceeds.

Count V: That the owners of Debtor (which changed over time), including Target, each breached the fiduciary duties that they owed to Debtor and its creditors at the respective times that they owned it.

Target responded to the Amended Complaint by filing the Motion on April 3, 2009. On May 20, 2009, the adversary proceeding was stayed pending the resolution of a motion to disqualify Kirkland & Ellis LLP, as counsel to Sun Capital Defendants, which the Court denied. (Adv.Dkt.125).

Target now seeks an order from this Court dismissing the claims against it in the Amended Complaint, with prejudice, pursuant to Rules 8, 9(b), and 12(b)(6) of the Federal Rules of Civil Procedure, made applicable by Rules 7008, 7009, and 7012 of the Federal Rules of Bankruptcy Procedure.

STANDARD OF REVIEW

Rule 12(b)(6) of the Federal Rules of Civil Procedure, made applicable here by Federal Rule of Bankruptcy Procedure 7012(b), governs a motion to dismiss for failure to state a claim upon which relief can be granted. "The purpose of a motion to dismiss is to test the sufficiency of a complaint, not to resolve disputed facts or decide the merits of the case." *Paul v. Intel Corp. (In re Intel Corp. Microprocessor Antitrust Litig.)*, 496 F.Supp.2d 404, 407 (D.Del.2007) (citing *Kost v. Kozakiewicz*, 1 F.3d 176, 183 (3d Cir.1993)). The complaint "must contain either direct or inferential allegations respecting all the material elements necessary to sustain recovery under *some* viable legal theory." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 127 S.Ct. 1955, 1969, 167 L.Ed.2d 929 (2007) (quoting *Car Carriers, Inc. v. Ford Motor Co.*, 745 F.2d 1101, 1106 (7th Cir. 1984)) (emphasis in original).

In considering a motion to dismiss under Fed.R.Civ.P. 12(b)(6), the court must accept as true all factual allegations in the complaint and draw all inferences from the facts alleged in the light most favorable to the plaintiff. *Worldcom,*

Inc. v. Graphnet, Inc., 343 F.3d 651, 653 (3d Cir.2003). The court may not consider matters outside of the pleadings unless the court is willing to treat the matter as a motion for summary judgment. Fed.R.Civ.P. Rule 12(d). A complaint need not contain detailed factual allegations, but "a plaintiff's obligation to provide the `grounds' of his `entitlement to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do . . . . Factual allegations must be enough to raise a right to relief above the speculative level." *Twombly*, 127 S.Ct. at 1964-65 (internal citations omitted).

The relevant record under consideration consists
495 of the complaint and any "document *495 integral or explicitly relied upon in the complaint." *U.S. Express Lines, Ltd. v. Higgins*, 281 F.3d 383, 388 (3d Cir.2002) (citing *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1426 (3d Cir.1997)). When considering a motion to dismiss, "it is axiomatic that the complaint may not be amended by the briefs in opposition to a motion to dismiss." *Pennsylvania ex rel. Zimmerman v. PepsiCo, Inc.*, 836 F.2d 173, 181 (3d Cir.1988) (citing *Car Carriers*, 745 F.2d at 1107). The movant carries the burden of demonstrating that dismissal is appropriate. *Intel Corp.*, 496 F.Supp.2d at 408.

However, Bankruptcy Rule 7009 further provides that Fed.R.Civ.P. 9 applies in adversary proceedings. While Fed.R.Civ.P. 9(b) provides that: "all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity," Rule 9(b) *only* applies to allegations of actual fraud. Furthermore, this Court takes the view that claims of constructive fraud, i.e. fraudulent transfers, are evaluated using Rule 8(a)(2).[5] A fraudulent transfer complaint "need only set forth the facts with sufficient particularity to apprise the defendant fairly of the charges made against him." *In re AstroPower Liquidating Trust*, 335 B.R. 309, 333 (Bankr.D.Del.2005) (holding that a constructive fraud count need not comply with Rule 9's heightened pleading standard). Fed.R.Civ.P. 8(a), made applicable to this proceeding by Fed. R. Bankr.P. 7008, requires only "a short and plain statement of the claim showing that the pleader is entitled to relief." A plaintiff need not set out in detail the facts upon which he bases his claim, so long as he gives the defendant(s) fair notice of what the claim is and the grounds upon which it rests. *Leatherman v. Tarrant County Narcotics Intelligence & Coordination Unit*, 507 U.S. 163, 167, 113 S.Ct. 1160, 122 L.Ed.2d 517 (1993) (quoting *Conley*, 355 U.S. at 47, 78 S.Ct. 99, 2 L.Ed.2d 80). In reference to a constructive fraud claim, the Court has stated: "all that is needed at this stage is an allegation that there was a transfer for less than reasonably equivalent value at a time when the Debtors were insolvent." *In re DVI*, 2008 WL 4239120, at *9 (Bankr.D.Del. Sept.16, 2008) (finding complaint sufficient because "the Trustee has identified the transfer by date and face amount and has alleged that it was for no consideration").

[5] *Brandt v. Trivest II, Inc. (In re Plassein Int'l Corp.)*, 352 B.R. 36, (Bankr.D.Del.2006) ("Accordingly, the Court joins with those decisions that have (either implicitly or explicitly) evaluated fraudulent transfer complaints using Rule 8(a)(2)'s notice pleading standard") *Id.* at 40-41. *See. e.g., Giuliano v. U.S. Nursing Corp. (In re Lexington Healthcare Group, Inc.)*, 339 B.R. 570, 574-75 (Bankr.D.Del.2006) (applying "liberal notice pleading standard"); *AstroPower*, 335 B.R. at 333 (holding that a fraudulent transfer complaint "need only set forth the facts with sufficient particularity to apprise the defendant fairly of the charges made against him"); *Official Comm. of Unsecured Creditors v. DVI Bus. Credit, Inc. (In re DVI, Inc.)*, 326 B.R. 301, 305-306 (Bankr. D.Del.2005) (applying Rule 8(a)(2)); *Tese-Milner v. TPAC, LLC (In re Ticketplanet.com)*, 313 B.R. 46, 68 (Bankr.S.D.N.Y.2004) ("While there is authority to the contrary, the better and majority rule is that a claim for constructive fraud. . need not be pleaded with particularity. . . ."); *Nisselson v. Drew*

Indus. (In re White Metal Rolling & Stamping Corp.), 222 B.R. 417, 429 (Bankr.S.D.N.Y.1998) ("The sole consideration should be whether, consistent with the requirements of Rule 8(a), the complaint gives the defendant sufficient notice to prepare an answer, frame discovery and defend against the charges.").

DISCUSSION

The claims against Target in Counts I and II of the Amended Complaint are for fraudulent transfer, and Count V of the Amended Complaint alleges a breach of *496 fiduciary duty. In reference to the fraudulent transfer issue, Debtor alleges actual fraud and constructive fraud through a series of transactions that occurred in September 2004.

The Court Will Not Consider Some Documents in Target's Appendix

As a preliminary matter, Target attached an Appendix with exhibits in support of the Motion, including press releases, affidavits, wire transfer documents, Debtor's operating agreement and a cash flow statement. Target claims that these exhibits fall under the Third Circuit's "integral exception" doctrine because they are all a part of the Agreement. In *In re Burlington Coat Factory Securities Litigation,* 114 F.3d 1410 (3d. Cir.1997), the Third Circuit formulated a narrow exception to Fed.R.Civ.P. 12(d). The court held that "a document integral to or explicitly relied upon in the complaint may be considered without converting the motion into one for summary judgment." *Id.* at 1426. Additionally, another exception to Rule 12(b) exists and that is the public record exception. In the Third Circuit, courts may take judicial notice of public records to acknowledge that the facts contained in the records existed in the public realm at that time. *Benak v. Alliance Capital Mgmt. L.P.,* 435 F.3d 396, 401 (3d Cir. 2006). The court may not, however, consider the truth of the information in the records. *Id.*

The Court will take judicial notice of the press releases and will further consider the commitment letters and the Agreement; however, the affidavit, operating agreement, cash flow statement and wire transfer documents will be excluded in considering the Motion. The Court is taking judicial notice of the press releases because they are public documents. However, the documents will not be considered for truth or veracity. *Benak,* 435 F.3d at 401; *see also In re Nuvelo, Inc., Sec. Litig.,* 2008 WL 5114325, at *2 (N.D.Cal. Dec.4, 2008)(the court took judicial notice of SEC filings and press releases but not for the purposes of truth or veracity.).

The Court will also consider the Agreement and commitment letters because these documents fall within the "integral" exception. As the Third Circuit stated in *Burlington Coat,* "the rationale underlying this exception is that the primary problem raised by looking to documents outside the complaint-lack of notice to the plaintiff-is dissipated." *Burlington Coat,* 114 F.3d at 1426. Here, both parties are on notice as to the Agreement and commitment letters. Not only has Target relied upon them in the Motion, but Debtor heavily relies on these documents in its Amended Complaint. If these documents did not give Debtor notice or were in any way inaccurate, Debtor would not have relied on them in the Amended Complaint. Debtor did not rely upon the affidavit, wire transfers, operating agreement and cash flow statements in the Amended Complaint.

Counts I & II

The Amended Complaint Alleges Sufficient Facts to Find the 2004 Sale was a Fraudulent Transfer

In the Motion, Target argues that the 2004 Sale is not governed by either the Uniform Fraudulent Transfer Act ("UFTA") or Delaware's codified statute, 6 *Del. C.* § 1304, based on five assertions.

6 [6] Since the Delaware bankruptcy court has jurisdiction over this matter, the Court should apply the "most significant relationship" choice of law standard to

determine which state law applies to the fraudulent transfer claim. *Travelers Indemn. Co. v. Lake*, 594 A.2d 38, 47 (Del. 1991). There are three possible state's laws that can apply: 1) Delaware, the state of reorganization and incorporation for Mervyn's Holdings; or 2) California, where the Agreement was executed and is Debtor's state of incorporation and headquarters; or 3) Minnesota, the state of incorporation and headquarters for Target. All three states have similarly adopted the UFTA, and therefore the result is the same regardless of the choice of law issue.

Target contends that the 2004 Sale fails to fall within the confines of the UFTA and state law because: 1) Target sold its membership interest in Debtor, not Debtor's property; 2) Target was not a transferee or subsequent transferee of Debtor's property; and 3) was not a guarantor or an initial transferee for whose benefit the transfers were made. According to Section 17300 of the California Corporations Code, "a membership interest and an economic interest in a limited liability company constitute personal property of the member or assignee." Because Debtor was a California limited liability company, Target claims it only possessed a membership interest and not a direct stake. Furthermore, Target claims that Mervyn's Holdings (instead of Debtor) paid the purchase price to Target through various loan obligations (Am.Compl.s 58, 59) and therefore Target was neither a guarantor nor an obligee of any initial transferee when the Agreement was executed.

