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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
Case No. 10-14997-BRL

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In the Matter of:

BLOCKBUSTER, INC., et al.,

Debtors.

- - - - -x

United States Bankruptcy Court
One Bowling Green
New York, New York

October 27, 2010

10:03 AM

B E F O R E:
HON. BURTON R. LIFLAND
U.S. BANKRUPTCY JUDGE

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INITIAL CASE CONFERENCE

HEARING re Debtors' Motion for an Interim Order Requesting (I) Authority to Pay Certain Prepetition Claims of Movie Studios and Game Providers and (II) Administrative Expense Priority Status for All Undisputed Obligations Arising Postpetition

HEARING re Debtors' Motion for Entry of an order, on an Interim and Final Basis, (I) Authorizing the Debtors to Obtain Postpetition Superpriority Financing, (II) Authorizing Debtors' Use of Cash Collateral, (III) Granting Liens and Super priority Claims to DIP Lenders, (IV) Providing Adequate Protection, and (V) Scheduling a Final Hearing

HEARING re Application to Employ, Weil, Gotshal & Manges LLP as Attorneys for the Debtors

HEARING re Application to Employ Rothschild, Inc. as Financial Advisor and Investment Banker

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HEARING re Application of the Debtors to (I) Retain Alvarez & Marsal North America, LLC to Provide the Debtors a Chief Restructuring Officer and Certain Additional Personnel and (II) Designate Jeffrey J. Stegenga as Chief Restructuring Officer for the Debtors Nunc Pro Tunc to the Commencement Date

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P R O C E E D I N G S

MR. SOSLAND: Let people get settled. Good morning,
Your Honor.

THE COURT: Good morning.

MR. SOSLAND: Martin Sosland of Weil, Gotshal & Manges
on behalf of the debtors.

THE COURT: Kay, can I get a pad?

(Pause)

MR. SOSLAND: Your Honor, we have several matters set
on the agenda this morning. If it pleases the Court, we would
like to begin with the DIP and cash collateral motion, which is
tab two in the binder. It's item B on the agenda letter that
we filed with the court.

THE COURT: Go ahead.

MR. SOSLAND: Your Honor, I'm pleased to report that
we've made significant progress on resolving both formal
objections that were filed on the Court's docket, as well as
informal concerns that were raised by the creditors' committee
in connection with the motion.

The reason that you did not see a formal objection
filed by the creditors' committee, is that because virtually
from the formation of the committee and their retention of
Cooley, in particular, as well as FTI as professionals for the
committee, there was a dialogue, basically a three-way dialogue
among the debtors, the secured lenders, and proposed DIP

1 lenders, and the committee regarding certain concerns that the
2 committee had with the form of the DIP agreement.

3 And to that end, Your Honor, there were several
4 changes that have been made in the final -- in the form of
5 final order that we have to address their concerns. And I'll
6 go through them. I have a blackline if that would assist Your
7 Honor.

8 THE COURT: That might.

9 MR. SOSLAND: Your Honor, what we've provided you is a
10 blackline between the form of -- between the interim order that
11 the Court entered on October 27th -- on September 27th, and the
12 form of final order that we propose be entered today. And the
13 notable -- I can go to the specific provisions, but let me
14 first highlight the most notable changes that have been made at
15 the request of the creditor's committee.

16 First of all, Your Honor, regarding the roll-up. Upon
17 entry of the final order, the order would now provide that 125
18 million dollars of pre-petitioned secured notes will be rolled
19 in accordance with the provisions of the existing DIP
20 agreement, and the draft -- and the order has been revised to
21 provide the 125 million as opposed to the previous 250 million
22 dollars. So that's a one-to-one rather than a two-to-one ratio
23 of the amount of the pre-petition debt that's rolled out to the
24 new financing under the DIP agreement.

25 Another change, Your Honor, with regard to the budgets

1 -- budgeting process, we will continue to submit to the lenders
2 for approval, budgets on a monthly basis; however, if a budget
3 is not timely approved or rejected by the secured lenders, the
4 debtors will continue to operate under the prior budget, and
5 the parties will negotiate in good faith to try to resolve the
6 dispute relating to the budget. So there's no automatic
7 termination provision, as there was in the original proposed
8 DIP. So that's a change that the committee negotiated that's
9 an additional, a significant change beneficial to the estate.

10 Your Honor, with regard to avoidance actions, the DIP
11 lenders will have a lien on avoidance actions for new money
12 advanced under the DIP credit agreement, but there will be no
13 lien on the avoidance actions for any of the rolled up DIP, the
14 rollover, or for the pre-petition secured notes, and the liens
15 supporting the new money is basically -- should be applied
16 last.

17 So if the DIP is satisfied by other assets of the
18 estate, there will not be a lien on the avoidance actions.
19 There would only be a lien on avoidance actions, to the extent
20 that the debtors are -- have not or cannot pay off the DIP,
21 basically and to feasibly satisfy the obligations for the new
22 money under the DIP agreement.

23 And then there's also a change with regard to the
24 milestones under the plan, so that both -- under the DIP
25 agreement that tie to the plan support agreement. The

1 milestone date both for the approval of the business plan by
2 the secured lenders and for submission of a plan and disclosure
3 statement are November 30th. That's basically the same date.

