

**RAMIFICATIONS OF AUTO INDUSTRY  
BANKRUPTCIES (PART III)**

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**HEARING**  
BEFORE THE  
SUBCOMMITTEE ON  
COMMERCIAL AND ADMINISTRATIVE LAW  
OF THE  
COMMITTEE ON THE JUDICIARY  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED ELEVENTH CONGRESS  
FIRST SESSION

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JULY 22, 2009  
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## RAMIFICATIONS OF AUTO INDUSTRY BANKRUPTCIES (PART III)

WEDNESDAY, JULY 22, 2009

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON COMMERCIAL  
AND ADMINISTRATIVE LAW,  
COMMITTEE ON THE JUDICIARY,  
*Washington, DC.*

The Subcommittee met, pursuant to notice, at 10:14 a.m., in room 2141, Rayburn House Office Building, the Honorable Steve Cohen (Chairman of the Subcommittee) presiding.

Present: Representatives Cohen, Conyers, Sherman, Maffei, Johnson, Scott, Franks, Jordan, Coble, Issa, and King.

Staff Present: (Majority) James Park, Counsel; Adam Russell, Professional Staff Member; and (Minority) Daniel Flores, Counsel.

Mr. COHEN. This hearing of the Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, will now come to order. Without objection, the Chair will be authorized to declare a recess of the hearing.

I will now recognize myself for a short statement.

We continue our hearings on the ramifications of auto industry bankruptcies and their effect on dealers and other issues. In my opening statement yesterday, I raised concerns about the impact of the Chrysler and General Motors bankruptcies on automobile dealers and tort claimants. We heard responses from Mr. Bloom and the Administration's auto task force on these and other issues. Today, we will have the perspectives of Chrysler and GM as well as other interested parties.

As was noted yesterday, one issue that has raised bipartisan concerns in Congress is the mass closure of GM and Chrysler dealerships. The car dealers contend that GM and Chrysler selected dealerships for termination using an arbitrary selection process. Additionally, I am concerned about the impact of these closures on minority dealers—and I may qualify that when I say “minority,” I don't necessarily mean women. I am speaking about it from my district African Americans, and those statistics may be different and I appreciate your referencing those; I feel they will suffer in a disproportionate manner.

Yesterday, I briefly spoke about Mr. John Roy, who was the only African American Chrysler dealer within a 300-mile radius of Memphis, his dealership being in South Haven. He was a dedicated and outstanding Chrysler dealer. Chrysler decided to terminate his franchise. There were business decisions that he had to engage in,

because of that, that affected his business and terminated it. I am very interested in what criteria were used to determine which dealers are allowed to remain in business and those which weren't, particularly minority dealers.

Another issue that the Subcommittee will explore is whether the use of section 363 sales in the Chrysler and GM cases threatens to undermine Chapter 11. The court in both cases approved the sale of a substantial number of assets by Chrysler and GM to newly created entities that were to become the "new" Chrysler and the "new" GM. Notwithstanding the court's approval of these sales, some critics have charged this sale constituted an end-run around the Bankruptcy Code's plan confirmation process and may have constituted improper sub-rosa reorganization plans. I hope that our witnesses can, and I am sure they will, shed some light on these issues and the use of this particular procedure.

I thank our witnesses for appearing today and for adding to our understanding of the implications of these historic bankruptcy cases which has affected business and culture in America in a great way.

I now recognize my colleague, Mr. Franks, the distinguished Ranking Member of the Subcommittee, for his opening remarks.

Mr. FRANKS. Thank you Mr. Chairman. Good morning to you.

And good morning to you folks. Due to the kind of—the nature of the hearing this morning, I hope you will grant me diplomatic immunity. I appreciate all of you for just having the courage to be here.

Mr. Chairman, many decades ago in a much younger country some remarkable things took place. The founding of General Motors and its repeated resurrection from hard times through the spirit of private American enterprise was one of them. It produced an industrial giant the likes of which the world had never seen. Walter P. Chrysler's salvation of the first Willys-Overland Company from bankruptcy, then the Maxwell-Chalmers Company, which he turned into Chrysler Corporation, was another. Walter P. Chrysler took companies from the ash heap and then he made Chrysler strong enough to take a sustained break from production and built the Sherman tank and the B-29 bomber engines that powered us to victory in World War II.

In America today, remarkable inspiring things still take place, but sadly, they are not taking place through the auto task force or the bankruptcies of General Motors and Chrysler. In the Chrysler bankruptcy, a once-proud company confronting a deadly credit crunch and falling sales, came to Washington for handouts and a few months' time. And I understand that. But it got a handout and a few months' time only. But in those few months, Chrysler shifted from being a privately owned company to being owned by the UAW, the U.S. Government, the Canadian Government and an Italian auto maker.

General Motors, confronting the same credit crunch and the same falling sales, came to Washington and got even more money and more time, but sure enough it became a company owned almost entirely by the UAW and the U.S. Government; and in the blink of an eye, American icons were turned into American tragedies. And I have got to ask the question, Why? Because their man-

agement, unlike their companies' founders, didn't rely on private enterprise and the time-tested American remedy for corporate failure, that being bankruptcy and reorganization. I know it is always easy to say that from outside the perspective, but I believe that the axiom holds true.

And because the Obama administration, the auto task force, saw a chance to take the limited bridge loans and the precious few months the Bush administration had granted to companies had extended them, they chose to turn those things into tools that to subject into penchant for political patronage—its radical climate and energy agenda and its broad plans to inject government deeper than we have ever seen into the bloodstream of the American economy.

I had many questions yesterday for the man responsible for this at the auto task force, that being Ron Bloom. And, of course, I have questions for GM and Chrysler today and they are simple, and I hope and believe that they will be answered truthfully.

But what political pressures for instance did the Obama administration and the auto task force bring to bear upon General Motors and Chrysler? What forced General Motors and Chrysler to sell crown jewels of iconic American industry to the UAW and to the U.S. Government, Canada and an Italian auto maker? What caused GM and Chrysler to shred absolutely the rights of their secured bondholders, that being the retired firemen, teachers, policemen, and nurses who helped GM and Chrysler survive, unfortunately, until the companies and the auto task force buried them alive?

What caused General Motors and Chrysler to sign up to an inexorable death march under UAW ownership, and this being the same UAW whose wage demands and work rules plunged them down the path of bankruptcy in the first place?

What caused GM and Chrysler to obliterate the thousands of loyal dealer franchises that sold their products for decades? If these dealerships were so ineffective, if they were so incapable, why not just let them die a natural death? If they were not profitable, they would have gone the way of the dinosaur by themselves.

The loyal dealers they shed like so much confetti that no one can explain, based on criteria that no one can identify—other than, of course, perhaps some of the bloggers and investigators who seem to have concurred that it was dealers who contributed to Republicans who were shed and dealers who gave to Democrats who were saved?

Why did GM and Chrysler leave behind their storied pasts and shrink into the minions and pawns of the Obama administration's climate change program, energy program, union patronage and Socialist dreams?

And finally, for anyone who loves America and American business, I ask, why did General Motors' and Chrysler's management not simply follow the examples of their forebearers and prevent this from happening the way that they did? William Durant built General Motors from—again, beginning in a bankruptcy, Buick's bankruptcy, which he turned into a triumph of private enterprise.

Walter P. Chrysler left GM chafing under Durant's leadership, rescued Willys-Overland from bankruptcy and then rescued the Maxwell-Chalmers Company and turned it into Chrysler. With

Chrysler, he took on Ford and General Motors and turned the Detroit Big Two into the Detroit Big Three.

Why did General Motors and Chrysler management not accept accountability, assume responsibility and prepare for bankruptcy when it was obviously coming in 2008? This is not a new conclusion on my part; some of us believed at the time that the bailout was being voted on that the bankruptcy should have been the first approach.

If they had, they could have gone through bankruptcy as private companies seeking private solutions. They have could have found those solutions and emerged again, in my opinion, as private companies. America would have been the stronger, not the weaker, and taxpayers would have saved money they may now never see again.

I know that we will ask many questions today and we will hear the best answers people can give us, but I do mourn for the spirit that once animated these great companies and pray for the country and for the future of American free enterprise.

And with that, Mr. Chairman, I yield back.

Mr. COHEN. I thank the gentleman for his statement.

Before I recognize Mr. Conyers, the distinguished Member of the Subcommittee and the Chairman of the full Committee, Mr. Franks referenced the Big Two in Detroit at one time. Well, we have the “big two” here, and the other of the “big two” is Representative Kilpatrick, and we want to welcome her to the Subcommittee for her attendance and appreciate her interest in this issue.

Now I recognize the senior member of the “big two,” the Chairman of the Committee, Mr. Conyers.

Mr. CONYERS. Thank you very much, Chairman Cohen.

This is the second part of this hearing. And I always dare hope that we come out of the hearing with knowing a little bit more and feeling a little bit more congenial than the first day. But my hopes are dashed again. My dear friend, the Ranking Member, insists on—I don’t know what the collective bargaining movement ever did to him or his friends, but this is a vital part of our system and after all President Gettelfinger has suffered from very disturbed members of his union by all the concessions that he has given up, he is now informed that he and his crew are running two automobile companies. And, goodness, I just want to say in his defense that that is not exactly the case.

The auto bailout activity was created under the Bush administration, and you were against that. Okay—well then, I guess I should just get used to it.

But the whole idea is that this wasn’t our idea. We didn’t ask the two largest automobile companies of the three to come to us and that we wanted to give them money. They are the ones that came and asked for help. And we have collectively agreed to do it. The current President has agreed to do it.

And the mention of Walter P. Chrysler, my father came from Monroe, Georgia, to Detroit and the first job he got was working for the Chrysler Corporation on East Jefferson in Detroit. I worked there summer during law school, and the whole idea—he had met Chrysler; I never met him. But we know a lot about the automobile industry in our family. My brother is the senior minority auto deal-



er in the United States, past president of the National Association of Minority Auto Dealers.

And, Mr. Chairman, here is what we are up against: We are trying to save a noble and important industry. But what we are also trying to do is to create as much cushion as we can as we have to do all this downsizing.

Plant after plant is being closed in Michigan and Ohio. To my dislike, there is plenty of outsourcing going on at the same time. The people whose plants are closed, they not only lose their job, they lose their health care. They lose their pensions. And frequently they end up on the foreclosure list as Detroit and Wayne County forecloses on an average of 147 homes every day.

So what I think that this Committee is charged with, what I think Carolyn Cheeks Kilpatrick's concern that brings her over to this hearing room is that we are trying to ease what we all know we have to do. To me, the suppliers are probably in a little bit better shape because I think their parts, the demand for their work is going to continue on. But the dealers, how can we modify the pain that they are going to have to sustain?

We are not saying we can't close any dealerships. We are just talking about perhaps a nonlegislative way to reduce this. That is what brings us here today and I hope that in that spirit we can work our way through these considerations.

Mr. COHEN. I thank the gentleman for his statement.

Is there any other Member that would like to make a statement?

The gentleman from North Carolina, Mr. Coble.

Mr. COBLE. Mr. Chairman, I appreciate that, and I won't use my 5 minutes. It is good to have our witnesses with us today.

Mr. Chairman, I indicated yesterday, in communities if you are going to categorize groups between thugs and heroes and leaders, there are certain groups that would automatically fall in the thug category. On the hero and leader side, with rare exceptions, the local automobile dealer, they are the heroes and leaders in their respective communities. They are the ones who support Little League baseball, Boy Scouts, Girl Scouts efforts. They are the first ones oftentimes to be at the head of the line in supporting causes of charity and to extend a hand to the impoverished. And now, unfortunately, many of these dealers and their employees may end up in the impoverished category. I hope not.

I believe, Mr. Chairman, we are going to overcome, we are going to prevail finally. But we won't prevail today or tomorrow, Mr. Chairman, probably not this year; and that assurance that we will prevail may not be too comforting to the dealer who may have lost his dealership and even to the management of GM and Chrysler with us today. It is just not a good time for any of us. But I do believe that ultimately we will come out of it on top.

I look forward to the hearing today, Mr. Chairman, and I appreciate your calling it.

And with that, I yield back my time.

Mr. COHEN. Mr. Coble, I appreciate your statement.

The other Members' opening statements will be included in the record, without objection.

[The prepared statement of Mr. Maffei follows:]

PREPARED STATEMENT OF THE HONORABLE DANIEL MAFFEI, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK, AND MEMBER, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

Thank you, Mr. Chairman for holding continued hearings on the ramifications of the auto industry bankruptcies. Automobile dealers are one of the largest private sector employers in the United States, providing tens of thousands of local jobs and contributing millions of dollars in tax revenues to states. They are anchors in communities throughout the country and many times ownership is passed down from generation to generation. In addition, many auto dealerships are minority owned and have traditionally provided strong local community support.

As I pointed out in yesterday's hearing, there has been a lack of transparency in the means by which Chrysler and GM have chosen to reject dealers' franchise agreements, and I still believe there is a lot of confusion out there as to how the closing of hundreds of dealerships will be financially beneficial to these two auto companies. Over time, automakers created the franchise dealer network specifically to lower their costs, as they outsource virtually all costs associated with selling and servicing cars.

There are some arguments that in the long run you need to have a smaller dealer network to help make sure the prices are stabilized and there are some expenses that auto companies have to service these dealerships but, in the short run, we can't find anything. In my district, we have already lost 11 dealers in the last couple of years because of market forces, so it seems like the market is working in some cases.

This is precisely what led me, along with my good friend from Maryland Frank Kratovil, to introduce H.R. 2743, the "Automobile Dealer Economic Rights Restoration Act of 2009," which would require Chrysler and GM to continue to honor their commitments to auto dealers. Specifically, the legislation requires that auto manufacturers in which the Federal Government has an ownership interest continue to honor their commitment and not deprive economic rights to the dealers, essentially protecting small business owners, workers, communities, and jobs.

This bill has widespread bipartisan support, as there are currently over 250 House cosponsors. We have Members signing on who are on the left of the left, the right of the right, and everything in between. From all over the country from rural areas to urban areas, this affects all local communities. These are family businesses that are really part of the fabric of our communities. I look forward to the testimony of our witnesses.

---

Mr. COHEN. I would like to thank all our witnesses for their willingness to participate in today's hearing. Without objection, your written statements will be placed into the record, and we ask that you limit your oral remarks to 5 minutes. There is a pictured color system that shows you 5 minutes, 4 minutes, 1 minute. If you have green, you are in the 5-to-1-minute territory; yellow, you are in your last minute; and red, you are beyond your time. And there you go.

Ms. Van Der Wiele and Mr. Orr will split the time between the two of you, as I understand it, and you will note the lighting system. After each witness has presented his or her testimony, Subcommittee Members will be permitted to ask questions subject to the 5-minute limit.

To my understanding Mr. Miller will not have oral remarks, but will be available for questioning on behalf of General Motors Corporation.

Mr. COHEN. I am pleased to introduce the witnesses on our first panel for today's hearing.

Our first witness is Ms. Louann Van Der Wiele. Ms. Van Der Wiele is Vice President and Associate General Counsel in the Office of General Counsel of Chrysler Group in Auburn Hills, Michigan. Her responsibilities include overseeing employment litigation, environmental litigation, and defense of product liability, class action,

and warranty litigation involving Chrysler, Dodge, and Jeep. She also advises the company on other vehicle-related consumer protection matters, regulatory affairs, and risk management issues. Ms. Van Der Wiele joined Chrysler in 1986.

Thank you, Ms. Van Der Wiele, and I would like to ask you to proceed with your testimony.

**JOINT TESTIMONY OF LOUANN VAN DER WIELE, VICE PRESIDENT AND ASSOCIATE GENERAL COUNSEL, CHRYSLER GROUP LLC; AND KEVYN D. ORR, PARTNER, JONES DAY**

Ms. VAN DER WIELE. Thank you, Mr. Chairman.

Chairman Cohen, Ranking Member Franks, and Members of the Subcommittee, thank you for providing this opportunity to discuss the ramifications of the former Chrysler LLC's bankruptcy.

I sit here today representing the new Chrysler Group LLC as Vice President and Associate General Counsel. With me is Kevyn Orr, representing our outside legal counsel. Kevin will outline the bankruptcy process, and then I will discuss the ramifications of the bankruptcy. Throughout my testimony I will refer to the former Chrysler as Old Carco, which is a term the bankruptcy court uses, and I will refer to the new company as Chrysler Group.

Mr. ORR. Good morning, Mr. Chairman, Mr. Ranking Member, and Members of the Committee.

Mr. COHEN. Mr. Orr, this is kind of unique for me to split the testimony, but I want to recognize Kevyn Orr and introduce you as a partner in the Jones Day firm.

Prior to that he was with the Department of Justice. In June, 1995, he was Deputy Director of the Executive Office for the United States Trustees; in February of 2000, he became director of that program. He joined the litigation department of FDIC in 1991 and transferred to the Resolution Trust Corporation. By 1994, Mr. Orr rose to the position of Assistant General Counsel for Complex Litigation of Bankruptcy at the RTC.

We appreciate your testimony and you may proceed.

Mr. ORR. Thank you for the recognition, Mr. Chairman.

Mr. COHEN. You are welcome, Mr. Orr.

Mr. ORR. As Louann stated, my name is Kevyn Orr, and I am a Partner at the law firm of Jones Day. I and my partners have provided Old Carco with restructuring advice and, eventually, its bankruptcy planning since last fall.

The circumstances that resulted in the bankruptcy have been well chronicled. Last fall, Old Carco sought Federal assistance to continue its ongoing restructuring. Old Carco received interim funding in January and in February submitted a viability plan to the U.S. Treasury.

On March 30, the Automotive Task Force informed Old Carco that although it could not survive as a stand-alone entity, the company could become viable with an appropriate strategic partner, such as Fiat, if it obtained additional concessions from key stakeholders.

When certain creditors would not agree to the necessary concessions, Old Carco filed for bankruptcy. In connection with this filing, Old Carco, Fiat, and Chrysler Group entered into an arms-length purchase agreement under which Old Carco would transfer the ma-

majority of its operating assets to the new Chrysler Group in exchange for cash and Chrysler Group's assumption of certain liabilities. The Bankruptcy Court approved the Fiat transaction, and after several court challenges were resolved, the transaction was consummated on June 10, 2009.

As part of the process of putting together this package, Old Carco decided to reject 25 percent of its dealers. Old Carco selected dealers for rejection using a thoughtful, rigorous and objective process. The Bankruptcy Court approved the dealership rejections as a sound exercise of business judgment.

Chrysler Group has worked hard to assure a soft landing for Old Carco dealers whose contracts have not been assumed by arranging for the redistribution of 100 percent of inventory, parts, and special tools. Chrysler Group has helped 436 displaced dealership workers find jobs at 239 dealers.

Similarly, the new company did not assume product liability claims out of the sale of vehicles before bankruptcy. However, Chrysler Group has agreed to indemnify its dealers against product liability lawsuits. As a result, in the vast majority of product liability cases involving Old Carco vehicles sold before the bankruptcy, Chrysler Group will defend its dealers pursuant to its dealership agreements.

Louann.

Ms. VAN DER WIELE. While difficult and painful, the bankruptcy and subsequent sale of assets to Chrysler Group were vastly preferable to the only other alternative, the complete liquidation of Old Carco.

Customers benefit because Chrysler Group is now able to provide them with a quality sales and service experience. Employees benefit because Chrysler Group will continue to employ more than 30,000 people in the United States and, to a large extent, maintain retiree benefits.

Suppliers benefit because Chrysler Group intends to move forward with approximately 1,100 production suppliers that employ thousands of people throughout the country. Dealers benefit because 75 percent have become Chrysler Group dealers and the remainder have the benefit of the soft landing that Chrysler Group has agreed to provide. Taxpayers benefit because Chrysler Group is well positioned to become a viable company that will fully repay its debt to the taxpayers.

None of these benefits would have accrued if Old Carco had liquidated. Customers would have lost access to warranty coverage, service, and parts. Tens of thousands of employees would have lost their jobs and retirees, their benefits. Almost 3,200 dealerships would have closed. Taxpayers would have had to pick up significant costs for unemployment support, health care, and pensions that would default to the Pension Benefit Guaranty Corporation.

We appreciate the opportunity to testify before the Subcommittee today and look forward to answering your questions.

Mr. COHEN. Thank each of you for your testimony.

[The joint statement of Ms. Van Der Wiele and Mr. Orr follows:]

JOINT PREPARED STATEMENT OF LOUANN VAN DER WIELE AND KEVYN D. ORR

**House Judiciary Subcommittee on Commercial and  
Administrative Law**

**July 22, 2009**

**Ramifications of Auto Industry Bankruptcies**

**Louann Van Der Wiele  
Vice President and Associate General Counsel  
Chrysler Group LLC**

**Kevyn Orr  
Partner  
Jones Day**

**Introduction - Louann Van Der Wiele**

Chairman Cohen, Ranking Member Franks and Members of the Subcommittee, thank you for providing this opportunity to discuss the ramifications of Chrysler LLC's ("Old Carco") bankruptcy. I sit here today representing the new Chrysler Group LLC ("Chrysler Group") as Vice President and Associate General Counsel. With me is Kevyn Orr, representing our outside legal counsel. Together we will provide you with a thorough accounting of the legal ramifications of Old Carco's bankruptcy.

I also sit here today as a 20-year employee of Chrysler Corporation, DaimlerChrysler Corporation, Chrysler LLC and Chrysler Group. While there is much about bankruptcy that is dry, legal, and technical, I have first-hand knowledge of the real human impact of a bankruptcy. In the end, the best thing that can be said in favor of the bankruptcy process Old Carco is undergoing is that, as difficult and painful as it has been, it is vastly preferable to the only alternative – the complete liquidation of Old Carco. I hope that the experiences we have gone through will provide useful insights to you about this important process entrusted to your jurisdiction.

Kevyn Orr will provide for you an outline of the bankruptcy process and the transaction that resulted in an entirely new company, Chrysler Group. I will follow with an outline of how the sale of Old Carco's assets to Chrysler Group will benefit the stakeholders in Old Carco, including the taxpayers.

**Chrysler's Bankruptcy Process – Kevyn Orr**

As Louann stated, my name is Kevyn Orr and I am here today as outside counsel. I am a partner at the law firm of Jones Day. I have provided Old Carco with restructuring advice and eventually its bankruptcy planning since last fall.

Old Carco's efforts to avoid bankruptcy began in early 2007, when the company initiated an operational restructuring effort that met targets through the first half of 2008. Part of that restructuring effort included a search for potential partners and strategic alliances that would produce operational synergies and allow expansion into new products, market segments, and geographic locations. Specifically, Old Carco sought a strategic partner with expertise in smaller, more fuel-efficient vehicles that would also enhance its global presence. To that end, in 2007 and 2008, Old Carco discussed potential alliances with GM and with Fiat.

In the fall of 2008, the global credit crisis affected the liquidity markets and severely restricted the availability of loans to both dealers and consumers. This resulted in an erosion of consumer confidence and a sharp drop in retail vehicle sales. Old Carco was forced to use cash reserves to compensate for the resulting losses and reduced cash flow.

As a result, in late 2008 Old Carco and other domestic entities sought financing from the government to fund their operations during the credit crisis and the economic downturn. At the same time, Old Carco continued to pursue an alliance with Fiat because it viewed Fiat's products and distribution network as complementary and capable of strengthening Old Carco for the long-

term, thereby maximizing the value of its enterprise for the benefit of all constituents, including U.S. taxpayers, employees, creditors, dealers, and suppliers.

The Fiat Alliance was conditioned on Old Carco meeting other parts of a viability plan required by the federal government, including concessions from various stakeholders such as the International Union, United Automobile Aerospace and Agricultural Implement Workers of America (the "UAW"), secured lenders, dealers, and suppliers.

On February 17, 2009, Old Carco submitted a viability plan to the U.S. Treasury that included three potential scenarios: (1) a stand-alone restructuring of Old Carco (the "Stand-Alone Viability Plan") with concessions from all key constituents, some of which had already been agreed upon and others of which remained subject to ongoing negotiations; (2) a scenario showing the positive synergies from the Fiat Alliance (the "Alliance Viability Plan"), and (3) an orderly wind-down or liquidation plan for all of Old Carco's operations if neither the Stand-Alone Viability Plan nor the Alliance Viability Plan could be achieved. The February 2009 submission included the proposed concessions from all key stakeholder groups, including equity holders, union and non-union employees and retirees, first and second pre-petition lien holders, suppliers, and dealers.

On February 20, 2009, the President's Auto Task Force (the "Task Force") was established to evaluate Old Carco's Viability Plan. The Task Force initiated discussions with Old Carco and its advisors and other key stakeholders to negotiate with all parties to obtain concessions and agreements consistent with Old Carco's Viability Plan submission.

On March 30, 2009, the Task Force informed Old Carco that although Old Carco could not survive as a stand-alone entity, the company could become a viable entity with an appropriate strategic partner, such as Fiat, if Old Carco modified certain other aspects of the Alliance Viability Plan and obtained additional concessions from key stakeholders. The U.S. Treasury gave Old Carco an additional 30 days to meet these conditions. Consistent with these goals, a revised term sheet for a Fiat Alliance was signed and the U.S. government agreed to fund Old Carco's working capital needs through April 30, 2009.

Old Carco, Fiat, and Chrysler Group tentatively entered into a Master Transaction Agreement dated as of April 30, 2009 (the "MTA"), pursuant to which Old Carco agreed to transfer substantially all of its operating assets to Chrysler Group. In exchange for those assets, Chrysler Group agreed to assume certain liabilities of Old Carco and pay Old Carco \$2 billion in cash. In consideration for this transaction, Fiat agreed to contribute to Chrysler Group access to competitive fuel-efficient vehicle platforms, certain technology, distribution capabilities in key growth markets and substantial cost saving opportunities, and Chrysler Group agreed to issue Membership Interests in Chrysler Group, with 55% going to an employee health care trust fund, 8% to the U.S. Treasury and 2% to Export Development Canada. The Fiat transaction contemplated that a subsidiary of Fiat would own 20% of the equity of Chrysler Group, with the right to acquire up to an additional 31% of Chrysler Group's Membership Interest under certain circumstances, including: 5 percent for bringing a 40 mpg vehicle platform to Chrysler to be produced in the U.S.; 5 percent for providing a fuel-efficient engine family to be produced in the U.S. for use in Chrysler vehicles; and 5 percent for providing Chrysler access to its global

distribution network to facilitate the export of Chrysler vehicles. Fiat's ownership share could not exceed 49% until after all U.S. government loans have been completely repaid.

The U.S. Treasury and Export Development of Canada also agreed to provide debtor-in-possession financing for 60 days and additional loans to support Chrysler Group's operations after the sale.

Despite entering into these transactions and agreements, Old Carco still hoped to avoid a bankruptcy filing and actively engaged in negotiations with its major stakeholders. However, it became apparent that certain creditors would not agree to the concessions necessary to avoid a bankruptcy filing. Thus, on April 30, 2009 (the "Petition Date"), Old Carco and 24 of its affiliated debtors and debtors in possession commenced their reorganization cases by filing voluntary petitions for relief under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code").

In order to preserve the value of Old Carco's assets, the Bankruptcy Court approved an order on May 1, 2009, allowing Old Carco to continue warranty, incentive, and extended service program payments. This critical order allowed the Debtors to preserve the value of Old Carco's assets and continue to operate their businesses and manage their properties as debtors in possession pursuant to the Bankruptcy Code.

On May 5, 2009, the Office of the United States Trustee for the Southern District of New York (the "U.S. Trustee") appointed an official committee of unsecured creditors, pursuant to the Bankruptcy Code (the "Creditors' Committee"). The Committee, charged with protecting the interest of Old Carco's creditors in the bankruptcy process, was composed of representatives from the various creditor groups including dealers, suppliers, tort claimants, and other unsecured creditor representatives. The Committee actively participated in the sale process and remains active to this date.

In connection with the commencement of the bankruptcies, Old Carco and its Debtor subsidiaries, Fiat S.p.A. ("Fiat") and Chrysler Group entered into a MTA dated as of April 30, 2009. The Purchase Agreement provided, among other things, that: (a) Chrysler would transfer the majority of its operating assets to New Carco Acquisition LLC now known as Chrysler Group LLC ("Chrysler Group"), a newly established Delaware limited liability company formed by Fiat; and (b) in exchange for those assets, Chrysler Group would assume certain liabilities of Old Carco and pay to Old Carco \$2 billion in cash (collectively with the other transactions contemplated by the Purchase Agreement, the "Fiat Transaction"). On May 3, 2009, the Debtors filed a motion to approve the Fiat Transaction or a similar transaction with a competing bidder and supplemented this motion on May 22, 2009.

It is important to remember that this was an arms-length transaction with a third-party purchaser. Old Carco had to present an attractive package of assets and liabilities to Fiat in order to avoid liquidation; had Old Carco included additional liabilities that Fiat did not believe it was in the new company's interest to assume, no deal would have been consummated.

Among the liabilities that the new company specifically did not assume were product liability claims arising out of the sale of vehicles before bankruptcy as part of the Sale Transaction.



Assuming future claims on products sold before the bankruptcy was not a feasible option for Chrysler Group because of resource constraints; obviously, Chrysler Group would have needed additional resources if it had agreed to cover these claims. However, Chrysler Group has agreed to indemnify its dealers against product liability lawsuits. These dealers sold approximately 85% of the vehicles sold by Old Carco. As a result, in the vast majority of product liability cases involving Old Carco vehicles sold before the bankruptcy, Chrysler Group will defend its dealers pursuant to its dealership agreements.

Similarly, the Fiat Transaction contemplated that Chrysler Group would assume the dealership agreements of 75% of Old Carco's dealers, representing 86% of the volume of that company's sales. Chrysler Group has estimated that bringing forward 100% of Old Carco's dealers would increase its costs and decrease its revenues by an average of \$2.1 billion annually over the next four years. Obviously, the Fiat Transaction would have been quite different if Chrysler Group had contemplated that it would be forced to assume dealership agreements with 100% of Old Carco's dealers.

Old Carco selected dealers for rejection using a thoughtful, rigorous and objective process designed to have the least negative impact while still creating a new dealer footprint scaled to be viable and profitable for the long term. The methodology was consistently applied to every dealer in the company's U.S. operations, and reviewed many factors that are unique for each market and dealer.

These factors included:

- Total sales potential for each individual market
- Each dealer's record of meeting minimum sales responsibility
- A scorecard that each dealer receives monthly, and includes metrics for sales, market share, new vehicle shipments, sales satisfaction index, service satisfaction index, warranty repair expense, and other comparative measures
- Facility that meets corporate standards
- Location in regard to optimum retail growth area
- Exclusive representation within larger markets

A team of people within Old Carco's local business centers around the country, as well as headquarter's staff reviewed every market and dealer situation as a group many times. From this analysis, the 2,392 dealers who would best carry the new company forward were identified.

Although Old Carco submitted a plan to reduce total dealer count by 25 percent, those dealers represent only 14 percent of the company's sales volume. Half of these dealerships sell fewer than 100 vehicles a year, or less than nine vehicles per month on average (that compares with 125 vehicles sold per month on average at Toyota dealerships). About 44 percent of the discontinued dealers who reported revenues were profitable, earning \$84 million last year, while the remaining 56 percent were unprofitable, losing a total of \$136 million.

The bankruptcy court held a hearing to consider approving the Fiat Transaction on May 27, 2009 through May 29, 2009 (the "Sale Hearing"). All interested parties were given the opportunity to appear at the Sale Hearing. During this hearing, numerous parties examined multiple witnesses

and also were permitted to make oral argument in support of and against the proposed Fiat Transaction.

The un rebutted testimony of Old Carco's financial advisor showed that the \$2.0 billion that Chrysler Group agreed to pay for Old Carco's assets exceeded the value that the lien holders could have recovered in an immediate liquidation. The liquidation analysis was confirmed and reinforced when no legitimate bidders aside from Fiat came forward with an offer to purchase Old Carco's assets.

The Sale Hearing comprised three full days during which more than ten Old Carco witnesses appeared, more than four dealer witnesses were presented and CEO Bob Nardelli was cross-examined for more than seven hours. On May 31, 2009, the Bankruptcy Court issued: (a) an Opinion Granting the Debtors' Motion Seeking Authority to Sell, Pursuant to § 363, Substantially All of the Debtors' Assets (the "Sale Opinion"); and (b) an Opinion and Order Regarding Emergency Economic Stabilization Act of 2008 and Troubled Asset Relief Program (together with the Sale Opinion, the "Opinions"). On June 1, 2009 and consistent with the Sale Opinion, the Bankruptcy Court entered an Order authorizing the Fiat Transaction (the "Sale Order"). In the Opinions and the Sale Order the Bankruptcy Court specifically found that: Old Carco had exercised sound business judgment in entering into the Fiat Transaction; that the deal was negotiated at arms' length with a third-party purchaser and in good faith for a proper purpose; that the value realized via the Fiat Transaction was greater than the value that would be realized via a liquidation; and that Old Carco had presented an adequate factual basis to support the sale under applicable law. On June 5, 2009, the United States Court of Appeals for the Second Circuit affirmed the Opinions and the Sale Order. Several of the objectors then sought a stay of the Second Circuit's opinion. After a brief consideration of the objectors' request, the Supreme Court declined to grant a stay of that opinion on June 9, 2009, and, consistent with the Sale Order, the Fiat Transaction was consummated on June 10, 2009.

After the Sale process was complete, the Bankruptcy Court dealt with the assumption of certain dealership franchise agreements. The Bankruptcy Court heard two days of testimony and oral arguments regarding Old Carco's business decision to reject certain franchise agreements and pass on other franchise agreements to Chrysler Group. At an evidentiary hearing held on June 4, 2009, 15 witnesses testified and approximately 66 witnesses presented testimony by declaration.

For Old Carco, excess dealerships were burdensome in several ways. First, many dealerships did not sell all three Old Carco brands, so Old Carco had to provide similar products in each of the three different brands so all dealers would have access to as broad a market as possible. This was inefficient and expensive. For example, Old Carco supplied dealers with two similar minivans, Chrysler Town & Country and Dodge Grand Caravan; two similar full-size sport-utilities, Chrysler Aspen and Dodge Durango; two similar mid-size SUVs, Dodge Nitro and Jeep® Liberty; and two similar sedans, the Chrysler Sebring and Dodge Avenger. Based on six major vehicle launches between 2005 and 2008, Old Carco incurred approximately \$1.4 billion in incremental costs to develop these multiple pairs of "sister vehicles."

Second, as a result of overdealering, the marketing and advertising messages were split between multiple products, diminishing the reach and frequency of each campaign. For example, in 2008 Old Carco spent about \$100 million on each of two marketing and advertising campaigns to launch two redesigned minivans, instead of spending half as much to support a single launch to attain virtually the same sales volume.

Finally, poor performing dealers cost Old Carco customers and lost revenue. Poor performing dealerships cannot afford to keep facilities up-to-date or hire and train the best people, resulting in poor customer experience and lower sales. In fact, in 2008, the 789 discontinued dealers achieved sales of only 73 percent of the minimum sales responsibility, representing 55,000 lost unit sales and \$1.5 billion in lost revenue in 2008.

On June 9, 2009, the Bankruptcy Court heard oral arguments on the legal issues related to the rejection of certain franchise agreements. After arguments concluded, the Court issued an Order Pursuant to Sections 105 and 365 of the Bankruptcy Code and Bankruptcy Rule 6006, (A) Authorizing the Rejection of Executory Contracts and Unexpired Leases with Certain Domestic Dealers and (B) Granting Certain Related Relief (the "Rejection Order") and issued its Opinion Regarding Authorization of Rejection of All Executory Contracts and Unexpired Leases with Certain Domestic Dealers and Granting Certain Related Relief (the "Rejection Opinion") on June 19, 2009. Again, in examining the company's decision to reject 789 dealership agreements, the Bankruptcy Court found that "[t]he decision-making process used by [Old Carco] was rational and an exercise of sound business judgment," and amply supported by both the factual record and prevailing case law. The court also found:

The Debtors identified numerous advantages of having a smaller dealership network, including better and more sustainable sales and profitability for each dealer, which in turn would provide greater resources for marketing, reinvesting in the business, improving facilities, enhancing the customer experience and customer service, and keeping and attracting more experienced and highly qualified personnel to work at the dealerships. . . . A smaller dealership network is expected to concentrate profits such that more capital improvements will be made to a dealership facility, thereby attracting more customers and providing customers with a better experience. A smaller dealership network would also enable the Debtors to reduce expenses and inefficiencies in the distribution system, including reducing costs spent on training, new vehicle allocation personnel, processes, and procedures, dealership network oversight, auditing, and monitoring, and additional operational support functions. Consolidation of "partial line" dealerships would eliminate redundancies and inefficiencies in the dealership network. In re Chrysler LLC *et al.*, No. 09-50002, slip op. at 9 (S.D.N.Y. June 9, 2009).

Only one dealer has chosen to appeal this ruling. This appeal is currently pending before the Second Circuit Court of Appeals.

Bankruptcy is not an easy or pleasant process. All bankruptcies are not alike, and in Old Carco's bankruptcy the ability to sell substantially all its assets to a third party purchaser to form a new company with a stronger balance sheet, more competitive labor agreements, and a right-sized dealer network was essential to the new company's survival in the short term and its ability to remain viable in the future. Legislation that would reverse some of the difficult but necessary

actions taken during Old Carco's bankruptcy will endanger the new company's viability efforts and the investment of U.S. taxpayers.

**Ramifications of Chrysler's Bankruptcy – Louann Van Der Wiele**

While the Treasury-supported bankruptcy adversely impacted all of Old Carco's stakeholders, the alternative – liquidation – would have been far worse. Let me give you a brief update on the benefits that this bankruptcy has provided – especially when compared to the complete liquidation of Old Carco:

**Customers:** Treasury provided product warranty guarantees during the bankruptcy to ease potential customer concerns. Had Old Carco been completely liquidated, Old Carco's existing customers would have effectively lost their warranty coverage, and servicing and parts production would have been inadequate to meet their needs. Chrysler Group is now able to provide Old Carco's customers with a quality sales and service experience.

**Dealers:** The new Chrysler Group formed as a result of the bankruptcy was able to assume 2,392 dealers -- approximately 75% of the existing dealership network, responsible for approximately 86% of Old Carco's sales. Chrysler Group determined that a reduced number of dealers were necessary in order for the new Company to survive and compete in the realities of today's smaller market. While the industry averaged 16 million new vehicles sold in the U.S. each year between 1990 and 2007, the expected Seasonally Adjusted Annual Rate (SAAR) for 2009 is only 10.1 million units. The average SAAR between 2009-2012 is expected to be no greater than 10.8 million units. Such numbers simply do not support the dealer body that Old Carco maintained before the bankruptcy. If Old Carco had been forced into liquidation, *the entire dealership network* would have lost their franchises, resulting in massive job losses.

Chrysler Group has worked hard to assure a soft landing for the Old Carco dealers whose contracts have not been assumed, including the redistribution of 100% of inventory, parts, and special tools. Chrysler Group quickly put together a program with GMAC to provide wholesale financing so all remaining inventory would be redistributed to the dealers going forward. There were 42,000 vehicles in stock at discontinued dealers on May 14, and to date approximately 39,500 have been sold to customers or transferred to retained dealers. The remaining approximately 2,500 vehicles will be transferred to retained dealers by July 24. Chrysler Group has pledged to complete the redistribution of special tools and parts within 90 days, and to date, commitments are in place for 87% of parts inventory value of the discontinued dealers.

As expected, many discontinued dealers are remaining open as used vehicle retailers or operating competing franchises and are therefore reducing the number of displaced workers. To assist dealership workers who lose their jobs, Chrysler Group has expanded its current online job posting hiring process to help place dealership employees who lose their positions. This job posting site averages 600 job views per week, and as of July 11, 436 displaced workers have found jobs at 239 dealers.

As noted earlier, Chrysler Group continues to stand behind its products and its dealers. As part of the Sale Transaction, Chrysler Group specifically did not assume product liability claims arising out of the sale of vehicles before bankruptcy. However, because Chrysler Group will indemnify its dealers against product liability lawsuits, we anticipate being involved in future

claims on Old Carco's products. While we are saddened anytime someone is injured in one of our vehicles, vehicles sold by Old Carco, like the vehicles sold by Chrysler Group, meet or exceed all federal safety standards and have warranties that remain in full force and effect.

**Suppliers:** As noted, in prior years Old Carco had more than 1,300 production suppliers and purchased more than \$30 billion of goods and services from suppliers annually. Chrysler Group intends to move forward with approximately 1,100 production suppliers that employ thousands of people throughout the country. Chrysler Group anticipates spending \$22 billion with suppliers in 2009. Had Old Carco completely liquidated instead of selling substantially all of its assets to a new company, many of these suppliers would not have been able to survive. Their failures would have cascaded across the entire industry and further added to the nation's economic woes. Even with the creation of Chrysler Group and the new GM, many automotive suppliers are financially strained given the events of the last 12 months.

**Employees:** Chrysler Group will continue to employ more than 30,000 people in the U.S. – including approximately 20,000 employees in Michigan, which as you know has the highest unemployment rate in the nation. The company was able to maintain workers' compensation payments during bankruptcy and to a large extent has maintained retiree benefits. Liquidation would have wiped out these jobs and benefits, shifting an enormous economic burden upon our fragile local and state governments.

**Taxpayers:** Chrysler Group is well-positioned to become a viable company capable of fully repaying its debt to American and Canadian taxpayers. Old Carco's liquidation would have caused taxpayers to pick up significant costs for unemployment support, health care and pensions that would default to the Pension Benefit Guarantee Corporation (PBGC) the government agency that insures private sector pension plans. In addition, given the current economic downturn, a failure of Chrysler Group would be a severe setback to the efforts to restore confidence and revive growth.

#### **The Alternate Scenario: Liquidation**

The only alternative to bankruptcy was liquidation of Old Carco and all of its assets. In a liquidation analysis prepared for Old Carco,<sup>1</sup> Robert Manzo of Capstone Advisory Group, a financial advisor to the company as part of its bankruptcy process, stated that this would be the first liquidation of a major domestic automaker. He noted that due to the depressed circumstances in the automotive industry and economy in general, under a liquidation scenario the recovery for assets such as tooling, plant property, equipment, product lines, and other corporate assets would be only a fraction of their value.

Plants would have remained mothballed until they were sold and the resulting unemployment and economic impact in our plant communities would have been swift and severe. All dealer and supplier contracts likely would have been voided, leading to further bankruptcies and economic distress. Mr. Manzo's analysis concluded that at the completion of the liquidation there would not be any residual value available for the benefit of any other class of claimant (with the exception of first lien creditors), including the general unsecured creditors.

<sup>1</sup> "Preliminary Hypothetical Liquidation Analysis – Orderly Liquidation," (January 30, 2009).

The impact of liquidation on Old Carco's employees would have been severe. Due to the lack of liquidity in Old Carco, private debtor-in-possession financing was not available. If Old Carco collateral had been used to fund the administration of the bankruptcy, Old Carco would have had to cease all benefit payments, including supplemental unemployment benefits to UAW employees. The only employees that would have remained on payroll would have been those administering the liquidation.

Furthermore, the PBGC could have faced significant additional liabilities from Old Carco in the event of liquidation. The health care and benefits of both active employees, retirees and their spouses and dependents also would have been at risk.

The consequences of liquidation would not have been confined to Old Carco. Its collapse could have resulted in the failure of other auto manufacturers due to the shared supplier base. The ripple effects of such a catastrophe would have been felt in thousands of communities around the country in all 50 states. According to a research memorandum published November 4, 2008, by the Center for Automotive Research, 4.5 million people depend on the U.S automotive industry. This memorandum estimates the impact of a domestic auto maker failure to the overall economy, and the result is devastating: 2.3 – 3 million in lost jobs, \$275-\$400 billion in lost wages, and \$100-\$150 billion in lost Government revenue.

This alternate scenario of liquidation is important because it illustrates that, while this bankruptcy has required painful concessions from all of Old Carco's stakeholders, the alternative would have had much more painful consequences for employees, retirees, dealers, suppliers, and creditors (including unsecured tort claimants).

#### **Chrysler Group's Position Post-Sale**

We have previously stated that the goal of the sale of Old Carco's assets to the new company was to create a strong, financially sound automotive company serving customers with a broader and more competitive lineup of environmentally friendly, fuel-efficient, high-quality vehicles and an equally high level of customer service through an efficient dealer network. Through the steps already taken, Chrysler Group is in a position to achieve that goal.

The future of Chrysler Group is undoubtedly challenging, but the company has a real chance not just to survive, but to thrive. Through the alliance with Fiat, Chrysler Group has access to new technologies that will allow it to deliver more fuel-efficient new products to the American people and has access to global markets. Funding is available to Chrysler Group to devote to the development of high-quality vehicles that customers will enjoy driving and want to buy again. More than that, Chrysler Group is a strong company with an efficient management structure and leadership clearly committed to change.

Nonetheless, Chrysler Group faces a tough road ahead. Our economy continues to suffer and unemployment remains high. Many observers note that we face a few more quarters of slow economic growth before we will see auto sales improve. In this difficult environment, it is very important to recognize that legislation aimed at reversing some of the painful but necessary actions taken during Old Carco's bankruptcy will simply take Chrysler back to the future that Old Carco faced not long ago – and this time, without the option of a purchaser for substantially

all of its assets. Complete liquidation, with all of its dire consequences, could follow.

We appreciate the opportunity to testify before this subcommittee today and we look forward to answering your questions.

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Mr. COHEN. Our final witness to give oral testimony is Mr. Michael Robinson. Mr. Robinson is Vice President and General Counsel of North America for General Motors and formerly held the same position for the old General Motors, the one your grandfather knew.

Mr. Robinson joined General Motors in 1984 and has held a number of positions on the legal staff for GM. Before assuming the North America General Counsel role in 2008, he served as Practice Area Manager and Managing Attorney, and prior to that he was Corporate Compliance Officer.

In the 1990's, he provided counsel to General Motors leadership on matters involving lobbying and government ethics issues.

I think that may be an oxymoron, but maybe not.

Mr. Robinson, you may proceed with your testimony.

**TESTIMONY OF MICHAEL J. ROBINSON, VICE PRESIDENT AND GENERAL COUNSEL OF NORTH AMERICA, GENERAL MOTORS COMPANY, ACCOMPANIED BY HARVEY R. MILLER, PARTNER, WEIL, GOTSHAL & MANGES LLP**

Mr. ROBINSON. Good morning, and thank you, Chairman Cohen and Ranking Member Franks. I am Michael Robinson, General Counsel for North America's GM operations. I have with me and I appreciate your recognizing, Mr. Chairman, Harvey Miller from the Weil, Gotshal law firm. Mr. Miller is not making introductory remarks this morning, but he is here, we hope, to assist the Subcommittee in answering any questions that they may have that relate to bankruptcy, especially the intricacies of bankruptcy.

Mr. Miller represented General Motors in the filing on June 1. He represented us through the asset sale that took place and is a renowned expert in the bankruptcy field. So we look forward to your questions this morning.

Upon the day we emerged from bankruptcy as a new car company, our President and CEO, Fritz Henderson, said business as usual at GM is over. The last 100 days have shown everyone, including us, that a company not known for quick action can, in fact, move rather fast.

There are many who contributed to our moving through the bankruptcy process as quickly as we did. First, the American public. I know this has been controversial within a political context, but without our Nation's support, we would not have this precious second chance. We understand our responsibility to the taxpayer, and we will repay that investment.

Secondly, there are many who have been called upon to make sacrifices to create a new GM, one that competes, wins, and is profitable for the long run. Behind each action we are taking to reinvent GM, there is a human story; we recognize that.

As those familiar with bankruptcy law know all too well, this is a painful process that spares no particular group. This collective sacrifice was necessary to put GM on a brighter path to long-term viability and success: to deliver and reduce debt, to operate under competitive labor agreements, to have manufacturing capacity and dealer networks that match today's market realities, and most importantly to continue to design and build winning cars and trucks with leading technologies.

Let me briefly touch upon a couple of groups that I know are of particular interest to this Committee and how our restructuring affects them. With respect to GM dealers, we cannot go through this sweeping transformation without a comparable effort to reshape our retail dealer network, one which was, frankly, created during



the 1950's and 1960's before we had the infrastructure of interstate highways.

We worked very hard to restructure GM's dealer network as carefully, responsibly and objectively as we could. It is important to note that of our approximately 6,000 dealerships in GM's network, we were able to retain 4,100 of those dealerships. We also expect another 600 or so dealerships will stay in business as Saturn, Hummer or Saab dealerships if the sale of those brands to new ownership closes, as we hope it will.

This left us with the hard choice to send wind-down agreements to about 1,300 dealerships. From the start, we wanted to help these dealerships wind down their dealerships in an orderly fashion with a structured financial assistance package that was very beneficial to them compared to their alternative, that is, where most contracts in bankruptcy are typically rejected with no assistance whatsoever.

GM is providing, in aggregate, nearly \$600 million in available assistance to these dealers, with the first installments, by the way, having already been paid to these dealers just this past Monday.

With normal dealership attrition factored in, we are building a profitable business plan for GM, having between 3,600 and 3,800 U.S. GM dealers by the end of year 2010, which, with a retail sales market of just over 10 million cars and trucks and a conservative market share assumption, means that the number of units sold per dealership should nearly double. For dealers, this translates into greater return on investment, ability to have the best locations and facilities and the best sales personnel to take care of customers, all of this is to attract new customers.

Second, a concentrated and highly profitable dealer network will reduce costs for GM at a time when every dollar really counts. These cost savings come in two categories. About \$2 billion in cost is in direct dealer support programs, or subsidies that have been incorporated and accumulated over time to help support the weaker parts of our dealer network. These are costs, by the way, that Toyota does not have. Another \$415 million or so in gross fixed cost savings is the potential here. These cost burdens are just not sustainable as we go forward.

However, even with these changes, GM will have the largest dealer network in the country, more than any of our competitors, in our case, 3,800 versus Toyota's 1,200. This would include an extensive rural and small town network of 1,500 dealers nationally in markets where we hold, on average, a 10 percent market share advantage.

The restructured dealer network, the right number of dealers in the right locations with the right brands is key to our success. These dealers are helping to create a viable GM that will preserve over 200,000 jobs at GM and hundreds of thousands of jobs beyond that with our direct manufacturing and supplier networks.

In closing, we developed a restructuring plan that meets the high standards of the President's auto task force and was approved by the U.S. Bankruptcy Court that permits us to roll up our sleeves and get back to work. Now we can place a singular focus on customers, cars, and the changes we need to make to our culture to

succeed. We want to repay the taxpayer as quickly as we can, and this plan gives us the best chance to do that.

We remain grateful for the government's support during this critical time and we promise to continue to be open and transparent in everything we do every step of the way.

Thank you, Mr. Chairman. I look forward to the questions of the Committee.

[The prepared statement of Mr. Robinson follows:]

PREPARED STATEMENT OF MICHAEL J. ROBINSON

**United States House of Representatives  
Subcommittee on Commercial and Administrative Law  
Committee on The Judiciary**

**Testimony of  
Michael J. Robinson  
Vice President and General Counsel of North America  
General Motors Company**

**Ramifications of Auto Industry Bankruptcies, Part III  
July 22, 2009**

My name is Michael J. Robinson, and I am Vice President and General Counsel of North America for General Motors Company. Prior to July 10, I was employed by General Motors Corporation, then a debtor-in-possession in a bankruptcy case pending in the United States Bankruptcy Court for the Southern District of New York, in essentially the same capacity. Thank you for the opportunity to address your Subcommittee on the topic of the Ramifications of Auto Industry Bankruptcies.

General Motors Corporation filed its bankruptcy petition on June 1, 2009. The circumstances facing the company at that time are common knowledge, and I will not elaborate upon them at length. In brief, following the collapse of Lehman Brothers in September of 2008 and consistent with the substantial dislocation in the credit, housing and other markets at that time, the demand for vehicles in this country fell to levels not seen since World War II. Virtually the entire global automotive industry suffered substantial operating losses. In that environment, General Motors, which was burdened with substantial legacy costs, was unable to implement its existing business plan that provided for funding its transformation through asset sales and access to the credit markets. But for loans extended by the United States Treasury on December 31, 2008 and afterwards, General Motors Corporation would have had no option but to liquidate the company, with catastrophic impact upon its employees, dealers, suppliers and the national economy as a whole.

On February 17, 2009, General Motors Corporation submitted its then current viability plan to the Automotive Task Force of the U.S. Treasury as required by the outstanding Loan Agreement. On March 30, President Obama addressed the nation and announced that the Task Force had determined that the plan was not adequate to assure a viable enterprise that would be able to pay back the outstanding government loans. The administration allowed the company sixty days to develop an appropriate plan. Although the President did not at that time rule out the possibility that the company might restructure outside the bankruptcy process, he clearly communicated that a bankruptcy might be necessary and that, in that eventuality, the government would pursue an accelerated approach. That determination was consistent with the company's view, as expressed in the February 17 Viability Plan and elsewhere, that bankruptcy posed profound risks for any auto manufacturer.

On April 27, 2009, General Motors Corporation launched a bond exchange offer in an effort to address its approximately \$27 billion of outstanding public debt. When that exchange offer expired on May 26 without receipt of sufficient tenders to implement the exchange, the company was left with no alternative to a bankruptcy filing. Moreover, given the large sums required to finance the transformation of General Motors' business, as well as the current state of the capital markets and the outstanding debt to the United States Treasury, the implementation of any transaction other than liquidation of the business clearly required an approach fully supported by the government.

After extensive discussions and negotiations with the Automotive Task Force and its advisors spanning the entire period between March 30 and the end of May, the Board of Directors of General Motors Corporation approved the commencement of a Chapter 11 bankruptcy case to implement the sale of substantially all of the assets of the company pursuant to Section 363 of the United States Bankruptcy Code 11 U.S.C. § 363 to a purchaser created and funded by the United States Treasury on terms set forth in a Master Sale and Purchase Agreement negotiated with the Automotive Task Force. The

Board concluded that the Section 363 transaction offered the only alternative to liquidation of General Motors Corporation and was therefore in the best interests of the company and all of its economic stakeholders.

On June 1, General Motors Corporation filed for bankruptcy in the United States Bankruptcy Court for the Southern District of New York, and the case was assigned to Judge Robert E. Gerber.

Fundamentally, the purpose of Chapter 11 of the Bankruptcy Code is to preserve and protect, to the extent possible consistent with applicable legal provisions, the value of an enterprise as a going concern. There is no doubt the bankruptcy of a major corporation almost inevitably imposes severe hardship on employees, creditors, suppliers, customers and other interested stakeholders. However, by preserving the value of the enterprise, Chapter 11 maximizes the value for each constituency.

The bankruptcy of General Motors Corporation amply illustrates these principles. As of March 31, 2009, as reflected in its last published financial statements, the company had liabilities exceeding \$172 billion. In contrast, the liquidation value of its assets, as reflected in an affidavit and analysis filed in connection with the Section 363 transaction, was \$6 billion to \$10 billion. Furthermore, as of June 1, the company had outstanding more than \$25 billion of secured debt with its assets. As a consequence, in the event of liquidation unsecured creditors, including dealers, suppliers, employees and customers would have received no recovery.

The Section 363 sales transaction negotiated with the United States Treasury was the only viable alternative available to General Motors Corporation to avoid the liquidation scenario. The terms of its approval by the Bankruptcy Court were the subject of extensive negotiations with numerous parties, including the National Association of Attorneys General. As confirmed by Judge Gerber's finding in his written decision, the government was the only source of financing for any alternative as well as the only party that expressed any interest in any acquisition. The basic decision to pursue a sale transaction reflected a determination by the Automotive Task Force that alternative approaches, including in particular a traditional Chapter 11 Reorganization Process, would be unduly risky and expensive for taxpayers. As Judge Gerber stated in his opinion approving the sale, "[a]s nobody can seriously dispute, the only alternative to an immediate sale [was] liquidation—a disastrous result for GM's creditors, its employees, the suppliers who depend upon on GM for their own existence, and the communities in which GM operates. In the event of liquidation, creditors now trying to increase their incremental recoveries would get nothing."

In exchange for the operating assets of General Motors Corporation, the purchaser assumed many of the liabilities of the seller necessary to continue the business and provided 10% of its equity (plus warrants for 15% more) to the seller for ultimate distribution to creditors. Thus, the 363 transaction was highly favorable to the stakeholders of General Motors Corporation. As a result of the 363 transaction, hundreds of thousands of jobs at GM and its suppliers and dealers were preserved. The GM dealer and supplier network was largely preserved. The fundamental viability of the US automotive industry was preserved. Even creditor and other constituencies that will not have a relationship with the purchaser going forward can expect to receive a substantial recovery through the equity to be distributed through the bankruptcy process, depending on the success of General Motors Company. In liquidation, which was the

only available alternative, various creditor constituencies would have received nothing. Although bankruptcy is necessarily a painful process, GM's bankruptcy accomplished the statutory purpose of preserving the value of the assets to the benefit of all constituencies.

Inevitably, given the size and scope of economic interests at stake, not all parties have been fully satisfied with the outcome of the bankruptcy process. As an initial matter, some have criticized the decision to sell assets instead of pursuing a traditional Chapter 11 reorganization process for General Motors Corporation. However, as Judge Gerber found, the use of Section 363 to sell assets in circumstances like those that faced the company is well established. The company lacked financing for an extended bankruptcy case, which presented numerous significant risks. It broke no new ground to pursue a sale of the business on an expedited basis. Again, the Court said it best:

Neither the Code, nor the caselaw. . . requires waiting for the plan confirmation to take its course when the inevitable consequence would be liquidation. Bankruptcy courts have the power to authorize sales of assets at a time when there still is value to preserve—to prevent the death of the patient on the operating table”

Nor is it in any sense unusual that the purchaser chose to assume certain obligations of General Motors Corporation but not others. The government sponsored purchaser, like any purchaser, had an interest in maintaining the business relationships with employees, suppliers, dealers and customers necessary to continue the business as a viable enterprise moving forward. In the negotiations leading up to the transaction, it pursued an express philosophy emphasizing a willingness to assume obligations necessary to the successful operation of the purchasing entity, but not other obligations. In Judge Gerber's words, “[a]rrangements that will be made by the Purchaser do not affect the distribution of the Debtor's property, and will address wholly different needs and concerns—arrangements that the Purchaser needs to create a new GM that will be lean and healthy enough to survive.”

Nevertheless, I take this opportunity to briefly address some of the specific concerns expressed regarding the 363 sale.

The impact of the bankruptcy on dealers has received considerable attention. Dealer restructuring was an essential aspect of GM's viability plan. A strong dealer body is vital to the enterprise. Nevertheless, dealer restructuring is quite painful – for the company, for our customers, and especially for our dealers. GM's current dealer network was largely established in the late 1940s and '50s, before the U.S. Interstate Highway system was built. Because of our long operating history and existing dealer locations, many dealerships now operate in outdated facilities that are no longer located where they can best serve our customers. Many of our dealers operate businesses that have been in their families for generations.

Unfortunately, times have changed. In particular, virtually every knowledgeable observer of the automotive industry has long expressed the view that General Motors had too many dealers. With the current economic crisis, GM no longer had the luxury of relying on the evolutionary approach to address the dealer network pursued in recent years. Indeed, the direction we received from Congress, the current and previous Administrations, the Automotive Task Force, and countless industry analysts and

pundits, was clear and to the point: to remain viable, GM needed to enact a dramatic restructuring, with speed, across all parts of our business. Prior to the bankruptcy filing, GM had roughly 6,000 dealerships in the U.S., compared to 1,240 for Toyota and 3,358 for Ford. Going forward, General Motors Company will still have more dealerships than any of our competitors, including Toyota, Honda, Nissan, Ford or Chrysler.

In recent years, many GM dealers could not earn enough profit to renovate their facilities and retain top-tier sales and service staffs. At the same time, the company sustained very substantial costs to support an uncompetitive network. A right-sized dealer network built around strong dealers will allow us to drastically reduce, and in some case eliminate, many direct dealer support programs – programs such as the incentives paid to the dealer, factory wholesale floorplan support, and the one percent market support for each vehicle. In the long run, the reductions in direct dealer support will result in annual savings of over \$2 billion. Dealer network reductions will also save an estimated \$415 million per year in structural cost savings – items like local advertising assistance, service and training, and information technology systems. In total, the dealer restructuring should result in approximate savings of over \$2.5 billion per year. At the same time, a strong and profitable dealer network can provide the industry's best customer service and enhance the image of our four remaining brands: Chevrolet, Cadillac, Buick and GMC. GM's remaining dealerships will be better positioned to serve their current GM customers, while aggressively marketing to take sales from competitors.

It is well established that debtors in bankruptcy are entitled to reject unfavorable contracts that are a burden on their business. Nevertheless, the company did not pursue this approach as its preferred option. Instead, GM developed a unique wind-down process that we believe is considerably more favorable to dealers. It started with a thorough analysis of every GM dealer in every market throughout the U.S. to assess individual market requirements and dealer performance, which focused on critical objective criteria. The company carefully considered our dealer network coverage in rural areas and small towns versus urban/suburban markets, taking great pains to ensure that minority dealers were considered equitably and proportionally in our process. In fact, the percentage of minority dealers overall may actually increase slightly after the consolidation is completed.

After identifying dealers that would not be retained in the GM dealer network, GM offered such dealers wind-down agreements which, when accepted, permits them to remain in business until October 2010 – the expiration date of their current dealer agreement – to facilitate the disposition of vehicle inventories and provision of warranty service to customers. This allows dealers to exit their businesses in an orderly fashion – for the benefit of GM, our dealers and our customers. The wind-down agreements also offered some financial assistance to smooth that process. In the aggregate, this will be about \$600 million. GM notified dealers about our planning as soon as possible – on May 15, in most cases. While this process is far from painless, we think it is far preferable to an abrupt termination. GM also implemented an appeals process, reviewing approximately 900 appeal requests to date, and acted favorably on 70 to date.

By reducing the number of GM dealers, our remaining dealers will see increased sales throughput at more competitive levels. This will provide a greater return on their investment, especially in metropolitan markets. They will be able to retain top sales and service talent, invest in their facilities and focus more resources on selling vehicles to

people who don't currently own a GM car or truck. Most importantly, they will be able to improve the overall customer experience and retain current customers.

Another aspect of the bankruptcy that has been the subject of comment is its effect on personal injury claims. Like all motor vehicle manufacturers, General Motors Corporation was subject to product liability claims by individuals injured in accidents involving GM products.

As a threshold matter, like every other creditor constituency, product liability claimants benefit substantially from the Section 363 transaction. In a liquidation of General Motors Corporation, they would likely have received no recovery. Moreover, subsequent to the commencement of GM's bankruptcy filing, the government sponsored purchaser agreed to also assume responsibility for claims that may arise by reason of future accidents involving vehicles manufactured and sold earlier. This was consistent with the Automotive Task Force's basic philosophy of accepting responsibility for obligations tied to and supportive of the future operation of the acquired business.

The purchaser did not assume responsibility for existing claims or categories of claims that do not arise from the performance of vehicles. These would include claims alleged to arise from asbestos exposure and other miscellaneous claims. Obviously, the company is sympathetic to injured persons, regardless of the merit of their individual claims. However, to the extent claims have merit, they give rise to general unsecured claims against the bankrupt entity, to be satisfied on a *pro rata* basis with other claims out of available proceeds of the sale. This represents the straightforward application of basic bankruptcy law to the prevailing circumstances.

A number of concerns have been expressed about the use of Section 363 of the Bankruptcy Code to protect the purchaser from successor liability under state law. Ultimately this presents a question of law, which we believe was correctly decided by Judge Gerber in the GM bankruptcy case, following decisions rendered by both the Bankruptcy Court and United States Court of Appeals for the Second Circuit in the *Chrysler* Chapter 11 case and other consistent opinions. However, there is also a strong level of common sense underlying this outcome. In the Section 363 transaction, the government funded purchaser provided financial support and consideration that substantially exceeded the objective value of the assets acquired, to the benefit of all creditors. Tort claimants, like all other creditors, will receive substantial benefit from that consideration under a Chapter 11 liquidating plan that will need to be approved as appropriate by the Bankruptcy Court. To permit such claimants to also pursue the purchasing entity would, in effect, require the purchaser to pay twice, to the benefit of a single class of creditors and to the detriment of all others.

Finally, I would like to comment briefly on environmental issues related to the Section 363 transaction. Under the relevant agreements and the terms of the Sale Approval Order, new General Motors Company has assumed the legal obligations that flow with properties it has acquired. With respect to properties that remain with the Chapter 11 debtor, the government has provided substantial funding, with a budget of \$1,175,000 to support administrative and wind down costs including environmental remediation. Accordingly, the debtor's remedial obligations should be appropriately discharged.

In conclusion, bankruptcy is always an unfortunate event and we recognize and regret the hardships it has imposed upon many. However, with the support of the United

States government, General Motors Corporation was able to implement a speedy process which preserved and enhanced the value of its assets to the substantial benefit of the national economy and all of the economic stakeholders. In short, the system worked. We are grateful to the government for its assistance and I appreciate the opportunity to address you today.

I look forward to your questions.



Mr. COHEN. Thank you for your testimony, Mr. Robinson.

And you did recognize Mr. Miller, whom we have had before our Committee before. But Mr. Miller is always kind of different in his testimony. The last time, because of airplanes, he wasn't able to be here; so we had his picture and his voice. Now we have had him in person, but not testifying—but his great gray matter with us, so we appreciate that.

Mr. MILLER. Thank you, Mr. Chairman.

