UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

In re:	§	**Chapter 11**
	§	
SPECTRUM JUNGLE LABS CORPORATION, *ET AL.*	§	**Case No. 09-50455 (RBK)**
	§	
	§	
Debtors.	§	**Jointly Administered**

SENIOR SECURED LENDERS' OBJECTION TO FIRST PROPOSED DISCLOSURE STATEMENT WITH RESPECT TO JOINT PLAN OF REORGANIZATION OF SPECTRUM JUNGLE LABS CORPORATION, ET AL., DEBTORS

COMES NOW Goldman Sachs Credit Partners, L.P., as Administrative Agent at the direction of and on behalf of the Senior Secured Lenders (the "Agent"), and files this Objection to the First Proposed Disclosure Statement (the "Disclosure Statement") with Respect to the Joint Plan of Reorganization of Spectrum Jungle Labs Corporation, et al., Debtors[1] (the "Plan"), and in support thereof respectfully states as follows:

INTRODUCTION

1. The proposed Plan described in the Disclosure Statement represents nothing more than a naked, flawed endeavor by three hedge funds, acting in concert, to leverage their subordinated, unsecured claim positions into a bankruptcy takeover of the Debtors. The Plan purports to engineer that takeover by "reinstating" approximately $1.4 billion of structurally senior debt owed to the Senior Secured Lenders, who are the creditor constituency with the largest economic stake in the Debtors, and who have the most to lose if the Plan were to be confirmed and thereafter fail.

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[1] The Debtors are: Spectrum Jungle Labs Corp., Spectrum Brands, Inc., ROVCAL, Inc., ROV Holding, Inc., Tetra Holding (US), Inc., United Industries Corp., Schultz Co., Spectrum Neptune US Holdco Corp., United Pet Group, Inc., DB Online, LLC, Aquaria, Inc., Perfecto Manufacturing, Inc., Aquarium Systems, Inc., and Southern California Foam, Inc.

2. The proposed Plan does not leave the Senior Secured Lenders' rights unimpaired, nor does it "reinstate" their loans without alteration, as is legally required for confirmation of the Plan. Instead, the proposed Plan creates new, incurable, non-monetary Events of Default under the Senior Secured Lenders' Credit Agreement, preventing reinstatement under Section 1124 as a matter of law. Moreover, for the proposed Plan to be remotely feasible under Section 1129(a)(11), the Debtors would be required to "restate" and materially alter many of the financial representations set forth in multiple historical Compliance Certificates previously furnished to the Senior Secured Lenders -- all of which were attested to through certifications of truth and accuracy by the Debtors' senior officers. Not only that, but to make their Plan numbers appear to work, the Debtors must also contradict and disclaim their own public statements and sworn testimony by their Chief Executive Officer before this Court just weeks ago. In short, as shown in detail below, the Disclosure Statement describes a Plan that is patently unconfirmable and destined to fail, and approval of the Disclosure Statement should therefore be denied.

JURISDICTION

3. This Court has jurisdiction pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding under 28 U.S.C. § 157(b). Venue is proper under 28 U.S.C. §§ 1408 and 1409.

BACKGROUND

4. On February 3, 2009, the Debtors filed their voluntary petitions for relief under chapter 11. Since that time, the Debtors have continued to operate their businesses and manage their properties as debtors-in-possession pursuant to 11 U.S.C. §§ 1107(a) and 1108.

5. The Debtors owe the Senior Secured Lenders approximately $1.4 billion under a Credit Agreement dated as of March 30, 2007 (the "Credit Agreement"), secured by a first priority lien on all of the Debtors' domestic assets (other than domestic accounts receivable and

inventory) and 65 percent of the equity interests of the Debtors' first tier foreign subsidiaries, and a second priority lien on all domestic accounts receivable and inventory.

6. Subordinate to the claims of the Senior Secured Lenders are approximately $1.09 billion of unsecured claims of certain noteholders (the "Noteholders") under (i) the 8 1/2% Senior Subordinated Notes due 2013, (ii) the 7 3/8% Senior Subordinated Notes due 2015, and (iii) the Variable Rate Toggle Senior Subordinated Notes due 2015.

