The following constitutes the order of the Court.

Signed October 29, 2003.

United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE:	§	
	§	
GPR HOLDINGS, L.L.C.,	§	CASE NO. 01-36736-SAF-11
	§	
AURORA NATURAL GAS, L.L.C.,	§	CASE NO. 01-36709-SAF-7
	§	
GOLDEN PRAIRIE SUPPLY SERVICES,	§	
L.L.C.,	§	CASE NO. 01-36904-SAF-7
	§	
D E B T O R S.	§	

MEMORANDUM OPINION AND ORDER

GPR Holdings, L.L.C., moves the court to approve a settlement with John Litzler, the Chapter 7 trustee of the bankruptcy estate of Golden Prairie Supply Services, L.L.C., (GPSS); Robert Newhouse, the Chapter 7 trustee of the bankruptcy estate of Aurora Natural Gas, L.L.C., (ANG); and Bayerische Hypo- und Vereinsbank Aktiengesellschaft, New York Branch (HVB). Litzler and Newhouse request that the settlement be approved for their respective estates, as well. Duke Energy Trading and

Marketing, L.L.C., objects to the settlement.[1] The court conducted an evidentiary hearing on the settlement on October 14, 2003.

The determination of a motion to approve a settlement by a bankruptcy estate under Bankruptcy Rule 9019 constitutes a core matter over which this court has jurisdiction to enter a final order. 28 U.S.C. §§ 157(b)(2)(B) and (O) and 1334. This memorandum opinion contains the court's findings of fact and conclusions of law. Bankruptcy Rules 7052 and 9014.

The court may approve a settlement if the settlement is "fair and equitable and in the best interest of the estate." Connecticut Gen. Life Ins. Co. v. United Cos. Fin. Corp. (In re Foster Mortgage Corp.), 68 F.3d 914, 917 (5th Cir. 1995). The words "fair and equitable" are terms of art, referring to the creditor priority scheme of the Bankruptcy Code. In deciding whether a settlement is fair and equitable, the court must make a well-informed decision, comparing the terms of the compromise with the likely rewards of litigation. Matter of Cajun Elec. Power Co-op., Inc., 119 F.3d 349, 355-56 (5th Cir. 1997). The court must consider the probability of success in the litigation with due consideration for the uncertainty in fact and law; the complexity and likely duration of the litigation and any

[1]Edge Petroleum Operating Co. also objected to the settlement. The Edge objection was resolved on the record at the hearing on October 14, 2003.

attendant expense, inconvenience and delay; and other factors bearing on the wisdom of the compromise. Id. The "other factors" include the best interest of the creditors, with deference to their reasonable views, and the arms length nature of the negotiations. Id.

All three bankruptcy estates and HVB have filed lawsuits against Duke for gas purchases and sales and related transactions. They assert claims for fraud, breach of contract, conversion and bankruptcy avoidable transfers. The trustees assert that the claims filed against Duke by HVB belong to the bankruptcy estates.

HVB has filed proofs of secured claims for approximately $23.5 million dollars against each of the three bankruptcy estates. HVB asserts a security interest in assets of the estates. The security interest does not reach the avoidance claims held by the estates under Chapter 5 of the Bankruptcy Code. In addition, GPR has asserted a claim against ANG.

The bankruptcy estates and HVB have agreed to pool their respective claims against Duke, with GPR litigating the claims against Duke, and HVB funding the litigation. From any recovery from Duke, after payment of litigation expenses, the ANG estate would receive 25% of the recovery, GPSS 12% (with a minimum of $175,000) and GPR 63%. GPR would have an allowed claim against the ANG estate of $30 million, with the HVB lien attaching to the claim. From ANG’s share of a Duke recovery, Newhouse would be paid a 3% trustee commission, 87.5% would be paid to HVB, and the balance would be available for ANG’s unsecured creditors. HVB would receive 70% of the net Duke recovery. HVB would receive the 70% based on its distribution on its claims in the ANG and GPSS cases, with the remainder of the 70% from the GPR estate.

The first $450,000 recovered by ANG from assets other than the claims against Duke will be paid to creditors other than GPR or HVB. The first $3.5 million received by GPR from GPR assets, after satisfying the 70% distribution to HVB, will go to other creditors, after which HVB will share as a deficiency unsecured creditor with the other unsecured creditors pro rata. After payment of the 70% of the net Duke recovery to HVB, HVB will subordinate any remaining secured claim in the GPR estate to assure the $3.5 million distribution to other creditors. HVB further waives a claim to the first $3.5 million received from GPR assets other than the Duke recovery, regardless of the success on the claims against Duke.

Duke has filed claims against the bankruptcy estates for approximately $25 million. In its capacity as a creditor, as contrasted with its capacity as a defendant, Duke objects to HVB being paid as a secured creditor from any recovery from Chapter 5 causes of action. In effect, Duke contends that HVB is selling its claims against Duke to the bankruptcy estates in exchange for a 70% recovery from Duke. That recovery, however, may derive solely from Chapter 5 causes of action. HVB does not have a security interest in the Chapter 5 causes of action. Consequently, Duke argues that recovery by HVB as a secured creditor from a Chapter 5 judgment would alter the fair and equitable standards of the Bankruptcy Code. By doing so, Duke's share of the unencumbered assets would be diminished unfairly and inequitably.