[The prepared statement of Mr. Miller follows:]

PREPARED STATEMENT OF HARVEY R. MILLER

Testimony of

**Harvey R. Miller**<sup>1</sup>

before the

**Subcommittee on Commercial and Administrative Law**

of the

**House of Representatives Committee on the Judiciary**

111th Congress, 1st Session

for Hearing on

**“Ramifications of Auto Industry Bankruptcies, Part III”**

July 22, 2009

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<sup>1</sup> Senior Partner, Weil, Gotshal & Manges LLP, New York, New York. The views expressed in this testimony are expressed solely on behalf of myself and not on behalf of any other person or entity.

I greatly appreciate the opportunity to testify in these oversight hearings as to the actions taken by General Motors Corporation (“GM”) in connection with GM’s commencing cases under chapter 11 of the Bankruptcy Code and the role the United States Government played in connection with the chapter 11 cases, including the decision to close certain GM dealerships.

I am a practicing attorney and senior member of the international law firm of Weil, Gotshal & Manges LLP (“WGM”) that maintains its principal office in New York, New York. For the past 50 years,<sup>2</sup> I have specialized in matters relating to debtor-creditor relationships with an emphasis on restructuring, rehabilitating, and reorganizing distressed business entities. I created the Business Finance and Restructuring group at WGM. I have represented debtors, secured and unsecured creditors, trustees, and creditors’ committees and have served as a trustee in cases under the Securities Investor Protection Act of 1970 (15 U.S.C. 78aaa *et seq.*).<sup>3</sup>

I am currently an Adjunct Professor of Law at the New York University School of Law, where I have taught a seminar on chapter 11 bankruptcy and reorganization law since 1975. I also am an Adjunct Lecturer in Law at Columbia Law School, Columbia University, where I have taught a course on Corporate Reorganization and Bankruptcy Law for the past ten years.

It is my understanding that the Subcommittee is desirous of understanding the circumstances concerning the commencement of chapter 11 cases by GM, its restructuring efforts, the decision to restructure its dealer network, and the role that the United States

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<sup>2</sup> During the period of September 1, 2002 to March, 2007, I was a Vice Chairman and Managing Director of Greenhill & Co., LLC, an investment banking firm located in New York, New York.

<sup>3</sup> Since approximately 1973, I have been a conferee and member of the National Bankruptcy Conference and I also am a fellow of the American College of Bankruptcy.

Government has played in the chapter 11 cases. I am certain that a review of the economic realities and circumstances that precipitated the commencement of GM's chapter 11 cases and the sale of substantially all of GM's viable assets to a U.S. Treasury-sponsored entity pursuant to section 363(b) of the United States Bankruptcy Code, 11 U.S.C. § 101 *et seq.*, will demonstrate that the sale and the restructuring that resulted, including the adjustment of the dealer network, was in the best interests of all economic stakeholders as well as the public interest.

**The Events Leading Up to the Commencement of General Motors' Chapter 11 Cases**

In December 2008, GM was confronted with a crisis situation as its liquidity dried up. Despite its efforts to alleviate its growing illiquidity, the consequences of the collapse of Lehman Brothers Holdings Inc. in September 2008 caused a freezing of the credit markets. As a result, GM had to turn to the only available source of liquidity, i.e., the United States Government, and more specifically, the United States Department of the Treasury ("U.S. Treasury"), to prevent the immediate shutdown and liquidation of this huge, American-based enterprise. The federal government/U.S. Treasury recognized there was a compelling need to finance GM's ongoing operations. Accordingly, it entered into a Loan and Security Agreement with GM on December 31, 2008 ("LSA"), which anticipated an emergency secured loan and advance in the aggregate amount of \$13.4 billion. At the time the first advance of \$4 billion was made on December 31, 2008 pursuant to the LSA, it appeared to be the belief of the U.S. Treasury that the loans would be repaid as GM achieved the milestones provided for in the LSA.

Unfortunately, as 2009 progressed, the economic circumstances deteriorated, particularly as they related to the automotive industry. Sales continued to deteriorate, and liquidity remained a major problem. In short order, the entire \$13.4 billion was drawn down, but nevertheless, was insufficient to enable the continuation of GM's operations. Although the LSA

required GM to develop a proposal to transform its business and demonstrate future viability, it was ultimately determined that the viability plan GM submitted to the automobile task force appointed by President Obama (“Presidential Task Force” or “Automobile Task Force”) was not sufficient for GM to attain sustainability and ultimately profits. President Obama announced on March 30, 2009 that the viability plan did not justify a substantial new investment of taxpayer dollars.

The crisis continued as the Presidential Task Force became intensely involved in the affairs of the automotive industry. Consistent with its obligations, GM honed its viability plan to meet the directives of its largest secured creditor and provide a deeper and faster restructuring of its business.

Once again, economic circumstances pre-ordained GM’s actions. Its efforts to avoid the consequences of seeking relief under the Bankruptcy Code were in vain as a proposed debt for equity bond exchange was rejected by bondholders. The terms of this public exchange offer had been the subject of extensive negotiations between GM and the U.S. Treasury. When the exchange offer was launched, GM understood that at least 90% of the aggregate principal amount of outstanding bonds were required to be tendered in order to achieve a sufficient level of debt reduction to meet the viability requirement. On May 26, 2009, the exchange offer expired without achieving this threshold of required tendered acceptances.

To avoid a shutdown and termination of GM’s business, GM needed to borrow, and the U.S. Treasury loaned and advanced, an additional \$6 billion. June 1, 2009 was established as a watershed date for an effective plan to restructure the business of GM. As that date approached, it became clear that GM had no alternative but to initiate chapter 11 cases to maintain the going concern value of its assets. In doing so, GM and the U.S. Treasury had the

benefit of the results that had been achieved in the chapter 11 cases that had been initiated by Chrysler LLC and its affiliates on April 30, 2009.

**The Chapter 11 Process and the Reduction in Dealerships**

The essence of restructuring is to preserve going concern values and create a viable economic unit. This process typically involves the contraction of the overall business enterprise of a chapter 11 debtor to its core business and the concomitant elimination of operations, facilities, executory contracts, and unexpired leases that provide no benefit or contribution to ongoing future viability. This is the normal process that occurs in the restructuring and reorganizing of a chapter 11 debtor.

GM's chapter 11 cases were more complex and difficult given the nature of GM's business and its dependency on consumers. It was the almost universal opinion that a traditional chapter 11 case would not be successful as consumers would be hesitant and ultimately decline to purchase cars and trucks manufactured by a company in chapter 11 with an uncertain future. Consumers seek reliability and value when they purchase an automobile or truck. Consumers are concerned about residual value, replacement parts, warranty obligations, servicing, and maintenance of the manufacturers' products, all of which are critical to the preservation of the value of the assets. To preserve this value and instill confidence on the part of consumers, speed was of the essence.

Regrettably, bankruptcy reorganization is a zero-sum game. It has dual objectives: (i) creating a viable economic unit and (ii) providing recoveries to those creditors that have a cognizable economic stake in the assets based on the value of the debtor. Chapter 11 bankruptcy entails a determination of reorganization value, which is sometimes referred to as the going concern value of the debtor entity.

The only feasible manner of preserving GM's going concern value was to propose and implement a sale of all of GM's viable assets pursuant to section 363(b) of the Bankruptcy Code ("363 Transaction"). Specifically, the 363 Transaction was designed to continue the business represented by the assets that were sold that will make the U.S. Treasury-sponsored purchaser (sometimes referred to as "New GM," now the General Motors Company), a linchpin of the domestic automotive industry so that the United States can once again assume its place as the domicile of one of the leading automotive manufacturers in the world. The 363 Transaction provided the only means for GM to preserve and maximize the value, viability, and continuation of GM's survivable business and, by extension, preserve and provide jobs for GM's employees and its dependent supplier entities, and enhance the interests of all such economic stakeholders. Notably, the 363 Transaction was only made possible because it was a critical element of the objective adopted by the United States Government to preserve the domestic automotive industry, avoid systemic failure in the automotive industry and other sectors of the economy, as well as offer hope for hundreds of other businesses and their thousands of employees that supply or otherwise are dependent on GM.

The purchaser of assets pursuant to a section 363(b) sale typically plays a dominant role. The purchaser's objective generally is to acquire a viable business. Therefore, the purchaser determines which assets it will purchase and which liabilities it will assume that will contribute to the future success of the business to be created. Section 363(b) sales are the daily grist of bankruptcy courts. In today's economic environment, secured creditors usually dominate the sale process as they possess the largest economic stake. The U.S. Treasury, as GM's largest secured creditor as well as GM's post-chapter 11 financier to the extent of \$33.3 billion, acted as any other secured creditor would in selecting the assets it would purchase and

liabilities it would assume, and the terms and conditions under which it would purchase the assets. This was the only manner in which the going concern value of the assets that were being purchased could be preserved for the benefit of the direct economic stakeholders, including GM's 235,000 employees worldwide, that includes 91,000 domestic employees, the overall supplier industry, and its employees.

No purchaser of assets of a chapter 11 debtor would purchase assets that would not contribute to the ultimate success of the successor business using the purchased assets. It was incumbent on GM to provide an attractive package of assets to the U.S. Treasury-sponsored purchaser. As stated by Mr. Michael J. Robinson, the Vice President of GM's North American operations, in order to achieve economic viability, a condition precedent for the U.S. Treasury-sponsored purchaser, GM had to analyze its dealer network in conjunction with representatives of the Presidential Task Force to determine the best way in which to make New GM a viable, profitable Original Equipment Manufacturer. It was patent that a leaner, more profitable dealer network with higher annual vehicle sales per dealership was critical to reducing GM's staggering dealer support costs and creating an economically viable New GM. The failure to achieve the objective of a viable economic business would have imposed on the U.S. Treasury-sponsored purchaser unsupportable obligations that would continue some of the problems that caused the demise of Old GM and might cause the failure of New GM and an even worse catastrophe.

GM conducted a comprehensive, objective, and quantitative evaluation of each dealership, including, among other things, minimum sales thresholds, customer satisfaction indices, working capital needs, profitability, whether a dealership sold competing non-GM brands, dealership location, and other market factors. The substantial majority of GM's dealers were offered Participation Agreements, which provided for their dealership franchise agreements

to be assumed and assigned to New GM, subject to certain modifications. Over 99% of the dealers that were offered Participation Agreements signed and returned such agreements.

The remaining dealers that were not offered Participation Agreements were not to be retained as part of the dealer network of New GM. Nevertheless, GM did not seek to abruptly reject and terminate their dealer franchise agreements with these dealers. Instead, GM offered these dealers the opportunity to accept Wind-Down Agreements which provided such dealers with substantial monetary payments and allowed them to remain in business until October 2010 and sell down their inventories in an orderly fashion while continuing to provide warranty and other services to their customers with the continued support of New GM. The Wind-Down Agreements were designed to help minimize the financial and other hardships that would have been associated with an immediate rejection and shutdown of the dealerships. Indeed, GM provided a review process that could be initiated by aggrieved dealers. As of the beginning of July 2009, over 845 dealers initiated such review, and GM did reverse at least 60 decisions and agreed to retain such dealers. Not surprisingly, over 98% of such dealers accepted and executed the Wind-Down Agreements.

### **Conclusion**

Chapter 11 is not a painless process. It results in losses and hardships to many constituencies. But, as Congress recognized when it enacted the United States Bankruptcy Code, it is in the best interests of the nation to provide a process for distressed businesses to preserve and protect going concern values and enable restructured businesses to go on and achieve success. The negative effects of the contraction of the number of dealers as well as the liabilities not assumed by the U.S. Treasury-sponsored purchaser have to be balanced with the fact that the 363 Transaction permitted thousands of dealerships to survive while providing an orderly wind-



down of those dealerships not being retained and enabled the rehabilitation of a business that hundreds of thousands rely upon for their survival. GM did everything in its power to provide a soft landing for discontinued dealers by helping to ease the disruptions and financial hardships that would otherwise result from an abrupt shutdown and rejection of its dealer contracts. It would have been foolhardy for the U.S. Treasury-sponsored purchaser to purchase assets and operate a business with the same burdens that caused the demise of GM. Indeed, it would have resulted in a failure of the U.S. Treasury to protect the ability to recover the taxpayers' investments in New GM. The alternative to the exercise of the sound business judgment by GM and the U.S. Treasury-sponsored purchaser would have been the liquidation of GM – and *all dealerships* would have terminated, including the thousands of dealerships that otherwise are continuing to operate and prosper under New GM.

Once again, I want to express my appreciation for the opportunity extended by the Subcommittee to testify at this Hearing.

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Mr. COHEN. Thank you. A great reputation in the bankruptcy litigation area.

I will now recognize myself for questioning, and we will be limited to the 5-minute rule as well. I would first like to ask Mr. Robinson.

There were some questions in the opening statement by the Ranking Member about bankruptcy and how this came about and all the capitalism, socialism, et cetera.

Why did General Motors come to the United States Government, President Bush at the time, and say, Please help us? What were the causes in the economy that caused General Motors to come to this position?

Mr. ROBINSON. First of all, Mr. Chairman, I don't mean to argue with Mr. Franks, but we are capitalists. I can assure you of that.

Secondly, we—as the facts have been revealed through various processes, hearings in front of Congress and, of course, in the bankruptcy court itself, there were no other options. The capital markets had dried up. We had no other opportunities—

Mr. COHEN. The capital markets dried up. You couldn't get borrowed money?

Mr. ROBINSON. There was no way to borrow money.

Mr. COHEN. Something happened during the previous Administration where they didn't have regulations or something, and the country was about to go kerflooy?

Mr. ROBINSON. I don't think of it in terms of Administrations; I think of it in terms of the financial markets. But, yes, during the 2008 economic crisis, the financial market crisis, the housing crisis, there were sufficient reasons for the market to have done what it did; but the practical fact of the matter is, there was no capital from which we could sustain the business.

Mr. COHEN. And these conditions also affected dealerships, right? Certain dealerships would have had problems because they couldn't access to capital and financing?

Mr. ROBINSON. It affected everybody.

Mr. COHEN. Ms. Van Der Wiele and Mr. Orr, with Chrysler, we have a situation in the mid-South area, greater Memphis area, with a minority dealer. They had financial problems because they couldn't get financing, et cetera.

I spoke to you yesterday and asked you about minorities that are affected. While I am concerned, indeed, about all minorities, in the particular situation in my jurisdiction, as an African American dealer, is there a different effect among African American dealers than there was with either Latino men or women in terms of Chrysler?

Mr. ORR. Mr. Chairman, there was no effect in terms of any of the traditional minority categories with regard to our rejection decision for minority dealers. In fact, it is exactly the same whether you are a minority dealer or a mainstream dealer.

Mr. COHEN. So you are saying the percentages are exactly the same?

Mr. ORR. The percentages are exactly the same. Seventy-five percent of our dealers were saved; 25 percent of our dealers, unfortunately, we had to reject. The exact percentages regarding those numbers are the same for minorities.

Mr. COHEN. The same for African Americans?

Mr. ORR. The same for African Americans.

Mr. COHEN. Okay.

Mr. Robinson, is it the same thing for you?

Mr. ROBINSON. Pretty much, Mr. Chairman. Our ratios are a little bit different. Actually, in an incremental way, the minority population of our dealerships actually fared better than the general population of our dealerships. I think the percentage was—80 percent, I think, of our minority dealer population will remain after the 1,300 or so dealers get the wind-downs completed, and I think 76 percent of our overall dealer population survives that process.

Mr. COHEN. Mr. Miller, welcome. The issue of tort liability is one that is before this Committee and one that we will be hearing about. GM, separate from Chrysler, is accepting certain liability, but only for post-petition tort claims.

Why not pre-petition tort claims?

Mr. MILLER. The question, Mr. Chairman, related to the assumed liabilities that the purchaser would undertake as part of the asset sale. There was a substantial negotiation with the U.S. Treasury representatives and the auto task force in connection with the product liability claims. And as you must know, during the course of the hearings before the Bankruptcy Court, there was a compromise agreed to in which the assumption of product liability claims was greatly increased.

It was a question of survivability of the successor corporation or business.

Mr. COHEN. You think that that would have been in jeopardy if they would have accepted the pre-petitioned tort claims? Is it that great of a potential—

Mr. MILLER. Mr. Chairman, it is a question of how many liabilities does the purchaser assume without going into that dangerous area of being not feasible as a business operation.

As pointed out by my colleague, my learned friend Professor Baird, in his statement, there is no assurance of feasibility or success, even now after this sale; and you are on a very difficult path. As Mr. Robinson said, bankruptcy is painful and you have to draw the line at some place.

Mr. COHEN. Professor Baird also suggested that tort claims, if I quote him, are among those that should be protected with a super-priority lien.

Mr. MILLER. I understand that, Mr. Chairman. And the problem with creating super-priority liens is when do you stop doing that? And if you create enough super-priority liens, there can never be a bankruptcy reorganization, because you will never be able to sustain the cost of that restructuring process.

Mr. COHEN. Let me give myself a few extra seconds here to ask you this.

In your long experience, in most cases where there are large bankruptcies like this—and there is a question about civil—doesn't most of the liability still attach or is the liability extinguished for tort claims?

Mr. MILLER. In most cases, the liability for tort claimants is extinguished; it remains with the old company in the context of a section 363 sale.

If it is a traditional Chapter 11 in which there is a plan of reorganization and it is a negotiation over a long process, it may be different because of the bargaining. You have to take into account the assets you are dealing with.

In the context of GM and, I assume, Chrysler you are dealing with a wasting asset. If you compare, for example—if I can refer to the Delphi case, which is about to enter its fourth year of bankruptcy if it doesn't come out, you had a company that went into Chapter 11. At the time it went in, there was a substantial basis to think that that company was solvent. During the course of the bankruptcy, it has turned into an insolvent company—in fact, administratively insolvent.

So that a traditional Chapter 11 in the context of the economic circumstances we are in today is not feasible for a large company.

Mr. COHEN. Thank you, Mr. Miller.

I now recognize the Ranking Member of the Subcommittee for 5 minutes, Mr. Franks.

Mr. FRANKS. Thank you, Mr. Chairman.

Ms. Van Der Wiele, I might go ahead and address this both to you and Mr. Orr. As I understand it, there was a significant effort on the part of the Chrysler earlier on, when they began to see some of the dealers have—tell the dealers that they were going to have to be terminated, that you tried to use some of the Treasury money to assist them and that there was some resistance on the part of Treasury to that end; is that correct?

Mr. ORR. Mr. Franks, I am not exactly sure to what you are referring. You are talking about the early stages of the bankruptcy?

Mr. FRANKS. Yes. From the Treasury itself, that there was a resistance in the bankruptcy process where you tried to—in the process that you tried to help some of your dealers, much the same way as Mr. Robinson has said, where General Motors made some efforts to assist them, that you also tried to do the same thing and that there was resistance on the part of the Treasury; is that correct?

Mr. ORR. I think I know to what you are referring, Mr. Franks.

Actually, we received support of Treasury in trying to help our dealers. In the case we recognized that some of our dealers were going to have problems obviously with bankruptcy filing and our financier, where two-thirds of our dealers—Chrysler Financial announced on the date that we filed, April 30, that they would no longer be providing wholesale financing to our dealers. We had begun on April 23 to go back and seek alternative wholesale financing—ironically, through GMAC—to benefit our dealers for wholesale flooring; and we also put in place in the case a structure, a reallocation program, that assisted our dealers with reallocating the inventory, the vehicles that they had on their lots, to other dealers that were going forward.

The reality is that Treasury was somewhat supportive in our efforts to do that and recognizing that it was for the benefit of both the dealers that were rejected and the dealers that would be—75 percent going forward that would be assumed.

Mr. FRANKS. If the airline companies came to you now and asked you, what were the worst things and the most political things to which the President and the auto task force subjected Chrysler since it became involved—I know it is a very loaded question, but I hope you will be as candid as you can.

What would you try to redirect the airlines' focus on? What would you warn them about? What would you say, be careful here, be careful there?

Mr. ORR. Well, honestly, Mr. Chairman, my role as counsel to the company was focus on the legal doctrine, the law and the case law. The political aspects, I will leave to—another day to someone else.

Mr. FRANKS. Let me shift gears.

Mr. Robinson, if the airlines came to you and asked what things the Administration and the auto task force had done that most harmed your ability to raise private capital or attract private ownership, going forward, what would you tell them?

Mr. ROBINSON. Well, I wouldn't—I wouldn't get into a political discussion, quite frankly. I think the reality for us is that there was a benefit to us, quite frankly, in some of the objectivity with which the task force took the task of evaluating our business plan and forcing us to take harder looks at some things that we needed to do to be successful in the long term.

So, to the contrary, I didn't view this—my exposure to it, anyway—as not a political process so much as it was an objectivity exercise with some soul searching from the outside.

Mr. FRANKS. So your perspective is that the government's—of the things that they pressured you or didn't pressure you to do, is all objective; and it all worked out perfectly for you?

Mr. ROBINSON. I think we made the business decisions we had to make without any political interference.

Mr. FRANKS. Does that include firing of Mr. Wagoner and the purging of your board? Do you think that was a good thing?

Mr. ROBINSON. I didn't have anything to do with it. I will tell you I heard the testimony yesterday and I accept it for what it is.

Mr. Wagoner is somebody I know personally. I know what kind of person he is.

But I also heard the criticism that we didn't move fast enough, far enough and aggressively enough; and I accept the criticism of the Treasury for what it was.

Mr. FRANKS. As a capitalist, does it concern you that government can come in and fire your CEO and purge your board? Does that not concern you some?

Mr. ROBINSON. Well, we—we don't intend to be in the business of being run by the government. I think the government has made it clear they want us to be successful so they can get out of the car business as an investor. So we want to oblige them as soon as we can.

Mr. FRANKS. I don't want to be too insistent, but I mean, I believe you when you say you want to be a capitalist. I really do.

But obviously this has put you in a compromised position. And I am sorry that it has, because I do think that the gas prices and some of the pressure in capital markets made impossible circumstances for a lot of you.

But the fact remains that our government has come in and seized a lot of power there. If we can't come to that conclusion together, we are on a different planet. And I am sure that it has to concern you some that capitalism is challenged here in this way for government, as in other socialist environments, has tried to exert force over the economic mechanisms.

Does that not concern you as a capitalist?

Mr. ROBINSON. Going to the government for a loan was not our first choice. We were in the position we were in because there were no other capital markets available to us. And having been through this process, I think we have made most of the opportunity that has been given to us.

It is what it is, sir.

Mr. FRANKS. Thank you, Mr. Robinson.

I yield back, Mr. Chairman.

Mr. COHEN. Thank you, Mr. Franks.

I would now like to recognize the gentleman from Michigan, the distinguished Chairman of this Committee, Mr. Conyers.

Mr. CONYERS. Thanks, Chairman Cohen.

The interesting thing about these hearings is that you get testimony all over the spectrum. We get it. I just hope that you leaders here in the first panel can just stay quietly around to listen to some of the other testimony.

The dealers are going to be hollering their heads off about this. I want you to examine with us some of the unfairness and some things that may be able to be rectified. So I don't want you to, you know, leave the room and go to your commercial flights, but that you stick around with us and let's wade through this hearing today. I think it is pretty important.

I notice that my colleague, Carolyn Cheeks Kilpatrick, is here. I am sorry that she can't ask any questions. She knows how strict the rules are in Judiciary.

Ms. KILPATRICK. I accept them.

Mr. CONYERS. And, of course, Sheila Jackson Lee is always around, and under these circumstances, she can't even say anything.

So here is what I am trying to do. Here is what I am trying to get out of these two excellent hearings that have been held. Is there any way we can cushion some of the problems of the accident victims, of the dealers themselves, of the suppliers? Are there some strategies that we can consider that are not legislative? We are not trying to pass some more laws in this.

How open are you to—all four of you on this panel, to that kind of a concept?

Mr. COHEN. Can we get a witness?

Ms. VAN DER WIELE. Mr. Chairman, I think that certainly—as it respects the dealers, I think that there is a good possibility to have discussions in a nonlegislative context. I believe that Mr. Press, who has testified here before, has initiated some of those discussions; and we support continuing those discussions.

Mr. ROBINSON. Mr. Chairman, General Motors—as accelerated as all this timing has been for all of us, General Motors has engaged the dealers as Chrysler has, through the NADA in particular. We think there are a lot of possibilities available to us. We have been very interested in having those discussions move forward.

We have got a number of ideas to do things in addition to the things we have already been done, which is, quite frankly, a lot beyond what normal bankruptcy would allow us to do; and we are certainly interested in sitting at the table with the representatives of NADA and talking, in addition, with any individual dealers that have an individual point of view about their circumstances.

We have had an appeals process to address some of the concerns that Chairman Conyers has mentioned. We have attempted to soften the blow with wind-down dealers, with a substantial financial package, some of which they have already received; and others have asked if they can accelerate that process.

We have actually had a few dealers in the last couple of weeks ask if they can get the wind-down package although they were offered continuation agreements. I think we have had nine or ten of those that have come to my attention.

So we are trying to work with the dealers. We will do that and continue to do that, but we have to work through a mechanism that allows us to deal with the entire dealer population; and we prefer that to be NADA.

Thank you, sir.

Mr. CONYERS. Mr. Orr, Chrysler has taken a little harder line in the kind of discussion that I am outlining. You folks have terminated your dealers, period, and up here on the panel we are beginning to distinguish—and this is not unusual, but even after Trent Franks went into this great soliloquy about Chrysler, you guys are toeing a tougher line.

Can you look at this with us? And maybe as you listen to some of the other discussion from the scholars and the dealers, maybe we can loosen up a little bit.

Mr. ORR. Mr. Chairman, on behalf of Old Carco, our approach was necessitated by a little bit of a difference in terms of both the structure of our dealer relationship—Chrysler had legacy perpetuity agreements; that is, they did not terminate on a certain date, they went on and on and on. The only time to reject those agreements was in the course of the bankruptcy pursuant to section 365 of the Bankruptcy Code.

In addition, our purchase was with an ancillary third-party purchaser, Fiat Group, now New Chrysler. We don't even own the name anymore; we are called Old Carco. So under the terms of our purchase agreement, our purchaser had the right to select which assets, including those assets in the dealer network it chose to purchase.

So the structure of our deal was a little bit different, and perhaps that results somewhat in the perception that we are taking a little bit harder line. Our requirements in both the naming of our purchaser and the nature of our transaction were different.

However, to the extent Ms. Van Der Wiele has spoken on behalf of the new company, I think there is some commonality in terms of an expression going forward with the new company. It would not benefit dealers to talk to me. We are Old Carco. We do not manufacture cars. They are rejected dealers on my behalf.

Mr. CONYERS. Well, so you were legally forced to take what appears to be a little bit tougher stance than this wind-down. I hope you are right. I hope the discussion bears up the position that you are sharing with us today.

Mr. ORR. Well, respectfully, Mr. Chairman, I believe the case law, both *Lionel* and *Bildisco*, regarding rejection and the obligation of the debtor to exercise its fiduciary duty regarding burdensome contracts, was substantiated both by the Bankruptcy Court,

the Second Circuit Court of Appeals, and implied by the U.S. Supreme Court's implicit rejection issue of stay into our transaction.

In fact, of the 789 dealers that Old Carco rejected, only one dealer has taken an appeal of the rejection order opinion, and that appeal is pending.

Mr. CONYERS. I know that, but citing all of these authorities that you had to be tough doesn't change my position at all.

Mr. ORR. I understand. I understand.

Ms. VAN DER WIELE. Mr. Chairman, if I could point out, Chrysler Group, the new company, has made an effort to provide a soft landing to the rejected dealers. It has taken its promise to redistribute all of the vehicle inventory, parts, and special tools; and as I said before, it is willing to discuss some type of nonlegislative solution, and it has already offered to dealers the opportunity to provide total transparency in the dealer selection process for that individual dealer. And in addition to that, it is willing to consider a dealer for further business opportunities with Chrysler Group.

Mr. CONYERS. Mr. Chairman, just concluding, if you pulled us all in a back room after these hearings—and we have all heard each other in the way that this is going on—and you brought in coffee and locked the door, I think we could work something out that is considerably more favorable to the people that are going to have to feel this pain.

And I just want all of you to know that that is where we are all coming from. We would include Kilpatrick and Jackson Lee and everybody—and Coble and, of course, Trent Franks, by all means—and we could probably get somewhere, maybe sandwiches later on after the coffee runs out.

Mr. ISSA. I will do the sandwiches.

Mr. COHEN. Thank you, Mr. Chairman. I appreciate the suggestion.

I would like—before I recognize Mr. Jordan who, I think, will be next on the questioning, I would like it if the four of you would be kind enough to stay, if you can, after your panel to hear the next panel, and possibly come—because Starbucks is being ordered. But if you could stay, it might be very helpful to hear the testimony, et cetera.

Mr. Jordan, you are recognized for 5 minutes.

Mr. JORDAN. Thank you, Mr. Chairman. I want to thank the witnesses for being here today and thank you for the role your respective companies have played in the United States of America.

My dad, a 30-year worker at General Motors in Dayton, Ohio, put three kids through college working for that company, so we do appreciate that.

But I want to go, Mr. Robinson, back to where my colleague, Mr. Franks, was with his questioning, this interaction between the task force and General Motors.

Mr. Bloom went to great lengths yesterday to describe that, to say that General Motors makes decisions about how the company operates, not the auto task force, even though—as Mr. Franks pointed out, even though the former CEO was told to take a hike by the government, even though the government is the majority owner of the company, even though the government controls the board, even though Fritz Henderson said 2 weeks ago in an inter-



view that he is on a, quote, “short leash” in running the company and has to deal with the task force on a regular basis.

You seemed to indicate that you agreed with Mr. Bloom’s depiction of how that interaction takes place. Give me your thoughts on how that works out, because I think a lot of Americans, a lot of taxpayers, who now own the company, would look at the facts and say, it looks like these 10 guys on the auto task force, who have no experience in the auto dealer business, no experience in the auto manufacturing business, are actually running the company.

Mr. ROBINSON. Well, the best way I could answer that, Congressman, is that in my experience—and I am not in every conversation, by any means; I certainly am not. But my understanding from the people that are in a lot of the conversations that have taken place over time is that the description he gave you is a very accurate description of the way I understand it has worked.

Mr. JORDAN. Isn’t it true that the auto task force had to sign off on the restructuring plan, so in the end they gave the thumbs up or thumbs down to the plan that included which dealerships would be closed, which dealerships would remain open, and just as importantly which manufacturing facilities would be closed and which ones would remain open?

Mr. ROBINSON. Well, you have asked a couple of questions that contradict each other in terms of what the answer would be that I give you.

They absolutely reviewed the restructuring plan in the aggregate. There is no question about that. To my knowledge, they did not review individual dealerships. They did not review individual plants.

Mr. JORDAN. But that is my point. Same difference. If they are going to sign off on the whole plan, which includes which facilities are going to close on the manufacturing side and which dealerships are going to close, which are going to stay open, they, in effect, made a decision on the final restructuring plan. Is that right?

Mr. ROBINSON. They looked at aggregate numbers as far as I can tell. I don’t think they say individual—

Mr. JORDAN. Let me ask you this question. Were there previous plans submitted to the task force?

Mr. ROBINSON. I believe so, yes. We had a February 17 mandate to provide a plan to the task force—

Mr. JORDAN. How many plans were before the task force?

Mr. ROBINSON. At least two, one on February 17 and then one subsequent to the President’s comments on March 30, that was provided to the task force consistent with the President’s direction.

Mr. JORDAN. So the first plan that comes before the auto task force, they said, We don’t like this?

Mr. ROBINSON. Correct.

Mr. JORDAN. And there could have been dealerships in that plan, manufacturing facilities in that plan that were slated to stay open that in the subsequent plan, the final plan, the one adopted that are now closed?

Mr. ROBINSON. That is mathematically true.

Mr. JORDAN. Is there—can the public have access to that first restructuring plan? Is that public knowledge?

Mr. ROBINSON. No it is not. It is confidential business information.

Mr. JORDAN. So the taxpayers who are now paying for the company, we may have had, in fact—and this is back to the point. If GM is running the affairs, the first plan that was submitted to the task force could, in fact, have included for example the GM manufacturing facility in the Fourth District of Ohio in Mansfield, it could have said that facility should stay open and the auto task force says, We are saying no to that plan?

Mr. ROBINSON. I don't know whether it did or it didn't. But it could have. I don't know.

Mr. JORDAN. Do you think that is some information that the taxpayers of the country would like to see and should have a right to see?

Mr. ROBINSON. I can't answer that, but I can tell you—

Mr. JORDAN. I know there are a lot of people in Mansfield, Ohio, a lot of people I have the privilege of representing, who would like to see that.

Mr. ROBINSON. I can certainly understand that, sir. But I can tell you this: that our own management, confronted with the rejection of that initial plan, came to the conclusion the government was right in forcing us to take another hard look—

Mr. JORDAN. Of course they are right. They are paying the bill. You had to come to that conclusion. It is the same conclusion that Kent Lewis came to when Ben Bernanke and Hank Paulson told him, You either go through with the Merrill Lynch acquisition or you are gone and your board is gone.

You have to come to that conclusion. That is why it is important for the public to be able see what took place, what was in that first restructuring plan—a great example of the fact that the auto task force is running the company; it is not GM who is running the company.

Mr. ROBINSON. I would have to disagree with you, sir, on that. I understand your point—

Mr. JORDAN. But the facts, I think, support my conclusion.

Mr. ROBINSON. Well, the fact is that they provided a level of objectivity in reviewing a plan that we thought was adequate, and they pointed out the inadequacy of it which—

Mr. JORDAN. A level of objectivity from 10 guys who had never been in auto manufacturing, had never been in the auto dealership business.

This is the problem when you start down this road where you have this kind of unprecedented involvement of the government in the private sector, back to Mr. Franks' important point that he made in his opening statement.

Mr. COHEN. Mr. Miller, do you seek recognition to respond?

Mr. MILLER. If I might, Mr. Chairman, I would like to add some perspective to the concept of capitalism and private capital. Mr. Franks referred to Mr. Wagoner's departure.

You have to remember the government was a creditor for, I believe, about \$19.4 billion as a secured creditor. The government acted in the same manner as any secured creditor in a distressed situation; and it is not unusual in those situations for the secured creditor in that situation to say, we have lost confidence in the

CEO. And in many of those situations what happens is, either the CEO is retired or a chief restructuring officer is appointed at the suggestion of the secured creditor. And that is just normal debtor/creditor relationships, and it is the secured creditor who has largest economic stake.

And when you look at a company like GM, which had \$19.4 billion of outstanding secured debt, the ability to get any kind of additional capital—nobody would lend money unless it could prime the government. And putting aside the fact that there was no private capital, since Lehman went down, from September 15 on through the balance of the year and into 2009, what was being done was not the government acting as this great 1,800-pound gorilla, or whatever you want to call it; it was a secured creditor trying to protect its economic investment in this company.

Thank you, Mr. Chairman.

Mr. JOHNSON. Would the gentleman yield?

Mr. COHEN. The Chairman always recognizes the distinguished gentleman from Georgia.

Mr. JOHNSON. Thank you, Mr. Chairman. And again I appreciate your holding this hearing.

I wanted to ask you, sir, do you believe that the auto manufacturers had to be bailed out by the taxpayers of the United States of America? Was that a good decision or was it a bad decision?

Mr. JORDAN. If you are asking if I supported the bailout, I did not. I did not vote for the initial \$700 billion bailout which—the funds were taken from that to give that, so I did not support that.

Mr. JOHNSON. Let me ask you about the auto bailout, auto manufacturers' bailout. Do you think, in retrospect, that that was a worthwhile endeavor for the taxpayers?

Mr. JORDAN. Again, I did not support that legislation either.

Mr. JOHNSON. All right. So you would have supported just letting our manufacturing base in this country, the auto makers, just simply go out of business—

Mr. ISSA. Mr. Chairman, could I have regular order, please.

Mr. COHEN. I think that is probably a pretty good idea at this point. We should take advantage of our witnesses.

Thank you, Mr. Johnson.

Mr. JOHNSON. I would yield back.

Mr. COHEN. I would now like to recognize Mr. Maffei from the great State of New York for 5 minutes.

Mr. MAFFEI. Thank you, Mr. Chairman. And as one of the lead sponsors of one of the proposals addressing the auto dealers' concerns, H.R. 2743, the Automobile Dealer Restoration Rights Act, I want to thank you again, and the Chairman of the full Committee and the Ranking Member, as well, for being willing to hold these hearings. And I want to thank the witnesses especially for coming.

Yesterday it was quite interesting with Mr. Bloom. He mentioned a number of things. One thing he did was he did at one point characterize where the National Automobile Dealers Association was on one issue that they take issue with, and I did want to, by unanimous consent, submit to the record just a news release they have, just stating their view on that particular comment.

Mr. Chairman, I submit the statement into the record.

Mr. COHEN. Without objection.

[The information referred to follows:]

**FOR IMMEDIATE RELEASE**  
**July 21, 2009**

## **NADA Response to Comments by the Head of the White House Auto Task Force**

WASHINGTON (July 21, 2009) – Today's characterization by the head of the White House Auto Task Force with regard to the position of the National Automobile Dealers Association (NADA) on the question of dealer cuts is inaccurate. In comments at a hearing before the House Judiciary Commercial and Administrative Law Subcommittee, Ron Bloom maintained that NADA's only point of contention was the speed of dealer cuts. Not true. NADA is on record as consistently disagreeing with the idea of drastic cuts in the number of auto dealers. Auto dealers are independent business owners, entrepreneurs who invest millions of dollars in land, facilities, vehicle inventory, parts, training and employees. It is the dealer who should decide, based on market conditions, when to exit the business. Since dealers cost automakers next to nothing in overhead expenses, cutting dealers at this time does nothing to make either GM or Chrysler more viable.

NADA's position on the issue of dealer cuts has been outlined on numerous occasions, including in multiple meetings with the Auto Task Force. These positions were also stated publicly in an [Open Letter to President Obama](#) that was published in major newspapers around the country (see attached).

Here's a partial list of other occasions when NADA voiced its strong opposition to dealer cuts:

- June 12 - Press release: [NADA Welcomes Congressional Oversight of Dealership Closures](#)
- June 10 - Press release: [NADA Applauds Congressional Efforts to Restore Dealer Rights](#)
- May 23 - NADA asks all dealers to contact their U.S. Representatives to urge them to cosponsor H.R. 2743 and S. 1304, the "Automobile Dealer Restoration Rights Act."
- May 13 - Dealers and dealer association executives from around the country converge on Capitol Hill to impress upon lawmakers that the drastic, rapid dealer cuts demanded by the President's auto industry task force will have a detrimental effect on automakers, the economy and the country... NADA press release: "[Auto Dealers Are Urging Congress to Intervene With the Obama Administration to Oppose Drastic Dealer Cuts](#)"

Contact:

David Hyatt  
Vice President  
NADA Public Affairs  
(703) 821-7120  
(202) 281-4550 mobile  
[dhyatt@nada.org](mailto:dhyatt@nada.org)

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Mr. MAFFEI. Thank you.

On the question of the auto companies, we asked him, several Members asked him about what the rationale was for needing to do the reductions. I asked him whether it was the policy of the Administration that the dealer cuts needed to be done; and if they had not been done, then the companies would not have been viable. He did not directly answer that question; he simply said it was a part of the whole package.

I do believe, as I pointed out in yesterday's hearing, that there has been a lack of transparency and a lack of consultation with the dealers in the means by which Chrysler and GM have chosen to decide which franchise agreements to reject. And I still believe there is a lot of confusion as to how the closing of these dealerships, hundreds across the country, will be financially beneficial to the two auto companies.

It seems to me that although there might be some long-run cost savings that the automobile companies provided these dealer networks over time in a way to lower their costs. And most of the costs, as I mentioned yesterday, the employees, the rent or the mortgage, a lot of—the equipment is all dealt with—the dealers all do that.

So I do want to ask our witnesses, both Ms. Van Der Wiele and Mr. Robinson, and I will start with Mr. Robinson. Can you describe in terms that Members of Congress can understand, and their constituents, how reducing these dealer networks this substantially makes General Motors more viable?

Mr. ROBINSON. Mr. Maffei, I would break it down into two categories. And I know from your comments about Mr. Bloom's remarks yesterday, you are not interested in hearing a lot of detail about financial analysis. But I will tell you as a matter of fact over time, because of the inefficiencies in the network and a host of reasons, there are a bunch of built-in costs that have accumulated over time for General Motors that one of our competitors, Toyota, doesn't have.

Mr. MAFFEI. Actually, on the contrary, Mr. Robinson. At least some example; I would be happy to hear actually some real specific examples.

Mr. ROBINSON. Let me give you an example. In terms of the brand equity that we are trying to protect and develop here—and that is really what drives this, because without successful brands we are not going to be successful with this second chance we have been given. So the driving force is to build brand equity and be successful that way.

One of the symptoms of a weak brand is subsidizing at the distribution network. Now, we have done it in various forms and we can provide you with an overall breakout of basic categories of expense. But, for instance, we have a 1 percent program with our dealers where, essentially, for all the revenue we receive on the sale of cars, the dealers get back 1 percent because the weaknesses in the network have required that over time. We provide dealers with other subsidy supports on advertising and various programs that, quite frankly, Toyota doesn't have to engage in.

From my perspective—and I am not an expert on marketing, I am a lawyer. But from my perspective, this falls in much the same category as the things we had to do with our labor agreements, for instance, to get our costs comparable to Toyota to be competitive.

But let me give you another example that is more concrete than talking about numbers. The City of Cleveland is an example that comes to mind. We sell the same number of vehicles, more or less, than Toyota in that marketplace, about 9,000. For Chevrolet 9,000, the same for Toyota. They have 5 dealers, we have 14 dealers. The

weaknesses that that generates in our dealer distribution network are profound and need to be fixed.

We have other weaknesses in rural markets, as well, with dealers that aren't meeting standards. And we have tried to help these dealers with, as you know, these wind-down agreements.

But from my perspective as a lawyer in dealing with the folks that are trying to fix the business, it is a brand issue, and the dealers are a symptom. The weaknesses in the dealer network are really a symptom of the brand issue.

Mr. MAFFEI. Thank you, Mr. Robinson. I would point out that UAW, in terms of labor agreements and indeed the creditors, were included in discussions that the dealer networks never were, at least not until recently.

I ask the Committee's indulgence that I just let Ms. Van Der Wiele to just address my question.

Ms. VAN DER WIELE. Thank you, Mr. Congressman. Going forward, the new Chrysler Group LLC will reduce the number of overlapping products. We are moving forward from 27 nameplates covering 13 product segments in the 2007 calendar year, to a target 20 nameplates covering 17 segments by the 2013 calendar year. Fewer nameplates with better product and customer market coverage will help improve the overall return on our product capital investment. This means that dealers need to have all three of our brands under one roof in order to offer a full range of products and to optimize their profit potential.

I have some examples here of lost revenue and costs associated with discontinued dealers: product engineering and development for sister vehicles.

Mr. MAFFEI. Ms. Van Der Wiele, I am already out of time. Why don't we just submit that? We can submit that to the record.

But I would caution you that that doesn't really answer my question in a way that I can explain to any of my constituents. And that is part of the problem here.

Anyway, I yield back the time that I have already used up.

Mr. COHEN. Thank you.

Mr. Coble from North Carolina, you are recognized for 5 minutes, sir.

Mr. COBLE. Thank you, Mr. Chairman.

Witnesses, thank you all for being here with us today. I had to momentarily leave, so this may have already been covered, but let me put a two-part question to Mr. Robinson and/or Mr. Miller.

If you would, Mr. Robinson, explain the significant distinctions between the Chrysler plan and the GM plan on the one hand.

And, secondly, I have cosponsored H.R. 2743 and 2794, which were introduced by Representatives Maffei and LaTourette. Both bills came to me strong, with a strong endorsement of the Auto Dealers Association in North Carolina.

Explain, if you will, to me the dealership wind-down process, including in your bankruptcy plan; and also, if either of these two bills is enacted, how that would affect the dealerships that participate in the process.

Mr. ROBINSON. Congressman Coble, I will answer the second question first, if that is okay, because I have some concerns about that.

I mentioned earlier in my testimony that General Motors has a plan to allow for a soft landing for these wind-down dealers. The first installment on that wind-down plan—by the way, 99 percent of the dealers that were given the notification that they had this opportunity signed up for it. That was approved by the bankruptcy court. The bankruptcy court concluded these are not coercion contracts. That is in the language of the sale order.

And, by the way, just so you know, there were originally some objections by 45 State attorneys general in the process of looking at the sale process. They withdrew their objection, and they accepted the fact that these wind-down agreements are not coercive as part of the language of the sale order.

I can't talk to Chrysler's program. I can only tell you about ours. I have concerns about the legislation in this respect. We could have a nice constitutional argument, constitutional law argument about a lot of the issues that it raises, but a practical issue for me is this: We have already started making payments to dealers, according to the terms of the wind-down, to this point in the neighborhood of \$150 million. Dealers are coming to us now saying: "Can you accelerate the process? I have sold down my inventory. I would like to get out of this business and terminate my dealership. You didn't terminate me, but I would like to terminate my dealership arrangement with you. Can you provide the rest of the money?"

And we want to honor those requests. We have had probably 25 or so to this point. I don't know as I sit here what the consequences will be for dealers, for us, if Congress passes a law that says we have to take these dealers back. We will obviously comply with whatever the ultimate ruling on the law is, but I am confused as to what this is going to do to a lot of people that have received a lot of money from us at this point.

Mr. COBLE. And how about the first question?

Mr. ROBINSON. The first question on the difference is I can talk about our program of wind-down. And the dealers basically, for any new car in inventory, if they have gotten a wind-down agreement from us for any franchise, it is \$1,000 per vehicle. Plus, if it is a complete wind-down of their operation, 8 months of rent coverage, whatever they say it is based on their financial statements. We are not quibbling with them about the rent factor.

Mr. COBLE. I thank you for that, Mr. Robinson.

Ms. Van Der Wiele and/or Mr. Orr, let's shift to your situation. Why did not you all at Chrysler include a dealership wind-down similar to the GM proposal? Obviously there was a good reason; I would just like to know what it is.

Mr. ORR. Mr. Coble, the nature, as I mentioned before, the nature of the dealership agreements at Chrysler were essentially perpetuity agreements that went on and on. We did not have term agreements that would expire, and it was necessary for us and our debtor, pursuant to our master transaction agreement, our purchase and sale agreement, to make a determination about what assets we would reject and pass on to our purchaser. That necessarily included a reduction in dealer network.

In fact, the testimony in the court below, both by the purchaser, was that the analyses—the dealer network needed to be downsized. Three of the dealer witnesses in the case below testified that there

were too many dealers at Chrysler. They testified that there are economies of scale and efficiencies for consolidation of our dealer networks. These are the witnesses of the dealers objecting to our sale. And they also testified that there would be increased sales to the remaining dealers through winding down the network.

So the decision made economic sense, both increasing the probability of gaining market share and what the industry calls through-put, which is basically sale of cars, that was required by our purchase and sale agreement. And frankly, Mr. Congressman, we did not have the cash on hand to institute the type of program that would require wind-down and payout of certain benefits to our dealers.

Mr. COBLE. Thank you, sir.

Mr. Robinson, in your testimony you indicated there were certain costs that were not borne by Toyota. What were those costs?

Mr. ROBINSON. Well, part of it, sir, is an arrangement we have created with the dealers where we flow money back to the dealerships for advertising purposes and things like that. And that is quite a sum of money. It is probably half—I haven't got the figures in front of me, but it is probably half of the \$2 billion or so associated with that. There are other fixed costs associated with the size of this dealer network to the tune of another \$400 or so million. The total cost that is associated with this series of accumulated subsidies is about \$2.5 billion.

Mr. COBLE. I thank you. I see my time has expired. Thank you, gentlemen, for being with us. Mr. Chairman, I yield back.

Mr. COHEN. I thank the gentleman for his questions. I now recognize the gentleman from Georgia, the Subcommittee Chairman, Mr. Hank Johnson.

Mr. JOHNSON. Thank you, Mr. Chairman.

You know, the taxpayers have spent—and some would say invested—\$60 billion in bailout money for the automobile manufacturers. And I myself think that was a much better way to go than to allow our manufacturing base to wither away. Doom was impending.

And so it is understandable that you would take your last resort, which is to go to the government and ask for money. And that was the practical reality of things. What would we do? Would we just do nothing? We certainly couldn't do that.

So with this \$60 billion investment in the companies, the American people deserve aggressive protection as to how that money would be spent and the effects of corporate decisions, including things like corporate bonuses. And if there is someone at the company who is not equipped to lead the companies into the future, then they certainly need to come out.

And taxpayers are the ones that are represented by the government, and the government thus has a role to play in overseeing the \$60 billion investment. You know, it is not meddling in the affairs of the companies, it is just wise and pursuant business decisions being made by, he government which never desired to be an automobile business.

And so I will ask, though, from the representatives from GM and Chrysler, the amount of cars sold by Chrysler, Ford, and GM has decreased over time. And, now, about 3 years ago Ford, I guess,



saw things coming; they mortgaged the company to the tune of, I believe, about \$18 billion, and they have been able to avoid asking for any taxpayer bailout money.

GM, which had the most market share, did not escape that fate, and neither did Chrysler, who is coming back for the, actually, I think second time over the last 30 years or so for a bailout.

And so meanwhile, the domestic automobile manufacturers are victims of a declining market, and Ford has been able to weather the storm. In fact, Chrysler and GM went bankrupt. Ford never did go bankrupt.

Now, Ford does not have a program of closing dealerships, but GM and Chrysler do. Now, is that difference a result of basic mismanagement, wrong decision-making by the folks at GM and Chrysler? I mean, how could we account for it?

Mr. COHEN. Mr. Johnson asked: Did Ford have a better idea? Can anybody tell us?

Mr. ROBINSON. I will try to answer your question, Congressman, this way. I can't speak for why Ford did what it did when they did it. I do know, from what I can read in the trade publications, that they did have an extensive dealership network program that preceded where we are today. Their dealer count is going to be in the neighborhood of where we are, when we are done with our program.

Why didn't we do what they did 3 years ago? I can't answer that question. I don't think anybody foresaw 3 years ago the environment that we would be in at the end of 2008, quite frankly. If they did what they did to monetize their assets at a time when they did it, I am sure they had good reasons for it. I am not sure they saw the economic tsunami any more clearly than anybody else, but they must have had good business reasons for doing what they did.

Ms. VAN DER WIELE. Yes, Mr. Congressman. I also can't speak to Ford's decision-making, but what I can do is put the dealership issue in perspective. And that is, between 1990 and 2007, the average number of new vehicles sold in the United States was 16 million. This year, they are projecting no more than 10.1 million.

So, obviously, all the auto companies, particularly those that have—the Big Three that have the legacy dealerships had to reduce the size in order to cope with the drastically lowered sales volume.

Mr. JOHNSON. Is it true that Ford sales has a lower market share than GM or Chrysler? Is that true or is that false? And if it does, then isn't it a fact, then, that GM going down to the number of Ford dealerships, the number of dealerships that Ford relies upon, wouldn't that cancel out that argument that we are just simply going down to the number of dealerships that Ford has?

And I appreciate the Chairman's allowing me to just exceed the time, and this will be my last question.

Mr. ROBINSON. Congressman, we will still have more dealerships, I believe, than Ford. If you look at the difference in our market share, I don't think it is proportional to the difference in the number of dealers we have or have had up to this point time, where we have had over 6,000 versus the difference in our market share. Again, that is a lawyer's reaction to a market analysis question, so bear with me.

Mr. COHEN. Thank you, sir.

Mr. Issa from California is recognized for 5 minutes—or even a few seconds further.

Mr. ISSA. Perhaps. Thank you, Mr. Chairman.

Mr. Miller, you had an analysis earlier about what an ordinary creditor would do; right?

Mr. MILLER. An ordinary secured creditor, sir.

Mr. ISSA. So for going \$3.8 plus-or-minus billion of DIP financing in Chrysler, that wouldn't be routine, would it?

Mr. MILLER. The amount is very substantial. The question is, if you have an outstanding secured creditor, the ability to get DIP financing—as we call it—nobody would do it unless you could prime the existing secured creditor. So that eliminates the possibility of getting DIP financing. And also, the amount—

Mr. ISSA. No. In the case of Chrysler, the Federal Government has simply walked away from a portion of the money it loaned in the transaction at the time of sale.

Mr. MILLER. I wouldn't say that they walked away. They took an equity interest. And that is exactly almost the same thing that has been done in GM. The new GM—

Mr. ISSA. Why take equity and forgive debt? Why not keep the debt and forget the equity?

Mr. MILLER. Because the new company, the successor, the purchaser, whatever you want to call it, cannot service that debt. That is the recognition that you had to—you have a smaller company. Its ability to service its leverage ratio has to be consistent with what the market will appreciate. The hope is that someday these companies will be able to go into the private market and get financing. And so you can't be overleveraged.

That is why debtors—in many situations, including the automobile companies, secured creditors will exchange debt for equity in the hope that the successor company will be viable and profitable.

Mr. ISSA. Well, I appreciate that. But Chrysler reeks of the government deciding what they wanted to do without much consideration to their original charter under the TARP, the money they used.

Mr. Robinson, is General Motors as committed as Chrysler, the new Chrysler Corporation, seems to be in her statements that they will provide, if you will, somewhat of a first—and correct me if I am wrong, ma'am—a right of first refusal to those displaced dealers in future considerations? I heard it pretty profoundly that you wanted to make business opportunities available to them.

Ms. VAN DER WIELE. Yes. I don't think I used the term “right of first refusal.”

Mr. ISSA. Right. I realize it was less than that.

Is General Motors committed to recognize that the dealers who lost their dealerships lost them to dealers that got the value that was once theirs delivered to the dealer across town? Is General Motors equally committed to finding innovative ways to accomplish that for dealers who could meet criteria in the future for whatever opportunities become available?

Mr. ROBINSON. Congressman, I would put that specific proposal on the list of things that we would be prepared to sit down across

the table and work out with the NADA and their membership. Our intent is not to go back into places that we have had to exercise—go through this wind-down process.

I hope we have that problem 2, 3, 4 years from now, that things turn around, the markets are stronger, the opportunities are greater. But I think on behalf of the company, I can commit that we are very interested in having that conversation with the authorized representatives of the dealer body.

Mr. ISSA. And Ms. Van Der Wiele and Mr. Robinson.

Mr. ROBINSON. And I would call it a right of first proposal.

Mr. ISSA. That is fine.

The second point I want to make sure that both of you are willing to commit to is the dealers that lost their dealerships, by and large, no matter what you say on the wind-down, they got screwed. They got less in the wind-down than the value of their dealerships before your bankruptcies caused them to lose their dealership. Is there any argument there here today?

You don't have to use my particular parochial term, but they got less than the fair value in an ordinary market. Isn't that true?

Ms. VAN DER WIELE. I don't know specifics. But I can say that the dealers, like all other stakeholders, had to accept less than they would have anticipated but for the bankruptcy situation. But it wasn't just the dealers.

Mr. ISSA. Let's make sure we are clear here. They were protected by State franchise. They had an asset which they had purchased; in many cases, they had purchased the right—the exclusive right in an area to sell a Chrysler, a Dodge, a Jeep, to sell a Chevy, a Pontiac, some of them.

Mr. ROBINSON. Oldsmobiles, too.

Mr. ISSA. But they had purchased that. And that was diminished to zero, other than whatever compensation you gave them. Is that a fair statement, that that purchase right was eliminated?

Mr. ROBINSON. Well, I would agree, Congressman. They couldn't sell a franchise at the point they received the wind-down agreement and signed up for the program. In some cases the dealers, quite frankly, may be doing better with the wind-down agreement than they would have if they otherwise didn't get the wind-down.

Mr. ISSA. That would be a rare case, I suspect.

Let me ask one or two quick follow-ups. In the case of a dealer who purchased a dealership and has a loan from one of your finance arms, particularly in the case of General Motors, so they have a liability that is offsetting the asset they purchased.

Why in the world shouldn't we envision here on the dais that they can essentially default without personal guarantees? Because one taking from one part of your company to another is, in fact, a fair offset, even though technically under bankruptcy it isn't.

When we are sitting up here looking at a flaw in the bankruptcy system, if I have a dealer who owes 4.5 or 5.5 or 6.5 million to GMAC and they have taken the dealership, and the wind-down is not 4.5 million, it is not offsetting, why shouldn't they be able to say: "Here's my building. It is your problem," and be able to say "You can't go after my personal guarantee, because in fact an arm of the very entity took it?"

Now, there are not a lot of those, but there are some where it is literally two parts of your company.

Mr. ROBINSON. Mr. Miller may be closer to this than I am at this point, but, quite frankly, GMAC was once upon a time a wholly owned subsidiary of General Motors. It is not, and we own less than 10 percent.

Mr. ISSA. I appreciate all of that. But taxpayer money went into turning around both of your companies and forgiven for stock. My question is: Shouldn't we on the dais find a solution for those dealers who essentially have been screwed by the bankruptcy system? And I apologize for using that word twice, but I don't know a more accurate term than when billions of dollars go to taking care of making sure that your entities are going concerns, and in a sense they get no better, perhaps worse, of a deal than they would otherwise.

I am looking at car deals around the country—I am sure there are many more examples than I presently know about—who are going to lose their homes because the asset they had was wiped out in bankruptcy and their liability is to the very group that said, "Buy the dealership, we will carry back this loan."

And you may say it is only 10 percent today, but you had an effective control at the time the deal was made. That is why the relationship was created, why they didn't go to some other bank. General Motors—to a lesser extent Chrysler—was in the business of if you wanted a dealer, you helped him with the financing.

I am only asking, Do you think that we should consider, not, Do you have the power to do it?

Mr. ROBINSON. That is a policy consideration that I would think the Subcommittee would want to take a look at; but I can't answer the question any differently than that, sir.

Mr. COHEN. The gentleman's time has expired.

Does Mr. Sherman seek recognition? You are recognized for 5 minutes.

Mr. SHERMAN. First—and other questioners may have done this. I guess I will address this to the vice president of Chrysler. Why is it thought to be in the automobile company's interest to have fewer sellers charging a higher margin for your product when those in other businesses seem to want the smallest possible gap between what the manufacturer gets paid and what the consumer pays?

Ms. VAN DER WIELE. Mr. Congressman, I can answer that in a general fashion, although with your permission I think my colleague could provide more specificity than I can.

Mr. ORR. Mr. Sherman, if I may. Much has been made about why don't we have more dealers, "Why would you want to reduce your dealer network? It seems to me you are reducing the outlets for selling your product. It doesn't make sense."

Automobiles are not Starbucks, which, by the way, is reducing its profile, and automobiles are not yogurt.

Mr. SHERMAN. Starbucks is reducing because they have to pay the people behind the counter. You had this dealer network at no cost.

Mr. ORR. But understandably, Congressman, respectfully, the efficiencies involved in having too many outlets actually at some level can reduce your ability to sell cars. The analysis for us, mean-

ing Chrysler, in terms of making its decision, was that in order for the company to go forward, saving 75 percent of its dealer network and reducing 25 percent of its dealer network would yield greater efficiencies to the dealers, allow those dealers to sell more cars themselves, and thereby increase their capital profile and survivability, and allow the company to sell more cars through those dealers because of overarching marketing concerns in specific marketing pools.

Mr. SHERMAN. What particularly concerns me is the statements made, if not by Chrysler then by GM, is that one of the things you are seeking is a larger margin, a bigger gap between the manufacturer's price and what the consumer pays. And it is quite possible that if consumers pay an extra 100 or 200 bucks, because they can't play one dealer off against another, that that will be to the benefit of the manufacturer of—maybe it works better, but it does mean that people in my district and all our districts are paying a few hundred bucks more for a car because you can't pit one dealer off against another.

Shifting to the legal issue, though. It is my understanding that in bankruptcy the claims of general creditors can be wiped out and the claim of these dealers to a franchise was just such a general claim. And, that in fact it would have been legal in bankruptcy for you to have voided all the franchises, and then—I don't know who would have paid for them, but then you could have sold them again. I don't know who would have paid you for them.

But would that have been legal under bankruptcy, instead of just voiding some franchises, voiding them all?

Mr. ORR. Mr. Sherman, section 365 of the Bankruptcy Code does allow you to terminate burdensome contract leases. It is a requirement of that code that in exercising that judgment, there is a benefit to the debtor. In exercising the judgment—

Mr. SHERMAN. Well, clearly, there are some good franchises. If you could have canceled the one on Van Nuys Boulevard and then sold it, you would have made some money.

Mr. ORR. Well, perhaps, Mr. Sherman. But we made the decision not to cancel all the franchises; 75 percent, comprising almost 85 percent of our sales, we retained, recognizing that we needed our dealerships under the existing agreements.

The concept is you have to balance the potential benefit to the debtor against the potential—not the harm to the dealer, but the potential harm to the debtor. We don't sell our franchise agreements. That is somewhat of a misperception. Dealers are awarded contracts and they capitalize their businesses, but we do not sell franchises.

Mr. SHERMAN. So you just awarded franchises to those you thought could do a good job, and they didn't write you a check as part of that award?

Mr. ORR. They do not write the company a check, but they do have to capitalize the business. They have marketing, they have finance, so on and so forth.

Mr. SHERMAN. Needless to say, good to explore the law with you, was once a summer associate with your firm. But the idea—

Mr. ORR. Glad you remember us, Congressman.

Mr. SHERMAN. But the idea of canceling dealer franchises was more an exploration of what the law is or could be, not any business advice for you. I yield back.

Mr. COHEN. Thank you. We are almost at the slosh and cutoff. But before we get there, we are going to give the Ranking Member a minute for mea culpas.

Mr. FRANKS. I just wanted to point out, Mr. Chairman, I have been pretty hard on these guys here today. And while I believe everything I have said, I think it is important to realize that there were two giant things that caused the bankruptcies to occur. One was an increase in the gasoline prices that had an impact on your markets, and of course the dry-up of the capital market. You would essentially agree with that; correct? That was the big things that impacted? And those things weren't your fault. Those things I believe were catalyzed ultimately by government policy. I won't get into the details.

But I just wanted to say that to you, even though in my criticisms here I have been sincere. I do know that these things have happened, and I think that ultimately government is to blame here more than you are.

So, with that, I yield back. Thank you, Mr. Chairman.

Mr. COHEN. Thank you, Mr. Ranking Member. And implicit within that, it wasn't the UAW's fault either.

We are now at a time when we are going to be taking some votes. The votes should take approximately 45 minutes, and then we will resume with the second panel. We have concluded this first panel.

I would reiterate the Chairman of the full Committee's suggestion—and mine, also—that if you can stay, we would appreciate it. The four of you, can you all stay to listen to the next panel and possibly have a cup of coffee? It seems reasonable. I am sure you are on the clock. This is part of the stimulus package.

So thank you, and I appreciate it. Mr. Chrisie is the only person who hasn't accepted that offer, and he is on television about not staying, so you don't want to leave. So we accept that.

We will be back in about 50 minutes, and in the interim we are in recess.

[Recess.]

Mr. COHEN. This hearing of the Committee on the Judiciary, Subcommittee of Commercial and Administrative Law will now come to order. Without objection, the Chair will be authorized to declare a recess of the hearing.

I am now pleased to introduce our witnesses. Our first witness is Douglas Baird, whose name was mentioned earlier. Mr. Baird is the Harry Bigelow Distinguished Service Professor of Law at the University of Chicago. His research and teaching interests focus on corporate reorganizations and contracts. He served as dean of the law school from 1994 to 1999. Before joining the faculty in 1980, he was a law clerk for the Court of Appeals for the Ninth Circuit.

Professor Baird, will you please proceed with your testimony? We welcome you.

**TESTIMONY OF DOUGLAS G. BAIRD, HARRY A. BIGELOW DISTINGUISHED SERVICE PROFESSOR OF LAW, UNIVERSITY OF CHICAGO LAW SCHOOL**

Mr. BAIRD. Mr. Chairman, Ranking Member Franks, Members of the Committee, I want to thank you for the chance to speak to you today about the recent automobile bankruptcies.

The willingness of the Federal Government to contribute substantial resources was a necessary but not sufficient condition to the survival of General Motors and Chrysler. Without Chapter 11 or some similar process, General Motors and Chrysler would likely have gone out of business. In this respect, these cases show the good that modern bankruptcy judges and lawyers are able to do, especially in troubled economic times.

Bankruptcy law, however, provides no panacea. The challenges General Motors and Chrysler face are far from over. There is no guarantee either will survive. Much depends upon whether domestic automobile consumption rebounds significantly over the next several years, and whether these companies can transform their corporate culture quickly enough in a highly competitive marketplace.

These two cases also underscore the limitations of bankruptcy law in another way. Companies that are insolvent—and Chrysler and General Motors were hopelessly insolvent—are unable to meet all their obligations. Bankruptcy law can do nothing to change this. No matter what bankruptcy provides, many worthy stakeholders, tort victims, unpaid suppliers, pension funds, dealers, workers, will not be paid in full or will not be paid at all.

One can try to protect some stakeholders by favoring one group, but favoring one group necessarily comes at the expense of another. Moreover, there are sharp limits on the ability of bankruptcy law to do even this.

First, most firms that fail never file bankruptcy petitions. Indeed, fewer than 1 percent of all financially distressed firms file for Chapter 11; and those that do are typically encumbered by liens that at the time of the bankruptcy filing have the status of constitutionally protected property interests.

If you decide to protect some stakeholders of failed firms—which you can do—such as tort victims, the best way to do this is by giving a super priority lien to those stakeholders. But it has to be a lien that is good both inside of bankruptcy and outside of bankruptcy. And that is possible. Some environmental claims have this feature, but it comes at a cost.

Now, in my own view, tort claims are among those that should be protected with a super priority lien. But I should emphasize that this view is both controversial and not in the first instance a question of bankruptcy policy. Again, only a law that trumps liens and applies generally, regardless of whether the assets are sold and regardless of whether the firm is in bankruptcy, will work in this environment.