Target's fourth argument for why Debtor's claims do not come within the purview of the UFTA is that the transaction did not render Debtor insolvent. In the Motion, Target asserts that the 2004 Sale was merely a change in ownership and that Mervyn's Holdings represented to Target that it had adequate capital for the purchase price.

Lastly, Target asserts that the 2004 Sale was not made to "hinder, delay, or defraud" creditors. Instead, Target's aim was to promote the "Target" brand.

The Court is satisfied that in deciding the Motion, it must collapse the events integral to the 2004 Sale, including the execution of the Agreement, the stripping of the real estate assets, and the leases, into a single conveyance. The Court will take the totality of the circumstances approach by looking at the overall economic consequences of the 2004 Sale.

In the Third Circuit, the leading authority on the propriety of collapsing multiple individual transactions when determining whether a transaction constitutes a fraudulent transfer is *United States v. Tabor Court Realty Corp.*, 803 F.2d 1288, 1302 (3d Cir.1986). The court in *Tabor Court Realty* held that when a series of transactions were "part of one integrated transaction," courts may look "beyond the exchange of funds" and "collapse" the individual transactions of a leveraged buyout. *Id.* Instead of focusing on one of several transactions, a court should consider the overall financial consequences these transactions have on the creditors. *In re Hechinger Inv. Co.*, 327 B.R. 537, 546-47 (D.Del. July 19, 2005). To make this determination, courts consider three factors in their analysis. First, whether all of the parties involved had knowledge of the multiple transactions. *Id.* Second, whether each transaction would have occurred on its own. *Id.* And third, whether each transaction was dependent or conditioned on other transactions. *Id.*

While the Court will not rule on the merits as to whether the 2004 Sale was a fraudulent transaction, the Court does find after considering the factors listed in *Tabor* and *Hechinger*, that the Amended Complaint states facts to support a finding that Target is liable as a transferee in the
498 *498 alleged fraudulent conveyance. As to the first requirement, knowledge of the multiple transactions, Debtor's facts establish the ability to show that Target had constructive knowledge of the transactions that were going to take place subsequent to the conveyance of their membership interest in Debtor. Target was aware of the identity of Mervyn's Holdings and acknowledged in the Motion that it was comprised of a group of private investment firms. The Agreement refers to the

commitment letters. In fact, in the Motion, Target admits to receiving the actual commitment letters from Mervyn's Holdings addressed from the various banks. The clauses requiring Debtor's conversion to a limited liability company and prohibiting the sale of real estate assets also evidence Target's knowledge. Certainly, all of the transactions comprising the 2004 Sale required the execution of the Agreement. Of particular concern is the clause requiring Target to convert Debtor into an LLC. Without this conversion, Target would not have been able to transfer its membership interest, a major factor in the fraudulent transfer claim. The actions of the parties (including converting Debtor into an LLC, the clause prohibiting the sale of Mervyn's real estate assets, the letters of credit from the banks, the execution of the sale and the substantial increase in the rents) were each dependent on the others.

Pursuant to *Tabor Court Realty* the Court must also examine the overall financial consequences the transactions have had on creditors. Here, they were devastating, including the stripping of Debtor's real estate assets, the increasing of rent from the leases to enable Mervyn's Holdings to meet its acquisition debt, and the creation of a conflict of economic interest for Mervyn's Holdings as the owner and managing member of Debtor because the ultimate owners of Mervyn's Holdings and the owners of MDS Companies were one and the sameâ the PE owners acting through the PE Sponsors. Debtor was subsequently left with working capital as little as $22 million and acquired additional debt totaling over $800 million. (Am. Compl., *passim*).

For the above-mentioned reasons, Debtor has successfully established a valid claim under *Tabor Realty* and *Hechinger* for collapsing the transactions surrounding the 2004 Sale such that the Court can find a fraudulent transfer upon proof.

The Amended Complaint Satisfies Rules 8(a) and 9(b)

In the Amended Complaint, Debtor asserts fraudulent transfer claims based on both actual and constructive fraud that are respectively subject to Fed.R.Civ.P. 8(a) and 9(b). The basic notice pleading standard applies to the constructive fraudulent transfer claim because "all that is needed at this stage is an allegation that there was a transfer for less than reasonably equivalent value at a time when the Debtors were insolvent." *In re DVI,* 2008 WL 4239120, at *9 (Bankr.D.Del., Sept.16, 2008).

Debtor specified facts to describe the 2004 Sale, the property and dates involved in the transaction, the value of the transfers made, the amount of money transferred to Target, the source of the funds and the negative implications of the 2004 Sale. (Am.Compl.ss 17, 62-71, 76, 100-102, 129-137, 139-147).

Similar to the constructive fraud argument, the Amended Complaint also satisfies the heightened Rule 9(a) requirement for the actual fraud claim. Rule 9(a) is satisfied on the basis that there is an opinion letter quoted in the Amended Complaint describing in definitive terms the Debtor's allegations that the leases demonstrate Target's knowledge and fraudulent intentions of separating Debtor *499 from its real estate assets. (Am. Compl. s 92). The Court therefore finds that both Rules 8(a) and 9(b) are satisfied.

The "Settlement Payment" Exception of Section 546(e) is not Applicable

Target asserts that even if the 2004 Sale was considered a fraudulent transfer, the Debtor is barred from avoiding the transaction because the transaction falls within the safe harbor of section 546(e). Target contends it satisfied all of the requirements of 546(e): 1) properly received a settlement payment from a financial institution via wire transfer; and 2) the "settlement payment" fits the definition of section 741(8). Target further argues that the fact that the transaction did not involve a publicly traded entity is irrelevant because the Court in *In re Plassein Int'l Corp.,* 366 B.R. 318 (Bankr.D.Del. 2007) found that the

"broad application of what constitutes a settlement payment mandated in *Resorts* covers . . . purchases of non-public securities." *Id.* at 325.

Section 544(b) of the Bankruptcy Code authorizes the Trustee to "avoid any transfer of interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law." 11 U.S.C. § 544(b). Section 546(e), however, provides that, notwithstanding section 544, "the Trustee may not avoid a transfer that is a . . . settlement payment, as defined by section 101 or 741 of the Bankruptcy Code, made by or to a . . . financial institution." 11 U.S.C. § 546(e). . . . "settlement payment" is defined under section 741(8) to include "a preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment, or any other similar payment commonly used in the securities trade." 11 U.S.C. § 741(8). Put simply, "a settlement payment is generally the transfer of cash or securities made to complete a securities transaction." *Lowenschuss v. Resorts International, Inc. (In re Resorts International, Inc.),* 181 F.3d 505, 515 (3d Cir.1999). The Court of Appeals for the Third Circuit has repeatedly held that this definition is "extremely broad" and encompasses almost all securities transactions. *In re Resorts International,* 181 F.3d at 515 (quoting *Bevill, Bresler & Schulman Asset Management Corporation v. Spencer Savings & Loan Association,* 878 F.2d 742, 751 (3d Cir.1989)). In *Resorts,* the Third Circuit held that a payment to a shareholder for his shares as part of a leveraged buyout was "obviously a common securities transaction" and, therefore, a settlement payment under section 546(e). *In re Resorts International,* 181 F.3d at 516; *see also Hechinger,* 274 B.R. at 87 (applying *Resorts* and holding that payment for shares of stock was an unavoidable settlement payment).

The second prong of section 546(e) requires that payment for the securities must be made by or to a financial institution. "So long as a financial institution is involved, the payment is an unavoidable `settlement payment.'" *Hechinger,* 274 B.R. at 87. The term "financial institution" is defined under the Bankruptcy Code as "a Federal Reserve bank or an entity that is a commercial or savings bank. . . when any such Federal Reserve bank. . . or entity is acting as agent or custodian for a customer . . . in connection with a securities contract." 11 U.S.C. § 101(22)(A). This requirement is satisfied when a leveraged buyout payment is made by wire transfer. *In re Resorts International,* 181 F.3d. at 515. Indeed, federal regulations require that a wire transfer *must* be performed by a bank; thus, a wire transfer must be
500 made through a financial institution. *See In re* *500 *Loranger Mfg. Corp.,* 324 B.R. 575 (Bankr. W.D.Pa.2005) (taking judicial notice of federal regulation requiring that a wire transfer must be accomplished by a bank, rejecting plaintiff's arguments that bank's involvement was "mere facilitation" and holding that debtor's leveraged buyout of defendant's shares was a "settlement payment" under § 546(e) because payment was made by wire transfer).

The Court previously held that a "settlement payment" includes privately held securities in *In re Plassein Int'l Corp.,* 366 B.R. 318, 326 (Bankr.D.Del.2007), *aff'd,* 590 F.3d 252 (3d Cir.2009). Therefore, the only issue within Target's 546(e) claim that the Court must address is whether section 546(e) even applies to the 2004 Sale. The Court believes that section 546(e) does not apply.

First, as a general rule, section 546(e) does not apply to "collapsed" transactions. The conveyance in *In re Plassein Int'l Corp.,* was not collapsed because "the complaint did not allege fraud or bad faith . . . and the Trustee conceded he was not claiming actual fraud. The complaint also did not allege any relationship whatsoever among the transactions or the shareholders. Moreover, there were no allegations calling into question the good faith of the shareholders." 366 B.R. at 326. Debtor's case could not be more different. The Amended Complaint contains pointed allegations of actual fraud and how the events surrounding the 2004 Sale were interdependent.

Second, although "settlement payments" include non-publicly traded securities, section 546(e) does not apply to the other transactions surrounding the sale because they do not fall within the section 741 definition of "settlement payment." The Court firmly believes that because of the multiple conveyances made surrounding the 2004 Sale, section 546(e) does not apply. Target's attempt to have this Court apply section 546(e) to a single conveyance within the entire transaction is not persuasive. In the Motion, Target represents to the Court that the 2004 Sale involved only transferring the loan proceeds from MDS to Target. Target fails to recognize that this was only one part of the 2004 Sale. The other transactions to this sale do not fall within the parameters of section 546(e). For instance, when Debtor transferred its real estate assets to MDS for virtually no consideration, this was not a conveyance of a "preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment or any other similar payment commonly used in the securities trade." The conveyance was conditioned on the subsequent transaction of MDS securitizing the real estate assets to obtain financing.

Count Vâ Breach of Fiduciary Duty Claim

a. *California law imposes a fiduciary duty upon a member of a Limited Liability Company*

Target contends that because there is "zero" case law addressing whether a sole member of a California LLC owes fiduciary duties to the LLC or to its creditors, that no such duties exist. In a majority shareholder context, Target also argues, in relying on *Trenwick America Litigation Trust v. Ernst & Young, LLP,* 906 A.2d 168, 173 (Del.Ch.2006), *aff'd,* 931 A.2d 438 (Del.2007), that wholly owned subsidiaries (such as Debtor in this case) are expected to act for the benefit of the parent corporation and for this reason parent corporations do not owe fiduciary duties to subsidiaries. *See also, Official Committee of Unsecured Creditors v. Nat'l Amusements, Inc.,* 2010 WL 399295 (Bankr. D.Del. Jan.29, 2010).

