UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF FLORIDA
WEST PALM BEACH DIVISION
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In re:	CHAPTER 11
PALM BEACH FINANCE PARTNERS, L.P., PALM BEACH FINANCE II, L.P.,	Case No. 09-36379-PGH Case No. 09-36396-PGH (Jointly Administered)
Debtors. _____/	

PARTIAL JOINDER BY GEOFFREY VARGA, AS JOINT OFFICIAL LIQUIDATOR OF PALM BEACH OFFSHORE, LTD. AND PALM BEACH OFFSHORE II, LTD. TO LIQUIDATING TRUSTEE'S MOTION TO APPROVE DISTRIBUTION SCHEME PURSUANT TO 11 U.S.C. § 510(b) AND BANKRUPTCY RULE 9019

Geoffrey Varga, as Joint Official Liquidator ("JOL") of Palm Beach Offshore, Ltd. ("***PBO***") and Palm Beach Offshore II, Ltd. ("***PBO II***" together with PBO, the "***Offshore Funds***"), by and through undersigned counsel, files this partial joinder ("***Joinder***") to the *Liquidating Trustee's Motion to Approve Distribution Scheme Pursuant to 11 U.S.C. § 510(b) and Bankruptcy Rule 9019* ("***Motion***") and states as follows[1]:

On November 15, 2016, the Offshore Funds participated in a mediation ("***Mediation***") conducted by Harley E. Riedel ("***Mediator***") that addressed the impact of 11 U.S.C. § 510(b) on LP claims in the estates of PBFP and PBF II. The Offshore Funds participated in the Mediation in their capacity as creditors of PBF II, having claims superior in priority to any claims of limited partners ("***LPs***") of PBF II.

The Offshore Funds hold over $718 Million of allowed unsecured claims against the PBF II estate. Although the proposed distribution scheme does not affect the superior priority of the Offshore Funds claims, the Offshore Funds could, and but for the settlement for which the

[1] Capitalized terms used but not otherwise defined herein have the respective meanings given in confirmed PBF II Second Amended Joint Plan of Liquidation (the "Plan").

Liquidating Trustee seeks approval in the Motion, would assert an interest in all funds available for distribution as a result of their priority position; thus, the participation of the Offshore Funds and their agreement to the proposed distribution scheme and to fund the carve-out described in the Motion is greatly beneficial to the Estate. The Plan itself expressly provides that Class 3B Claims are subordinated to Class 2B Claims (and to Class 1B Claims as well). The issue of subordination of Class 1B Claims to Class 2B Claims was not determined by the Plan and will have to be litigated absent the proposed settlement described in the Motion.

The position of the Offshore Funds is that the Class 1B Claims are clearly and expressly subordinated to Class 2B Claims as a matter of contract and as a matter of law, and to the extent the Motion argues or suggests otherwise the Offshore Funds do not join in the Motion.

Contractual Subordination. The Offshore Funds were PBF II's lenders, through a series of unsecured "Funding Notes" issued by PBF II to the Offshore Funds. Principal and interest due on the Funding Notes give rise to the Class 2B Claims. As lenders, the Offshore Funds were promised a fixed rate of return and seniority over PBF II's limited partners. The distributions to limited partners (ie, both Class 1B and 3B Claims) are explicitly and unambiguously contractually subordinated to distributions to the Funding Notes pursuant to the PBF II limited partnership agreement. Among other provisions, Section 11.3 of the PBF II limited partnership agreement to which all Class 1B (and Class 3B) Claim holders are bound explicitly provides, with respect to distributions of proceeds upon liquidation, that liabilities owed to creditors of PBF II (ie, Class 2B Claims) – <u>specifically excluding liabilities for distributions of withdrawn amounts</u> – are to be paid first, ahead of any payments to partners in satisfaction for distributions of withdrawn amounts (ie, on account of Class 1B and Class 3B Claims). Pursuant to Section 510(a) of the Bankruptcy Code, such contractual subordination must be respected.