7. On February 3, 2009, together with their chapter 11 petitions, the Debtors filed their Disclosure Statement [Docket No. 25] and their Plan [Docket No. 26].

8. The Plan was proposed subject to a pre-petition "lock-up" agreement with the hedge funds that are the three largest Noteholders -- affiliates of Harbinger Capital Partners, Avenue Capital Group, and D.E. Shaw & Co. (collectively, the "Noteholder Group") -- and that collectively hold approximately 70 percent of the unsecured Noteholder claims. The Plan provides for the repayment of the Noteholder claims through issuance to the Noteholders of (i) substantially all of the new equity in the reorganized Debtors (subject only to a holdback for the Debtor's management), plus (ii) new notes representing 20 percent of the face amount of the Noteholders' prepetition claims. Thus, under the terms of the proposed Plan, the Noteholder Group would take over majority equity ownership of the Debtors through a change of control.

9. The Plan proposes to reinstate the approximately $1.4 billion of senior secured debt owed to the Senior Secured Lenders. Plan § 3.2(c). The Disclosure Statement reflects the Debtors' intention to reinstate the Senior Secured Lenders' loans by paying to the Senior Secured Lenders "principal, non-default interest, fees, expenses, costs, charges or other amounts due and payable" prior to the effective date of the proposed Plan. Disclosure Statement at 30. The

Debtors contend that, with this treatment, the Senior Secured Lenders will be unimpaired and therefore are not entitled to vote on the Plan.

OBJECTION

THE COURT SHOULD NOT APPROVE THE DISCLOSURE STATEMENT BECAUSE THE PLAN IS UNCONFIRMABLE

10. The Disclosure Statement should not be approved because it describes a Plan that is unconfirmable on its face. The Debtors should not engage in a wasteful exercise of distributing a futile Disclosure Statement to creditors and soliciting votes for a Plan that has no hope of success. *See In re Atlanta West VI*, 91 B.R. 620, 622 (Bankr. N.D. Ga. 1988) (denying approval of disclosure statement describing unconfirmable plan "to avoid . . . a wasteful and fruitless exercise" that would "further delay a debtor's attempts to reorganize").

11. The Senior Secured Lenders are mindful of the distinction between issues that are appropriately addressed at the disclosure statement hearing and those more typically reserved for consideration at confirmation. However, it is well established that courts may consider substantive plan issues at the disclosure statement hearing and deny approval to disclosure statements predicated upon facially unconfirmable plans. *See, e.g.*, *id.*; *In re Felicity Assocs., Inc.*, 197 B.R. 12, 14 (Bankr. D.R.I. 1996) ("It has become standard Chapter 11 practice that when an objection raises substantive plan issues that are normally addressed at confirmation, it is proper to consider and rule upon such issues prior to confirmation, where the proposed plan is arguably unconfirmable on its face.") (internal quotation omitted); *In re Market Square Inn, Inc.*, 163 B.R. 64, 68 (Bankr. W.D. Pa. 1994) ("Where it is clear that a plan of reorganization is not capable of confirmation, it is appropriate to refuse the approval of the disclosure statement."); *In re Dakota Rail, Inc.*, 104 B.R. 138, 145 (Bankr. D. Minn. 1989) (denying approval of "facially defective disclosure statement" describing infeasible plan); *In re S.E.T. Income Props., III*, 83

B.R. 791, 794 (Bankr. N.D. Okla. 1988) (denying approval of disclosure statement because "the disclosure statement . . . demonstrates that the debtor's proposed plan of reorganization is not feasible").