Next, I want to focus on the particular lessons we can draw from the bankruptcies of General Motors and Chrysler. The active participation of the Federal Government dramatically altered the dynamics of these bankruptcy cases, and not always for the better. The most striking feature of these Chapter 11s was their speed,

particularly in the use of section 363 to sell these firms as going concerns. Now, going concern sales are very common in large Chapter 11 cases. Perhaps half or more of all Chapter 11 cases now are now sales.

Now, in principle, the ability to sell a firm as a going concern and take advantage of the marketplace is a salutary development. In principle it is a good thing. The stakeholders get the maximum value and the company gets the best shot at reinventing itself and competing in the marketplace. But we need to ensure the sales process is conducted in such a way that the firm is in fact sold for top dollar. Without appropriate procedures, there is a risk that too many 363 sales and other going concern sales are firesales. These firesales work to the advantage of those in control, not the stakeholders as a group. Over this dimension, the sales in Chrysler and GM may have been conducted too quickly.

There is another danger to which attention needs to be given. The sale itself should not dictate the way in which the proceeds of the sale are distributed. The sales that were conducted in Chrysler and General Motors were troubling over this dimension as well. In both Chrysler and General Motors, the bankruptcy judge approved sales procedures that narrowly limited the form of the bid. It insisted that everyone who bid, not just the Federal Government, pay specified amounts to specified claimants. The sales procedures approved by the bankruptcy judge effectively dictated the distribution of assets. The bankruptcy courts in these cases may have tolerated these highly unusual and highly restrictive sales procedures in large part because they thought it wouldn't make a difference. It seemed to them unlikely another bidder would merge, even if more time were taken or different or better rules were put in place.

The conditions of the companies, the illiquidity of the current markets, and the strong desire of the Federal Government to dictate the outcome were sufficient to chill competing bids regardless of the procedures.

Nevertheless, the question of whether other bidders might appear and provide different alternatives is one the marketplace is supposed to answer. The judges could have done more to test the waters, and there may have been little cost in opening up the process more, as for example the bankruptcy judge in the Delphi bankruptcy has done. When process is neglected, as it was in these cases, rights of stakeholders are inevitably compromised, as is their ability to sit at the negotiating table and be heard.

Now, the special circumstance to the automobile cases may mean that these circumstances are not likely to be repeated and no special legislation is required. But the procedures followed in these cases should not become the norm, and legislative reform would be appropriate if they did. But reform should be limited. It would be a mistake, again, to limit the ability of bankruptcy judges to conduct sales and thereby give buyers clean title.

In summary, the bankruptcies of General Motors and Chrysler raise a number of problems. At the same time, however, it should be recognized they arose because of the large role the government played. And this may not have been inappropriate, as the government acted in this way only because of its perception—of correct,



in my view—that aggressive use of the bankruptcy process was necessary to save these companies.

Thank you, Mr. Chairman.

Mr. COHEN. Thank you, Professor Baird.

[The prepared statement of Mr. Baird follows:]

PREPARED STATEMENT OF DOUGLAS G. BAIRD

I am the Harry A. Bigelow Distinguished Service Professor at the University of Chicago Law School where I teach bankruptcy law. I joined its faculty in 1980 and was its Dean from 1994 to 1999. I have also been a visiting professor at Stanford, Harvard, and Yale. I am a fellow of the American Academy of Arts and Sciences, I have served as the Vice Chair of the National Bankruptcy Conference, and I am currently the scholar-in-residence at the American College of Bankruptcy. I have written several dozen articles on bankruptcy and related subjects, and my one-volume overview of U.S. bankruptcy law, *Elements of Bankruptcy*, is now in its fourth edition. I appear at your invitation today to try to draw some general lessons from the recent automobile bankruptcies. I speak as a scholar committed to the effective operation of our bankruptcy system and not on behalf of any individual or group.

The General Motors and Chrysler bankruptcies provide powerful illustrations of how Chapter 11 can give financially distressed companies a second chance. Without Chapter 11 or some similar process, General Motors and Chrysler would likely have gone out of business. The willingness of the federal government to contribute substantial resources was necessary, but not sufficient. In this respect, these cases show the good that modern bankruptcy judges and lawyers are able to do, especially in troubled economic times. Bankruptcy law, however, provides no panacea, only a fighting chance.

Even with a substantially reduced debt burden, the challenges General Motors and Chrysler face are far from over. They have been mismanaged for decades and find themselves in an industry in which there is massive overcapacity. There is no guarantee that either will survive. Much depends on whether domestic automobile consumption rebounds significantly over the next several years and whether these two companies can transform their corporate culture quickly enough in a highly competitive marketplace.

These two cases also underscore the limitations of bankruptcy law in another way. Companies that are insolvent—and General Motors and Chrysler were hopelessly insolvent—cannot meet all of their existing obligations. Bankruptcy can do nothing to change this. No matter what bankruptcy provides, many worthy stakeholders—tort victims, unpaid suppliers, pension funds, dealers, workers—will not be paid in full or at all.

One can try to protect some stakeholders, but this is not without major consequences. Favoring one group necessarily comes at the expense of another, and legitimate questions can be raised about when it is justified to favor one group over another. Moreover, there are sharp limits on the ability of bankruptcy law to do even this. Most of the firms that fail never file bankruptcy petitions. Indeed, fewer than one percent of financially distressed businesses end up in Chapter 11. Even for companies reorganizing in Chapter 11, merely giving a priority claim is likely to be ineffective. Businesses today have multiple layers of secured debt. The secured creditor enjoys a nonbankruptcy property right that has to be paid first. For these reasons, the best way to protect particular stakeholders is to give them a superpriority lien over other existing stakeholders across the board, inside of bankruptcy and out. Some environmental claims have this feature.

In my own view, tort claims are among those that should be protected with a superpriority lien, but I should emphasize that this view is both controversial and not in the first instance a question of bankruptcy policy. Again, only a law that applies generally whenever the question of priority arises will work. Alternatively, a law, again of general applicability, could require companies to carry sufficient insurance.

Another problem arises with respect to the obligations of a reorganized company to those who suffer harm in the future as a result of products the company made before bankruptcy. On the one hand, it is important to give companies a fresh start, but on the other, tort victims need to have their day in court. These problems have arisen in cases involving everything from asbestos to airplanes. They have been carefully studied and there are sensible, concrete proposals for the treatment of future tort victims that have been put forward by the National Bankruptcy Conference and others. These provide a sensible starting place for legislative reform.

In the balance of my testimony, I want to focus on the particular lessons we can draw from the bankruptcies of General Motors and Chrysler. One must recognize that only massive intervention by the federal government made it possible for the bankruptcy process to give these companies another chance. Both General Motors and Chrysler were experiencing massive and ongoing operating losses. When companies are hemorrhaging cash to this extent, it is generally too late for Chapter 11 to save them in the absence of an extraordinary infusion of outside capital and it is only rarely available. The active participation of the government fundamentally altered the dynamics of these bankruptcy cases—and not always for the better.

The most striking feature of these Chapter 11s was their speed. Section 363 of the Bankruptcy Code allows the judge to approve the sale of a business's assets outside of the ordinary course of business. In General Motors and Chrysler, this mechanism was used to sell the businesses as going concerns to a new entity created by, or, in the case of Chrysler, with the cooperation of, the federal government within the course of a few weeks.

Going-concern sales are common in large Chapter 11 cases. Over half of all large Chapter 11 cases now involve sales of one kind or another. In principle, this is a salutary development. A sale often converts an unwieldy and illiquid asset into cash that can be readily divided among the various stakeholders according to their legal entitlements. A sale can provide the best way to maximize the value of the assets. Even when a reorganization provides a better alternative, the *possibility* of a sale improves the process as it tends to keep everyone honest. A cash bid of a company for \$100 makes it impossible for one of the competing claimants to argue that it is worth less.

But we need to ensure that the sale process is conducted in such a way that ensures that the firm is sold for top dollar. Companies that are put up for sale are often in severe financial distress. They are melting ice cubes, and those in control of the process assert that they are willing to pump new money into the company to keep it alive only if the sale is done quickly to a buyer they have already identified. The danger that the business will not have enough cash to stay open puts enormous pressure on the judge to move the case quickly.

Without appropriate procedures, there is a risk that too many § 363 sales are fire sales that work to the advantage of those in control, not to the stakeholders as a group. The Bankruptcy Code itself offers no guidelines beyond a general requirement of notice and a hearing. Courts have begun to develop procedures. These, in conjunction with the rule-making process, might be sufficient to create procedures that ensure that these sales do in fact yield top dollar. If they do not, it may make sense for Congress to revisit this issue and ask whether procedures and protections for going concern sales should be explicitly addressed in the Bankruptcy Code.

There is another danger to which attention needs to be given. The sale itself should not dictate the distribution of the proceeds of the sale. The distribution of proceeds should recognize the existing rights of the various stakeholders. The procedures for the confirmation of a Chapter 11 plan of reorganization set out in § 1129 are designed to do this. The sale should not short-circuit them. The sales that were conducted in both Chrysler and General Motors, however, were troubling over this dimension.

The newly created entities that bid on the assets of Chrysler and General Motors agreed to take on some obligations of the old company. This itself seems unobjectionable in theory. If a new buyer decides to pay some obligations and not others, it should be free to do so. As a buyer, the assets belong to it, and it should be free to do whatever it wants with them. All that matters is that this buyer has produced the top bid after the company has been fully marketed. But the plan of a buyer to pay existing obligations becomes problematic if, at the same time, the freedom of action of other bidders is limited. For this reason, a buyer's decision to continue the debtor's relationship with some stakeholders, but not with others, has always been treated with suspicion.

In both Chrysler and General Motors, the bankruptcy judge approved sale procedures that narrowly limited the form of the bid. They required that the bidder agree to assume the same burdens the government-created entity was willing to assume.<sup>1</sup> By insisting that each bidder commit to pay specified claimants specified amounts, the sale procedures effectively dictated the distribution of assets. A buyer who takes a \$10 company free and clear will bid \$10 for it. But a buyer of the same company who is required to assume \$6 in obligations will bid only \$4. If the \$6 goes to a different stakeholder, then the process not merely converts the assets into cash, but also dictates how the cash is distributed. It becomes both a sale and a *sub rosa* plan.

<sup>1</sup>In Chrysler, the court did provide that the debtor could deem other bids qualified after consultation with the UAW, but the debtor had neither the obligation nor the incentive to do so.

Those who lose out (those forced to share in proceeds of \$4 instead of \$10) enjoy none of the protections of Chapter 11 plan process.

In both the Chrysler and General Motors bankruptcies, the courts tolerated highly restrictive sales procedures in large part because they did not think it made a difference. It seemed to them unlikely another bidder would emerge even if different rules were in place. The sorry condition of the companies, the illiquidity of the current credit markets, and the strong desire of the federal government to dictate the outcome were sufficient to chill competing bids, regardless of the procedures. Importantly, the judges found that, in the absence of the proposed sale, a liquidation was inevitable and objecting creditors would do worse in a liquidation than they were doing in connection with the proposed sale.

Nevertheless, the question of whether other bidders might appear and provide different alternatives is one that the marketplace is supposed to answer. The judges could have done more to test the waters and there would have been little cost in opening up the process more, as the judge in Delphi has been willing to do. When process is neglected, rights of stakeholders are inevitably compromised, as is their ability to sit at the negotiating table and be heard. The special circumstances of the automobile cases may mean that these circumstances are not likely to be repeated and no special legislation is required, but the procedures followed in these cases should not become the norm. Reform of Section 363 is appropriate should such practices persist.

In thinking about legislation affecting going-concern sales, however, it is important to distinguish between the procedures designed to maximize asset value and restrictions on the ability of firms in bankruptcy to give buyers good title. Granting a buyer clean title is the principal virtue of having the sale in the first place, and it is the device that ensures that the company is sold for top dollar. Those who buy in bankruptcy auctions will not pay for the same asset twice. If a firm is worth \$10 when sold free and clear, it will bring the creditors as a group \$10 only if the proper procedures are in place. If the law were changed to require that the buyer assume a \$3 obligation, then the sale proceeds will be only \$7. The effect of imposing limits on the title that can be conveyed is not to benefit the creditors as a group, but merely to alter the way in which the value of the underlying assets is divided among them. Allocating the sale proceeds is utterly different from ensuring that they are as large as possible. One should not confuse the size of the slices with the size of the pie.

Limiting the ability of the debtor to convey good title will also make sales relatively less attractive and hence less likely. The effect in the end may not even be to alter priorities, but simply to leave everyone with less.

By the conventional understanding, debtors in bankruptcy can reject franchise agreements just as they can reject other executory contracts. The effect is to put dealers in the same position as other stakeholders—such as investors, tort victims, and suppliers. This rule likely works to the advantage of the debtor going forward. To compete in any market, manufacturers must have an effective way of distributing their products. Regardless of whether a manufacturer distributes a product itself or outsources distribution to a third party, the less efficient the distribution system, the harder it will be for the manufacturer to compete. If a distributor is located in the wrong place, is the wrong size, or provides an inferior package of services, the manufacturer's position in the marketplace suffers. It does not matter whether the manufacturer pays the distributor or the distributor pays the manufacturer.

The distribution system in place for the automobile industry has remained essentially unchanged for decades. Even if it made sense in the 1950s when the industry was far less competitive and these firms enjoyed far larger market shares, it would be surprising if it still made sense today.

One can argue, however, that this understanding of the law governing franchisees is wrong as a matter of bankruptcy policy. Unlike other claimants, auto dealers are protected by specific state and federal laws. These make their rights different from those who enter ordinary contracts with the debtor. That these laws came into being in an utterly different and far less competitive market is, under this view, irrelevant. These dealership laws must be obeyed until they are changed. In principle, bankruptcy should provide no special break from government regulations, no matter how ill-advised they might be or how much they undermine a company's ability to survive as a going concern. Under this argument, debtors in bankruptcy must play by the same rules as everyone else.

Whether this argument justifies a fundamental shift in the treatment of executory contracts under the Bankruptcy Code outside the context of these cases is best left to another day. The involvement of the federal government in these two cases alters the dynamic significantly. While providing special protection for the dealers will

likely decrease somewhat the chances that the companies will survive, its principal effect is merely to reduce the value of the government's stake in the companies as restructured. Put differently, a law protecting automobile dealers in these cases is, in the main, an indirect subsidy of the dealers by the federal government. It may or may not be a good idea, but it is quite different from what goes on in other bankruptcies.

In summary, these two cases raise a number of problems, most arising by virtue of the role the government played. One can fault the particulars and one must ensure that the infirmities that existed in these cases—principally the procedures used in conducting the §363 sale—are not replicated elsewhere. At the same time, however, it should be recognized that the large role that the government played was the result of its perception—correct in my view—that only aggressive use of the bankruptcy process on its part would allow either of these companies to survive in a form that would minimize the cost to the U.S. taxpayer of keeping them alive.

Mr. COHEN. Our second witness is Mr. Dan Ikenson, Associate Director of the Cato Center for Trade Policy Studies focusing on WTO disputes, other trade agreements, U.S.-China issues, steel and textile trade issues, antidumping reform, and capitalism in general.

Before joining Cato in 2000, Mr. Ikenson was Director of International Trade Planning for an international accounting and business advisory firm, co-founded the Library of International Trade Resources.

And we welcome him today. And you may begin your testimony.

**TESTIMONY OF DANIEL J. IKENSON, ASSOCIATE DIRECTOR,  
CENTER FOR TRADE POLICY STUDIES, CATO INSTITUTE**

Mr. IKENSON. Thank you, Chairman Cohen, Ranking Member Franks, and Members of the Subcommittee. I am Dan Ikenson from the Cato Institute. Today I would like to share some general concerns about the ramifications of the auto industry bankruptcies.

I have been analyzing closely developments in the auto industry since last November when Detroit's public relations blitz took form and the companies sought a Federal bailout. Eight months later, the emergence of Chrysler and then General Motors from bankruptcy marked the end of the first chapter of what is a cautionary tale about the triumph of politics over markets and the rule of law. As the next chapter unfolds, we are likely to witness the consequences of what were extremely politicized bankruptcy prophecies.

Bankruptcy was always the best option for both of these companies; indeed, both should have been in bankruptcy before last November, long before President Bush circumvented the wishes of Congress and lent Chrysler and GM \$13.4 billion from the Troubled Assets Relief Program; long before President Obama had the chance to provide billions more and assume a larger role for the U.S. Government in Chrysler's and GM's restructuring operations; long before President Obama created a huge moral hazard by strong-arming Chrysler's and GM's preferred lenders into pennies on their dollars, while giving preference to claimants of lesser priority.

Instead, on account of the so-called prepackaged surgical bankruptcies, taxpayers are now majority shareholders in a company whose success depends on stewardship from 536 CEOs with disparate ideas of GM's mission.

Meanwhile, the United Auto Workers, typically more concerned about how corporate profits are carved up rather than how they attained, is majority owner of Chrysler. Perhaps most troubling, particularly in the case of GM, is the fundamental conflict inherent when operating and regulating a company falls to one entity.

The pursuit of profits and political objectives often work at cross purposes. The dealerships issue is a case in point. Notwithstanding the possibility that the choice of dealership closings was made arbitrarily if not politically, the fact remains that the companies must cut costs to survive.

Excessive dealership networks are an area that is ripe for cutting. The plan in effect as of this moment could save GM hundreds of millions of dollars per year according to Fritz Henderson. That the companies might be forced to abandon the plan because a majority of its 536 CEOs have political reasons for opposing it doesn't inspire much confidence that GM will be allowed to succeed. Successful companies are not run through referendum.

The dealership issue elevates doubts that politics will not infect operational decisions at GM in particular, and it portends highly erratic management as the President and Congress wrestle for primacy in formulating policy of this majority taxpayer-owned entity.

There are many other potential conflicts. For instance, has the President been endorsing people for key executive positions who are best qualified to run a profitable enterprise or who might be more amenable to the Administration's plans for converting the economy from a carbon-based to a renewables-based one? Has he decided that had GM won't supplement its fleets with cars produced at its plants in Mexico and China because it is bad for the bottom line or because it bothers the UAW? And how does Congress feel? Where does this Committee stand? Where does that caucus stand on this operational issue or that one?

Returning GM to profitability will require higher revenues and lower costs, neither of which was made easier by imposing more rigid CAFE standards on the automakers GM will be forced to sell fewer high-profit vehicles, its trucks, SUVs, muscle cars and luxury cars, and more low-profit or no-profit vehicles of small cars to achieve a 35.5 mile per gallon fleet average, all at a time when demand for small cars is falling.

Forcing automakers to produce vehicles that Americans demand only when fuel prices are in the \$4 range might appease the Sierra Club, but it won't help GM or Chrysler.

Between the congressional pushback over the dealerships issue and the insistence on higher fuel efficiency standards, we see the objectives of two broad groups of policymakers: those who want green production and treat the costs of that goal as immaterial, and those who want the auto industry to remain a jobs program regardless of the imperative of shedding workers to become more competitive.

Let us not lose sight of the fact that \$65 billion in taxpayer funds have been directed to GM and Chrysler over the past 8 months. In the case of GM, for taxpayers to get back their investment, the company would have to be worth about \$83 billion. At its historic high value in 2000, GM's worth, based on its market capitalization, stood at \$60 billion. Thus the company's value must increase by

about 38 percent from its historic high achieved in the year 2000, when Americans were purchasing 16 million vehicles per year, just to return principal to the taxpayer. But U.S. demand projections for the next few years come in really at around 10 million.

So as the Administration seeks to justify its wisdom in intervening and taking ownership of GM, I worry it will be tempted to use public policy and the Tax Code to tip the scales further in GM's favor, increasing the likelihood that the public outlay will grow larger, and dimming prospects that taxpayers will ever be made whole on their \$50 billion coerced investment.

So what will happen to Ford if lawmakers and the Administration have a favored horse in the race? Ford is relatively healthy now, but continued support for GM and Chrysler could well drive Ford to the trough, too, presenting the specter of another taxpayer bailout to the tune of tens of billions of dollars and another government-run auto company.

In closing, I would like to make one last point. The recent misfortune to Chrysler and GM and the government's assumption of responsibility for their rehabilitation occasioned a direct appeal from President Obama to American economic patriotism a few months ago. The President said: If you are considering buying a car, I hope it will be an American car.

But even if one were inclined to buy an American car, the tricky question remains: What constitutes an American car?

In 2008, the Big Three accounted for roughly 55 percent of the U.S. fleet vehicle production and 50 percent of sales. To speak of the U.S. auto industry these days, one must include Honda, Toyota, Nissan, Kia, Hyundai, BMW, and other foreign-nameplate producers who manufacture vehicles in the U.S. They are the other half of the auto industry. They employ Americans, they pay U.S. Taxes, support other U.S. businesses, contribute to local charities, have genuine stakes in their local communities, and face the same difficult economy as do GM, Chrysler, and Ford.

In a properly functioning market economy, the better firms, the ones that are more innovative, more efficient, more popular among consumers, gain market share or increase profits while the lesser firms contract. Efforts to pick winners disrupt that process and can only weaken the entire lot.

Thank you for your time and attention.

Mr. COHEN. Thank you, Mr. Ikenson.

[The prepared statement of Mr. Ikenson follows:]

PREPARED STATEMENT OF DANIEL J. IKENSON

**Testimony of Daniel J. Ikenson  
Associate Director, Center for Trade Policy Studies, Cato Institute  
Before the U.S. House of Representatives, Judiciary Committee,  
Subcommittee on Commercial and Administrative Law**

Good morning, Chairman Cohen, Ranking Member Franks and members of the committee. I am Daniel Ikenson, associate director of the Center for Trade Policy Studies at the Cato Institute. Today, I would like to share some general concerns about the ramifications of the auto industry bankruptcies. The views I express are my own and should not be construed as representing any official positions of the Cato Institute.

**The Past Eight Months**

On November 5, the morning after Election Day 2008, a report was published by the Center for Automotive Research, a Detroit-based consulting firm, warning that three million jobs were at stake in the automotive sector unless the U.S. government acted with dispatch to ensure the continued operation of all of the Big Three automakers.<sup>1</sup> Detroit's media blitz was underway. And it was timed to remind the president-elect, as he contemplated his victory the morning after, of the contribution to his success of interests now seeking some help of their own.

The CAR report's projection of three million job losses was predicated on some fantastical worst case scenario that if one of the Big Three were to go out of business and liquidate, numerous firms in the auto supply chain would go under as well, bringing down the remaining two auto producers, as well as all of the foreign nameplate U.S. producers and, subsequently, the rest of the parts supply chain. Oddly, the report gave no consideration to the more realistic scenario that one or two of the Detroit automakers might turn to Chapter 11 reorganization.

The subsequent public relations effort to make the case for federal assistance was pitched with an air of certitude and immediacy that the only real alternative to massive federal assistance was liquidation and contagion. The crisis-mongering was reminiscent of former-Treasury Secretary Henry Paulson's and Federal Reserve Board Chairman Ben

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<sup>1</sup>David Cole, Sean McAlinden, Kristin Dzikczek, Debra Maranger Menk, "The Impact on the U.S. Economy of a Major Contraction of the Detroit Three Automakers," Center for Automotive Research Memorandum, November 4, 2008, available at [http://www.cargroup.org/documents/FINALDetroitThreeContractionImpact\\_3\\_\\_001.pdf](http://www.cargroup.org/documents/FINALDetroitThreeContractionImpact_3__001.pdf)

Bernanke's insistence six weeks earlier that there was no time for Congress to think, only time for it to act on a financial sector bailout, lest the economy face financial ruin.

The mainstream media obliged the script, elevating the automobile industry "crisis" to the top of the news cycle for the next month, and helping to characterize the debate in the simplistic, polarizing dichotomy of "Main Street versus Wall Street." The notion that some financial institutions took risks, lost big, and were rescued by Washington became the prevailing argument for bailing out the auto companies, and the specific facts about viability and worthiness were tertiary.

But public opinion that was initially accommodating of that characterization quickly changed when the CEOs of GM, Ford, and Chrysler laid waste to months of public relations planning and millions of dollars spent trying to cultivate a winning message when they each arrived in Washington, tin cups in hand, aboard their own corporate jets. That fateful incident turned the media against Detroit and reminded Americans – or at least opened their minds to the prospect – that the automakers were in dire straits because of bad decisions made in the past and helped convince them that a shake out, instead of a bailout, was the proper course of action.

Although legislation to provide funding to the automakers passed in the House of Representatives last December, the bill did not garner enough support in the Senate, where it died. Prospects for any form of taxpayer bailout seemed remote and the proper course of action for GM and Chrysler, reorganization under Chapter 11, appeared imminent. An interventionist bullet, seemingly, had been dodged. But then, just days after then-Secretary Paulson claimed to have no authority to divert funds from the Troubled Assets Relief Program to the auto companies, President Bush announced that he would authorize bridge loans from the TARP of \$9.4 billion and \$4.0 billion to GM and Chrysler, respectively.

As the companies were incurring \$6 billion of operating losses per month at that time, it did not require a Ph.D. in finance to recognize that they would exhaust those funds in a matter of months and be back at the trough. And when they returned – as stipulated in the terms of the loans – to present their revitalization plans, it was evident that central to those plans were billions more dollars in taxpayer assistance.



As President Obama was correct to conclude at that point, the companies had not produced viable business plans worthy of continued financing. At that point, the president should have pointed the way toward the bankruptcy courts and moved on. Instead, he asserted a major role (and responsibility) for the administration by choosing to facilitate the bankruptcy processes of both companies by brokering pre-bankruptcy deals with major stakeholders. He even “influenced” the occasional personnel move and operational decision.

Both companies entered and emerged from bankruptcy protection in short order, restructured according to the plans crafted by the Obama administration. This testimony discusses some of the potential ramifications of the unusual bankruptcy processes and outcomes.

#### **Ramifications of the Auto Bankruptcies**

The emergence of General Motors from bankruptcy on July 10 marked the end of the first chapter of what is an evolving cautionary tale about the triumph of politics over markets and the rule of law. As the next chapter unfolds, some of the adverse consequences of a gratuitously political bankruptcy process for both GM and Chrysler are likely to become evident.

Bankruptcy was always the best option for GM and Chrysler. But both companies were resistant to filing for bankruptcy protection, allegedly because they were concerned that car buyers would eschew purchasing from companies in bankruptcy. Though it is difficult to make the case that car buyers would prefer to purchase from companies in limbo, bouncing from one bailout prospect to next, it is likely that resistance to standalone Chapter 11 filings had more to do with the kinds of changes an independent bankruptcy judge would have required to meet the threshold of a viable “going concern.” But after reassuring consumers that bankruptcy did not mean liquidation and that car warranties would be honored regardless, President Obama escorted both companies into the bankruptcy process.

Indeed, the process should have begun long before then. It should have happened long before President Bush felt compelled to circumvent the wishes of Congress and “lend” Chrysler and GM \$13.4 billion from the TARP allotment. It should have

happened long before President Obama had the chance to promise billions more and assume a large role for the U.S. government in Chrysler's and GM's restructuring and future operations. It should have happened long before President Obama created a huge moral hazard by strong-arming Chrysler's and GM's preferred lenders into taking pennies on their loan dollars, while giving preference to claimants of lesser priority. It should have happened long before Ford, Toyota, Honda, BMW, Kia, and the rest of America's automobile industry were implicitly taxed by the government's insistence on preventing two firms from exiting the market or otherwise reducing their presence by restructuring in accordance with established bankruptcy provisions. And it should have happened long before other businesses in other industries started to get the idea that failure is the new success.

President Bush's extension of "loans" to Chrysler and GM, in circumvention of the wishes of Congress and in contravention of the express purpose of the Troubled Assets Relief Program to support "financial institutions," was the original policy sin. Without those loans, both automakers likely would have sought protection under Chapter 11 of the bankruptcy code before the end of 2008. The duration of bankruptcy may have been longer than it ultimately turned out to be, but the outcomes might have been more in line with the precedents and orthodoxy of established bankruptcy law, and consistent with expectation of how market economies are supposed to function.

Instead, on account of President Obama's doubling down by taking responsibility for crafting and ramming through the courts his prepackaged "surgical" bankruptcies, the entire auto industry faces a precarious set of circumstances. Taxpayers are now majority stakeholders in a company whose success depends on good stewardship from a 536 CEOs with disparate political interests that are not necessarily aligned with GM's business interests. Prospects that taxpayers will be made whole for their \$50 billion coerced investment are dimmer than prospects that the public outlay will grow larger. As the Obama administration seeks to justify its wisdom in intervening, it will be tempted to use public policy and the tax code to tip the scales further in favor of GM, while hamstringing the competition.

Meanwhile, the United Autoworkers Union, typically more concerned about how corporate profits are carved up, rather than attained, is majority owner of Chrysler.

Neither GM's nor Chrysler's management situation is particularly confidence-inspiring, which bodes ill for the companies' prospects for raising capital to make the kinds of investments policy makers are intent on thrusting upon them in the name of emissions reduction. Prospects for raising capital in the form of debt have already suffered from the Obama administration's poor treatment of secured debt holders. Not only will that temper demand for GM's and Chrysler's debt, but for corporate debt across industries. With the economy still fragile and the number of bankruptcies still increasing, typically risk-averse preferred debt holders will be more inclined to remain on the sidelines, which will bid up the cost of debt at a time of tight credit and exploding budget deficits. It's not a pretty picture.

As one bankruptcy expert attested before this committee, the Obama administration's takeover of the bankruptcy process was a bit gratuitous.<sup>2</sup> The implication that our bankruptcy laws are incapable of handling reorganization of companies this large in a timely manner is at odds with historical experience.

But perhaps even more troubling in the case of GM are the fundamental conflicts inherent in simultaneously operating and regulating the same company. How will the administration and Congress balance law, compliance, policy, and the profit objective at the same time?

### **Conflicts between Profits and Policy**

#### ***The Dealerships Issue***

Support in Congress for legislation to compel the two automakers to restore contracts with dealerships slated for closure under their respective recovery plans affirms the views of skeptics: the pursuit of profits and political objectives often work at cross purposes. What is good for the bottom line is often incompatible with political objectives and political objectives are often incompatible with the bottom line. When decision makers are only concerned with one or the other, there is no problem. But when business operating decisions are also made or even just influenced by people who have politics to consider, something is going to give.

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<sup>2</sup> Testimony of David A. Skeel, Jr., U.S. House of Representatives, Judiciary Committee hearing, May 21, 2009.

Notwithstanding the possibility that the choice of dealership closings was made arbitrarily, if not politically, the fact remains that the companies must cut costs to survive, and excessive dealership networks are an area that is ripe for cutting. According the GMs nominal CEO, Fritz Henderson, the planned distributor closings will save GM about \$100 in distribution costs per vehicle. That translates into a few hundred million dollars of savings per year when factoring in the millions of units GM expects to produce.<sup>3</sup> That the companies face the specter of having to abandon those efforts because a majority of its 536 CEOs have political reasons for doing so bodes ill for the companies' prospects.

Not only does the dealership issue seriously elevate doubts that politics will not infect operational decisions at GM in particular, but it portends highly erratic management as the president and Congress wrestle for primacy in formulating policy at this majority taxpayer-owned entity. And since the Constitution is silent on the matter of which branch furnishes the CEO of a nationalized company, we may be in for a long period of uncertainty and instability.

The dealership issue represents just one of many potential conflicts on the horizon. We have already witnessed other clashes between what is right from a business perspective and what is imperative politically. The president's firing of Rick Wagoner and his subsequent endorsement of Fritz Henderson to fill GM's CEO slot, as well as his role in influencing the selection of GM's board members, raises questions about the administration's motivations. Is the president interested in filling key executive positions with people who are best qualified to run a profitable enterprise or who might be more amenable to the administration's plans for converting the economy from a carbon-based to a renewables-based one?

#### ***Profits vs. Green Production***

The conflicts inherent between the objectives of returning GM to profitability and making it a showcase for green production should be obvious. Returning GM to profitability will require higher revenues and lower costs, neither of which is made easier by imposing more rigid CAFE standards on the automakers. To quote my Cato colleague Alan Reynolds, "General Motors can survive bankruptcy far more easily than it can

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<sup>3</sup> [http://voices.washingtonpost.com/economy-watch/2009/06/gm\\_chrysler\\_heads\\_face\\_senate.html](http://voices.washingtonpost.com/economy-watch/2009/06/gm_chrysler_heads_face_senate.html).

survive President Barack Obama's ambitious fuel economy standards, which mandate that all new vehicles average 35.5 miles per gallon by 2016.”<sup>4</sup>

Fuel efficiency standards are particularly punitive toward automakers that sell larger vehicles. The Big Three – GM and Ford in particular – have had their greatest success in the larger vehicle market. Their pickup trucks, sport utility vehicles, luxury cars, and muscle cars all have higher profit margins than their small vehicle offerings. But to even be eligible to sell an adequate number of these vehicles and reach overall profit targets, they must sell a sufficient number of small cars to attain a fleet efficiency of 35.5 miles per gallon. In other words, to satisfy consumer demand and realize profits on their most popular models, GM will have to sell—at low or no profit, or at a loss—a sufficient number of high mileage vehicles that are not as popular as policymakers imagine them to be.

GM in particular is at a huge disadvantage vis-à-vis the foreign nameplate producers in the United States, who already have loyal customers for their high-mileage vehicles. So Toyota and others will be able to compete with greater maneuverability in the market for large and luxury vehicles (where GM is most competitive), while GM is forced to divert resources to cultivate a skeptical market for its small cars.

Warren Brown, the *Washington Post's* auto expert, reviewed the Toyota Yaris S in his column this past Sunday. Although he is favorably disposed to the car, he writes: “[F]or all of its many virtues, the little Toyota Yaris is selling poorly in this country, where its retail numbers are down 40.4 percent in the first six months of 2009.”<sup>5</sup> And then in a passage that speaks directly to policymakers obsessed with fuel efficiency standards, he writes: “But here is what for many of you will be a hard-to-swallow truth: Fuel-sippers such as the Yaris are selling in numbers well below those of the Ford F-series and Chevrolet Silverado pickup trucks... We want cars such as the Yaris and Fit when gasoline prices are high, or when gasoline is in short supply. But when gasoline is flowing at prices that make us smile, which it usually does in the United States, we’d much rather have a Chevrolet Camarro SS with a 6.2-liter, 426-horsepower V-8 engine.

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<sup>4</sup> WSJ, July 2, 2009

<sup>5</sup> Warren Brown, “What We Say We Want, Not What We Really Want,” *Washington Post*, p. G12, July 19, 2009

Strange as it might seem in these hard times, Chevrolet isn't having any trouble selling that one."<sup>6</sup>

The lesson here is that forcing automaker to produce vehicles that Americans demand only when fuel prices are in the \$4 dollar range is not going to help GM or Chrysler. The direct and honest approach to increasing demand for small vehicles – although I do not endorse it – is a national fuel surcharge that keeps the price of gasoline relatively constant at high levels. That idea is unlikely to be very popular around the country.

Between the Congressional pushback over the dealerships issue and the insistence on higher fuel efficiency standards, we see the objectives of two broad groups of policymakers: those who want green production and treat the costs of that goal as immaterial, and those who want the auto companies to remain a jobs program, regardless of the imperative of shedding workers to become more competitive. Neither camp seems to understand or care very much that fulfillment of their objectives will only hamper recovery, at best, if not drive the automakers out of existence.

#### **Making the Taxpayers Whole**

Let us not lose site of the fact that \$65 billion in taxpayer funds have been directed to GM and Chrysler over the past eight months—not as many zeroes on the end as seems to be required to get Washington's attention these days, but still a lot of money. Most Americans are not too pleased about having these "investments" made on their behalf. But Washington may be forgiven if the government divests of these companies quickly, with large enough profits and returns on investment to help soothe the public's misgivings.

In the case of GM, for taxpayers to get back their principal (without any interest or capital gain) the company will have to be worth \$83 billion. That figure is derived by considering that taxpayers have "invested" roughly \$50 billion in GM, which is deemed by the bankruptcy plan to be worth a 60 percent share in the company. And 60 percent of roughly \$83 billion equals \$50 billion. How likely is it that the value of GM will reach \$83 billion anytime soon (barring dramatic inflation)?

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<sup>6</sup> Ibid.

At its historic high value in 2000, GM's worth (based on its market capitalization) stood at \$60 billion. Thus, the company's value must increase by 38 percent from its historic high, achieved in the heady days of 2000, when Americans were purchasing 16 million vehicles per year, just to return principal to the taxpayers. But U.S. demand projections for the next few years come in at around 10 million vehicles, which suggests that prospects for the government divesting of GM profitably are extremely remote.

In fact, it is much more likely that the taxpayer investment in GM, directly or implicitly, will increase further, as the administration and some in Congress have incentive to use policy (tax policy, trade policy, and regulations) to induce consumers to purchase GM products, to subsidize production and, indeed, to hamstring GM's competition. And this all raises the question of what will happen to Ford and the other foreign nameplate producers when the lawmakers and administrators have a favorite horse in the race. Ford is relatively healthy now, but continued support for GM and Chrysler could well drive Ford to the trough, too. At some point, Ford's management might reckon that their closest competitors, who made terrible business decisions over the years, just got their debts erased and their downsides covered. Why not travel down that path, if things get too tough? That calculation, if it is ever made, presents the specter of another taxpayer bailout to the tunes of tens of billions of dollars, and another government-run auto company.

#### **The U.S. Auto Industry is Healthy**

In 2008, the Big Three accounted for roughly 55% of U.S. light vehicle production and 50% of U.S. sales. To speak of the U.S. automobile industry these days, one must include Honda, Toyota, Nissan, Kia, Hyundai, BMW - and other foreign nameplate producers who manufacture vehicles in the U.S. They are the other half of the U.S. auto industry. They employ American workers, pay U.S. taxes, support other U.S. businesses, contribute to local charities, have genuine stakes in their local communities and face the same contracting demand for automobiles as do GM, Chrysler, and Ford. The important difference is that these companies have a better track record of making products Americans want to consume.

If GM or Chrysler or Ford went belly up and liquidated, people would lose their jobs. But the sky would not fall. In fact, that outcome would ultimately improve prospects for the firms and workers that remain in the industry. That is precisely what happened with the U.S. steel industry, which responded to waning fortunes and dozens of bankruptcies earlier in the decade by finally allowing unproductive, inefficient mills to shutter.

Bailouts or forced subsidizations are clearly unfair to taxpayers, but they are also unfair to the successful firms in the industry, who are implicitly taxed and burdened when their competition is subsidized. In a properly functioning market economy, the better firms—the ones that are more innovative, more efficient, and more popular among consumers—gain market share or increase profits, while the lesser firms contract. This process ensures that limited resources are used most productively and that the most successful firms lead us into the future.

Last November, one day before the CEOs of GM, Ford, and Chrysler told the Senate Banking Committee that their industry faced imminent collapse without an emergency infusion of \$25 billion, a new automobile assembly plant opened for business in Greensburg, Indiana. Although the hearing on Capitol Hill received far more media coverage, the unveiling of Honda's latest facility in the American heartland spoke volumes about the future of the U.S. car industry.

There are plenty of healthy auto producers in the United States, all of whom are facing contracting demand. The ones that are best equipped to survive the recession will emerge stronger. But we undermine the objective if Ford, Toyota, Kia, Honda, Volkswagen and all the others cannot compete on a level playing field with GM to come up with the next generation of fuel-efficient cars.

### **Some Final Thoughts**

The demise of these two iconic American automakers, Chrysler and GM, and the U.S. government's assumption of responsibility for their rehabilitation occasioned a direct appeal from President Obama to American economic "patriotism" a few months ago. The president exclaimed, "If you are considering buying a car, I hope it will be an American car." Ignoring, for the moment, the impropriety of the U.S. president



attempting to influence commercial outcomes by endorsing particular products, even if one were inclined to buy an American car, the tricky question remains: What constitutes an “American” car? Economist Matthew Slaughter, in a recent *Wall Street Journal* opinion-editorial, attempted to elucidate:

What exactly makes a car “American?” Does it mean a car made by a U.S.-headquartered company? If so, then it is important to understand that any future success of the Big Three will depend a lot on their ability to make—and sell—cars outside the United States, not in it. A big reason Chrysler has fallen bankrupt is its narrow U.S. focus. It has not boosted revenues by penetrating fast-growing markets such as China, India and Eastern Europe. Nor has it lowered costs by restructuring to access talent and production beyond North America.<sup>7</sup>

However, the incredulous, angry reactions from American labor unions, their patrons in Congress, and rabble-rousing television and radio personalities to GM’s since-reversed announcement that its revitalization plans include shifting more production to Mexico and China suggest that the above definition of an American car is not universally embraced. For those who object to GM’s plans, it is not the company’s bottom line that matters, but rather the company’s capacity to create U.S. jobs and stimulate U.S. economic activity. That GM might need to start making profits in order to create U.S. jobs and stimulate U.S. economic activity somehow doesn’t factor into the equation for these detractors. Instead, in zero-sum fashion, they see investment in foreign operations as antithetical to domestic job creation and economic growth.<sup>8</sup>

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<sup>7</sup> Matt Slaughter, *Wall Street Journal*, May 7, 2009

<sup>8</sup> For the record, the empirical evidence supports a positive relationship between the growth of a company’s foreign operations and the growth of its domestic operations. Following is an excerpt from Daniel T. Griswold, “‘Shipping Jobs Overseas’ or Reaching New Customers? Why Congress Should not Tax Reinvested Earnings Abroad,” *Cato Institute Free Trade Bulletin* No. 36, January 13, 2009: “Investing abroad is not about ‘shipping jobs overseas.’ There is no evidence that expanding employment at U.S.-owned affiliates comes at the expense of overall employment by parent companies back home in the United States. In fact, the evidence and experience of U.S. multinational companies points in the opposite direction: foreign and domestic operations tend to compliment each other and expand together. A successful company operating in a favorable business climate will tend to expand employment at both its domestic and overseas operations. More activity and sales abroad often require the hiring of more managers, accountants, lawyers, engineers, and production workers at the parent company.”

Perhaps, then, they would find Slaughter's alternative definition of an American car more accurate:

Or is an "American" car one made within U.S. borders? If so, then it is important to understand that America today has a robust automobile industry thanks to insourcing. In 2006, foreign-headquartered multinationals engaged in making and wholesaling motor vehicles and parts employed 402,800 Americans—at an average annual compensation of \$63,538—20% above the national average. Amid the Big Three struggles of the past generation, insourcing companies like Toyota, Honda and Mercedes have greatly expanded automobile operations in the U.S. In fiscal year 2008, Toyota assembled 1.66 million motor vehicles in North America with production in seven U.S. states supported by research and development in three more.<sup>9</sup>

But many Americans have rejected this definition of an American car as well. Ironically, the people who are most inclined to oppose outsourcing and define it as "shipping jobs overseas" tend to be the same people who criticize insourcing for shipping control of U.S. assets overseas. Even though the top 10 selling models of cars and trucks in the United States in 2008 were all produced in the United States, by American and foreign nameplate producers, and even though foreign nameplate producers employ hundreds of thousands of American workers, pay local and national taxes, support local economies, reinvest part of their earnings in their U.S. operations, and invest in other local businesses, the fact that corporate headquarters are located in Tokyo or Stuttgart or Seoul seems to hold sway.

At best, there is grudging acceptance of the possibility that these "insourcing" companies are part of the American manufacturing landscape, but it is impossible to imagine that the U.S. government would have ever rescued Toyota or Honda, if they had presented with financial prospects as dire as Chrysler's and GM's. Yet, as put in another recent Wall Street Journal article:

Once you put down the flags and shut off all the television ads with their Heartland, apple-pie America imagery, the truth of the car business is that it transcends national boundaries. A car or truck sold by a "Detroit" auto maker such as GM, Ford or Chrysler could be less American—as defined by the government's standards for "domestic content"—than a car sold by

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<sup>9</sup> Slaughter.

Toyota, Honda or Nissan—all of which have substantial assembly and components operations in the U.S.<sup>10</sup>

The automobile industry is one of many that “transcends national boundaries” and is only one example of why international competition can no longer be described as a contest between “our” producers and “their” producers. But the same holds for industries throughout the manufacturing sector. The fact is that the distinction between what is and what isn’t American has been blurred by foreign direct investment, cross-ownership, equity tie-ins, and transnational supply chains.

It’s time for U.S. economic policy to catch up to that commercial reality.

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<sup>10</sup> Joseph B. White, “What is an American Car?” *Wall Street Journal*, January 26, 2009.

Mr. COHEN. Our third witness is Mr. Richard Mourdock, Indiana State Treasurer, elected as 53rd Treasurer of the State of Indiana in November 2006, who is the chief investment officer for the State of Indiana, and, in that capacity, seeks to maximize a return of the State's investment portfolio. He serves on 13 boards or commissions in his official capacity.

Recently, he was in the center of the national automobile industry bailout as he pursued a case all the way to the United States Supreme Court on behalf of Indiana pensioners and taxpayers. I presume you know Steve Adams?

Mr. MOURDOCK. No, sir, I do not.

Mr. COHEN. All right. Prior to his appointment, he served two terms as county commissioner of Vandenberg County.

Mr. Mourdock, please proceed with your testimony.

**TESTIMONY OF RICHARD E. MOURDOCK,  
INDIANA TREASURER OF STATE**

Mr. MOURDOCK. Thank you, Chairman Cohen, Mr. Franks, honorable Members of the Committee. Let me first say that it is a true honor to be before you today. I have always had great reverence for our government and its systems, and frankly never imagined that I would be testifying to a congressional committee. I truly do consider this an honor to be invited.

Mr. COHEN. I never thought I would ever be the Chairman of the Committee. So we are both here.

Mr. MOURDOCK. I understand.

In being here today, I guess I am the only person who is a witness in either this panel or the previous panel who, like the Members of the Committee, has a political constituency. As you just stated, I represent a number of different funds including pension funds for Indiana State Police Officers, the Teachers Retirement Fund of Indiana, and also an infrastructure fund called the Major Moves Construction Funds.

Those three funds a year ago this month bought the secured debt of Chrysler Corporation. We bought that debt at a discount, and we did that for two reasons:

Number one, because it was secured debt. We saw it as a good investment. We bought it at 43 cents on the dollar.

And secondarily—and this is not an unimportant point. Secondarily, we purchased it because Chrysler Corporation has a very large footprint in the State of Indiana, as we have some 6,000 employees for Chrysler that work in the area of Kokomo.

When we made that investment decision, we never imagined that as secured creditors, the pension funds that I have mentioned would be ripped off and see their values greatly diminished, in what is an unprecedented act, through the bankruptcy process.

I come here today to tell you that I have been asked dozens of times: You took this case all the way to the United States Supreme Court, Richard. What was this about? Was it about the money? Was it about the law? Was it about the principle? Was it about the precedent?

And the answer is yes, it was about all those things because they are truly indivisible. They are indivisible when we consider the fact

of law and the precedents that we have seen now set for our financial markets.

I will not rehash the entire case for you. I will simply say that as a fiduciary of those funds, it is my utmost responsibility to not leave any stone unturned in trying to find the remuneration that our pensioners are due. I will continue to do that, hopefully, back to the United States Supreme Court.

We realize, even as I say that, that we cannot unring the bell. The sale of Chrysler will not be undone. The rights of all the other secured creditors have been vaporized by that sale. However, because the Supreme Court did choose to hear our case briefly, issued us a short stay, we have 90 days to go back to the Court to again seek redress. We are considering how we might best do that.

Questions that we could put before that Court, and I expect we will, are about the valuation of Chrysler. Clearly there is item after item that shows the valuation method that was done on a liquidation basis was not appropriate. It was said here this morning that liquidation was the only option. We do not agree. Once the United States Government agreed to partner up with Chrysler, it might have found some other partners and might have found a more reasoned and historically precedented decision and basis upon which a bankruptcy could have occurred. The reason that didn't happen was, along with it, came the date that this deal had to be done by June 15th. The big question became: Where did that date come from?

Ultimately, even the president of Fiat, upon whom it was continually said he would walk away from the deal if it didn't happen by June 15, on the day the sale took place he said, "No, that was never my date. I don't know where that date came from." In fact, that date also was derived by the government in making the sale happen very quickly.

There are a whole series of questions I might ask rather than answer here today. One of those questions is if the word "secured" creditor no longer has meaning, we need in the world of finance new definitions. Do the words "good faith and credit of the United States Government" still have meaning? Do the letters FDIC still have meaning?

Those are government entities. We need to make sure the bond market is secure.

You know, in June of this year, Secretary of the Treasury Timothy Geithner went to China, tried to convince the Chinese to keep buying our bonds. And let's all hope they do so. When he completed his official business, he spoke at the University of Beijing to a group of business students. He told them the American dollar was sound because of the sound and consistent practices of the American government and Administration. The room erupted in laughter. Chinese business students understand we must have consistency in the financial markets.

I could not agree more with the Obama administration on the point that we need more investment in American manufacturing if we again hope to be globally competitive. I hope we all see that. But this act, in stripping away the rights of secured creditors, is antithetical to good investing.

Investors, institutional investors especially, are changing the way they look at the world, and that is because of Chrysler. That is not a good precedent that we have before us.

I look forward to any questions you have to ask. I come here not as a lawyer. I am actually a geologist by training, as I was sharing with Mr. Franks, but I learned in 30 years of business a lot about the business world, and I know in that world there must be consistency if you hope to succeed. And that is what we have lost here in this process.

Mr. COHEN. Thank you, Mr. Mourdock. The man I was referencing was a State treasurer, but way before you were elected. So I missed your year in Tennessee.

[The prepared statement of Mr. Mourdock follows:]

PREPARED STATEMENT OF RICHARD E. MOURDOCK

**The Honorable Richard E. Mourdock**

Indiana State Treasurer

July 21, 2009

*Ramifications of Auto Industry Bankruptcies, Part III*

Mr. Chairman and distinguished Members of the Subcommittee, I would first of all like to thank you for allowing me the opportunity to participate in today's hearing. I am Richard Mourdock, Treasurer of the State of Indiana.

In providing testimony to you, please note that I am not an attorney though it is clearly the issues of law that cause me to be before you today. I come today as the elected official with strict fiduciary duties on behalf of all Hoosiers. More specifically, I come as the fiduciary of two specific funds in Indiana, the Major Moves Construction Fund and the Indiana State Police Pension Trust, and as a representative of the Teachers' Retirement Fund of Indiana.

As a result of the recent Chrysler filing, I was placed in the difficult position of asking the Southern Bankruptcy Court of New York to stop the proceedings on behalf of the funds that I represent. Simultaneously, Chrysler and the Obama administration were arguing that if the bankruptcy did not occur in a prompt manner all of the Chrysler jobs would be lost. Specifically, it was said that Fiat SpA, the company interested in "purchasing" twenty percent of the assets, would walk away from the deal causing the company to collapse if all aspects of the bankruptcy were not completed by June 15<sup>th</sup>, 2009.

Please note, Chrysler is a major employer in Indiana with some 6,000 jobs in the Kokomo area. Chrysler had recently contracted with a German firm, Getrag, to expand its operations in nearby Tipton County. In short, taking a position that was perceived to be against the company and its workers was not convenient, but it was the right thing to do.

I'm frequently asked why I decided to take on the administration and risk possibly losing thousands of Hoosier jobs. The answer to that is as simple as my oath of office. Like each of you, I pledged to "uphold the Constitution of the United States." As a fiduciary of public funds AND as an official who has taken a solemn oath to serve, I could not NOT act in a circumstance when I saw our beneficiaries losing value as a result of the law being violated.

I'm also often asked if I sought to stop the bankruptcy: 1) as a result of the monetary loss to the Hoosier funds or, 2) as a result of the violation of the law or, 3) as a protest in general principle of what was occurring. My answer is simply "yes". When viewed in the context of American law, fairness and propriety, these three issues are indivisible in the Chrysler case.

The legal points of contention will be discussed subsequently in my testimony. The fundamental chronology of events that causes me to be before the subcommittee today is as follows:

- In July of 2008, acting on behalf of the three Indiana funds, Reams Asset Management, (a private sector money-manager working for the state), purchased 'secured' debt of Chrysler with a face value of \$42 million dollars for approximately \$17 million dollars, \$0.43 on the dollar. The essence of their valuation is based on collateral claimed by Chrysler to be in excess of \$29 billion in the prior year. Also, as a most conservative approach, they valued Jeep's brand and revenues ALONE to be worth more than \$3 billion dollars. Indiana was pleased to make the investment as Chrysler's footprint in Indiana is a large one. We hoped to be a party to their success and certainly never imagined at the time we would have long-held, established investor rights ripped away from us.
- In September, 2008, the collapse of Lehman Brothers began a steep slide in the stock market and sent a serious shock wave through the economy. As a result, for the first time in fifty-six years of record keeping, the Federal Reserve noted a decrease in average American household indebtedness and the purchasing of "big ticket" items decreased dramatically. Heavily leveraged automakers, (Chrysler and General Motors), were devastated.
- In October, 2008, the Congress debated and subsequently passed the Troubled Asset Relief Program (TARP) to "aid the ailing financial industry."



- In December, 2008, Congress debated the “Automobile Bailout Bill” that failed to pass. Failing to find funding from Congress to assist the automakers, an executive order was signed by President George W. Bush to allow the auto companies, (Chrysler and General Motors), access to billions of dollars of bailout funds from the TARP.
- In early 2009, it had become apparent that funds from TARP would not be enough to save Chrysler and discussions between company executives and officials of the U.S. Treasury Department began to place Chrysler, LLC into a Chapter 11, Section 363 bankruptcy procedure, which would ultimately result in an auction of the assets.
- Details of the bankruptcy were unprecedented. For the first time in American history and totally counter to all established laws of bankruptcy, secured creditors would receive less than non-secured creditors. A majority of the secured debt was held by JP Morgan, Citigroup, Goldman Sachs Group, Inc. and Morgan Stanley which, in the prior six months, had received a total of \$90 billion in TARP proceeds. They were owed *in total* some \$6.3 billion.
- Officials of the U.S. Treasury convinced secured creditors of JP Morgan, Citigroup, Goldman Sachs Group, Inc., and Morgan Stanley to accept \$0.29 on the dollar for their investments instead of seeking just compensation through traditional bankruptcy proceedings despite the fact that they had previously all made loans to Chrysler based on claims of as much as \$29 billion in collateral the prior year.
- Private equity funds and pension funds held approximately \$300 million of secured Chrysler debt. Upon hearing of the unprecedented nature of the “settlement,” several private equity funds filed objections in the bankruptcy proceeding arguing the assets were being undervalued and that secured creditors rights were being grossly violated.

- President Obama in a press conference said those who would file objections to stop the sale were “unpatriotic,” “hedge funds,” “greedy speculators,” and “unwilling to sacrifice.” The case was stated to be, “One of the most complex bankruptcies in American history.”
- As widely reported, executives from the funds that filed the court cases began to receive threats and within three days withdrew their lawsuits and petitioned the court that the records be sealed to protect their identities.
- Bankruptcy documents identified that a number of states and localities had pension fund investments in Chrysler secured debt including funds representing public employees in California, Michigan and Indiana.
- At 10:00 am, on Monday, May 18, 2009, the United States Bankruptcy Court for the Southern District of New York notified the Indiana Treasurer of States’ Office by first class mail that in this, “.one of the most complex bankruptcies in American history” Indiana’s funds had thirty hours or until Tuesday, May 19, 2009, at 4:00 p.m. to file objections or claims.
- On Tuesday, May 19, 2009, an objection was filed on behalf of Indiana’s Major Moves Construction Fund, The Indiana State Police Pension Fund and the Indiana State Teachers’ Retirement Fund.

Indiana’s legal filings in the Chrysler, LLC bankruptcy sale made three essential points: First, the bankruptcy laws which have been in place protecting the rights of secured creditors cannot be arbitrarily overthrown by an act of the Executive. This is a violation of Article I, Section 8 of the U.S. Constitution in that Congress is solely assigned the role to determine uniform bankruptcy law. Neither the Courts nor the Executive can do this arbitrarily. Our funds suffered a “taking” in violation of the Fifth Amendment in that there was no “due process of law”. There was, and is in all financial arrangements between debtor and

creditor, a contractual relationship, which is here being rendered null and void. If allowed to stand, this violation of two party contracts undermines a basic and essential tenet of debt financing in the capital markets.

Second, money provided by the federal government to Chrysler is being provided illegally and clearly counter to the intent of Congress. When TARP was being debated then Secretary of the Treasury Henry Paulson testified the money was NOT for the auto companies. It was targeted to aid the ailing financial industry, i.e., those with "Troubled Assets" that needed a "Recovery Program." Evidence that the money was NOT intended to be an automotive bailout bill could not be more clearly illustrated than to review the failure of the separate automobile bailout bill presented in Congress in December 2008. If Congress had intended the TARP bill to cover the auto companies when it passed in October 2008, why were they even attempting to pass a separate automobile bailout bill just two months later? We believe both the Bush and Obama administration have acted illegally in this use of TARP funds.

Third, we argue that a *sub rosa* or "under-the-table-arrangement" between the Treasury and Chrysler prevented a fair valuation of the assets. In a legitimate auction sale, no potential bidder would be allowed to set the value of the assets being auctioned. But that is precisely what happened in this case as the Treasury was assigning values to creditors, determining which assets would be liquidated, what new parties, (i.e., Fiat SpA), would be brought into the deal, and how a new dealership network would be defined, etc. It was known from the outset that when the Chapter 11, Section 363 sale of the assets would occur, there would be only one bidder: the U.S. Treasury. Secured creditors could not have their rights protected or fairly valued in such an arrangement. Such an "insider-deal" reeks of impropriety.

Indiana's legal case began at the Southern Bankruptcy Court of New York where we participated vigorously in the hearing in order to raise our objections in the hopes that the plan might be rejected and a structured bankruptcy sale might occur pursuant to precedent. The bankruptcy court judge seemed interested only in ratifying the government's preferred plan as quickly as possible and failed to even address the merits of many of the legal issues we raised. Following his ruling, Judge Gonzales shortened the usual 10 day stay

period typically granted in bankruptcy cases. The District Court for the Southern District of New York has previously declined to take up the case but noted from the bench that the points of law raised in our petition had merit.

Officials of the U.S. Treasury then asked that the case be certified for immediate appeal to the United States Court of Appeals for the Second Circuit. We were pleased with this potential opportunity to have the merits of our case heard. During the hearing before the three judge panel, one of the judges commented from the bench to our attorney, "Don't you think the United States Supreme Court should be taking a swing at this?" Perhaps reflecting that sentiment, on Friday, June 12<sup>th</sup>, 2009, the Second District Court of Appeals issued a perfunctory order ratifying the bankruptcy court's decision and issuing a stay until 4:00 pm the following Monday to allow for United States Supreme Court review.

Indiana requested that the United States Supreme Court issue a stay to prevent the sale so that the points of law that we raised be reviewed in full context. Justice Ginsburg granted the stay on Monday, June 15<sup>th</sup>.

At approximately 7:00pm on Tuesday June 16<sup>th</sup>, 2009, The Supreme Court issued an order *per curiam* removing the stay and allowing the sale to proceed. The order stated that Indiana had failed to meet all the conditions required to stop the sale but did add: **"A denial of stay is not a decision on the merits of the underlying legal issues."**

The sale of Chrysler to the U.S. government occurred within forty-eight hours and the assets were promptly divided among the selected field of creditors and newly chosen stakeholders. Indiana is currently weighing its options for further legal action to establish the wrongfulness of the precedent set in the Chrysler case.

My purpose in providing testimony is not to re-state all of the intricacies of the case. I have included as an addendum to my testimony the filing of our legal brief for that purpose. I believe my presence before you

today is best served to ask the questions that Congress, and only Congress, can address in light of all that has happened in the Chrysler case. Indeed, while I am available to answer any of your questions to the best of my ability, the most significant questions that linger I cannot answer.

Questions and issues regarding the Chrysler bankruptcy are specific:

- Were the assets of Chrysler, LLC valued correctly for the purposes of the bankruptcy? Some questions had been raised by various groups that certain assets or automobile lines of Chrysler, LLC were intentionally undervalued. For example, the Jeep product accounts for more than \$500,000,000 in annual revenue from licensing arrangements for the use of its name. An appraisal not long before the auction had the value of Jeep at \$6 billion yet the total auction for all of the Chrysler assets resulted in a value of just over \$2 billion. Why should secured creditors feel they received anything close to fair value given these facts?
- Also, it has been reported that one existing, experienced, savvy, automotive investor group had negotiated with Chrysler in late February '09 for the purchase of the Dodge Viper brand for \$35 million. And yet, Chrysler executives told the bankruptcy court less than sixty days later the brand could only be assigned a value of \$5 million. How can a good-faith purchaser be told "no" when he offers \$35 million only to see the same product valued for \$5 million weeks later in a government auction?
- The crisis mentality that drove the process was totally undermined by the President of Fiat. Prior to the bankruptcy sale in each court, the federal government argued that if the sale didn't close by June 15<sup>th</sup>, the deal with Fiat would fall apart. I argued throughout the several weeks of Indiana's involvement that this made no sense whatsoever as Fiat was not required to expend a single penny to acquire the 20% stake in Chrysler. Said differently, if someone is offered a \$400,000,000 asset at no cost and told that it wouldn't be available until next week, I'm betting

they'd return one week later. Or one month later. \$400,000,000 for zero expenditure is too good a deal to walk away from. Sure enough, on the day of the sale Fiat's president said exactly this and indicated he was unsure where the June 15<sup>th</sup> date had originated. Clearly, it came from the Treasury in its rush to close the deal in haste which was again, greatly to the detriment of the investors.

For a detailed analysis of the legal consequences of this case see the attached article *Assessing the Chrysler Bankruptcy*.

Broader and greater questions related to the precedents set if the actions of the Congress continue to be ignored by the Executive and if the rules of law no longer have application:

- If the term "secured creditor" no longer have meaning, what other terms of art in the world of finance no longer have meaning? The long-standing rights of secured creditors have been so well understood that during the War of 1812 the U.S. government continued to pay principal and interest to British citizens even as we were at war with their nation! Our government realized then that if you default to "secured creditors" regardless of the circumstance, you have begun to destroy your own credit rating. Recent discussions by Russia and China to seek a new international reserve currency are not unrelated to the message of the Chrysler bankruptcy. Change the rules and the players will change. If foreign investors in U.S. Treasury debt sense that "good faith and credit of the United States government" can be swept away with an arbitrary act to deal with a momentary crisis, we will have a problem far, far greater than Chrysler in scope and impact.
- If investors no longer feel the law is uniform, predictable, and based on precedent, why would they continue to invest in American markets? I could not agree more with the Obama administration's belief that the American manufacturing sector must be revitalized if we are to again become globally competitive. But the Chrysler precedent of stripping value and rights

from secured bond holders flies in the face of maintaining a sound investment environment. It is easy to predict that hundreds of billions of dollars will begin to be invested in foreign markets as a result of this decision.

I realize that most who come to testify before committees of Congress typically come to demand some change or some new set of laws or regulations. They come to revise a set of laws that may no longer apply to modern circumstances but I do not.

I appreciate the opportunity to come before you to plead simply that Congress act pursuant to Article I, Section 8 that mandates that you, not the Executive, not the Judicial, make a uniform set of bankruptcy laws. It is your job but you have already done it. You need not do it again. You do not need to revise what you have already done. You need only stand to argue that what has been put in place has worked for almost two hundred years. And what is the evidence of that success? The strongest, most vibrant economy on the planet over that period. Investors seek stability in the market place and that's what our laws have provided. It is also why investment houses often use in their advertising words that paint mental images of stability. They include the image of rocks or bluffs, cliffs, or mountains. Never do they send a message of shifting sands. Yet that is what today's investors see when secured investors rights are thrown away in the name of momentary economic crisis or perceived threat. It is a dangerous message to send. The members of this Subcommittee need to stand firm on what the investing community has long held in violate: sound, consistent, and stable bankruptcy laws.

If you do that, investment will flow back into American corporations. If you fail to do so, it, like so many American jobs, more American capital will flow overseas as investors will want to put their money in more stable markets where the rules don't change with the moment.

Mr. Chairman and distinguished Members of the committee, I would like to thank you for allowing me to testify at this hearing today and to express my views and concerns about current bankruptcy laws and unintentional consequences that could affect the financial markets in the future.

**ATTACHMENT**

**Institute for Law & Economics**  
**University of Pennsylvania Law School**  
Research Paper No. 09-22

**Public Law and Legal Theory**  
**University of Pennsylvania Law School**  
Research Paper No. 09-17

**Assessing the Chrysler Bankruptcy**

**Mark J. Roe**  
*Harvard Law School*

**David A. Skeel**  
*University of Pennsylvania Law School*

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## Assessing the Chrysler Bankruptcy

Mark J. Roe and David Skeel

### Abstract

*Chrysler entered and exited bankruptcy in 42 days, making it one of the — perhaps the — fastest major industrial bankruptcies in memory. It entered as a company widely thought to be ripe for liquidation if left on its own, obtained massive funding from the United States Treasury, which pumped in cash to fund paying several billion dollars to pre-bankruptcy creditors, brought in FLAT to manage the post-bankruptcy operation, and exited through a pseudo sale of the main assets to a new government-funded entity. The unevenness of the compensation to prior creditors raised considerable concerns in capital markets, which we evaluate here. We conclude that the Chrysler bankruptcy cannot be understood as complying with good bankruptcy practice and that it resurrected discredited practices long thought interred in the 19<sup>th</sup> and early 20<sup>th</sup> century equity receiverships. The bankruptcy court opinion — one that neglected to even mention the Code section, § 1129, that enumerates the standards for plan confirmation, much less apply those standards — needs to be rejected as hastily done: bankruptcy practice would be improved by a sharp appellate rejection of the Chrysler bankruptcy's structure. Some of that restoration of good bankruptcy practice could be facilitated via the circuit court's pending opinion, which could focus on the plausible elements of priority compliance in the record.*

**ASSESSING THE CHRYSLER BANKRUPTCY**

Mark J. Roc and David Skeel

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## Assessing the Chrysler Bankruptcy

Mark J. Roe and David Skeel\*

### INTRODUCTION

The Chrysler chapter 11 proceeding went blindingly fast. One of the larger American industrial companies entered chapter 11 and exited 42 days later. Clearly speed was achieved because of the government's cash infusion of \$15 billion on noncommercial terms into a company whose assets were valued at only \$2 billion.<sup>1</sup> The influx came at a time when the American economy was sinking, financial institutions were weakened, and the government feared that a collapse of the auto industry would have grave consequences for the rest of the economy. As a matter of bankruptcy technique, the chapter 11 was a tour de force.