4 Your Honor, those -- with those primary changes, and
5 Mr. Seary (ph) and Mr. Kanowitz are here also to address that.
6 That resolves the committee objections.

7 I'd also like to point out that we've made changes to
8 the -- proposed changes to the DIP agreement that resolve the
9 landlord, all of the landlord objections that were filed.
10 Those are basically a continuation of changes that were made in
11 the form of interim order that continue through, and we've
12 resolved all of the landlord objections.

13 And with regard to the taxing authorities, in addition
14 to the changes that we announced on the record, for example,
15 that there are no -- that the DIP doesn't prime existing tax
16 liens that had priority the -- we've resolved all of the
17 objections of the various taxing authorities that were filed.

18 And so that would leave outstanding only the objection
19 of Lyme Regis. And, Your Honor, to the extent that Lyme Regis'
20 papers have requested a contested hearing, we rely on the
21 testimony that we've submitted in connection with the interim
22 hearing, but we are here today to make the witnesses in support
23 of the DIP available for cross-examination.

24 With regard to the actual substance of the objection
25 that was filed by Lyme Regis, a lot of that went to the

1 protections, if you will, that were -- that are afforded the
2 pre-petition secured lenders under the DIP agreement, and
3 because of the investigation work that the committee will do,
4 I'd like to cede the podium to Mr. Kanowitz, because I'm
5 hopeful, and I don't know whether this is the case, that the
6 work that the committee will do in that regard, would alleviate
7 some of the concerns of Lyme Regis. But I can answer any other
8 questions that the Court has.

9 THE COURT: I have none.

10 MR. KANOWITZ: Your Honor, may I be heard?

11 THE COURT: Sure.

12 MR. KANOWITZ: Good morning, Your Honor. Richard
13 Kanowitz of Cooley, proposed counsel to the creditors'
14 committee.

15 Mr. Sosland sort of stole my thunder going through a
16 laundry list of things, but I think Your Honor should hear from
17 us as to how we viewed the DIP and our negotiations.

18 When the committee was formed, they tasked Cooley to
19 improve on both the business, as well as legal aspects of the
20 DIP, and I think we've accomplished that. The key to the DIP
21 here, at the proposed DIP was a two-for-one roll-up, which
22 really was problematic on multiple reasons.

23 First is, it was a blocking position on any type of
24 alternative transaction, putting 250 million dollars of
25 additional cash on the table, just to try to do an alternative

1 transaction was problematic from our view. Clearly, also,
2 looking at the DIP two-to-one roll-up as a preference, meaning
3 in a liquidation, that would be rolled up and it would have to
4 be paid out before any distribution to other creditors was also
5 problematic.

6 Under the threat of litigation, including subpoenas
7 and other document requests, the DIP lenders, as well as the
8 debtor, as well as the committee, negotiated a one-for-one
9 roll-up. We preferred no roll-up, but we recognized the fact
10 that DIP lenders will not lend without some sort of
11 protections, including a roll-up, and we're satisfied that the
12 one-to-one is appropriate, given the circumstances that we face
13 today in the case.

14 Another aspect of the DIP that was problematic was the
15 protections granted to the pre-petition lender, as well as the
16 DIP lender in the avoidance actions. We negotiated out the
17 fact that the avoidance actions will not be -- or the proceeds
18 thereof, will not be protections for the pre-petition lenders,
19 they will be last money out for the DIP lenders and only on the
20 new money advance. And if there's a hole at the end of the
21 case, that's where this will come into play.

22 We've already put in the order the provisions that all
23 the parties in interest, if there is a dispute, over how those
24 avoidance action proceeds get applied, we'd come before Your
25 Honor.

1 The next item that the committee focused on was the
2 business terms, making sure the covenants did not trip up this
3 company as they moved along in this case. It is a very fast
4 track case. The way we viewed the budget before, was that at
5 any four-week period, the DIP lenders could very well say, well
6 we don't approve the budget, and the DIP terminates. That
7 would invoke the DIP roll-up, and all the bad things that we
8 want to try to avoid in this case would happen.

9 So with the negotiations that went on, they've agreed
10 to allow, while the company, as well as the DIP lenders work on
11 the four-week budget, and any particular period, the debtors
12 will be able to operate under the then current thirteen-week
13 budget.

14 So those are the highlights, Your Honor. Suffice it
15 to be said, it's not like we're going to sing Kumbaya in the
16 hallway. There are a lot of issues to be worked out in this
17 case, including the proposed plan that's on the table. I mean,
18 because that is the end game to get a better distribution to
19 unsecured creditors of the parties in interest.

20 One of the things we could not agree upon is the
21 challenge period and the automatic standing of the committee,
22 and that could be found in paragraph 28 of the proposed DIP
23 order. Suffice it to say, I expect the cooperation of both the
24 debtors, as well as the DIP lenders in allowing us to fulfill
25 our fiduciary duties to investigate the things that, I would

1 call, a lot of noise in the background so far as we embark on
2 this case, that a lot of people have raised issues, we're going
3 to look at that. We expect the DIP lenders, as well as the
4 pre-petition lenders and the debtors to cooperate with us.