501 *501 At the outset, the Court recognizes that California, not Delaware, corporation law applies to this matter. The internal affairs doctrine directs federal courts sitting in Delaware to apply the law of the state of organization to claims that implicate an organization's internal affairs. *In re PHP Healthcare Corp.,* 128 Fed. Appx. 839, 843 (3d Cir.2005). In this case, because a breach of fiduciary duty is alleged, this matter directly relates to Debtor's internal affairs. Therefore, the Court will apply California law.

While no California court has directly and explicitly stated that a sole member of an LLC owes the company fiduciary duties, the Court believes that were the California Supreme Court to decide that issue, that court is more likely to find that such duties are owed to the LLC. According to *First American Real Estate Information Services, Incorporated, v. Consumer Benefit Services, Incorporated,* 2004 WL 5203206, at *6 (S.D.Cal. Apr.23, 2004), although the California Code is silent, a court is likely to find that a member of a California LLC does owe the LLC fiduciary duties:

> While California law does permit the members of the LLC to specifically vest managers with the duties of managing the LLC, *see* Cal. Corp.Code § 17151(b), that act does not extinguish the members' fiduciary duties to each other and to the LLC. *See* Cal. Corp.Code § 17150 (stating that where members manage a LLC, the members shall have the same rights and be subject to all duties and obligations of managers as set forth in this title; but silent on whether members otherwise have fiduciary duties).

Id. at *6.

Although no case directly addresses this issue, the *First American Real Estate* decision sufficiently indicates that a member of a California LLC owes fiduciary duties to the entity and its other members. Secondly, the Court rejects Target's reliance upon *Trenwick* because *Trenwick* is a Delaware Court of Chancery opinion interpreting

Delaware corporation law and is thus inapplicable. Target also argues that fiduciary duties are not owed to creditors when the company is insolvent. However, California law takes the opposite view. There are two cases, *In re Jacks*, 243 B.R. 385, 390 (Bankr.C.D.Cal.1999) and *CarrAmerica Realty Corp.*, 2006 WL 2868979, at *5 (Bankr.N.D.Cal., Sept. 29, 2006) that definitively recognize a member's duty to a company's creditors when the company is insolvent. According to *In re Jacks:*

> A corporation's directors and officers owe no fiduciary duty to creditors under California law until the corporation becomes insolvent. *In re Jacks*, 243 B.R. 385, 390 (Bankr.C.D.Cal.1999), *aff'd in part, rev'd in part*, 266 B.R. 728 (9th Cir. BAP 2001). "Because a director's fiduciary duties to creditors do not arise until the corporation is insolvent, the timing of the insolvency is critical." *In re Jacks*, 266 B.R. at 738. The time of insolvency as determined under California law is the point at which the corporation is unlikely to be able "to meet its liabilities . . . as they mature." *Id.* (quoting Cal. Corp.Code § 501).

California law appears to be clear that Target, as a member of Debtor, owed a fiduciary duty to Debtor's creditors. The Amended Complaint sufficiently pleads that at the time the Agreement was executed, Debtor was or became insolvent due to the stripping of the real estate assets. Consequently, Target, which was in control of Debtor at the time of the closing, owed fiduciary duties to Debtor's creditors. (Am.Compl. s 43).

b. *The exculpatory clause is not a proper defense*

Target argues in the Motion that even if it owed a fiduciary duty, an exculpation *502 clause in Debtor's operating agreement provides that Target cannot be held liable to Debtor for conduct that is "at worst, negligent, or grossly negligent."

The Third Circuit has been clear that "protection of an exculpatory charter provision appears to be in the nature of an affirmative defense. As we have said, affirmative defenses generally will not form the basis for dismissal under Rule 12(b)(6)." *In re Tower Air, Inc.*, 416 F.3d 229, 242 (3d Cir.2005). The Delaware District Court has taken an even more rigid approach by refusing to even consider the defense on a motion to dismiss. *Ad Hoc. Comm. of Equity Holders of Tectonic Network, Inc. v. Wolford*, 554 F.Supp.2d 538, 561 (D.Del.2008). This Court arrived at the same conclusion: "The court agrees. . . the exculpation clause is an affirmative defense and the determination of the viability of that defense is not proper at this stage." *In re The Brown Schools*, 368 B.R. 394 (Bankr.D.Del.2007).

> 7 [7] In *In re Fedders North America, Inc.*, 405 B.R. 527, 543 (Bankr.D.Del.2009), Judge Shannon dismissed a duty of care claim and applied the exculpation clause. However, unlike *Fedders*, the breach of fiduciary claims here are "inextricably intertwined" with other claims. The Amended Complaint pleads with particularity that the 2004 Sale resulted in a fraudulent transfer which triggered a breach of the fiduciary duties of care, loyalty, and good faith. All of these alleged breaches, as cited in the Amended Complaint, arise from the same transaction and therefore are "inextricably intertwined" which each other. (Am. Compl.ss 172, 175, 176, 178-180). Moreover, the Court is not considering the operating agreement per its earlier ruling. --------

c. *Debtor timely filed the breach of fiduciary claim*

Target contends that Delaware's statute of limitations applies and that the that Mervyn's breach of fiduciary duty claim is barred. In the alternative, Target argues that Delaware's "borrowing" statute impedes the breach of fiduciary duty claim pursuant to 10 Del. C. § 8121. In Delaware, the limitation period for breach of fiduciary duty claims is three years. 10

Del. C. § 8106. In California, there is a four year period for such claims. Cal. Code Civ. Proc. § 343. Debtor commenced this adversary proceeding more than three years but less than four years after the 2004 Sale.

The Court must apply Delaware's choice of law rules to determine which statute of limitations applies. *See, e.g., In re PHP Healthcare Corp.*, 128 Fed.Appx. 839, 843 (3d Cir.2005) (applying the choice of law rules of the state in which the bankruptcy court sits); *In re Garden Ridge Corp.*, 338 B.R. 627, 632 (Bankr.D.Del.2006) ("To determine which state's law to apply, the Court turns to Delaware choice of law rules."). Delaware's choice of law rules require application of "the law of the state of incorporation to issues involving corporate internal affairs." *VantagePoint Venture Partners 1996 v. Examen, Inc.*, 871 A.2d 1108, 1115 (Del.2005). A breach of fiduciary duty involves the internal affairs of the corporation. *Coleman v. Taub*, 638 F.2d 628, 629 n. 1 (3d Cir.1981). Delaware has a borrowing statute that in pertinent part states:

> where a cause of action arises outside of this State, an action cannot be brought in a court of this State to enforce such cause of action after the expiration of whichever is shorter, the time limited by the law of this State, or the time limited by the law of the state or country where the cause of action arose, for bringing an action upon such cause of action.
>
> 10 Del. C. § 8121.

However, the Delaware Supreme Court in *Saudi Basic Industries Corp. v. Mobil Yanbu Petrochemical Company, Incorporated*, 866 A.2d 1, 16 (Del.2005), *cert. denied*, 546 U.S. 936, 126 S.Ct. 422, 163 L.Ed.2d 322 (2005) (emphasis added), explained that the rationale of the Delaware borrowing statute is to help prevent forum shopping: *503 *503

> Borrowing statutes are typically designed to address a specific kind of forum shopping scenario-cases where a plaintiff brings a claim in a Delaware court that (i) arises under the law of a jurisdiction other than Delaware and (ii) is barred by that jurisdiction's statute of limitations but would not be time-barred in Delaware, which has a longer statute of limitations.
>
> *Id.*

In another Delaware Bankruptcy Court case where this issue arose, Judge Walrath reasoned that because the internal affairs doctrine applied, the statute of limitations of the state law in the state of incorporation applied to the breach of fiduciary claims. *In re Circle Y of Yoakum, Texas*, 354 B.R. 349, 359 (Bankr.D.Del.2006) The Debtor was a Texas corporation, with a mailing address in Yoakum, Texas. Therefore, despite the trustee's contention that Delaware law applied, the court ruled that Texas law governed the applicable limitations period. *Id.*

The breach of fiduciary duty claim is not barred by the Delaware statute of limitations because California law applies. As in *In re Circle Y of Yoakum, Texas*, the Court will apply the internal affairs doctrine and concludes that the Delaware statute does not apply. This is not a case where forum shopping might even remotely be an issue. Debtor, the plaintiff in this adversary proceeding, came to Delaware with a shorter (instead of longer) statute of limitations period and chose Delaware for the Chapter 11 case and not for the adversary proceeding which the Committee brought. There is absolutely no threat of forum shopping and the Delaware "borrowing" statute is inapplicable.

CONCLUSION

The Amended Complaint contains detailed facts which, if proven true, make a troubling case of wrongdoing. Although Target points at others to blame, it is at the center of the 2004 Sale. The Motion is denied in all respects.

ORDER DENYING MOTION TO DISMISS

The Court has carefully considered Defendant Target Corporation's Motion to Dismiss (the "Motion"), and the briefs and respective arguments of the parties in support of and against the Motion. For the reasons stated in the Memorandum Opinion of even date,

IT IS ORDERED.

https://www.greensboro.com/news/general_assignment/guilford-mills-to-close-plant/article_240b56fa-1724-5e15-8960-1493cdcdd508.html

Guilford Mills to close plant

By Stan Swofford Staff Writer Apr 19, 2005

GREENSBORO — And then there was one.

Just one. With the announcement Tuesday that Guilford Mills is closing its manufacturing plant on Hornaday Road, one plant is all that remains in the city of a once-proud Fortune 500 textile empire whose center was Greensboro.

In a cursory four-paragraph letter to Mayor Keith Holliday — a public notice required by law — the company's management said the plant at 5644 Hornaday Road will close June 18. The last work days for the facility's 101 employees could occur sooner, "based on business needs," the notice said.

Hornaday plant employees were also told Tuesday, said David Taylor, the company's chief financial officer.

The closing announcement came on the heels of the sudden resignation of the Guilford Mills president and CEO, John Emrich, whose departure was announced Friday in a statement released by Guilford Mills' new owners, Cerberus Capital Management. The New York-based private equity company bought Guilford Mills 14 months ago.

Taylor said there was no link between Emrich's departure and the decision to close the Hornaday plant, although "it's understandable how one might jump to that conclusion."

Taylor said Hornaday is being closed because it and another Guilford Mills

plant in Fuquay-Varina do essentially the same type of work and that "both are underutilized." The plants manufacture fibers for material used in the manufacture of automobiles and for other uses.