The economic policy and political background is worthy of its own analysis, but we shall mention it only in passing, and it will not be our focus, except as it interacts with the Bankruptcy Code. Briefly, Chrysler was a weak producer, making cars that had limited consumer acceptance, in an industry facing substantial domestic and world-wide over-capacity. Normally, industries facing such pressure need to shrink and their weakest producers, like Chrysler, are the first candidates for shrinkage.

Our primary focus, though, will be on the technical structure of the Chrysler bankruptcy under the Code. Did the bankruptcy introduce, or magnify, tactics, procedures, and doctrines that would facilitate sound, fast bankruptcies in the future? Did the Chrysler reorganization reveal defects latent in the chapter 11 mechanisms? Could the rapid results only be obtained in the future if the government is willing to flood the bankrupt firm with cash on subsidy-type terms? Or was the process sufficiently innovative as to be new? And, if new, is it fully desirable?

Our overall conclusions are not favorable to the process, results, and portents for the future. The Chrysler bankruptcy process used undesirable mechanisms that federal courts and Congress struggled for decades to suppress at the end of the 19<sup>th</sup> and first half of the 20<sup>th</sup> centuries, ultimately successfully. If the mechanisms are not firmly rejected, either explicitly or via judicial (or legislative) distinction or via a collective forgetting of the event among bankruptcy institutions, future reorganizations in chapter 11 will be at risk, with the risks sufficient to affect capital markets. (Some of this rejection, or at least reinterpretation, could occur in the Second Circuit's opinion on the appeal, which is pending as we write.) Although the government's presence obtained

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\* Professors, Harvard and the University of Pennsylvania Law Schools, respectively. Special thanks to A. David Lander for research assistance. Barry Adler, Douglas Baird, Martin Bienenstock, Lynn Lopucki, and Robert Rasmussen were generous with their comments.

<sup>1</sup> "The Governmental Entities loaned the Debtors at least \$4 billion prepetition, and nearly \$5 billion postpetition, all of which is a secured debt obligation of the Debtors." *In re Chrysler LLC*, 405 B.R. 84, 108 (Bankr. S.D.N.Y. 2009). In addition, they are providing \$6 billion in secured loans to New Chrysler. *Id.* at 92.

judicial deference, the government's presence is not needed to use the defective procedures. Every reorganization in chapter 11 can use the same, defective process.

The Chrysler case warrants attention for other, albeit related reasons. Credit markets reacted negatively to the Chrysler reorganization process and results. George J. Schultze, a manager of a hedge fund holding Chrysler debt, said "one reason we went into it was because we expected normal laws to be upheld, normal bankruptcy laws that were developed and refined over decades, and we didn't expect a change in the priority scheme to be thrust upon us." He warned that those "who make loans to companies in corporate America will think twice about secured loans due to the risk that junior creditors might leap frog them if things don't work out. It puts a cloud on capital markets and the riskiest companies that need capital will no longer be able to get capital."<sup>2</sup> Warren Buffett worried in the midst of the reorganization that there would be "a whole lot of consequences" if the government's Chrysler plan emerged as planned, which it did. If priorities are tossed aside, as he implied they were, "that's going to disrupt lending practices in the future." "If we want to encourage lending in this country," Buffett added, "we don't want to say to somebody who lends and gets a secured position that the secured position doesn't mean anything."<sup>3</sup>

Were they right? Were priorities violated?

Perhaps priorities were breached, perhaps they weren't. The most troubling Code-based aspect of the Chrysler bankruptcy is that it is difficult, perhaps impossible, to know from the structure of the reorganization. Yet obtaining that knowledge is one of the core goals of chapter 11 practice. Chrysler breached appropriate bankruptcy practice in ways that made the valuation and allocation of Chrysler's value to pre-bankruptcy creditors opaque. The requirement in § 1129(a)(8) that each class of creditors consent or receive full payment wasn't used. A market test wasn't used.

<sup>2</sup> Tom Hals, *Chrysler Secured Creditor to Fight "Illegal" Plan*, REUTERS, May 7, 2009, <http://www.reuters.com/article/ousiv/idUSTRE5464WC20090507>.

<sup>3</sup> Lou Whiteman, *Buffett Warns of Chrysler Crandown Ramifications*, THE DAILY DEAL, May 5, 2009. These were not isolated comments in capital markets. Cf. Nicole Bullock, *Painful lessons for lenders in Chrysler debacle*, FIN. TIMES, May 7, 2009, available at <http://www.ft.com/cms/s/0/8ae2592e-3b31-11de-ba91-00144feabdc0.html>.

"Given that so much of total borrowing across all asset classes is first lien in nature, the damage that would occur to the economy as a result of higher first lien borrowing costs resulting from lenders requiring a higher return to compensate them for an unknown interpretation of claim priorities could be substantial," says Curtis Arledge, co-head of US fixed income at BlackRock, Inc. ...

....

"It is particularly important at this stage of the distressed cycle for lenders to have confidence in pre-existing contracts and rules. We are entering a period of record corporate defaults and the need for bankruptcy financing and financing for distressed companies will only continue to grow," says Greg Peters, global head of credit research at Morgan Stanley.

....

"People are pretty comfortable with the bankruptcy rules. What they are trying to do in the Chrysler situation is unprecedented," says Jeff Manning, a managing director specialising in bankruptcy and restructuring at Trenwith Securities, the investment bank. "This isn't the way the game is supposed to be played."

....

"Now there is a new risk: government intervention risk," Mr Persky says. "And it is very hard to hedge." Steve Persky, managing director of Dalton Investors, a Los Angeles-based hedge fund that specialises in distressed debt.

There was no judicial valuation of the firm. Chrysler simply went through the motions of selling its principal assets to a newly formed entity controlled by its previous principal creditors.

Stunningly, the bankruptcy court did not analyze the § 1129 issues. Indeed, that section — the core to the modern Bankruptcy Code, outlining the conditions the judge must find prior to confirming a plan of reorganization — is not even mentioned once in the central judicial opinion in the Chrysler proceeding. If the pseudo sale was a de facto plan of reorganization because it did so much more than simply selling assets for cash, then it was incumbent upon the bankruptcy process to assess the terms for overall, satisfactory consistency with § 1129. One can have confidence that if a capable bankruptcy judge does not see fit to mention § 1129 in a sale that is making many of the determinations normally made in chapter 11 under § 1129, then something peculiar is happening. The most obvious hypothesis is that one could not mention it, if one feared that one were witnessing a reorganization that could not comply with § 1129.

We can hope that the breach of proper practice will be confined to Chrysler. But the structure of the deal is not Chrysler-specific and plan proponents are already citing the Chrysler arrangement as precedent.<sup>4</sup>

The Chrysler process may have revealed fault lines in the structure of chapter 11: Although the government may have been needed in the case to obtain judicial deference, the government's presence as a noncommercial lender isn't needed, as a matter of Code structure, for the interested players to use the Chrysler mechanism. Any coalition of creditors and managers can use the § 363 sale in the same way, if they can persuade a judge to approve their proposed fictional sale. Hence, the Chrysler bankruptcy, if it becomes a pattern, has the potential to disrupt chapter 11 overall, with potentially negative consequences for lending markets as well. Without strong appellate rejection of Chrysler, perhaps via dictum in a § 363 appellate decision from the Second Circuit, we could be in for a rough ride in bankruptcy reorganization for years to come.

A roadmap for the article: In Part I, we outline the structure of the Chrysler bankruptcy, which was effectuated as a § 363 sale. In Part II, we analyze the best theoretical structure for how § 363 should interact with the rest of the Code, particularly § 1129. Section 363 has the potential to do much good — by repositioning companies quickly in the merger market — and the potential to do much damage, by running roughshod over the rest of the well-honed chapter 11 structure. In Part III, we examine the cases, which largely but not completely conform to the theoretical structure for § 363 sales that we outline in Part II. To substitute for usual creditors' protections of § 1129, courts had previously developed makeshift remedies in § 363 sales, requiring consent and a genuine market test. In Parts IV and V, we show that the Chrysler sale failed to use such checks. We also point to valuation inconsistencies in the deal structure that the courts needed to resolve, but did not.

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<sup>4</sup> Ashby Jones & Mike Spector, *Creditors Cry Foul at Chrysler Precedent*, WALL ST. J., June 13, 2009, at B1; Peter Kaufman, president of investment bank Gordian Group, questioned "[t]he excuse that [the auto cases] are 'special circumstances,'" saying "I'm sure that's right until the next time it's a 'special circumstance.'"

After briefly exploring in Part VI how the government might have structured its investment in Chrysler differently, to reach its policy goals without stressing normal bankruptcy practice, we speculate in Part VII about Chrysler's implications for future bankruptcy practice. Nothing about the Chrysler sale limits its template to cases in which the government is a creditor, and barely two weeks after the sale order was stamped the *Chrysler* decision had already become an issue in several other cases.

In Part VIII, we remark on the similarity of the Chrysler reorganization to 19<sup>th</sup> century reorganization via the equity receivership. On the positive side, the Chrysler reorganization handled a practical business problem via a sale format as did the equity receivership's reconstruction of the American railroad system. On the negative side, the Chrysler reorganization reintroduced the equity receivership's most objectionable attributes, particularly its casual regard for priority — attributes that the reorganization machinery regularly rejected throughout the 20<sup>th</sup> century, until now. Before concluding, we speculate on business features that might push toward more Chrysler-like bankruptcies in the future: if major creditor groups increasingly not only supply funding, but also provide critical goods and services for the debtor's operations, then Chrysler could represent a new direction, one for which chapter 11 as now constituted is not fully prepared.

The damage will need to be undone. Eventually, one can hope that the Chrysler deal will be seen as an anomaly. The Second Circuit could more quickly limit the reorganization's mischief by emphasizing the least objectionable aspects of the sale, and rejecting its excesses, when it explains its decision not to halt the sale.

## I. THE DEAL STRUCTURE

The basic deal structure is straightforward to summarize. Pre-bankruptcy, Chrysler was a private firm, owned by Cerberus, a large private equity fund. As of the bankruptcy, its two largest creditors were secured creditors owed \$6.9 billion and an unsecured employee benefit plan, owed \$10 billion. It also owed trade creditors about \$5 billion, and it had warranty and dealer obligations of several billion dollars.<sup>5</sup>

The government created and funded a shell company that, through a § 363 sale, bought substantially all of Chrysler's assets for \$2 billion, giving the secured creditors a return of 29 cents on the dollar. This New Chrysler (formally: New CarCo Acquisition LLC) then assumed the old company's debts to the retirees, most dealers, and trade creditors. The unsecured claims of the retirees' benefits plan were replaced with a new \$4.6 billion note as well as 55% of the new company's stock.

Priority seemed violated because unsecured retiree claims were getting a promise of well over 50 cents on the dollar and unsecured trade creditors were being paid in full, while the secured creditors were getting 29 cents of the dollar. The pseudo-sale made no provision for creditors such as present and future products liability claimants for defects in Chrysler cars now on the road. Their claims can only be brought against the Old Chrysler, which will shortly have no assets.

<sup>5</sup> Affidavit of Ronald E. Kolka in Support of First Day Pleadings, 405 B.R. 84 (No. 09-50002), 2009 WL 1266134, ¶¶ 27, 30, 35, 39.

In an ordinary bankruptcy, the structure would indeed be *prima facie* improper. But this was not an ordinary bankruptcy, because the government was lending on noncommercial, policy-oriented terms. The United States Treasury and the government of Canada had lent roughly \$4 billion to Chrysler prior to bankruptcy, and then agreed to provide \$5 billion in debtor in possession financing and \$6 billion in exit financing.<sup>6</sup> Some of the excess promised to the retiree trust was surely spilling over from the government's concessionary lending. The difficulty — the core Chrysler bankruptcy problem — is that the bankruptcy process failed to reveal how much. Its structure was consistent with several sharply differing real results. Maybe the retirees' payout came solely from the government's new money as funneled through New Chrysler, maybe some of it came from the prior secured creditors, maybe the reorganization created unusually lucrative synergies, or maybe the government even subsidized the secured creditors as well. It's impossible to tell because the process was opaque, with none of the standard mechanisms used to validate the process: a judicial valuation, an arms-length bargained-for settlement, or a genuine market test.

Simply stated, although the secured creditors received \$2 billion on their \$6.9 billion claim, there is nothing in the *structure* of Chrysler's bankruptcy process inconsistent with the proper number for the secured being not \$2B, but \$3B, or \$1B. Or zero.

## II. THE § 363 PROBLEM: CONCEPT

Section 363 of the Bankruptcy Code authorizes the debtor to sell assets out of the ordinary course of business at any point in the bankruptcy case, upon obtaining the bankruptcy court's approval. But § 1129 — arguably the core of the chapter 11 — requires that, before the court approves a plan of reorganization, it ascertain that the plan complies with the usual priorities, absent creditor consent to deviation from those priorities.

In a simple sale, these two sections do not conflict. The debtor petitions the court to sell, say, a subsidiary that the firm cannot manage well and that's deteriorating in value. The asset leaves the debtor's estate but cash comes back in. The cash for the sale is then available to all of the pre-bankruptcy creditors, who can thereafter litigate their claims to priority, equitable subordination, post-petition interest, and so on.

A complex sale, however, can determine priorities and terms that the Code is structured to determine under § 1129, and is not structured to determine under § 363. For example, consider the possibility that in addition to the sale, some pre-bankruptcy creditors come over to the purchasing firm, but others do not. The purchaser buys the debtor's principal operating subsidiary, say, and agrees to pay one of the subsidiary's creditors, but not its other creditors. Some of the subsidiary's dealers are terminated, left behind, and have damage claims left unpaid, but others move over to the purchaser and remain in operation. The purchaser agrees to assume some of the subsidiary's ongoing warranty claims, but not liability for previously sold products that turn out to be defective. Or, the purchaser earmarks some of the consideration used in the sale as only being usable by a particular set of previous creditors of the subsidiary.

<sup>6</sup> 405 B.R. at 92, 108.

All these sales terms would then determine core aspects that would normally be handled under § 1129, with disclosure, voting under § 1129(a)(8), and if voting fails, via a judicial cram-down under § 1129(b). If the restructuring is done via § 363, courts would have to resolve how to reconcile such sales with § 1129.

The simplest reconciliation would be to bar such sales that determine core chapter 11 terms, on the theory that § 363 could not, and should not, be allowed to eat up the rest of chapter 11. Congress intended that the chapter 11 proceeding end with the bankruptcy judge going through the § 1129 check-list for compliance, typically including full disclosure of the company's business operations and the impact of the plan on the creditor groups, with creditors thereafter voting and the judge evaluating the plan. If the sale determined creditor priorities *sub rosa*, there would be little — and at the limit, nothing — for the judge to check off. In form at least, the courts have said as much, with the operative phrase being that a bankruptcy court cannot approve a *sub rosa* plan of reorganization in the guise of a § 363 sale.

But that kind of formalistic reconciliation isn't good enough for two reasons, one theoretical and one practical. The theoretical one is that every sale affects the § 1129 bargaining. Simply by reducing a variable outcome to a fixed number, by collapsing the probability distribution of a firm's future income stream, a sale for cash reduces the range of bargaining tactics. Imagine a firm whose assets are worth between \$1 billion and \$3 billion, because its industry faces an uncertain future during the bankruptcy period. Its senior creditors are owed \$2 billion, and it proposes to sell its assets to a buyer for \$2 billion. Before the sale, when the firm was worth somewhere between \$1 and \$3 billion, the juniors had a shot at obtaining value in the chapter 11 proceeding, even though the firm owed \$2 billion to seniors. The juniors could stall to see if the \$3 billion number turned up. Or the possibility of the \$3 billion value turning up gave them leverage with the juniors in negotiating a consented-to plan of reorganization. But with the variable future outcomes reduced to \$2 billion in present cash, there's no wedge left here for the juniors to work with. More generally, behind the § 1129(a)(8) process is the "what if" alternative — what if the parties cannot bargain to a settlement? If they cannot settle, the judge can cram the plan down, but that cram-down ultimately needs a judicial valuation of the firm and its claims, a process that is usually thought to be highly inaccurate.<sup>7</sup>

The second, practical problem with rejecting all *sub rosa* plans as not being good enough is quite important: a sale is just too attractive a business disposition for many bankrupts to give up. Bankrupt companies come disproportionately from declining industries that should shrink. An excellent way for a declining industry to consolidate capacity is via merger, so that the strongest parts of each partner can be molded together. And bankrupt firms, if poorly managed, can be repositioned to be managed by a better managerial team. If a few terms have to be handled in the § 363 sale that would ordinarily be handled under § 1129, then courts, and bankruptcy

<sup>7</sup> See, e.g., Walter Blum, *The Law and Language of Corporate Reorganization*, 17 U. CHI. L. REV. 505, 571-580 (1950) ("[reorganization value] is a fictional value.... It is set by the estimates of persons who are not standing back of them with a willingness to invest their own funds."); Mark J. Roe, *Bankruptcy and Debt: A New Model for Corporate Reorganization*, 83 COLUM. L. REV. 527 (1983); Kerry O'Rourke, *Valuation Uncertainty in Chapter 11 Reorganizations*, 2005 COLUM. BUS. L. REV. 403, 427.



doctrine, should find a way to accommodate the quick sale, but without giving up the entire § 1129 structure of protections and priorities. One potential negative fallout from the Chrysler bankruptcy is that the eventual push-back to its casualness in handling priority could become an attack on § 363 in its entirety, as opposed to its specific implementation. If sales were sharply curtailed, as opposed to being conditioned and properly structured, then bankruptcy would be set back.

Fast sales with some priority determinations can be reconciled. The court can identify the offending feature of the § 363 sale and ascertain whether it would have succeeded under § 1129. For example, if a single creditor objects to the sale, because some prior creditors are indeed going over to the new entity, the court can determine that the creditor received liquidation value (§ 1129(a)(7)) and that the creditor class to which the dissenter belongs consented to any deviation in priority in allocation of the going concern value (§ 1129(a)(8)). If a class consented overall but a dissenter would clearly be getting liquidation value, then the court could determine that even though the sale had aspects of a sub rosa plan, those features if done above-board would still have permitted plan confirmation under § 1129.

### III. THE § 363 PROBLEM: THE APPELLATE CASES

Overall, the prior appellate cases conformed to the concepts laid out above. Bankruptcy law, based on leading 1980s decisions in the Second and Fifth Circuits, was largely in good shape doctrinally before the Chrysler sale. These decisions established that there must be an appropriate business justification for the sale, as exemplified by a business emergency or a deteriorating business situation best handled by a sale; the sale cannot be a sub rosa plan of reorganization; and if the plan does determine critical § 1129 features, it can only do so if the court fashions a makeshift safeguard — a substitute that’s overall consistent with the mandates of § 1129.

#### A. Reconciling § 363 with § 1129

Prior to the modern Bankruptcy Code, asset sales were only allowed when the asset was perishing or wasting away. In *In re Lionel Corporation*, the Second Circuit freed Code sales from that restriction, but firmly stated when rejecting the proposed sale in the case that, although “the new Bankruptcy Code no longer requires such strict limitations on a bankruptcy judge’s authority to order disposition of the estate’s property..., it does not go so far as to eliminate all constraints on that judge’s discretion.”<sup>8</sup> The court established the modern test for a § 363 sale:

The rule we adopt requires that a judge determining a § 363(b) application expressly find from the evidence presented before him at the hearing a good business reason to grant such an application.<sup>9</sup>

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<sup>8</sup> *Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.2d 1063, 1069 (2d Cir. 1983).

<sup>9</sup> *Id.* at 1071.

Moreover, and more importantly for the Chrysler reorganization, the court in *Lionel* also stated that:

[I]t is easy to sympathize with the desire of a bankruptcy court to expedite bankruptcy reorganization proceedings for they are frequently protracted. "The need for expedition, however, is not a justification for abandoning proper standards." Protective Committee for Independent Stockholders of TMT Trailer Ferry, Inc. v. Anderson, 390 U.S. 414, 450, 20 L. Ed. 2d 1, 88 S. Ct. 1157 (1968).... In fashioning its findings, a bankruptcy judge must not blindly follow the hue and cry of the most vocal special interest groups; rather, he should consider all salient factors pertaining to the proceeding and, accordingly, act to further the diverse interests of the debtor, creditors and equity holders, alike.<sup>10</sup>

While the *Lionel* decision evinces a skepticism of the § 363 sale, over time, courts became more comfortable with § 363 sales, partly because they make so much business sense for a failing business, partly because the merger market deepened and thickened in the 1980s. Such sales have become much more frequent in chapter 11.<sup>11</sup>

By relaxing the standard for a § 363 sale, the courts introduced the risk that the § 363 sale process could be used to circumvent the carefully crafted protections of the chapter 11 process emanating from § 1129. The court addressed this issue in *In re Braniff Airways*:

The debtor and the Bankruptcy Court should not be able 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 the sale of assets.<sup>12</sup>

The *Braniff* court concluded that the proposed sale in that case — which would have distributed travel scrip (coupons), promissory notes, and a share of profits in differing amounts to different groups of creditors — was indeed a de facto plan of reorganization:

Were this transaction approved, and considering the properties proposed to be transferred, little would remain save fixed based equipment and little prospect or occasion for further reorganization. These considerations reinforce our view that this is in fact a reorganization.<sup>13</sup>

Courts continue to reaffirm and interpret the *Braniff* standard.

<sup>10</sup> *Id.*

<sup>11</sup> See Douglas G. Baird & Robert K. Rasmussen, *Chapter 11 at Twilight*, 56 STAN. L. REV. 673 (2003); Douglas G. Baird, *The New Face of Chapter 11*, 12 AM. BANKR. INST. J. REV. 69, 78 (2004) (stating that "sales are now part of the warp and woof of chapter 11 practice. Of the 10 largest chapter 11s of 2002, eight used the bankruptcy court as a way of selling their assets to the highest bidder, whether piecemeal or as a going concern."); Cf. Lynn M. LoPucki & Joseph W. Doherty, *Bankruptcy Fire Sales*, 106 MICH. L. REV. 1, 24-25 (2007) (criticizing sales).

<sup>12</sup> *Pension Benefit Guar. Corp. v. Braniff Airways, Inc. (In re Braniff Airways, Inc.)*, 700 F.2d 935, 940 (5th Cir. 1983).

<sup>13</sup> *Id.*

[T]he provisions of § 363 permitting a trustee to use, sell, or lease the assets do not allow a debtor to gut the bankruptcy estate before reorganization or to change the fundamental nature of the estate's assets in such a way that limits a future reorganization plan.<sup>14</sup>

In 2007, the Second Circuit said, in *In re Iridium Operating LLC*:

The trustee is prohibited from such use, sale or lease if it would amount to a sub rosa plan of reorganization. The reason sub rosa plans are prohibited is based on a fear that a debtor-in-possession will enter into transactions that will, in effect, "short circuit the requirements of [C]hapter 11 for confirmation of a reorganization plan."<sup>15</sup>

Although courts regularly indicate the impermissibility of sub rosa plans, they do not bar all plans that make § 1129 determinations in the § 363 sale. The sale may go through, but only if an appropriate, even if makeshift, protection is used to substitute for the foregone conditions to plan confirmation. As the court stated in *In re Continental Air Lines*:

[W]e hold that when an objector to a proposed transaction under § 363(b) claims that it is being denied certain protection because approval is sought pursuant to § 363(b) instead of as part of a reorganization plan, the objector must specify exactly what protection is being denied. If the court concludes that there has in actuality been such a denial, it may then consider fashioning appropriate protective measures modeled on those which would attend a reorganization plan.<sup>16</sup>

One commentator, summarizing the cases, stated:

The sound business purpose test requires a debtor to establish four elements: (1) a sound business purpose justifying the sale of assets outside the ordinary course of business, (2) accurate and reasonable notice provided to interested persons, (3) a fair and reasonable price obtained by the debtor, and (4) a good faith sale without offering lucrative deals to insiders.<sup>17</sup>

Keep in mind the cautionary indication about "lucrative deals to insiders," as the Chrysler sale could be interpreted as a lucrative deal to non-standard insiders, one that the judge would ordinarily want to examine carefully.

<sup>14</sup> *In re Babcock & Wilcox Co.*, 250 F.3d 953, 960 (5th Cir. 2001). See Craig A. Sloane, *The Sub Rosa Plan of Reorganization: Side-Stepping Creditor Protections in Chapter 11*, 16 BANKR. DEV. J. 37 (1999) (surveying cases as of 1999).

<sup>15</sup> *In re Iridium Operating LLC*, 478 F.3d 452, 466 (2d Cir. 2007) (quoting *In re Bramiff*, 700 F.2d at 940). Furthermore,

whether a particular settlement's distribution scheme complies with the Code's priority scheme must be the most important factor for the bankruptcy court to consider when determining whether a settlement is "fair and equitable" under Rule 9019. The court must be certain that parties to a settlement have not employed a settlement as a means to avoid the priority strictures of the Bankruptcy Code.

*Id.* at 464.

<sup>16</sup> *In re Continental Air Lines, Inc.*, 780 F.2d 1223, 1228 (5th Cir. 1986). *Cf. In re Crowthers McCall Pattern, Inc.*, 114 B.R. 877, 885 (Bankr. S.D.N.Y. 1990).

<sup>17</sup> Scott D. Cousins, *Chapter 11 Asset Sales*, 27 DEL. J. CORP. L. 835, 839-40 (2002). Multiple circuits explicitly require that these conditions be satisfied prior to a § 363 sale.

When a firm sells nearly all of its assets to a shell company that also assumes many but not all of its prior liabilities, we are not seeing a true sale solely to benefit creditors as a group. Instead, the sale is a de facto reorganization plan, which the courts had previously regularly rejected as requiring, at a minimum, a set of makeshift remedies in place of the § 1129 standards to confirmation.

### **B. Makeshift Remedies: Valuation**

The most straight-forward makeshift remedy would be for the bankruptcy court to hear valuation evidence, ascertain priorities, and determine whether the plan conformed to what would have been distributed had the plan gone through § 1129(b). Valuation though is not a favored process, partly because judicial valuation is itself often seen to be inaccurate and slow.<sup>18</sup>

### **C. Makeshift Remedies: Class Consent**

Section 1129(a)(8) allows plans to deviate from absolute priority, if the impaired class consents, by a vote of 2/3 in dollar amount and more than ½ in the number of claims. Few modern reorganizations reach a bargaining impasse — eventually the classes usually make a deal. The concept behind the consent procedure is that value may be uncertain and parties often compromise their claims to get a deal done so that the business can move on.

But that consent must be valid, as § 1126(e) states that “the court may designate any entity whose acceptance or rejection of such plan was not in good faith.”<sup>19</sup> That the lack of good faith exists if a claim holder is acting “in aid of an interest other than an interest as a creditor.”<sup>20</sup>

### **D. Makeshift Remedies: The Auction**

The main safeguard in most § 363 sales comes from the bidding rules that facilitate an auction, or some lesser market test of the sale. In 2006, the Southern District of New York posted general guidelines for bankruptcy sales.<sup>21</sup> These guidelines — which require that bidders be given access to relevant information, that the debtor demonstrate a sound business purpose, that the debtor market the property adequately and show that the price received will be “the highest or best under the

<sup>18</sup> See H.R. Rep. No. 595, 95th Cong., 1st Sess. 227 (1977); Report of the Commission on the Bankruptcy Laws of the United States, H. Doc. No. 137, Part I, 93d Cong., 1st Sess. 256 (1973).

<sup>19</sup> 11 U.S.C. § 1126(e) (2006).

<sup>20</sup> *In re Allegheny Int'l, Inc.*, 118 B.R. 282, 289 (Bankr. W.D. Pa. 1990) (quoting *In re P-R Holding Corp.*, 147 F.2d 895, 897 (2d Cir. 1945)). See also *In re Dune Deck Owners Corp.*, 175 B.R. 839, 845 (Bankr. S.D.N.Y. 1995).

<sup>21</sup> *In re Adoption of Guidelines for the Conduct of Asset Sales*, General Order M-331 (Bankr. S.D.N.Y. 2006), available at <http://www.nysb.uscourts.gov/orders/m331.pdf>.

circumstances,” and that the insider status of any buyer be disclosed — appear to be consistent with the practice in other courts as well.

Courts usually agree to the sale eventually, but often stretch its time frame, during which they remove problematic provisions from the debtor’s proposed bidding procedures and give the creditors committee an opportunity to investigate the lender’s lien and to object to any problems with the proposed sale. In the *Lifestream Technologies* bankruptcy, for instance, the parties requested that the § 363 sale be conducted shortly after the case was first filed. Judge Markell refused the request, which induced the parties to renegotiate the terms of the sale.<sup>22</sup> As the Supreme Court said in an analogous setting, in *North LaSalle*:

Under a plan granting an exclusive right, making no provision for competing bids or competing plans, any determination that the price was top dollar would necessarily be made by a judge in bankruptcy court, whereas the best way to determine value is exposure to a market.<sup>23</sup>

#### IV. THE CHRYSLER SALE

The Chrysler sale violated all these principles. The § 363 sale determined the core of the reorganization, but without adequately valuing the firm via § 1129(b), without adequately structuring a § 1129(a)(8) bargain, and without adequately market testing the sale itself. Although the bankruptcy court emphasized an emergency quality to the need to act quickly, stating that “if a sale has not closed by June 15<sup>th</sup>, Fiat could withdraw its commitment,”<sup>24</sup> there was no such immediate emergency. Chrysler’s business posture in early June gave the court weeks to sort out priorities, even if in a makeshift way.

That core terms to § 1129 were determined is not in doubt. The sale set the consideration for the secured creditors at \$2 billion. It set the retirees’ VEBA payment at \$4.6 billion.<sup>25</sup> The Chrysler sale was a sub rosa plan. The only question is whether the makeshift procedures the judge used were adequate substitutes for a real § 1129 confirmation. In most cases the answer is clearly no, because no substitute was attempted. For a few features, a partial substitute was employed — such as a market test — but the substitute was inadequate.

##### A. Valuation

Had the judge determined after a contested valuation hearing that the liquidation value of the Chrysler creditor claims, as well as their going concern value

<sup>22</sup> See, e.g., Debtor’s Supplemental Brief in Support of Motion for Order Pursuant to Section 363 of the Bankruptcy Code, *In re Lifestream Technologies, Inc.*, No. BK-S-06-13589 (Bankr. D. Nev. 2006) (noting that principal lender agreed to give 25% of any overbid to unsecured creditors and to extend the auction for four additional weeks).

<sup>23</sup> *Bank of Am. Nat’l Trust & Sav. Ass’n v. 203 N. LaSalle St. P’ship*, 526 U.S. 434, 457 (1999).

<sup>24</sup> *In re Chrysler LLC*, 405 B.R. 84, 96-97 (Bankr. S.D.N.Y. 2009).

<sup>25</sup> VEBA is the acronym for the trust that handles the retiree health benefits — the voluntary employees benefit association.

was \$2 billion (and had he done the same for the miscellaneous other creditors, such as the products liability claims), then a plausible makeshift alternative would have existed. The courts could have said that a cramdown under § 1129(a)(7) and § 1129(b) would have led to the secured creditors getting \$2 billion, so that the sale, although determining core terms under § 1129, was not defective.

Chrysler did present a valuation to the court, with the liquidation value centered on \$2 billion, although with a range that went substantially higher. (Chrysler's status was such that liquidation value and going concern value were, without the government's cash, likely to be approximately the same, Chrysler's going concern value came, in all likelihood, from the government's infusion of cash.) Shortly before the hearing on the proposed sale, Capstone, Chrysler's financial advisor, revised its valuation downward (to 0-\$1.2 billion), pointing to a decrease in Chrysler's cash, a general decrease in car sales, and the unprofitability of two of Chrysler's car lines as warranting the adjustment.<sup>26</sup> No other valuations, either by a party or someone outside the case, were considered.

The problem with the valuation as it occurred in the Chrysler proceeding is that the court did not give the objecting creditors time to present an alternative valuation from their experts. Such valuation contests are notoriously difficult, as each party tends to come to court with experts sporting a number remarkably supportive of the client's best interests. But that's the system we're saddled with, and judges have done the best they can under the circumstances. Here, though, the judge saw evidence from only one side's expert.

This aspect of the reorganization may, in retrospect, be the sale proponents' best case: they presented valuation evidence and the objecting creditors did not. The objecting creditors indicated that they lacked time to do so, but regardless, the litigation posture was that a single valuation was available to the judge and it stood un rebutted by better evidence.<sup>27</sup>

## B. Consent

The makeshift remedy for the Chrysler sale could analogize to § 1129(a)(8) consent, positing that parallel to that section, the Chrysler deal had the secured creditors consenting de facto to the sale. Hence, the makeshift procedural alternative was met.<sup>28</sup>

On the surface, there seemed to be an informal vote in favor, by 2/3 of the dollar amount of the class. While the larger creditor class initially objected strongly in negotiations with the U.S. Treasury, four major creditors — Citigroup, J.P. Morgan

<sup>26</sup> 405 B.R. at 97.

<sup>27</sup> The dissenting creditors did, however, contest the credibility of the valuation and the advisory opinion author's incentives. See Brief for Appellants Indiana State Police Pension Trust, et al., *In re Chrysler LLC*, No. 09-2311 (2d Cir. 2009), 2009 WL 1560029, at \*15-19.

<sup>28</sup> For a more elaborate proposal based on similar intuitions, see David A. Skeel, Jr., *The Nature and Effect of Corporate Voting in Chapter 11 Reorganization Cases*, 78 VA. L. REV. 461, 497-501 (1992) (vote by residual class of creditors on § 363 sales).

Chase, Goldman Sachs, and Morgan Stanley — holding 70% of the dollar amount of the claims eventually acceded to the \$2 billion number.<sup>29</sup>

The difficulty with crediting such a vote as informally satisfying § 1129(a)(8) is that these creditors were beholden to the U.S. Treasury, which was emerging as Chrysler's principal creditor, and the Federal Reserve, not just as their regulators, but as the banks' financial patrons via the TARP program. The four banks had recently received \$90 billion in investments from the Treasury.<sup>30</sup> Their vote was tainted, perhaps sufficiently under § 1126(e) to be bad faith votes.

There's another way to look at the big banks' votes. These banks were plausibly controlled by the United States Treasury at the time. Not only were they dependent on the Treasury for financing, but there was even serious talk that the major banks — including two or three of Chrysler's major creditors — would need to be nationalized. If the Treasury was a controlling person, then how would we look at the banks' consent? We'd then have to see Chrysler's major debtor-in-possession, bankruptcy lender as controlling the votes of Chrysler's major pre-bankruptcy creditors, on a plan it designed. The conflict would be too large to keep the various minority creditors in the same class as the four major banks.

The principal pre-bankruptcy bank lenders and the government, as DIP- and exit-finance-lender, were approximately the same entity, or at least tightly related. De facto, the same party controlled the purchase and the sale. As such, with the same player on both sides of the sale, the best result conceptually would be to view the DIP lender's vote as tainted under section § 1126 or to separately classify the DIP lender's pre-bankruptcy loans from the other, non-DIP lenders' loans. Thus conceptualized, the DIP lender could not carry along the minority loan syndicate's lenders in a vote.<sup>31</sup>

Best view: the class consent was inadequate to bind the dissenters under § 1129(a)(8).

### C. The Market Test

An alternative to a judicial valuation or a bargained-for result (achieved in the shadow of a potential valuation hearing) is a market test. If Chrysler were put up for sale in a suitable market and no one bid more than \$2 billion, then that plausibly was its value. Creditors would then have had their makeshift substitute and the § 363 sale would have been proper.

There was a market test, but it was a test that no one could believe adequately tested Chrysler's value, as what was put to market was the sub rosa plan itself. Chrysler and the government asked the court to only permit the firm to be marketed

<sup>29</sup> Neil King Jr. and Jeffrey McCracken, *USA Inc.: U.S. Forced Chrysler's Creditors To Blink*, WALL ST. J., May 11, 2009, at A1.

<sup>30</sup> *Id.*

<sup>31</sup> Business media hype about government pressure on the lenders to accede to the government's plan is beside the point. *E.g.* Michael J. de la Merced, *Creditors Opposing Chrysler's Overhaul Plan End Alliance*, N.Y. TIMES, May 9, 2009, at B2. While not admirable if the acts occurred (and there may have been some exaggeration), such pressure isn't needed to make the case that a conflicted vote — a vote by ostensibly separate entities comprising a majority of a creditor class, but effectively controlled by the DIP lender, which was proposing its own plan and seeking consent to that plan — was in play.

with multiple pre-bankruptcy claims on Chrysler, including the UAW retiree claims, in place. But that's exactly what was at stake: whether Chrysler's assets were more valuable without those claims. The bankruptcy court turned down the objecting creditors' request to market the assets alone.<sup>32</sup>

Here is perhaps the weakest link in the government's and Chrysler's case. They argued, and surely sincerely believed, that the firm was worth no more than \$2 billion. As such, they should not have stymied the Chrysler creditors from seeking to sell the assets for more than \$2 billion, as they — the government and Chrysler — believed that the creditors would fail.

The government and Chrysler argued that they had scoured the world for a bidder for Chrysler and had found only one, FIAT.<sup>33</sup> This was surely so, but they were marketing a variant of the plan actually used, one that didn't separate Chrysler's assets from its largest preexisting liabilities. As such, their efforts were efforts to market the plan they preferred, not the plan the Code requires to be tested.<sup>34</sup>

And in the bankruptcy itself, the Chrysler bidding procedures discouraged competing bids — and indeed, none were received. To be deemed "qualified," bids had to, among other things, conform substantially to the terms set out in the Treasury's proposed Purchase Agreement. Bidders were bound into the government's deal, which includes agreeing to take on UAW collective bargaining agreements. Bidders were not free to bid on Chrysler's assets alone. A nonconforming bid would only be considered if the debtor, after consulting with creditors, the U.S. Treasury and the UAW, accepted it as qualified. While one must assume that had a party, *sua sponte*, come into the court with a competing bid on differing terms, the court would not have ignored the bid, there was nothing in the court's approval of the bidding procedures to indicate that such an appearance with a bid and a check would have been welcomed. Even if an outsider valued the assets alone at more than \$2 billion, it had to know that neither the court nor the central parties were ready to allow those assets to be priced loose.

This is a serious defect in the bidding procedures. First, with the government having committed itself to rescuing Chrysler, bidders who contemplated buying pieces of Chrysler — the Jeep product line, for example, or piecemeal equipment — had to know that they were not dealing with a commercial bidder who realistically could be outbid. Since the Treasury wouldn't be outbid, why should a commercial bidder bother to study the company carefully enough to place a bid? Given this baseline, getting a valid bidding process for Chrysler was not going to be easy, but the court too readily accepted Chrysler's, the government's, and the UAW's preferences that there not be a

<sup>32</sup> Order ... Approving Bidding Procedures for the Sale of Substantially All of the Debtor's Assets ... , *In re Chrysler LLC*, 405 B.R. 84 (Bankr. S.D.N.Y. 2009) (No. 09-50002), 2009 WL 1360869, at \*18.

<sup>33</sup> Motion of Debtors and Debtors in Possession...for an Order Approving Bidding Procedures ... [and] Authorizing the Sale ... , *In re Chrysler LLC*, 405 B.R. 84 (Bankr. S.D.N.Y. 2009) (No. 09-50002), 2009 WL 1227661, ¶ 46.

<sup>34</sup> Bidding procedures "must not chill the receipt of higher and better offers..." General Order M-331 of the United States Bankruptcy Court, Southern District of New York, *supra* note 21, at 3. "Structured bid procedures should provide a vehicle to enhance the bid process and should not be a mechanism to chill prospective bidders' interests." *In re President Casinos*, 314 B.R. 784, 786 (Bankr. E.D. Mo. 2004). More generally, as the Supreme Court has said, "the best way to determine value is exposure to a market." *Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 N. LaSalle St. P' ship*, 526 U.S. 434, 457 (1999). That implies a real exposure, not one designed to chill market reaction.



serious bidding process at all. With the Treasury and the UAW as parties who would evaluate the bids, the court signaled that there would not be a substantial, serious bidding process, thereby chilling outside interest, after the court approved the bidding procedures and, presumably, when Chrysler shopped the company in the months before it entered chapter 11. Conditioning that outside bids be acceptable to the Treasury and the UAW does seem peculiar, or at least nonstandard.

This auction defect extended back to the pre-bankruptcy marketing: Since bidders knew that the government had a structure in mind — keeping Chrysler's operations and employment as intact as possible — bids for the assets alone would not have been forthcoming. The problem has its analogue in more usual bidding informational problems: if insiders have better information, outsiders have reason to fear that if they value the firm more highly than insiders, they'll over-pay. So they don't investigate and bid in the first place. Here the insiders have not just better information but policy goals that made a wide range of Chrysler's potential sales configurations unacceptable to those that the court seemed to allow to control the firm's disposition.

Moreover, with the court accepting the proponents' request that Chrysler be sold quickly, outside bidders were given a little more than a week to place bids, which did not make for easy due diligence or financing. Bidders were required to put down a cash deposit of 10% of the purchase price proposed. Chrysler reserved "the right, after consultation with the Creditors' Committee, the U.S. Treasury and the UAW, to reject any bid if such bid" was "on terms that are materially more burdensome or conditional than the terms of the Purchase Agreement."<sup>35</sup> The reality was that the deal as proposed was going forward, so if there were a potential bidder who thought Chrysler's assets, Jeep line, and some other pieces was worth more than \$2 billion, it had to know that its bid, if it bothered to make one, would likely be rejected.

A good market test could validate the § 363 sale process, but there was no valid market test in the Chrysler reorganization. True, a market test is not a cure-all. It will never perfectly assure that a company receives top value for its assets and there are inherent defects in any auction. But the bidding structure in Chrysler was far removed from a genuine market test that could validate the actual § 363 sale that occurred.

#### **D. The Emergency — How Immediate?**

*Lionel* requires that sales be made only if there is a valid business purpose. The posture of the Chrysler case seemed to rely on the business emergency — Chrysler would, it was said, be forced to liquidate shortly after June 15, if the sale to FIAT did not close by then. Indeed, the proponents at some points seemed to rest solely on the emergency standard, as sufficient in itself and to justify cutting § 1129

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<sup>35</sup> Order Approving Bidding Procedures, *supra* note 32, at \*20.

corners and doing so quickly.<sup>36</sup> This is an aggressive view, one that courts had not previously promulgated.<sup>37</sup>

Much was made early in June that FIAT had agreed to purchase Chrysler's core on June 15. This was portrayed as providing both the business justification for the sale — a buyer who might turn the company around — and the pressing need to approve that sale immediately, because any stay to the proceedings that went past June 15 jeopardized the sale.

But the emergency status was greatly exaggerated in the process, with the threat that Chrysler would promptly liquidate if the FIAT deal did not go forward on June 15<sup>th</sup> quite implausible. To understand why the liquidation threat — which seemed to move the courts both in approving the sale and in not staying its closing for a closer look — we need to follow the money in the Chrysler deal.

While a deadline from a typical purchaser who is providing, say, \$2 billion in fresh money is something for the bankruptcy courts to take very seriously, Chrysler was *not* in that situation. FIAT was *not* that kind of cash purchaser. The cash came from the United States Treasury, none came from FIAT. The real player who could pull the plug was the Treasury, not FIAT. And the Treasury was not about to walk away. While the judge stated a fear that the Treasury would walk, one wonders how credible this fear was, when the Treasury was a major architect of the plan and was simultaneously actively preparing an analogous reorganization of General Motors.<sup>38</sup>

Without FIAT, Chrysler and the Treasury could have followed the GM path to reorganization, without a figurehead outsider as a purchaser that provides no cash. And, in any case, FIAT's chief executive admitted, perhaps in an unguarded moment, that FIAT would never walk away from the deal.<sup>39</sup> And why would it? It was not asked to pay anything. The party that could have sunk the deal by walking away was the US Treasury, not FIAT.

If Chrysler's operations were like the melting ice cube metaphor that's been used in this setting<sup>40</sup> — about to collapse and only the sale could allow any value to be obtained — then a court would have to balance out competing considerations. But the emergency fact cited — that a bidder was potentially about to disappear — was not as important as is typical, because the disappearing bidder was not the true party providing the cash. Chrysler did not have all the time in the world, but there was sufficient time — weeks, maybe a month — for the courts to fashion the makeshift checks that prior case law demanded, to confirm that the plan complied with § 1129 and, if it did not, to reshape the plan.

<sup>36</sup> Brief for Debtors-Appellees Chrysler LLC, et al., *In re Chrysler LLC*, No. 09-2311 (2d Cir. 2009), 2009 WL 1560030, at \*22-24.

<sup>37</sup> Also, in the appeal, dissenters asked for a continuing stay, which was decided on a balance of harms test, with the business emergency offered to support an immediate sale without a continuing stay.

<sup>38</sup> The Treasury itself, and not FIAT, created the June 15 deadline in its DIP financing. If it wanted to extend a few weeks, while the plan was adequately vetted under § 1129 for compliance, it could have. FIAT would, the indicators strongly suggest, have waited.

<sup>39</sup> Serena Saitto, *Fiat Will 'Never' Walk Away From Chrysler, CEO Says*, BLOOMBERG, June 8, 2009, [http://www.bloomber.com/apps/news?pid=20601087&sid=s5\\_6JivCqJImA](http://www.bloomber.com/apps/news?pid=20601087&sid=s5_6JivCqJImA).

<sup>40</sup> *E.g.*, *In re Summit Global Logistics, Inc.*, 2008 Bankr. LEXIS 896 at \*31 (Bankr. D.N.J. Mar. 26, 2008).

Moreover, the emergencies in the past have been judicially cited to support that there be a sale instead of a full-scale § 1129 reorganization, not to support the idea that no protections, makeshift or substantial, are needed. If the Second Circuit accepts the implications of this argument, it should understand that it's breaking new — and dangerous — ground.

\* \* \*

For the Chrysler sale to comport with prior case law, it could not have been a *sub rosa* plan of reorganization. Terms that ordinarily are resolved under § 1129 could not have been resolved in the § 363 sale, unless the process provided satisfactory, even if makeshift, substitutes.

But, with one possible exception, this was not done. The market test was one that could not have elicited suitable bids, because it was set to replicate the deal then at hand, the one already engineered by the insiders, when the very question was whether creditors could have obtained more money via a different deal. Some core problems could have been seen as substantially remedied by the consent of the large creditor class. But the consenting majority was largely dependent on the U.S. Treasury's good graces at the time, to the point that they — the Treasury and the consenting banks — could have been seen as nearly alter egos. This leaves only the valuation, which is the least favored of the makeshift remedies, and in this case consisted only of Chrysler's own valuation. But it's the best justification, even if it's a weak one, for the sale.

#### **V. STRUCTURAL INCONSISTENCIES IN THE CHRYSLER SALE**

Chrysler's and the government's valuation arguments set up some potential inconsistencies, which need highlighting. First, the implicit preexisting value of Chrysler and the government's cash infusion seem disproportionate. Chrysler was contributing \$2 billion in value to the new firm, while the government was investing upwards of \$15 billion. These numbers suggest more than a simple rescue.

Second, although the favored treatment of the employee retirement claims seems, on its surface, to come from the government subsidizing the firm — justifying any priority deviation if it's the government that's paying for it — the actual structure is more complex.

Since the government's claims come first in the New Chrysler's capital structure, before the retirees' claims, then either the government sees going concern value in the structure beyond their own contribution, or the government is really making an equity investment, in that it plans to forgive its loans eventually, to the benefit of the employees.

But if a future reorganization is needed so that Chrysler can restructure the new and the carried-over debts, then the sale wouldn't comply with § 1129(a)(11), which requires that the judge find the plan not likely to be followed by a future reorganization of the debtor. To be sure, this section is not core to the § 1129 plan confirmation standards and it's not regularly used to strike down plans. And one could formalistically state that Old Chrysler will not need further reorganization other than as contemplated in the plan and only Old Chrysler counts under the plan, even if the New

Chrysler is a strong candidate for future reorganization. Properly seen, though, it's all one plan of reorganization, with the major part of that de facto reorganization facing the contradiction we've just noted. This analysis emphasizes a point made by critics of the Chrysler sale: it's not a sufficient business restructuring, in that it's unlikely to alleviate the business problems Chrysler faces. It kicks the can down the road.

The not-likely-to-be-followed-by-further-reorganization standard in § 1129(a)(11) asks the judge to confirm that the reorganization plan is likely to handle the bankrupt's operating and financial problems. The Code is looking via (a)(11) to avoid reorganization recidivism, seeking to resolve a firm's financial troubles as best it can in one proceeding. The only way to interpret the actual deal structure, however, is that either (a) there was value in Chrysler sufficient to pay tens of billions of dollars of unsecured claims (since the government's loans were superior in right payment and could not be providing much value to those claims) or (b) the inside players expected a future reorganization of New Chrysler that will either wipe out those claims or have the government forgive its claims on the reorganized entity. If the former, priorities were violated. If the latter (which seems plausible), § 1129(a)(11) was violated.

We point this out not because it seems highly likely that such going concern value existed independently of the government's \$15 billion rescue, but to demonstrate that the process didn't uncover logical difficulties with the plan, much less actual valuation difficulties.

Section 506(a)(1) of the Bankruptcy Code states that a claim "secured by a lien on property in which the estate has an interest ... is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property.... Such value shall be determined *in light of the purpose of the valuation and of the proposed disposition or use of such property...*"<sup>41</sup> In *Assocs. Commercial Corp. v. Rash*, the Supreme Court ruled that:

That actual use, rather than a foreclosure sale that will not take place, is the proper guide under a prescription hinged to the property's "disposition or use."<sup>42</sup>

If the assets are used in a going concern, the value of collateral is, under *Rash*, its contribution to the going concern, — typically the cost of replacing those assets — even if its shut-down, liquidation value would be less. To be sure, from the perspective of Old Chrysler, the assets were ostensibly being sold. But the security interest covered substantially all of Chrysler's assets, and those assets were being sold as a going concern that largely replicated Old Chrysler's core business.

Indeed, in the Chrysler reorganization, the expedited sale was justified by the debtors in part on the need to preserve a going concern value that would be lost if the sale were delayed. The debtors stated that:

Chrysler continues to hold value as a going concern. The Debtors' core group of operating assets function as an integrated business engaged in designing, assembling and selling automobiles. Those assets include a

<sup>41</sup> 11 U.S.C. § 506(a)(1) (emphasis supplied).

<sup>42</sup> *Assocs. Commer. Corp. v. Rash*, 520 U.S. 953, 963 (1997). *Rash* was a chapter 13 case and the contested concept was whether replacement value or liquidation value was to be used to value the collateral. But because *Rash* interpreted § 506, which applies to chapter 11 as well as to chapter 13. It's apt.

skilled and well-trained workforce, a national system of independent dealers, and an integrated network of suppliers that provide the thousands of components used to build automobiles. Moreover, Chrysler has a number of high-performing brands and models — including its Jeep and Dodge Truck nameplates and certain minivan lines — that have enjoyed strong sales and provided solid returns to the Company for many years.<sup>43</sup>

*Rash* implies that this going-concern value, if it truly existed, belonged to Chrysler's secured creditors, not, absent some exception, to its trade creditors or retirees. Under the plan, New Chrysler will satisfy the claims owed to its VEBA with a note in the amount of \$4.6 billion and a 55% equity interest in New Chrysler. The government is financing New Chrysler's operations with \$6 billion in senior secured financing. Any returns on the \$4.6 billion note and equity owned by VEBA would ordinarily come from earnings beyond those necessary to pay back the government's loan. This structure, if it's viable, would indicate that Chrysler has a going concern value above the \$2 billion benchmark for the secured.

A cluster of priority valuation ambiguities would have needed to have been resolved, several of which would not favor the lenders: For example, the preexisting trade creditors may have been ripe for a critical-vendor priority. And payments on the ongoing retirement obligations are entitled to an administrative priority under § 1114; Chrysler's secured creditors would not, under *Timbers*, be entitled to the time value of delay in realizing on their security, if there were a multi-year chapter 11 proceeding.<sup>44</sup>

Yet, while much of the public discussion focused on the financial creditors as priority creditors, a more basic rule may be in play and it would have further favored the financial lenders. Chrysler's lenders were entitled to pro rata treatment with unsecured creditors on the unsecured portion of their claim (the "deficiency" that the security did not cover). With the lenders receiving 29 cents on the dollar, while others were promised more, this rule, the prohibition against "unfair discrimination" in § 1129(b), was on the surface not complied with. And, on the lenders' side, although the § 1114 adjustments are relevant, they seem unlikely to account for the full difference in treatment under the plan.<sup>45</sup> Some larger justification would be needed, perhaps by analogy to a critical vendor payment to Chrysler's labor force.

Moreover, again disfavoring the lenders, Chrysler may not have been an effective organization without the UAW's agreement; when one understands the realpolitik that the government would not provide cash without the UAW being roughly satisfied and that a plan that didn't preserve many jobs would not be acceptable to the UAW, then the real range of plans that were viable had limits. Even a purely financial bidder without the government's policy motivations may have decided to keep similar UAW terms for current employees, as it would need a trained labor force and none other was available. But without a viable auction having been

<sup>43</sup> Memorandum of Law in Support of Motion of Debtors and Debtors in Possession ... for an Order Approving Bidding Procedures ... [and] Authorizing the Sale ..., *In re Chrysler LLC*, 405 B.R. 84 (Bankr. S.D.N.Y. 2009) (No. 09-50002), 2009 WL 1227662, at \*19.

<sup>44</sup> *United Savings Ass'n v. Timbers of Inwood Forest*, 484 U.S. 365 (1988).

<sup>45</sup> The § 1114 bonus to the retirees' claims, if doctrinally in play, would only cover the period of the reorganization itself, which is typically a two-year affair. And Chrysler's desperate shape could have led the bankruptcy court to reduce the § 1114 payment obligation. 11 U.S.C. § 1114(h).

attempted, we don't know whether that's likely and, hence, can't be sure whether value came from the lenders instead of just from the government.

Whether all of these ambiguities would have been resolved against Chrysler's lenders if they were fully played out is hard to say. But it is easy to say that the sale determined the result, demonstrating it was indeed a sub rosa reorganization plan, without makeshift remedies for the problems raised.<sup>46</sup>

## VI. COULD THE TREASURY HAVE ACTED ANY DIFFERENTLY?

Could the United States, once it decided to rescue Chrysler for policy reasons, have structured the deal any differently? Was national policy just on a collision course with proper bankruptcy practice? In the prior section, we analyzed how the policy objectives could have been implemented with a better bankruptcy process. Here, we indicate that there were alternatives available.

One alternative is that the government could have picked up old Chrysler's VEBA obligations directly, as it did with Chrysler's ongoing warranty obligations. This would have been a different deal, because the government is a more creditworthy debtor than the reorganized Chrysler. But making the UAW somewhat dependent on the equity value and debt repayment capacity of the new Chrysler does better align its

<sup>46</sup> We relegate to a footnote a weak justification for the sale. The weak justification is that the assets were sold cleanly to the New Chrysler, without the Old Chrysler's debts, but then the New Chrysler, sua sponte, picked up obligations to some, but not all, of Old Chrysler's creditors. This idea represents the kind of formalistic thinking that courts usually — and the Second Circuit should surely — reject.

The bankruptcy judge claimed that “the UAW, VEBA, and the Treasury are not receiving distributions on account of their prepetition claims. Rather, consideration to these entities is being provided under separately-negotiated agreements with New Chrysler.” 405 B.R. at 99. But given that the VEBA provides for legacy obligations, it's hard to think that this view is correct: the VEBA plan excludes active employees — who provide new value to Chrysler — but covers Chrysler's retirees, who are not providing current value to Chrysler. Indeed, the Old Chrysler *required* that New Chrysler pick up a wide range of obligations to trade creditors. This is hardly an indicator of an arms-length sale, with the purchaser then deciding which players' interests it needed to assuage to best move forward. See Master Transaction Agreement among FIAT S.p.A., New Carco Acquisition LLC, Chrysler LLC and the other Sellers identified herein, April 30, 2009, ¶2.08. Why did the legacy players need to require this, if it were in New Chrysler's interest, expressed sua sponte? Similarly, the Old Chrysler Official Creditors Committee *approved* the sale of the assets to New Chrysler, despite that the creditors they represented would not receive *any* compensation from the Old Chrysler. They knew what was coming to them from the New Chrysler; it wasn't separately negotiated. This was all one deal — a plan of reorganization — not an arms-length sale.

Had the bankruptcy judge given himself more time for the decision, the overly formalistic passage at the beginning of the prior paragraph (in which he says that the Old Chrysler creditors were “not receiving distributions on account of their prepetition claims”) is unlikely to have found its way into the opinion intact. More generally, it's a bedrock principle that courts will not countenance a series of steps that in isolation are defensible, but when done together change the fundamental character of the transaction.

*Gleneagles* illustrates. There, a cleverly-designed leveraged buyout left the target insolvent. No single step in the transaction violated fraudulent conveyance law. But the Third Circuit compared the final to the initial structure, added that all active parties knew where the deal was going, and held the transfer to be a fraudulent conveyance. *United States v. Tabor Court Realty Corp.*, 803 F.2d 1288 (3d Cir. 1986). The Chrysler bankruptcy is similar: the final structure has most pre-bankruptcy assets and creditors in place in the New Chrysler. While some steps could have stood on their own, alone, had there been no more, the totality is that Old Chrysler was reorganized in chapter 11 via a pseudo sale to a new company controlled by those who had control of Old Chrysler. It was a de facto reorganization, not an arms-length sale.

incentives with those of the company, and Chrysler's operations may very well be worth more because the deal cleverly mixes the UAW's post-sale motivations.

A second alternative is that the government could have offered its subsidy not to Chrysler directly but to qualified bidders, in a way that's analogous to the plans discussed to encourage bidding from banks' toxic assets. If done well, that could have elicited a range of bids and terms, yielding a true market test.

Moreover, there is an irony to the business-political setting. Chrysler's major secured lenders, which were asked to accept the \$2 billion for \$6.9 billion deal, were recipients of government rescue money via other channels. One wonders why the Treasury decided to be tough on them in this dimension, while propping up the same players elsewhere.<sup>47</sup>

## VII. CHRYSLER AS CHAPTER 11 TEMPLATE?

If Chrysler turns out to be a one-off reorganization that was not Code-compliant, the damage to bankruptcy practice will be minimal. A hurricane comes, destroys infrastructure, and then we rebuild.

### A. Replication without the Government

But the deal structure used does not need the government's involvement or a national industry in economic crisis. The bankruptcy techniques and doctrines used are readily replicable in ordinary bankruptcies. The deal shows fissures and weaknesses in chapter 11's structure. And the case is already being cited as a precedent.

First off, a § 363 sale does not require § 1129(a)(8) consent.<sup>48</sup> So even the tainted consent of the large creditors isn't needed to make § 363 work. In general, the question is whether the courts will insist on strong makeshift alternatives when a § 363 sale determines core elements of § 1129, or whether it will accept empty ones. The Chrysler makeshift substitutes were weak. Hence, a coalition of creditors, managers, and (maybe) shareholders could present a § 363 "plan" to the court for approval, and the plan could squeeze out any creditor class. We are, for now, going to see a bankruptcy process that's more fully in the individual judge's discretion, but, with prior case law not followed, and § 1129 jettisoned, no standard is in place to guide the judge.

In the pending Delphi bankruptcy, the judge insisted on a real market test. Rejecting arguments by General Motors and the government that Platinum Equity,

<sup>47</sup> Two possibilities: Popular opinion had just seen the Treasury as rescuing wrongdoing financiers as much as it was rescuing a weakened financial system in the TARP bank bailouts. The AIG bonus imbroglio did not assuage public opinion. Hence, the government could have wanted to be seen as tough on financiers and accommodating for blue collar workers. Chrysler gave it the opportunity to do both.

The second possibility is that the Treasury auto players were strong dealmakers previously. They continued to make the strongest deal possible for their client.

<sup>48</sup> Technically, secured creditors' liens on the assets need to be released, and consent is one basis for release, so some § 363 sales do require consent. Without security, though, even that consent is not in play.

their preferred buyer, was the only acceptable purchaser for Delphi's assets, Judge Drain said "I don't know what makes Platinum acceptable to GM and why Platinum is unique. Unless I hear more, there's something going on here that doesn't to me make sense."<sup>49</sup> "What's so special about Platinum?" he asked. "They're just guys in suits. Why can't the other guys in suits just pay more?"<sup>50</sup>

In the pending bankruptcy of the Phoenix Coyotes NHL team, the debtor argued that Chrysler set the precedent for the court to approve a rapid timeline because the team was losing money while only one firm offer had been made for the team. The judge dismissed this argument, rejecting the breakneck pace because "the court does not think there is sufficient time (14 days) for all of these issues to be fairly presented to the court given that deadline."<sup>51</sup>

We can also speculate about the announced structure for the General Motors bankruptcy. The government has used the same template for the proposed § 363 sale in GM as it did in Chrysler, and the sale raises some of the same concerns. As in Chrysler, the buyer is not a true third party, the ostensible urgency of the sale is debatable, and the § 363 bidding procedures require that would-be bidders agree to the retiree settlement negotiated by the government and GM. But GM's secured creditors, unlike their counterparts in Chrysler, are expected to be paid in full. The GM sale is in this dimension thus easier to reconcile with ordinary priority rules than Chrysler, although issues may emerge among its unsecured creditors. True, GM is a stronger company than Chrysler and, hence, might have more value to distribute. But it's plausible that the Treasury adjusted to the pushback from capital markets and the media criticism that accompanied the Chrysler deal.

## B. Recommendations

It's too late to get the right decisional structure for the Chrysler reorganization. But courts can at least confine the problems.

The Second Circuit has yet to write its opinion rejecting the appeal. We can hope that it will express a view that it's greatly troubled by the bankruptcy process, by the lack of a real auction, and by the determination of too many core § 1129 terms in a § 363 sale. It can, we hope, latch onto the least objectionable features of the Chrysler reorganization for validation, such as the plausible, un rebutted initial liquidation value study, which centered the range of liquidation values at \$2 billion, the amount allocated for the secured creditors. Or the court could focus on the apparent consent, indicating that if the class had appealed as a group to the Second Circuit, the result might well have differed.

Similarly, it could reject the auction procedures used, but note that there was no evidence of interest, suggesting that even improved auction procedures might not have elicited a better bid. It could also indicate that were it not for the government's

<sup>49</sup> *DIPing into Delphi*, WALL ST. J., June 16, 2009, at A14.

<sup>50</sup> Peter Lattman, *Judge Orders Auction in a Rebuke to Delphi Plan*, WALL ST. J., June 11, 2009, at B1.

<sup>51</sup> *In re Dewey Ranch Hockey, LLC*, 2009 WL 1702767, at \*10 (Bankr. D. Ariz. June 15, 2009).



presence as quite possibly lending on noncommercial terms, the sale would have to be rejected as not being Code-compliant.

In addition, the type of plan can be rejected in dictum in the future in other circuits. Legislation could also correct, but an appropriate judicial interpretation of § 363 would be quicker. Appellate criticism of the inappropriateness of a bankruptcy opinion approving the reorganization in chapter 11 of a major American business without once citing § 1129 is in order.<sup>52</sup>

### VIII. THE BIG PICTURE

While we are interested in proper bankruptcy practice for its own sake and for fidelity with the Code, we obviously have other motivations for writing this article. The opacity of the Chrysler deal gave credit markets a scare, with major investors fearing that priorities were being violated. If that sense were widespread, creditors would adjust interest rates for companies seen to be at risk of priority wars, or decide not to invest in some marginal companies. That would be unfortunate for the economy.

It's important for courts to reject the Chrysler structure, so that we can be better assured that credit markets will continue to function properly for weak firms. If courts do indeed readjust away from the Chrysler scenario, in time creditors will forget the Chrysler structure, or remember it as a one-off anomaly.

The Chrysler deal was structured as a pseudo sale, mostly to insiders (in the Chrysler case to the UAW and the government), in a way eerily resembling the ugliest equity receiverships at the end of the 19<sup>th</sup> century. The receivership process was a creature of necessity, and it facilitated reorganization of the nation's railroads and other large corporations at a time when the nation lacked a statutory framework to do so.<sup>53</sup> But the early procedure created opportunities for abuse. In the receiverships of the late 19<sup>th</sup> and early 20<sup>th</sup> century, insiders would set up a dummy corporation to buy the failed company's assets.<sup>54</sup> Some old creditors — the insiders — would come over to the new entity. Other, outsider creditors, would be left behind, to claim against something less valuable, often an empty shell. Often these were the company's trade creditors. *Boyd* is the famous case. Its deal structure resembled Chrysler's — in that insiders moved over to the new company in a pseudo-sale, to the detriment of outsiders — although the insider types (the UAW and the government today, some well-positioned bond creditors and shareholders in *Boyd*) differed.