5 We anticipate because we did not get automatic
6 standing in the DIP order to be filing a 2004 motion very
7 shortly, to be able to conclude the investigation on the
8 timeline that really the DIP lenders has set forth. We have a
9 sixty-day period in accordance with the local rule to conduct
10 the investigation. We anticipate doing it as fast as we can,
11 and if we do not get an extension consensually, come back
12 before Your Honor to talk about that issue.

13 With that said, Your Honor, I'm more than happy to
14 answer any questions of you or any party-in-interest concerning
15 these DIP negotiations.

16 THE COURT: Does anybody else want to be heard?

17 There's no response.

18 MR. SOSLAND: Your Honor, if the Lyme -- if the
19 statement of the committee counsel does not satisfy the Lyme
20 Regis objection, then if they wish to cross-examine either Mr.
21 Augustine (ph) or Mr. Stegenga, who are the -- presented
22 testimony in connection with the presentation on the interim
23 order, both Mr. Augustine and Mr. Stegenga are in the courtroom
24 and we would make them available for cross-examination.

25 THE COURT: Does Lyme Regis want to be heard?

1 MR. KAGAY: Your Honor, yes, Charles Kagay, I
2 represent the Lyme Regis Partners.

3 I'm not going to ask for any cross-examination of
4 those witnesses here today. I don't think that would really
5 add significantly to the record. I did want to express to the
6 Court the reason for our concerns, and I'm happy to hear about
7 the changes that have been made, and today is the first I've
8 heard of them, and I've absorbed them as well as I could. I
9 think they're important.

10 But it seems to me it's still may be sort of a matter
11 of rearranging the deck chairs on the Titanic. As you've
12 probably seen from our papers, we consider this to be a very
13 important issue in this proceeding, because it seems to be very
14 much aimed at determining how it's going to be resolved at the
15 end. And that seems to be a pretty far sweep for a first day
16 motion.

17 We see it as complimentary to the motion to pay the
18 studios, because this proposal here that it's absolutely
19 necessary to pay the studios 125 million dollars right off the
20 bat for unsecured pre-petition claims, or excuse me, 118
21 million dollars to the studio, and at the same time, it's
22 absolutely essential for Blockbuster to have 125 million
23 dollars of liquidity to keep going. And it sort of sounds like
24 money going in one door and out the other.

25 The premise of the motion is that the DIP motion,

1 there's only one way to keep Blockbuster afloat, and that's for
2 this Court to bless a financial deal that is already worked out
3 in advance. The key provisions, as I understand them, are --
4 is that they're designed to deliver Blockbuster to the hands of
5 the secured lenders with nothing left over for the unsecured
6 creditors, particularly the noteholders.

7 THE COURT: Do you have anything particularly on the
8 merits other than a position statement with respect to your
9 constituency?

10 MR. KAGAY: On the merits, the essential point that we
11 want to make is it does not seem appropriate at this time to
12 release the secured lenders from any possible claims against
13 them, which is something that was just -- it was just buried in
14 this motion, that the -- the Court remarked at the previous
15 hearing that the nine pages of single-spaced type in the motion
16 that explained the essential parts of the deal were a form of
17 boilerplate. But that boilerplate never even mentioned that
18 these releases -- there's absolutely been no justification
19 given by any witness or by anybody else why there has to be
20 releases of all the secured lenders, in order to secure this
21 financing. And to decide in advance why that this Court is
22 no --

23 THE COURT: Do you have any alternative financing,
24 sir?

25 MR. KAGAY: I do not, no.

1 THE COURT: Thank you.

2 MR. KANOWITZ: May I be heard just briefly?

3 THE COURT: Sure.

4 MR. KANOWITZ: Your Honor, I don't believe there's any
5 release of the pre-petition lenders, and in fact, paragraph 28
6 addresses that exact situation, so that we could come before
7 Your Honor and get appropriate relief if necessary. The DIP
8 lenders clearly are getting releases for the new money put in.
9 It's different than the pre-petition lenders. That's my
10 understanding of how that language works.

11 THE COURT: Does anyone else want to be heard?

12 Well subsuming that the record of the prior hearing
13 within today's, I overrule the objections, and I will approve
14 the DIP proposal as modified.

15 MR. SOSLAND: Thank you, Your Honor.

16 THE COURT: I'll entertain an order if you have it. I
17 would like to say I approve the order, but I can't find the
18 signature page. If you have some stickies, next time use them.

19 I've approved the order.

20 MR. SOSLAND: Thank you.

21 THE COURT: Go ahead.

22 MR. SOSLAND: Your Honor, if I may, we'd like turn
23 next to the movie studios' motion, which is tab A in the
24 binder, the first item on our agenda letter.

25 Your Honor, there were two written --

1 THE COURT: If your associate has a disk, I would
2 appreciate that, too.

3 You're not going to get it back.

4 UNIDENTIFIED SPEAKER: I know.

5 THE COURT: Go ahead.

6 MR. SOSLAND: Your Honor, the studio motion which was
7 approved on an interim basis by the Court on September 27th has
8 received written opposition from Lyme Regis Partners, as well
9 as a response and request for modification from the official
10 committee of unsecured creditors.