Emrich, a highly respected figure within the textile industry who guided Guilford Mills through bankruptcy, could not be reached for comment Tuesday. He said last week that he was not being forced out, but that he was leaving Guilford Mills "by mutual agreement."

But Sam McNeil, a consultant who works with financially troubled companies, said it is likely that Emrich's departure and the Hornaday closing are, indeed, linked.

McNeil noted that Emrich had shifted the company away from apparel manufacturing to focus primarily on automotive textiles. Rising oil prices make that a risky proposition, he said.

"Guilford Mills placed a big bet on the auto industry, and, clearly, that industry is just not doing well," McNeil said.

If there was a disagreement between Emrich and Cerberus on closing Hornaday, Cerberus was going to win, McNeil said. "They're interested in what the bottom line is going to look like next quarter," he said.

Hornaday employees, meanwhile, wonder whether they will have another job next quarter. Taylor said Guilford Mills will do all it can to help its former workers find new jobs. He said they will be the first to be hired at "other Guilford-Greensboro operations."

Taylor acknowledged, however, that, except for the plant's administrative office on West Market Street, there is only one other Guilford Mills operation in Guilford County, and that's the Friendship plant off West Market Street near the airport.

Less than 10 years ago Guilford Mills was a Fortune 500 company boasting record textile sales and profits that employed more than 1,600 people in

Greensboro alone.

Those figures plummeted. In less than five years, the company's Greenberg plant on West Wendover Avenue, where 550 employees worked, had been sold and was being torn down to make room for a shopping center. The Cushman plant, with more than 400 workers, had closed in 2000.

The company, which was begun by James Hornaday in a garage on Sycamore Street in 1946 and came to prominence under Chuck Hayes in the 1960s and 1970s, was a shell of its former self by 2002, the year it filed for bankruptcy protection.

Emrich guided it through bankruptcy reorganization and its sale to Cerberus in February 2004. Today, the company has 2,600 employees worldwide, with 1,700 in North Carolina — 480 in Greensboro.

When the Hornaday employees work their last day, there will be 379.

Contact Stan Swofford

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https://www.greensboro.com/guilford-mills-ceo-resigns-john-emrich-s-departure-from-the/article_37b8154b-92ce-5fba-975f-d8afe3f16083.html

GUILFORD MILLS' CEO RESIGNS JOHN EMRICH'S DEPARTURE FROM THE TEXTILE FIRM SURPRISES THOSE INSIDE AND OUTSIDE THE COMPANY.

BY DONALD W. PATTERSON Staff Writer Apr 16, 2005

John Emrich, one of the most vocal supporters of the troubled textile industry, has left his position as president and CEO of Guilford Mills.

Guilford Mills' new owners, Cerberus Capital Management, announced Emrich's departure in a statement released within the company Friday.The move was effective immediately.

Emrich, 60, had led Guilford Mills through bankruptcy in 2002 and positioned it for its sale to Cerberus, a New York-based private equity firm, 14 months ago.

He also had shifted the company away from the apparel business to one that deals primarily with automotive textiles.

"I have had five years of tough stuff," Emrich said Saturday. "It wasn't easy, one, to save Guilford and, two, get it sold."

Cerberus announced in February 2004 that it would buy the company for $107 million. Before that, Guilford Mills' major lenders had owned 90 percent of the company.

In an internal statement released Friday, the chairman of the company's board of directors, David Thursfield, praised Emrich.

"We wish to place in record our appreciation for John's tenure and stewardship at Guilford through very difficult times," the statement said. "His successful transition ... from an apparel-dominated business into a premier automotive-textile business is one of his clear accomplishments."

Thursfield also praised Emrich for protecting employee benefits during the bankruptcy.

Thursfield's statement did not mention a successor, but Richard E. Novak, Guilford Mills' vice president for human resources, said Cerberus hopes to have a replacement within 30 to 60 days.

In the interim, Novak said, Bob Nolan, executive vice president of operations, will run the company.

Efforts to reach Nolan, 67, were unsuccessful Saturday. He has worked for the company for more than 30 years.

Emrich's sudden departure caught employees off guard.

"People were surprised and very concerned that John was leaving," Novak said. " ... When a leader has brought the stability he has after we emerged from bankruptcy, it is only natural for people to have anxiety as to what will happen in the future."

Observers of the textile industry also were surprised by Emrich's departure, especially given the fact that Cerberus did not identify his permanent replacement.

"This would indicate that something happened that was unexpected," said Sam McNeil, managing director of River Capital Advisers, a Charlotte firm that works with financially troubled companies. "Clearly, when the head of the company leaves without a successor being ready to go that suggests that this was a sudden type of thing and not a planned exit."

Emrich says he wasn't forced out.

"I wasn't asked to leave," he said. "This was by mutual agreement. ... I feel like a new kid. It is always hard when you are working for somebody else, and now I am working for myself."

He would not discuss his plans.

Emrich, who joined the company in 1985, became Guilford Mills' president and chief operating officer when the legendary Chuck Hayes stepped down as president in 1995. He took on the title of CEO after Hayes left that position in 2000.

Most recently, Emrich has pushed for the Bush administration to provide protections for the textile industry.

\ Contact Donald W. Patterson at 373-7027 or donpatterson@news-record.com

BONDS NEWS AUGUST 13, 2007 / 2:37 PM / 12 YEARS AGO

UPDATE 2-Aegis Mortgage files for Chapter 11 bankruptcy

3 MIN READ

(New throughout, adds byline)

By Jonathan Stempel

NEW YORK, Aug 13 (Reuters) - Aegis Mortgage Corp., a mortgage lender controlled by private equity firm Cerberus Capital Management, on Monday filed for Chapter 11 bankruptcy protection, a week after it stopped making home loans and fired 60 percent of its employees.

The Houston-based lender and several affiliates filed for protection from creditors with the U.S. Bankruptcy Court in Wilmington, Delaware. In a statement, Chief Executive Dan Gilbert said Aegis plans to "wind down" its operations as expeditiously as possible.

Aegis joined Melville, New York's American Home Mortgage Investment Corp. AHMIQ.PK and Atlanta-based HomeBanc Corp. HMBN.PK among mortgage lenders to seek protection from creditors this month. Several others have filed for Chapter 11 this year, while dozens more have quit the industry.

Aegis has described itself as one of the 30 largest U.S. mortgage lenders. It made "prime" and "Alt-A" wholesale loans, and "subprime" retail and wholesale loans to residential borrowers who couldn't qualify for the best rates.

In court papers, Aegis listed more than $100 million of assets, and estimated it owes more than $600 million to creditors. The latter included $178 million of unsecured debt owed to Madeleine LLC, a Cerberus affiliate that has an 80.9 percent equity stake, the papers show.

Aegis said it fired 782 of its 1,305 employees on Aug. 7, a day before Connecticut's banking regulator ordered it to stop lending. The company said it is continuing to service loans.

"Extreme changes in market conditions, coupled with the rapid decline in the secondary mortgage market severely impacted (Aegis') operations," Chief Financial Officer Edward Robertson said in a court filing.

He said Aegis suffered "extraordinary increases" in defaults among borrowers who had just obtained loans, "substantial" margin calls from its own lenders, and growing demands that it buy back soured loans it had sold.

Home loan providers have been struggling with rising defaults, the refusal of investors to buy loans they make, and the unwillingness of many banks to extend credit.

New York-based Cerberus did not immediately return calls seeking comment.

According to the bankruptcy filing, Aegis' largest unsecured creditors included affiliates of Morgan Stanley (MS.N) and Countrywide Financial Corp CFC.N, among others. Both claims are disputed, it said. (Additional reporting by Michael Flaherty)

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The darker side of buyout firms

The case of Aegis Mortgage shows that when private equity loses a high-risk bet, ordinary employees are the ones who suffer, reports Fortune's Katie Benner.

By Katie Benner, Fortune reporter
August 20 2007: 1:24 PM EDT

NEW YORK (Fortune) -- Buyout firms like to present themselves as a can't-fail combination of operational genius and financial support that can heal sick businesses and create thriving companies. But sometimes, as in the case of Aegis Mortgage, genius fails and bankruptcy is declared. The private investment firm Cerberus bought a controlling stake in the Houston-based mortgage lender in 1998, but despite an infusion of cash and talent, Aegis ceased operations on Monday, August 6. Now hundreds of employees have been laid off - all without health insurance. It's a reminder that risky turnarounds can mean real pain for more than just investors raising questions about how Cerberus will treat other ailing companies it has purchased, notably Chrysler.

Aegis, which was founded in 1993, closed its mortgage production operations on August 6. Two days later, employees were warned that there would be layoffs within 60 days and that benefits would be terminated effective midnight August 10, according to Aegis employees. They were also told that earned paid-time off would not be paid out and that there would be no severance. When the layoffs came on Monday, August 13, 782 people out of 1,302 employees were fired. Those let go were shocked to find that they were not eligible for COBRA. While Federal law requires businesses with more than 20 employees to offer departing workers the chance to buy an extra 18 months of health insurance, it is only required for companies with an active benefit plan, and Aegis had terminated its plan days before. Moreover, Aegis admitted in its bankruptcy filing that it didn't have the money to pay employee benefits anyway.

What do you think of this?

Those actions have some up in arms. Richard Thompson, who co-founded Aegis in 1993, is asking Cerberus and Aegis to take care of its employees. "As a founder of Aegis, one of our stated corporate values was to always do the right thing," says Thompson, who was CEO until October 2006, when Cerberus ousted him. "The right thing is to reinstate the company's health insurance policy for the thousands of families affected by their actions last week."

Thompson, of course, has reason to dislike Cerberus. Not only was he fired, he is suing Cerberus for mismanaging the company and destroying its chance to go public. Other observers note that many companies that go bankrupt leave their employees stranded. John Challenger, head of executive outplacement firm Challenger Gray Christmas, says: "Creditors will line up, so the company is taking these harsh actions to save what they can. You're going to see lots of fighting over the company assets." In its bankruptcy filing, Aegis said it had $625 million in debt and owed banks including Goldman Sachs, Deutsche Bank, Merrill Lynch and Morgan Stanley. Madeleine LLP, a subsidiary of Cerberus, is also in line for money.

Cerberus declined to comment; an Aegis spokesman said that the company is doing what it can to help its remaining 500 or so employees, including providing health care and job training.

Trust Cerberus

What happened to Aegis? The company managed to survive the mortgage meltdown and S&L problems of the '90s, but it had been wounded. Plans in 1997 to hold an IPO for its REIT business were scrapped when the REIT sector began to exhibit problems. The conditions were perfect for a company like Cerberus, which regularly scoops up distressed businesses it believes will be winners in the future. The mortgage business was suffering in the late 1990s, but the industry is cyclical and Cerberus was betting on returns during the upswing. (Indeed, even as the subprime business began to melt down this spring, Cerberus agreed to buy sub-prime lender Option One Mortgage from H&R Block this April.)

