

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re:

CYNERGY DATA, LLC, *et al.*,¹

Debtors.

Chapter 11

Case No. 09-13038 (KG)
(Jointly Administered)

Hearing Date: September 15, 2009 at 2:00 p.m. (ET)
Objections Due: September 10, 2009 at 4:00 p.m. (ET)
Ref. Nos. 11, 49

**LIMITED OBJECTION OF TERM B PARTIES TO ENTRY OF FINAL ORDER
(I) AUTHORIZING USE OF CASH COLLATERAL, (II) AUTHORIZING
POSTPETITION FINANCING, (III) GRANTING SENIOR PRIMING LIENS
AND SUPERPRIORITY CLAIMS, AND (IV) GRANTING ADEQUATE
PROTECTION TO THE PREPETITION SECURED PARTIES**

Ableco Finance LLC, A3 Funding LP, Garrison Credit Investments I, LLC, and Garrison Credit Opportunities Holdings L.P., as lenders (the "Term B Lenders") under that certain Credit Agreement (the "Prepetition Senior Credit Agreement") dated as of August 1, 2008 among the Debtors, the various lenders party thereto from time to time (the "Prepetition Senior Lenders") and Comerica Bank, as agent for the Prepetition Senior Lenders, and Dymas Funding Company, LLC, as agent for the Term B Lenders (together with the Term B Lenders, the "Term B Parties"), submit this limited objection to entry of a final order (the "Final DIP Order") approving the proposed debtor in possession financing (the "DIP Financing") for the above-captioned debtors and debtors-in-possession (collectively, the "Debtors"), and, in support thereof, respectfully state as follows:

PRELIMINARY STATEMENT²

1. As a prerequisite for the priming envisioned by the DIP Financing, the

¹ The Debtors are the following entities (with the last four digits of their federal tax identification numbers in parentheses): Cynergy Data, LLC (8677); Cynergy Data Holdings, Inc. (8208); Cynergy Prosperity Plus, LLC (4265). The mailing address for the Debtors is 30-30 47th Avenue, 9th Floor, Long Island City, New York 11101.

² All capitalized but not defined terms used in this Preliminary Statement have the respective meanings ascribed to them below.

Debtors must either have the consent of the holders of those interests that are being primed or must conclusively demonstrate that those interests are adequately protected. With respect to the Term B Parties, neither condition is satisfied.

2. The Term B Parties were willing to consent to the priming contemplated by the proposed DIP Financing, but only on the condition that the liens granted to the Working Capital DIP Lenders not extend to any prepetition causes of action, choses in action, or commercial tort claims which were not subject to validly perfected unavoidable liens in favor of the Working Capital DIP Lenders in their capacities as Term A Lenders as of the Petition Date (collectively, the "Prepetition Causes of Action"). The Working Capital DIP Lenders have to date been unwilling to limit their liens in the manner set forth above and thus the Term B Parties have not and do not consent to the priming of their prepetition liens.

3. However, the Debtors have not shown, and are unable to show, that the Term B Parties' interests are adequately protected, such that the Court may prime those interests. Accordingly, the requirements of section 364(d) of the Bankruptcy Code have not been met, and the Court cannot approve the DIP Financing on the final basis in the form proposed.

FACTUAL BACKGROUND

4. On August 3, 2009 (the "Petition Date"), the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code, 11 U.S.C. §§ 101-1532 (as amended, the "Bankruptcy Code"). Pursuant to sections 1107 and 1108 of the Bankruptcy Code, the Debtors are continuing to operate their businesses and manage their properties as debtors in possession.

5. The Debtors' obligations under the Prepetition Senior Credit Agreement, although all secured by a first priority lien on substantially all of the Debtors' assets, are contractually divided into two tranches, based on agreed upon priority of distribution. As of the Petition Date, \$77,112,351.40 in principal amount was outstanding under the Prepetition Senior

Credit Agreement, of which \$50,210,618.75 was owing to the Prepetition Senior Lenders entitled to be paid down first (the "Term A Lenders"), and \$26,901,732.65 was owing to the Term B Lenders – the Prepetition Senior Lenders entitled to be paid down after the Term A Lenders have been paid in full.