11 With regard to the creditor committee papers, Your
12 Honor, I'm happy to report that based on discussions that have
13 been and will continue to be ongoing with the committee, that
14 we have no opposition to the -- from the committee to the
15 motion, Your Honor.

16 The motion, and with regard to that, as you will
17 recall, the motion basically deals with two groups of studios,
18 three of whom, Fox, Warner and Sony, benefit from the Canadian
19 lien agreement that was executed in March of 2010, and they
20 have a lien on all of the assets of our Canadian subsidiary.
21 And in exchange for that, they extended their trade credit
22 terms, and made other concessions and agreed to continue to do
23 so through the Chapter 11 case, if we would file a motion and
24 obtain Court approval to continue that arrangement, and that's
25 what we've asked to do.

1 With regard to the unsecured -- what we referred to as
2 the unsecured studios, those who do not benefit from the
3 Canadian lien agreement, Your Honor, what we -- the relief
4 we've requested in the motion is to pay pre-petition claims for
5 studios provided that the studios enter into a combination of
6 agreements to provide terms on credit to the debtors, shipping
7 throughout the -- through the during of the Chapter 11 case.
8 And the motion attached a form of agreement.

9 Under the DIP agreement, Your Honor, we have to -- if
10 there are material agreements we have to obtain the consent of
11 the DIP lenders to those accommodation agreements, and we've
12 agreed with the creditor's committee, which is one of the
13 requests in the creditor committee response that was filed,
14 that we work with a subcommittee of the creditors' committee to
15 -- that we have a dialogue with them, consultation rights with
16 them with regard to accommodation agreements that we enter into
17 during the course of the case.

18 At this point we've executed exactly one accommodation
19 agreement with the studio that does not benefit from the
20 Canadian lien, and that's been made available to both the
21 secured lenders and to the committee professionals.

22 Your Honor, we will continue to work with the
23 committee on these issues as we go forward, and when we've --
24 we have committed to do that.

25 With regard to the three secured studios, Your Honor,

1 the three that benefit from the Canadian lien agreement, the
2 committee requested that -- because those agreement -- the
3 current supply agreements with those creditors expires on
4 December 31st of this year, that the studios agree that they
5 will extend those terms through the duration of the case, not
6 with a December 31st termination agreement -- date.

7 Your Honor, we're actually -- the debtors are in
8 discussions with the studios regarding not just extending those
9 terms, but actually improve terms that the debtors would like,
10 as we go forward, and as we think as we will emerge with a much
11 improved capital structure. But we do have a commitment from
12 at least one of the studios that it will continue its terms
13 through the duration of the case, from another that we actually
14 want more from than we currently have, they would be happy to
15 continue that relationship through the remainder of the case,
16 but the debtors are asking for some other concessions, and
17 we're in dialogue with the third studio.

18 We are keeping the creditors' committee in the loop on
19 all of that, Your Honor, and consulting with them as we go
20 forward, but we've committed to continue to do so. And I think
21 with those commitments, we've resolved the committee objections
22 or response, it wasn't styled an objection, but if Mr. Indyke
23 or Mr. Kanowitz would like to address it, I would call on them,
24 and then that would leave Lyme Regis again, Your Honor.

25 MR. KANOWITZ: Your Honor, Richard Kanowitz. May I be

1 heard?

2 THE COURT: Sure.

3 MR. KANOWITZ: Your Honor, the committee did file a
4 position paper on this motion. Essentially, we understand the
5 importance of the studios to this case. Under the motion, they
6 are getting benefits, and from our perspective, they should be
7 providing benefits to the estate. And I believe the debtor has
8 spent a significant amount of time, both management as well as
9 advisors with committee members and our financial advisors
10 explaining the business and explaining the importance. So
11 we've consented to the motion on conditions.

12 One of the conditions Mr. Sosland, you know, advised
13 the Court, which is to have committee participation in the
14 process. That these accommodation agreements don't just get
15 entered into, which have benefits to the studios, and not have
16 benefits back to the estate without the committee being aware
17 of these things. So there will be a subcommittee forum.

18 There is a studio member on the committee. That
19 member will be excluded from the subcommittee. So that the
20 committee will have real time information concerning these
21 important transactions that are going to be going on during the
22 course of this case.

23 The second is a condition for the studios, that it's
24 just not a one-way street, and we understand that the debtor's
25 business management is in active negotiations, and we're not

1 going to second-guess their business judgment, and they're
2 making supposedly progress, and we believe that the committee's
3 instrumental in making further progress, and we look forward to
4 working with the debtors, as well as the DIP lenders in this
5 regard.

6 So unless you have any questions.

7 THE COURT: I have none.

8 MR. KANOWITZ: Thank you.

9 THE COURT: Does anybody else want to be heard?

10 MR. KAGAY: Yes. Your Honor, Charles Kagay again for
11 Lyme Regis Partners.

12 Our concern all along with this is that there has not
13 been a showing that giving this money to the studios is going
14 to guarantee product. There hasn't been a showing that there
15 will be any assurance at all, and the fact that -- the way it
16 was structured and the papers presented to us, was that the
17 debtor will have complete freedom to pay the studios without
18 any guarantee at all on their part.