So in 1998, Cerberus agreed to buy a controlling stake in Aegis, which had $2.5 million in equity. Following a familiar pattern, Cerberus immediately injected a huge amount of money into the company ($47 million), placed its own people on the board and kept the management team, including Thompson, in place. It rolled pieces of other dying lenders into Aegis and built a thriving mortgage lending operation.

Cerberus: Inside the Wall Street power-house

In late 2006, the company had grown its capital in reserves to $361 million, and like all other lenders it couldn't issue mortgages fast enough for the Wall Street machine that used them to create high-risk, very profitable bonds. At the height of the mortgage origination boom, Aegis employed about 3,500 people, mostly in the Houston area. But Aegis lost it all in just nine months when the market for mortgage loans tanked.

The failure calls into question the management and health of Cerberus's other loan plays. Cerberus owns a majority stake in GMAC and its mortgage subsidiary ResCap. Thanks to the credit crunch, the ratings agencies have downgraded ResCap, thus making it more expensive for the company to operate. The rising cost of capital may hurt Chrysler Financial, too, the healthy operation within Chrysler that should have been able to help fund the ailing automaker's turnaround. At a minimum, Cerberus will take a financial hit because of Aegis and the bankruptcy is an embarrassment amid the firm's recent spate of high-profile acquisitions.

"Cerberus has become a major player in the global economy. Its many constituents rightly will expect a higher standard of behavior than was exhibited last week with Aegis," says Thompson. It's a sober reminder that even the vaunted geniuses of private equity can't save every company, and that employees - more than investors - are the real victims when they go under.

Do you think this is a sign of what would happen if more private equity deals go bust? Tell us what you think. ■

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Total high-interest loans 2005-2007:

At least $11.5 billion

Federal bailout money received:

None

Company overview

- **Status:** CLOSED. Filed for bankruptcy, August 2007.
- **History:** Aegis Mortgage Corp. was founded in 1993 in Houston. Private equity firm Cerberus Capital Management bought the firm in 1998. Cerberus, which along with other investors owns 51 percent of General Motors Acceptance Corp., was unable to keep Aegis in business through the subprime crisis. Aegis filed for Chapter 11 bankruptcy protection in August 2007, one week after ceasing all new home loans.
- **Parent/subsidiary companies:** Cerberus Capital Management (parent)
- **CEO:** Founder: Rick Thompson founded the company in 1993 and led it through 2006. Dan Gilbert was appointed CEO in 2007 and held the job only a few months before the company filed for Chapter 11 protection in August 2007.
    - **Most recent salary:** Not available
- **Location:** Houston
- **Year founded:** 1993
- **Backers:** In its bankruptcy filing, the company listed unsecured claims owed to Morgan Stanley, Countrywide, and Goldman Sachs. The company also sold hundreds of millions of dollars in loans to investment banks such as Morgan Stanley and Merrill Lynch.

Lobbying overview

- **Lobbying:** Cerberus reported $5,360,000 in lobbying expenditures since 2005.
- **Total Contributions:** At least $926,375 *
- **Top Recipients:**
  1. Democratic National Committee $101,000 (tie)
  1. National Republican Congressional Committee $101,000 (tie)
  3. Democratic Senatorial Campaign Committee $83,000
  4. Defend American PAC $69,500
  5. Majority Leader's Fund (former Representative Dick Armey, R-Texas) $50,000

Investigations

- **Settlements:**
  • In 2007, Aegis agreed to pay $475,000 to settle charges filed with the Department of Housing and Urban Development that it denied loans on American Indian reservations, row homes, or group homes for the disabled located throughout the United States.

https://publicintegrity.org/business/no-25-of-the-subprime-25-aegis-mortgage-corp-cerberus-capital-management/

Cerberus: Inside the Wall Street power-house

With the closing of the Chrysler deal, the (very) private equity shop is poised to succeed or fail very publicly, say Fortune's Katie Benner and Geoff Colvin.

By Katie Benner and Geoff Colvin
August 5 2007: 11:40 PM EDT

(Fortune Magazine) -- They're already taking the "Daimler" off the DaimlerChrysler signs at headquarters in Auburn Hills, Mich. It's happening at the big Fenton, Mo., plants where the company makes pickup trucks and minivans, and at other plants across North America. The new corporate stationery is ready. Chrysler dealers nationwide are sending out invitations, filling balloons with helium, and ordering chicken wings for the parties they're going to throw. The occasion: Chrysler is becoming American again, being bought from its German parent by Cerberus Capital Management, a buyout firm that it's safe to say most of Chrysler's employees, dealers, and customers had never heard of until the agreement was announced a few months ago.

The historic deal (which closed Friday) vaults Cerberus to a new level of fame and prominence in the U.S. economy. It also ties the fortunes of Chrysler and its ecosystem of suppliers and dealers to the increasingly troubled world of private equity, which is being dented by rising interest rates and a nasty credit crunch. Cerberus differs markedly from its competitors in many ways, especially in its willingness to take on companies in peril. "They consistently go where angels fear to tread, and they're doing it at scale and profitably," says Glenn Hutchins, co-founder of competitor Silver Lake. With Chrysler, Cerberus will succeed or fail more visibly than ever.

All that attention is actually a downside as far as Cerberus is concerned. Founder and chief Stephen Feinberg has shielded his firm, which is named after the mythical three-headed hound of Hades, from the press for 15 years. (True to form, he refused to be interviewed or photographed for this article.) But the spotlight is unavoidable: Cerberus's portfolio companies now generate revenues of more than $60 billion a year and employ about a quarter-million people, including 80,000 at Chrysler, a company that's in the news every day and that does business with consumers across America.

To understand the firm, one must understand Feinberg. "Everything runs through him, full stop," says a lawyer who has worked with Cerberus on several deals. "Cerberus is Steve Feinberg." No one interviewed for this story could imagine a successor.

Unlike such private equity czars as KKR's Henry Kravis or Blackstone's Steve Schwarzman, Feinberg is an anti-celebrity, man-of-the-people guy who just happens to be a centimillionaire. The 47-year-old son of a steel salesman from Spring Valley, N.Y., he lives in a Manhattan apartment that is modest by Master-of-the-Universe standards and an even more modest house in Stamford, Conn. He drives a Dodge pickup, loves guns and motorcycles, and wears off-the-rack suits.

The firm's Park Avenue offices may be the tattiest in the private equity business. Walk down the narrow corridors on threadbare, coffee-stained carpets and you'll see a warren of bare cubicles and rows of gray-steel filing cabinets. The walls are institutional beige or gray, adorned with cheap framed prints that would suit an inner-city nursing home. The overall effect is that of a ministry of finance in a former Soviet satellite state. And that seems to suit Feinberg just fine.

If you're doing business with him, expect to be neither wined nor dined, ever. "Invariably Feinberg and I would eat sandwiches out of boxes while we worked," says Robert Milton, CEO of Cerberus-controlled ACE Aviation Holdings, parent of Air Canada. A veteran dealmaker says, "His philosophy is having a relationship as opposed to rubbing your back. He won't do lunch or play golf, but he'll help you out. It's very different from what you find everywhere else."

Feinberg went to Princeton (class of '82) and there revealed the intensity and drive that characterize him still. A tennis teammate recalls, "If he'd had any natural ability at all, he would have been national champion," so ferociously did he practice and compete. Colleagues today say he breaks from work only for hunger, and if he leaves the office at 9 p.m. he'll continue working from home. He expects everyone on his staff to be available 24/7, as he is.

To see what Feinberg does care about, observe him in his weekly deal meeting, which all 280 employees are expected to attend in person or by phone. Many staffers are former executives from a range of companies, such as former MCI president and COO Tim Price, former Johnson & Johnson COO Jim Lenehan, and a number of executives from General Electric, including Michael Williams, Jeffrey Fenton, and Paul Bossidy. Other buyout firms arrange for such managers to be on call; Feinberg pays them to staff his so-called operations team and works them full-time. High up in the org chart - if not at the actual day-to-day control levers - are Dan Quayle and John Snow, the ex-Vice President and Treasury Secretary, respectively.

As talk progresses through possible target companies and the state of the portfolio, Feinberg asks his team of corporate veterans to contribute ideas, experiences, connections, and on-the-spot analyses. Through it all, he seems to release an overflow of nervous energy with a peculiar tic: He flicks his wrist back and forth, "playing tennis with his pen," says a former member of his operations team.

The questioning is nonstop, and participants are amazed by Feinberg's memory for numbers. "He fires off granular questions about cash flow from specific divisions over the trailing 12 months, and you'd better have that answer or get it quickly," says one witness to a Feinberg grilling. "The questions are insightful. There's no bullshit, no wasting time. His capacity to recall financial details on all the companies they have an interest in, and at the same time have a big picture in mind, is just astonishing. The people at Cerberus say this guy can see through walls."

If a potential target looks hot, Cerberus throws massive resources at it. An executive at the firm recalls a fast-moving situation involving a troubled company outside the U.S. In 72 hours he had war rooms in New York and overseas occupied by a 35-person SWAT team of Cerberus operations pros, investment analysts, and industry experts from the outside. Thus began a five-week, no-days-off, forced-march due diligence process that yielded thousands of pages of Excel spreadsheets. "The average day went to midnight," this executive recalls. "And many people never went home."

The obsession of that team and all Cerberus teams - other than making lots and lots of money, of course - is risk. All downside risk is modeled, just as every move is thought out in a game of chess (another Feinberg enthusiasm). Cerberus buys companies that look extremely risky, assumes the worst will happen, and plans accordingly.

The risk-centric approach is pure Feinberg. His first finance job out of college was with 1980s junk-bond house Drexel Burnham Lambert, where he learned how high-risk businesses borrow money and, more important, what happens when

cerberus_illus.03.jpg

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they can't repay their loans. He later worked for the small Gruntal brokerage. (Those two firms are now defunct; Drexel, you'll recall, went bust amid the Mike Milken scandal. Feinberg emerged from both stints unscathed.) He then started Cerberus in 1992 at age 32. Its specialty was distressed debt, a Wall Street term for loans that the borrowers can't repay. It's a nasty business. The distressed bonds Cerberus bought produced a decent return if the borrower recovered. If it died, Cerberus used sharp elbows and teams of lawyers to fight over the remains; hence the usual term for this species: vulture investors.

"Cerberus had a lending arm called Madeleine LLC that gave money to companies that were filing for bankruptcy or ready to throw the Hail Mary pass," says a lawyer who has worked in M&A for 20 years. "Sure, they'd lend you the $10 million, but it would cost millions in fees, and they'd also get 10% of the company."

Cerberus became a part owner of many troubled firms, and Feinberg realized there was money to be made by rehabilitating them, says Tim Price. So Feinberg switched gears and began to focus on undervalued companies and distressed businesses that could be turned around.

