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Attorneys for the California Plaintiff Studios

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF UTAH, CENTRAL DIVISION**

In re:

VIDANGEL, INC.,

Debtor.

Case No. 17-29073

Chapter 11

Judge Kevin R. Anderson

**THE CALIFORNIA PLAINTIFF STUDIOS' LIMITED OBJECTION TO THE
DEBTOR'S MOTION TO EMPLOY KAPLAN, VOEKLER, CUNNINGHAM & FRANK,
PLC AS SPECIAL COUNSEL**

Disney Enterprises, Inc., Lucasfilm Ltd. LLC, Twentieth Century Fox Film Corporation, Warner Bros. Entertainment Inc., MVL Film Finance LLC, New Line Productions, Inc. and Turner Entertainment Co. (collectively, the “California Plaintiff Studios”), all of whom are creditors in the above-entitled case holding substantial unliquidated claims, through counsel, respectfully submit this objection (the “Limited Objection”) to the *Application of VidAngel, Inc., as Debtor-in-Possession (the “Debtor”), for Entry of Order Authorizing Retention of Kaplan, Voekler, Cunningham & Frank, PLC (“KVCF”) as Special Counsel under Section 327(e) and 328(a) of the Bankruptcy Code [ECF No.158]* (the “Application”), and respectfully represent as follows:¹

Limited Objection

Through this Limited Objection, the California Plaintiff Studios seek clarification and additional disclosure regarding the nature of KVCF’s intended retention,² as well as changes to the proposed compensation structure. The California Plaintiff Studios do not seek to disqualify KVCF from serving as special counsel to the Debtor through this Limited Objection but do not

¹ For the avoidance of doubt, California Plaintiff Studios are not hereby consenting to jurisdiction over the claims asserted in the pending action in the District Court for the Central District of California (the “California Action”). As this Court knows, the California Plaintiff Studios previously appeared for the limited purpose of seeking dismissal of VidAngel’s Chapter 11 bankruptcy as filed in bad faith or, alternatively, asking the Court to lift the automatic stay so they could liquidate their claims in the California Action. The Court continued the motion until the Utah district court (Chief Judge Nuffer) ruled on a pending motion to dismiss, transfer or stay of VidAngel declaratory judgment action. Since then, VidAngel has attempted to leapfrog both Judge Nuffer and this Court’s decisions in an attempt to have the California Action heard in the Utah district court by filing an adversary complaint and seeking withdrawal of the reference of that complaint from this Court. The California Plaintiff Studios have opposed that motion to withdraw the reference, which is currently pending before the Utah district court as well.

² The Application states that “[t]he professional services that the Debtor may request KVCF to provide may include the following: Advising the Debtor on matters relating to the restructuring of the Debtor, including formation of a broker-dealer and transfer agent, and creation of agreements related to intended new business lines of the Debtor.” Because the nature of such services is not clear to the California Plaintiff Studios and appears wholly unrelated to the Debtor’s stated objectives in respect of its reorganization, the Debtor should at a minimum provide additional detail on the scope of KVCF’s engagement and the reasons for that scope.

agree that the current proposed compensation structure for KVCF should be approved.

Depending on the substance of the Debtor's responses, if so warranted, the California Plaintiff Studios respectfully reserve their rights to proceed otherwise in respect of the Application.

A. KVCF's Proposed Compensation Structure Creates an Interest Adverse to the Estate.

Section 327(e) of the Bankruptcy Code allows the Debtor to retain an attorney for "a specified special purpose . . . if in the best interest of the estate, and if such attorney does not represent or hold any interest adverse to the debtor or to the estate." Though not defined in the Bankruptcy Code, "adverse interest" has been interpreted to include "an economic interest that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute in which the estate is a rival claimant." *In re Greystone Holdings, L.L.C.*, 305 B.R. 456, 461 (Bankr. N.D. Ohio 2003); *see also In re Amdura Corp.*, 121 B.R. 862, 865 (Bankr. D. Colo. 1990) ("As a general principle, professional persons employed by the trustee should be free of any conflicting interest which might, in the view of the trustee or the bankruptcy court, affect the performance of their services or which might impair the high degree of impartiality and detached judgment expected of them during the administration of a case.").

The Application asks the Court to approve a compensation structure for KVCF that would pay KVCF, in addition to a fixed amount of \$100,000, "\$275,000 paid in non-statutory options for 203,706 shares of common stock from VidAngel's authorized option pool with the trigger price set at the lesser of \$3.00 or the current fair market price at the time of issuance, *issued pursuant to a filed Chapter 11 Plan of Reorganization and subject to the approval of the Bankruptcy Court.*" [Application at 4 (emphasis added)] The second part of the proposed compensation structure – options for 203,706 shares of common stock that would be issued

pursuant to a yet-to-be-filed plan (the “KVCF VidAngel Options”) – is impermissible for at least two reasons.