19 If you look at the form agreement that was connected
20 -- that was served with the papers, paragraph one was, the
21 money will be paid to the studios. Paragraph two was,
22 provision of product TBD. And essentially, the Court is being
23 asked to allow the debtors to write a blank check without any
24 showing that, in fact, the studios are going to give anymore
25 product. And the Court asked a question about this at the

1 previous hearing when the witness' proffer was given, and
2 asked, you know, where is the guarantee, we haven't seen it
3 here. And the further proffer was given, well, there was
4 another case, a movie studio's case that the -- where some of
5 the studios would not give product to the debtor even though
6 this type of order was entered.

7 That seems to me to suggest that there isn't any
8 guarantee. And that was our concern. There has just not been
9 a showing that the --

10 THE COURT: Thank you. I've read your papers.

11 MR. KAGAY: Okay. Thank you.

12 THE COURT: Anyone else want to be heard?

13 It's quite clear to me that -- some studios have a
14 very strong leverage position in these proceedings, which is
15 part of the justification that was offered previously and
16 continues to be offered. Others will get pre-petition
17 treatment on a quid pro quo basis, but more importantly, the
18 creditors' committee here, the unsecured creditors' committee
19 has undertaken a monitoring posture on -- with respect to all
20 of these ongoing supply agreements. I don't think that anybody
21 is in a position to extract guarantees from a party who is in a
22 bargaining and negotiating position, as all of you here are.

23 The motion is approved. The objection is overruled.

24 MR. KANOWITZ: Thank you, Your Honor.

25 MR. SOSLAND: I have a hard copy order.

1 THE COURT: I've approved the order.

2 MR. SOSLAND: Your Honor, that leaves for today three
3 retention applications. Ours, which is contested, by Lyme
4 Regis, and I believe that the issues of the UST to Rothschild
5 and -- have been resolved and that there are no objections
6 regarding the A&M retention. I don't know if anybody wants to
7 address either of those.

8 MR. KANOWITZ: For the record again, Richard Kanowitz,
9 proposed counsel for the committee.

10 Your Honor, we made slight modifications concerning
11 both retentions of A&M and Rothschild concerning what happens
12 in a liquidation relative to their completion fees or success
13 fees, if you will. They've made the appropriate changes in
14 language to indicate that going out of business liquidation-
15 type of sales, which do not involve sale of substantially all
16 of the company will not be counted towards their completion or
17 success via bonus fee, however -- however defined in those
18 engagement letters. So you'll see new language in the proposed
19 retention orders that addresses that. Thank you.

20 MR. MASUMOTO: Good morning, Your Honor. Brian
21 Masumoto for the office of the United States Trustee.

22 Your Honor, as Mr. Sosland indicated, our office did
23 reach an agreement with respect to the objections filed to the
24 Rothschild retention. For Your Honor's information, the
25 resolutions were that we've incorporated language with respect

1 to the attorney's fees to essentially defer the issue to the
2 time of fee application.

3 THE COURT: Why?

4 MR. MASUMOTO: Well, we're making it consistent with
5 the posture that we took with respect to A&M, but we've made it
6 clear that the issues regarding the permissibility of
7 attorney's fees will be determined at that time.

8 There were some concerns on the part of Rothschild
9 that in some cases where there are litigation costs that are
10 involved in connection with subpoenas and so forth, if all
11 attorney's fees were eliminated at the outset, would put them
12 at a disadvantage. However, they're aware of our position
13 regarding the impermissibility of attorney's fees related to
14 retention matters, and a fee application preparation and
15 review.

16 Accordingly, they've agreed to defer that issue for
17 the fee application period, and we are conforming, I guess, the
18 treatment between Rothschild with A&M, which has a similar
19 provision of deferring the issue.

20 THE COURT: In another case which has nothing to do
21 with this case?

22 MR. MASUMOTO: No.

23 THE COURT: I can only speculate what that case is.
24 It's probably Lehman; is that right?

25 MR. MASUMOTO: No, I'm sorry. Alvarez & Marsal is

1 retained as the chief restructuring officer under a 363, but
2 they -- there also is included in their order a provision since
3 their fees are subject to a 330, 331 review regarding attorney
4 fees. In that instance it's a --

5 THE COURT: I have a problem with in advance. Let's
6 say the concept that a retaineo is entitled to compensation for
7 services that are rendered and by its own counsel on --
8 throughout Title 11 there are special carve-outs under the 502
9 and 3 that would deal with that, but I don't see that in here.
10 Do we also have to pay for their secretaries or other kinds of
11 ancillary costs of their doing business? As a matter of
12 principle, I don't see that this is appropriate, and I'm not
13 prepared to bless it in advance, nor do I want the contineence
14 deferring it. Let's bite the bullet right up front. I don't
15 know under what circumstances they're ever going to come along
16 and say we want our attorney's fees paid. You're speculating.

17 MR. MASUMOTO: That's correct, Your Honor.

18 THE COURT: Maybe they have D&O insurance and we
19 should pay for the premiums on that. I don't know.

20 MR. MASUMOTO: Well, Your Honor --

21 THE COURT: But you're asking me to give a green light
22 with your --

23 MR. MASUMOTO: No. We're --

24 THE COURT: Or you're asking me for an amber light and
25 I'm telling you this may be the time for the red light.

1 MR. HAHN: Your Honor, may I speak to this issue
2 because I don't think --

3 THE COURT: I've dealt with this issue over thirty
4 years and I've even dealt with it with Rothschild, and I can
5 think of the area and the incident maybe twenty-five years ago.
6 You didn't get it then and I don't know why it should be
7 creeping to get it now.