With all that debt expertise, it's no surprise that finance and consumer-lending companies form the bulk of Cerberus's portfolio. Those businesses could come in handy. As bond markets roil, it's getting tougher to secure financing the way most private equity players do - through investment banks. An ability to fund one's own deals could be valuable; KKR has said publicly that it would like nothing more. But so far it's Cerberus that's building the banking empire.

Calling Cerberus a private equity firm, as most on Wall Street do, isn't quite right. As with most PE firms, investors must commit money for a long lockup period (in this case seven years) and accept that portfolio companies will be held for as long as it takes to create value. But unlike most PE firms, which only take public companies private in the hope of reselling later at a profit, Cerberus uses its enormous war chest - it raised $8 billion for its newest fund - for pretty much any asset it believes is undervalued. That includes equity stakes, debt, real estate, whatever. Cerberus also runs funds with the fee structure and much shorter lockup period (2 1/2 years) of a traditional hedge fund. These funds don't generally trade public equities or use leverage as most hedge funds do, however, and the holdings are largely similar to those of the longer lockup funds. Cerberus doesn't call itself a PE firm or a hedge fund, instead saying it's a private investment firm.

Limited partners (as such a firm's investors are called) report that returns are remarkably consistent, probably because of this unique structure. One longtime investor says his firm invests in both the long-term commitment and the more liquid funds, and that Cerberus is consistently returning more than 20% a year after fees. All four of its buyout-type funds are in the top quartile of distressed funds, according to research firm Private Equity Intelligence. "That is a pretty amazing track record," says Mark O'Hare, PEI's managing director. "Very few if any other firms could claim this."

The deals that Cerberus really likes are the ones most other PE firms really don't: complicated deals that involve lots of hard-to-assess risk, some kind of finance business, and labor unions. Not all Cerberus deals possess those attributes, but a surprising number do - Chrysler being the most famous.

An earlier example, critically important to the firm's decision to go after the automaker, was its purchase last year of a controlling interest in GMAC, the finance arm of General Motors (Charts, Fortune 500). Whether the deal will pay remains to be seen, but the company has dramatically slashed losses in the most recent quarter. It was also the crucial foundation for the Chrysler deal. Cerberus probably wouldn't have looked at a money-losing auto business with $19 billion in pension and retiree health-care liabilities if a healthy auto-finance business weren't part of the package. "I think that Cerberus is probably uniquely positioned as the logical owner because of the fact that it's involved with GMAC," says Wilbur Ross, the distressed-industries investor who has made fortunes in steel and coal.

Much could go wrong at Chrysler. If Congress enacts stringent new fuel-economy rules this fall, as it might, then some analysts believe Chrysler's car business could simply die. Even in the best case (solvency, upbeat sales), the future of the business will depend heavily on the behavior of the unions - and here we see another way in which Cerberus is different.

In general, labor unions hate private equity firms because they see them as asset strippers that close plants and fire workers. Cerberus certainly isn't shy about doing that - it laid off about 10% of the employees within a year of taking control of Guilford Mills in 2004, and moved the headquarters of Vanguard Car Rental (parent of Alamo and National) from Florida to Oklahoma for the cheaper labor pool. Nevertheless, Cerberus has managed to keep the unions mostly happy, as it did with some San Francisco hotels it bought.

Canadian Auto Workers president Buzz Hargrove was a bitter opponent when the Chrysler deal was announced but became a Feinberg fan after they met in Auburn Hills. "We were impressed with his knowledge of Chrysler and its key problems," says Hargrove. "He didn't just give us rhetoric about labor costs. He gave me his cellphone number." And what makes Hargrove think it isn't just talk? Mainly a recent decision to keep jobs at an Ontario plant where the company had good reason to cut them. Hargrove's conclusion: "It shows that under Cerberus, Chrysler is making an extra effort to live up to its commitments to keep jobs."

As Cerberus takes its place in the top rank of buyout firms and as a force in U.S. business, it may yet emerge from the shadows. But that will be a struggle. Teach for America recently honored Feinberg for his fundraising efforts, naming him guest of honor at its latest gala. But even in the Waldorf-Astoria ballroom, he was a ghost. Goldman Sachs president Jon Winkelried praised him in a long speech, but when it came time to invite Feinberg to the mike to say a few words, Winkelried instead said thank you and good night. Feinberg didn't budge from his table. Attendees were stunned. It's hard to think of anyone else too diffident even to stand up at a dinner being given for him.

Other challenges will include those facing the whole PE industry. This sector's supergrowth has been fueled by cheap debt and easy credit that suddenly aren't so cheap or easy. Cerberus was extraordinarily lucky to get the Chrysler deal closed just as the door was slamming, but future prospects will be pricier, requiring even more creativity. Even if Cerberus does keep coming up with deals, there's no guarantee they'll succeed. The firm has had some big flops - Mervyn's, the downmarket retailer, has floundered since Cerberus bought it; bottlemaker Anchor Glass filed for bankruptcy in 2005; GDX Automotive, the car-parts manufacturer, may soon do the same.

Maybe Cerberus's run will end. Or maybe its habit of shaping its business model to follow opportunities will come to its rescue. Like how? Well, in this environment, interest rates on risky loans are rising sharply, and shaky companies will have a hard time making payments. That means lots of turmoil - and opportunity - in the market for distressed debt. And at least one "private investment" firm knows that business quite well.

REPORTER ASSOCIATE Doris Burke contributed to this article. ■

Chrysler is American again
Wilbur Ross: Watch the Chrysler deal

The Money Issue

How America's Oldest Gun Maker Went Bankrupt: A Financial Engineering Mystery

When a secretive private equity firm bought Remington, sales were strong and the future bright. A decade later, the company couldn't escape its debts.

By JESSE BARRON MAY 1, 2019

The news spread around Huntsville, Ala., in the winter of 2014. Remington, the country's oldest gun maker, had decided to expand from its historic home in upstate New York to a gigantic former Chrysler factory near the airport. Workers at the new plant, the company said, would earn a minimum average of $19.50 an hour assembling shotguns, pistols, hunting rifles and AR-15-style semiautomatics. The city's mayor wrote in a newspaper column that he was thrilled that Remington's quest for a new factory space had ended in Huntsville. He calculated the typical annual salary as $42,500.

Huntsville is a boomtown in the Southern mold. The unemployment rate is lower than the country's, and educated workers are in high demand. Southwest of downtown, in a facility that synthesized chemical weapons during World War II, the Army maintains a major research center and garrison. Orbiting the Army base are military and aerospace contractors: Raytheon, Lockheed Martin and Northrop Grumman. Car companies from Japan, an electronics manufacturer from Korea and many other concerns churn out goods for the domestic market. "Cutting taxes and simplifying regulations makes America the place to invest!" President Trump tweeted

courting automakers and then becoming an all-purpose workshop and technology hub. Airbus produces A320 jetliners; Toyota makes engines for Rav4s and Tundras; Blue Origin, Jeff Bezos's "spacefaring" company, recently broke ground on a rocket-engine plant. These companies are drawn here partly by the benefits that Trump cited, but most forcefully by the generous tax-incentive packages doled out by officials in Montgomery, the state capital, in concert with pro-business mayors.

Huntsvillians take pride in their economy, and when a new company comes to town, good will cascades toward it. In early 2015, wearing a shirt and hat from Remington could even score you the best table at a restaurant. In the display cases at Larry's Pistol and Pawn, Huntsville's most respected gun shop, managers made room for Remington pistols stamped with "Huntsville, AL": It was a point of pride to carry a weapon made in-state. "Locked and Loaded," ran the headline in The Huntsville Times, for an article describing how the factory would ultimately create more than 1,800 jobs.

Doors opened in spring 2015. News from the inside was scarce, but this was more or less to be expected. Workers in the gun industry endure a special kind of scrutiny, like metal detectors at the exits and visits to their homes from A.T.F. agents looking for weapons that have gone missing. When Remington forbade employees to speak to outsiders about their jobs or fired a person who removed a smartphone from his pocket in the vicinity of the line, the explanation was assumed to be that the company was protecting its secrets, including the pace of its production. "Those assault rifles," one employee told me, "they couldn't make them fast enough." That year, Remington earned $191 million in gross profit on $809 million of revenue.

At the top of the employees' checks, the name "Remington Arms" was printed, along with the address of the company's new facility at 1816 Remington Circle SW in Huntsville. But this was somewhat misleading. While the guns were still stamped with the thick-footed Remington R, the company no longer existed as a fully independent entity. Seven years before

The firm, Cerberus Capital Management, takes its name from the three-headed, dragon-tailed dog who, in Greek mythology, stands guard at the gates of Hades.

Stephen Feinberg, co-founder and chief executive of Cerberus, came of age alongside his field. He was born in the Bronx, N.Y., in 1960, went to Princeton, where he studied politics, then after graduation, took a job at the brokerage house Drexel Burnham Lambert. As the journalist Connie Bruck recounted in her 1988 best seller, "The Predators' Ball," Drexel was a feral place in the early '80s. Under the direction of its star financier, Michael Milken, the firm developed a way to help clients purchase whole companies using high-interest loans — a practice mainstream investment banks found far too risky to imitate. Milken could whip together nine figures for a client just by picking up the phone. The client took the borrowed cash, bought an obscure or struggling company, and tried either to renovate it or to stamp out costs — often through layoffs — and make it profitable. When these so-called "leveraged buyouts" worked, investors made a hundred or a thousand times their money. When they failed, the bought-out businesses crumbled.

Milken made hundreds of millions of dollars from the fees he earned on leveraged buyouts. At Drexel's parties at the Beverly Hills Hotel, Milken would unleash his male clients on a bungalow filled with what Bruck referred to as "extremely attractive young women" the firm had paid to be there. His career came to an abrupt halt in 1990, when he was convicted of securities fraud and was permanently banned from the stock market. (Steven Mnuchin, the secretary of the Treasury, has reportedly lobbied Trump to pardon Milken.)

Milken's conviction coincided with the declining popularity of the term "leveraged buyout." In the winter of 1988, the acquisition of R.J.R. Nabisco by a firm called KKR — one of the most televised news stories of the year — had taken the opaque practice directly into people's kitchens and cigarette packs, where it turned out to be threatening and unwelcome. In 1990, Susan Faludi at The Wall Street Journal wrote a Pulitzer Prize-winning

the early 1990s talked about leveraged buyouts. Faced with all this bad publicity, Wall Street decided it had only one option. It would have to change the name. Stephen Feinberg founded Cerberus in 1992 as the euphemism "private equity" was coming into currency.