First, the proposed engagement seeks to compensate KVCF in the form of equity in the reorganized debtor when there is no plan on file (let alone confirmed), making it impossible for either the Court or the California Plaintiff Studios or other creditors and interested parties to determine the potential value of such options or to evaluate reasonableness. Moreover, such a grant would have the effect of predetermining at least one aspect of the Debtor’s post-confirmation capital structure—equity options issued to KVCF—outside of the plan confirmation process. Just last March the Supreme Court cautioned courts in the *Jevic* case to carefully scrutinize proposed transactions that “circumvent the Code’s procedural safeguards.” *See Czyzewski v. Jevic Holding Corp.*, ___ U.S. ___, 137 S.Ct. 973, 986 (March 22, 2017). The proposed engagement with KVCF appears to do exactly what the Supreme Court cautioned against.³

Second, the compensation structure gives KVCF an interest that is potentially adverse to the estate and other creditors in the valuation of any equity that would be issued pursuant to any plan of reorganization. Because KVCF will receive the majority of its compensation only in the event that the equity value of the Debtor increases beyond the “trigger price” of the KVCF

³ Although most commonly arising in the context of Section 363(b) sales outside of the plan process, courts have rejected attempts by debtors to dictate the terms of an ensuing plan or constrain parties from exercising their confirmation rights outside of a plan confirmation process. *See, e.g., The Sub Rosa Plan of Reorganization: Side-stepping Creditor Protections in Chapter 11*, 16 Bankr. Dev. J. 37 (1999); *In re Braniff Airways, Inc.*, 700 F.2d 935, 940 (5th Cir. 1983) (prohibiting an attempt to “short circuit the requirements of Chapter 11 for confirmation of a reorganization plan by establishing the terms of the plan *sub rosa* in connection with a sale of assets”); *In re Lionel Corp.*, 722 F.2d 1063, 1069 (2d Cir. 1983) (reversing bankruptcy court’s approval of an asset sale after holding that § 363 does not “gran[t] the bankruptcy judge *carte blanche*” or “swallo[w] up Chapter 11’s safeguards”); *In re Biolitec, Inc.*, 528 B.R. 261, 269 (Bankr. N.J. 2014) (rejecting a structured dismissal because it “seeks to alter parties’ rights without their consent and lacks many of the Code’s most important safeguards”).

VidAngel Options at the time when they are granted, KVCF would have an interest in the initial value of any post-confirmation equity being set artificially low to maximize the value of such options. Consequently, such a compensation structure would make KVCF an interested party in the terms of any potential reorganization plan that would create an interest adverse to the broader estate and to other claimants, including the California Plaintiff Studios, who would like the post-confirmation equity to be valued at a higher price.

B. It is Not Possible to Determine the Reasonableness of KVCF's Proposed Compensation.

Section 328(a) provides that a debtor “with the court’s approval, may employ or authorize the employment of a professional person . . . on any reasonable terms and conditions of employment.” However, as noted above, it is not possible to determine the value of the KVCF VidAngel Options and therefore their reasonableness in the absence of a plan of confirmation and an understanding of the post-reorganization capital structure. Additionally, the Debtor’s proposed order also states that “KVCF need not apply to the Court for allowance of its flat-fee compensation” (which encompasses the KVCF VidAngel Options). To put it differently, the Debtor seeks to pay KVCF with equity in the reorganized Debtor with a value that cannot be determined now without the Court’s oversight or review as well as the oversight and review of other interested parties, including interested creditors and the office of the United States Trustee. Such a compensation structure is not reasonable and thus is not permissible under Section 328(a).

WHEREFORE, for the foregoing reasons, the Court should deny the Debtor’s Application to employ KVCF on the terms set forth in the Application, and the Court should make such other and further rulings as are appropriate in light of the concerns set forth above.

DATED this 23rd day of March 2018.

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/s/ Michael R. Johnson

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CERTIFICATE OF SERVICE

I hereby certify that on March 23, 2018, I electronically filed the foregoing *The California Plaintiff Studios' Limited Objection To The Debtor's Motion To Employ Kaplan, Voekler, Cunningham & Frank, Plc As Special Counsel* with the Clerk of Court using the CM/ECF system, which sent notification of such filing to the electronic filing users in this case as follows:

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I further certify that on March 23, 2018, I served the foregoing *The California Plaintiff Studios' Limited Objection To The Debtor's Motion To Employ Kaplan, Voekler, Cunningham & Frank, Plc As Special Counsel* on the following via first class mail, postage prepaid:

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