8 MR. HAHN: Your Honor, Richard Hahn of Debevoise &
9 Plimpton for Rothschild, Inc.

10 THE COURT: Who would be the beneficiary, I would take
11 it, if there's ever a request for your fees to be paid by the
12 estate.

13 MR. HAHN: Yes. Yes, that's quite true, Your Honor.
14 This is part of a broader expense provision which
15 is --

16 THE COURT: Well, why don't you put in an application
17 for retention?

18 MR. HAHN: Well, we are not representing the debtors,
19 we're representing Rothschild.

20 THE COURT: Well then why should I in advance bless
21 your efforts for your particular client?

22 MR. HAHN: Your Honor, this is not a blank check. The
23 provisions in the retention in the order would require these
24 fees, including the traditional back-up information be included
25 in Rothschild's retention -- excuse me, in Rothschild's fee

1 applications, and thus be subject to Your Honor's review.

2 They, as Mr. Masumoto said, preserve his rights to
3 object on any and all grounds for reasonableness to his
4 position that they are per se and permissible.

5 It's Rothschild's view that the -- under applicable
6 authority the test for the permissibility fees is a
7 reasonableness test, as it is with all compensation for
8 retained professionals, that it is best to make that judgment
9 at the time of the retention because --

10 THE COURT: If I ask you today to give me an
11 application as to what services you would be providing to the
12 estate through this secondary retention that you have with your
13 own particular client, what would you tell me?

14 MR. HAHN: Well, I can give you --

15 THE COURT: What services would you render to this
16 estate --

17 MR. HAHN: I can --

18 THE COURT: -- that's over and above and different
19 than the services you would render to your particular client,
20 what you do day in and day out, I assume?

21 MR. HAHN: Well, I understand that Your Honor --

22 THE COURT: And by the way, don't give me the
23 shibboleth that outside of bankruptcy you do get this kind of
24 agreement.

25 MR. HAHN: I was going to suggest, Your Honor, that

1 those fees may well typically include representation in
2 connection with retention and fee applications. I think we
3 understand Your Honor's position on that, and certainly
4 Rothschild will take that into account, if and when it comes
5 time to make application.

6 THE COURT: I have a gang of lawyers, why should I
7 increase the posse?

8 MR. HAHN: Well, frequently, Your Honor, when there's
9 litigation in cases, and Rothschild is, as it often is, subject
10 to discovery in deposition requests --

11 THE COURT: Should Rothschild file a petition, I would
12 gladly entertain your application to be their counsel. And I'd
13 bring a petition for bankruptcy under Chapter 11.

14 MR. HAHN: Well, unfortunately, Rothschild is not in
15 need of protection of the bankruptcy court at this point.

16 THE COURT: I hope not. And I assume not. Therefore,
17 they don't need your services.

18 MR. HAHN: Well, in the event that there's
19 discovery --

20 THE COURT: Nor do we.

21 MR. HAHN: -- requests, we are often asked by debtor's
22 counsel to assist Rothschild in responding to subpoenas because
23 of our greater familiarity with their personnel and systems,
24 and the resulting efficiency of using us, and their fees in
25 those circumstances --

1 THE COURT: You mean when you give an opinion letter
2 to Rothschild, there's a potential for this estate having to
3 pay for that?

4 MR. HAHN: In the years I've represented them in
5 connection with attendance I've never given an opinion letter
6 to them.

7 THE COURT: So why do we need this concept?

8 MR. HAHN: As I was suggesting, Your Honor, frequently
9 they do ask for our services in connection with discovery.
10 They are subject to subpoenas or deposition requests by other
11 parties in the case, in litigation in which the debtor is the
12 party, not Rothschild; the litigation of the DIPs, the plan
13 confirmation, valuation disputes, and we are asked by the
14 debtor to represent Rothschild in that connection. And those
15 services redound to the benefit of the estate, not Rothschild
16 specifically.

17 So in those cases, we would suggest that even given
18 Your Honor's view about more run of the mill expense requests,
19 reimbursement would be appropriate, and we'd like to retain the
20 ability to apply for expense reimbursement and allow Your Honor
21 and the U.S. Trustee to judge the reasonableness of those
22 requests in the specific circumstances.

23 THE COURT: Well, there's a provision in the Code for
24 you to be compensated to the extent that you add value and help
25 protect the estate. But to the extent that you're doing this

1 on behalf of your client and helping to protect your client, I
2 don't see why the estate should have to bear that cost.

3 MR. HAHN: Well, Your Honor, I think --

4 THE COURT: And with all deference to Mr. Masumoto who
5 was willing to wait to wage this battle when and if it comes
6 up, I don't know why I, in advance, have to bless this. If you
7 render services that are compensable under Title 11, I'd be
8 glad to consider that and award it if appropriate.

9 MR. HAHN: Your --

10 THE COURT: But not in advance.

11 MR. HAHN: The provision that we have in our retention
12 is a provision that's regularly approved in this district and
13 many others.