If Feinberg resembles Milken, it's in superficial ways. Milken cultivated a "blue-collar billionaire" persona, speaking brashly and wearing jeans and loafers; Feinberg wore off-the-rack suits to his gray, dingy offices in New York. The young Milken would take a predawn bus from New Jersey to the Drexel offices in New York City while reading regulatory filings with a flashlight; when researching a deal, Feinberg is said to establish "war rooms" at his office and keep his staff until midnight or later. According to Bruck's book, Milken seldom granted interviews, because "you can't make a dime off publicity"; Feinberg is reported to have joked to a private meeting of his investors in 2007 that "if anyone at Cerberus has his picture in the paper, and a picture of his apartment, we will do more than fire that person. We will kill him. The jail sentence will be worth it." (Feinberg declined to comment for this article.)

Milken financed leveraged buyouts, but Feinberg made his name by investing directly in distressed assets, businesses that were in bad shape financially. His deal to acquire the parent company of National Car Rental is emblematic of his shrewdness. In 2003, the company was bankrupt, and Feinberg bought it for just $230 million. In four years, he realigned it toward the airport market, then sold it to Enterprise Rent-A-Car for $3 billion. During the rest of the '00s, the firm expanded to mortgage lenders, real estate, department stores, automakers: anywhere it saw an inefficiency it could exploit. The industry had matured, too. No longer executing leveraged buyouts exclusively, private-equity firms had a host of investment strategies at their disposal. Twenty-seven years after Feinberg founded it, Cerberus was managing $39 billion.

Because private-equity firms appear frequently as villains in the press, many people assume that they cater mostly to the superrich, earning high returns on investments for billionaire clients. They do. But by far the most

the funds were obligated to pay out and the money they had — the so-called pension gap. An investment strategy that could return 15 to 20 percent a year and close that gap was an irresistible solution. The pension fund for the Boston-area public water utility invests in Cerberus. The California State Teachers' Retirement System, CalSTRS, is a Cerberus client, as is a pension fund for the Presbyterian Church as well as many university endowments, sovereign wealth funds and philanthropic foundations.

Private-equity buyouts are associated in the public imagination with layoffs, but the research on that topic isn't conclusive. Private-equity-owned firms don't necessarily occasion more layoffs than publicly traded ones, but some studies suggest that private-equity firms may be responsible for increased polarization in the job market, that is, for eliminating midlevel roles and thereby contributing to the shrinking of the middle class. A company purchased by private equity can expect to be realigned aggressively, in a five- or 10-year window, to become more "efficient," which often entails firing, automation and offshoring. For a pension fund, then, and especially the pension fund of a union, investing in private equity can be a devil's bargain: helping retiring workers by using tools that may harm younger ones.

When Cerberus bought Remington in 2007, the world was hurtling through the greatest rush of private-equity acquisitions in history. From 2002 to the crash in 2008, hundreds of billions of dollars a year were deployed in private-equity deals by firms like Cerberus, KKR and Blackstone. There were never fewer than 1,700 private-equity transactions annually; in 2007 the figure peaked at 7,400. After the crash briefly interrupted its momentum, the industry came back in force. The United States government was responding to the crisis by lowering borrowing costs to kick-start the economy. For private-equity firms, the access to cheap debt was a gift: It allowed them to purchase a long list of targets, then borrow more money using those targets as collateral. During the recovery, private-equity firms made an average of one trillion dollars' worth of acquisitions every year. In 2017 there were a record 9,500 deals. By 2019, according to

In 2017 there were a record 9,500 deals. By 2019, according to the consulting firm McKinsey, the industry controlled $3.4 trillion in assets globally. If private equity were a country, it would be the fifth-largest economy on earth, beating India, Britain and France.

the eighth floor of Huntsville's City Hall, he has a plaque from Mazda and Toyota that looks like a pro-wrestling belt, a blue-tipped shovel with Facebook printed on the head and a long-barreled Remington rifle mounted on a wooden board. Each commemorates the opening of a factory or an office that Battle helped entice to move to Huntsville, mostly using tax incentives.

Battle was re-elected in 2016 with 80 percent of the vote. His popularity springs from his ability to generate jobs — and to generate headlines about generating jobs. Though his endorsement of Roy Moore, who lost his bid for a seat in the United States Senate amid sexual-assault accusations, alienated some Huntsvillians — northern Alabamians consider themselves more socially liberal than their southern neighbors — Battle is mostly beloved by his constituents. When I met him in his office, his business-relations officer leaned over my recorder on the table and said, "If Amazon Web Services is reading right now, tell them we'd love to have a data center."

In 2013, Battle learned that a site-selection consultant, someone who helps businesses looking to expand or relocate, was sniffing around the South on behalf of an unnamed manufacturer. The consultant, Michael Press, was an old hand in the tax-incentive game. In the 1980s, advising the New York City mayor Ed Koch, he wrote many of the incentives that Amazon recently claimed in its ill-fated bid to build a headquarters in Long Island City. When Press was hired to find a Remington factory, he did what he always did, sending letters to multiple states soliciting bids, inciting competition without disclosing his client. Press had learned that if workers at a company's existing plants heard a new one was being sought, they would panic about the impending layoffs.

By choosing to place Remington in a Southern state, Press was acknowledging how much the gun business had transformed. Historically, gun makers operated in the North, in New England's "Gun Valley" or, like Remington, in upstate New York. Smith & Wesson and Colt were established in the 1850s by businessmen in Massachusetts and

Battle summarized to me the message the law sent to gunmakers: "If you like guns," he said, "then you need to go somewhere else."

There was a secondary benefit. Composed entirely of "right to work" states, the South allowed employees in unionized shops to opt out of paying dues, effectively guaranteeing that any union encountered by Remington would be worse-funded, and therefore less powerful, than a counterpart in the North. At Remington's factory in Ilion, N.Y., employees had health care and long-term contracts thanks to the United Mine Workers of America. They were difficult to fire, and they stuck together. In some cases, multiple generations of men in the same family had worked on the line. "That union," a former Remington executive told me disdainfully, "had them by the balls."

If Press had every reason to send his client south, though, he lacked any special affection for Huntsville. For one thing, he explained to me, the airport had a shortage of worthwhile direct flights. For another, the technical labor pool was limited compared with those of larger cities. Press fine-tuned his list, disclosed the name of his client, and flew to Huntsville for a series of meetings, still skeptical. Across the table sat Battle, the head of the Chamber of Commerce and the state's economic-development director. They flipped their cards one by one. The governor's office would give Remington a significant abatement of their income tax for 10 years. The Tennessee Valley Authority would provide discounted electricity. Alabama Industrial Development Training, a state agency, would train Remington's workers free, as it had done for 800,000 others at big-name companies in Alabama, like Boeing, Raytheon and Mercedes.

Then Battle flipped the fourth ace: He agreed to purchase and renovate the former Chrysler factory in Huntsville for $12.5 million and give it to Remington rent-free. Press could scarcely believe his good fortune. "It is hard to think of a deal that is better than the Remington deal from the perspective of the company," he told me. "And I've done easily 200."

In exchange for tens of millions in incentives, Remington had only to

In exchange for tens of millions in incentives, Remington had only to commit to a few terms, laid out in a fat document called a development agreement. First, it had to hire enough employees every year so that, in 2021, it would have a local work force of 1,868. Second, starting immediately, it had to pay those employees a minimum average hourly wage of $19.50, rising to $20.19 in 2017. All parties signed.

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Private-equity firms typically replace existing managers and install handpicked lieutenants. At Remington, George Kollitides was made chief executive in 2012. A Cerberus managing director until that year, Kollitides was a private-equity star and a fixture in New York philanthropy circles. He received his M.B.A. from Columbia in the late 1990s and, like Feinberg, was a firearms enthusiast. (Kollitides declined to comment for this article.)

Kollitides spent much of 2013 and 2014 zigzagging across the country in Remington's Piaggio turboprop. Handsome and charming, he persuaded a number of sought-after executives to relocate to Huntsville. "George picked me up in the plane in New Hampshire," said Ginger Chandler, a former Smith & Wesson executive who served as senior vice president of new-product development at Remington from 2014 to 2017. "He brought me to Huntsville, and he showed me the engineering lab," she said. "That's how he convinced me. For an engineer in the gun industry, these facilities were superior to everyone else's, except maybe Sig Sauer's. George convinced me that they had a dream in Huntsville, and I believed him."

The dream was lofty and ambitious, and Huntsville was only a piece of it. Cerberus had been trying for years to assemble a dominant American gun company. First, in 2006, it purchased Bushmaster, known for its AR-15-style rifles. Then it paid $118 million in cash for Remington and assumed the company's debt. Other acquisitions followed, until by 2013, 18 businesses were rolled up together under Cerberus's roof. One of Kollitides's jobs was to oversee the necessary layoffs. In Ilion, where Remington has operated for 191 years on the same site — unfinished weapons had to travel from one brick building to the next — 231 people lost their jobs. There were 160 layoffs at Montana Rifleman in Kalispell, Mont. The Advanced Armament Corporation, a manufacturer of suppressors and silencers, closed its plant in Georgia, and 68 people were let go from D.P.M.S. Panther Arms in St. Cloud, Minn.; 65 from Para USA in Pineville, N.C. What remained was to increase profit margins by combining all these scattered production lines into a single megafactory.

revenue. In 2014, it earned $939 million. Guns sales are driven by anti-gun rhetoric; a popular joke in the industry is that Barack Obama was the greatest gun salesman of all time. The numbers bear this out. In 2013, the year following his second electoral victory, American gun companies produced 10,844,792 firearms, 222 percent more than they produced in the year after the 9/11 terrorist attacks. In 2015, expecting another Democrat in the White House, many manufacturers thought the party would continue, stoked by a combination of gun-control rhetoric and the right-wing media's confiscation conspiracies.

There was, however, a hidden, vaguely mysterious quirk of the company's finances. In 2012, more or less in the middle of the best climate for gun makers in a generation, America's oldest continually operating manufacturer abruptly, and for no easily discernible reason, borrowed hundreds of millions of dollars. When the company came to Alabama, it owed $828 million to its creditors. While this number, compared with the company's earnings, represented a comfortable ratio on the balance sheet, it was nonetheless curious. The debt could conceivably have been explained by the cost of opening a new factory were it not for the fact that Remington got its factory free.

Last fall, a former Remington executive, who asked that his name not be used for fear of a backlash, opened the door to his house in Huntsville and beckoned me into his study, where we sat on either side of a fireplace. A four-volume edition of "The Adventures of Huckleberry Finn" bound in dark green leather sat on the mantle, next to Howard Zinn's "A People's History of the United States" and a copy of the United States Constitution.

I had met the executive in a bar in Huntsville, where I was looking for a different Remington executive, one who ultimately refused an interview because I couldn't satisfy his condition of getting a prominent American war journalist to send him a personal email. This one told me he would talk if I showed up at his house the next morning with a Dunkin' Donuts pumpkin latte, which I now set in front of him on his Oriental rug.

