
ARTICLES

S.D.N.Y. Bankruptcy Court Provides Guidance on Fixture Classification and Valuation

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In an incredibly detailed and lengthy 205-page post-trial ruling, Judge Martin Glenn of the Southern District of New York Bankruptcy Court delved into the weeds of a dispute between the Avoidance Action Trust (the “Trust”)—a body serving on behalf of Old GM’s unsecured creditors—and certain secured term lenders of Old GM in *Motors Liquidation Co. Avoidance Action Trust v. JPMorgan Chase Bank, N.A. (In re Motors Liquidation Co.)*, No. 09-50026, 2017 WL 4280934 (Bankr. S.D.N.Y. Sept. 26, 2017). The defendant term lenders initially held a security interest in approximately \$1.5 billion of Old GM’s assets, with a perfected security interest originating from a UCC-1 financing statement filed in Delaware. *Id.* at *3. In an earlier stage of the litigation, the perfected security interest was terminated when a UCC-3 termination statement was mistakenly filed. *Id.* Despite the termination statement, the term lenders argued that at the time of the historic section 363 sale of GM’s assets in 2009, they held a perfected security interest in over 200,000 fixtures at various GM plants because of 26 fixture filings in counties where the disputed assets were located. *Id.*

In the dispute before Judge Glenn, the parties argued about two overarching issues: (1) whether the assets were fixtures or realty; and (2) how to value the assets. *Id.* Because it was impractical to litigate fixture and valuation issues for each and every one of the 200,000 assets, in pretrial proceedings the court directed the parties to designate 40 sample “representative” assets to be subject to a trial. *Id.* at *4. The representative assets included metal presses, conveyor systems, machining systems, robots, furnaces, and paint shop assets, among other items, all of which were used in the auto manufacturing process. *In re Motors Liquidation Co.*, 2017 WL 4280934 at *16-38. The parties then agreed that after the court issued its opinion, they would attempt to settle as to the remaining disputed assets using the court’s guidance in its ruling. *Id.* at *4. The court received significant amounts of evidence at trial, including competing expert reports and opinions on various methods of valuation. *Id.* at *86. Further, as part of the trial, the court even conducted an on-site visit to two of the Old GM facilities in Michigan. *Id.* at *10.

In its ruling, after examining the factual background regarding the relevant GM plants and describing the representative assets, the court analyzed the relevant legal standards for fixtures under both Michigan and Ohio law – the two states at issue where the disputed assets were located. *Id.* at *39. Under Michigan state law, property is a fixture if: (1) it is annexed to the realty, whether the annexation is actual or constructive; (2) its adaptation or application to the realty being used is appropriate; and (3) there is an intention to make the property a permanent accession to the realty. *Id.* Ohio state law on fixtures has a similar three-part test for fixtures: (1) annexation to some extent to the realty; (2) application to the use or purpose to which the realty to which it is attached, is devoted; and (3) actual or apparent intention upon the part of the owner of the chattel in affixing it to the realty to make such chattel a permanent part of such realty. *Id.* at *41.

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After canvassing each state's law, the court distilled several guiding principles in fixture determinations, including the following: (1) "concrete pits, trenches, slabs, or specialized foundations are strong indications that an asset is a fixture"; and (2) "when a particular asset is closely integrated, assimilated, or interlocked with other assets, the notion that the asset was intended to remain in place is reinforced. On the other hand, where an asset stands apart from other assets and the assembly line processes generally, and has a lower level of integration and assimilation, there is less of an apparent intent for an asset to remain in place indefinitely." *In re Motors Liquidation Co.*, 2017 WL 4280934 at *50-52. In reaching its fixture determinations for the 40 representative assets, the court reached various results for each asset.

The court then determined the appropriate valuation method for the assets. *Id.* at *75-97. The primary dispute between the parties on valuation was whether the assets sold to New GM should be valued at liquidation value or going-concern value. *Id.* at *75. The Trust argued that because the U.S. Government paid an above-market price in the section 363 sale, the court should imagine that the section 363 sale never took place at all and value the representative assets as if Old GM had liquidated. *Id.* By contrast, the defendant term lenders argued that going-concern value was appropriate, and they urged the court to use RCNLD amounts² developed as an interim step by KPMG in a contemporaneous fresh start exercise.³ *Id.* The court agreed with the Trust that the above-market portion of the section 363 sale price should not be relied upon as an indicator of the value of the representative assets but would not value the Representative Assets under the assumption that Old GM would have liquidated—a hypothetical outcome that was never the intended disposition of the assets. *Id.* at *5. Instead, the court agreed with term lender defendants that going-concern value is appropriate for those assets that were sold to New GM, but it disagreed that the interim RCNLD amounts are the best measure of that value. *In re Motors Liquidation Co.*, 2017 WL 4280934 at *5. The court instead used KPMG's final valuation—which included a significant reduction for the earning power of the business upon emerging from bankruptcy in the midst of the Great Recession—as the best available evidence of the value of the fixtures sold to New GM. *Id.* For the two representative assets that were intended to remain with the Old GM estate and never to continue operating, the court found that OLVIE was the appropriate premise for the value of those assets, in keeping with the principle that assets should be valued according to their proposed disposition on the valuation date and not based on a hypothetical outcome.⁴ *Id.*

This latest decision in the long-running GM bankruptcy saga provides helpful guidance to practitioners dealing with fixture and valuation issues. In addition, the unique procedure used by the court and the parties to set up a guidance ruling with certain sample assets from a much larger group of assets that had to be valued can serve as a model in future bankruptcy litigations where individualized determinations are not feasible in liquidations of large manufacturing companies. Although the Trust has sought leave to appeal the court's decision to use the selected valuation method, the court's ruling will most likely lead to future settlements for the remaining assets, which will save the parties and the court much time and expense in bringing the dispute to its conclusion.

² "RCNLD" stands for "Replacement Cost New Less Depreciation." *Motors Liquidation Co. Avoidance Action Trust v. JPMorgan Chase Bank, N.A. (In re Motors Liquidation Co.)*, No. 09-50026 (MG), 2017 WL 4280934 at *18 (Bankr. S.D.N.Y. Sept. 26, 2017).

³ KPMG was retained by New GM in 2009 following the closing of the section 363 sale to provide an opinion regarding the fair value of certain assets acquired by New GM, including hundreds of thousands of individual assets, as well as 33 of the representative assets. *Id.* at *5.

⁴ "OLVIE" stands for "Orderly Liquidation Value in Exchange." *Id.* at *87.