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Judge Refuses Washington Mutual Bankruptcy Confirmation

For the second time, bank holding company Washington Mutual was refused a confirmation of their reorganization efforts by bankruptcy judge Mary Walrath in Delaware without first engaging in mediation with various creditor groups. Judge Walrath brought up several reasons for her decision that included claims by a committee of equity security holders that hedge funds supporting the plan had engaged in insider trading of WMI debt based on information they obtained during the bankruptcy.

As such, Judge Walrath ordered the various warring parties to resolve their differences through a mediator without letting the three year old bankruptcy case degenerate into a "litigation morass." The parties concerned are several creditor groups (including the committee of equity security holders), the hedge funds and Washington Mutual's committee of unsecured creditors.

In response, Washington Mutual filed a court filing this week in which it gave its assurance it would make several modifications such as the interest rate to be paid to creditors.

At the same time, the filing urged Judge Walrath to limit mediation only to the insider trading claims arguing that the insider trading claims were not directly related to confirmation of a reorganization plan but instead a matter under securities law.

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But after holding a hearing on the matter, Judge Walrath disagreed, saying, “There’s just way too many issues, and I’m not going to have another contested confirmation hearing without trying to have this mediation and resolve all the issues.” She further added that she felt the issues at hand were essentially confirmation issues and set an initial deadline of November 7 for the mediator to submit a report on whether a consensus has been between the parties.

But Judge Walrath agreed with attorneys for JPMorgan Chase and the Federal Deposit Insurance Corp. (FDIC) that they should not be required to participate in the mediation.

Three years ago, in what has become the largest bank failure in the US, the FDIC seized Washington Mutual’s Seattle-based flagship bank in 2008 and sold its assets to JPMorgan for \$1.9 billion. This triggered a slew of lawsuits between Washington Mutual, the FDIC and JPMorgan Chase. Washington Mutual’s reorganization plan is based on the proposed settlement of lawsuits.

Under the proposed settlement, the competing lawsuits would be dismissed and some \$10 billion in disputed assets would be distributed among Washington Mutual, JPMorgan and the FDIC.

Although Judge Walrath has ruled that Washington Mutual’s proposed settlement was reasonable, she has thus far refused to confirm the reorganization plan for other reasons. This has already happened twice, once in January and again last month.