He explained that he was "a realist" about business, a game in which not everyone gets "a shiny rose at the end," but even so he sensed that something had gone deeply wrong. Executives were fired at a fast clip. Line employees came and went. Parts piled up on the factory floor. Most worrying, Cerberus, which was trying to integrate disparate brands — the father-son pastoralism of Remington with the urban-militia aesthetic of AAC, for instance — seemed to him miserly when it came to marketing. "The decisions were all about: Where can I save another dime?" he told me.

Despite all this frenzy, he was certain that Cerberus had somehow made a great deal of money on Remington even before opening the Huntsville factory. According to him, Cerberus had made "hundreds of millions of dollars" almost immediately. "They pulled out all that money up front, took as much cash as they could."

"How?" I said.

He squinted cryptically. "They get their money."

I realized he didn't know. I went back and reread Remington's public filings. It was obvious when the debt appeared, in 2012. What wasn't clear was where the money went. I showed the filings to a professor of finance. He said it looked as if Cerberus had wound up in debt to itself. "Seems like they did something stupid," he said. "But that can't be right, because they're not stupid."

I asked Gustavo Schwed, a professor of private equity at New York University who spent 24 years in the industry, to help me review the documents. Schwed pored over the many years of financial data and located two separate debt transactions, one of which was so esoteric I would never even have known to look for it. Together, these transactions explained not just the mysterious 2012 loan but, indirectly, the way the deal finally unraveled.

In order to buy Remington, Cerberus, as most private-equity firms would, created a new entity, a holding company. Instead of Cerberus buying a gun company, Cerberus put money into the holding company, and the holding company bought Remington. The entities were related but — and this was crucial — each could borrow money independently. In 2010, Cerberus had the holding company borrow $225 million from an undisclosed group of

lenders, most likely hedge funds. Because this loan was risky — the lenders would be paid only if Remington made a lot of money or was sold — the holding company offered a generous interest rate of around 11 percent, much higher than a typical corporate loan. When the interest payments were due, the holding company paid them not in cash but with paid-in-kind notes, that is, with more debt. These are known as PIK notes.

The holding company now had $225 million in borrowed cash. Cerberus, meanwhile, owned most of the shares of the holding company's stock, basically slips of paper they acquired when they created the holding company. The handoff happened next: The holding company spent most of the $225 million buying back its own stock, effectively transferring all the borrowed cash to Cerberus. Cerberus would keep that money no matter what. Meanwhile Remington continued rolling along as though nothing had happened, because Remington itself was not responsible for the holding company's debt. Remington was just an "operating company" that the holding company owned, something that allowed the holding company to borrow money, the way you would take a necklace to a pawnshop. These were garden-variety maneuvers in a private-equity buyout. In the trade, this is called "financial engineering." People get degrees in it.

In April 2012, Cerberus did something fateful, which probably seemed smart at the time. It had Remington borrow hundreds of millions of dollars and use it to buy the holding company's debt, effectively transferring responsibility for the principal and the interest payments onto Remington. America's oldest gun company now owed the money that Cerberus had used to pay itself back for having bought the company in the first place. There were plenty of sensible reasons to do this. Gun sales were high, and the debt that Remington took out was cheaper to service than the paid-in-kind debt.

But there was a catch. Because the operating company borrowed the money with a normal loan — and not with PIK notes — interest payments were required in cash. Suddenly Remington was carrying hundreds of millions of

Suddenly Remington was carrying hundreds of millions of dollars in debt that, if it could not be paid, would cause the business to go bankrupt.

By the time the factory opened in Huntsville, the various players stood in vastly different positions. The private-equity firm had made back its initial investment and was playing with house money. Remington owed hundreds of millions that it hadn't borrowed. And its workers, urgently, had to make a lot of guns.

investment and was playing with house money. Remington owed hundreds of millions that it hadn't borrowed. And its workers, urgently, had to make a lot of guns.

Huntsville is a de facto segregated city. Pastor T.C. Johnson, of St. Luke Missionary Baptist Church, recounted to me how while he was in the Army in the early 1990s, real estate agents didn't show him houses in South Huntsville, the white side of town. He was unaware South Huntsville existed until some of his Army subordinates, who were white, bought homes there. Since 1965 Huntsville's schools have been under a federal desegregation order, which compels school districts to remedy race-based inequality. Johnson's oldest son attended Mae Jemison High, a predominantly black school that the state classified as failing. White students at nearby schools "were so far ahead of my child it was almost sickening," he said.

Johnson's experience was of a piece with the racial hierarchy in Huntsville. Blacks make up 31 percent of the city's population but make up 16 percent of its police force. Unlike Birmingham and Mobile, there has never been a black mayor in Huntsville. Though blacks, like all Huntsvillians, paid the taxes that supported lucrative incentive packages, they seldom reaped the rewards of the best-paying jobs. This reality was of course not felt by whites, Johnson said. For whites, "that's just the way it is."

The Remington factory was housed in a gray building the size of 14 football fields set back behind fencing topped with razor wire. Inside, the building was divided in half, the production line on the left and the administrative and engineering offices on the right, along with a classroom set up by the state agency that provides free worker training for private businesses. Classes for new hires were held three days a week, every week.

About a year after the factory opened, leaders in Huntsville's black community, including Johnson, began to hear reports from inside. Johnson was disappointed but not surprised to learn from his parishioners that on the Remington line, the usual racial divisions manifested. Most of the line

Facebook posts — as they should have been, per the development agreement — no one seemed to be earning anything close to $19.50. Johnson, along with the president of the Huntsville N.A.A.C.P. chapter at the time, the Rev. Robert Shanklin, invited a union organizer from the United Mine Workers of America, the same union that organized Remington's Ilion plant, to use its church facilities and offices as necessary in order to hold clandestine meetings.

The organizer arrived in Huntsville in 2016. He was born in Birmingham and spent most of his career organizing throughout the South. As a result, he tended to be suspicious of Southern bosses — "I have a warped mind when it comes to Alabama," he told me — and he expected an oppositional management at Remington. But another obstacle surprised him. From week to week, in Johnson's church or Shanklin's N.A.A.C.P. office, the organizer rarely saw the same face twice. It seemed to Shanklin that in order to prevent unionization, the factory was exchanging its full-time workers for temps, who came and went rapidly, never sticking around long enough to have a stake. (Remington declined to comment for this article.)

The presence of the temp workers, who were exempt from the minimum average hourly wage in the development agreement, also served as a cautionary tale, a reminder of how much lower you could sink if you raised trouble. Temps started at $9.20 an hour with no benefits. Full-time workers, for their part, were often unaware that the tax-incentive package might entitle them to higher wages than they were receiving. And when they did realize, they were unsure what to do.

While I was in Huntsville, Remington employees told me that if they spoke to me for this article, they would be fired. One woman, a line worker, told me over the phone: "These people, they have ways of finding out if you talked. I talk to you, no ifs, ands or buts, I'm gone. It makes us feel they have something to hide. But we keep our mouths shut. Clock in, clock out."

I eventually met a former employee, who asked to be identified by her first initial, D., and agreed to talk about her experience at Remington. D. started

newspaper article in which the company promised a minimum average hourly wage of $19.50.

After taking her two-week course at A.I.D.T., D. started work. She was assigned to a boxing station, which was not on an assembly line but at a static counter where the workers stood side by side. The job was boring. She received the guns — they were long guns, for hunting — placed them in boxes, then weighed the boxes on a digital scale. If the scale displayed a red light, that meant D. had missed a part. When she opened her first paycheck, she saw that she was earning $12.36 an hour — gross. After taxes and benefits, her take-home pay amounted to $353.70 a week.

After two years, according to paystubs that D. shared with me, she was earning $14.16 an hour. She decided to move into a better apartment in North Huntsville, a two-bedroom with a linoleum square cut out of gray carpeting for a welcome mat. Rent was $675. She bought a Dodge Avenger and a Ruger .380 for protection.

Then, in 2016, D. slipped on a metal pole that a maintenance worker had left outside the factory, grabbed the fence with her right hand to break her fall and felt a muscle tear in her wrist. After missing several days for a second surgery, she says she was called into the office of her supervisor, told that she had missed too much work and fired, three years to the day after she started. As the union effort had fizzled, there was no one she could appeal to for help.

We were sitting in her apartment last October when her cellphone rang. "Tracir Financial's calling," she said. "'Cause I owe on the car." She pressed decline. The fingers of her left hand returned to her right wrist and massaged it.

Over the winter, facing several months of back rent and payments on the Dodge, D. ran out of cash. One morning she woke up to find her car had been repossessed. Bankruptcy offered the only way out, and she filed her petition three weeks before Christmas. Just before the New Year, she was

After the 2016 election, researchers at Cerberus saw an omen in their data. Applications through the National Instant Criminal Background Check System, which are known as "NIC checks," were dropping by double-digit percentages. A plunge in NIC checks foreshadows a corresponding plunge in gun sales, which is what happened in the months that followed. Remington's profit slid toward zero. The debt, meanwhile, was racing upward, like a flame licking a fuse.

For Cerberus's executives, the predicament was like being bitten by a trusted pet. Cerberus has a habit of hiring power brokers from the United States government, many of them prominent Republicans. The former vice president Dan Quayle became chairman of Cerberus Global Investments in 1999; the former Treasury secretary John W. Snow joined Cerberus seven years later. The Republican donor William Richter is a founder. Since May 2018, Feinberg has been a member of Trump's Intelligence Advisory Board, an independent entity created to advise the president on national-security matters. But if Obama was the best, Trump was proving to be the worst gun salesman of all time. Magnifying his negative impact, gun makers had already ramped up production ahead of Hillary Clinton's expected victory: In 2017 the market was choked with surplus product, and Trump's Second Amendment enthusiasm was dousing any hope of a panic buy.

Remington executives arranged a meeting with their creditors. They calmly explained the situation. Remington had been loaded with debt; now it couldn't pay the interest. After listening politely, the banks made a proposal: They would exchange the money they were owed for an ownership stake in Remington, a so-called Chapter 11 bankruptcy or "debt-for-equity swap." This arrangement would allow Remington to stay running, albeit under distant ownership, until a plan could be drawn up for its future, such as a sale or a liquidation of assets.

In March, Remington announced that it would lay off about 200 employees between its Ilion and Huntsville factories. Shortly after that, the state of Alabama, in a routine payroll audit, found that Remington had missed its hiring targets: Only 450 people were working at the plant at the beginning of 2018, as opposed to the 680 promised in the development agreement. In response, the county and state revoked a number of their tax incentives and demanded the return of $500,000. Remington, not Cerberus, will be responsible for the sum.

responsible for the sum. By the time the state finished its audit, the private-equity firm had long since exited the scene.

A source told me that Cerberus executives were disappointed in the way the Remington transaction turned out; you never want your companies to end up in bankruptcy. Even so, for the firm, at least, the decade-long saga had been profitable.

Jesse Barron is a writer in Los Angeles. He last wrote for the magazine about investors' attempts to profit from climate change.

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