Subordination Pursuant to Section 510(b). The Class 1B (and Class 3B) Claims are also subject to subordination pursuant to Section 510(b) of the Bankruptcy Code. Limited partnership interests - such as those underlying Class 1B Claims – are "securities" under Section 101(49)(A)(xiii) of the Bankruptcy Code. Section 510(b) of the Bankruptcy Code provides, in relevant part, that "a claim arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, for damages arising from the purchase or sale of such a security … shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such a security …"

Section 510(b) "sweeps broadly". *In re Tristar Esperanza Properties*, 782 F.3d 492, 495 (9th Cir. 2015). The statute "extends beyond the securities fraud claims that the House of Representatives explicitly discussed in its report and reaches even ordinary breach of contract claims so long as there is a sufficient nexus between the claim and the purchase of securities." *Id.* (citations omitted). In *Tristar*, the 9th Circuit, held that Section 510(b) subordination also applies to a fixed, liquidated damages claim arising from the debtor's breach of an agreement to pay an LLC member the fair market value of her membership interest (analogous to a contractual obligation to pay redemption proceeds to redeeming limited partners/equity holders). The claimant's argument that her equity interest was converted to a debt as a result of such contractual obligation was rejected. The same result must apply to redeeming limited partners who now hold Class 1B (and Class 3B) Claims.

If 510(b) subordination applies to a liquidated breach of damages claim, which it does, it also applies, *a fortiori*, to a claim for recission in connection with the purchase or sale of a security. "The critical question for purposes of §510(b), then, is not whether the claim is debt or equity at the time of the petition, but rather whether the claim *arises from* the purchase or sale of

a security. The claim must be subordinated if there is a sufficient 'nexus or causal relationship between the claim and the purchase' or sale of securities." *Id. at p. 497* [citations omitted]. Thus, any argument that Class 1B Claims should be *pari passu* with Class 2B because of "fundamental fairness concerns" must fail. "Put simply, 'creditors stand ahead of the investors on the receiving line.'" *In re Geneva Steel Company, 281 F 3d 1173, 1179* (10th Cir. 2002) (*Citing In re Granite Partners, L.P., 208 B.R. 332* (Bankr. S.D.N.Y. 1997).[2]

Notwithstanding the Offshore Funds' belief that Class 1B (and Class 3B) are clearly and unambiguously subordinated to the Offshore Funds' Class 2B Claims and thus not entitled to any distribution until Class 2B Claims are paid in full, in order to avoid potentially protracted and costly litigation and the further delay of distributions to creditors, the Offshore Funds agree to the Liquidating Trustee's proposed distribution scheme resulting from the Mediation and join in the Motion to the extent it seeks approval of such distribution scheme.

WHEREFORE, the Offshore Funds, by and through their JOL, respectfully request that this Court enter an Order approving the proposed distribution scheme and granting such other relief this Court deems just and proper.

Respectfully submitted,

LEVINE KELLOGG LEHMAN SCHNEIDER + GROSSMAN LLP
Local Counsel for Geoffrey Varga as JOL
201 South Biscayne Boulevard, 22nd Floor
Miami, Florida 33131
Phone: 305.403.8788; Fax: 305.403.8789
Email: rjr@lklsg.com

By: **/s/ Robin J. Rubens**
ROBIN J. RUBENS
Florida Bar No. 959413

[2] There are numerous cases that confirm that securities based claims are subordinated by Section 510(b) and such conclusion is black letter law. In the interest of brevity and the nature of this Joinder, the Offshore Funds have limited the number of cites and discussion of applicable case law.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that the foregoing Joinder was served on January 11, 2017 via the Court's CM/ECF filing system to all recipients registered to receive notices of electronic filings generated by CM/ECF for this case.

By: **/s/ Robin J. Rubens**
Robin J. Rubens