The judicial result in *Boyd*, however, differed sharply from that in *Chrysler*. Rather than denying certiorari, the Supreme Court in *Boyd* rebuked the lower courts, instructing them to determine whether priorities were followed before allowing such a

<sup>52</sup> The bankruptcy court was not averse to otherwise citing the Code in an opinion that was long enough. While it did not cite § 1129, it cited § 363 three dozen times.

<sup>53</sup> See DAVID A. SKEEL, JR., *DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA 48-70* (2001) (chronicling the emergence of equity receiverships in the late 19<sup>th</sup> century)

<sup>54</sup> The receiverships were structured as pseudo-"sales" of the company to a portion of its existing creditors and shareholders. The process was devised from ordinary foreclosure sales, with the parties pretending to conduct a foreclosure sale, but in reality effecting a restructuring by selling the assets to a group of the preexisting investors.

sale to go forward that de facto determined the priorities and compensation of lenders.<sup>55</sup>

After the *Boyd* decision, insiders could no longer simply ignore disfavored creditors. But critics continued to worry about the dominant role of insiders — principally Wall Street banks, favored bondholders, and their law firms.<sup>56</sup> In the 1930s, William Douglas oversaw a massive Securities and Exchange Commission study that documented abuses in many large cases.<sup>57</sup> The study led to major reforms that replaced the old receivership practice with judicially overseen reorganization as part of the Chandler Act of 1938.<sup>58</sup> Both before and after the Chandler Act, the Supreme Court insisted that creditors' priorities be respected, most prominently in a 1939 decision that struck down a proposed reorganization that would have given insiders stock in the new company.<sup>59</sup> The reforms of the 1930s and the Supreme Court decisions of the early 20<sup>th</sup> century eliminated the artificial sales of the past, sales that risked warping priority, and assured that creditors' priorities would be respected.

It is ironic that the Supreme Court invested considerable energy in the late 19<sup>th</sup> century and early 20<sup>th</sup> century, and the Congress did as well with the Chandler Act, to make sure the priorities were adhered to in a way that the Chrysler reorganization did not require.

One feature of *Chrysler* that differed from *Boyd* may portend future problems. Major creditors in Chrysler were not pure financiers, but were deeply involved in the automaker's production. The company had major trade creditors and the UAW and its retirees were also major creditors. Only the secured creditors were plain vanilla financiers, uninvolved in producing Chrysler's cars (and even they, in principle, brought the factories and equipment to the negotiating table). Chapter 11 is well-suited to reorganizing a firm's financial side, with the court and the parties sorting out priorities and then bargaining to a settlement. Neither the traditional bargaining process nor the § 363 sales process seem well-suited to resolve claims when the major creditors are also major parts of the firm's production chain.

## CONCLUSION

Chrysler entered and exited bankruptcy in 42 days, making it one of the fastest major industrial bankruptcies in memory. It entered as a company widely thought to be ripe for liquidation if left on its own, obtained massive funding from the United States Treasury, which funded the payment of several billion dollars to pre-bankruptcy creditors, brought in FIAT to manage the post-bankruptcy operation, and exited

<sup>55</sup> *Northern P. R. Co. v. Boyd*, 228 U.S. 482 (1913).

<sup>56</sup> See, e.g., Jerome N. Frank, *Some Realistic Reflections on Some Aspects of Corporate Reorganization*, 19 VA. L. REV. 541 (1933), (calling the equity receivership sale "a mockery and a sham") "A sale at which there can be only one bidder," Frank complained, "is a sale in name only." *Id.* at 555. See also WILLIAM O. DOUGLAS, *DEMOCRACY AND FINANCE* (1935).

<sup>57</sup> SECURITIES AND EXCH. COMM'N, REPORT ON THE STUDY AND INVESTIGATION OF THE WORK, ACTIVITIES, PERSONNEL AND FUNCTIONS OF PROTECTIVE AND REORGANIZATION COMMITTEES (1936-1940).

<sup>58</sup> See, e.g., SKEEL, *supra* note 53, at 109-23.

<sup>59</sup> *Case v. Los Angeles Lumber Products*, 308 U.S. 106 (1939).

through a pseudo sale of the main assets to a new government-funded entity. The unevenness of the compensation to prior creditors raised considerable concerns in capital markets.

Appellate courts had previously developed a strong set of standards for a § 363 sale: The sale must have a valid business justification, the sale cannot be a sub rosa plan of reorganization, and if the sale infringes on the protections afforded creditors under Chapter 11, the court can only approve it after fashioning appropriate protective measures.

The Chrysler reorganization failed to comply with these requirements. Although Chrysler needed to be repositioned, and needed to be repositioned quickly, it had a few weeks, maybe a month, to get the process done right in a way that would neither frighten credit markets nor violate priorities. Chrysler's facilities were already shut down and not scheduled to reopen immediately. The nominal buyer was providing no cash. The party with the money was the U.S. Treasury, and it wasn't walking away.

The plan surely was a sub rosa plan, in that it allocated billions of dollars — the core determination under § 1129 — without the checks that a plan of reorganization requires.

Even the informal, makeshift checks that courts had previously required when there were strong § 1129 implications were in *Chrysler* weak or nonexistent. The bankruptcy court did not even see fit to mention § 1129 in its opinion. There was de facto consent, but the consent came from parties controlled by the player controlling the reorganization — the United States Treasury. There was a pseudo-market test, not a real market test, because the plan marketed only marketed the reorganization plan itself, when the issue at stake was whether the assets alone had a higher value.

The Chrysler bankruptcy failed to comply with good bankruptcy practice, reviving practices that were soundly rejected nearly a century ago. Going forward, bankruptcy practice would be improved by a sharp appellate rejection of the Chrysler bankruptcy's structure.

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Mr. COHEN. Our fourth witness is Jeremy Warriner. Mr. Warriner has brought a claim against Chrysler regarding an accident he was involved in driving a Jeep Wrangler that he owned. As a result of injuries suffered during the accident, Mr. Warriner spent over a year in and out of hospitals and has had 38 surgeries since the accident. His medical bills are over \$1 million. His case against Chrysler was scheduled for mediation on May 5, but it was canceled due to Chrysler filing for bankruptcy on April 30.

Mr. Warriner, we ask you to begin your testimony. We appreciate your coming here.

**TESTIMONY OF JEREMY WARRINER, INDIANAPOLIS, IN**

Mr. WARRINER. Thank you. Thank you, Mr. Chairman and Members of the Committee, for giving me the opportunity to speak today.

As you listen to my testimony, I ask that you think about your friends, your family, your loved ones, your constituents, and yourselves. Please understand that the safety risks created by the auto industry bankruptcies have the potential to affect all of us.

In October of 2005 I was in a car accident. The damage left me trapped, pinned between the dash and the seat, and suspended in my 2005 Jeep Wrangler Unlimited which had rolled onto its passenger side. I had several severe injuries, all of which would have healed. Then, a fire ignited in the engine compartment that burned through the firewall into the passenger compartment.

Somehow I was rescued. But when you look at the wreckage, which is pictured in my written statement, the fact that I am here alive to speak to you today is unbelievable.

Five and a half weeks later, I awoke from a medically induced coma to learn that my legs had been amputated from above each knee. My lower legs had sustained fourth-degree burns. The burns had caused my body to become deathly ill from infection. My kidneys failed, my lungs failed, and the only chance that the doctors had to save my life was to amputate both of my legs. My parents had to make that decision without being able to speak with me, without knowing what my wishes were.

Expert engineers determined that a plastic reservoir that held my Jeep's brake fluid shattered during the accident and caused the fire. The reservoir was not protected from impact, and Chrysler had used a safer metal reservoir in prior Jeep Wrangler models. I believe that this was a defective design.

In July of 2006 I filed a lawsuit against Chrysler. In November of 2008 Chrysler delayed the court-ordered mediation, based on its financial instability, until May 5th. And then they declared bankruptcy on April 30th.

Through the bankruptcy process, Chrysler was relieved of responsibility for approximately 300 pending claims, including my own, and any future claims resulting from vehicle defects in any of the approximately 10 million pre-bankruptcy vehicles on the road today.

GM was relieved of responsibility for approximately 1,000 pending claims, as well as any injuries or deaths caused by GM vehicles before or during the bankruptcy process that have not been filed yet.

Each of the approximately 1,300 pending claims against these auto manufacturers represent potential defects that could lead to immediate safety recalls. If these cases are not heard in court, these defects will not get tracked by the National Highway Traffic Safety Administration, Chrysler and GM will not admit these defects exist, recalls will not be issued, and more injuries and deaths will occur. Ignoring the pending claims and the safety data from over 10 million pre-bankruptcy Chrysler vehicles will lead to tens of thousands of needless disabling injuries or deaths. I have submitted a study published by Safety Research Strategies to support that statement.

In an effort to stabilize these companies, our tax dollars have been used in a manner that prevents injured taxpayers from exercising their right to hold these companies accountable. In the case of Chrysler consumers, that right has been taken away from any taxpayer who was injured by a pre-bankruptcy vehicle in the future as well.

The fact that we are stabilizing these companies with our tax dollars should require them to have greater responsibility to the taxpayers, not less.

If our laws allow that, then the laws must be changed and new ones must be written. Legislation must be passed that holds Chrysler to the same level of accountability that every other automobile manufacturer in this country has.

The pending cases of current victims of Chrysler and GM must also be heard. As I said, they represent dozens of dangerous defects that need to be tracked by the NHTSA to determine if and when recalls need to be issued which will make our roads and our future vehicles safer.

I also want to lend my support to the effort by the auto dealers to have their original franchise agreements restored. Under those agreements, Chrysler and GM agreed to indemnify auto dealers for product liability lawsuits, which would help a lot of people against Chrysler and GM get compensated. Settlements in these cases would benefit our economy by allowing many of the victims to, once again, become functional taxpaying members of society. Settlements would also provide immediate financial relief to the government by allowing victims like me to stop relying on Social Security Disability, Medicare, and other government-funded assistance programs.

Congressman Carson's bill, H.R. 3088, the Jeremy Warriner Consumer Protection Act, addresses these issues and will provide these benefits.

At the end of the day, the sanctity of human life, our safety and the safety of our loved ones must come first, before anything else. There is not a single person in this room who wouldn't drop what they were doing and rush to the hospital if they learned that their loved one had been injured and was laying in the hospital bed in the state that I was. There is not a single person in this room who would not hold the manufacturer accountable if they learned that it was because of a defect that they were injured or one of their loved ones lost their life.

A defective vehicle does not care whether you are a Democrat or a Republican, if you are a member of the UAW, if you work for Chrysler or GM, or where your money comes from.

I trust the Members of this Committee to act quickly, because doing nothing increases the risk that you, your loved ones, and your constituents will be severely injured or killed by a defective vehicle. After you have experienced something like I have, you learn that the theory of "It won't happen to me" doesn't really protect you or those you love. You also learn to see what can't be changed and what can. I can never regain my legs or the subsequent loss that has come from that, but we can regain our right to hold Chrysler and GM accountable in court for the injuries caused by their vehicles.

It is time for Congress to take action to restore that right and to ensure our safety. This is a tremendous opportunity for the Members of Congress and for our President. By taking action to right this wrong, our government can clearly prove that it is still a government for the people. Thank you.

Mr. COHEN. Thank you, Mr. Warriner.

[The prepared statement of Mr. Warriner follows:]

PREPARED STATEMENT OF JEREMY K. WARRINER

## **Written Testimony of Jeremy K. Warriner**

### **Victim of a defective pre-bankruptcy Chrysler vehicle**

**Wednesday, July 22, 2009**

### **Ramifications of Auto Industry Bankruptcies, Part III**

As you read this testimony please think of your friends, family, loved ones, constituents, and yourselves. The auto industry bankruptcies have created safety issues that threaten all of us. I do not want what happened to me to happen to anyone else. Congress has the opportunity to fix these issues and protect the safety of every American Citizen.

In October of 2005 I was in a car accident. The damage left me trapped, pinned between the dash and the seat, and suspended in my 2005 Jeep Wrangler Unlimited, which had rolled onto its passenger side. I had several severe injuries, all of which would have healed. Then a fire ignited in the engine that burned through the firewall into the passenger compartment. Somehow, I was rescued, but when you look at the wreckage (pictured at the end of this statement), the fact that I'm alive is unbelievable.

Five and a half weeks later I awoke from a medically induced coma to learn that my legs had been amputated from above each knee. My lower legs had sustained fourth degree burns, the burns caused my body to become deathly ill from infection, my lungs had failed, and my kidneys had failed. The only chance the doctors had to save my life was to amputate my legs and that wasn't a guarantee. My parents had to make that decision without being able to speak to me. My four year old niece, who didn't know what was happening, became selectively mute from the overwhelming sadness she felt around her.

I have endured over 38 surgeries throughout the past three years. I lost my career in the hospitality industry, a field in which I have a degree, as a direct result of the loss of my legs. My medical bills total over two million dollars. My prosthetics, which the insurance company initially denied as "not medically necessary", cost approximately \$60,000 per leg. I am currently on COBRA and will soon be on Medicare. I have not been able to find appropriate employment. The few jobs that I have been able to find do not pay enough for me to keep my house on a single income. As a result, I now rely on Social Security Disability to survive, and that barely covers my living expenses.

At my request, my attorney's hired expert engineers to examine the wreckage of my vehicle. They determined that the fire was caused by highly flammable brake fluid. The plastic reservoir that held the brake fluid shattered during the accident and leaked all of the brake fluid into the hot engine. I believe this happened because of an unsafe defective design due to the fact that the reservoir was not protected from impact, and Chrysler had used a safer metal reservoir in prior Jeep Wrangler models. In July of 2006 I filed a lawsuit against Chrysler. In November of 2008 Chrysler used its financial instability at the time to delay the court ordered mediation until May 5<sup>th</sup>, and then declared bankruptcy on April 30<sup>th</sup>.

Through the bankruptcy process Chrysler was relieved of responsibility for approximately 300 pending product liability claims, including my own, and any future claims resulting from potential vehicle defects in any of the approximately 10 million pre-bankruptcy vehicles on the road today. GM was relieved of responsibility for approximately 1000 pending product liability claims as well as any injuries or deaths caused by defective GM vehicles before or during the bankruptcy process that have not been filed. Each of the approximately 1300 pending claims against these auto manufacturers represent potential defects that could lead to immediate safety recalls. If these cases are not heard in court these defects will not get tracked by the National Highway Traffic Safety Administration, Chrysler and GM will not admit these defects exist, recalls will not be issued, and more injuries and deaths will occur. Ignoring the pending claims and the safety data from over 10 million pre-bankruptcy Chrysler vehicles will lead to tens of thousands of needless disabling injuries and deaths.

I am including with my testimony a study by Safety Research Strategies, Inc that clearly shows the risk to the American people caused by preventing product liability claims from being heard. This study was done at a time when GM intended to follow in Chrysler's footsteps by using the bankruptcy process to avoid future claims for injuries and deaths. Even though GM has accepted responsibility for future injuries and deaths caused by their pre-bankruptcy vehicles, until Chrysler accepts the same responsibility, and the pending claims have been heard, the risk remains. Not all Chrysler and GM vehicles are defective, but we all know that dangerous defects do exist. They can and will cause disabling injuries and deaths, which will only lead to more people who rely on Social Security Disability, Medicare, and other government funded assistance programs.

We have a Constitutional 7<sup>th</sup> Amendment right to have our cases heard in court. If Chrysler and GM will not accept responsibility for these defects and the injuries they have caused, then a jury must weigh each case and make that decision for them. Yet, in an effort to stabilize these companies, our tax dollars have been used in a manner that prevents injured tax payers from exercising that right. In the case of Chrysler consumers, that right has been taken away from any tax payer who is injured by a pre-bankruptcy vehicle in the future as well. The fact that we are stabilizing these companies with our tax dollars should require them to have more responsibility to the tax payers, not less. If our laws allow that, then the laws must be changed and new ones must be written.

Legislation must be passed that holds Chrysler to the same level of accountability that every other automobile manufacturer in the country has. The "new Chrysler" must have successor liability for future injuries and deaths caused by defects in the pre-bankruptcy vehicles. This was done in the case of GM and must also be done for Chrysler, because the alternative creates a danger to the American People.

The pending cases of the current victims of Chrysler and GM must also be heard. They represent dozens of dangerous defects that need to be tracked by the NHTSA to determine if and when recalls need to be issued, which will make our roads, and future vehicles, safer. Settlements in these cases would provide immediate financial relief to the government by allowing many of these victims to once again become functional tax paying members of society. Many victims would be able to stop relying on Social Security Disability, Medicare, Medicaid, and other government funded assistance programs to survive.

Congressman Andre Carson, of Indiana, has introduced H.R. 3088, the Jeremy Warriner Consumer Protection Act, to the US House of Representatives. While it is an honor to have my name attached to this bill please remember that I am but one of hundreds, if not thousands, of people who have been injured by Chrysler and GM. (I have included a few of their stories at the end of this statement.) H.R. 3088, when signed into law, will require Chrysler and GM to purchase liability insurance to cover current and future claims for injuries and deaths. This holds Chrysler to the same accountability that every other auto manufacturer has and it allows the pending claims against both Chrysler and GM to be heard.

If H.R. 3088 is not passed then a Congressional relief fund must be established for the current victims of these companies. Our government has used our tax dollars to invest in Chrysler and GM. If our government will not hold Chrysler and GM accountable for injuries and deaths caused by their pre-bankruptcy products, then our government must accept those liabilities as their own. Just as they have invested in these American companies, they must invest in the American people who have been injured by these companies.



At the end of the day the sanctity of human life, our safety, and the safety of our loved ones must come before anything else. There is not a single person who wouldn't drop what they were doing and rush to the hospital if they learned that their loved one had been severely injured. There is not a single person who wouldn't hold the vehicle manufacturer accountable if you learned that their product caused your injuries, or the death of a loved one. Allowing Chrysler and GM this immunity takes away our right to face them in court, and we have bought that immunity for them with our tax dollars. This is a mistake that needs to be fixed.

I don't care about who was responsible for the mistake, I care about who is going to take responsibility for fixing it. Congressman Carson took the crucial first step by introducing H.R. 3088. I believe in our President, his Administration, and the Members of Congress. I trust all of the members of this Committee to understand that this is not an issue for political debate. A defective vehicle does not care whether you are Democrat or Republican, if you are a member of the UAW, if you work for Chrysler or GM, or where your money comes from. I trust our Government to treat this issue with the same sense of urgency that has been given to the Chrysler and GM bankruptcies. I trust the members of Congress and our President to either support H.R. 3088, or an alternative solution, because doing nothing dramatically increases the risk that they, their loved ones, and their constituents will be severely injured or killed by a defective vehicle.

After you've experienced something like I have you learn that the theory of "it won't happen to me" doesn't really protect you or those you love. You also learn to see what can't be changed, and what can. I can never regain my legs and the subsequent loss that has come from that, but we can regain our right to hold Chrysler and GM accountable in court for the injuries and deaths caused by all of their products. It is time for Congress to take action to restore that right and ensure our safety. This is a tremendous opportunity for the Members of Congress, and our President. By taking action to right this wrong our Government can clearly prove that it is still a Government for the People.



**Victims Cases 'Wiped Out' Due To  
General Motors and Chrysler Bankruptcies**



**Lyle Austin (age 19)  
Dorothy Austin (mother) John Paul Austin (father)  
Bridgeton, NJ**

**Lyle was severely injured when the van in which he and his family were riding was hit; his defective seat moved upon impact**

On Columbus Day in 2007, Lyle Austin was headed to spend the day at the beach with his family in a 1996 Dodge Ram Van. An SUV traveling in the opposite direction swerved across the midline. Though his father tried to swerve, the vehicle hit the left passenger side of the car, where Lyle was seated. "It sounded like a bomb," said Lyle's mother Dorothy. Though she, her husband, and their second son were not injured, the Lyle's defective seat moved upon impact and as a result he was paralyzed from the waist down.

"Lyle also ruptured his intestine and fractured his hip, but the doctors weren't going to operate on that because they thought he would never walk again," Dorothy said. She moved to Philadelphia with Lyle, who is autistic, to advocate on his behalf while he underwent rehabilitation. After 7 months away from the other half of the family, Lyle has regained some feeling in his arms and legs and can now use a walker for short distances, though he still relies primarily on a wheelchair. Dorothy clarified, "the hospital bills were \$15,000, which is actually pretty moderate, but the real cost has been emotional." The family has filed a lawsuit.



**Ralph Binder (deceased)  
Joy Wolf (widow) and two sons  
Los Angeles, CA**

**Ralph Binder, Emmy-winning ABC News cameraman, was killed when the roof of his GM Suburban caved in during an accident.**

Ralph Binder, a loving father to two young boys, was a news cameraman who worked almost exclusively for ABC News. Over the years, he covered everything from the President and the White House to California Wildfires. A three time Emmy award winner, Ralph was an integral part of major network news coverage for the last 30 years.

On December 6, 2007, Ralph, driving with soundman Daniel Johnson, were on their way to cover a story in Nebraska, when his GM Chevy Suburban swerved on an icy road. The car rolled 1 1/2 times. By the time it came to a stop, the roof had crushed in on the drivers' side, killing Ralph, in what should have been a benign crash. At the time the 1998 Suburban was built, other roof designs were readily and inexpensively available that would have saved Ralph's life.

Ralph was married to Joy Wolf, a renowned photojournalist, ABC News freelance producer and writer. To try to cover Ralph's love, guidance and all the things he did for and with his two young sons, and their devastating loss, would take pages and pages of details.



**Callan Campbell (age 23)  
Williamstown, PA**

**The GMC Jimmy's weak roof collapsed during an accident that left Callan a quadriplegic**

On August 17, 2004, 18-year-old Callan Campbell was a front-seat passenger in a 1996 GMC Jimmy operated by her friend who lost control of the vehicle. The vehicle entered into a low speed roll, rolled 1.5 times, and ended on its roof. Callan should have walked away from this accident. Instead, the collapsing roof caused her spine to partially dislocate and she became a C6 incomplete quadriplegic. She had just graduated from high school with awards in June 2004, and was one week away from starting college.

Today Callan cannot walk, does not have bowel or bladder control, and does not have full use of her arms and hands. All of Callan's injuries are the result of the known weak roof of the GMC Jimmy, a vehicle with a high propensity to roll.

Callan's medical bills for treatment immediately following the crash total about \$200,000. In addition, Callan's parents made \$160,000 of renovations to their home to accommodate Callan's new physical and medical needs. Callan has lost her independence, her mobility, much of her dignity, and her ability to pursue her dreams. She has fought through years of therapy and multiple surgeries to regain what she can, but her life has been forever changed. Callan's parents are obviously concerned about what will happen to their daughter when they can no longer take care of her. Callan's needs cannot be met unless GM is held accountable for its decision to put a weak roof on a heavy, unstable Jimmy.



**Linda Catalano (deceased)  
Brian and Christina (children, Christina is active UAW member)  
Detroit, MI**

**Linda Catalano was killed when her Chrysler min-van “self-shifted” into reverse, dragging her under the car.**

On the evening of August 3, 2008, then 55-year-old mother and grandmother, Linda Catalano, had completed a garage sale and had left her home several blocks away to collect the remaining sale signs along the road. She evidently stopped the vehicle along the roadway to pick up a sign.

Ms. Catalano then placed her vehicle into what she must have believed to be “park” and opened the door and stepped out of the Chrysler Mini-Van to pick up her signs, with the engine running and the driver’s side door open. The vehicle then “self-shifted” into reverse, knocking Ms. Catalano to the ground and dragging her underneath the left front tire, where it pinned her. She was killed. Ms. Catalano left behind three children - Brian, Christina, and Bradley - and grandchildren, who adored her and miss her to this day. The family has filed a lawsuit against Chrysler.



**Terry Cole**  
Sikeston, MO

**Terry Cole, who had lived successfully for 35 years in a wheelchair, was severely burned by a defective seat heater because he does not have normal sensation in the lower half of his body.**

Terry Cole, a businessman from Sikeston, Missouri, had a very successful life despite being confined to a wheelchair for the last 35 years. He took great care of his skin so that remarkably he had never suffered from any the skin problems as many wheelchair-bound individuals do. In November 2007, he took a 45-minute trip in his brand new GM

Cadillac Escalade. He was using a seat heater. Terry does not have normal sensation in the lower half of his body and was unable to feel that the seat had heated to 150 degrees during the trip, severely burning him with third degree burns.

The burns laid up Terry for 90 days and left him with permanent skin problems. He is far less mobile than he previously had been. Before the incident he was receiving experimental stem cell treatments in China and was making remarkable progress, to the point he was even able to stand with assistance. Yet all of that progress was lost after he experienced the burns. He is now unable to travel long distances. His business and his social life have suffered greatly. Terry continues to be a loyal GM customer – buying

GM vehicles for his business, but said, "GM should pay for what they have done to me and shouldn't get to squirm out through bankruptcy." Terry has filed a lawsuit against GM.



**Amanda Dinnigan (age 10)**  
**Robert Dinnigan (father)**  
**Smithtown, NY**

**As an 8-year-old, Amanda Dinnigan spinal cord was dislocated during an accident due to a faulty seat belt; she is paralyzed from the chin down.**

On February 21, 2007, Amanda's mother was driving her and three cousins near their home in their 2003 GMC Envoy. Amanda, then 8, was strapped into the vehicle's third-row seats. Her mother had an accident and hit a tree. The seatbelt and shoulder restraint, designed for an adult which came across the necks of the children, dislocated Amanda's spinal cord. Her young cousin who was seated next to her broke her neck. Her cousin recovered from surgery, but Amanda is paralyzed from the chin down. She has no feeling and can hardly move her head. She cannot breathe on her own and is dependent on a ventilator. She requires 24-hour nursing care. Next year, Amanda's parents would like her to go to a school that fits her needs, but it is 45 minutes away from their home. They are not sure they will uproot their family.

The family spent \$100,000 to build a "mini ICU" in their house with two ventilators and a hospital bed with a lift. Medical bills are going on \$500,000 each year and will continue every year for the rest of her life. Robert's union insurance as an ironworker will cap out soon at \$1 million. Her lawsuit has been filed in Suffolk County, Long Island.



**Shaun Nicolas Doss (age 8)**  
Gilbert, AZ

**As a 6-year-old, Shaun Nicolas Doss became severely injured and is now paraplegic when his seatbelt failed during an accident.**

On May 15, 2007, 6-year-old Shaun Doss was riding in the third-row passenger seat of his family's Dodge Durango, along with his father Robert and three siblings, when another vehicle ran a red light, "T-boning" the Doss's Durango at the driver's side rear wheel. Because the seatbelts in the Doss's Durango had not been properly affixed to the vehicle's frame, they did not function properly upon impact. As a result, Shaun suffered internal bleeding from the spleen, appendix, and intestines—and was ultimately rendered a T4 paraplegic. Shaun spent three months in the hospital, incurring medical bills in excess of \$1 million. Although Shaun remains as active as he can and is trying to resume a career as a child model, he will be confined to a wheelchair for the rest of his life.

Robert Doss, a single father and army veteran, says trying to keep up with the medical expenses incurred from the accident has been impossible. Caring for Shaun has ultimately cost him his job, house, and car. "An experience like this really opens your eyes," said Robert. "You respect life a lot more when you endure something like this."

The emotional toll on the family has been devastating as well. Shaun has been utterly "distracted" and prone to terrible "mood swings" as a result of the trauma he suffered. And as Robert said, "I'm not a crying person, but I cried every day of the three months I spent at Shaun's side in the hospital." Robert currently has a lawsuit pending against Chrysler.



**Kissan Howard (age 15)**  
**Renee Howard (Mother)**  
**Wildwood, NJ**

**As a 2-year-old, Kissan Howard's neck was broken during an accident when she slipped out of her seatbelt; she needs round the clock care.**

In 1996, Renee, her husband, and then two year-old Kissan, riding in their Jeep Grand Cherokee, were hit head on. Kissan had been in the rear middle seat wearing a lap belt. When the collision occurred, her upper body jackknifed forward causing a complete C2 fracture. She could not breathe on her own. Renee's husband, who was a registered nurse at the time, breathed for Kissan until help arrived. As a result she did not suffer from any brain damage. She was in the hospital for two months and on a ventilator for four years. She was put into a halo – a steel cage that screwed into her head and still has the marks on her head today. She is paralyzed, close to a quadriplegic.

Renee stopped working for years, but now she is able to work again as Kissan is in school and a straight-A student. Before the accident, Kissan could walk and talk and could go to the bathroom on her own. However, now she still needs around-the clock care, gets oxygen throughout the night and she cannot use the bathroom on her own. They have no state-paid nursing care and take care of her entirely on their own. They have filed a lawsuit.

**Mark Jones (deceased)**  
**Kimberly Jones (widow)**

**Well-known gasoline tank defect in the Chevrolet Tracker allowed gas to leak from a low-speed collision igniting a fire that killed Mark Jones**

On October 26, 2006, retired US Navy submarine chief Mark Jones and his son Zach were rear-ended outside of the National Guard Armory in Salisbury, Maryland in their 1995 Chevrolet Tracker. Neither Mark nor Zach Jones suffered serious injuries from the impact forces in the crash, which was recorded by the other vehicle's SDM (black box) as only an 18 mph impact.

However during the accident, the fuel tank behind the rear axle was punctured and leaked fuel – a known defect that caused recalls in later models. The gasoline ignited and engulfed Mark Jones in flames causing thermal burns to his body until the fire hose extinguished the flames. Mark continued to suffer until he succumbed to these horrific injuries four days later. He is survived by his wife Kimberly Jones and his two children Amanda and Zachary Jones. The case brought by his family was in mediation in Maryland.



**Jeremy Warriner**  
Indianapolis, IN

**Jeremy Warriner's Jeep Wrangler was hit and during the accident, the cheap plastic brake fluid container broke apart, causing a fire and burning his legs so badly that both legs had to be amputated.**

On October 22, 2005, Jeremy Warriner was driving home from work in his 2005 Jeep Wrangler when a 16-year-old driver drove through a stop sign and struck his vehicle. The Jeep slid off the road and hit a pole. That impact caused the cheap plastic brake fluid container to break apart. A fire ensued. Jeremy was rescued from his Jeep but only after he had suffered 3rd and 4th degree burns to his legs. When he awoke from a medically induced coma nearly two months later, he found that both legs had been amputated.

Jeremy suffered for over a year in and out of hospitals and has had 38 surgeries since the accident. His medical bills are over \$2 million. His insurance has almost maxed out. He had been working in the hotel/hospitality industry and it took him a year and a half to get back to work. But then, his position was eliminated. He will probably have to go back to school to get trained in something else. He is single and in his 30s, but very much wants to start a family someday. This is not the life he had planned. He has sued Chrysler and his case was scheduled for mediation on May 5th, but it was canceled due to Chrysler filing for bankruptcy on April 30th.



**Kimberly Young**  
**Dionne Sales (cousin and attorney) Rose Young (mother and caretaker)**  
**Oakland, CA**

**Kimberly Young's neck was broken, rendering her quadriplegic, when the roof of her Jeep Grand Cherokee caved in during an accident.**

On August 29, 2008, 44-year-old Kimberly Young was driving her mother's 2004 Jeep Grand Cherokee with her daughter, Keyona Chester, when the vehicle was involved in an accident and rolled over. Her neck was broken when the roof caved in, rendering her quadriplegic. Her daughter was practically unscathed.

Before the accident, Kimberly was very active socially and with her daughters. Months prior to the incident, she received a promotion from Accounting Technician to Accountant I with the State of California. As a result of the incident, Kimberly has not returned to her position with the state. She has lost her home to foreclosure, and her 16-year old daughter has temporarily moved in with her father. Kimberly is unable to bathe, wash her face, or brush her teeth without assistance of a caregiver. Kimberly's mother, Rose, has moved Kimberly in with her and cares for her before and after work. Rose's home has been modified with wheelchair accessible ramps. Her 24-hour care is being supplied by family members while Rose is at work. Kimberly remains in constant pain, and her hands are constantly in splints in an attempt to relieve the pain.

Since Kimberly lacks a wheel-chair accessible van, she relies on Paratransit to get to and from any appointments, which is not always reliable. Kimberly also has acquired a number of phobias related to

going out in public, being in crowds, and sleeping. She is unable to participate in physical therapy, because she is 100% responsible for the cost, but she cannot currently afford it.

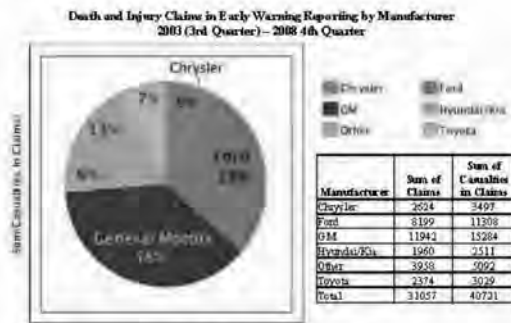
# **Public Safety at Risk:**

## **Bankruptcies Leave Legacy of Defects, Injuries and Deaths**



Under the terms of the bankruptcies, General Motors and Chrysler will shed all product liability claims for tens of millions of vehicles currently on the road, leaving thousands of individuals and families uncompensated for the permanent injuries or deaths caused by vehicle defects. Allowing these automakers to continue as new entities with no due care responsibilities for the vehicles built before bankruptcy will also decrease public safety. The story is in the numbers.

From the third quarter in 2003 to the fourth quarter in 2008, Chrysler fielded 2,464 death and injury claims, according to its Early Warning Reporting (EWR) data, which all automakers are required to file with the National Highway Traffic Safety Administration. Collectively, they represent 3,497 individual fatalities and injuries. General Motors generated many more claims. In the same time period, the automaker received 11,942 claims, representing a total of 15,284 individual fatalities and injuries.<sup>1</sup>



(Source: Quality Control Systems Corp.)

Chrysler's average annual number of death and injury claims in the reporting period is 477, resulting with an average of 636 casualties per year (casualties are individual deaths and injuries). For General Motors, the average annual claims rate is 2,171 with an average of 2,779 casualties per year. The average combined casualties per year for both companies is 3,415.

These claims can be expected to continue at the same pace, resulting in approximately 3,400 new casualties each year during the next couple of years. This is based on data showing that Americans are holding onto their vehicles longer. According to the latest survey by R.L. Polk and Company, the average age of the passenger car in the U.S. rose

<sup>1</sup> EWR require manufacturers to report claims on vehicles 10 years old or less. These counts are for non-duplicative claims.

from 9.2 to 9.4 years over the last year alone, due, in part, to the weak economy and the cost of a new car. The elusive economic recovery in the U.S. is likely to strengthen this trend.

Early Warning Reporting Claims, 2003 Qtr 3 - 2008 Qtr 4

	Total EWR Claims	Average EWR Claims per Year	Total Casualties in EWR Claims	Average Casualties in EWR Claims per Year
Chrysler	2,624	477	3,497	636
GM	11,942	2,171	15,284	2,778
Chrysler/GM Combined	14,566	2,648	18,781	3,415

An examination of the claims for all vehicle manufacturers required to report EWR data to NHTSA shows that Chrysler claims are approximately proportionate to its average market share of about 13.5 percent. However, GM commands a disproportionate number of claims, given its average market share of 25.25 percent over the same time period.

GM and Chrysler Market Share, 2003-2008

Manufacturer	2003	2004	2005	2006	2007	2008	Average Market Share
GM	28.30%	27.50%	26.20%	24.50%	23.70%	21.30%	25.25%
Chrysler	14.10%	14.40%	14.90%	12.90%	12.90%	12.10%	13.55%

Source: Automotive News Data Center, U.S. Passenger and Light Truck Sales by Make

Neither General Motors nor Chrysler will have the data or the incentive to correct defects that emerge post-bankruptcy. Automakers use death and injury claim trends to identify defects, as does NHTSA, which collects this information. If people can not recover for the human and property damage caused by GM or Chrysler vehicles, these claims will not be filed. The automaker will be hampered in its quest to monitor the quality of its products in the field.

This will have serious consequences for public safety. First, the absence of death and injury claims will decrease the number of recalls and remedies for which GM and Chrysler will be responsible after the bankruptcies. Manufacturers typically resist recalls – especially if the defect is widespread – because recalls can be expensive and enforce a negative image of their brand in consumers' minds. In the last five years, both manufacturers have recalled millions of vehicles for extremely serious safety problems, including roofs that fly off their frames, seat belts that become unlatched in crashes, wiring that shorts causing engine fires, and broken brake pedals that don't apply the brakes.

From 2004 to 2008, Chrysler has issued 109 recalls affecting 11.4 million vehicles. GM launched 129 recalls affecting 19 million. For example, in 2004, General Motors recalled 92,863 Chevrolet Malibus with sticky accelerator arm pedals that wouldn't return to idle

when the driver took his foot off the gas. In 2006, Chrysler recalled 42,469 2002-2003 Jeep Liberty vehicles originally sold in Salt-Belt states with front suspension upper control ball joints that had a tendency to separate while driving – meaning the driver would suddenly have no steering capability.

Recalls by Calendar Year and Manufacturer				
Year	Chrysler		General Motors	
	Total Recalls	Number of Vehicles Affected	Total Recalls	Number of Vehicles Affected
2004	29	5,842,746	41	10,272,219
2005	11	766,162	30	4,997,923
2006	29	2,349,919	17	1,369,916
2007	27	2,063,506	20	538,214
2008	13	361,065	21	1,754,720
Total	109	11,383,398	129	18,932,992

These are defects with potentially catastrophic consequences. If neither company is responsible for the past and future claims involving 40 million vehicles, few will file death or injury claims. If death and injury claims data do not reflect the status of real-world problems on the road, safety is compromised. And, if GM and Chrysler no longer bear the liability for uncorrected defects, the automaker has few motivations to fix the pre-bankruptcy problems.



## General Motors EWR Claims by State, 2003 Qtr 3 – 2008 Qtr 4

State	Counts of EWR Claims with Deaths and Injuries	Total Casualties in EWR Claims	Deaths in EWR Claims	Injuries in EWR Claims
ALABAMA	295	368	56	312
ALASKA	30	39	1	38
ARIZONA	259	354	61	293
ARKANSAS	191	246	27	219
CALIFORNIA	935	1288	189	1099
COLORADO	152	189	12	177
CONNECTICUT	89	95	1	94
DC	8	8	0	8
DELAWARE	41	49	0	49
FLORIDA	727	903	70	833
GEORGIA	387	472	27	445
HAWAII	34	41	5	36
IDAHO	45	55	6	49
ILLINOIS	497	628	71	557
INDIANA	281	353	24	329
IOWA	82	94	4	90
KANSAS	97	113	8	105
KENTUCKY	272	335	21	314
LOUISIANA	344	442	51	391
MAINE	52	69	5	64
MARYLAND	172	204	13	191
MASSACHUSETTS	178	201	2	199
MICHIGAN	495	600	63	537
MINNESOTA	107	119	5	114
MISSISSIPPI	240	306	38	268
MISSOURI	332	413	28	385
MONTANA	53	64	8	56
NEBRASKA	54	72	3	69
NEVADA	108	149	27	122
NEW HAMPSHIRE	36	39	0	39
NEW JERSEY	293	340	11	329
NEW MEXICO	90	129	24	105
NEW YORK	486	597	28	569
NORTH CAROLINA	327	411	10	401
NORTH DAKOTA	16	21	1	20
OHIO	481	606	25	581
OKLAHOMA	186	243	29	214
OREGON	88	119	10	109
PENNSYLVANIA	497	586	37	549
RHODE ISLAND	30	37	3	34
SOUTH CAROLINA	216	271	29	242
SOUTH DAKOTA	28	35	4	31
TENNESSEE	335	420	34	386
TEXAS	1213	1670	290	1380
UTAH	58	103	20	83
VERMONT	23	30	4	26
VIRGINIA	233	287	17	270
WASHINGTON	122	162	13	149
WEST VIRGINIA	191	249	17	232
WISCONSIN	214	274	11	263
WYOMING	28	38	9	29
US TERRITORIES/FOREIGN	193	348	110	238

Source: Quality Control Systems ([www.quality-control.us](http://www.quality-control.us))

## Chrysler EWR Claims by State, 2003 Qtr 3 – 2008 Qtr 4

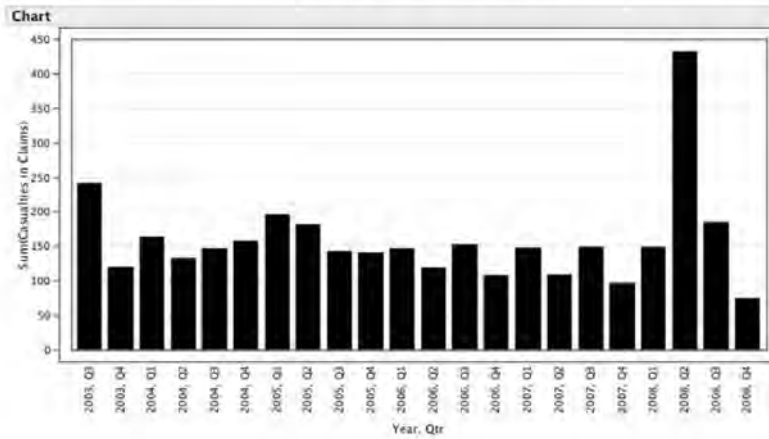
State	Counts of EWR Claims with Deaths and Injuries	Total Casualties in EWR Claims	Deaths in EWR Claims	Injuries in EWR Claims
ALABAMA	60	85	22	63
ARIZONA	44	72	11	61
ARKANSAS	29	43	9	34
CALIFORNIA	206	294	34	260
COLORADO	31	42	3	39
CONNECTICUT	25	31	2	29
DC	1	1	0	1
DELAWARE	12	12	4	8
FLORIDA	211	298	54	244
GEORGIA	71	91	31	60
HAWAII	16	24	4	20
IDAHO	10	15	0	15
ILLINOIS	86	96	15	81
INDIANA	48	55	5	50
IOWA	11	18	6	12
KANSAS	13	20	3	17
KENTUCKY	43	49	6	43
LOUISIANA	55	82	18	64
MAINE	12	34	12	22
MARYLAND	48	57	8	49
MASSACHUSETTS	53	63	6	57
MICHIGAN	85	98	10	88
MINNESOTA	27	30	0	30
MISSISSIPPI	49	81	26	55
MISSOURI	60	73	15	58
MONTANA	8	23	4	19
NEBRASKA	12	16	2	14
NEVADA	24	32	5	27
NEW HAMPSHIRE	11	15	1	14
NEW JERSEY	100	110	4	106
NEW MEXICO	32	54	16	38
NEW YORK	100	123	13	110
NORTH CAROLINA	46	55	8	47
OHIO	78	96	11	85
OKLAHOMA	34	44	7	37
OREGON	38	43	1	42
PENNSYLVANIA	141	178	15	163
RHODE ISLAND	10	10	1	9
SOUTH CAROLINA	53	65	11	54
SOUTH DAKOTA	4	5	0	5
TENNESSEE	60	91	15	76
TEXAS	309	441	97	344
UTAH	18	29	5	24
VERMONT	4	4	0	4
VIRGINIA	58	71	6	65
WASHINGTON	23	25	0	25
WEST VIRGINIA	39	47	7	40
WISCONSIN	27	35	3	32
WYOMING	5	7	2	5
US TERRITORIES/FOREIGN	84	114	25	89

Source: Quality Control Systems ([www.quality-control.us](http://www.quality-control.us))

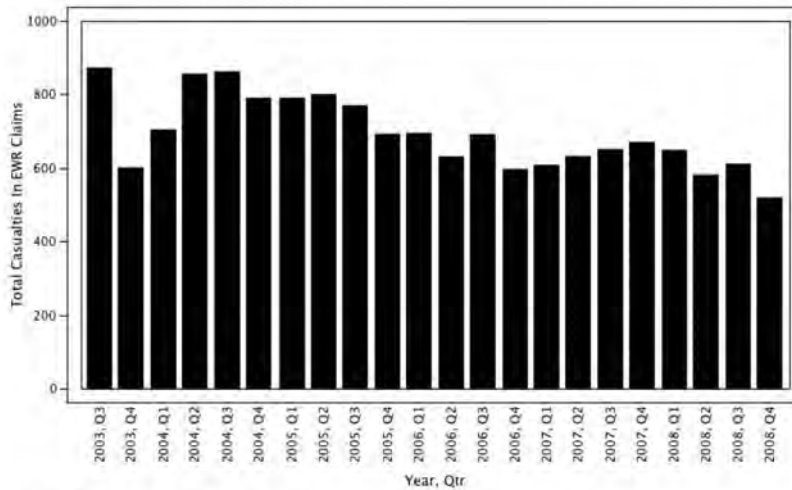
## Chrysler and GM EWR Claims by State, 2003 Qtr 3 - 2008 Qtr 4

State	Chrysler - Total Claims	Chrysler - Avg Claims per Year	GM - Total Claims	GM - Avg Claims per Year	Chrysler/GM Combined - Total Claims	Chrysler/GM Combined - Avg Claims per Year
Alabama	60	10.91	295	53.64	355	64.55
Alaska	0	0.00	30	5.45	30	5.45
Arizona	44	8.00	259	47.09	303	55.09
Arkansas	29	5.27	191	34.73	220	40.00
California	206	37.45	935	170.00	1141	207.45
Colorado	31	5.64	152	27.64	183	33.27
Connecticut	25	4.55	89	16.18	114	20.73
DC	1	0.18	8	1.45	9	1.64
Delaware	12	2.18	41	7.45	53	9.64
Florida	211	38.36	727	132.18	938	170.55
Georgia	71	12.91	387	70.36	458	83.27
Hawaii	16	2.91	34	6.18	50	9.09
Idaho	10	1.82	45	8.18	55	10.00
Illinois	86	15.64	497	90.36	583	106.00
Indiana	48	8.73	281	51.09	329	59.82
Iowa	11	2.00	82	14.91	93	16.91
Kansas	13	2.36	97	17.64	110	20.00
Kentucky	43	7.82	272	49.45	315	57.27
Louisiana	55	10.00	344	62.55	399	72.55
Maine	12	2.18	53	9.64	65	11.82
Maryland	48	8.73	172	31.27	220	40.00
Massachusetts	53	9.64	178	32.36	231	42.00
Michigan	85	15.45	495	90.00	580	105.45
Minnesota	27	4.91	107	19.45	134	24.36
Mississippi	49	8.91	240	43.64	289	52.55
Missouri	60	10.91	332	60.36	392	71.27
Montana	8	1.45	53	9.64	61	11.09
Nebraska	12	2.18	54	9.82	66	12.00
Nevada	24	4.36	108	19.64	132	24.00
New Hampshire	11	2.00	36	6.55	47	8.55
New Jersey	100	18.18	293	53.27	393	71.45
New Mexico	32	5.82	90	16.36	122	22.18
New York	100	18.18	486	88.36	586	106.55
North Carolina	46	8.36	327	59.45	373	67.82
North Dakota	0	0.00	16	2.91	16	2.91
Ohio	78	14.18	481	87.45	559	101.64
Oklahoma	34	6.18	186	33.82	220	40.00
Oregon	38	6.91	88	16.00	126	22.91
Pennsylvania	141	25.64	497	90.36	638	116.00
Rhode Island	10	1.82	30	5.45	40	7.27
South Carolina	53	9.64	216	39.27	269	48.91
South Dakota	4	0.73	28	5.09	32	5.82
Tennessee	60	10.91	335	60.91	395	71.82
Texas	309	56.18	1213	220.55	1522	276.73
Utah	18	3.27	58	10.55	76	13.82
Vermont	4	0.73	23	4.18	27	4.91
Virginia	58	10.55	233	42.36	291	52.91
Washington	23	4.18	122	22.18	145	26.36
West Virginia	39	7.09	191	34.73	230	41.82
Wisconsin	27	4.91	214	38.91	241	43.82
Wyoming	5	0.91	28	5.09	33	6.00
US Territories/Foreign	84	15.27	193	35.09	277	50.36

**Death and Injury Claims in Early Warning Reporting by Quarter: Chrysler**  
2003 (3<sup>rd</sup> Quarter) – 2008 4<sup>th</sup> Quarter



**Death and Injury Claims in Early Warning Reporting: General Motors**  
2003 (3<sup>rd</sup> Quarter) – 2008 4<sup>th</sup> Quarter



Source: Quality Control Systems Corp. ([www.quality-control.us](http://www.quality-control.us))

## Summary Counts for GM

Year, Qtr	Counts of EWR Claims with Deaths and Injuries	Total Casualties In EWR Claims	Deaths in EWR Claims	Injuries in EWR Claims
2003, Q3	688	873	128	745
2003, Q4	486	602	70	532
2004, Q1	565	704	102	602
2004, Q2	707	856	75	781
2004, Q3	659	862	78	784
2004, Q4	664	791	69	722
2005, Q1	668	791	78	713
2005, Q2	631	801	89	712
2005, Q3	569	771	58	713
2005, Q4	550	693	64	629
2006, Q1	540	695	52	643
2006, Q2	503	631	58	573
2006, Q3	507	692	71	621
2006, Q4	439	597	102	495
2007, Q1	470	609	62	547
2007, Q2	443	632	68	564
2007, Q3	479	651	82	569
2007, Q4	533	671	66	605
2008, Q1	500	649	47	602
2008, Q2	442	582	51	531
2008, Q3	493	612	51	561
2008, Q4	406	519	41	478

## Summary Counts for Chrysler

Year, Qtr	Counts of EWR Claims with Deaths and Injuries	Total Casualties In EWR Claims	Deaths in EWR Claims	Injuries in EWR Claims
2003, Q3	170	242	48	194
2003, Q4	76	120	22	98
2004, Q1	135	164	21	143
2004, Q2	111	133	25	108
2004, Q3	119	147	20	127
2004, Q4	123	158	25	133
2005, Q1	148	196	20	176
2005, Q2	135	182	31	151
2005, Q3	106	143	22	121
2005, Q4	105	141	22	119
2006, Q1	101	147	26	121
2006, Q2	92	119	15	104
2006, Q3	115	153	26	127
2006, Q4	82	108	15	93
2007, Q1	119	148	27	121
2007, Q2	88	109	19	90
2007, Q3	98	149	28	121
2007, Q4	81	97	18	79
2008, Q1	101	149	22	127
2008, Q2	324	432	77	355
2008, Q3	136	185	27	158
2008, Q4	59	75	7	68

Source: Quality Control Systems Corp. ([www.quality-control.us](http://www.quality-control.us))

Mr. COHEN. Our fifth witness is Mr. Jack Fitzgerald. His automobile businesses started with Bethesda Dodge dealerships some years ago, and had grown into 9 locations and 35 franchises before the recent attenuation of those there in the States of Maryland, Florida, and Pennsylvania. He has been a member of the Maryland

New Car and Truck Dealers Association, the Washington Area New Automobile Dealers Association, and the National Automobile Dealers Association since 1967. He served on different councils and committees as an officer and director for WANADA, an organization called WANADA. I think you have a fish called Wanda. It's close.

Mr. Fitzgerald, would you begin your testimony.

**TESTIMONY OF JOHN J. FITZGERALD, PRESIDENT,  
FITZGERALD AUTO MALLS**

Mr. FITZGERALD. You have a great sense of humor. And thank you very much for allowing me to be here. I agree it is the highest honor for a citizen to be allowed to appear before Congress. You know, I was born on North Capitol Street and I have always lived in the shadow of the Capitol. When I was young, I lived in the shadow of the Capitol. I never thought I would be in here talking to you, though.

I represent the Committee to Restore Dealer Rights, CRDR. We are the dealers that got dumped. We are the losers. There are 169,000 jobs that you could recreate by just passing our bill; 169,000. Plus, you would give all of your constituents better service than they are going to get.

And I see you walked in. I would love to have a cup of coffee with Chairman Conyers. We are all here. We will go in the back room, and the two of you can work us over. We are here and we are ready.

We have not been able to talk to anybody. But our cause is just. And the reason we have so much support here on the Hill is because, you know, Americans fundamentally want to do what is right. They are going to want to do what is right for Mr. Warriner too. It is the right thing to do. That is what our country is all about. That is what we are all about. You know, you do the right thing. Do the honorable thing. It is the American way. Now, we have coined the phrase—we coined the phrase. We copied the phrase "the big lie."

I want to tell you about the big lie. The big lie involves there are too many dealers. Well, when I started selling cars, there were 40,000 car dealers that just sold domestic cars, and there were only 50 million cars on the road. Now you have got 150 million cars on the road, and last year, there were only 13,000 domestic dealers left. When GM and Chrysler get finished with us, there will be about 9,600, 9,400, I guess, left. So 50 million cars, 40,000 dealers; 150 million cars; 9,600, 9,400 dealers. It doesn't compute.

There are 10,000 import dealers and they have only got 87 million on the road. The problem is the task force looked at Toyota and said that is a great company, let's copy what they are doing. Well, for your information, General Motors was a great company before Toyota ever got here. General Motors was one of the truly great companies of all time and Chrysler too. And I agree with the President, they can rise again. Their problem is they have had some bad managers for the last 28 years or the early '80's is when this began, when the finance guys got ahold of both those companies. And for your information, UAW builds cars, or UAW workers build cars, in California, and they build Corollas there. Ever heard

of a bad Corolla? I haven't. I am a Toyota dealer. I will confess to that. That is a little commercial maybe.

But those are UAW workers in California building Toyotas under Toyota management. The difference is the management. The difference in all business is the management. The difference is always the management.

Now, I am not going to say the UAW hasn't been twisted arms and beating on them and work rules and a lot of bad things. But management is responsible. When you diss your employees, they have got a right to take it out on you, and they do. This is America. That is the American way. We don't get pushed around. Nobody treads on us. That is not the way we are. And that is why we dealers are here. We are getting ripped off.

But the consumer is suffering even more. If you do the math and think about the numbers, there are too few dealers and there is going to be a lot too few. These dealers that were cancelled were profitable, sustaining businesses. They were employing people, paying taxes, doing the right thing, and they don't get any money from the government or the manufacturers. We pay them—if we never sell a single car we have got to pay them at least 40 grand a year, \$40,000 in my smallest store, which sells 100 new cars a year, 100 new cars a year, sells about 400 or 500 used.

And that is another thing. We didn't talk about used cars. I will get back to that. We pay \$40,000 plus in that small store. Now I have got stores, I have got one that sells 6,000 a years. Does it make me wonderful? No. Part of them were Toyotas. That is why I am so wonderful. When Jim Press was selling Toyotas, he was pretty wonderful, wasn't he? He hasn't done so well at Chrysler. Failed at Chrysler. Chrysler management failed. General Motors management failed. And yet they are in place getting paid bonuses to stay and I am here talking to you. What is wrong with that picture? It makes no sense, does it?

Management should be held accountable. Management must manage. That is the oldest rule in the book. And they didn't manage; so they shouldn't keep their jobs. They should not be there. But they are expert on handling outside directors, and they handled the task force like they have always handled outside directors: They manipulated them. The guys on the task force told you yesterday they had never run a business. They don't run businesses. They buy and sell them. So they didn't know the difference. And I think that is really what happened to the task force. We haven't heard consumer reports mentioned once in this room, and yet GM and Chrysler, if it weren't for Chrysler, GM would be dead last in *Consumer Reports'* rankings.

That is what your customers think of you. That is what really matters. It doesn't matter what Wall Street thinks; it matters what the consumers think because that is who writes the check to buy the car. And I have got 43 years of data at Consumer Reports and I can show you when Chrysler and GM made the best cars in the world, the best cars in the world, and they also made a lot of money, and they put a lot of people to work. The union was three times, four times, five times the size it is now. We could put the people in the Midwest back to work. We could put the whole country back to work. There were 55 million cars sold last year around

the world. We should be getting a piece of that. We are the best industrial country in the world. We have four or five generations of people that know how to build cars. In my lifetime I sold those cars. I know what they can do, before the finance guys came along and took over those companies and ruined them.

This is America and we should be building American cars the American way in Detroit and every place else. We can put those people back to work. But you have got a board of directors on these two new companies, none of them ever built a car before. There is not one experienced manufacturer—car manufacturer on that board and there is nobody running one. The guy who used to make telephones is running one of them and another guy who used to make batteries. Now, how is that going to get us a great car again? We need our car manufacturing to go hire some of the Toyota—retired Toyota executives. They are available.

Mr. COHEN. You have gone a little over the——

Mr. FITZGERALD. Oh, I am sorry.

Mr. COHEN. That is all right.

Mr. FITZGERALD. Maybe you can ask me some questions.

Mr. COHEN. Thank you, Mr. Fitzgerald.

[The prepared statement of Mr. Fitzgerald follows:]

PREPARED STATEMENT OF JOHN J. FITZGERALD

STATEMENT OF JACK FITZGERALD  
OWNER / DEALER, FITZGERALD AUTO MALLS

HOUSE COMMITTEE ON JUDICIARY  
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE  
LAW

HEARING ON RAMIFICATIONS OF AUTO INDUSTRY  
BANKRUPTCIES

JULY 22, 2009



STATEMENT OF JACK FITZGERALD  
OWNER / DEALER, FITZGERALD AUTO MALLS

Chairman Cohen and Members of the Committee, I am testifying as one of three co-chairs of the Committee to Restore Dealer Rights, which represents many of the automobile dealerships recently – or soon to be – terminated by old GM and Chrysler. We formed the Committee in the wake of the Chrysler and GM bankruptcies to protect the rights of thousands of auto dealerships and the 169,000 employees who may lose their jobs, and the customers and communities they serve. (See attached table of job losses)

I have over 40 years experience as an auto dealer and am the founder and owner of the Fitzgerald Auto Malls located in Maryland, Pennsylvania, and Florida. I am the owner of five dealerships whose agreements Chrysler has rejected, and three whose dealership agreements GM has opted to wind down.

We appreciate the opportunity to testify and to shed light on what we call the “Big Lie.” I wish we didn’t have to take up your valuable time. Our Committee has made clear for weeks that we are prepared to sit down with the White House Auto Task Force, the CEOs of GM and Chrysler, and others to work toward the reinstatement of the nearly 3,400 dealers terminated or slated for termination. But, there is silence on the other end of the line.

At the outset, I want to stress that we all want the auto manufacturers to succeed — there is no alternate agenda. Dealers are part of the solution, not part of any problem. If McDonalds wants to sell more Big Macs, would it close 3,400 franchises?

It is clear to us that the White House Auto Task Force misunderstood the vitally important role the dealerships play in the success of Chrysler and GM. I hope today to set the record straight, to show how the Bankruptcy Code was used inappropriately, and to explain why the dealers should be reinstated, either by the legislation we support or through a nonlegislative solution worked out with GM, Chrysler, and the Task Force.

Congress created the Bankruptcy Code and the Bankruptcy courts and it is up to you to ensure that your intent is followed and not ignored. In this case, the failed management of GM and Chrysler, abetted by unelected neophytes on the Auto Task Force, have turned the Bankruptcy Code on its head and needlessly extinguished profitable small businesses that were neither failing nor in need of a government bailout.

Rather than assuring that the new Chrysler and new GM are well-positioned to succeed by having a robust national distribution chain, their management instead handicapped the companies by drastically reducing their points of sale. You have the opportunity to correct this.

This reduction is a problem because there are nearly two domestic vehicles on the road for every one import vehicle. The Task Force made a glaring error in its analysis of the marketplace by not focusing on vehicles in operation. A principal reason for dealers to exist is to service cars and to provide consumers with sufficiently good service that the next time they are in the market for a new car, they will purchase the same brand of vehicle. There is nothing more

important than enhancing the customer's experience with a vehicle and that is why the companies should be adding dealers, not extinguishing them, particularly in states where imports are outselling domestics. But, we have heard that the Task Force directed the companies to drop dealers and we can only surmise that the management of both companies, in an effort to save their own necks, went along and decided that the bankruptcy process could be hijacked to accomplish this goal.

Chrysler and GM have conceded that they need dealers in many locations where dealerships are closed, or in GM's case, slated to close. Both have taken steps to award closed or closing franchises to other local dealers. It is appropriate for this Subcommittee to find out whether the White House Auto Task Force intended, as part of a restructuring of Chrysler and GM under the bankruptcy process, to interfere with local profitable distribution points and to pick winners and losers. It is necessary for the Subcommittee to ascertain what the basis was for the selection of dealers for closure and wind-downs using the cover of the bankruptcy code.

### **The Big Lie**

Congress, the White House, and the American people have been misled by GM and Chrysler. Dealer terminations will be counterproductive. GM and Chrysler vastly exaggerated possible savings and underestimated the adverse impact of closing dealerships and ceding market share.

It is time to end the "Big Lie" perpetrated by GM and Chrysler. Dealers are not an economic liability for an auto manufacturer. Dealers are the robust economic engine that permit auto manufacturers to sell their products and consumers to receive quality service and parts at convenient locations. Dealers are the backbone of product support at the local level, with 1.1 million employees and \$234 billion invested.

Let me share with you examples of misleading statements made by GM and Chrysler.

In a document provided by GM to the House Energy and Commerce Committee last month, the company stated that terminating a couple thousand dealers will "allow GM to systematically reduce virtually all direct dealer support programs, which cost GM approximately \$2.1 billion, or \$928,000 per "rooftop" or dealership.

This is a highly inflated figure not borne out by the facts. The savings cited by GM are all related to the sale of a car. If GM does not sell the car to a dealer, and the dealer does not sell that car to a consumer, GM does not make an incentive payment to a dealer. It is a distortion to cite \$2.1 billion in potential savings since these are payments that are not tied to the number of dealers, but are related to the number of cars sold.

For example, it is not true that GM will save:

\$380 million because there will be fewer dealers collecting incentive payments. Eliminating any specific dealer will not eliminate GM's incentive expenses because the cost of the incentives follows the sale of the car - regardless who sells it.

\$350 million from reductions associated with prepping cars. Dealers must inspect new cars to ensure that a GM vehicle is safe to drive. Is GM suggesting that it will choose not to inspect vehicles?

\$120 million through reductions in filling gas tanks. GM reimburses the dealer for providing the purchaser of a new GM car or truck a full tank of gas at delivery. The only way GM can eliminate this expense is to not fill the tank or not to sell a car; it is unrelated to the number of dealers.

Another misleading statement by both GM and Chrysler in testimony to the Energy and Commerce Committee is their claim that dealers cost their companies money.

The truth is that dealers invest significantly in their businesses in the form of land and facilities, inventory and working capital. Dealers are sources of revenue, not cost centers, for manufacturers. At a minimum of \$40,000 per year per franchise, the manufacturer makes money from the dealer over and above any revenue from the sale of cars, parts and services. Without choice, dealers pay thousands of dollars annually to the manufacturers for parts manuals, service mailers, special tools, websites and computers, tech training, tow programs, and promotional kits. Closing dealerships does not materially reduce manufacturers' costs and will materially lessen Detroit's chances of success in the future.

As one notable industry analyst stated recently, "Far from being a burden to the manufacturer it represents, the automobile dealer supports the manufacturer's efforts by providing a vast distribution channel that allows for the efficient flow of the manufacturer's products at virtually no cost to the manufacturer." (Casasa Shapiro Group report, "The Franchised Automobile Dealer: The Automakers' Lifeline," 11/08).

As indicated by the numerous messages from customers I've received since Chrysler announced it intended to reject my dealerships, customers appear to be more loyal to the dealership than the brand. As Chrysler and GM extensively reduce their number of dealers, making it more difficult and less convenient for current customers to get service, they decrease the likelihood that customers will remain loyal to a Detroit brand. This is particularly the case in Montgomery County, Maryland, where Chrysler has proposed to reject each of my longstanding Dodge and Chrysler-Jeep dealerships, as well as other Dodge and Jeep dealerships, leaving the Chrysler-Jeep-Dodge franchise represented by only two dealerships owned by the same principal in a service area with a population of nearly 1.4 million people.

Most assuredly, GM and Chrysler will fail if a significant number of the 150 million current owners of their vehicles don't continue to do business with them. GM and Chrysler assert that with fewer dealers, each dealership will be more profitable, presumably because of the reduced price competition and resulting higher sales prices. Will consumers remain loyal to these brands then? Most likely the dealer termination plan will put in motion a process that will lead some brands to fail, putting the billions of taxpayer dollars invested in the two companies at great risk. (See map of United States attached)

Another area of statements for the Subcommittee to explore is that several Chrysler dealers have told our Committee that Chrysler was not paying the warranty expenses and incentives payments for sales before the June 9 closing, as authorized by the Bankruptcy court. Further, Chrysler has not, to my knowledge, implemented fully the promised programs to “redistribute” vehicles and parts.

#### **Other Legal Issues Pertaining to the Bankruptcy Cases**

As you examine how the bankruptcy laws have been relied upon for these severe economic dislocations, the Subcommittee should analyze additional legal issues that have arisen.

For example, GM and Chrysler, along with the Task Force, used the bankruptcy laws to eviscerate the long-standing state franchise laws that protect dealers. The Subcommittee needs to know that in an attempt to bring about fairness, every State has enacted legislation concerning new car and truck franchises to protect consumers, jobs, and dealers. Car and truck manufacturers can change the terms of their franchises at any time, simply by sending us letters in the mail. The Federal Trade Commission has not historically regulated franchises of automobile and truck manufacturers, making state law the only area of regulation. Accordingly, it is critical that GM and Chrysler should not be permitted to avoid state regulations in their termination and wind-down decisions. Surely, the Bankruptcy Code was not intended to eliminate the only kind of protection that consumers and dealers have in our industry.

Another abusive use of the bankruptcy process is that GM and Chrysler are leaving their dealers out to dry regarding product liability. Our insurance companies had certain expectations as to the way liability for GM and Chrysler products would be handled, and the bankruptcy process has confused the matter for dealers and consumers and may result in fewer protections all around.