Duke further argues that the settlement conflicts with the GPR confirmed Chapter 11 plan. Duke contends that under the plan, all unsecured creditors would share Chapter 5 recoveries pro rata. If HVB held an unsecured claim based on a deficiency, it would share in the pro rata distribution. Under the settlement, 70% of a net Chapter 5 recovery from Duke would go to HVB, thereby depriving the unsecured creditors, including Duke, of their pro rata share of that recovery.

In the settlement, HVB agrees to fund the litigation against Duke. The bankruptcy estates estimate that the cost of the litigation will be approximately $1 million. By order entered July 8, 2003, the court approved a joint prosecution agreement between the GPR and GPSS estates, whereby counsel was retained on a contingency fee arrangement. This settlement obviates the contingency fee arrangement, without relief from the court order. Duke opposes that action.

The bankruptcy estates respond that the settlement assures funds for unsecured creditors in each estate, resolves any dispute with HVB of whether its claims against Duke actually belong to the bankruptcy estates, and resolves inter-estate claims. In the event of a recovery from Duke, the estates retain what would have been paid as a contingency fee to counsel. In the event that Duke prevails in the litigation, HVB would not be recovering the 70%, but the remainder of the agreement would remain in place, thereby assuring the availability of some assets in each estate for distribution to unsecured creditors.

For each estate, the settlement assures that assets will be available for distribution to creditors, including Duke, other than HVB, irrespective of the success in the litigation against Duke. As the court understands the settlement, HVB subordinates its secured claim to assure that $3.5 million is available in the GPR estate, $450,000 in the ANG estate and $175,000 in the GPSS estate. HVB pays the costs of litigating against Duke. Duke, of course, wearing its defendant’s hat, asserts that the claims against it are meritless. From its creditor’s perspective, therefore, the settlement should be in the best interest of the unsecured creditors in each estate. The recovery of the litigation costs and the payment of the 70% from a Duke recovery only occur if there is a Duke recovery. If the Duke litigation lacks value to the estates, then the settlement is in the best interests of the creditors, including Duke. But, of course, at this stage of the litigation against Duke, considering the complexity of the claims against Duke and the range of probable success, the court cannot conclude that the claims against Duke do not have value. As a result, the court must consider whether the portion of the settlement that provides for payment to HVB of 70% of a net recovery from Duke is fair and equitable.

GPR attempted to demonstrate that in the event Duke lost the litigation, but paid any resulting judgment, its recovery would be within a reasonable range of what it would have received without the settlement. But the testimony was general in nature and insufficient to support fact findings.

So, the court must focus on the best interest of creditors under the fair and equitable standard, with due deference to Duke’s reasonable views, in its role as a creditor. In that regard, the court considers three scenarios.

First, if Duke prevails in the litigation, the settlement is in the best interests of the creditors of all three estates, and is fair and equitable. The 70% recovery to HVB would not be applicable. Yet, the settlement assures a distribution to unsecured creditors in each estate, irrespective of HVB’s status as a secured creditor.

Second, if the estates prevail against Duke on a non-Chapter 5 claim only, then the settlement is in the best interests of the creditors of all three estates, and is fair and equitable. HVB's lien would presumably attach to the proceeds from the recovery on non-Chapter 5 claims. The 70% distribution would then be made to HVB in its status of a secured creditor, and made from proceeds deriving from its collateral.

Third, if the estates prevail against Duke on a Chapter 5 claim only, then the settlement may not be in the best interests of the creditors and may not be fair and equitable.[2] Duke would receive 70% of proceeds not covered by its lien. Without the settlement, it would only share in those proceeds in its capacity as an unsecured creditor. There is no evidence what its likely unsecured deficiency claim would be. If Duke paid the Chapter 5 judgment, it would have an allowed claim that could be in the range of $45 million. There is insufficient evidence to compare the range of its recovery with or without the settlement. If the comparison demonstrates recoveries to Duke as an unsecured creditor within a reasonable range with or without the settlement, then the 70% distribution to HVB from unencumbered proceeds may be in the best interests of the creditors. If so, Duke's view would not be reasonable and the court would owe it no special deference as a large creditor. Instead, the court would

[2]Of course, the litigation results could be more complicated, as the estates could conceivably recover on claims in which HVB could assert a security interest and on Chapter 5 claims. GPR must demonstrate the factors to consider as part of the complexity of the litigation.

discount Duke’s view, as being that of a defendant. But if the range is not reasonable, then HVB, under this scenario, may be unfairly and inequitably taking unencumbered assets from unsecured creditors to be applied to its status as a secured creditor. Duke’s view as a creditor would then be entitled to deference.

Without a complete evidentiary record addressing the third scenario, the court cannot determine if the settlement is in the best interests of creditors and fair and equitable. Until the court makes that determination, the court cannot assess whether the settlement would be consistent with the GPR confirmed plan. For this reason, the court will reopen the record to allow the presentation of evidence addressing the potential range of recoveries from Chapter 5 claims with and without the settlement.

Based on the foregoing,

IT IS ORDERED that the court will resume the evidentiary hearing on the motion to approve the settlement on **December 1, 2003, at 1:30 p.m.**

###END OF ORDER###