A. The Plan Cannot Be Confirmed Because It Is Not Feasible.

12. The Debtors' proposed Plan is patently unconfirmable because the Debtors cannot satisfy Section 1129(a)(11) of the Bankruptcy Code. That provision requires that "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan." 11 U.S.C. § 1129(a)(11). Section 1129(a)(11) requires that "courts scrutinize carefully the plan to determine whether it offers a reasonable prospect of success and is workable." *In re Beyond.com Corp.*, 289 B.R. 138, 145 (Bankr. N.D. Cal. 2003). The Debtors' proposed Plan in this case is not feasible for two principal reasons, each of which is independently fatal to confirmation.

13. ***First***, the proposed Plan is not feasible because the Debtors will lack sufficient cash to exit bankruptcy at consummation. *See In re M&S Assocs., Ltd.*, 138 B.R. 845, 848-52 (Bankr. W.D. Tex. 1992) (King, J.); *see also In re Save Our Springs (S.O.S.) Alliance, Inc.*, 388 B.R. 202, 239-44 (Bankr. W.D. Tex. 2008). While the Disclosure Statement projects that the Debtors will have sufficient liquidity at exit to meet their required cash uses, the Debtors' most recently filed cash flow forecast shows liquidity of only $3.1 million at May 8, 2009 (after giving effect to the $235 million cumulative cap on the Debtors' revolver and DIP loan, taken together, pursuant to the Credit Agreement). The Debtors will be not able to generate sufficient liquidity in the seven weeks between May 8 and their expected emergence to satisfy all of the costs associated with a successful exit (currently estimated in the Disclosure Statement to be in excess of $80 million).

14. In addition, the Debtors' projection of the cash costs of exiting bankruptcy (as set forth in the Disclosure Statement) fails to account for a number of significant additional cash costs that they will have to pay in order to exit bankruptcy. Among other things, the Debtors' projections do not account for the payment of: (i) tens of millions of dollars in estimated incremental professional fee costs; and (ii) approximately $11 million of default rate interest to the Senior Secured Lenders. When these additional Plan funding requirements are included, the Debtors' own projections show that if the Plan were confirmed, the Debtors will lack sufficient cash to consummate it. Moreover, the Debtors claim that the timing of their projected exit in June 2009 will come on the heels of a seasonal low-point in their cash position and that their cash flow will improve quickly thereafter. However, the Debtors have offered no evidence that a sudden rapid cash inflow will be forthcoming.

15. Moreover, for their Plan to be feasible at consummation, the Debtors must "roll over" or refinance their existing revolving credit facility in today's extremely tight credit environment. The Debtors appear to have no commitment from Wachovia Bank (the lead bank for their existing revolving lender group) nor from any other lender to provide the credit they will require to exit bankruptcy. The Plan therefore places "a substantial burden of the debtor's risk of failure on the secured creditor"; the Debtors should not be permitted to "gamble, with [the Senior Secured Lenders'] money, on the . . . possibility of a drastic improvement in the . . . market." *In re M & S Assoc.*, 138 B.R. at 850, 852.

16. For each of these reasons, the projections in the Disclosure Statement are inadequate, incomplete, stale, and misleading. The Debtors should be required to disclose the most up-to-date internal projections available, including a disclosure of their "sources and uses," in the Disclosure Statement, and to demonstrate that the Plan will be feasible based upon an

inclusive comparison of all expected exit funding obligations and availability at consummation. *See, e.g.*, *In re J.D. Mfg., Inc.*, 2008 WL 4533690, at *2 (Bankr. S.D. Tex. Oct. 2, 2008) (denying motion to approve disclosure statement containing "outdated" information). The Disclosure Statement should also be amended to explain how the Debtors intend to address each of the substantial obstacles to feasibility of the proposed Plan identified above.[2]