#### **Conclusion**

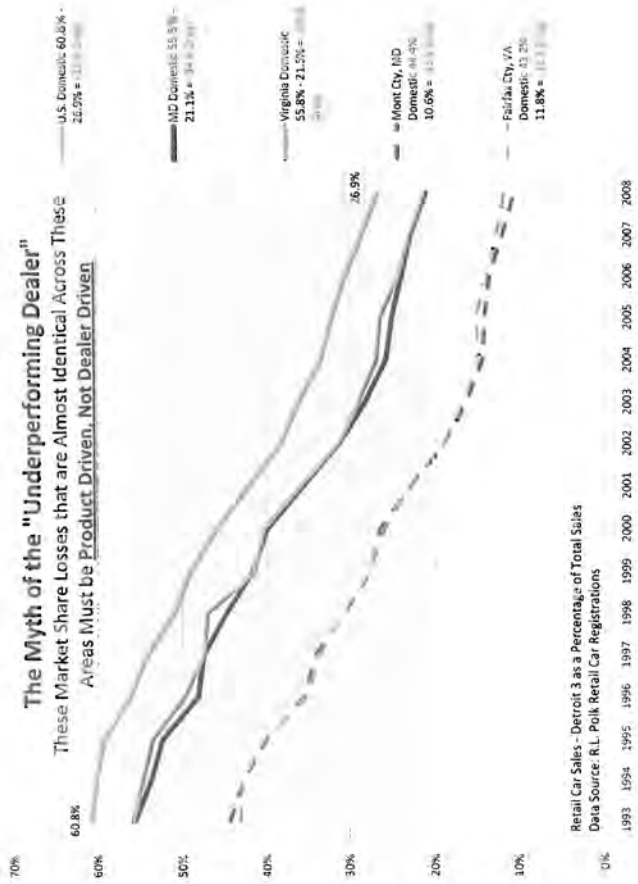
Thank you, again, for having this important hearing today and thank you for allowing me to testify on behalf of the thousands of terminated dealers who could not be here. Livelihoods and economic progress depend on our policymakers making the right decisions during this difficult time. I am hopeful that I have succeeded through this testimony in conveying sufficient information for you to have reasonable doubt as to the appropriateness of the dealership terminations that I and many other dealers are facing as you hold this important hearing. I urge Congress to enact the Automobile Dealer Economic Rights Restoration Act or the LaTourette Amendment, so that we can get back to doing what we do best, selling cars and generating economic and social benefits in thousands of communities from coast to coast.

ATTACHMENT

Facts The Task Force Didn't Consider?

Source: NADA DATA from AutoExec - May 2008. Chrysler Dealer Closure List, GM Dealer Closing - Wash Post  
 \* Includes Estimated 2009 Domestic Import Dealer Closures (U.S.) - Source: Paul Taylor NADA

STATE	TOTAL New Car Dealerships	Exclusive Import Dealerships	Exclusive Domestic and Import Dealers *	Chrysler Closures	GM Announced Closures	GM Filioiped Closures	TOTAL Closures	Remaining Domestic Import Dealers *	Percent Reduction DS	TOTAL Dealership Employment	Estimated Job Loss From Chrysler and GM Dealer Closures
Alabama	207	74	133	8	17	18	43	152	21.3%	8,911	1,766
Alaska	27	13	14	0	0	0	0	13	48.1%	317	154
Arizona	327	132	195	20	44	40	104	270	30.9%	31,562	5,012
Arkansas	369	77	292	22	86	44	152	186	38.5%	16,777	3,700
California	1,238	69	1,169	17	28	28	73	1,135	30.4%	110,083	33,998
Colorado	700	158	542	38	37	30	105	448	23.8%	38,452	7,843
Connecticut	482	101	381	18	39	38	95	342	33.1%	18,710	4,290
Delaware	484	120	364	27	14	14	55	318	14.9%	21,738	2,396
District of Columbia	182	40	142	4	16	15	35	97	38.5%	4,224	1,154
Florida	713	45	668	8	21	20	49	119	16.8%	6,603	1,527
Georgia	395	18	377	8	9	8	25	360	20.4%	3,138	852
Hawaii	305	208	97	47	78	78	203	485	20.6%	41,184	8,661
Idaho	299	29	270	12	17	16	45	178	20.0%	20,035	3,042
Illinois	1,117	78	1,039	7	16	15	38	861	30.2%	115,110	1,452
Indiana	619	50	569	17	25	24	66	533	55.6%	42,253	3,447
Iowa	391	129	262	13	50	49	112	329	24.8%	21,482	4,185
Kansas	203	21	182	3	8	8	19	174	34.3%	2,450	368
Kentucky	377	14	363	6	17	16	39	338	28.9%	19,221	3,887
Louisiana	327	118	209	16	10	10	36	183	18.3%	18,188	1,625
Maine	144	52	92	4	14	14	32	57	15.4%	5,339	1,168
Maryland	242	92	150	8	38	37	83	88	33.8%	8,438	3,148
Massachusetts	146	57	89	3	10	10	23	66	27.3%	7,448	1,201
Michigan	1,111	404	707	54	88	87	229	626	36.5%	51,084	10,158
Minnesota	269	130	139	11	24	23	58	132	30.0%	18,888	2,879
Mississippi	429	161	268	14	38	38	90	195	28.3%	22,290	3,887
Missouri	1,348	466	882	57	55	53	165	897	19.8%	87,480	10,341
Montana	144	11	133	0	0	0	0	11	7.6%	1,111	134
Nebraska	295	143	152	0	11	11	22	78	25.8%	29,184	3,244
Nevada	284	131	153	13	15	14	42	111	27.8%	17,040	2,949
New Hampshire	85	32	53	2	2	2	6	29	21.0%	4,500	495
New Jersey	348	48	300	3	3	3	9	102	28.2%	19,784	4,244
New Mexico	620	242	378	13	24	23	60	301	18.7%	33,768	3,368
New York	1,118	59	1,059	3	3	3	11	48	15.5%	18,074	1,013
North Carolina	488	76	412	6	8	8	18	23	19.0%	7,588	1,417
North Dakota	1,112	884	228	22	80	58	160	502	22.5%	48,529	8,420
Ohio	652	272	380	14	36	35	85	358	20.0%	32,524	3,583
Oklahoma	374	129	245	9	21	20	50	85	34.7%	13,074	2,884
Oregon	161	61	100	10	8	8	26	71	23.4%	6,323	1,235
Pennsylvania	671	86	585	2	3	3	8	43	29.1%	8,873	514
Rhode Island	301	244	57	25	29	29	73	241	24.0%	33,000	4,560
South Carolina	327	118	209	16	10	10	36	183	18.3%	18,188	1,625
South Dakota	144	11	133	0	0	0	0	11	7.6%	1,111	134
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Vermont	144	52	92	4	14	14	32	57	15.4%	5,339	1,168
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Wyoming	203	21	182	3	8	8	19	174	34.3%	2,450	368
<b>71.7 - 88.4 % DS U.S.</b>	<b>5,757</b>	<b>1,438</b>	<b>4,319</b>	<b>282</b>	<b>487</b>	<b>478</b>	<b>1,247</b>	<b>3,088</b>	<b>28.8%</b>	<b>178,737</b>	<b>50,401</b>
Alabama	349	139	210	12	33	32	77	140	35.4%	18,580	3,688
Alaska	38	19	19	0	0	0	0	19	30.0%	2,288	51
Arizona	173	44	129	3	6	6	15	60	11.7%	7,711	892
Arkansas	324	307	17	44	88	64	174	458	27.9%	43,884	7,600
California	268	100	168	9	23	22	54	130	28.7%	13,111	2,788
Colorado	327	118	209	16	10	10	36	183	18.3%	18,188	1,625
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<b>84.4 - 72.7% DS U.S.</b>	<b>5,854</b>	<b>2,112</b>	<b>3,742</b>	<b>227</b>	<b>401</b>	<b>387</b>	<b>1,015</b>	<b>3,728</b>	<b>37.1%</b>	<b>298,911</b>	<b>49,424</b>
Alabama	295	143	152	0	11	11	22				



**It acts the Jack Force didn't consider?**

# Fact – Nearly two-thirds of U.S. Parc are GM, Ford, or Chrysler Models

Therefore, at least two-thirds of all dealers should be domestic dealers. But, with the proposed cuts, there will be more import than domestic dealers and Chrysler and GM may not "rise again", they may fall.

The proposed dealer cuts in the "red" states will severely inconvenience customers (up to 86% of the cars on the road there) and open the door for imports to move into the abandoned locations.

The proposed dealer cuts in the "blue" states will inconvenience customers and make it all but impossible for domestic car sales to "rise again" there.

**Domestic Share of Lt. Vehicles in Operation**  
 Today, where there are more domestic dealers, there are more domestic autos, where more import dealers, more import sales.

**Domestic VIO Share**  
 73.7 to 86.1 (16)  
 64.5 to 73.7 (13)  
 55.1 to 64.5 (13)  
 40.2 to 55.1 (9)

**VIO = Vehicles In Operation**

**Most import new car sales and import cars on the road are in the "blue" states where there are already more import than domestic dealers.**

The good news is that even in the "blue" states, 40 to 64% of the cars on the road are domestic brand. They are the best prospects for new domestic cars.

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 R.L. Pook provided this information to me at no charge. I assume they want to help the government make better decisions. All boxed commenting by Jack Fitzgerald - jpf@fzmail.com

Page 1



**2007 MODEL YEAR  
CARAVAN SE**

**DOODGE**

MSRP: \$14,999  
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 MSRP: \$100,999

For more information visit: [www.dodge.com](http://www.dodge.com)  
 or call 1-800-4ADODGE

**DaimlerChrysler  
Motors Company LLC**

15-SPK Wheel Covers  
 210701-LSM AF Season Tire  
 Compact Spare Tire  
**OPTIONAL EQUIPMENT**  
 Customer Preferred Package IZE  
 Front and Rear Floor Mats  
 AM/FM Stereo Radio with Cassette and CD Player  
 8 Speakers  
 16-Valve Power Top  
 16-VALVE POWER TOP  
**EXTRAS**  
 \$150  
 \$50  
 \$175

**TOTAL PRICE: \$19,875**

MSRP. Excludes tax, title, license, dealer fees, and optional equipment. Dealer sets actual price. MSRP. Excludes tax, title, license, dealer fees, and optional equipment. Dealer sets actual price. MSRP. Excludes tax, title, license, dealer fees, and optional equipment. Dealer sets actual price.

15-SPK Wheel Covers  
 210701-LSM AF Season Tire  
 Compact Spare Tire  
**OPTIONAL EQUIPMENT**  
 Customer Preferred Package IZE  
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 AM/FM Stereo Radio with Cassette and CD Player  
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City MPG 20 Highway MPG 26

Fuel Mileage Information

Actual mileage may vary. City 20, Highway 26, Combined 23. Fuel economy limited by load and distribution. Always use proper tie-down technique. Always use proper tie-down technique. Always use proper tie-down technique.

City 20 Highway 26 Combined 23

Actual mileage may vary. City 20, Highway 26, Combined 23. Fuel economy limited by load and distribution. Always use proper tie-down technique. Always use proper tie-down technique. Always use proper tie-down technique.

FOR THIS VEHICLE:

FROM THIS COUNTRY INFORMATION:

U.S. CANADIAN PARTS CENTER, INC.  
 1000 EAST 10TH AVENUE, SUITE 100  
 DENVER, COLORADO 80202

FOR THIS VEHICLE:

FROM THIS COUNTRY INFORMATION:

U.S. CANADIAN PARTS CENTER, INC.  
 1000 EAST 10TH AVENUE, SUITE 100  
 DENVER, COLORADO 80202







BARS Document Display

Page 1 of 1

2008 COBALT 2-DOOR LT COUPE			GENERAL MOTORS CORPORATION
39U BLUE FLASH METALLIC /L4G			& SUBSIDIARIES
19C EBONY			RENAISSANCE CENTER
ORDER NO. WQWZ/TRE	STOCK NO.		DETROIT MI 48243-1114
VIN 1G1AL18F187234587			VEHICLE INVOICE 1AD19607453
*****13*14322S			
MODEL & FACTORY OPTIONS	MSRP	INV AMT	RETAIL - STOCK
1AL17 COBALT 2-DOOR LT COUPE	14635.00	13930.08	INVOICE 02/05/08
CP5 POWER SUNROOF	750.00	660.00	SHIPPED 02/05/08
L61 2.2L DOHC 4 CYL ENGINE	N/C	N/C	EXP I/T 02/11/08
MH5 5-SPEED MANUAL TRANSMISSION	N/C	N/C	INT COM 02/11/08
NE1 CT/HA/HE/NY/PA/BI/VT EMISSIONS	N/C	N/C	PRC EFF 02/05/08
TV5 PERFORMANCE APPEARANCE PACKAGE	795.00	699.60	KEYS XXXXX XXXXX
*WHEELS, 16" ALUMINUM,			WFP-S QTR OPT-1
MACHINE FACED			BANK: GMAC - 020
(REPLACES STD/OPT WHEELS)			CHG-TO 14-322
*FOG LAMPS			
*CHROME EXHAUST TIP			SHIP WT: 2752
*REAR SPOILER			HP: 18.4
*WHITE FACED GAUGES			GMS: 16865.78
*LEATHER WRAP STEERING WHEEL,			SUPPLER: 17617.99
STEERING WHEEL AUDIO CONTROLS			MEM: 18430.00
UE1 1 YR ONSTAR SAFE & SOUND	N/C	N/C	MEMO 738.50
(ASK DLR ABOUT TURN-BY-TURN			
NAV UPGRADE)			
2LT ZLT TRIM PACKAGE	1295.00	1139.60	
*WHEELS, 16" STYLED STEEL			
(REPLACES STD/OPT WHEELS)			
*1 YEAR ONSTAR SAFE & SOUND			
(ASK DLR ABOUT TURN-BY-TURN			
NAV UPGRADE)			
*ANTILOCK BRAKE SYSTEM			
*CONVENIENCE NET, CARGO			
*CRUISE CONTROL			
*BODY COLOR, BOOYSIDE MOLDINGS			
39U BLUE FLASH METALLIC	295.00	259.60	
TOTAL MODEL & OPTIONS	17770.00	16588.88	ACT 231 16715.78
DESTINATION CHARGE	660.00	660.00	H/B 261 533.10
LAM DEALER CONTRIBUTION		177.70	ADV 261 177.70
LAM GROUP CONTRIBUTION		177.70	EXP 65A 177.70
TOTAL	18430.00	17604.28	PAY 310 17604.28
MEMO: TOTAL LESS HOLDBACK AND			
APPROX WHOLESALE FINANCE CREDIT	16778.48		
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INVOICE DOES NOT REFLECT DEALER'S ULTIMATE COST BECAUSE OF MANUFACTURER			
REBATES, ALLOWANCES, INCENTIVES, HOLDBACK, FINANCE CREDIT AND RETURN TO			
DEALER OF ADVERTISING MONIES, ALL OF WHICH MAY APPLY TO VEHICLE.			
*****			
THIS MOTOR VEHICLE IS SUBJECT TO A SECURITY INTEREST HELD BY GMAC.			
REMIT TO GMAC NO. 020			
VIN 1G1AL18F187234587			
FITZGERALD CHEVROLET-CADILLAC			

Mr. COHEN. Our sixth witness is Mr. Jim Tarbox. He is a native of Rhode Island car dealership owner and operator. As part of the Chrysler bankruptcy and restructuring, he has spent much of his personal time in D.C. representing many independently owned dealerships along with NADA. Born and raised in North Kingstown, Mr. Tarbox studied management and automotive marketing at Northwood University in Michigan. The closing of his two dealerships will have a significant impact on his family and potentially cause his personal bankruptcy as well as that of his business.

Mr. Tarbox we appreciate your coming to testify and will you proceed with your testimony.

**TESTIMONY OF JIM TARBOX, PRESIDENT,  
TARBOX MOTORS, INC.**

Mr. TARBOX. Good morning, Mr. Chairman and Members of the Committee. My name is Jim Tarbox and I am a former Chrysler new car dealer from North Kingstown, Rhode Island. Thank you for the opportunity to testify before you today on legislation that could change the course of my life and the lives of many other dealers across the Nation.

I introduced myself as a former Chrysler dealer because just over a month ago, my two dealerships were taken from me. I was stripped of my right to operate under this car maker. Despite my franchise agreement, I was told there would be no more new cars to sell, no more parts to ship, no more inventory to keep or sales goals to meet and beat. I was told I was closing. I was not given any justification for my selection, and worst of all, I had less than a month to make it happen. All I had worked for, all I built, all I had achieved was gone within a few seconds.

When I read the letter, my first thoughts were not about the property I would lose, the cars still on my lot, or the hundreds of thousands of dollars in machines I had purchased for car repairs. All that came later. My first thought and those that plague me as I sit here today were about my employees, their families, and as you might expect, my family. How do you tell your employees they are headed for the unemployment line and how do you tell your wife that all you worked for may be gone, especially when your success was well known? It is not easy. I am 42 years old. I have a wife, Kim, who is here with me today, and I have three young girls.

If my dealership is not restored, we will lose everything, including college savings for my children and my home. I am at a loss as to how a small business person like me found myself in this position. If it weren't for some damaging testimony at the Chrysler bankruptcy hearing, I might have never known. During that hearing, a witness had read out loud some e-mail exchanges. Chrysler executives said in an e-mail discussing closures that I was a belligerent and combative dealer. Why would they say this? They said this because I opposed, and was able to stop, the allowance of another Jeep dealership within miles of my facility. I knew after hearing this that Chrysler targeted me for closure.

To give you some background, due to my success with Chrysler, they urged me to purchase another dealership in neighboring Massachusetts in 2007. They made promises of getting me Dodge and were negotiating site control. Once I closed, they attempted to use their promises as leverage. They tried to put another Jeep franchise in my market in Rhode Island. I protested under State franchise laws. They withdrew their intent and went bankrupt. They chose to reject both my dealerships because of the protest. This protest put me in their line of fire for closure. Chrysler executives wrote in the e-mail, This is going to be a tough one. His dealerships are performing fine with good score cards. And the reply was from Phil Scroggins, the northeast business center director: "He is a belligerent, combative dealer to litigates and protests any new

Jeep franchise in Providence, Rhode Island. Management made decision to cut him. He has not operated in good faith.”

There is no criteria, no data-driven criteria here. This e-mail makes it quite evident that the selection process was arbitrary, unfair, and inappropriate. I was targeted. I am sure many others were randomly selected as well. Everything I have worked for, all my success, my businesses, and my rights gone in seconds and, even worse, given to the competitor up the road. And despite their claim I was closed because I was a stand-alone Jeep dealer. Forty-four stand-alone Jeep dealers and more than 100 stand-alone Dodge dealers remain in business. There is no criteria and I would request that Congress look closely at this issue and work to save our businesses, restore them, and restore our rights.

My family has been in the car business for three generations. My dealership was founded in 1935. And as in the case with many dealers, my family name Tarbox is well known and respected in my home State and beyond. This is the industry I grew up in, the industry I know, and the industry I love. I am proud to say I helped build a well-regarded and high-performing Jeep dealership in Rhode Island. I was one of the highest volume Jeep dealers in the northeast. I have maintained a volume of 450 percent planning potential. I have sold 750 new Jeeps a year, and I am in the top 10 percent nationally with Chrysler. My dealership exceeded sales goals and performed above and beyond any expectation set by Chrysler. They have indicated that they value high-performance top-notch employees and those dedicated to aggressive marketing their product. Including the millions I have spent branding Tarbox with Jeep, we are on top in all categories. But Chrysler is refusing to release their specific criteria. It certainly begs the question, if not for performance, what was the criteria for closure?

In fact, it seems closure was decided based on personality and relationships, not performance. This is not fair and sound business practice. This is not in the best interest of the taxpayer, who suddenly has a stake. This company is playing with our lives.

As you have seen likely right in your districts, there are dealers or should I say former dealers suffering. These closures may result in the bankruptcy of many productive small businesses, foreclosures of their homes and filling up the unemployment rolls when our country is experiencing the highest unemployment rate in decades. In fact, my State boasts the second highest rate in the Nation at 12.4 percent. My employee count alone has dwindled from 60 to 15. In my case, my businesses will go bankrupt and I may have to go personally bankrupt as well. There is no fallback plan. This dealership was my plan. It is my livelihood.

As dealers, our property rights have been violated. Our contractual rights have been violated. And our faith and trust in the system of good business practice have been violated. We have invested in everything and they are leaving us with nothing. As entrepreneurs, as successful business operators, as employers, and as Americans, we deserve to retain our rights and protections.

I ask you on behalf of dealers across the country and our communities to support this legislation, support the restoration of our dealerships and our rights. Thank you.

Mr. COHEN. Thank you for your testimony, Mr. Tarbox.

[The prepared statement of Mr. Tarbox follows:]

PREPARED STATEMENT OF JIM TARBOX

Good morning, Mr. Chairman and esteemed members of the committee.

My name is Jim Tarbox and I am a former Chrysler new car dealer from North Kingstown, Rhode Island. I thank you for the opportunity to testify before you here today on legislation that could change the course of my life and the lives of many other dealers across the nation.

I introduced myself as a former Chrysler dealer because, just over a month ago, my two dealerships were taken from me. I was stripped of my right to operate under this carmaker. Despite my franchise agreement, I was told there would be no more new cars to sell. No more parts to ship. No more inventory to keep, or sales goals to meet and beat.

I was told I was closing. I was not given any justification for my selection and best of all, I had less than a month to make it happen.

All I worked for. All I had built. All I had achieved was gone within the few seconds it took me to open a letter from the Chrysler home office.

When I read this letter my first thoughts were not about the property I would lose, the cars still on my lot or the hundreds of thousands in machines I had purchased for car repairs . . . all that came later. My first thoughts, and those that plague me as I sit here today, were about my employees, their families and as you might expect, my family.

How do you tell your employees they're headed for the unemployment line? And how do you tell your wife all you've worked for may be gone? Especially when your success was well-known?

I'll tell you: It's not easy.

I am 42 years old and my wife, Kim—who is here with me today—and I have three young girls.

If my dealership is not restored, we will lose everything—including college savings for my children and my home.

I am at a loss as to how a small businessperson like me found himself in this position. If it weren't for some damaging testimony at the Chrysler bankruptcy hearing, we might never know. But, during that hearing, a witness had to read out loud some e-mail exchanges. . . .

Chrysler executives said in an e-mail discussing closures that I was a "belligerent" and "combative dealer."

Why would they say this?

They said this because I opposed, and was able to stop, the allowance of another Jeep dealership within miles of my facility.

I knew after seeing this, that Chrysler targeted me for closure.

To give you some background: due to my success, Chrysler had urged me to purchase a dealership in neighboring Mass. They made promises of getting me Dodge and were negotiating site control.

Once I closed, they attempted to use their promises as leverage. They tried to put another Jeep franchise in my market in RI.

I protested under state franchise laws. They withdrew their intent and went bankrupt.

They chose to reject BOTH my dealerships because of the protest.

This protest put me in their line of fire for closure.

Chrysler executives wrote in the e-mail: "This is going to be a tough one—His dealerships are performing fine with good scorecards."

And the reply from Phil Scroggins—the northeast business center director? "He's a belligerent, combative dealer who litigates & protests any new Jeep franchise in the Providence, RI area . . . Management made decision to cut him—He has not operated in good faith."

There is NO data driven criteria here.

This e-mail makes it quite evident that the selection process was arbitrary. It is arbitrary, unfair and inappropriate. I was targeted and I am sure many others were randomly selected as well.

Everything I have worked for, all my success, my businesses and my rights—gone in seconds. And even worse—given to my competitors on a silver platter.

And despite their claim I was closed because I was a stand alone Jeep dealer, 44 stand alone Jeep dealers and more than 100 stand alone Chrysler dealers remain in business. There was no criteria and I request that Congress look closely at this issue and work to save our businesses. Restore them and restore our rights.

My family has been in the car business for three generations. My dealership was founded in 1935. And, as is the case with many dealers, my family name, Tarbox, is well-known and respected in my home state and beyond.

This is the industry I grew up in, the industry I know and the industry I love. I am proud to say, I helped build a well-regarded and high-performing Jeep dealership in Rhode Island. We:

- Are one of the highest volume Jeep dealers in the northeast
- Have maintained a sales volume at 450 percent of planning potential
- Have sold over 750 new jeeps a year
- and, are in the top 10 percent nationally with Chrysler

My dealership has exceeded sales goals and performed above and beyond any expectations set by Chrysler.

They have indicated they value high performance, top-notch employees and those dedicated to aggressively marketing their product. Including the millions I have spent branding Tarbox with Jeep, we are top in all categories. But Chrysler is refusing to release their specific criteria.

It certainly begs the question, if not for performance, what was the criteria for closure?

In fact, it seems closure was decided based on personality and relationships, not performance. This is not a fair or sound business practice. This is not in the best interest of the taxpayer who suddenly has a stake. And this company is playing with our lives.

As you have seen, likely right in your districts, there are dealers—or I should say former dealers—suffering. Sure there are those dealers who own dozens of dealerships or more and maybe these closures, although having an impact, will not put them out of business.

But let me be clear in saying, for small dealers with one or two dealerships—the dealers I represent here today—this action by Chrysler and the Task Force will produce grave consequences.

These closures may result in the bankruptcy of many productive small businesses, foreclosures of their homes, and filling of the unemployment rolls when our country is experiencing the highest unemployment rate in decades. In my state in fact, we boast the second highest rate in the nation at 12.4 percent.

My employee count alone has dwindled from 60 to 15.

In my case, my businesses will go bankrupt and I may have to go bankrupt personally as well. There is no fall back plan—this dealership was my plan. It is my livelihood.

As dealers, our property rights have been violated. Our contractual rights have been violated. And our faith and trust in the system of good business practice and good faith have been violated.

We have invested in everything and they are leaving us with nothing: not even answers to back up their closures.

As entrepreneurs. As successful business operators. As employers. And as Americans. We deserve to retain our protections. And I ask you, on behalf of dealers across the country, and our communities, to support this legislation. Support the restoration of our dealerships and our rights. It WILL change the lives of so many.

Thank you.

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Mr. COHEN. Our seventh witness is Gregory Williams. Mr. Williams is the former President of Huntington Chevrolet located in Huntington Station, New York. A veteran of the automotive business industry for more than 30 years, he has appeared on the Black Enterprise list every year since 1979. A founding member of both General Motors Minority Dealers Association and the General Motors Minority Dealer Advisory Council, elected two times chairman of the Minority Dealer Advisory Council and held board seats with both organizations and was recently a board member of the National Association of Minority Automobile Dealers and the GM Northeast and GMC central dealer councils.

Mr. Williams, will you proceed with your testimony.

**TESTIMONY OF GREG WILLIAMS, PRESIDENT,  
HUNTINGTON CHEVROLET, INC.**

Mr. WILLIAMS. Thank you, Mr. Chairman. I would like to thank the Chairman and the Members of the Committee for inviting me here to speak. My name is Gregory Williams, and I have worked for over 30 years as a dedicated and faithful GM dealer. I am a former dealer at Huntington Chevrolet. While I am here today representing the numerous minority GM and Chrysler terminated and rejected dealers, I would like to share my personal and tragic story with you regarding the disparate treatment that I suffered at the hands of GM and GMAC.

In 1999, GM asked me to go to Long Island and investigate the purchase of Huntington Chevrolet. After performing due diligence on the store, I told GM that the potential was there but the location was wrong and the facility was too outdated. GM informed me that they would take care of these problems and find a new location and build a new facility. Based on these assurances, I purchased the dealership, paying the former dealer \$1.3 million in goodwill. I put in \$500,000 of my own and the remaining \$2.75 million went into investment with Motors Holding Division of General Motors. From the date of the purchase to 2005, the dealership was profitable. All the profits went toward paying dividends and purchasing stock from General Motors. During this period, over \$1.5 million was paid to them. At the same time, we were still looking to relocate the dealership.

In 2003, as a result of hard work and the dealership's performance, I was presented with GM's most prestigious award, the GM Dealer of the Year. This award is presented annually to the top 100 performing dealers out of 7,000 dealers nationwide. It is one of the accomplishments that I am most proud of. In 2005, I, along with most of the Motors Holding dealers were asked if we would consider an early buyout from Motors Holding. GM needed to raise additional capital at this time. I was informed by Motors Holding that I owed \$1.9 million to buy them out and that they had spoken to GMAC and that GMAC would take care of making the loans with us. I contacted GMAC and got approval for loan but was told by Motors Holding that I could not buy them out for \$1.9 million because they would miss the dividends that I had been paying. So they told me I would have to pay \$2.5 million to buy the store out. In effect, GM got a \$600,000 goodwill from me when I bought them out of my store.

During the financing process, I was told by GMAC that I had to personally guarantee the loan and also personally guarantee the floor plan line of credit. This had never been asked of me before and, you know, I went with it. GM gave me a note of \$20,000 a month and increased my expenses by that much.

The dealership struggled over the next few years as GM lost market share year after year. We made a little and we lost a little, but we were profitable for most of the time. And through the month—through the year of 2008 we were profitable until October when the bottom fell out. It was, at this time, stated that both GM and GMAC stated that they would need bailout money to survive and GM was openly questioning whether they would make it to December without the immediate infusion of cash. Needless to say,



business was terrible. At the end of November I received a notice from GMAC that stated that I did not have enough cash in the business largely due to the drastic drop in business at the end of 2008. They stated that I must infuse \$1.5 million into the business or lose my floor plan loan with them.

On May 17, I received a letter from GM stating that my location would be closed and I would not be moving forward as a GM dealer. It should be noted that there are 19 Chevrolet dealers on the Long Island metro New York City area and for the year 2008 my dealership was number three in retail sales and number one in customer satisfaction. On May 24 GMAC notified me that I no longer qualified for a floor plan loan with them because I was not able to invest \$1.5 million in additional capital.

Feeling that I had no options, I sent a voluntary termination letter to General Motors on May 25 because based on voluntary termination with the New York State franchise law, GM would be required to repurchase my inventory and the parts. That would have amounted to approximately \$6.6 million. GMAC would have gotten that \$6.6 million and the only thing I would have to negotiate with them on is what was left on my loan to pay off General Motors. GMAC gave me 90 days to find another floor plan and to comply with a number of unreasonable demands, including signing a confession of judgment for \$8.1 million. This confession of judgment was basically the total of my inventory along with the \$1.4 million that I still had left of the loan that I paid General Motors. These demands were both unreasonable and impossible and GMAC's demand that I find a floor plan in 90 days was equally impossible.

On June 1 when GM filed for bankruptcy, I was advised that they also decided not to honor my voluntary termination letter. GM ultimately determined in 2005 when I was buying them out that the dealership was worth well over \$2.5 million in addition to the \$1.5 million that I had already paid. Now they have unilaterally determined that the dealership is worthless, making it impossible to sell or repay this massive debt. On June 2, I received GM's wind-down agreement. The agreement provided a deadline date of June 11 to sign the agreement or be rejected in the bankruptcy proceeding. I reluctantly signed the agreement, although I strongly objected to the terms of the agreement and felt enormous pressure to sign it knowing that if I did not, I would lose the right to receive the proposed wind-down payment, which is the only form of financial support that I was to receive from GM.

It should be noted that the debt I owed to GM and GMAC far exceeded the amount of the proposed wind-down payment, and yet I am being held personally liable of the entire debt because of the personal guarantees.

Huntington Chevrolet was my only dealership. I have no other source of income as I used most of my life savings to reinvest in the dealership. I have no health insurance. I had to lay off all my employees and walk away from a business that I owned for 11 years and an industry that I have had for over 30 years—that I had been in for over 30 years. All of this occurred while I was still paying for the loan to buy out General Motors. I now owe \$1.4 million, and without the dealership, I have no way to pay it.

The only people who made money off my dealership was GM and GMAC. GM received all of its investment that they had in the dealership including a healthy profit, a minimum of 15 percent dividends plus \$600,000 goodwill at their buyout. GMAC also made millions of dollars on my inventory floor plan over the 11 years that I owned and operated the dealership. GMAC has now confiscated my entire inventory of vehicles along with all the parts and company assets and they have said that they will liquidate the inventory, parts, and assets, and will come after me personally for any shortfall since I signed the personal guarantee for the inventory and the loan.

Mr. COHEN. Mr. Williams, if you could start to wrap up, we are a little bit—2, 2½ minutes over.

Mr. WILLIAMS. Okay. I will go to the final page here.

We need your help not only to walk away from this tremendous debt that we have acquired while attempting to play by the rules, but to leave with financial stability to restart our lives all over again. At 60 years old, I am forced to face the reality that my employment future is limited. I was always of the opinion that my investment was my retirement and that when I decided to retire, I would sell my business and live off the proceeds. I had no idea that at this stage of my life, GM and GMAC would wreck my world as I knew it.

Thank you for the opportunity to share my personal story with you today. I plead for this Committee and all the Members of Congress who are listening to my testimony to please help us. We need your help to ensure that the auto manufacturers are required to treat us fairly and equitably as we watch our lives disappear without fairness, transparency, or due process of law. Thank you.

Mr. COHEN. Thank you, Mr. Williams.

[The prepared statement of Mr. Williams follows:]

**Testimony of Gregory Williams**

**President of Huntington Chevrolet, Huntington Station, NY**

**House Judiciary Subcommittee on Commercial and  
Administrative Law**

**Hearing: "Ramifications of Auto Industry Bankruptcies - Part III"**

**Wednesday, July 22, 2009**

**10:00 a.m. ET**

Testimony of Gregory Williams

Thank you Chairman Conyers and the members of the Committee.

My name is Gregory Williams and I have worked for over 30 year as a dedicated and faithful GM dealer. I am the former owner of Huntington Chevrolet in Huntington Station, New York.

While I am here today representing the numerous minority GM and Chrysler terminated and rejected dealers, I would like to share my personal and tragic story with you regarding the disparate treatment that I suffered at the hands of GM and GMAC

In 1999, I was asked by General Motors to come to Long Island, New York to investigate the purchase of Huntington Chevrolet. After doing due diligence on the store, I explained to the GM Regional General Manager, that the store had potential, but was located in the wrong area, as the facility was too outdated. The Regional General Manager and Vice President for General Motors informed me that they would take care of these problems and find a new location and assist me to relocate and build a new facility. Based on that assurance, I purchased the dealership after General Motors used its first right of refusal to purchase the dealership. The purchase price was \$3.3 million including goodwill, of which I used \$500,000 of my personal cash and financed the remaining \$2.75 million from the Motors Holding Division of General Motors.

From the date of purchase to 2005, Huntington Chevrolet made money and all profits made went towards paying dividends (15% when the market average 4%) and stock purchases totaling over \$1.5 million to my partner, Motors Holding Division a subsidiary of General Motors. At the same time, we were still looking to relocate the dealership. Also in 2005, I was asked along with other General Motors Minority Dealers to consider an early buy-out from Motors Holding for a total \$2.5 million largely due to the fact that General Motors needed to raise additional capital. I was

offered an early buyout for my dealership. I therefore, applied for a loan from GMAC, a sister company of General Motors.

During the financing process, I was told by GMAC that I had to personally guarantee the amount of the note; as well as the dealership's floor plan line of credit, which historically the floor plan line was collateralized by the vehicles not personally guaranteed. As a result of the buyout loan to GMAC the dealership's expenses increased by \$20,000 per month.

As a result of my hard-work and the dealership's top performance, I was presented with GM's most prestigious award, "Dealer of the Year" by General Motors Corporation in 2003. This award is only presented to the top 100 performing General Motors dealers out of the 7,000 GM dealers nationwide.

At the end of 2008, the economy experienced an unprecedented down-turn, both General Motors and GMAC requested a government bailout. At the same time, I received notice from GMAC that the dealership did not have enough cash largely due to the drastic drop in sales in the auto industry.

On May 17, 2009, I received a letter from General Motors stating that my location would be closed and I would not be moving forward as a General Motors dealer. There are 19 Chevrolet dealers on Long Island and Metro New York City, and for the year 2008, my dealership was #3 in retail sales and #1 in customer satisfaction index.

On May 25, 2009, I sent a "Voluntary Termination Letter" to General Motors via overnight delivery. This was done under extreme pressure from both GM and GMAC. GM had already sent the May 17<sup>th</sup> letter indicating that my dealership would not be allowed to go forward under the new GM. Additionally, GMAC advised me that I no longer qualified for a floor plan loan, and without a cash infusion in the amount of \$1.5 million, they threatened to terminate my floor plan immediately. They provided me with 90 days to find another floor plan loan, if I agreed to the following criteria:

1. A fee of \$32,500 for the 90 day extension, payable up front;
2. A fee of \$750.00 for each inventory audit, to assure that the inventory is on premises, or if sold, is paid for;
3. An \$81,000.00 non-compliance fee, if I'm not able to secure a floor plan loan within the 90 days; and,
4. Sign a "Confession of Judgment" which states that I confess to a judgment of \$8.1 million. (This is a combination of the remainder of the loan that I made to pay-off GM Motors Holding and the value of the entire vehicle inventory).

Requiring the aforementioned demands to maintain my floor-plan for 90 days was both unreasonable and impossible. GMAC's further demand that I find another financial institution to provide my dealership floor plan in 90 days, in today's economic and financial crisis is equally impossible.

On June 1, 2009, when GM filed for bankruptcy I was advised that they also decided not to honor my "Voluntary Termination Letter". Pursuant to state franchise law, GM would have been obligated to repurchase the inventory and parts. I had approximately \$5.8 million in new vehicle inventory and \$800,000 in parts that would have been repurchased by GM. I would have used this money to repay the cost of the vehicle inventory to GMAC.

GM unilaterally determined in 2005 (when we were in the buy-out process) that the dealership was worth well over \$2.5 million in addition to the \$1.5 million that I already paid. Now they have unilaterally determined that the dealership is worthless, making it impossible to sell or to repay this massive debt.

On June 2, 2009, I received a copy of the General Motors "wind-down" agreement. The agreement spelled out the new terms and provided a deadline date of June 11<sup>th</sup> to either sign or be rejected in the GM bankruptcy proceeding. On Thursday, June 11<sup>th</sup>, I reluctantly signed the agreement on behalf of my company, and returned it to General Motors. Although I strongly

objected to the terms in the agreement, I felt enormous pressure to sign, knowing that if I did not, I would have lost the right to receive the wind-down payment, based on GM's bankruptcy, which is the only form of payment that I was to receive. The debt I owed to GM and GMAC far exceeded the amount of the wind-down agreement, but yet I am being held personally liable because of the personal guarantee.

Huntington Chevrolet was my only dealership. I have no other sources of income as I used most of my life savings to reinvested into the dealership, no health insurance, I had to layoff my employees and walk away from a business that I owned for over 11 years, and an industry that I've been in for over 30 years.

All of this occurred while I was still paying for the loan to buy out Motors Holding Division. I now owe them \$1.4 million, which without the dealership, I have no way to pay.

The only people who made any money off of my dealership was General Motors (its Motors Holding Division), and its affiliate GMAC. GM received all of its investment that they had in the dealership including a healthy profit (minimum 15% dividends plus the \$600,000.00 "good will" at buy-out.) GMAC received \$20,000.00 per month pursuant to the contract (including interest) and they are now owed a balance of \$1.4 million (which they say that they will come after me personally to collect.) GMAC also made millions of dollars on my inventory floor plan loan over the 11 years I owned and operated the dealership. GMAC has now confiscated my entire inventory of vehicles along with all parts and the company assets. They have said that they will liquidate the inventory, parts and assets and will come after me personally for any shortfall since I signed a personal guarantee for the inventory, and the loan, when I borrowed the money to buy-out Motors Holding Division. GMAC is also asserting the right to the "wind down" payment that that the dealers were coerced to sign.

**I don't understand how this can be fair?**

How can I be left with nothing, when in January of this year, we had a General Motors approved deal to sell the dealership for \$1.5 million "good will", plus the inventory parts and assets. This deal would have gone through, but GMAC insisted that the proposed buyer along with his financial participants, personally guarantee the inventory, when traditionally, the inventory has always been used as the collateral.

Also, what is terribly disturbing is the fact that in 2008, of the 1,000 dealerships that closed, 200 were owned by ethnic minorities. These closures represented a total of 150,000 direct and indirect jobs lost. This year, it is projected that over 3,000 dealerships will close, of which over 300 will be minority owned dealerships who will run out of cash and/or lose their floor plan and be forced to close their doors by year end. These closures could result in an additional 350,000 direct and indirect jobs being lost, which would leave the entire minority owned dealership body to be less than 1,000 dealerships in the United States.

Because of all of the issues/concerns we've mentioned above, I am here today on behalf of not only myself, but the numerous terminated and rejected GM and Chrysler dealers. We are seeking the following immediate remedies:

**Grant Immediate Relief from Personal Guarantees for both Term and Floor Plan Loans:**

The affected dealers have no means to repay these enormous debts, especially since the manufacturers are forcing them to close their dealerships without fair compensation (i.e. inadequate wind-down payments). Pressure must come from the Government to prevent the manufacturers and banks who received TARP funds from enforcing personal guarantees upon the dealers. (Note: Dealers are losing their homes and personal assets as a result of the strict enforcement of the personal guarantees)



**Appoint an Independent Committee or review team to Re-evaluate the Terminated/Rejected Chrysler and GM Dealers:**

The process under which 38 Chrysler and 44 GM minority dealers were terminated and rejected was not fair, transparent or consistent. An independent review committee must be appointed to determine if there is a basis for the continuation of these dealers in their existing dealership locations or the opportunity to be appointed to another dealership location with their auto manufacturer. In cases where dealers cannot be reinstated after being reviewed by the independent review committee, fair and adequate compensation must be provided for these dealers.

**Future Dealership Opportunities for Terminated/Rejected Dealers:**

Reinstatement must be provided to the terminated and rejected dealers if/when the auto manufacturers decide to re-enter the market place. If the terminated and rejected dealers are not reinstated by an independent review committee, each dealer must be granted the ability of first right of refusal in the event the auto manufacturer decides to retain or re-open a dealership in their market area. The auto manufacturers must be required to memorialize this commitment in writing and provide it to Congress so that this process can be monitored appropriately.

**Reinstate the Enforcement of State Franchise Laws:**

The automotive manufacturers must be required to adhere to each states franchise laws and adequately compensate the Chrysler and General Motors rejected and terminated dealers accordingly to the rights and provisions set forth in their respective state franchise agreements.

**We need your help to not only walk away from this tremendous debt that we have acquired while attempting to play by the rules,**

but to leave with the financial stability to restart our lives all over again. At 60 years old, I am forced to face the reality that my employment future is limited. I was always of the opinion, that my investment was my retirement, and that when I decided to retire, that I would sell my business and live off of the proceeds. I had no idea that at this stage of my life that General Motors and GMAC would wreck my world, as I know it.

Thank you for the opportunity to share my personal story with you today. I plead for this committee and all the members of Congress who are listening to my testimony to please help us.

We need your help to ensure that the auto manufacturers are required to treat us fairly and equitably as we watch our lives disappear without fairness, transparency or due process of the law.

**Gregory M. Williams**  
President  
Huntington Chevrolet, Inc.

Mr. COHEN. Our final witness will be Mr. Knapp, and he will be introduced by agreement with the lead Member here on the minority side by our distinguished Member from Houston, Texas, Ms. Sheila Jackson Lee. Ms. Jackson Lee, a Member of this Committee but not the Subcommittee, is recognized for the purpose of introduction.

Ms. JACKSON LEE. Let me thank Chairman Cohen and Ranking Member Franks for their courtesies extended, and let me also thank them for allowing me to introduce Mr. Knapp and as well thank them for allowing the National Association of Minority Automobile Dealers to be present here because I believe these are the tragic stories that we need to hear.

Mr. Knapp is symbolic of many Americans, and he is an heir, if you will, of hard work. Some people might say of money. He is of hard work. Born in Harlingen, Texas where he attended Harlingen High School and graduated in 1976. That means he is from the valley, from South Texas, and he is proud of it. He married in 1979 to Debbie Knapp, graduated from Texas A&M University in 1980, and the rest of the State won't hold that against him, with a degree in finance and moved to Houston, Texas, where he immediately went to work for Knapp Chevrolet. And I think it is important to note his grandfather organized and built that company and started it in 1939.

He is a third-generation dealer in the heart of Houston, and he has been active in so many local community activities such as his good friends to his left, I believe, and he too has supported high schools, been active in his church, served as a civic leader, as a board member of the Greater Heights Area Chamber of Commerce, which I remember seeing him as we interacted as community and business and we worked together. He also has his district, has his particular dealership in the heart of the fourth largest city in the Nation, which has been known to be call a "little United Nations." Robert Knapp has reflected that by 43 percent plus of his employees being diverse, representing many families in my constituency. Bob Knapp is in appeal. He is one of the 900 appeals for GM, unlike Chrysler, which was recorded to have one because they have no administrative appeal, they only have bankruptcy. He is only symbolic of the pain, as he told me in my office, of so many who are suffering like him.

So I am hopeful that as he proceeds, he will be able to tell us how urgent it is for us to move forward. He will be able to tell us that the action is necessary now, that GM and Chrysler and the new CEOs that feel good and can be out on their patios or be at the beach right now because they are out of bankruptcy, how they can do this together with the Administration, together with Congress, and I hope that he will tell us how lost dealerships—because that means my community, for 50 miles around, will not have a dealership. My city of Houston will not have a dealership to buy discounted vehicles, how this will impact the competitive nature of our American automobile dealers by these dealerships being cut down or shut down. I would like to say cut down because they are. He will be able to share those thoughts with us.

Mr. Chairman, I am very pleased to introduce a gentleman who is symbolically representative of the true grit of America, raising

himself up by his bootstraps and working hard every day, and this is Robert Knapp of Knapp Chevrolet in Houston, Texas.

**TESTIMONY OF ROBERT G. KNAPP, PRESIDENT,  
KNAPP CHEVROLET**

Mr. KNAPP. Thank you for your kind words.

Mr. Chairman and Members of the Committee, my name is Bobby Knapp, and I am president of Knapp Chevrolet in Houston, Texas. Thank you very much for giving me this opportunity to testify at this hearing. I would also like to take the opportunity to give a special thanks to my congresswoman, the Honorable Sheila Jackson Lee of the 18th District of Texas for her support in facilitating my testimony here today.

The focus of my testimony is GM's decision to terminate Knapp Chevy franchise. The testimony regarding my dealership will relate to circumstances regarding other dealerships throughout the country.

Fact: Knapp Chevrolet sold over 1,000 new units in 2008. Fact: In Houston, the loss of Chevy dealers results in the loss of GM market share. Terminating Knapp will cause GM to lose more Houston market share than it has already lost. I included a graph in my package that kind of highlights this, but let me just go over some numbers.

Our district—at the beginning of 2008 our district in Houston contained 12 dealers. The first 8 months of the year those dealers sold an average of just over 1,200 units a month. At that time three dealers, including two very large ones in Houston, went out of business. The last 3 months of 2008, those dealers that were left sold an average of just over 500 units a month. That trend has continued through 2009. It shows that closing dealerships in our market will reduce market share.

Fact: Looking at the last 12 months including June, Knapp Chevy was operating at a profit in 11 months. The only down month being last September when we were without electrical power for 15 days due to Hurricane Ike. Fact: By terminating Knapp, GM is abandoning areas in and around downtown Houston. GM has documented the growth and potential of this market. I included a map that GM created showing our market share and neighborhood and the increase in households. In our actual neighborhood and not necessarily our whole market area but in our neighborhood, the increase in households is astounding. Why GM would want to abandon this market is beyond me.

Fact: GM is forcing us to take an agreement that essentially gives all rights to GM and all obligations to Knapp. Fact: GM references termination assistance as part of the wind-down process, but this proposal does not cover Knapp's losses associated with the forced closing. What GM is offering will not satisfy our third-party contractual obligations which total over 600,000 from things like computers and phone systems and other things. Although the termination process would not be complete until October 2010, GM is strangling our business by preventing us from ordering new vehicles thus eliminating one of our primary income strains.

Fact: At the time we received notice that GM would not renew our franchise agreement, we had over 40 sold orders on order in-

cluding a number of ambulances for the City of Houston. At that time, we were told by GM that these orders would not be honored.

Fact: Knapp moved into its facility December 6, 1941, 1 day before the bombing of Pearl Harbor and over the past 10 years, we have invested 3.75 million in these historic facilities and equipment upgrades.

Fact: The estimated job loss in the State of Texas with these proposed closed dealerships is over 10,000. Eighty-two of these hard-working people are Knapp employees whom we consider family. We offer substantially better benefit packages than others in the industry and our average employee tenure is 7 years with many employees having been with us for over 10 years. All will lose their jobs and livelihoods because of GM's termination. Since receiving GM's May 15 termination notice, we have been frustrated at every turn and trying to get a fair and just resolution of this matter. But because the government is now so deeply involved in keeping GM going, we feel we had no option but to appeal to you, our elected representatives to intervene. We have been very thankful for the support we have received from Congresswoman Sheila Jackson Lee and other members of the Houston delegation, in particular, Gene Green in the House, as well as Mr. Maffei of this Committee, who introduced H.R. 2743.

We—it is very important to say that we need action now. Dealers, thousands of them, are hanging by a thread. We need to pursue this legislation, but we also need to pursue an administrative solution to this situation, which is very possible. GM and the White House, along with Congress and dealers, need to sit down and work for an administrative solution to the matter, and I stress time is of the essence, because every day, guys like these are going out of business and when they are gone there is no way to bring them back. A few things I would like to share at the end of this is that in our—

Mr. COHEN. We need to wind up.

Mr. KNAPP. Okay. In our market—people buy their cars where they live and they service them where they work. The population of our area is experiencing phenomenal growth and GM needs to retain that. Almost 200,000 people work in the downtown area. GM needs to satisfy the service needs of the market created by this downtown group. The retention of Knapp Chevrolet in downtown Houston will allow GM to continue and increase their market share and their growing and vibrant downtown area. Since the government is bailing out GM, Members of Congress have the right to intervene to avoid destruction of viable dealerships. There are two things Congress can do: Force GM to negotiate fairly or if that doesn't work, it can attain final enactment of the Automobile Dealers Economic Rights Restoration Act of 2009 which by statute will preserve dealers' rights. I urge you to choose one of those two options. To take the third option would change the current crisis into a permanent disaster.

I will be pleased to answer your questions and just appreciate the chance to be here. Thank you.

Mr. COHEN. Thank you, Mr. Knapp.

[The prepared statement of Mr. Knapp follows:]

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PREPARED STATEMENT OF ROBERT G. KNAPP

**TESTIMONY**

**OF**

**ROBERT G. KNAPP**

**President of Knapp Chevrolet, Houston, Texas**

**July 22, 2009**

**Hearing on the Ramification  
of Auto Industry Bankruptcies, Part III**

**TESTIMONY**  
**of**  
**ROBERT G. KNAPP**  
**President of Knapp Chevrolet, Houston, Texas**  
**Before the Judiciary Subcommittee on Commercial and Administrative Law**  
**July 22, 2009**

Mr. Chairman and members of the Committee, my name is Bobby Knapp and I am President of Knapp Chevrolet in Houston, Texas. Thank you very much for giving me the opportunity to testify at this hearing on the ramifications of the auto industry bankruptcies.

The focus of my testimony is General Motors' unilateral and arbitrary effort to terminate Knapp's Chevrolet franchise. We at Knapp, a healthy and profitable Chevrolet franchise, are perplexed and outraged by GM's action, and believe our situation warrants your attention as you evaluate the way the GM and Chrysler bankruptcies and subsequent government bail-outs have been handled. Also, I strongly urge that Congress take remedial action to protect car dealerships like ours from GM's flawed dealership "rationalization" plan.

CURRENT SITUATION: TERMINATION PROCESS NOT RATIONAL AND IT IS UNFAIR

You all already are familiar with the broad outlines of the Chrysler and GM bankruptcies and the government's subsequent bail-out of the companies. I would add, however, that we at Knapp Chevy applaud the decision by the government to keep these two companies in operation. We think our brand—Chevrolet—is a great American brand that our country should not lose; we are proud to market Chevys.

Unfortunately, in the rush to complete the bankruptcy/bail-out process, the dealership terminations that went along with that process have been handled irrationally and unfairly, as a review of our situation will demonstrate.

On May 15, Knapp received a letter from GM proposing to terminate our franchise on October 31, 2010. We were then given just two weeks to prepare and submit an appeal, which we did. All told, we have submitted four appeal requests since receiving that May 15 notice. Three have already been summarily rejected even though doing so flies in the face of the facts and is unfair.

FACT: Knapp Chevrolet sold over 1,000 vehicles in 2008.

FACT: In Houston, the loss of Chevy dealerships results in loss of GM market share, so terminating Knapp is only going to cause GM to lose even more Houston market share than it has lost already—even though our city is as good a market for Chevrolets as any GM can hope to have.

Here is a graph and other data net show our Chevrolet district average sales for Houston over the last 12 months. That period started with 12 dealers, and GM sold over 1,200 Chevys a month through the first 8 months of the year. Then, three dealerships, including two very large ones, shut down. As you can see, our district sales numbers then dropped to just over 500 vehicles a month through the end of the year. One can only conclude that GM loses market shares when a dealer closes in this market. I thought the whole point of the bankruptcy/bail-out was to strengthen GM market share. GM can't be strengthened if it continues to lose market share.

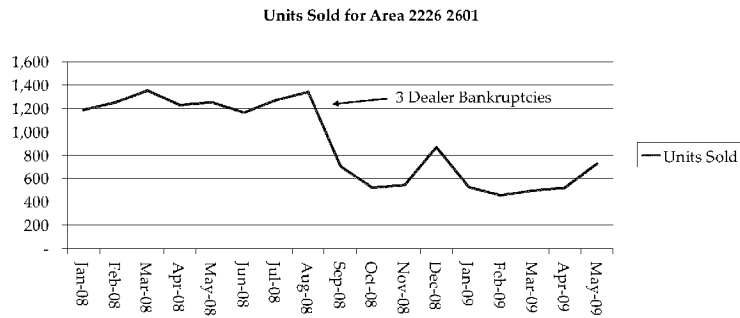


How much Market Share will GM lose by terminating Dealers?

It is our belief that there is empirical evidence and quantitative analysis that can be done to determine the impact of GM's mass dealer termination to GM's market share.

In the Houston Area, specifically categorized as Area 2226 2601 according to GM, there have been 3 dealers to file for Bankruptcy in September of 2008. As you can see from the chart below GM did not retain the sales in the market.

Will GM be able to retain their market share by terminating the dealers? NO



Digging Deeper into the Numbers we can determine the retained Market Share

If you take the total units sold from January through August 2008 (8 months) less the bankrupt dealers' sales you will get the normalized sales for the period. If the same analysis is done from October 2008 through May 2009 (also 8 months) you can determine the market share gain or loss if a dealer was to shut down.

From our analysis, GM lost a staggering 53.7% of their total sales volume. Even more alarming, GM lost 21.9% of their market share.

How does GM benefit from reducing its dealer body? According to empirical evidence and quantitative analysis, GM not only will lose significant unit sales, but also will lose significant market share.

	Jan - Aug 08	Oct 08 - May 09	Percent Loss
Total Units Sold	10,044	4,651	-53.7%
Less Bankrupt Dealers Units Sold	4,101	8	
Normalized Units Sold	5,943	4,643	-21.9%

Please note that this table is not adjusted for seasonality, but that effect would be minimal to this analysis.

FACT: Looking at the last 12 months, including June, Knapp Chevy was operating at a profit in 11 months, with the only down month being last September, when we were without power for 15 days.

FACT: By terminating Knapp, Chevrolet will be abandoning areas in and around downtown Houston, including the Sixth Ward Historic District, an area that is being revitalized and is growing unlike any other inner city in the entire country. GM itself believes in the potential of this market. Here is a map that GM put together showing that Knapp's service area is poised to grow explosively in the next four years, with incomes of its residents projected to increase dramatically. [Map to be supplied later.]

And, if Chevrolet abandons downtown Houston now, it simply won't be able to get back into the area once it completes its revitalization—it will be too expensive.

UNFAIR: GM is forcing us to take an agreement that essentially gives all the rights to GM and all the obligations to Knapp.

UNFAIR: GM will say that it offered Knapp termination assistance as part of the wind-down process. But, it is a sham; it will not come close to reimbursing Knapp for its losses associated with the forced wind-down of its business. What GM is offering will be eaten up by our losses on outstanding contract obligations we have to third parties that total over \$600,000 and the forced liquidation of special GM tools and parts at fire sale prices. And, even though the termination wouldn't be complete until October 2010, GM will strangle our business during the interim. They won't offer us new cars and won't buy back our existing inventory

UNFAIR: At the time we received notice that GM would not renew our franchise agreement, we had over 40 sold vehicles on order, including a number of ambulances for the City of Houston. We were told by GM that it will not honor those orders.

UNFAIR: GM needlessly is thumbing its nose at downtown Houston. Local businesses that we work with will be hurt; local charities will lose our support; and the 200,000 people who work in downtown Houston won't have anywhere to service their Chevys.

UNFAIR: Knapp has had a robust program to maintain and enhance the Chevrolet brand at its location. Over the past ten years, we have invested \$3.25 million in facilities, and we have invested another \$520 thousand in IT and equipment. All of this will go to waste with the termination.

UNFAIR: Knapp Chevrolet has gone the extra mile to help Chevy weather the storm of the depression in car sales. We have taken all of our inventory allotment, and then taken more. The reward for our loyalty is that GM wants to abandon us.

UNFAIR: We employ 82 hard-working people whom we consider family. We offer substantially better benefit packages than others in the industry, and our average employee tenure is seven years, with many employees having been with us for over 10 years. All will lose their jobs and livelihoods because of GM's termination.

## CONGRESSIONAL ACTION NEEDED

Since receiving GM's May 15 termination notice, we have been frustrated at every turn in trying to get a fair and just resolution of the matter. Because the government is now so deeply involved in keeping GM going, we felt we had no option but to appeal to you our elected representatives, to intervene. And, we have been very thankful for the support we have received from Congresswoman Jackson-Lee and other members of the Houston delegation in the House.

We are not alone. Hundreds of other GM and Chrysler dealers have come to Washington seeking justice, and have received similar support from their congressmen. Mr. Maffei of this Committee introduced H.R. 2743, the Automobile Dealers Economic Rights Restoration Act of 2009, which I understand now has 242 co-sponsors, a solid majority of the House. Senator Grassley has introduced a companion measure in the Senate, which has 27 cosponsors.

Just last week, the House included in the fiscal year 2010 financial services appropriations bill a provision very similar to H.R. 2743. Let me take this opportunity to publicly thank the House for this significant action. We hope it is just the first step toward a quick resolution of this crisis for car dealers. I would urge the House to insist that the Senate accept this provision. I believe GM won't sit down and negotiate with the dealers unless it has the threat of remedial legislation hanging over it.

## CONCLUSION

Again, I deeply appreciate the opportunity to testify today because a healthy, family-owned American business is on the verge of being needlessly destroyed.

Since the government is bailing out GM, you members of Congress have the right to intervene to avoid this destruction from taking place. There are two things Congress can do: It can force GM to negotiate fairly with its viable dealers; or, if that doesn't work, it can obtain final enactment of the Automobile Dealers Economic Rights Restoration Act of 2009, which will by statute preserve dealer's rights. I urge you to choose one of those two options. To take the third option—doing nothing—would change the current crisis into a permanent disaster.

I will be pleased to answer any questions you have, or provide any additional information or testimony you need. Thank you.

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Mr. COHEN. We have included in our panel—it is a large panel, but we have taken two and made it into one. I appreciate your testimony and I will first recognize myself for questions. Each Member will have 5 minutes to ask questions.

Mr. Warriner, let me ask you this: Your case against Chrysler how much were you seeking or are you seeking in damages from Chrysler?

Mr. WARRINER. We are seeking damages. Honestly, I don't have a total, but I can tell you that the amount of liens against any kind of settlement at this point are well over a million, which means that I would see not a dime. And the costs of my prosthetics, which insurance did not want to cover—it took me quite a while to fight that—was roughly over 60,000 per leg, and they are not expected to last as long as hopefully I am, which means I will incur that expense and continued expense throughout the course of my life.

Mr. COHEN. I presume you had discovery in litigation?

Mr. WARRINER. Yes.

Mr. COHEN. Did Chrysler ever admit any liability?

Mr. WARRINER. Chrysler has not admitted liability and they have not spoken with me across the table.

Mr. COHEN. Is this the case of first impression or have there been other cases with the same—

Mr. WARRINER. I am sorry?

Mr. COHEN. Have there been other cases that you know of where the same defect was alleged to cause the injury?

Mr. WARRINER. Not that I am aware of.

Mr. COHEN. So when you got to mediation level, had they made you an offer of any kind?

Mr. WARRINER. Mediation originally was supposed to happen on November 17 of 2008. They delayed it to May 5 and declared bankruptcy 5 days before that.

Mr. COHEN. But they never made any offers or—

Mr. WARRINER. No, never made an offer. They did contact us and wanted to know what we were asking, and I believe at that point, the demand was \$11 million.

Mr. COHEN. Thank you.

Professor Baird, you talked about some of these super priority liens and obviously you think this is one that should be one?

Mr. BAIRD. I don't know the facts and circumstances of this case—

Mr. COHEN. I mean tort liability.

Mr. BAIRD. Tort liability generally, because if tort law is working correctly, it forces the firm to internalize all the harm that it is causing to other people. If you give it to a super priority over secured creditors, I am sure you will have a bunch of banks in here saying well, wait a second, if that happens, we are going to have to look at these firms closely and make sure they don't do stuff like that to which the answer is, well, that is the point. Other people may say look, it may actually force some businesses out of business because they are creating such dangerous products. They are posing harm on other people that if you don't free them from tort liability, they will go on and keep on doing these things.

Well, one of the reasons you have tort law is to make sure that firms that are causing more harm go out of business. So again, a super-priority lien does that, but I should emphasize it has to exist inside of bankruptcy and outside of bankruptcy.

Mr. COHEN. Is there precedent for those—

Mr. BAIRD. There are some environmental laws that work this way.

Mr. COHEN. Can you cite me some examples where the liability has continued along with the company even though they have gone through either a 363 or a Chapter 11?

Mr. BAIRD. Typically speaking, if you don't have something like a lien that tracks the assets then when the asset is sold in a 363 sale, it is sold free and clear of all these liabilities, and the only recourse the tort victim has is to the proceeds of the sale. It is a slightly different case if we are talking about a future liability, but with respect to an accident that has already happened, the only recourse in the absence of a lien is to the proceeds of the sale.

Mr. COHEN. In the General Motors case they are accepting liability for future claims. Of course there are vehicles that may have been manufactured prior to the bankruptcy.

Mr. BAIRD. Yes.

Mr. COHEN. Obviously they are saving money, but what is their argument for having that line of demarcation?

Mr. BAIRD. The question is if the accident hasn't happened yet, do you treat it as a prebankruptcy claim? And there are proposals to deal with this. The bankruptcy code doesn't deal well with them now, but you have got two competing arguments against each other. On the one hand, you want to make sure the business continues free of past obligations. On the other hand, you want to make that future accident victims have their day in court, and they never had their day in court if the debt got discharged before the accident took place. And so you need a way to figure that out. But there are proposals to do that.

Mr. COHEN. It just seems like the defect is going to be the same if it is a vehicle produced after the bankruptcy. That may be one way to do it. But if the accident is afterward, it is just lottery and you have got your number when it came up.

Mr. BAIRD. The way to think about this is to figure out a way to estimate future liabilities and create a fund that is going to be there available for those—for those future tort victims. This is something that can happen in the Manville case. There is a way of trying to navigate through these problems. The big difficulty you have is you want to make sure that the tort victims get as much as possible but that is only going to happen if the assets are put to their best use. If you liquidate the assets, then no one is going to be paid anything.

Mr. COHEN. Mr. Ikenson, in your testimony, you had concerns and problems with the government's coming in and rescuing these two historically large corporations with so many employees. What would have been your suggestion if instead of having 536 CEOs, we had one and it was you? Sayonara Chrysler and General Motors and all their employees?

Mr. IKENSON. Well, first of all, I don't think that the situation was as bad as it was put out to be, Chairman. On November 5, the day after election, the Center for Automotive Research published a report which said that 3 million jobs were at stake, and that number was taken by the media and it became a central part of what I consider to be crisis mongering in the situation. The premise for those 3 million job losses was that if one of the Big Three went

down the supply chain, the parts supply chain, would be threatened and that would put too much pressure on the other two and ultimately not only would the Big Three go down but the foreign name plates as well, there would be no auto production in the United States. That was never part of the story in the media.

I think what could have happened was the companies could have entered bankruptcy well before November, and if they could have emerged as viable going concerns, then a bankruptcy judge would have figured out away to do that without the process being so politicized. One of them might have had to liquidate. Certainly there would have been job losses, as there are under the current circumstances. We are hearing about it right here. But I don't think it would have been as dire. I think the companies that stayed in business would pick up market share. That is how the process works.

Mr. COHEN. And that would be the Japanese companies and—

Mr. IKENSON. I would say that they are American companies in the sense they are here and they are—

Mr. COHEN. America once removed.

Mr. IKENSON. Pardon me?

Mr. COHEN. Once removed like a cousin, a shirttail cousin. It is a southern phrase.

I now recognize the Ranking Member, Mr. Franks.

Mr. FRANKS. Thank you, Mr. Chairman. Mr. Chairman, I guess I have made the point so many times here that it is probably a little bit redundant, but I just want to reiterate that our economy is not based just on competition; it is based on trust. And I think that that is really if there is any central theme that I sense here, it is that whether you are an investor, whether you are a worker, whether you are someone who has been hurt in an accident, you have a right to—in this country we—our rule of law and that people have a right to rely upon that. And when government especially does things that undermine that, we have a great deal of ancillary effects that sometimes snowball into absolute disasters.