6. On the Petition Date, the Debtors filed a motion seeking approval of the DIP Financing, a portion of which, in the amount of up to \$25,000,000 is being provided by the Term A Lenders (in such capacity, the "Working Capital DIP Lenders"). In addition to the priming liens on, among other collateral, the Prepetition Causes of Action, the DIP Financing provides for a creeping rollup of the Debtors' prepetition indebtedness to the Term A Lenders.

7. On the Petition Date, the Debtors also filed a motion seeking approval of certain bidding procedures in connection with a stalking horse asset purchase agreement (the "Asset Purchase Agreement") for the sale of substantially all of their assets. The purchase price offered under the Asset Purchase Agreement is \$81,000,000 (a portion of which consists of junior indebtedness at below-market interest rates), net of cure amounts payable with respect to the executory contracts and unexpired leases that the purchaser may wish to assume in connection with such sale. The Debtors did not even attempt to quantify what those cure payments may be, so it is impossible to determine what portion of the cash purchase price will actually be available for distribution to creditors. As such, the true value of the purchase price offered under the Asset Purchase Agreement is significantly less than the \$81 million "headline number."

8. Accordingly, it appears that, while both the Working Capital DIP Lenders and the Term A Lenders are fully secured and are not at risk, the Term B Parties may well end up being undersecured, and are thus the true fulcrum class in these cases bearing all the risk of the proposed priming.

9. In the Declaration of Charles M. Moore in Support of Chapter 11 Petitions and Various First-Day Applications and Motions filed by the Debtors on the Petition Date (Docket No. 3; the “Moore Aff.”), the Debtors disclosed the existence of “certain errors” in their internal accounting and financial reporting that “had the effect of misstating certain revenues and expenses” (Moore Aff. at ¶ 32), which are likely to be investigated and pursued by the Debtors' creditors. Based on the only indication of the value of the Debtors' estate available to the Term B Parties (the purchase price provided under the Asset Purchase Agreement), there is a high likelihood that the proceeds of the Prepetition Causes of Action may prove to be the sole source of full repayment for the Term B Parties. Instead, the current structure of the DIP Financing – through the rollup feature – makes the Prepetition Causes of Action available to the Term A Lenders in the highly unlikely scenario they may prove not to be oversecured and require additional protection. This is not warranted in the circumstances of this case, and amounts to the highly disfavored cross collateralization – despite the Debtors' representation to this Court that no cross collateralization is effected by the DIP Financing.

ARGUMENT

10. The ability to prime an existing lender is considered to be an “extraordinary remedy.” In re Seth Co., Inc., 281 B.R. 150, 153 (Bankr. D. Conn. 2002) (citing 3 Collier On Bankruptcy ¶ 364.05 (15th ed. Rev. 2002)). Because priming “financing displaces liens on which creditors have relied in extending credit, a court that is asked to authorize such financing must be particularly cautious when assessing whether the creditors so displaced are adequately protected.” In re First South Sav. Assoc., 820 F.2d 700, 710 (5th Cir. 1987) (citation omitted); In re Mosello, 195 B.R. 277, 289 (Bankr. S.D.N.Y. 1996) (same). In fact, the Third Circuit Court of Appeals has found it “disturbing” that a bankruptcy court would condone the eroding of a secured creditor’s position through priming without a “tangible” proof of adequate protection. In re Swedeland Dev. Group, Inc., 16 F.3d 552, 567 (3d Cir. 1994).

11. Absent the Term B Parties' consent, section 364(d)(1) of the Bankruptcy Code clearly authorizes priming *only* when “there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted.” Swedeland, 16 F.3d at 564. Furthermore, it is the debtor that “has the burden to establish that the holder of the lien to be subordinated has adequate protection.” Id. The Debtors have failed to meet their burden of satisfying either such element.