17. ***Second***, the Debtors' own future financial projections show that the Plan is not feasible because the Debtors will not be able to maintain covenant compliance under the Credit Agreement in future test periods. Section 7.11 of the Credit Agreement requires the Debtors to comply with a Senior Secured Leverage Ratio test, or else trigger an Event of Default under Section 8.01(b). The Debtors will breach this covenant shortly after consummation, thus rendering the plan infeasible for at least the following reasons:

a. The Debtors' projections contemplate that they will be able to stay within their contractually-mandated debt levels with only approximately a 12 percent cushion in the fourth quarter of 2009. Discovery will show that this cushion will only deteriorate in the first and second quarters of 2010. But even the slim covenant compliance cushion in 2009 is based on faulty assumptions that, when corrected, demonstrate that the Debtors will be in default of the Senior Secured Leverage Ratio covenant as soon as the fourth quarter of 2009. For example, based upon the quarterly Compliance Certificates that the Debtors have furnished to the Senior Secured Lenders -- the truth and accuracy of which has been repeatedly attested to by the Debtors' Treasurer, Mr. John Beattie -- as of December 2008, the Debtors had used up approximately $47.4 million of the $50 million basket of Restructuring Charges (as defined in

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[2] As with all of the confirmation-related issues, the Senior Secured Lenders will be exploring these matters in detail through the ongoing expedited discovery, and reserve all of their rights regarding the facts developed through discovery.

the Credit Agreement) and other cash charges permitted to be added back to Consolidated EBITDA for the purpose of calculating compliance with the Senior Secured Leverage Ratio (the "Permitted Basket Amount"). When the substantial additional expenses of these chapter 11 cases and other restructuring charges -- estimated by the Debtors to include at least $30 million in bankruptcy-related fees (a target the Senior Secured Lenders believe is significantly understated) -- plus another $21 million in other restructuring charges are deducted from the Debtors' last twelve months' Consolidated EBITDA for the fourth quarter of 2009, the Debtors will be in default of their Senior Secured Leverage Ratio covenant by a substantial margin.

b. In addition, the Debtors' projections assume that they are permitted to "add back" to Consolidated EBITDA (which is used in calculating the Senior Secured Leverage Ratio) tens of millions of dollars of historical losses and restructuring costs attributable to their wound-down Growing Media business. But the definition of Consolidated EBITDA in Section 1.01 of the Credit Agreement only permits the Debtors to add back losses with respect to businesses that were the subject of "Specified Dispositions." The Debtors have admitted that they shut down and liquidated the Growing Media business because they could ***not*** sell or otherwise dispose of it. For example, in announcing their fourth quarter 2008 financial results, the Debtors proclaimed that their Board had approved "*the shut down*" of the Growing Media business "only after attempts by the [Debtors] to sell this segment, in whole or in part, were unsuccessful." *See* "Spectrum Brands Reports Fourth Quarter 2008 Financial Results," Ex. 99.1 to Spectrum Brands, Inc. Form 8-K, filed Nov. 12, 2008 (annexed hereto as Exhibit A) (emphasis added). Likewise, at the March 4, 2009 hearing before this Court in these cases, Mr. Kent Hussey, the Debtors' Chief Executive Officer, repeatedly testified under oath that the Growing Media business was the subject of an orderly *shutdown*, and not a sale or other disposition. *See, e.g.*, 3/4/09 Hearing Tr. (annexed hereto as Exhibit B) at 12:4-6 ("We tried to sell it, were unable to sell it, and shut -- announced a shutdown of the business in early October of last year."); *id.* 13:6 ("orderly shutdown"); *id.* 13:23 ("close the business down"); *id.* 14:12 ("liquidation"); *id.* 23:24-24:2 (The Court: "[The Growing Media business is] being shut down . . . there's no sale?" Mr. Hussey: "Yeah. . . . We've actually closed virtually all of the facilities now."). Proper treatment of these losses alone will result in significant reductions to the Debtors' Consolidated EBITDA, making future covenant compliance impossible.