And again, because of the kindness of the Chairman, I have already mentioned that I believe that government catalyzed a lot of this. I believe that some of our meddling in the market, our guaranteeing of certain loans, our encouragement of—encouraging people to buy homes that they couldn't afford, catalyzed the subprime meltdown, which if those loans had performed as normal loans, it probably would not have resulted in this economic meltdown and then the dominos that fell and hit everyone, including the automobile industry and, of course, ultimately all of you. But I have heard some very compelling evidence and testimony today.

And Mr. Mourdock, I would like to start with you because I was especially moved by your testimony and Mr. Warriner's, but as it happens, you and I have a mutual friend in the State Treasury, Dean Martin in Arizona, who has gone through a crushing personal tragedy in the loss of his wife and child, and I just thought the question I would pose to you first was that do you believe that secured creditors—now you already answered this, but I just want you to expand on it a little bit.

Do you believe that the secured creditors received a fair opportunity to negotiate with the auto task force and Chrysler over the



terms of Chrysler's bankruptcy deal, and if you don't, tell us why not? And why do you think that secured creditors—why is that so important to me? Obviously, you and I agree on this, but please amplify on it if you would.

Mr. MOURDOCK. Let me deal with the second part first, if I may, which is kind of the macro-economic sense of how these secured creditors are viewed. I mentioned in the first part of my testimony, we have 6,000 Chrysler employees in the State of Indiana, and I think I heard from every one of them as I went through this process that ultimately took us to the United States Supreme Court. I was constantly being asked why are you putting my job at risk? And I understood those questions, and yet as a fiduciary, I had to look out for the rights of our pensioners. I have no regrets in standing up for the rule of law. What was happening, though, was bigger than what those Chrysler employees saw. It was bigger than Chrysler.

With all respect to those with me on the panel, it is bigger than them. This is about our entire economic investing system. When secured creditors no longer see their rights as being truly secured, they will not respond the same way. You change the rules, the players will change. What ultimately will happen is that hundreds of billions of dollars that might be invested in American companies will be shifted to places where the markets are not changing, where the rules are not changing. Like American jobs have fled overseas, those dollars will flee overseas.

I mentioned in my testimony that institutional investors are changing the way they are doing business. How do I know that? Because I am one. You know, I invest up to \$7 billion of the State of Indiana's money, and as a fiduciary, I have changed our investment policies so that—and this is hard for me frankly to say because if you cut me, I bleed red, white and blue, but the State of Indiana will no longer buy the secured or any debt of American corporations that have accepted bailout money. Why? Because it is too risky. That is not hypothetical theory; it is demonstrated fact.

We have lost millions of dollars when we thought we were secured creditors under the terms of that meaning for more than 200 years, and it meant nothing. After we adjusted the policy and said we are no longer going to buy the debt of those corporations that had taken bailout money, someone raised an interesting question in the meeting and said, wait a minute, what about Ford Motor Company? They haven't taken any bailout money, should we own them? And some of us looked at each other with puzzlement, and then they said don't you realize the same principled creditors there are the same majority creditors that were in the Chrysler case?

In other words, it was the same big TARP banks that initially argued for 100 cents on the dollar who ultimately, under pressure from the government, acquiesced to take 29 cents on the dollar. How impossible is it for us to believe that 6 months, 8 months, a year down the road, people will look at Ford and say, you know, they are doing okay, but GM and Chrysler, they are not making it and maybe we ought to level the playing field and someone from Treasury whispers in the ears of the bankers "level the playing field," and there we go again. We cannot take that risk as investors. And so we are looking in our office to see where might we best

invest and what other industries, American industries, American companies ought we not invest in because we may see this same scenario played out again.

And someone mentioned in the first session this morning the airline industry. If anyone doesn't see parallels between today's airline industry and you can name them company by company with the automotive companies in this country, then you are not really trying to connect the dots.

Mr. FRANKS. Thank you, Mr. Mourdock. As it happens, I was the one that mentioned the airline industry for the same exact reasons and I appreciate that. And the Chairman that has granted me an additional 30 seconds and I would like to quickly mention my question to Mr. Ikenson.

Mr. IKENSON, the Chrysler bankruptcy deal in particular destabled contract rights and secured investment, in my opinion, just as you have heard it eloquently stated here. Doesn't that jeopardize our ability to recover promptly from the current credit crisis and the recession itself?

Mr. IKENSON. Yes, I think so. I mean, I am not really the expert on the panel. I would defer to Mr. Mourdock on that. However, yes, we have created a bit of a moral hazard here. It is going to take changes as Mr. Mourdock just testified. People change their behavior. And I think there will be fewer willing participants in the corporate bond market, which will help to drive up the price of debt, and that will spill over into the general economy, particularly now at a time when we are incurring massive debts, deficit spending, and are going to be needing sources of funding not only for corporations but for our government's profligate ways. So yes, it concerns me that it will have adverse implications that could be costly. Thank you.

Mr. FRANKS. Thank all of you and thank you, Mr. Chairman, for the extra time.

Mr. COHEN. Thank you for your questions.

Now I would like to recognize the distinguished Chairman of the full Committee, Mr. Conyers.

Mr. CONYERS. Thank you, sir. We welcome you and thank you all for your views and presence here today.

Professor Baird, help me in my analysis with the Treasurer of Indiana in terms of how we put this into perspective because if he is right, that nobody wants to invest in companies that accept TARP money and yet the companies come to us and ask for help, what do we do? Leap out of the highest window in the Rayburn Building or bring out our Ouija board or some kind of—I mean that sounds like a pretty impossible situation. What do you think happened in 1978?

Mr. BAIRD. Well, I think—I don't think things are quite as dire as Mr. Mourdock. But in terms of protecting the rights of the people he cares about, which is something I do care about and I think secured creditors should be protected, what can happen if you have effective bankruptcy law is that we have effective procedures that give people like him the rights that they should get.

Now, if it turns out that the Federal Government's bid of \$2 billion was top dollar for Chrysler, then that is all he entitled to. All he is entitled to as a secured creditor is the value of the assets. If

the high bidder for the assets turns out to be the Federal Government, it is his lucky day that the Federal Government is there willing to bid. The problem in the case and the concern I have is not that \$2 billion wasn't the right amount; it is that procedures weren't there to ensure that it was the right amount. So the solution that I think is required in terms of what happened in 1978 with the bankruptcy code is just making sure that square corners are cut in these situations, and I have a concern that didn't happen here. But I also have a lot of confidence in our bankruptcy bench that it won't happen generally. If it starts to happen generally, then I would urge you to do something.

Mr. CONYERS. Well, were there procedures in place for this circumstance that brings us here today?

Mr. BAIRD. The difficulty is that when Congress enacted section 363, they didn't contemplate section 363 being used the way it is being used today. So if there aren't specified procedures set out in section 363, some courts have tried to develop rules, but section 363 just says there needs to be notice and hearing. That may not be enough. At least it won't be enough if we see practices like this continue.

Mr. CONYERS. Again, what are we to do? I mean, look, you trained the 44th President. Do you talk to each other anymore?

Mr. BAIRD. We worked together for 12 years. I didn't portend to train him. He had the office next to me.

Mr. CONYERS. Okay. Well, you were in pretty close proximity a lot of the time. You have got to take some responsibility for this, sir.

Mr. BAIRD. No. I am a great admirer of the President and I think there is a policy decision about what you do with these companies and whether or not the Federal Government rescues them, and then there is the question of having the bankruptcy process there to make sure that if these policy decisions are made, they are implemented in a sensible way. In the main, I think we have a very fine bankruptcy law that does allow these things to happen. But anytime you have a major event like this you have to reassess. You have to say wait a second, did we do enough? Can we do it better and what is the world going to look like going forward? I am cautiously optimistic about the system.

Mr. CONYERS. Well, the Cohen Committee in Judiciary here, we are going to be doing plenty of assessment. Don't worry. This will be the most active part of the Judiciary Committee for a long time to come.

Mr. BAIRD. Mr. Chairman, I am more than happy to help any way I can.

Mr. CONYERS. Well, look, we had informally agreed that the President incumbent was the smartest political person in the United States of America. He couldn't have gotten elected otherwise. I mean he broke the time pattern. He shattered—look, he was in Iowa. That is where it started happening for him, in Steve King's State, of all places. So we conceded him that. Now there are getting to be qualifications. His soaring popularity on some issues is not so hot, going down a little bit. And we are not sure if he is number one anymore. And, look, Baird, you are the one that I

know that was closest to him during his formative days, and we have to hold you accountable in some sense.

Mr. BAIRD. Well, I have a great deal of—

Mr. CONYERS. This business about, I was next door to him for 12 years, but we never talked about anything—

Mr. BAIRD. No. I am just saying that the President has a very strong personality and he listened very carefully and he responds critically, and I think you should have more confidence than you seem to have in him.

Mr. CONYERS. I think you were a larger influence on him than your modesty would allow you to admit to.

Mr. FRANKS. Mr. Chairman, just for the record, some of us were a little more skeptical early on, suggesting that sky-diving naked into a volcano was change.

Mr. CONYERS. Thank you, Mr. Chairman.

Mr. COHEN. Thank you. I think what you were asking, Mr. Ikenson spoke to it. He testified to his respect for Mr. Obama's abilities when he suggested there were 536 CEOs, not 537, which, of course, with Mr. Cheney, you would have had 537, but now with the Vice President it is certainly a different situation.

Mr. King from Iowa, you are recognized for 5 minutes, sir.

Mr. KING. Thank you, Mr. Chairman. I am trying to figure out that math and perhaps if I had Professor Baird I would have been able to do that.

Mr. COHEN. When you were not here, he testified that General Motors had 536 CEOs. I presume he meant the Congress, the Senate, and the President. The minority side, I don't think they would believe they are really CEOs because that is why they do so many 1 minutes, but maybe they are CEOs and they don't know it.

Mr. KING. Mr. Chairman, I am going to pass up that bait for debate, and also I am going to try to take Professor Baird off the hook because it is my information that my chief of staff also studied under you, Professor Baird; so however the popularity of President Obama may have diminished, my chief of staff still stands up as a good product of the University of Chicago. So I am happy to say that into the record, and I think she is monitoring this conversation. I am a little worried about that.

But I am very interested in how Mr. Mourdock might characterize some of these questions that I have, and that is the discussion that I had here yesterday with the new car czar and the discussion about how the White House might divest themselves from this massive investment in the private sector, and he uttered a statement that I interpreted to be within the context of perhaps in a year and a half or so, we will do a public offering and sell some or all of these shares off again.

So I direct it to Mr. Mourdock. Are you going to be ready to buy some of those shares if they offer them out in market in a year and a half or so?

Mr. MOURDOCK. As a fiduciary, obviously we always look to make investments that we can make prudently. The several pension funds that we have that deal in equities, most of our State investments like most States are more on the debt side than the equity side, but we would wait to see how those would come through. Regarding the testimony of yesterday and coming back slightly to

what Congressman Conyers was raising the issue of what might we do, I think it pertains to that question as well. You know, what might we do as the Congress of the United States? It is a real simple answer. It is follow the law. It is understand the law. Was flabbergasted in reading the statement from yesterday's testimony in which Mr. Bloom suggested that if Congress got involved with the dealerships, it would somehow have impact on the credit markets. Well, pardon me. It was already the Administration that got us in this situation that has already impacted the credit markets. I said at the outset I am not an attorney but I know that article I, section 8 of the United States Constitution gives to the Congress and Congress solely the mandate to set uniform codes of bankruptcy. When the Administration acts in such a way to say secured creditors, it doesn't have any meaning anymore, they just took away your rights. They just took away the power of the Congress. They started making the bankruptcy code and that is unacceptable.

Mr. KING. Mr. Mourdock, I take it from your testimony that your sense would be that Congress didn't assert its authority when the White House stepped in and usurped the property rights of the bondholder, the secured creditors.

Mr. MOURDOCK. That is exactly my point, yes, sir.

Mr. KING. And I would agree with that point. Now I would ask you if you could play out for us how you see it, would have unfolded with General Motors and Chrysler, had those property rights been preserved and protected as was understood by the investors, how this might have gone through a bankruptcy Chapter 11 or 7 and what we might see today?

Mr. MOURDOCK. Great question. And again, it was said earlier during the panel this morning that the only option that was out there was complete liquidation, and that would be true if the June 15 deadline was the driving force for everything. If you have got to get it done in a very short period of time, guess what. That probably was the only option. But what we have argued in our lawsuit and we will continue to argue is the point that once the government decided to link itself at the hip with Chrysler, that changed dramatically what the possibilities were. And had instead of been driving to a deadline with the mandated partner of Fiat at that point the government said, you know what, we are going to be there at the hip. We want to see what kind of real values can be set for this business.

I was stunned when the bankruptcy hearings took place. One of the assets of Chrysler Corporation is the Dodge Viper. It is a muscle car, sort of like a Corvette. It was testified at the bankruptcy hearing by Mr. Nardelli that that whole product line was worth at most about \$5 million. Well, that is pretty astounding because 2 months before Chrysler we know received an offer of \$35 million for that one asset. And along with it was a 44- page preclosing agreement and there had been significant negotiations to get to that point. So with those kinds of questions as to how the value was set, you can bet our secured creditors feel very much like they have been ripped off here.

Mr. KING. It might be that the Viper could have been spun off for seven times what they valued it at.

I would like to probe this question too, and I hope I will have an opportunity to listen to more than one witness answer this question, but is it your sense—and again to Mr. Mourdock specifically, and then hopefully broader. Is it your sense that the agreement that was made on Chapter 11 dealing with either General Motors or Chrysler—well, first, was any of the testimony before the bankruptcy—did any of that testimony alter the anticipated result of Chapter 11?

Mr. MOURDOCK. No, it did not. And I cannot speak a word to GM. I wasn't involved with that side. But in his opening remarks, Chairman Cohen raised the issue of the possible Sub Rosa arguments, and that too was part of our legal suit because throughout all that happened from the first of this year until the bankruptcy was announced by the government, not by Chrysler but by the government. You had the situation where one party was negotiating, setting values, determining which creditors would be in, which ones would be out, what they would be given, what would be liquidated, all to be set up for an auction sale for which there was only one bidder, the United States Government. It was on both sides of the table simultaneously. The impropriety of that in trying to establish value for a sale goes beyond plausible.

Mr. KING. Would anyone on the panel care to address that or rebut that so that there is a fair opportunity because I happen to agree with Mr. Mourdock? None on the panel? That makes a point that I wanted to hear made today and I thank you all for your testimony. You have been excellent witnesses, every one of you, and I wish I had time to indulge with more of that, but there are real human tragedies out here and a big tragedy is what happens to property rights in the United States of America.

Mr. Chairman, I thank you for this hearing today and I yield back.

Mr. COHEN. If you would like another 30 seconds. Thank you, sir. Mr. Conyers.

Mr. CONYERS. Mr. Chairman, could I get 2 minutes before we close up?

Mr. COHEN. Two minutes and 12 seconds.

Mr. CONYERS. This is the claims issue here. We have got, what, 300 claims outstanding at Chrysler, about 1,000 at GM. Is there any way that we can resolve these without really foreclosing any equitable relief from the claimants?

I mean, Warriner is here, but he is only one of an amazingly not-too-large pool of people that have a cause. I wouldn't like the idea of his claim, no matter how just it is, going before a company being settled for pennies because, "We are sorry, we just went through bankruptcy, we don't have the money." Too bad. If you had gotten here a little bit earlier, there would have been a regular trial.

Professor Baird, is it asking too much for a little fairness in these claims? All of whom, of course, are not of the nature and seriousness that is presented here by our witness. But, still, there may be a few that are. I would concede that most of them probably aren't.

Mr. BAIRD. This is a serious deficiency in the law that we have as it is today. I don't have any magic remedies for you, but this is a big problem in the law as it exists today.

Mr. CONYERS. I would like to urge my colleagues to study this with me further after this hearing today. And thank you, Mr. Chairman.

Mr. COHEN. Thank you, sir.

Mr. Williams, I would like to ask you a question. You may not be familiar with this, or not. But I asked the Chrysler folk and the GM folk about the proportion of dealerships in the African American community that might have been terminated. They said that they were all equal, everything was exactly the same. Do you have any reason to believe that that is accurate or inaccurate?

Mr. WILLIAMS. Well, it is inaccurate. You can do a lot of things with percentages. He said the African American dealers or the minority dealers, 20 percent of them were gone, as was 20 percent of the others.

If you look at the numbers, there are a lot smaller numbers. Less than 3 percent of the dealers are African American and minority dealers. Twenty percent of the smaller number is devastating when you are talking about getting those numbers done when you have a very small number of dealers. So you can make things sound like you want it to sound.

When this thing is all over by the end of this year, there will probably be less than 600 total minority dealers left; and General Motors, there will be less than 20 African American dealers left.

Mr. COHEN. In the entire country?

Mr. WILLIAMS. Yes, sir.

Mr. COHEN. Pretty devastating.

Mr. Knapp, what is your experience? Your testimony was really riveting to me. You seem like you have been there, your company, for 70 years. You are right in the heart of Houston. You are selling all these vehicles. What did you say, a thousand?

Mr. KNAPP. Over a thousand.

Mr. COHEN. That is pretty strong. Did they come to you and tell you that that wasn't a good number; You should have been producing more? What was your problem?

Mr. KNAPP. You know, we are a unique dealer. We are a downtown dealer in a metro market. And I don't know that there are any other than us in the whole country. And over the years they have always—we are not on a freeway; we are kind of in a neighborhood, and we just have a little different take than most.

And they have always told me, "Don't worry about—you know, we want a downtown dealer. We want the representation." And it was—obviously, it was a surprise to me, as to everybody, why they would want to terminate us.

But in our case, I think we make a very good anchor in downtown Houston. We are a servicing dealer for every dealership in Houston, because the people that buy there service their cars downtown. And when they lose that, when they lose us, I believe it is going to force these people or make them go to other makes and models.

Another thing that is not really talked about is GM assumes that the loyalty is to GM and not their dealer. And no doubt people are loyal to their Camero or their Caprice or their pickup, but they are also loyal to the dealer. And when their dealers get knocked out or when dealers say no, they are going to have a bad taste in their

mouth and may look to another manufacturer and another model to go to.

Mr. COHEN. General Motors has an appeal process, I think they said. Have you participated in that?

Mr. KNAPP. Yes, sir, I have. Right out of the chute, we got the letter, and they said you have to appeal—it was 2 weeks, so—and with some very vague criteria. You know, we scrambled and got some people to help, and I believe we came up with a very good package and a very good set of reasons why we should stay around.

Well, apparently they rejected every one of those appeals. Then they came back and said—and we never really got a notification from them. But we found out we could submit another appeal, which we did. It was denied.

I found out, because we had talked to our Congresswoman, that we could have a third appeal by telephone. We called them on the phone and I gave him a long list of reasons why we should remain, and that appeal was denied.

So lastly, I got a call from the Texas Auto Dealer Association. They had talked to the Texas Attorney General, and for whatever reason, the Texas dealers were going to be given a fourth appeal. And that was almost 3 weeks ago that we submitted it, and I talked to the man at GM that I had done the phone appeal with and he said, “Go ahead and put it in writing. It is a lot easier for me to explain it to people, the powers that be.”

So I did. I came up with what I believe is a top-notch, first-rate appeal. I have not heard, hopeful that that is a good sign that they are really looking hard.

Mr. COHEN. Thank you.

Mr. Williams, you were nodding. You filed your appeal, too, and they rejected it summarily?

Mr. WILLIAMS. I filed an appeal. They rejected. You can't get anyone to speak to you, so you don't know what they use, what criteria they used. They just rejected it.

Mr. COHEN. Mr. Fitzgerald, Mr. Tarbox, do you also have similar experiences with your appeals?

Mr. TARBOX. There was no appeal with Chrysler, and I appealed through the U.S. Bankruptcy Court.

Mr. COHEN. Mr. Fitzgerald?

Mr. FITZGERALD. There was no appeal with Chrysler, and General Motors rejected my appeal.

Mr. COHEN. Was there some figure they put out; they thought they could save like \$2 billion with GM?

Mr. FITZGERALD. That is the big lie. I talked too much and I didn't finish telling you about the big lie.

Mr. COHEN. I will give you the opportunity to finish.

Mr. FITZGERALD. Thank you.

Mr. COHEN. You liked my humor. I am giving you a chance to say.

Mr. FITZGERALD. I was. I was intrigued by it.

Mr. COHEN. You get an extra 30 seconds. Keep going.

Mr. FITZGERALD. Okay, I am going.

It costs them nothing for a dealer. All of that nonsense is contrived. If you look at the price label, that is why I sent you—I put two price labels with factory invoices with them in the package I



submitted. We pay almost sticker for the car when we buy it. We used to when—that sticker is on the car by Federal mandate, Monroney label. It was named after Senator Monroney from Oklahoma, his Committee. And at the time, all of us received a 25 percent discount, I was a Ford salesman then, 25 percent discount.

Over the years the manufacturers have found lots of reasons to change the discount, which increases their share of the transaction price. It has evolved to the point today where we receive somewhere between a 1 and 5 percent discount from sticker.

And all of those things that Mr. Henderson recited for you, the costs that they were going to save, for example, filling the gas tank; I am not sure how he makes that story stick, but I haven't even seen the media pick up on that. But he actually said this with a straight face, that they would save a lot of money, in the hundreds of thousands or maybe millions of dollars by not putting gasoline in the car for the customer. That hasn't got anything to do with the cost to the dealer.

The same thing is true with PDI: Prep it and deliver it. The manufacturers pay an allowance for prepping cars. I think they worked that out with the Department of Transportation some years ago why they had to do it that way. So that was an excuse to raise the price to us, and then they pay us to prep the car. Again, that is related to the car itself.

The 1 percent marketing allowance that somebody said something about that today. That is directly related to the car and it has to do with advertising. You have certain strings attached to that.

Oh, the incentives. One of the most significant things are incentives. If you read *The Washington Post*, there was a story there, Troy Clark, president of General Motors, talked about how the new Malibu brings \$20,000 whereas the old Malibu only brought 16.5. The difference is they don't have to pay as many incentives to sell it. Incentives change the price of the car.

If your car is not for example, like most of the GM cars, if you not recommended in Consumer Reports, the GM—if it weren't for Chrysler, GM would be in last place in Consumer Reports, and they have been there for many years. That is one of the reasons I was terminated; I keep waving this thing at them, because this is what my customers say.

My customers read this. You go ask your young staffers if they don't read this. And that may be why none of them drive American cars, because we are always at the bottom of that list.

So the incentives change the price of the car. It is a price change. If they don't have to pay the incentive to sell the car, they keep it. I don't get it; they get it. So it is all related to the price of the car.

There is not a single shred of truth in all of that sophistry that was painted for you concerning the savings on dealers. There is no such thing. And if we get in the back room with the coffee, I have got my numbers and I have got my factory invoice and I have got my MSRP numbers and I will show it to you.

Mr. COHEN. When they said—Mr. Robinson, I think he said that the reason that the automobile industry got in such trouble is because of the finance problems in the country and the gasoline

prices. You would submit that being ranked last in Consumer Reports might have contributed to it, too.

Mr. FITZGERALD. Well, everybody had the gasoline price to deal with and everybody had the finance problems to deal with. But General Motors and Chrysler had the overwhelming problem of Consumer Reports to deal with. And they have been dealing with it for 28 years and ignoring it.

One of the reasons I am terminated is because I made a crusade out of that. And I can show you letters from Rick Wagoner all the way back to 2000 promising that he is going to do something about it. And they did; they got rid of me. Now they don't have to listen to that.

Mr. COHEN. Thank you, sir.

Mr. King, you are recognized.

Mr. KING. Thank you, Mr. Chairman. Mr. Chairman, you raised an issue that caught my attention, and the question is to Mr. Williams.

And in your testimony, Mr. Williams—I am going from memory here—you have been in the car business about 30 years—or been in the business 30 years; 11 years as a dealership. Out of 90 competing dealers, you were ranked third in sales and number one in customer satisfaction. Is that all correct?

Mr. WILLIAMS. Yeah. I have been a dealer for 30 years. I have been in this location for 11 years. And I have 19 competitors, and we are number three in sales and number one in customer satisfaction.

Mr. KING. Nineteen competitors. I misheard that number and also I misheard that you were in the dealership that long. And that is the reason I asked the question, to some degree, because to build up that much capital, to find yourself in this much liability, that is a good hustle to get there in 11. In 30 years, I can see how you could get there.

It is interesting to me, the issue of race was raised by Mr. Cohen. And I just want to ask this as—I am not a lawyer, so I can ask a question I don't know the answer to. And that is, honestly, do you believe—and I am very sincere in my inquiry here—do you believe that race was a factor in the termination of your franchise?

Mr. WILLIAMS. You know, I don't know that somebody specifically said, hey, we are going to get rid of the minorities. But when I gave you the number, out of a thousand dealers that bit the dust last year, 200 of them were minorities. If we could have had that percentage of them putting in dealers, we wouldn't be making a lot of noise. We are less than 3 percent of the dealers. But 20 percent can go out? You can't stay with 20 percent go out and less than 3 percent are coming in.

Mr. KING. It is about seven times the rate.

Mr. WILLIAMS. They know how to take us out. They don't know how to put us in, I guess.

Mr. KING. And I appreciate the reemphasis of this end of the record. And one of the things that I admire about free enterprise is that you have to compete in the marketplace. And it doesn't matter what color you are or what gender you are or what ethnicity you might be. If you have got cars on the lot, people will drive by or stop in, and if they like doing business with you they are going

to do business. If they don't, they are going to move on to somebody else.

And you have made a living for 30 years in a free market system that doesn't have an affirmative action program except the one that you apply with your own energy and your own ingenuity and personality.

Mr. WILLIAMS. We would still be around if they didn't decide to give me the door.

Mr. KING. And I support the idea of doing all we can to keep you all around. And I brought this up because I wanted to flesh that out a little bit more. With a President today that I think is testimonial to the ability to be upwardly mobile in this society—and I think you are a testimonial to that as well, Mr. Williams, and I thank you for being here. I thank everybody for your testimony.

And I wanted to go back to Mr. Tarbox. And I know there was more within you that I didn't hear, but the frustration of leading your field and dominating the market in your area. And we are down to you have no recourse, I understand. But what do you believe was the motive, other than the fact that you were insistent and resistant about the idea? Are you just too outspoken and you are punished for being outspoken? I hope that is not coming my way.

Mr. TARBOX. Their reason was the protest that I had the year before on their intent to establish a Jeep dealer in Rhode Island. And it was evident on the e-mail that is on record with the U.S. Bankruptcy Court.

Mr. KING. And what do you have to say to the testimony of Mr. Mourdock about how property rights have been set aside here with regard to these bankruptcy cases? And what do you have to say about what appears to be fait accompli that was negotiated perhaps before the bankruptcy hearings?

Mr. TARBOX. I am not sure if I understood the second part of the question, but I certainly agree with the property right issue. I mean, it is evident in the fact that they are taking what I have and giving it to the dealer up the road. They claim that they set certain criteria, and I called the dealer up the road, and the dealer up the road specifically told me that she was surprised that she wasn't rejected as a dealer.

So it is not based on performance and criteria. Their decisions were based on spite and the fact that I protested that intent.

Now, in discussing different things with dealers that are in the same boat that I am, I wouldn't be surprised if they—when they made their decisions to reject dealers, that they didn't contact their legal departments and say: Hey, who has litigated or protested with us in the last 3 to 5 years? I want a list of those dealers.

And I wouldn't be surprised that you might find the majority of those dealers were in fact rejected.

Mr. KING. It would seem to me—and I thank all the witnesses. It would seem to me that in the United States of America, if you own something that I think we all on this panel would describe as a property right, that there should be some recourse to protecting your property rights through the litigation process. And it looks to me like that is what has been set aside here in this race to a pub-

lic/private model that may not have a lot of value in the private sector a year and a half or 5 or 10 years from now.

I thank all the witnesses. Again, this has been a good hearing.

Mr. Fitzgerald has a voice—if the Chair has enough patience, I would remind us that he said there is not a single shred of truth in all of that sophistry. I think that is a remarkable statement.

And I would be happy to hear from the gentleman. Mr. Fitzgerald.

Mr. FITZGERALD. Well, I do have the data. Now, of course, we believe that Mr. Warriner and people in his position should be addressed, too. It is the American way. But from the dealers' point of view, we are not asking for any money. Our property was taken from us. Just taken. You know, I have got 43 years of good will invested in Chrysler, and over 30 years in General Motors. That was taken without any compensation whatsoever.

Now, I can get real angry about it, but I don't have as much—what has been done to him is a travesty. He is 42 years old. I am almost 75. I mean, it is—I am okay financially. But what I have heard from dealers around the country, you would not believe the human suffering that is being caused by this reckless abuse of the bankruptcy laws. You just would not believe it. It is indescribable the things that I have heard, and it is just not the American way.

And that is why we have 260 votes and cosponsors, I mean in our bill, and we have 30 Senators. And that is because when people hear this story and they look at the facts and they look at my price labels and they see the real thing, H.R. 2743 and Senate bill 1304, it is easy to sign on when you see that injustice, when we don't cost any money. You know, this can be fixed with no money. And Congress writes the bankruptcy laws.

Mr. KING. I thank you, Mr. Fitzgerald.

Mr. Chairman, I have a couple documents that I would ask unanimous consent to introduce into the record that I am a little belated on. They are just simply related to dealerships within my district.

Mr. COHEN. No press releases of mine?

Mr. KING. Not this time, Mr. Chairman.

Mr. COHEN. Without objection.

Mr. KING. I thank you.

[The information referred to follows:]

Thank you Congressman King and members of the Committee:

Thank you for allowing me to share a brief outline of our dealership's history and involvement with General Motors.

My name is Eric Hoak, President of Hoak Motors Inc. in Sioux City, Iowa. I am 34 years old and run our family's dealership with my younger brother Christopher. This dealership has been in our family for 64 years, proudly selling and servicing GM cars, trucks, and SUVs. Our store, like many others, is being effected by GM's decision to terminate franchise agreements. I feel their decision is unfair and will deeply hurt my family, my business, and my community. We have had several setbacks in the last year which could ultimately cost my family our business.

- In the summer of 2005 we moved into a brand new facility designed to handle all four of our franchised lines (Cadillac, Pontiac, GMC, & Nissan). Our new building has a larger lot for more inventory, two floors for greater parts storage, large service bays to handle any vehicle on the market, as well as 2 acres for future expansion. We were not forced to move, but the move was highly encouraged by our GM zone manager. We had been in our older building for over 50 years and were highly capitalized.
- February 15<sup>th</sup> 2009 we had a major building fire causing over 3 million dollars in smoke and fire damage to our business. Though we have ample insurance we are still spending our own money to rebuild until the claim is settled by the insurance company.
- Currently we are still rebuilding from this fire, which was determined to have ignited from a wiring malfunction in a GM vehicle. In addition to that, we are now also dealing with the loss of our entire GM lineup. This announcement has made it difficult for us to operate our day to day business, affecting both our sales as well as our service. Many of our customers are unsure about how and where they can get their cars repaired and serviced in the future.
- While rebuilding we have had to repurchase several required elements for our dealership, i.e. brochure display racks (\$1800 x 2), beauty shots of the new models and frames (\$40 per picture x 30). We are also replenishing our parts inventory (over \$150,000), and the large number of specialized tools, all of which we are told will not be eligible for return due to our "wind-down".
- We are one of two GM dealerships in our city to get the termination notice from GM, leaving only one stand alone Chevrolet dealer to service any GM product. The Siouxland metropolitan statistical area, or MSA, encompasses 5 counties in 3 states including Iowa, South Dakota, and Nebraska, with Sioux City, IA (4<sup>th</sup> largest city in Iowa) being the economic hub, and having a population of 143,000. This population consists of people who have been driving vehicles sold buy us for the past 64 years. Now these customers will have longer wait times to get in for

repair or will need to shop elsewhere to get their needs met. Overall the selection of local cars to shop from has been greatly reduced, possibly sending our business out of town; this has a direct impact on our community.

We have been a partner with GM for over 60 years and have constantly and effectively advertised, promoted, sold and serviced their products. We have supported our community's organizations and maintained a presence in the community while averaging over 250 units a year for the last 5 year. We, as well as many others, feel General Motors is acting unfairly towards us and our community!

Thank you for your time in reading this.

Eric Hoak  
Hoak Motors Inc.

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Mr. KING. I thank you for this hearing. I sincerely thank all of the witnesses. Some of you have paid a very high price. And I yield back the balance of my time.

Mr. COHEN. I do have a press release of the minimum wage going up Friday.

Mr. KING. We will check that out.

Mr. COHEN. Mr. Scott from Virginia is recognized.

Mr. SCOTT. Thank you very much, Mr. Chairman. And thank you for holding the hearing because what has happened to these dealers is certainly tragic.

I served in the State legislature before I came to Congress, and most States have laws involving franchises and what parent companies can do and can't do to their franchisees. What has happened to these dealers is obviously what is protected by State law, because obviously when you have had people in business for generations being given a couple weeks' notice that they are out of business, everybody knows that that is just not fair.

So I thank you for holding the hearing, and we are going to do the best we can to get some fairness for the dealers, because this just isn't right. I yield back.

Mr. COHEN. Well, we ended with eloquence and brevity. Thank you, Mr. Scott. I don't believe we have any other questions.

I want to thank all the witnesses for their testimony today. I think that this has been an opportunity for General Motors and Chrysler to hear some of your testimony, and I think they heard it through different channels.

Without objection, Members will have 5 legislative days to submit any additional written questions, which we will forward to the witnesses and ask you to answer as promptly as you can to be made part of the record. Without objection, the record will remain open for 5 legislative days for the submission of any other additional materials.

Again, I thank everyone for their time and their patience. This hearing is adjourned.

[Whereupon, at 3 p.m., the Subcommittee was adjourned.]





## A P P E N D I X

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### MATERIAL SUBMITTED FOR THE HEARING RECORD

PREPARED STATEMENT OF THE HONORABLE CHRIS VAN HOLLEN, A REPRESENTATIVE  
IN CONGRESS FROM THE STATE OF MARYLAND

I thank Chairman Cohen and Ranking Member Franks for holding today's hearing. I would also like to thank Congressmen Maffei and Kratovil for introducing the Automobile Dealers Economic Rights Restoration Act and for their leadership on this issue.

This important legislation was motivated by a bi-partisan desire here in congress to come assist profitable auto dealers who have been unfairly treated by auto makers. The indiscriminate closing of many healthy, profitable auto dealerships is unfair and has put thousands of American jobs at risk at a time when our country can ill-afford to shed more jobs.

Further, the decision by automakers to close dealerships overlooks the fact that dealerships are one of the auto industry's key sources of strength and can be the source of their successful navigation out of these difficult economic times. Dealerships, and their more than 1 million employees, form personal relationships with customers that contribute to brand loyalty and will be key to the recovery of the auto industry.

Auto dealerships are also a cornerstone of our communities and deserve our support; they employ hundreds of thousands of Americans, ensure that quality American cars are sold and serviced.

As we move forward with legislative fixes to this flawed process, I am pleased that we have begun constructive and meaningful discussions with the auto manufacturers, the auto task force and with the auto dealers. I believe that we have an opportunity to save the auto industry and protect the rights of auto dealers in the process. They should not—and must not—be mutually exclusive goals.

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RESPONSE TO POST-HEARING QUESTIONS FROM LOUANN VAN DER WIELE, VICE  
PRESIDENT AND ASSOCIATE GENERAL COUNSEL, CHRYSLER GROUP LLC

**Questions for the Record**  
**Subcommittee on Commercial and Administrative Law**  
**Hearing on the Ramifications of Auto Industry Bankruptcies, Part III**  
**July 22, 2009**

**Louann Van Der Wiele, Vice President and Associate General Counsel,**  
**Chrysler Group LLC**

**Questions from the Honorable Steve Cohen, Chairman**

- 1. One of our witnesses, Greg Williams, disputed your contention that decisions concerning the closure of dealerships will not have a disproportionate impact on minority dealers. Mr. Williams further contended that there will be "less than 600 total minority dealers left." What is your response?**

Answer: Chrysler Group assumed **75%** of Old Carco's minority dealers. The number of rejected minority dealers was in proportion to the total dealer network at **25%**. Chrysler Group's minority dealer network represents 5% of our overall network and 7% of our sales, comparable to minority dealer representation at Old Carco. These network actions increase the percentage of minority dealers representing all three brands (Chrysler, Jeep and Dodge) from **66% to 70%**.

Minority Dealer Representation

- As of April 30<sup>th</sup>: **154**
- Rejected Dealers: **38**
- Retained Dealers: **116**

- 2. Please explain why you believe that a traditional Chapter 11 reorganization was not feasible for Chrysler.**

Answer: A car is the second largest investment most people make outside of their homes. We were concerned that consumers would be reluctant to make such a large investment in a bankrupt company. Traditional Chapter 11 reorganizations are a lengthy process and we wanted to preserve as much consumer confidence as possible by making it through this process quickly. Section 363, allowed Fiat to create a new company, Chrysler Group LLC, to purchase the operating assets of the bankrupt entity. Additionally, DIP financing was simply not available from traditional sources, so the DIP financing for Old Carco's bankruptcy was provided by the U.S. Treasury Department. A traditional Chapter 11 reorganization process would have been longer and therefore more costly to the taxpayers.

3. **To the extent that you are able to, please respond to the contention that Chrysler was under political pressure to make concessions to certain creditors that would not ordinarily be entitled to favored treatment in bankruptcy.**

Answer: The negotiations with our creditors were not politically motivated. The UAW agreed to place wages and benefits on par with foreign competitors and its related VEBA made the tough decision to take a chance on the future of Chrysler by agreeing to take equity in the company. The first lien creditors would potentially have received less than \$1 billion under a liquidation analysis that showed a range of possible values. They voted overwhelmingly to support the 363 sale in exchange for \$2 billion in cash and proceeds from the estate under bankruptcy. We attempted to create the most favorable situation for all parties involved and minimize the necessary sacrifices.

4. **Please outline any measures that Chrysler Group LLC has undertaken to address product liability claims arising from defects in Old Carco products.**

Answer: Chrysler Group assumed product liability claims on vehicles manufactured by Old Carco before June 10, 2009 that are involved in accidents on or after that date. This is in addition to our previous commitment to honor warranty claims, lemon law claims, and safety recalls regarding these vehicles.

5. **Please outline any efforts that Chrysler has undertaken to mitigate the economic harm suffered by its dealerships that were selected for termination.**

Answer: Chrysler Group has no relationship with Old Carco's 789 rejected dealers. That said, with regard to mitigating economic harm, Chrysler Group did undertake a number of actions to help the dealers that Old Carco rejected in bankruptcy. All of these actions were beyond what they would have received as unsecured creditors.

**Vehicles:** Chrysler Group has successfully found buyers for 100 percent of the outstanding eligible new vehicle inventory of rejected dealers.

**Parts:** Chrysler Group has worked with rejected dealers to redistribute their parts inventory and has committed to repurchase remaining qualified parts inventory from them at an average transaction price for all parts already distributed.

Dealers requesting assistance during this process have received commitments for 80 percent of their qualified parts inventory.

**Special Tools:** We continue to work with rejected dealers to redistribute remaining special tools.

Many of the rejected dealers have chosen to retain their tools because they intend to continue as repair shops.

**6. Please outline any efforts that Chrysler has undertaken to mitigate the economic harm suffered by its suppliers as a result of its reorganization.**

- (1) Prior to filing for bankruptcy, Chrysler LLC (now OldCarco) worked in collaboration with the US Treasury and Citibank to implement a supplier factoring and accounts receivable insurance program. We had numerous suppliers express interest in the program and initiated a dedicated team that worked diligently to enroll as many suppliers as possible prior to April 30, 2009. Sixty-seven suppliers were formally enrolled in the program and \$201 million in supplier payables were guaranteed and paid, post petition, per the program terms.
- (2) During the 363 sale process of transferring direct supplier purchase orders to Chrysler Group LLC (Newco) we "cured" them. This means substantially all outstanding accounts payable were paid to suppliers in addition to our good faith estimate of their other pre-petition claims. In a typical bankruptcy these amounts are characterized as unsecured debts and are usually only paid pennies on the dollar. (Suppliers not transferred to Newco were not "cured")
- (3) Chrysler has a Risk Management group within its purchasing organization that reviews requests for financial support for distressed suppliers. To date we have provided substantial financial support to over 30 distressed suppliers in 2009.

**7. If there are any additional points you wish to make—by way of elaborating upon your hearing testimony or responding to the testimony of the other witnesses — please do so.**

[Intentionally left blank]

**Questions from the Honorable Trent Franks, Ranking Member**

**1. Was Chrysler involved in the negotiation of the deal for 29 cents-on-the-dollar offered to Chrysler's secured lenders?**

Answer: Yes.

**2. If so, how could Chrysler offer such a poor deal to its secured creditors – especially compared to the UAW – when it knew it might have to rely on secured creditors for financing in the future?**

Answer: Chrysler LLC was heading toward bankruptcy and did not have the cash available to satisfy the demands of all secured creditors. The 29 cents was offered as a counter to the 18 cents they would have received under a liquidation

scenario. The first lien creditors would potentially have received less than \$1 billion under a liquidation analysis that showed a range of possible values. They voted overwhelmingly to support the 363 sale in exchange for \$2 billion in cash and proceeds from the estate under bankruptcy. We attempted to create the most favorable situation for all parties involved and minimize the necessary sacrifices.

- 3. Chrysler could have avoided a government bailout and the parade of horrors that has followed from it if only it had planned better in 2008 – like Ford did in 2006. Why did Chrysler management not plan better – particularly as the likely need for bankruptcy became clearer?**

Answer: Cerberus purchased Chrysler in a leveraged buyout and therefore substantially all U.S. collateral was pledged to lenders.

- 4. The Obama Administration now exercises ownership rights in Chrysler and law enforcement and regulatory duties tied to the Department of Justice, the SEC, the FTC, the EPA, and the Department of Transportation, just to name a few. What will Chrysler do to make sure that it does not gain an unfair competitive advantage from the federal government's conflicted role?**

Answer: The current US equity in Chrysler Group LLC is 9.85% which will be diluted to 8% when Fiat obtains more shares after the Class B events. Both Fiat and Chrysler Group would like to satisfy our debts to the US Treasury as soon as possible. The automotive industry remains one of the most heavily regulated industries in the US. We do not expect that the auto industry, including Chrysler, will become less regulated anytime soon.

- 5. If the airline companies came to you now and asked you what were the worst things and the most political things to which the President and the Auto Task Force subjected Chrysler since they became involved, what would you tell them?**

Answer: Throughout this process, members of the task force and personnel from U.S. Treasury played a key role in facilitating negotiations between all parties, primarily Old Carco, Fiat, the UAW, the CAW and the VEBA, Cerberus and Daimler AG as owners and second lien holders, and the first lien lenders. They also provided DIP financing for Chrysler's bankruptcy at a time when traditional financing was unavailable due to the credit crisis. The involvement of the U.S. Treasury and the Auto Task Force limited and targeted the expenditure of taxpayer dollars in connection with Old Carco and Chrysler Group and avoided a significant and potentially more costly disruption to the U.S. automotive industry and the U.S. economy.

**6. If the airlines asked you what things the President and the Auto Task Force had done that most harmed your ability to raise private capital or attract private ownership going forward, what would you tell them?**

Answer: Private capital was extremely scarce due to the global crisis in the credit markets. It was very clear to Chrysler and the outside independent bankruptcy consultants who we hired to work with us, that there was no funding available for dealers, consumers, and suppliers and that liquidation was the only other alternative. Government assistance was the only way forward.

**7. Do you think it's fair to the taxpayers for Chrysler to have accepted forgiveness of federal loans from the President and the Auto Task Force?**

Answer: No loans have been forgiven. The original loan is in Old Carco and the US government holds a claim as a secured creditor. Chrysler Group's debt to the U.S. Treasury is due in several different tranches. Payments are scheduled for 2011, 2016 and 2017. The interest payments on these loans are not immaterial to the company and our goal is to pay them back early, if possible. The U.S. Treasury also received, as additional consideration for the providing of financing, additional notes and PIK interest payable by Chrysler Group LLC and an equity share in Chrysler Group LLC. Chrysler Group also intends to pursue an IPO when appropriate, which represents additional upside value to the U.S. Government as an equity holder.

**8. As part of the House Oversight and Government Reform Committee's investigation, Chrysler was asked to produce documents, records and communications that would clarify the process used to identify dealerships to close and the extent of the Task Force's involvement in that process. Chrysler's responses were not timely and often incomplete. For example, in response to a request for production of all communications between Chrysler and the Task Force regarding public disclosure of the list of closed dealerships, Chrysler acknowledged such a communication occurred but provided no documents. Chrysler has also withheld documents from the Oversight and Government Reform Committee, citing confidentiality concerns.**

**a. How does Chrysler's resistance to the Committee's requests for information mesh with the President's pledge to hold his Administration to "a new standard of openness"?**

Answer: Chrysler Group believes it has fully complied with the requests it has received, consistent with the orders of the Bankruptcy Court.

**b. Did the Auto Task Force ask Chrysler not to comply with the Oversight and Government Reform Committee's or any other committee's requests?**

Answer: No.

**9. Why did Chrysler suppress evidence of offers for Viper before the bankruptcy court?**

Answer: Neither Old Carco nor Chrysler Group suppressed evidence of offers for Viper. See answer to question 3 below.

**Allegations of Wrongdoing in the Viper Sale**

**1. In a court filing, didn't Bob Nardelli state that it would be "extremely challenging" for Chrysler "to sell off select product lines" such as Jeep and Viper?**

Answer: Please see paragraph 18 of Mr. Nardelli's declaration, a copy of which is attached.

**2. Didn't Mr. Nardelli cite a lack of "purchaser interest" in response to the offering of Chrysler's Conner Avenue Viper manufacturing plant for \$10 million?**

Answer: Please see paragraph 18 of Mr. Nardelli's declaration, a copy of which is attached.

**3. Can you reconcile that statement with evidence that at least two bidders offered more than \$30 million for Viper prior to bankruptcy?**

Answer: Joseph Moch Jr. and Joseph Moch Sr. expressed an interest in the Viper business before Chrysler LLC ("Old Carco") filed for bankruptcy, and Old Carco and the Mochs had exchanged draft asset purchase agreements regarding Viper. However, that agreement was never finalized, and the parties never reached agreement on some key terms. In particular, the Mochs never agreed to provide proof of financial capability to complete the transaction (such as a commitment letter, or other standard and reasonable proof of funds), which Old Carco required. While other parties also expressed an interest in Viper before Old Carco filed for bankruptcy, none of them met Old Carco's requirements, and thus there were no qualified offers for the Viper business before Old Carco filed for bankruptcy.

**4. Some reports have the Viper plant being shuttered in December of this year. Others have the plant closing in two years, and still others have Vipers being produced indefinitely. What is the Auto Task Force's view on plans for Viper?**

Answer: The Auto Task Force is not involved in the day-to-day management decisions of Chrysler. Chrysler's Management Team recently announced that the plant would stop producing the current Viper SRT 10 in 2010. No decisions have been made with respect to a possible next model.

**5. Is Chrysler still accepting bids for Viper?**

Answer: Chrysler is not actively looking to sell the Viper business.

**6. Did the Auto Task Force advise Chrysler how to handle bids for Viper? If so, what did the Task Force suggest?**

Answer: The Auto Task Force did not advise Old Carco or Chrysler Group on how to handle bids for Viper.

**7. Did Chrysler have conversations or communications with any elected official about Viper?**

Answer: From time to time, Old Carco updated elected officials about all of its facilities, including the Conner Avenue facility where the Viper is assembled.

**8. Did Fiat impose as a condition of its purchase of Chrysler that the new company would cease production of Viper? If so, why was this not disclosed to the court during bankruptcy proceedings?**

Answer: No.

**9. Chrysler's responses to requests for information during the Oversight and Government Reform Committee's investigation into the Viper bidding process were incomplete and indicated a lack of a coherent plan. For example, on June 15, Chrysler lawyers met with Committee investigators and advised that it was too soon to ask Fiat what their plans were for the Viper plant. The very same day, Chrysler resumed production of the Dodge Viper, hailing the re-opening of the Viper assembly plant as an important milestone in Chrysler's restructuring.**

**a. Who is making the decisions about Viper at Chrysler?**

Answer: Ultimately, the Chrysler Group Management Team seeks Board approval for the Company's product plans.

**b. What is the source of the apparent confusion about the plans for Viper?**

Answer: Chrysler Group respectfully disagrees with the question's characterization of these events. Chrysler Group purchased the assets of



Old Carco on June 10, 2009, and has spent the last several months devising a business plan for the new company. On November 4, 2009, Chrysler Group announced its new business plan, including plans for Viper. See question 4 above.

**10. Isn't it true that Chrysler made public statements that the Dodge Viper model would be challenging to sell, and disclosed only one, \$5.5 million offer for it to the bankruptcy court?**

Answer: Please see answers to questions 1-3.

**11. Isn't it also true that Chrysler actually received a \$35 million offer to buy the Viper plant?**

Answer: Please see answer to question 3.

**12. Isn't it also true that Chrysler negotiated a contract with the \$35 million buyer and came close to completing the transaction?**

Answer: Please see answer to question 3.

**13. Did the Auto Task Force attempt to suppress the sale of Viper to reduce competition for Fiat, the buyer it recruited for Chrysler, in the super-car and sports car markets?**

Answer: No.

JONES DAY  
222 East 41st Street  
New York, New York 10017  
Telephone: (212) 326-3939  
Facsimile: (212) 755-7306  
Corinne Ball  
Veerle Roovers

JONES DAY  
North Point  
901 Lakeside Avenue  
Cleveland, Ohio 44114  
Telephone: (216) 586-3939  
Facsimile: (216) 579-0212  
David G. Heiman  
Robert W. Hamilton

JONES DAY  
1420 Peachtree Street, N.E.  
Suite 800  
Atlanta, Georgia 30309  
Telephone: (404) 521-3939  
Facsimile: (404) 581-8309  
Jeffrey B. Ellman

Proposed Attorneys for Debtors  
and Debtors in Possession

**UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK**

-----X	
In re	: Chapter 11
Chrysler LLC, <i>et al.</i> ,	: Case No. 09-50002 (AJG)
	: (Jointly Administered)
Debtors.	:
	:
-----X	

**DECLARATION OF ROBERT L. NARDELLI**

I, Robert L. Nardelli, make this declaration under 28 U.S.C. § 1746 and state:

1. I am the Chairman and Chief Executive Officer of Chrysler LLC (“Chrysler” or the “Company”), a position I have held since August 2007. In that capacity, I am familiar with the Company’s day-to-day operations, businesses, financial affairs and restructuring efforts.

2. I am authorized to submit this Declaration in support of Chrysler’s request that the Court approve the sale of assets (“Sale”) to Fiat Group S.p.A (“Fiat”). Except as otherwise indicated, all facts set forth in this Declaration are based upon my personal knowledge, my review of relevant documents, information supplied to me by other members of Chrysler’s management team or professionals retained by the Company, or my opinion based upon my experience and knowledge of the Company’s businesses and financial condition. If I were called upon to testify, I could and would testify competently to the facts set forth in this Declaration.

3. I understand that certain stakeholders (the “Objectors”) are challenging management’s decision to pursue the Sale transaction, insinuating, although never directly stating, that we should have done something else. Doing anything else in light of our precarious situation, however, would have been an unreasonable exercise of business judgment. We were burdened by enormous liabilities, our expenses were rapidly depleting our cash accounts and sales continued to plummet. We searched diligently for the financing we so desperately needed. No one would agree to provide Chrysler the billions of dollars vital to its survival; that is, until the U.S. Treasury (“UST”) agreed to do so.

4. The UST, as our lender, placed certain conditions on its willingness to lend billions of dollars to a suffering car company. The Objectors’ cast our acquiescence to those conditions as an abdication of our responsibilities to our stakeholders. It is just the

opposite. By securing this financing and pursuing this Sale, we have placed every stakeholder, including the secured lenders, in a position to maximize their return.

5. The Objectors speculate that they personally may have fared better if Chrysler liquidated. They seek to derail a Sale that will give life to NewCo, save thousands of jobs, avert further economic disaster and provide secured lenders a payout that, according to our experts' analyses, is higher than they would have otherwise received. They urge this Court to reject a Sale because they speculate that maybe, perhaps, they would have realized more through a liquidation. To my knowledge, they have submitted no studies, analyses or tests to support this supposition. We, on the other hand, relied on experts, our knowledge of this industry and our intimate knowledge of our own company.

6. The Objectors simply ignore the fact that the UST was the only lender willing to invest in us. As credit markets tightened and automotive sales deteriorated in the fall of 2008, Chrysler suffered a severe liquidity crisis. We were unable to obtain financing from banks or other traditional sources. As a result, and as a last resort, Chrysler approached the United States government for financial support. After extensive and highly publicized hearings, in which I participated, the UST loaned \$4 billion on January 2, 2009 under the Troubled Assets Relief Program ("TARP"), administered by the Office of Financial Stability. Pursuant to the terms of the TARP loan, Chrysler was required to submit a Long-Term Viability Plan to the U.S. Treasury by February 17, 2009.

7. We worked diligently on this plan and submitted it for consideration on February 17, 2009. The Viability Plan provided for three scenarios: (a) a standalone restructuring of Chrysler; (b) a Fiat alliance; and (c) a liquidation if neither the standalone plan nor the Fiat alliance could be achieved.

8. As outlined in the Long-Term Viability Plan, Chrysler's standalone option was dependent on substantial debt restructuring, targeted concessions from all constituents, and additional financing from the UST. The Long-Term Viability Plan also stressed that the standalone option would be viable only on a short or mid-term basis, and that Chrysler should continue to pursue strategic partnerships to achieve operational and financial viability in the long-term.

9. With the right mix of funding and concessions from other stakeholders, the standalone scenario may have proved viable, at least in the short term. Crucially, no one -- not a private source nor the government -- would agree to finance this scenario.

10. On March 30, 2009, the UST advised that it would lend no more money to Chrysler if we chose the standalone scenario. The UST would support only the Fiat alliance, assuming we could obtain significant concessions from key stakeholders. Chrysler was given thirty days to contract with Fiat and to obtain these concessions.

11. To meet this deadline, Chrysler devoted extensive resources pursuing the alliance and stakeholder concessions. Chrysler's management, including myself, worked every day, practically around the clock. Completing the transaction notably required a number of crucial elements. A new collective bargaining agreement was required between the United Auto Workers ("UAW") and Newco. Fiat and Chrysler needed to agree to the terms of their alliance. In addition, we negotiated with the UST for additional financing to support the transaction. Meetings with Fiat, the UST, the UAW, the Canadian Auto Workers, the VEBA, and the government of Canada were occurring on a daily basis, oftentimes late into the evening.

12. During this time we explained our business plan to the secured lenders, provided answers to their questions, and provided financial information and forecasts, among

other information. (The April 15, 2009 draft minutes of the Meeting of the Board of Managers, attached as Exhibit A, reflect these communications.) When it came to negotiations concerning their debt, however, the secured lenders demanded to negotiate directly with the UST, as memorialized in the March 29, 2009 draft minutes of the Meeting of the Board of Managers, attached as Exhibit B.

13. During this time Chrysler's Board of Managers met repeatedly with a singular objective: to best address the interests of all constituents. I presided over these meetings. At all times the Board and Chrysler's management were energetically engaged in the process. The members discussed Chrysler's restructuring efforts, including attempts to secure financing from other sources.

14. Aware of our responsibilities to various constituencies, throughout this process I shared with the UST and the Board my intention to not allow our cash balance to fall below an amount required to liquidate the Company, should it come to that. The April 15, 2009 draft minutes of the Meeting of the Board of Managers, attached as Exhibit A, provide that I "informed the Board that the Company had repeatedly discussed such preferred minimum cash level with both the First Lien Lenders and the UST . . ."

15. During those thirty days we achieved success on a number of fronts, securing the required concessions from almost all of the stakeholders. In the end, however, we were unable to convince a small minority that the Fiat alliance was in fact the best course of action. Accordingly, the Fiat alliance changed from an out-of-court transaction to a sale of assets to NewCo pursuant to section 363 of the Bankruptcy Code. Based upon the alternatives available – and the only other alternative was liquidation – the Sale presented the best opportunity for preserving and maximizing the value of Chrysler's assets and the return to the

various stakeholders. The Sale would strengthen Chrysler for the long-term, benefiting all constituents, including U.S. taxpayers, employees, creditors, dealers, suppliers and secured lenders. In the end, our sole aim was to benefit everyone.

16. I understand that the Objectors have criticized Chrysler's due diligence of Fiat. Such criticism reflects a fundamental misunderstanding of the identity of the parties and the nature of the transaction. Chrysler is not buying Fiat. If we were, we would have engaged in a granular analysis of Fiat's business. The objective of our April 2009 due diligence was simply to allow us to gain some comfort regarding the new owner of the assets about which we care deeply. We met with Fiat management, engaged in numerous discussions and reviewed various financial data. It was not as if Fiat was a stranger: we had been discussing a potential alliance with Fiat for months. Based on our familiarity with Fiat and the due diligence we conducted during April, Chrysler's management became comfortable with entrusting our precious assets to Fiat.

17. The Objectors apparently believe we should have pursued an alliance with GM. We tried that, diligently. GM, however, advised us in February 2009 that they were no longer interested in a transaction with us. By April 2009 we had signed an exclusivity agreement with Fiat, precluding our ability to return to GM. It would not have mattered, in my opinion, in light of GM's present situation. In any event, GM gave no indication that they wanted to reopen discussions.

18. Then there is the Objectors' mistaken notion that it would be a simple matter for us to sell off select product lines, such as Jeep, that might allow a recovery above \$2 billion. The Chrysler brand lines are, for the most part, not organized as separate manufacturing units or structured as stand-alone operations, making their sale extremely challenging.

Moreover, the market for such assets is extremely depressed at this time. For example, we recently offered for sale our entire Conner Avenue plant, the facility that manufactures the Dodge Vipers, for only \$10 million. We received no purchaser interest. And the recent efforts by other OEMs to sell stand-alone car lines, including Saturn, Opel, SAAB, and Hummer, provide additional evidence of the extremely depressed market for stand-alone automotive brands.

19. The fact is that the secured lenders, including the Objectors, will fare much better through the Sale than they would through a liquidation. There was never an attempt or an intention to harm the lenders. Just the opposite: I personally worked to obtain the highest amount possible for them. In fact, just before Chrysler filed bankruptcy, the UST considered offering more than \$2 billion to these lenders to achieve unanimous consent. In fact, I understand that, on April 29, 2009, the UST offered \$2.25 billion to the secured lenders but made it clear that this offer would be open for an hour only, and only if it received unanimous consent from the secured lenders. I understand that, while the secured lenders who are Objectors to the Sale agreed to accept this offer, unanimous consent was not obtained.

20. Based on my management team's expertise and business acumen, the work product of our advisors (which included a fairness opinion and liquidation analysis), and the notion and hope that Chrysler could continue and perhaps return to profitability, we chose the Sale over liquidation. While we all wish that customer demand would have increased drastically in time to provide us the liquidity we so desperately needed, it simply did not happen. Faced with the choices presented and the information before me, I am confident that approving the Sale was an exercise of sound business judgment.



I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

/s/ Robert L. Nardelli  
Robert L. Nardelli  
Chairman and Chief Executive Officer  
Chrysler LLC



RESPONSE TO POST-HEARING QUESTIONS FROM MICHAEL J. ROBINSON, VICE  
PRESIDENT AND GENERAL COUNSEL OF NORTH AMERICA, GENERAL MOTORS COMPANY

November 5, 2009

**Questions for the Record**  
**Subcommittee on Commercial and Administrative Law**  
**Hearing on the Ramifications of Auto Industry Bankruptcies, Part III**  
**July 22, 2009**

**Michael J. Robinson, Vice-President and General Counsel of North America, General Motors Company**

**Questions from the Honorable Steve Cohen, Chairman**

- 1. Greg Williams, an African-American former Chevrolet dealer, testified that General Motors will have "less than 20 African-American dealers left" after the dealership wind-down process is complete. What is your response?**

Throughout GM's bankruptcy process, we worked hard to try to ensure that we retained as many minority owned dealers as we could. As for African American dealers in particular, currently GM expects to have 30 African American dealer-operators, owning and running 36 dealerships businesses, when the dealer wind down process is complete. This number of African American dealers could increase over time as GM will continue with its efforts to expand the diversity in its dealer body. To that end, diversity candidates are included in the list of candidates which are sent requests for proposal for every "open " dealer location where GM is in the process of re-establishing dealer representation.

- 2. Please respond to the contention that a traditional Chapter 11 reorganization would have been sufficient for General Motors.**

The following response was developed by GM's bankruptcy counsel, Harvey Miller, who also testified at the July 22 hearing:

The essence of a traditional mega-chapter 11 case is liquidity in the form of debtor in possession (DIP) financing that would assure creditors and others that the debtor in possession will have the wherewithal to operate the debtor's business, as well as provide confidence for customers to deal with the business and buy its products. In the case of General Motors, there was no long-term DIP financing available, other than from the U.S. Treasury. The U.S. Treasury, as an existing secured creditor (\$19.4 billion) made it emphatically clear that it would not be amenable to any long-term DIP financing. Further, the uncertainty inherent in any traditional chapter 11 reorganization as to the outcome of the case would have adversely affected General Motor's sales and revenues. Any major contraction in revenues would have adversely affected the ability of the debtor in possession to continue operations.

Finally, in connection with DIP financing, the presence of an existing secured creditor that is the beneficiary of liens on substantially all of the assets of a debtor, generally, precludes the ability to obtain other financing. As a consequence, secured creditors are

able to impose conditions on a debtor as part of DIP financing as to the length of a chapter 11 case; the activities that may be pursued by a debtor in possession; the terms and conditions of a plan of reorganization; and, the prerogatives of management. In the case of General Motors, the U.S. Treasury was a secured creditor. As stated, there existed no source of funds to refinance the U.S. Treasury secured financing. No other party was available to satisfy the \$19.4 billion of outstanding secured debt and then provide liquidity for a traditional chapter 11 case. Further, there was no ability to existing precedent to in any way cram down the secured indebtedness held by the U.S. Treasury.

The purchase of an automobile or light truck is a major expenditure for most Americans. A lack of confidence as to the continued existence of General Motors and also as to the quality of products produced under a debtor in possession administration could have materially undermined a traditional chapter 11 with a resultant liquidation of the General Motor's business with systemic consequences to its suppliers, employees and the communities in which it operates its business.

The Bankruptcy Code is a complex statute. The processes that are part and parcel of the traditional chapter 11 case, including the appointment of a creditors' committee and, sometimes, multiple committees, as well as the surge in the formation of ad hoc committees of creditors and, sometimes, equity interest holders tends to slow down the process, increase administrative expenses, and doom the ability to rehabilitate and reorganize.

In that context, the use of the statutory process for dealing with sensitive and fragile assets was the most pragmatic approach to preserving going-concern value and the interests of all beneficiaries, including those of the Nation. It is fortunate that the Bankruptcy Code does enable the use of discretion on the part of bankruptcy courts to meet the needs to be served. The flexibility that is inherent in the bankruptcy process enables the preservation of going-concern values that might otherwise be lost in the drawn out and often litigious traditional chapter 11 mega cases, e.g. in re Delphi Corp. (Ch. 11 Case No. 05-44481 (RDD) (Bankr. S.D.N.Y. 2005))

3. **To the extent that you are able to, please respond to the contention that General Motors was under political pressure to make concessions to certain creditors that would not ordinarily be entitled to favored treatment in bankruptcy.**

I am unaware of any political pressure for GM to make concessions to creditors.

4. **Some critics of General Motors's reorganization contend that the General Motors Company will effectively be run by the federal government. In the times since the successful completion of the Section 363 asset sale transferring viable assets from the former General Motors Corporation to General Motors Company, has the Treasury Department, the Auto Task Force, or any other arm of the federal government attempted to dictate how General Motors Company should be run?**

During the bankruptcy of General Motors Corporation, GM worked closely with the Automotive Task Force to revise our operating plan and to identify and agree to the broad targets and overall components needed to create a viable GM. During that time and since GM emerged from bankruptcy, neither the Task Force, nor any federal agency, told us how to run our business or dictated the specific details of our plan. Rather, they exercised the due diligence as any purchaser of a business would. They questioned us and challenged us to ensure that we had a robust and viable plan for GM.

5. **In addition to the wind-down process, please outline any additional efforts that General Motors has undertaken to mitigate the economic harm suffered by its dealerships that were selected for termination.**

GM provided each dealership completely winding down its GM dealer operations with substantial financial assistance, generally 8 months of “rent support” based on the dealer’s operating report plus \$1,000 per new vehicles in the dealer’s stock at the end of May, 2009. The total amount of GM’s financial assistance is about \$600 million (the exact amount depends on the outcome of the potential sale of Hummer and Saab). In mid-July GM paid more than \$100 million of this amount to wind down dealers as called for in their agreements and just this week paid Saturn dealers approximately \$41 million as called for in their Deferred Termination Agreements. The remaining funds will be paid as the dealers wind down their operations. In addition, GM is taking these additional steps to support the dealers and their employees:

- a. **Wind down dealer activities:** Winding down dealerships may continue to sell their new vehicle inventories and service vehicles, and can do so, if they choose, through October 2010 when the dealer agreement expires. Dealers can still obtain “stock” new vehicles by dealer trading with other dealers. GM is also satisfying each bona fide sold customer order placed by dealers before the wind down agreement became effective.
- b. **Acceleration of wind down payments:** GM is working with individual dealers to satisfy their requests to accelerate receipt of the rest of the financial assistance GM agreed to provide the dealers when they completed their wind down. To date, about 300 wind down dealers have asked GM to accelerate the wind down process for the dealer agreement, choosing to cease those dealership operations now instead of waiting until October 2010 when their dealer agreements expire. About 160 of these dealerships have already actually completed the wind down of the dealer agreement. GM has agreed to pay these dealers, pursuant to the wind down agreement, the remaining 75% of their wind down financial assistance now as well. More of these early termination requests are coming in every day. GM is processing these requests and is prepared to promptly pay the amounts owed to those dealers under the terms of their wind down agreements with GM.
- c. **Placement assistance for dealer technicians:** GM has also agreed to provide assistance to technicians and if possible other employees working at dealerships to be wound down. GM is proud of the dealer technicians who service GM vehicles. Many of these technicians are highly trained and possess multiple technical certifications. Factory

trained individuals with these skills and credentials are highly sought after in the industry. GM shares concerns that these technicians may lose their current positions.