14 THE COURT: Well, you haven't convinced me, Counselor.

15 MR. HAHN: Well, sorry, Your Honor.

16 MR. MASUMOTO: Thank you, Your Honor.

17 I did also want to address the other issue that we
18 had, listed as part of the objection. We did have objections
19 related to indemnification and this context, the engagement
20 letters provided for indemnification for affiliates.

21 In the past, Your Honor, I mean, this is a fairly
22 stock language, but in the recent past, we've become aware
23 where financial advisors have, in fact, notwithstanding their
24 retention employed the services and/or resources of unretained
25 affiliates, and accordingly have raised concerns regarding

1 whether indemnification would be appropriate for unretained
2 entities.

3 The supplemental application filed by -- although our
4 concern still does remain, in this instance, the supplemental
5 applications by the Rothschild indicated that no services would
6 be performed by any other than the retained entity. And during
7 the course of our conversation because of an issue was raised
8 in terms of the uniform treatment, it was discovered that with
9 respect to Alvarez & Marsal that, in fact, there was a
10 possibility that perhaps services from an affiliate may have
11 been provided. It's not entirely clear. Some of it may have
12 been provided pre-petition, but my understanding with debtor's
13 counsel is that if, in fact, personnel from an entity other
14 than the Alvarez & Marsal entity retain had been provided post
15 petition, a supplementary disclosure would be paid.

16 So based upon the supplementary disclosures, we are
17 prepared to let the orders be entered as is.

18 THE COURT: Well, in that area, there's apparently
19 transparency now based on that provision. Does anyone else
20 want to be heard?

21 I'm not prepared to authorize the retention of
22 Rothschild with that particular provision in there at this
23 point.

24 MR. MASUMOTO: Very well. Thank you, Your Honor.

25 MR. SOSLAND: Could we have a short break on

1 Rothschild or however the Court wants to proceed? I just
2 wanted to see what we wanted to do with the form of order on
3 Rothschild. We have the form of order on Alvarez & Marsal.

4 THE COURT: Well, let's --

5 MR. SOSLAND: Or we can proceed with our --

6 THE COURT: Let's summarize, because the U.S. Trustee
7 has an objection. It was prepared to postpone the
8 implementation of that objection when, as and if there was a
9 request made, and the Court said that I'm not prepared to
10 address that in the future, I'm prepared to address that now,
11 and the answer is in the negative.

12 MR. SOSLAND: We can provide -- we can revise that
13 order accordingly, Your Honor, and then submit it.

14 THE COURT: Very well.

15 MR. SOSLAND: And -- but we do have the order on
16 Alvarez, though, Your Honor, if --

17 THE COURT: Benefit to the estate is something the
18 Court would consider if, and when, that is shown in connection
19 with a request for compensation by Rothschild's counsel.
20 Actually, it would be by Rothschild, not by the counsel.

21 Go ahead.

22 MR. SOSLAND: May I hand up the Alvarez order?

23 THE COURT: Yes.

24 MR. SOSLAND: I have the clean and a blackline against
25 the one submitted with the application.

1 THE COURT: I've approved the order.

2 MR. SOSLAND: Thank you, Your Honor.

3 With regard to the retention of our firm, Your Honor,
4 there is an objection by Lyme Regis on the basis that they
5 assert that we are not a disinterested party. They submit that
6 the disclosure in the form of the affidavit by my partner,
7 Stephen Karotkin is not adequate.

8 Your Honor, for the reasons in our responses -- that
9 we list in our responsive paper, we believe first of all that
10 our disclosures are complete and appropriate, and in accordance
11 with all applicable rules and statute, and we believe that the
12 firm is, in fact, disinterested and that our application should
13 be approved.

14 I'm prepared to answer any questions that the Court
15 has or respond to any arguments from Lyme Regis who is here.

16 THE COURT: Does anyone want to be heard?

17 MR. KAGAY: Yes, Your Honor. Charles Kagay again for
18 Lyme Regis.

19 As we stated in our papers, we think there is a
20 problem here, and it's not just because sometimes Weil has
21 represented some of the creditors here, but it seems to be a
22 very fundamental overlap in the functions. Because on the
23 first day of the bankruptcy, Weil has presented motions that
24 cause -- request preferential treatment for some of the
25 studios, particularly the secured studios, such as Sony. As

1 far as we can tell, they've represented about seven out of nine
2 major studios. Their clients include the -- some of the DIP
3 lenders that are subject to very important motion picture
4 again on the first day.

5 As to the completeness of their disclosures, it seems
6 that they've disclosed the representation of two of the DIP
7 lenders, and we spent some time on the internet in the last
8 twenty-four hours, and it appears to us they actually represent
9 three of the DIP lenders, another one called Stonehill
10 Associates we don't see in their disclosures, but we do see it
11 on their website as being representatives of a creditor in
12 another bankruptcy.

13 And we understand that they will try to do their best
14 to separate the different functions, but there seems to be a
15 conflict here because as an attorney for a client, you have to
16 represent that client's interest, and you have a fiduciary duty
17 to do so.