c. Finally, in calculating Consolidated EBITDA, the Debtors are not permitted to create more room in the Permitted Basket Amount (which, as described above, is limited to $50 million) by improperly restating prior historical Compliance Certificates provided to and relied upon by the Senior Secured Lenders. Specifically, the Debtors are not permitted to "reclassify" certain costs relating to the shutdown of the Growing Media business by taking them out of the Permitted Basket Amount and adding them back to the Specified Disposition basket instead. Having submitted numerous Compliance Certificates to the Senior Secured Lenders, and having told the Court that the Growing Media business was shut down rather than sold, the Debtors cannot now materially alter their historical Compliance Certificates to make their Plan appear to work. The Debtors attested that their Compliance Certificates under the Credit Agreement were true and accurate, and the Senior Secured Lenders have relied on them, in some cases for more than a year. Any *ex post* revisions of these Compliance Certificates would constitute an admission by the Debtors of the existence of multiple pre-petition Events of Default that could not be cured, which would in turn create additional bars to reinstatement of the Senior Secured Lenders' debt under the Credit Agreement.[3]

B. Reinstatement Is Prohibited Because the Plan Would Create Additional Events of Default Under the Credit Agreement, and in Any Event Does Not Propose Payment of Default Interest as the Credit Agreement Requires.

18. Section 1124(2) of the Bankruptcy Code requires, as a condition to reinstatement of the Senior Secured Lenders' loans, that the Debtors cure all Events of Default that are neither *ipso facto* nor "financial condition" defaults. As the legislative history makes clear, "reinstatement consists of curing any default (other than a default under an *ipso facto* or bankruptcy clause)." H.R. Rep. No. 95-595, at 408 (1977). In this case, confirmation of the proposed Plan would cause at least two independent Events of Default to occur under the Credit Agreement. Neither of these Events of Default can be excused as an *ipso facto* or financial condition default, and thus the Debtors cannot satisfy the requirements for reinstatement of the Senior Secured Lenders' loans. *See In re M & S Assoc.*, 138 B.R. at 853-54 (denying reinstatement of secured lender's loans based on failure to cure all required defaults).[4]

19. ***First*****,** confirmation of the Plan would result in a "Change of Control" that would cause an immediate Event of Default under of the Credit Agreement. Section 8.01(k) of the Credit Agreement provides that the occurrence of a Change of Control constitutes an Event of Default. A "Change of Control," as defined in Section 1.01 of the Credit Agreement, occurs

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[3] Section 8.01(d) of the Credit Agreement provides that it is an immediate Event of Default under the Credit Agreement if any "certification or statement of fact made . . . by or on behalf of the [Debtors] . . . in any document required to be delivered in connection [with the Credit Agreement] shall be incorrect or misleading in any material respect when made. . . ." Were the Debtors to declare now that their historical Compliance Certificates were inaccurate or incorrect, each such inaccuracy would constitute an additional, incurable prepetition Event of Default that would prevent reinstatement of the Senior Secured Lenders' loans.

[4] For the same reason that these Events of Default preclude reinstatement, they also render the Plan infeasible under Section 1129(a)(11).

whenever a "group" (as defined in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934) becomes the "beneficial owner . . . directly or indirectly, of 40% or more of either the aggregate ordinary voting power or the aggregate equity value represented by the issued and outstanding Equity Interests of the Borrower." Here, pursuant to the lock-up agreement entered into by the Noteholder Group, if the Plan were confirmed, the Noteholder Group would become the beneficial owner of approximately 70 percent of both the equity value and the ordinary voting power of the Debtors -- causing an immediate Event of Default under Section 8.01(k) of the Credit Agreement. Under the Plan, the Debtors propose to cease to be a widely-held public company and transform into a privately-held entity with ownership and control vested in three hedge funds that are acting in concert (as evidenced by their lock-up agreement). This is exactly the kind of "takeover" that causes a Change of Control Event of Default under Section 8.01(k).