I. Term B Parties Have Not Consented to Priming

12. While the Term B Parties were willing to consent to the priming contemplated by the DIP Financing, their consent was conditioned on the Working Capital DIP Lenders not obtaining a postpetition lien on the Prepetition Causes of Action. Since the Working Capital DIP Lenders refused to accommodate the Term B Parties' request, no consent to the priming of their liens and security interests has been given, as the Term B Parties stated at the interim hearing on the DIP Financing.

II. Term B Parties' Interests Are Not Adequately Protected

13. The Term B Parties' interests in their collateral are not adequately protected under the circumstances of these cases. While the Bankruptcy Code does not expressly define “adequate protection,” section 361 of the Bankruptcy Code provides that adequate protection may be provided by: (a) periodic cash payments; (b) additional or replacement liens; or (c) other relief resulting in the “indubitable equivalent” of the secured creditor’s interest in its collateral. See 11 U.S.C. § 361. According to the Third Circuit, “[t]he whole purpose of adequate protection for a creditor is to insure that the creditor receives the value for which he bargained pre-bankruptcy.” Swedeland, 16 F.3d at 564 (citations omitted); see also United Sav. Ass’n v. Timber of Inwood Forest Assocs., 484 U.S. 365, 370 (1988). “Whether protection is adequate depends directly on how effectively it compensates the secured creditor for the loss of value caused by the superpriority given to the post-petition loan. In other words, the proposal

should provide the pre-petition secured creditor with the same level of protection it would have had” if his security interest had not been primed. Swedeland, 16 F.3d at 564.

14. Clearly, the Term B Parties will not maintain their pre-bankruptcy contractual rights because the DIP Facility would layer up to an additional \$25 million of debt that would be entitled to payment ahead of them under any plan of reorganization or from the sale proceeds. There is no showing, as required by the Third Circuit precedent, that the Term B Parties will be compensated for any diminution in the value of their collateral caused by the priming of their lien or the use of their cash collateral. See Swedeland, 16 F.3d at 564. Indeed, the Debtors have not provided any quantitative evidence whatsoever to demonstrate the adequacy of the "adequate protection" that is being offered -- including evidence concerning the value of the collateral, the value of the proposed adequate protection package, or the ability of the proposed adequate protection package to compensate the Term B Parties for the decline in the value of their collateral.

15. Although not dispositive, one factor that could be examined in determining whether the Term B Parties' interests are adequately protected would be whether a sufficient "equity cushion" exists. Even if the \$81 million were the true value of the purchase price under the Asset Purchase Agreement, such a valuation could not provide a basis for priming by \$25 million as it demonstrates, at most, an equity cushion of less than \$4 million for the Term B Parties **before** taking into account the additional monies needed to pay the cure amounts. Because the Debtors cannot establish the existence of an equity cushion for the Term B Parties (let alone that any such equity cushion falls within an acceptable range to provide a component of adequate protection), they will need to provide the Term B Parties with other forms of adequate protection. Notably, no replacement liens of any value can be provided to the Term B Parties because prepetition liens encumber substantially all of the Debtors' assets and the sole source of paying the administrative expenses is the cash collateral of the Prepetition Senior

Lenders, including the Term B Parties. Not surprisingly, the Third Circuit has stated that adequate protection cannot be achieved by offering the secured creditor something he already has the right to. Swedeland, 16 F.3d at 565.

RESERVATION OF RIGHTS

16. The Term B Parties expressly reserve their right to amend or supplement this objection, to introduce evidence supporting this objection at the final hearing with respect to the DIP Financing, and to seek additional or different adequate protection at any point in the future.

CONCLUSION

WHEREFORE, the Term B Parties request that the Court deny entry of the Final DIP Order unless it is modified as set forth above, and grant such other and further relief to the Term B Parties as the Court deems appropriate.

Dated: Wilmington, Delaware
September 10, 2009

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