18 As an attorney for a debtor in a bankruptcy, you have
19 fiduciary duty to protect the estate for the benefit of all
20 creditors, and it's going to be very difficult in this
21 proceeding to go ahead if Weil is wearing so many different
22 hats. The Court will never be able to say for certain where
23 this interest lies. And for that reason, we think it is just
24 inappropriate for a firm with this many conflicts to become the
25 representative of the debtor in such a major bankruptcy. I

1 think that's really all I have to say about that.

2 THE COURT: Thank you. Anyone else want to be heard?
3 Do you want to respond? Do you want to be heard, Mr. Masumoto?

4 MR. MASUMOTO: I'll let debtors -- I'll respond to
5 debtor's counsel.

6 MR. SOSLAND: Your Honor, none of the relationships
7 that we have with our current clients that are fully disclosed
8 in Mr. Karotkin's affidavit have anything to do with
9 Blockbuster. Each representation is unrelated. The test is
10 not potential conflicts of interest but actual conflicts of
11 interest.

12 If there were -- if anything were to arise, which has
13 not yet in this case, conflicts counsel would be retained, Your
14 Honor. In addition, I don't know whether Stonehill's listed,
15 the debt holders in this case changed. Lyme Regis was not a
16 creditor of the case -- was a creditor of Blockbuster when we
17 commenced our representation in early 2010, because they just
18 bought their debt in June. As we become aware of additional
19 creditors, we will supplement, as we do in every case, Your
20 Honor.

21 We also represent -- in that very complete list of
22 conflicts of the firm, there are also subordinated debtholders.
23 People who are -- who have exactly the same position in this
24 case that Lyme Regis does.

25 But in this case, Your Honor, we have undivided

1 royalty and representation of Blockbuster. Blockbuster is our
2 -- and it's a non -- and its debtor affiliates are our client.
3 We represent them to the exclusion of all others in these
4 cases, and we will do so to the best of our abilities as I
5 would say we do in every case in which we appear before this or
6 any other court, Your Honor.

7 We do not believe that the objection is well taken and
8 we'd ask the Court to overrule it and approve our retention.

9 MR. MASUMOTO: Brian Masumoto for the office of the
10 United States Trustee.

11 Your Honor, based upon our review of the retention, we
12 did again note as mentioned the various representations of
13 creditors. However, as indicated by debtor's counsel, it was
14 disclosed that none of these matters related to the debtor's
15 affairs.

16 In addition, as Your Honor knows, we have somewhat of
17 a general test to determine whether or not the revenues
18 generated by a particular client might influence the decisions
19 of the debtor. And so we have perhaps a somewhat arbitrary,
20 but effectively a percentage threshold of revenue to determine.

21 Based upon those standards, the unrelated
22 representation and the relatively minor percentage of the
23 debtor's revenues would determine that any -- that there is no
24 actual conflict to be concerned at this point.

25 Should, as indicated, a conflict arise, I think -- I'm

1 sure debtor's counsel would be prepared to retain conflicts
2 counsel to deal with it. But at the present time, we do not
3 see and did not see any conflict matters that would require the
4 representation of conflicts counsel at this time.

5 THE COURT: Thank you. Upon these representations,
6 I'm going to overrule the objection. Clearly, there's no
7 current conflict and it's very dubious as to whether or not in
8 the future that there could be an actual conflict; however,
9 that is always possible, and in that possibility, the
10 interposition of conflicts counsel will be entertained by the
11 Court. I'll approve the application.

12 MR. SOSLAND: Thank you, Your Honor. I have the form
13 of order.

14 THE COURT: I've approved the order.

15 MR. SOSLAND: Thank you. I believe that concludes our
16 agenda for today, Your Honor.

17 THE COURT: Thank you all.

18 (Whereupon, the proceedings were concluded at 10:54 a.m.,
19 October 27, 2010.)

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I N D E X

RULINGS

	Page	Line
Debtors' Motion for Interim Order Requesting (I) Authority To Pay Certain Prepetition Claims Of Movie Studios and Game Providers And (II) Administrative Expense Priority Status for All Undisputed Obligations Arising Postpetition - approved	24	23
Debtors' Motion for Entry of an Order, on an Interim and Final Basis, (I) Authorizing the Debtors to Obtain Postpetition Superpriority Financing, (II) Authorizing Debtors' Use of Cash Collateral, (III) Granting Liens and Superpriority Claims to DIP Lenders, (IV) Providing Adequate Protection, and (V) Scheduling a Final Hearing - approved	18	14

1	1			
2	2			
3	3			
4	4			
5	5			
6	6			
7	7			
8	8			
9	9			
10	10			
11	11			
12	12			
13	13			
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17	17			
18	18			
19	19			
20	20			
21	21			
22	22			
23	23			
24	24			
25	25			

RULINGS

Page Line

Application to Employ, Weil,
 Gotshal & Manges LLP as Attorneys
 For Debtors - approved 39 11

Application to Employ Rothschild,
 Inc. as Financial Advisor and
 Investment Banker - denied 33 21

Application to Retain Alvarez &
 Marsal North America, LLC - approved 35 1

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C E R T I F I C A T I O N

I, Linda Ferrara, certify that the foregoing transcript is a true and accurate record of the proceedings.

Linda Ferrara
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Date: October 28, 2010