20. ***Second***, confirmation of the Plan would violate a negative covenant in the Credit Agreement that prohibits the Debtors from making distributions to the Noteholders in repayment of their subordinated debt, thus causing an immediate Event of Default under the Credit Agreement. Section 8.01(b) of the Credit Agreement provides that an Event of Default will occur if the Borrower fails to perform or observe any covenant in Article VII (negative covenants) of the Credit Agreement. Section 7.15 in turn provides, among other things, that the Debtors "shall not . . . [p]ay or make, or agree to pay or make, directly or indirectly, any payment or other distribution (whether in cash, securities or other property) . . . on account of the purchase, redemption, retirement, acquisition, cancellation or termination of any subordinated Indebtedness," with certain limited inapplicable exceptions. Of course, the Plan contemplates just such a prohibited distribution of new equity securities to the Noteholders on account of their subordinated debt. In a June 2008 presentation made to the Senior Secured Lenders, the Debtors

expressly recognized this covenant restriction, and sought a waiver of it, in the context of a proposed transaction involving an exchange of Notes held by Harbinger (a member of the Noteholder Group) for equity interests in the Debtors' Global Pet business. In the Debtors' own words: "Each of the credit agreements prohibits the retirement of junior indebtedness before the senior secured facility is retired in full." Consummation of the Plan would constitute a prohibited distribution on account of subordinated debt, and hence create an immediate Event of Default under Sections 7.15 and 8.01(b) of the Credit Agreement.

21. ***Finally***, the proposed Plan cannot be confirmed because it fails to provide for a complete cure and reinstatement of the Debtors' obligations under the Credit Agreement. The Plan fails to provide for the contractually required payment of default rate interest to the Senior Secured Lenders during the pendency of these chapter 11 cases. In the Compliance Certificate that the Debtors furnished to the Agent on February 11, 2009 (annexed hereto as Exhibit C), the Debtors conceded that Events of Default occurred under each of Sections 8.01(a), (f), and (g) of the Credit Agreement as of February 3, 2009, and that an additional Event of Default occurred thereafter under Section 8.01(e) of the Credit Agreement.

22. Notwithstanding the Debtors' admission that such Events of Default have occurred, the Plan proposes the payment only of "principal, *non-default interest*, fees, expenses, costs charges or other amounts due and payable" prior to the Effective Date. Plan § 3.2(c) (emphasis added). Fifth Circuit authority recognizes, however, that an oversecured creditor is presumptively entitled to the payment of its default rate interest as a condition to reinstatement. *See In re Southland Corp.*, 160 F.3d 1054, 1059-60 (5th Cir. 1998); *In re Laymon*, 958 F.2d 72, 75 (5th Cir. 1992); *see also* 11 U.S.C. § 506(b) (oversecured creditor entitled to "interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement or State

statute under which such claim arose"). Payment of default rate interest is also mandated by the 1994 amendment of Section 1123(d) of the Bankruptcy Code, which provides that "the amount necessary to cure the default shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law." 11 U.S.C. § 1123(d); *see also In re Southland*, 160 F.3d at 1059 n.6. Reinstatement therefore would require the Debtors to pay the Senior Secured Lenders interest at the default rate of interest. Reinstatement "does not . . . allow a debtor to avoid all consequences of its default, including, when its contract with a creditor so provides, liability for interest at the default rate." *See* BANKRUPTCY LITIGATION MANUAL (Michael L. Cook ed., 2008-2009). Because the Plan fails to provide for the payment of default rate interest to the Senior Secured Lenders, the Plan cannot be confirmed.

RESERVATION OF RIGHTS

23. Discovery on the foregoing issues with respect to approval of the Disclosure Statement and the contested Plan confirmation litigation are only just beginning. The Senior Secured Lenders and the Agent expressly reserve all rights to object to confirmation of the Plan, to any modification of the Disclosure Statement, and to any amended disclosure statement or modification of any subsequent plan, on any and all grounds, whether or not set forth herein.

WHEREFORE, the Senior Secured Lenders and the Agent respectively request that the Court deny approval of the Disclosure Statement and grant them such other and further relief as is just and proper.

Dated: March 31, 2009

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CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the foregoing was served by United States first class mail, postage prepaid, and via facsimile, in accordance with the Federal Rules of Bankruptcy Procedure, to the attached service list, on this 31st day of March, 2009.

/s/ Eric B. Terry
Eric B. Terry