- d. **Ability to re-enter the same market:** If GM determines in the future that it needs to re-establish a new dealership in an area formerly served by a dealership that was wound down, GM will provide that dealer (and any other wound-down dealership in the area or other interested candidates) with the opportunity to submit a proposal to GM to establish that new dealership. GM would review all such proposals in line with its normal business procedures and select the proposal that it determined was the best one for that particular market.

**6. Please outline any efforts that General Motors has undertaken to mitigate the economic harm suffered by its suppliers as a result of its reorganization.**

Below are some of the many steps that GM took to support our suppliers:

- Provided ongoing transparency on status of business to our supply base prior to, during and after the chapter 11 restructuring;
  - Moved up June direct material supplier payment to end of May prior to chapter 11 filing to reduce the amount of supplier outstanding receivables at the time of the filing;
  - Paid all pre-petition claims of direct material / essential vendors in full;
  - Minimized the impact of the extended summer shutdown by having some suppliers start production early to provide earlier cashflows, at the cost of GM carrying higher inventory;
  - Provided liquidity and financial support to suppliers when necessary, such as in the case of American Axle;
  - Actively and successfully advocated for the implementation of the U.S. Treasury Supplier Support Program;
  - Informed suppliers of changes to vehicle production schedules as early as possible to allow them to prepare and adjust their businesses as early as possible;
  - Continued vehicle production through the chapter 11 process (unlike in the case of Chrysler which shut down all vehicle production);
  - Implemented revised supplier cost reduction suggestion program in late August (suppliers now receive half of cost savings associated with implementation of supplier suggestion); and
  - Moving to pay GM direct material suppliers on a weekly basis (from a monthly basis) for materials received by GM beginning Nov. 1, 2009. This enables both GM and suppliers to better manage their cash flow and reduces the need for suppliers to use their bank lines of credit to run their businesses.
7. **If there are any additional points you wish to make—by way of elaborating upon your hearing testimony or responding to the testimony of the other witnesses — please do so.**

I have no additional comments.

**Questions from the Honorable Trent Franks, Ranking Member**

**1. Has GM been able to identify a single, clear standard defining when the Auto Task Force will intervene in its affairs and when it will not?**

We have had a constructive dialogue with the government to make GM a more competitive company and we appreciate their support throughout the bankruptcy process. Clearly they have an interest in protecting the government's investment and taxpayer dollars and therefore it is obviously interested in the business and financial performance of the new company. However, we do not have any reason to believe, nor has it been our experience, that there is an interest in being involved in day to day business operations.

**2. If so, has the Auto Task Force consistently honored that standard?**

n/a

**3. Didn't the President claim that he didn't want to run GM and Chrysler?**

This question is more appropriately answered by referring to congressional testimony of Ron Bloom of the Auto Task Force:

From the beginning of this process, the President gave the Auto Task Force two clear directions regarding its approach to the auto restructurings. The first was to refrain from intervening in the day-to-day management of these companies. Our role has been to act as a potential investor of taxpayer resources, and as such we have not become involved in specific business decisions like where to open a new plant or which dealers to close. This is the job of management and while we have been engaged in dialogue and discussion about their approach, we have not substituted our judgment about specific decisions for theirs.

Second, the President was clear that he wanted us to behave in a commercial manner – that is to be sure that all stakeholders were treated fairly and received neither more nor less than they would have, simply because the government was involved.

**4. Isn't it nevertheless the case that President Obama made the decision to fire GM CEO Rick Wagoner?**

Administration officials requested that Mr. Wagoner step down as CEO of General Motors Corporation. Any more information on this decision should be obtained from the Auto Task Force.

**5. Didn't President Obama also make the decision to purge GM's board? If not, who did?**

The GM Board recognized for some time before March 30 that the Company's restructuring will likely cause significant changes in the stockholders of the Company and create the need for new directors with additional skills and experience. The Board worked to nominate a slate of directors, under the leadership of then interim-Chairman Kent Kresa that included a majority of new directors taking into account the addition of new directors, retirement and decisions by individual directors not to stand for re-election.

**6. Why did the President fire Rick Wagoner?**

- a. **Did Mr. Wagoner disagree over the direction in which the Auto Task Force wanted to take the company?**
- b. **Did Mr. Wagoner object to the deal the Auto Task force wanted to offer to the UAW? GM's bondholders? Other GM creditors?**
- c. **Were there other issues between Mr. Wagoner and the President or the Auto Task Force? If so, what were they?**

These questions are most appropriately directed to the Auto Task Force.

**7. Why did the President and the Auto Task Force seek to purge and reconstitute the GM board of directors?**

- a. **Did the purged board members disagree over the direction in which the Auto Task Force wanted to take the company?**
- b. **Did they object to the deal the Auto Task force wanted to offer to the UAW? GM's bondholders? Other GM creditors?**
- c. **Were there other issues between the board members and the President or the Auto Task Force? If so, what were they?**

These questions are most appropriately directed to the Auto Task Force.

**8. GM offered multiple restructuring plans to the Obama Administration, but the President and the Auto Task Force rejected them. GM must have thought those plans were economically viable, correct – otherwise, why would it have proposed them?**

GM worked to develop plans that would ensure the viability of the company. Each plan was based on assumptions of economic activity, vehicle sales and the overall economic health of the country. As the months progressed, economic conditions worsened significantly, creating the need for the additional and more aggressive restructuring of all aspects of the business and the Company.

**9. On what basis – political or economic – did the President and the Auto Task Force not find them viable?**

The Administration's viability determination can be found at:  
<http://www.financialstability.gov/docs/AIFP/GM-Viability-Assessment.pdf>

**10. Did the Administration even give you a full explanation?**

See the response to question 9.

**11. What is your opinion now of whether those plans were in fact economically viable?**

The plans were developed over a period of constantly changing and deteriorating economic conditions. We believe that the current plan is the best one to ensure the viability of the Company given the significant economic conditions, including level of auto sales, availability of credit, instability in the financial markets, etc.

**12. Which parties did worse and which did better under the rejected plans?**

- a. The UAW?
- b. Salaried employees?
- c. Manufacturing plants?
- d. Secured creditors?
- e. Unsecured bondholders?

The bankruptcy and restructuring of General Motors has impacted all stakeholders, and they have each sacrificed for the viability of the Company. A viable GM will benefit all of the stakeholders, as well as the nation. Questions about how each of the stakeholder groups would be affected under the developing viability plans would need to be directed to the stakeholders themselves.

**13. Was GM involved in the negotiation of the poor deal for its bondholders as compared to the UAW?**

As stated in the answer to question 12, all stakeholders, including bondholders, sacrificed in support of making the new General Motors Company viable. Prior to the bankruptcy of General Motors Corporation, the Corporation offered bondholders the opportunity to exchange their debt in GM Corporation for common stock of the Corporation, knowing that if not enough bondholders participated in the exchange, that the Corporation would be expected to seek bankruptcy protection. The bondholders also knew that they would receive less in bankruptcy than what the Corporation offered in the exchange offer, and that they may receive no consideration at all. Ultimately, the conditions of the bond



exchange offer were not met and the bankruptcy filing took place. We disagree with the characterization that the bondholders received a poor deal.

**14. If so, how could GM offer such a comparatively poor deal to its bondholders, when it knew it would have to issue corporate bonds in the future?**

n/a

**15. GM could have avoided a government bailout and the parade of horrors that has followed from it if only it had planned better in 2008 – like Ford did in 2006. Why did GM management not plan better – particularly as the likely need for bankruptcy became clearer?**

Over the years, General Motors Corporation had been working to transform its business, renegotiating labor and benefit contracts with the UAW, rationalizing the dealer network, strengthening the supply base, selling non-core assets. GM had raised a significant amount of liquidity ahead of the credit crisis. Ford Motor raised more via a revolver in 2006 and had a stronger balance sheet going into the crisis. GM did more asset sales (including selling its interest in GMAC for \$7.4B in 2006 and Allison Transmission for \$5.6B in 2007) and individual secured and unsecured financings leading up to our 2007 labor negotiations.

GM's operating results and balance sheet were weak and we had to make significant contributions over the years to fund our pension and retiree health care liabilities (over \$100B). Our funding actions supported these capital needs, but could not also support the working capital and restructuring costs associated with the industry falling from selling over 17 million units annually in the US to less than 10 million units. No one in the industry was planning on that basis.

When we began to see auto industry volumes deteriorate, we sequentially tried to raise debt and equity in the capital markets but the markets were shut down. We also attempted to sell assets but there were limited takers due again to the capital markets and buyers lack of ability to get financing. We also tried to do a debt-equity exchange but were unsuccessful.

**16. The Obama Administration now exercises majority ownership rights in GM and law enforcement and regulatory duties tied to the Department of Justice, the SEC, the FTC, the EPA, and the Department of Transportation, just to name a few. What will GM do to make sure that it does not gain an unfair competitive advantage from the federal government's conflicted role?**

It is our experience and view that the federal government as a shareholder in the Company is not using other federal resources to provide any unfair competitive advantage to the Company.

**17. If the airline companies came to you now and asked you what were the worst things and the most political things to which the President and the Auto Task Force subjected GM since it became involved, what would you tell them?**

We have had a constructive dialogue with the government to make GM a more competitive company and appreciate their support throughout the bankruptcy process. Clearly they have an interest in protecting the government's investment and taxpayer dollars and therefore it is obviously interested in the business and financial performance of the new company. However, we do not have any reason to believe nor has our experience indicated that there is an interest in being involved in day to day business operations or in politicizing the operations of the Company.

**18. If the airlines asked you what things the President and the Auto Task Force had done that most harmed your ability to raise private capital or attract private ownership going forward, what would you tell them?**

The Bush and Obama Administration, as well as the Auto Task Force, gave GM a rare second chance for which we are very grateful. General Motors Company is an entirely new Company built from the strongest elements of the "old GM" – the strongest brands, the core plants and other hard assets that those brands rely on, the supplier relationships and contracts necessary to keep the business moving, and the equity in GM's domestic and global subsidiaries.

Future bondholders and stockholders will benefit from investing in a company with a clean balance sheet, a competitive cost structure, lower breakeven point, a streamlined and stronger dealer network, and a flatter, leaner and more focused organizational structure.

GM is very appreciative of the support provided by the stakeholders through the transformation process. Though the new Company will not initially be publicly traded, we will be transparent in our financial and other reporting to further strengthen trust and confidence. We expect to take the Company public again as soon as practical, starting in 2010, and to repay our government loans as soon as possible. We are required to pay off the loans by 2015, but our goal is to repay them much sooner.

**Do you think it's fair to the taxpayers for GM to have accepted forgiveness of federal loans from the President and the Auto Task Force?**

As stated in the answer to question 18, GM is very appreciative of the support provided by the stakeholders through the transformation process. Though the new Company will not initially be publicly traded, we will be transparent in our financial and other reporting to further strengthen trust and confidence. We expect to take the Company public again as soon as practical, starting in 2010, and to repay our government loans as soon as possible. We are required to pay off the loans by 2015, but our goal is to repay them much sooner.



RESPONSE TO POST-HEARING QUESTIONS FROM HARVEY R. MILLER,  
PARTNER, WEIL, GOTSHAL & MANGES LLP

Questions for the Record  
Subcommittee on Commercial and Administrative Law  
Hearing on the Ramifications of Auto Industry Bankruptcies, Part III  
July 22, 2009

Harvey R. Miller, Partner, Weil, Gotshal & Manges LLP

Questions from the Honorable Steve Cohen, Chairman

1. **Greg Williams, an African-American former Chevrolet dealer, testified that General Motors will have “less than 20 African-American dealers left” after the dealership wind-down process is complete. What is your response?**

I defer to General Motors in respect of this question. As an attorney for General Motors, I did not participate in the selection of individual dealers subject to the wind-down process.

2. **Please respond to the contention that a traditional Chapter 11 reorganization would have been sufficient for General Motors.**

The essence of a traditional mega-chapter 11 case is liquidity in the form of debtor in possession (DIP) financing that would assure creditors and others that the debtor in possession will have the wherewithal to operate the debtor's business, as well as provide confidence for customers to deal with the business and buy its products. In the case of General Motors, there was no long-term DIP financing available, other than from the U.S. Treasury. The U.S. Treasury, as an existing secured creditor (\$19.4 billion) made it emphatically clear that it would not be amenable to any long-term DIP financing. Further, the uncertainty inherent in any traditional chapter 11 reorganization as to the outcome of the case would have adversely affected General Motor's sales and revenues. Any major contraction in revenues would have adversely affected the ability of the debtor in possession to continue operations.

Finally, in connection with DIP financing, the presence of an existing secured creditor that is the beneficiary of liens on substantially all of the assets of a debtor, generally, precludes the ability to obtain other financing. As a consequence, secured creditors are able to impose conditions on a debtor as part of DIP financing as to the length of a chapter 11 case; the activities that may be pursued by a debtor in possession; the terms and conditions of a plan of reorganization; and, the prerogatives of management. In the case of General Motors, the U.S. Treasury was a secured creditor. As stated, there existed no source of funds to refinance the U.S. Treasury secured financing. No other party was available to satisfy the \$19.4 billion of outstanding secured debt and then provide liquidity for a traditional chapter 11 case. Further, there was no ability to existing precedent to in any way cram down the secured indebtedness held by the U.S. Treasury.

The purchase of an automobile or light truck is a major expenditure for most Americans. A lack of confidence as to the continued existence of General Motors and also as to the quality of products produced under a debtor in possession administration could have materially undermined a traditional chapter 11 with a resultant liquidation of the General Motor's business with systemic consequences to its suppliers, employees and the communities in which it operates its business.

The Bankruptcy Code is a complex statute. The processes that are part and parcel of the traditional chapter 11 case, including the appointment of a creditors' committee and, sometimes, multiple committees, as well as the surge in the formation of ad hoc committees of creditors and, sometimes, equity interest holders tends to slow down the process, increase administrative expenses, and doom the ability to rehabilitate and reorganize.

In that context, the use of the statutory process for dealing with sensitive and fragile assets was the most pragmatic approach to preserving going-concern value and the interests of all beneficiaries, including those of the Nation. It is fortunate that the Bankruptcy Code does enable the use of discretion on the part of bankruptcy courts to meet the needs to be served. The flexibility that is inherent in the bankruptcy process enables the preservation of going-concern values that might otherwise be lost in the drawn out and often litigious traditional chapter 11 mega cases, e.g. in re Delphi Corp. (Ch. 11 Case No. 05-44481 (RDD) (Bankr. S.D.N.Y. 2005))

3. **To the extent that you are able to, please respond to the contention that General Motors was under political pressure to make concessions to certain creditors that would not ordinarily be entitled to favored treatment in bankruptcy.**

As attorney for General Motors, I was actively involved in the negotiations with the U.S. Treasury and other parties in interest. During my participation, I was not aware of any political pressure imposed upon General Motors to make particular concessions to any group or class of creditor. In terms of an on-going New GM, constituencies such as the UAW and others negotiated directly with the U.S. Treasury as the sponsor of the purchaser of substantially all of the assets of General Motors.

4. **Some critics of General Motors's reorganization contend that the General Motors Company will effectively be run by the federal government. In the times since the successful completion of the Section 363 asset sale transferring viable assets from the former General Motors Corporation to General Motors Company, has the Treasury Department, the Auto Task Force, or any other arm of the federal government attempted to dictate how General Motors Company should be run?**

To the best of my knowledge, information and belief, no arm of the federal government "attempted to dictate how General Motors Company should be run." The Automobile Task Force did work closely with General Motors' management in a manner similar to that of secured creditors in traditional debtor/creditor relationships, analyzing and reviewing business and financial plans and commenting upon those plans. Those

activities fall generally under the characterization of due diligence and creditor evaluation of risk.

5. **In addition to the wind-down process, please outline any additional efforts that General Motors has undertaken to mitigate the economic harm suffered by its dealerships that were selected for termination.**

I defer to General Motors in connection with this question.

6. **Please outline any efforts that General Motors has undertaken to mitigate the economic harm suffered by its suppliers as a result of its reorganization.**

I defer to General Motors in connection with this question.

7. **If there are any additional points you wish to make—by way of elaborating upon your hearing testimony or responding to the testimony of the other witnesses — please do so.**

I have no additional comments.

**Questions from the Honorable Trent Franks, Ranking Member**

1. **Has GM been able to identify a single, clear standard defining when the Auto Task Force will intervene in its affairs and when it will not?**

I defer to General Motors in connection with this question. However, I do add that in all of the negotiations with the representatives of the U.S. Treasury as to the terms and conditions of sale and the DIP financing, at all times such representatives made it abundantly clear that the Auto Task Force and the federal government did not intend to intervene in the affairs of New GM or to direct it as to how to operate and manage its business. Indeed, such representatives often repeated that notwithstanding the significant equity interest ownership that the U.S. Treasury would hold, it did not intend to be involved in corporate governance and would be looking forward to an initial public offering of such equity interests.

2. **If so, has the Auto Task Force consistently honored that standard?**

I defer to General Motors in connection with this question.

3. **Didn't the President claim that he didn't want to run GM and Chrysler?**

I defer to General Motors in connection with this question.

4. **Isn't it nevertheless the case that President Obama made the decision to fire GM CEO Rick Wagoner?**

I do not have any knowledge that the decision to request Mr. Wagoner to step down as General Motors' Chairman and CEO was made by President Obama. Mr. Steven Rattner, a senior member of the Auto Task Force, has stated publicly that he is the person who on March 27, 2009 advised Mr. Wagoner that it would be best if he stepped aside as he had previously "graciously offered" to do.

**5. Didn't President Obama also make the decision to purge GM's board? If not, who did?**

I have no personal knowledge that President Obama made the decision "to purge GM's board." I defer to General Motors in connection with this question. I do note that Mr. Rattner has publicly stated that the GM board of directors needed "shuffling."

**6. Why did the President fire Rick Wagoner?**

I defer to the Auto Task Force in connection with this question.

- a. **Did Mr. Wagoner disagree over the direction in which the Auto Task Force wanted to take the company?**
- b. **Did Mr. Wagoner object to the deal the Auto Task force wanted to offer to the UAW? GM's bondholders? Other GM creditors?**
- c. **Were there other issues between Mr. Wagoner and the President or the Auto Task Force? If so, what were they?\_**

**7. Why did the President and the Auto Task Force seek to purge and reconstitute the GM board of directors?**

I defer to the Auto Task Force in connection with this question.

- a. **Did the purged board members disagree over the direction in which the Auto Task Force wanted to take the company?**
- b. **Did they object to the deal the Auto Task force wanted to offer to the UAW? GM's bondholders? Other GM creditors?**
- c. **Were there other issues between the board members and the President or the Auto Task Force? If so, what were they?**

**8. GM offered multiple restructuring plans to the Obama Administration, but the President and the Auto Task Force rejected them. GM must have thought those plans were economically viable, correct – otherwise, why would it have proposed them?**

I defer to General Motors in connection with this question.

**9. On what basis – political or economic – did the President and the Auto Task Force not find them viable?**

I defer to the Auto Task Force in connection with this question.

**10. Did the Administration even give you a full explanation?**

No

**11. What is your opinion now of whether those plans were in fact economically viable?**

I defer to General Motors in connection with this question.

**12. Which parties did worse and which did better under the rejected plans?**

I defer to General Motors in connection with this question.

- a. The UAW?
- b. Salaried employees?
- c. Manufacturing plants?
- d. Secured creditors?
- e. Unsecured bondholders?

**13. Was GM involved in the negotiation of the poor deal for its bondholders as compared to the UAW?**

I defer to General Motors in connection with this question.

**14. If so, how could GM offer such a comparatively poor deal to its bondholders, when it knew it would have to issue corporate bonds in the future?**

I defer to General Motors in connection with this question.

**15. GM could have avoided a government bailout and the parade of horrors that has followed from it if only it had planned better in 2008 – like Ford did in 2006. Why did GM management not plan better – particularly as the likely need for bankruptcy became clearer?**

I defer to General Motors in connection with this question.

**16. The Obama Administration now exercises majority ownership rights in GM and law enforcement and regulatory duties tied to the Department of Justice, the SEC, the FTC, the EPA, and the Department of Transportation, just to name a few. What will GM do to make sure that it does not gain an unfair competitive advantage from the federal government's conflicted role?**

I defer to General Motors in connection with this question.

**17. If the airline companies came to you now and asked you what were the worst things and the most political things to which the President and the Auto Task Force subjected GM since it became involved, what would you tell them?**

I would explain to the airline companies the nature of restructuring and the complications that are inherent in having a single, extraordinarily large secured creditor holding liens and security interest in all of the assets of the particular company and the consequences flowing from that position. I would equate the position of the U.S. Treasury to that of any significantly large secured creditor such as JPMorgan Chase, Goldman Sachs or, indeed, a large hedge fund. In that comparison, I might very well emphasize that unlike certain commercial secured lenders, one advantage that did exist in connection with the General Motors' chapter 11 case was the announced reservation on the part of the Auto Task Force and the federal government not to become involved in the corporate governance of the New GM.

As to other aspects of this question, I defer to General Motors.

**18. If the airlines asked you what things the President and the Auto Task Force had done that most harmed your ability to raise private capital or attract private ownership going forward, what would you tell them?**

I defer to General Motors in connection with this question.

**Do you think it's fair to the taxpayers for GM to have accepted forgiveness of federal loans from the President and the Auto Task Force?**

I believe that the Nation faced a substantial risk of systemic consequences from a liquidation of General Motors that would have adversely affected the national economy and exacerbated the difficulties that resulted from the collapse of Lehman Brothers, that included a crisis of confidence, a seizing up of the markets, a credit crunch and a flight to quality with concomitant contraction of consumer spending. In the then state of the economy, the conflagration ignited by the collapse of Lehman Brothers would have been significantly fueled and enlarged to the prejudice of the Nation's best interest.

As to this question, I likewise defer to General Motors.





RESPONSE TO POST-HEARING QUESTIONS FROM DOUGLAS G. BAIRD, HARRY A. BIGELOW DISTINGUISHED SERVICE PROFESSOR OF LAW, UNIVERSITY OF CHICAGO LAW SCHOOL

**Questions for the Record**  
**Subcommittee on Commercial and Administrative Law**  
**Hearing on the Ramifications of Auto Industry Bankruptcies, Part III**  
**July 22, 2009**

**Douglas G. Baird, Harry A. Bigelow Distinguished Service Professor of Law, University of Chicago Law School**

**Questions from the Honorable Steve Cohen, Chairman**

1. **Should the Bankruptcy Code be refined to better guard against the concerns that you raise with respect to the Section 363 asset sales in the General Motors and Chrysler bankruptcy cases? If so, what specific steps would you recommend that Congress take?**

As a general matter, a sale under section 363(b) should not take place without an open auction that ensures that the assets are being sold for "top dollar." *See* Bank of America v. 203 N. LaSalle Street Partnership, 526 U.S. 434 (1999) (emphasizing the need for market benchmarks in the context of plan confirmation). It is possible that a set of practices will evolve in the bankruptcy courts or local rules will be put in place that will prevent "fire sales." Such a development would make legislation unnecessary. Hence, I believe legislative action premature. If legislative reform is necessary, the changes should ensure that a section 363(b) sale is an open process in which assets are sold for their market value.

2. **Please identify any other cases involving Section 363 asset sales that give you pause with respect to the sale procedures used.**

There is a recent empirical study that suggests that sales are not yielding top dollar. *See* Kenneth M. Ayotte & Edward R. Morrison, *Creditor Control and Conflict* in Chapter 11, *J. Legal Analysis* (forthcoming 2009). Nevertheless, I believe bankruptcy judges are doing a good job given the constraints under which they are operating. The problem they often face comes from the control that the debtor-in-possession lender (someone who is often the senior secured creditor) is able to exercise. The DIP lender conditions financing on a quick sale, sometimes in just two or three weeks. Without financing, the debtor may not have the resources to keep operating otherwise and alternative sources of DIP financing may not be available. Judges are reluctant to insist on a fully open auction procedure if doing so jeopardizes the DIP financing and puts the survival of the firm at risk. They push back, but are reluctant to push back too hard. Control in the hands of a secured creditor is not inherently problematic if in fact the value of the business is less than the amount the secured creditor is owed, but determining this at the outset of the case is sometimes difficult.

3. **In response to your suggestion that tort claims receive a super-priority lien, Harvey Miller testified that “if you create enough super-priority liens, there can never be a bankruptcy reorganization, because you will never be able to sustain the cost of that restructuring process.” How do you respond?**

The obligation to pay tort victims first will affect the distribution of the firm’s assets, but not the firm’s ability to reorganize. While the costs of adjudicating tort liability may be substantial, these are costs that exist outside of bankruptcy, as well as inside. In the extreme case, superpriority tort liens may themselves exceed the value of the firm, but this means only that the costs of administering the bankruptcy will be borne by the tort victims. But the process can be administered even in these circumstances. If any changes were required in the Bankruptcy Code to accommodate superpriority tort liens, they would be modest.

The crucial issue here is a matter that is not properly one connected to bankruptcy law at all: ensuring that tort liability is sensibly defined in the first instance. Tort law should hold firms liable only for acts that impose unreasonable costs on others. If it does only this, it will not limit desirable investments. Investors will ensure that firms take sensible precautions, and they will adjust the terms of their investments to take account of potential tort liability. If tort liability is not sensibly defined and deters behavior on the part of firms that is socially desirable, then, of course, granting tort liability a superpriority will make a bad situation worse.

4. **With respect to how the Bankruptcy Code deals with product liability claims arising from defects in products that a debtor manufactured prior to its bankruptcy filing, you testified that the Bankruptcy Code “doesn’t deal well with them now” but that “there are proposals to deal with this” issue. Please describe what these proposals are and which among them you believe would be the best approach.**

When a company manufactures a product that will produce harm to as-yet unidentified people in the future, current law is unclear whether these future harms give rise to a claim that can be recognized in bankruptcy today. I believe that the definition of “claim” should be expansive. Future victims should be represented by a guardian ad litem. A fund should be established in the bankruptcy that is available to future victims when their claims arise. The fund should have assets sufficient to ensure that they receive the same pro rata share of the firm’s assets as they would receive as if their claims existed at the time of the bankruptcy.

This approach ensures both that these tort victims are paid to the extent assets are available to satisfy them and that the firm can be reorganized successfully and operate in the future free of the burden of its past mistakes. The approach adopted by Congress after Manville for asbestos cases more or less followed this general idea. This approach has not been successful in asbestos cases, but not because of any deficiencies in the basic idea. The devil is always in the details. But alternative proposals have been put forward that are sound. The one put forward by the National Bankruptcy Conference on the treatment of mass torts in bankruptcy provides a sensible starting place.

5. **If there are any additional points you wish to make—by way of elaborating upon your hearing testimony or responding to the testimony of the other witnesses—please do so.**

**Questions from the Honorable Trent Franks, Ranking Member**

1. **How deep is your concern that Chapter 11 – and particularly section 363 – can lead to the undervaluation of assets in bankruptcy?**

My concern lies not so much with the outcome of GM and Chrysler, but rather that they may foreshadow future problems that arise when the bankruptcy judge is under pressure to do sales quickly without ensuring that there is a genuine open auction. Empirical evidence exists that these problems can arise even when the government is not involved and the party pushing for the sale are the senior secured lenders who exercise control over the debtor because of the influence they have on the debtor's access to DIP financing and use of cash collateral. See Kenneth M. Ayotte & Edward R. Morrison, *Creditor Control and Conflict in Chapter 11*, J. Legal Analysis (forthcoming 2009).

2. **What evidence have you seen that the assets in either GM's or Chrysler's bankruptcy were undervalued?**

There is no direct evidence that assets were undervalued in either GM or Chrysler. The debtor claimed that the firm had been thoroughly shopped before bankruptcy and that it had failed to find buyers other than Fiat. Moreover, the opponents of the sale had the chance to put on evidence that the firm was undervalued and did not do so. But the value of the assets was never put to a market test in bankruptcy itself.

In *Chrysler*, the only bids that could be entertained either required the assumption of collective bargaining or VEBA obligations or had to be approved by the debtor after consulting with the UAW. It may well be that no one would have come forward to bid for Chrysler's assets without assuming the VEBA obligations and offering more than \$2 billion, but the process was flawed because no one was given the opportunity to do so.

Without open bidding, we cannot know whether someone would have been willing to pay more than \$2 billion for Chrysler. Given the size of the government's secured claim in GM and its right to priority, it is less likely the assets were undervalued by so much that it actually compromised the rights of the general creditors.

If the practice of locking in terms is extended to other situations, where there may be a greater likelihood of other bidders surfacing at higher prices if they can modify the terms of the transaction, it becomes even more pernicious.

**3. Who benefitted from the undervaluation and who lost?**

The only ones who may have lost (and who have a right to complain) in *Chrysler* were the secured bondholders who opposed the sale. Whether they lost is not clear, as they would have lost only if an open auction would have generated a liquidating bid in excess of \$2 billion. As it is unlikely that the assets were worth enough to pay secured creditors in full in *Chrysler*, unsecured creditors probably did not lose as a result of the speeding sale. Some unsecured creditors gained to the extent that their claims were assumed by the buyer.

If the government was committed to keeping the firms intact with the collective bargaining agreement and the VEBA in place and if the bankruptcy allowed it to obtain these assets at a lower price, then the government benefitted as a result of an undervaluation.

It is possible that the secured creditors might have received more than \$2 billion in a liquidation (contrary to the testimony of Chrysler's expert) in which the VEBA claims were not paid. It is also possible at the same time that the cost to the government of keeping Chrysler alive and paying the VEBA claims caused them to pay more than the firm was worth as a going concern. In other words, it is possible both that the government paid too much and the secured creditors received too little.

**4. Were the taxpayers among the losers?**

Taxpayers may lose substantial amounts as a result of the automobile bailouts, but only because the government is committing to running the businesses as going concerns in a way that may not maximize their value. This policy decision to rescue the companies and protect the jobs of workers and benefits to retirees does not implicate bankruptcy law.

**5. What steps could have been taken under the existing Bankruptcy Code to avoid undervaluation in these cases?**

The judges could have done more to insist on an open auction in which the form of the bids was not as constrained. Bidding procedures that limit the form of the bid and the use to which the assets must be put are not procedures that will yield top dollar. If no bidder appeared, the outcome would have been the same. But if another bidder appeared, the secured creditors might have received the value of their collateral. This outcome, however, might have required directly confronting the policy question implicit in the Administration's decision to rescue Chrysler. There might have been a liquidation of Chrysler at a higher value than the Fiat deal realized for the estate, but it might well have sacrificed the continuation of Chrysler as a going concern and the payment of the VEBA and other assumed liabilities.

**6. What revisions to the Bankruptcy Code do you recommend to keep these problems from recurring?**

It is possible that a set of practices will evolve in the bankruptcy courts or local rules will be put in place that will prevent “fire sales.” Such a development would make legislation unnecessary. Hence, I believe legislative action premature. If legislative reform is necessary, the changes should ensure that a section 363(b) sale is an open process in which assets are sold for their market value.

**7. Your written testimony suggests that the Bankruptcy Code could better protect the rights of all stakeholders to receive fairer distributions of the proceeds of a section 363 sale.**

**a. Is there anything in the current Code that prevented the Auto Task Force from assuring fairer protection of secured creditors’ rights in the Chrysler case?**

Nothing in the Bankruptcy Code prevented the judge from implementing a sales process that was more open. If Chrysler’s experts were correct that no one would top the government’s bid of \$2 billion, the government would lose nothing by opening up the process as long as Fiat would not have walked away from the deal. No other bidders would have appeared, and the Chapter 11 would have taken only a few weeks longer.

**b. Are there specific revisions to the Code that you would recommend to assure that priority creditors like these receive fairer treatment in connection with section 363 sales?**

I believe that legislative reform is premature and that the bankruptcy courts should be given a chance to develop sensible procedures on their own.

**8. In the Delphi bankruptcy, the Auto Task Force forced out existing debtor-in-possession financiers in favor of Platinum Equity. The existing DIP financiers got as little as 20 cents-on-the-dollar in return for their investment. Do you believe that the Auto Task Force’s actions in the Delphi case may chill future, private DIP lending?**

The bankruptcy judge in *Delphi* prevented auto task force, GM, and Platinum Equity from forcing out the DIP lenders and compromising their rights. As a result of the judge’s insistence on respecting the DIP lenders’ rights and opening up what had been proposed to be a closed auction, Delphi’s DIP lenders ultimately competed with the joint offer by Platinum and GM by bidding their claims as a “credit bid.” The DIP lenders ended up winning the auction and purchased substantially all of the assets of the firm other than those proposed to be purchased by GM under the Platinum transaction, which were ultimately purchased by GM. The DIP lenders will likely incur substantial losses, but those losses are likely to be far smaller than the losses they would have incurred had the Platinum transaction been allowed to be the only game in town. In fact, it has been reported that the trading prices of the junior DIP loans rose substantially as a result of the

successful credit bid. The open auction accordingly served to minimize the losses resulting from the decline in the value of Delphi over the course of its Chapter 11 due to market conditions. These losses were significantly less than those that would have occurred had the private transaction originally supported by the government gone through.

**9. If it does, could that make airline bankruptcies or other potential major bankruptcies more difficult to sustain in Chapter 11?**

*Delphi* illustrates the virtues of having a strong and independent bankruptcy bench that ensures that square corners are cut in every bankruptcy, even when the federal government is a significant player. If other judge do not follow this example, DIP lending could be chilled and future bankruptcies could become harder to accomplish. This chilling effect is one of the risks that the precedent of using less open procedures in cases like *Chrysler* creates.

**10. If so, won't the choices then be only federal bailouts or liquidation of these major companies?**

Government intervention in the marketplace, for whatever reason, should respect the reasonable expectations of investors. DIP financing, like any other source of credit, requires confidence on the part of investors that contract rights and property rights will be scrupulously respected. A process such as Chapter 11 that embraces the absolute priority rule and open competitive bidding if the estate must be sold and that is built upon a strong and independent judiciary is distinctly to be preferred to any alternative that fails to respect the rights of investors.

**11. What specific revisions to the Bankruptcy Code would you prescribe to better protect auto dealers and other franchise holders protected by state franchise laws?**

The protections appropriate for automobile franchisees are not in the first instance a question of bankruptcy law. The distinct bankruptcy question is whether the need to reorganize a firm trumps the protections that these franchisees would otherwise enjoy. Increasing the protections for franchisees necessarily limits the ability of a firm to survive in a marketplace in which competitors have more efficient ways to distribute their products. Exactly how this balance should be struck is a policy question over which I claim no special competence.

**12. What specific revisions to the Bankruptcy Code would you propose to better prevent *sub rosa* plans or "sham sales" under section 363?**

If a reform were necessary, it should ensure that the form of the bid does not dictate the distribution of the assets. Whatever is received in a section 363 sales should be allocated according to the absolute priority rule. A bidder sometimes may assume obligations of the firm (perhaps because a prepetition creditor is critical to the ongoing operations of the

business), but these commitments should not be counted as part of the purchase price when assessing the bid against competing ones.

In the Second Circuit's decision in *Chrysler*, the court accepted the idea that the assumed liabilities were not being paid with estate assets. By doing so, the court was able to reach the conclusion that the assumption of liabilities did not dictate the terms of a plan. But the Court's conclusion is only true if in fact no one would have paid more for the assets if the liabilities were not assumed. If someone would have paid more, the left-behind creditors might have been better off with an alternative transaction. Without an open auction, we can never know the answer to this question. For this reason, there is an even greater need for opening the process when liabilities are to be assumed by the buyer.



RESPONSE TO POST-HEARING QUESTIONS FROM DANIEL J. IKENSON, ASSOCIATE  
DIRECTOR, CENTER FOR TRADE POLICY STUDIES, CATO INSTITUTE

**Answers of Daniel J. Ikenson to  
Questions for the Record  
Subcommittee on Commercial and Administrative Law  
Hearing on the Ramifications of Auto Industry Bankruptcies, Part III  
July 22, 2009**

**Daniel J. Ikenson, Associate Director, Center for Trade Policy Studies, Cato Institute**

**Questions from the Honorable Trent Franks, Ranking Member**

*Recovery of the taxpayers' investment*

**1. In your estimation, what is the likelihood that the U.S. taxpayers will ever be able to recover the investment made on their behalf in GM and Chrysler?**

I believe it is highly unlikely that taxpayers will fully recover their coerced investments in Chrysler and GM. In fact, Chrysler already announced that it will not repay the nearly \$4 billion "bridge loan" made to it from the TARP in January 2009. As to the U.S. taxpayers' equity stake in Chrysler, recovery depends on the performance of the company, which doesn't seem very promising from industry reports.

With respect to General Motors, CEO Ed Whittacre recently announced plans to pay back the debt portion of the taxpayers' "investment." That amounts to \$6.9 billion out of \$52 billion, leaving \$45 billion in taxpayer equity, which has been ordained by the bankruptcy court to be worth 60 percent of the company. In the world of mathematics, \$45 billion is 60 percent of \$75 billion, a figure that is 25 percent greater than GM's record-high valuation (market capitalization) of \$60 billion in the year 2000. At that time, Americans were purchasing 16 million vehicles per year, whereas in 2009 and 2010, annual sales figures are in the neighborhood of 10 to 11 million units. Market conditions are highly unlikely to be hospitable enough (even considering fast-growing markets in developing countries) to support a General Motors valued at \$75 billion.

But even if GM's profits were to surge in the years ahead (an unlikely scenario for so many reasons, including the fact that the company is compelled by law to produce and sell more low-profit, high mileage vehicles to comply with tighter CAFÉ standards – a market segment in which the company has never been competitive), the specter of its largest shareholder liquidating 60 percent of the company's shares will have a systemic, depressing impact on the value of GM shares. Whereas some common share investors might be allured by the "safety" of investing in a company that is "too big to fail," others will be deterred by the fact that stock prices will be continuously suppressed and depressed to reflect GM's largest shareholder's need to liquidate.

**2. How likely is it that the events that have taken place so far in these bankruptcies – particularly concerning the Obama Administration's disregard for contract rights –**



**will make it harder for the U.S. to sell off its shares in the companies to private investors?**

The administration's role and behavior in the auto bankruptcies are likely to be the subject of future dissertations on rule of law, ethics, and constitutional matters. The tactics reportedly employed by the Obama administration to "encourage" senior, priority creditors to back off their claims so that chosen parties could take priority—tactics reported to include closed-door reminders that some of those creditors had received and might seek more TARP funding, threats of bringing the full weight and measure of the White House press office to bear down on dissenters, public condemnation, and other forms of arm-twisting—would be found unseemly by most Americans. In the process, long-established and often-reinforced protections for secured creditors in bankruptcy proceedings—a "guarantee" that has underpinned a relatively stable corporate lending market in the United States—are now in question. And that greater uncertainty will carry a higher risk factor, which is likely to have an elevating effect on interest rates in the corporate bond markets.

How that added risk impacts equity markets—specifically, how it affects demand for GM shares—is difficult to discern. Arguably, the equity value of a company that has to pay more to borrow should be suppressed. But, all of this depends on a multitude of factors, including whether, and how much, investors perceive intrinsic value in a company deemed "too big to fail." I would suggest that if the market places a premium on that attribute and it persists, then we as a nation will have a very difficult time rescuing our economy from the slippery slope.

*Ramifications for economic recovery and the investment and lending markets*

**3. The Chrysler bankruptcy deal in particular has destabilized contract rights and secured investment. Doesn't that jeopardize our ability to recover promptly from the current credit crisis and recession?**

The raiding of Chrysler's secured debt-holders in the bankruptcy process will no doubt give pause to would-be creditors in the corporate bond market going forward. And that could potentially undermine economic recovery by systemically raising the cost of borrowing for business. But it is important to recognize that the economy has been in a perpetual phase of adjustment to the various government interventions since September 2008, beginning with the legislation establishing the TARP. A steady stream of new laws, rules, and regulations over the past 15 months (many often working at cross-purposes or intending to mitigate the effects of earlier policy changes) has made for an unstable policy environment. Recovery and economic growth are less likely to be sustained under conditions of policy flux because flux means uncertainty and uncertainty causes capital to flee to safety.

In other words, it will be difficult to isolate the effects of the Chrysler saga on the economy, given the effects of the other interventions, which have also adversely impacted lending markets.

**4. Have you seen any evidence that the Auto Task Force ever considered the adverse ramifications its actions might have for the broader economic recovery?**

No. But I'm not suggesting that it didn't.

**5. Doesn't the treatment of secured creditors and other creditors in these bankruptcies severely undermine the ability of lenders who received TARP funds to recruit private investment capital in the future – and therefore exit TARP?**

Sure. The meaning of "secured creditor" has changed as a result of these bankruptcies. Secured creditors are now less secure, and as a result should and will demand higher returns on their loans than in the past. The level of risk associated with secured credit, generally, is probably systemically higher now than before the auto bankruptcies. But that level is also affected by industry- or company- or circumstance-specific factors as well, such that the increase in the cost of debt will be higher for some TARP recipients than others.

**6. The Auto Task Force's disregard of the bankruptcy laws for secured creditors in Chrysler has broad, adverse, long-term ramifications for the corporate, municipal and U.S. bond markets, doesn't it?**

Yes. In addition to the adverse potential described above, the Auto Task Force has weakened an institution that has worked to America's advantage in the global economy. Though politicians routinely bemoan the flight of capital to poorer countries where labor standards and environmental laws are alleged to be primitive or ignored, the facts are that internationally mobile capital overwhelmingly seeks jurisdictions where the rule of law is abided, where property rights are established, where markets are relatively fluid, and where the risk of asset expropriation is minimal. Most U.S. investment abroad is in Europe and most European foreign investment is here. The many benefits of being a choice destination for foreign investment include easier and cheaper access to the financing that helps make U.S.-based businesses more competitive in the global economy. (One downside of this access to capital is that it has made government profligacy less painful on a year-to-year basis, since the textbook "crowding out" effect of government spending that causes interest rates to rise has been largely contained by enormous pools of foreign capital.)

The Auto Task Force's cavalier disregard or misguided underestimation of the importance of these institutions may prove one of the greatest costs of the bankruptcy episodes, as Americans and foreigners alike become less certain of the endurance of that American advantage.

**7. Couldn't the Auto Task Force's actions also specifically impair the ability of Chrysler and GM to make successful corporate bond offerings in the future – bond offerings they, like any other major corporations, are sure to have to make?**

Certainly, the cost of a "successful corporate bond offering" is likely to be much higher.

**8. Are you aware of the degree to which interest rates in the bond markets already have risen due to the loss of investor confidence after the Auto Task Force's actions in the Chrysler and GM bankruptcies?**

No. Given the number of interventions and policy changes witnessed over the past 15 months, it is difficult to discern with the naked eye whether, and to what extent, the bankruptcy episodes have impacted bond markets. But it is my understanding that at least a few econometric studies examining these very issues are forthcoming in the near future.

**9. If the Auto Task Force's actions in the Chrysler and GM bankruptcies cause interest rates on bonds to rise, couldn't that in turn cause mortgage interest rates to rise – harming our recovery and the ability of families to purchase or refinance homes?**

It could, although probably not through the direct channels implied by the question. I don't think corporate bond rates are strong determinant of mortgage rates. And, arguably, if demand for corporate bonds at a given interest rate declines because of higher risk, then demand for securitized mortgages might actually increase, reducing interest rates.

But, the habit of intervention in the financial and auto markets could create greater uncertainty in the mortgage lending business, which could have the effect of driving up rates.

**10. Are the precedents set in these cases also likely to impact the secured lending market adversely?**

Yes, as described above.

**11. If so, couldn't that make it possible for airlines and other struggling companies to finance their way around potential bankruptcy – like Ford did in 2006?**

It could make it more costly and thus more difficult for airlines, beleaguered newspapers, auto parts producers, and a host of other struggling companies to find financing.

**12. Aren't those adverse impacts especially likely for companies in sectors – like the airline sector – that are especially likely to tempt government intervention?**

Yes, as described above.

**13. It is impossible to discern a legal or economic principle between the Obama Administration's treatment of Chrysler's secured creditors and its treatment of GM's creditors. Isn't that deeply destabilizing for the bond markets and the lending markets?**

Markets like rules, not exceptions to rules. Rules provide greater certainty, while exceptions invite discretion which begets more discretion, greater uncertainty, and greater risk. Markets deal with exceptions to rules through the pricing mechanism, which, in the bond market, means higher interest rates.

**14. Isn't the only principle that explains the difference in treatment political?**

If I have to speculate, yes.

**15. As a result of the Obama Administration's actions in Chrysler and Delphi, won't private debtor-in-possession lenders either raise interest rates and other terms or just get out of the DIP market altogether in any sector in which the Obama Administration might intervene?**

DIP financing is the life-blood of Chapter 11 restructuring. Without it, bankrupt companies would have few alternatives to liquidation. Though the likely adverse impact of the forced Obama restructuring on the secured bondholder market is obvious enough, its impact on DIP creditors is more difficult to discern. DIP financiers are often attracted by the fact that they get special liens that puts them at the top of the list of creditors for repayment. It is a similar "guarantee" to secured bondholders that was abrogated by the Auto Task Force, so the precedent is unlikely to be lost on DIP financiers. But DIP financing might become more lucrative as a result of the higher underlying debts of companies that enter Chapter 11—higher because of the higher interest rates they will be forced to pay their primary creditor. And the potential for greater profits in the DIP market could sufficiently compensate the added risk.

**16. If private DIP lending dries up, won't that leave the government as the leading source of DIP financing – putting the taxpayers' even further into hock to bailout private industry?**

Theoretically, either that outcome or the demise of Chapter 11 restructuring in favor of Chapter 7 liquidation would prevail.

*Entanglement of the government, the UAW and private companies, conflicts of interests, and impairment of law enforcement*

**1. The Auto Task Force brokered deals that leave the UAW the majority owner of Chrysler and a minority owner and potential future majority owner of GM. Are you concerned that the UAW will self-deal when it comes time to negotiate new contracts with GM and Chrysler?**

The UAWs' new status as "owner" presents numerous potential conflicts of interest within and between the Big Three automakers. What is the UAW's optimal strategy for maximizing its membership's utility? Is it to maximize Chrysler's and GM's profits, which means keeping labor costs in check? Is it to push for maximum concessions to labor, which would increase labor's take, but reduce Chrysler's and GM's profits? Is it somewhere in between? Whatever that strategy may be, the UAW's fidelity is to the union membership, not the company shareholder, which is what should be expected of company management. So, yes, as taxpayers who own majority and significant shares of GM and Chrysler, respectively, we should all be concerned about how these conflicts will be reconciled.

**2. Are you concerned about the UAW's ability to leverage its ownership of GM and Chrysler into deals that it can then use to leverage sweeter union contracts out of Ford?**

This scenario presents a similar quandary. Under longstanding U.S. law, labor has a right to organize if there is sufficient support among workers to form a union. But what if the workers are organized by a direct competitor of the company? Does that not tip the balance of rights and obligations considerably against management of the company whose labor force organizes under its competitor's banner? Should majority and significant owners of GM and Chrysler, respectively, be allowed to organize Ford's work force and seek potentially ruinous concessions under threat of strike? Those are legitimate concerns that will haunt the auto industry landscape as long as these dynamics persist.

**3. Do you think it threatens consumer interests – consumer prices, consumer safety, and consumer choices – that the UAW will now be the owner and strike-ready labor force of Chrysler and GM and the strike-ready labor force of Ford?**

Fortunately, competition in the auto market is robust, thanks in large measure to the availability of imports and foreign nameplate producers who manufacture about half of all car and trucks purchased in the United States. That competition protects consumer interests, by keeping prices in check and ensuring that the costs of safety and quality problems are felt by the respective manufacturers, and quickly. That good news notwithstanding, I am concerned that the UAW's simultaneous roles as organizer of Ford's labor force and owner of GM and Chrysler could undermine Ford's profitability, and ultimately its capacity to compete effectively.

**4. Are you concerned about the adverse impacts for labor law enforcement against the UAW raised by the UAW-U.S. government partnerships in Chrysler and GM?**

The unholy trinity of UAW - U.S. Government - GM/Chrysler presents all sorts conflicts of interest that are not healthy for business or consumers.

**5. Isn't there an appearance that the Obama Administration will give the UAW not only sweetheart bankruptcy deals, but sweetheart law enforcement deals – or simply give the UAW's labor law violations a blind eye?**

Yes.

**6. Isn't there an apparent conflict of interest inherent in the federal government being both an owner in and a law enforcement agent against GM and Chrysler?**

Yes.

**7. Isn't it likely that there will be real conflicts of interest over time?**

Yes.

**8. Won't the real and apparent conflicts of interest be particularly acute regarding GM, since the government owns more than 60 percent of the company?**

Yes.

**9. Aren't there also be real and apparent dangers that the UAW and the Obama Administration will conspire to the competitive disadvantage of Ford and other private automakers – whether through labor, law enforcement or other practices?**

Yes.

**10. Couldn't that be with regard to labor practices that will harm Ford or antitrust-related practices that could harm all of GM's and Chrysler's competitors?**

Yes.

**11. Isn't there also a danger that lax labor law enforcement will lead to poorer GM and Chrysler vehicle quality, and thus lower vehicle safety?**

Possibly.

**12. The Chrysler and GM deals consolidate auto company ownership and auto labor decisions into the hands of the UAW. Are you concerned that the results will be a less competitive market, producing higher priced cars that serve consumers' needs less?**

Not really. The auto market is highly competitive, and as long as consumers can avail themselves of the offerings of auto companies that are not organized by the UAW, then, ironically enough, the UAW-owned auto companies will have to find a way to be competitive or they will perish.

**13. Are you concerned that the joint ownership relationship between the UAW and the federal government also threatens to undermine government willingness to enforce safety laws and other laws designed to protect working people and consumers?**

As stated above, there are many conflicts of interest that sprout from this unholy alliance. This is one of many potentially adverse consequences.

**14. The Chrysler and GM deals make the federal government ownership partners with the UAW in that same arrangement. How can we credibly expect the government to enforce federal labor, antitrust and other laws against Chrysler, GM and the UAW?**

The appearance of a conflict or the potential for conflict undermines that credibility. And until the issue is resolved systemically, there will be tough questions raised in the wake of every decision that produces and aggrieved party. Perhaps that process will inspire the appropriate changes.

**15. How can we possibly expect the UAW and the government not to be tempted to use their market power and conflicted enforcement authority to the disadvantage of non-union and foreign-transplant automakers?**

Eternal vigilance. Observers will simply have to keep a watchful eye on the evolving rules and regulations and cry foul when appropriate. In light of the administration's desire to demonstrate to the public that its intervention in GM was the right decision, it will want to make strides toward making the taxpayer whole. But that could be slow-going given GM's lack of favorability among consumers. Accordingly, I am concerned that consumers will be enticed with special incentives that only a government-owned company can offer, thereby hurting the competition.

**16. Have you seen any evidence that the President or the Auto Task Force ever considered *any* of these problems before weaving these tangled relationships between the UAW and the federal government in the ownership of GM and Chrysler?**

No. But I'm not suggesting that it didn't.



RESPONSE TO POST-HEARING QUESTIONS FROM RICHARD E. MOURDOCK,  
INDIANA TREASURER OF STATE

**Questions for the Record**  
**Subcommittee on Commercial and Administrative Law**  
**Hearing on the Ramifications of Auto Industry Bankruptcies, Part III**  
**July 22, 2009**

**Richard E. Mourdock, Indiana Treasurer of State**

**Questions from the Honorable Trent Franks, Ranking Member**

- 1. Do you believe that secured creditors received a fair opportunity to negotiate with the Auto Task Force and Chrysler over the terms of Chrysler's bankruptcy deal? If not, why not?**

The only meaningful "negotiations" that appear to have occurred were with the major TARP bank lenders. As reported in the Wall Street Journal during May/June, there were several intense periods of negotiations with those who held \$6.6 billion of the \$6.9 billion in secured debt.

- 2. In your written testimony, you assert for a number of reasons your belief that Chrysler's assets were dealt away by the Auto Task Force at less than fair value. Could you explain your reasons further for us?**

In this bankruptcy two sets of values were used for the basis of distribution of assets. The secured creditors values were determined on a liquidation basis while the "preferred" non-secured lenders received values determined on an "on-going concern" basis. That the non-secured received the higher values is inherent evidence that there was a greater value than that received by the secureds.

- 3. Why would the Auto Task Force have undervalued Chrysler's assets? Wouldn't that harm both the ability of Chrysler's secured creditors to receive the value they were entitled and the ability of the taxpayers to recover their debtor-in-possession investment as soon as possible?**

Simply stated, it is seen as a scheme that would evict the secured creditors from the deal at the lowest possible price while surrendering the assets to the "preferred" new owners at the highest possible value.

- 4. As a state treasurer, what are your perspectives on the dangers of government's squandering assets the way the Auto Task Force did?**

As an institutional investor whose fundamental "tools" for investing are fixed income, long term investments I recognize the greatest threat to those instruments is instability in the market place. There is a normal ebb and flow of all markets. That is a part of the risk in the market place. But when government intervenes to overturn two hundred years of established



law regarding bankruptcy and creditor rights it will <not might, not may, not possibly shall, but will>: a) cause businesses to pay more in interest cost, b) cause American investment dollars to flow to other markets where the rules are not being arbitrarily re-written, and c) cause institutional investors to seek other investing options.

**5. Do you believe the Indiana pension funds were able to get a fair hearing in the bankruptcy court? If not, why not?**

Indiana pension fund attorneys were given less than a week to review 87,000 hard copy documents containing more than 385,000 pages. During this brief time we were expected to present a logical argument as to why the \$.29 on the dollar we were to receive was unjustified. Chrysler and the US government had months to prepare their arguments. We were not afforded due process in this regard. Also, Chapter 11 bankruptcy law requires that the court certify the valuation of assets so that all classes of creditors can vote to accept or deny the valuation. Uniquely in this case, no certification process ever occurred; no creditor vote was ever taken.

Regarding the expedited handling of the case: From the outset it was the government's argument that if the "sale" to Fiat were not completed within 45 days they would walk away from the deal? Really? The foreign automaker stood to gain (at a minimum) \$400,000,000 of assets on day one without be required to invest a single penny. How can any logical argument be made that they would walk away from a \$400,000,000 windfall? Indeed, the date the "sale" was completed, Fiat's Chairman Sergio Marchionne commented that the date that had been driving the deal had never originated from Fiat but came from elsewhere, i.e., the Auto Task Force and/or Department of the Treasury.

**6. Do you believe that the Indiana pension funds were able to get a fair hearing from the appellate courts in your case? If not, why not?**

The failure of due process in this case occurred at all levels of the judicial system, hence the reason we have a Writ before the US Supreme Court seeking that the High Court take a position on what we feel would be, should it remain uncorrected, a dangerous precedent. For two hundred years there has been "absolute priority" of claims in bankruptcy until the Chrysler case. Setting aside that essential concept of bankruptcy law, even at a time of financial crisis, solves nothing but induces uncertainty. Law is not made for the best of times but for the times of crisis.

In the opinion offered by the 2<sup>nd</sup> District US Court, it was stated that "Indiana pensioners raise interesting and vexing questions regarding the Constitutional appropriateness of the Treasury Secretaries actions..." regarding the distribution of Troubled Asset Recovery Program funds to the automakers. The court then explains that while some court should rule on this issue, it opted not to by ruling that the Indiana pensioners did not demonstrate "standing" in the case. Lack of standing, in the court's opinion, occurred because the Indiana pensioners never proved under any other bankruptcy outcome that they would receive more than \$.29 on the dollar. It remains the Pensioners' claim that they were never afforded the

opportunity to prove otherwise due to the artificially expedited nature of the bankruptcy proceedings (see answer to #5, above).

**7. What improvements to the Bankruptcy Code could you suggest to help ensure that secured creditors' absolute priority under the code is better respected by debtors, the courts and other participants in the bankruptcy process?**

The error is not in the code. The error is in the court's lack of support for the code. Absolute priority and a uniform method of valuation for all classes of creditors in a bankruptcy are long established but now, apparently, ignored concepts.

**8. Do you think the White House's and the Auto Task Force's participation in the Chrysler bankruptcy yielded a just result for anyone concerned? If not, why not?**

It is impossible for me to discern a just result in the outcome at this point in time. However, it is easy to see the preferred treatment of a "political" class or group, the United Auto Workers and Fiat, the foreign automaker. Ironically, it was other classes of unionized workers (retired teachers union members and Indiana's State Police retirees, among others) who were disadvantaged immediately by the actions taken to benefit the Administration's politically preferred groups.

**9. What are the long-term ramifications of the precedents laid down by the Chrysler and GM bankruptcies for Indiana's decisions over how and where to invest its pension fund monies?**

Indiana's investment policy statements are being reviewed and redrafted to avoid purchasing the debt of those manufacturing/service firms that have received bailout moneys from the federal government. Our decision is not based on a theory or hypothetical concept but on the proven fact that such investments have now become, due to the politicization of the process, too risky.

**10. What are the long-term ramifications of these cases for the Indiana Treasury's ability to make successful state and municipal bond offerings?**

Indiana's State Treasurer's office does not issue bonds but is solely an investment office. More broadly stated however, the impact of the case may actually benefit the offerings of Indiana state government because of the demonstrated position to act according to the rule of law even when it is seen as political disadvantaged to do so. In several recent discussions with rating agencies the state was cited for standing up for bondholder's rights.

**11. Do you believe that these precedents send equally troubling messages to other investors – such as other pension funds, China and other foreign investors?**

Markets crave stability. They thrive based on consistency. The market works best not when the expectations are, to use the sports metaphor, consistent singles, not occasional home runs.

Throwing away long established bankruptcy protections will have a deleterious effect for some time. It is not inconceivable to wonder if foreign investors are beginning to ask, "If the terms 'secured creditor' or 'absolute priority' have no meaning, do the words 'good faith and credit of the United States Treasury' still have meaning?" It is not impossible to imagine foreign investors wondering, "If the US government will act in such a way toward Indiana pensioners and retirees, why should I think they will honor the debt owed to a foreign nation if the financial crisis continues?" Admittedly, that is a concerning thought, but those markets that are driven best by consistency and stability, react to speculation and emotion. The equal application of the rule of law trumps emotion. Indeed, that's why it should be applied in time of emotional crisis.

**12. Are the messages equally bad for other bond or secured debt issuers – such as the United States or corporations trying to avoid insolvency?**

As stated in #4 above, the effect of the misuse of bankruptcy law here can have no good outcome as it will: a) cause businesses to pay more in interest cost, b) cause American investment dollars to flow to other markets where the rules are not being arbitrarily re-written, and c) cause institutional investors to seek other investing options.

**13. Do you believe the Obama Administration has shot itself in the foot with these cases as it confronts the need to finance the massive U.S. debt it is accumulating?**

Interest rates will rise as the perception of risk is seen to increase. The possibility that absolute priority is not really "absolute" and/or the risk that the government will arbitrarily and conveniently change rules to its benefit are stunning messages to send to the marketplace. Perhaps the greatest but clearly non-definable uncertainty that now exists is "will the administration do this again in other industries and thus add even more debt to the balance sheet?"

**14. If the U.S. has to offer higher interest to be able to sell its bonds to China and other investors, couldn't that drive up our future debt burden even further?**

Debt builds debt. Though it is slightly an aside from the issue at hand, the +\$12 trillion national debt levels now being seen are virtually an impossibility to repay. That is not conservative vs. liberal rhetoric nor is it Republican vs. Democrat thinking. It IS, pure mathematics. In the entire history of man it is estimated that \$60 trillion of wealth has been created. To repay \$12 trillion of debt requires far more than \$12 trillion in wealth be created and taxes that pay off government debt result only from the creation of wealth. The possibility that the United States can generate in the next 20 years the equivalent of all wealth ever created by mankind in all the centuries prior to this is pure sophistry.

**15. How fair do you think the Auto Task Force's decision has been for Indiana auto plants and dealerships?**

Respectfully, I'm not qualified to answer this question as "fairness" is something that must be judged (in the framework of the question) vs. how other non-Indiana auto plants and dealerships have been treated.



RESPONSE TO POST-HEARING QUESTIONS FROM JOHN J. FITZGERALD, PRESIDENT,  
FITZGERALD AUTO MALLS

**Questions for the Record**  
**Subcommittee on Commercial and Administrative Law**  
**Hearing on the Ramifications of Auto Industry Bankruptcies, Part III**  
**July 22, 2009**

**John J. Fitzgerald, President, Fitzgerald Auto Malls**

**Questions from the Honorable Steve Cohen, Chairman**

1. **Since July 22, 2009, has there been any further interaction between you or (to your knowledge) other terminated automobile dealers and General Motors and Chrysler to find non-legislative solutions to ease the economic harm of dealership closures? If so, what was the result of these interactions?**

As has been reported in the media, under the auspices of and at the request of several leading Members of Congress, dealer representatives have met with representatives of General Motors and Chrysler to find non-legislative solutions to ease the economic harm of dealership closures. As of this writing (November 9, 2009), it is still too early to tell whether these negotiations will result in a meaningful and fair non-legislative solution. Since the details of the conversations are confidential, I am not in a position to divulge anything beyond the fact that the discussions have taken place and that the dealer groups have pushed for reinstatement of terminated GM and Chrysler dealers using fair and objective criteria.

2. **If there are any additional points you wish to make—by way of elaborating upon your hearing testimony or responding to the testimony of the other witnesses—please do so.**

I would like to elaborate on the points I raised during the hearing as follows. The Administration's unelected, unaccountable, inexperienced and ill-advised Auto Task Force made a series of missteps and miscalculations based on bad advice and used the bankruptcy process to create the current dealer crisis. More than any other decision, the Task Force's decision to reduce GM and Chrysler dealer ranks, if not reversed, will most likely be the cause of the slow death of Chrysler and perhaps GM that many predict. The Task Force used hopelessly flawed criteria to make decisions affecting the livelihoods of tens of thousands of their fellow countrymen and have reacted with arrogance when we have tried to bring this to their attention and to seek a mid-course correction based on facts.

It is clear to us that the White House Auto Task Force misunderstood the vitally important role the dealerships play in the success of Chrysler and GM. Dealers should be reinstated, either by the legislation we support or through a nonlegislative solution worked out with GM, Chrysler, and the Task Force.

In this case, the failed management of GM and Chrysler, abetted by the Auto Task Force, under the guise of Bankruptcy Code, needlessly extinguished profitable small businesses that were neither failing nor in need of a government bailout. We believe that we arrived in this position because the Auto Task Force received bad advice regarding the costs associated with dealerships, the appropriate number of dealerships, the differences between import-dominated States and domestic-dominated States, and the accuracy of termination criteria such as Dealer Performance Scores and the Customer Satisfaction Index.

The Task Force incorrectly believed GM and Chrysler could save substantial amounts of money by shedding dealers through the bankruptcy process. The truth is that dealers invest significantly in their businesses in the form of land and facilities, inventory and working capital. Dealers are sources of revenue, not cost centers, for manufacturers. At a minimum of \$40,000 per year per franchise, the manufacturer makes money from the dealer over and above any revenue from the sale of cars, parts and services.

This reduction is also a problem because there are nearly two-domestic vehicles on the road for every one-import vehicle. The Task Force made a glaring error in its analysis of the marketplace by not focusing on Vehicles In Operation (VIO). A principal reason for dealers to exist is their mission to provide product support to the owners of that Brand's cars. Approximately, 90% of Dealer employees are devoted to service, parts, body shop and used cars. Only about 10% of dealers' employees sell new cars. This means that 150,000 of the jobs at stake here are necessary to support the cars already on the road.

It should be clear to the Subcommittee that the Auto Task Force did not really consider the different characteristics of your Districts and States when it called for radical reductions in the number of Chrysler and GM dealers. The Task Force members probably would have ignored the bad advice of its consultants if they had seen the R.L. Polk data shown on the red and blue colored map I provided the Subcommittee depicting the national distribution of import and domestic car registrations and on page 2 a state by state breakout. (Attachment 1) By studying this map we can see that the proposed dealer cuts in red States will inconvenience customers and open the door to the import brands. By reducing service in the blue States the import advantage will grow even faster. Mr. Bloom told you the best prospect for a new GM car is the current owner of a GM car. That is not true if you reduce service to the current owners of GM cars. The best way to ruin brand loyalty is to make service inconvenient for your current owner base.

CRDR has heard repeatedly that the Task Force made GM and Chrysler remodel their dealer organization after Toyota. The problem is that most of the business for Toyota and other Imports comes principally from the metro markets in nine states concentrated on the East and West coasts. Ford, GM and Chrysler get most of their business from sixteen states in the middle of the country, a land area that's four times the size of the nine states on the East and West Coasts. Arguably, to be competitive, you need four times the dealer count, and those dealers must be smaller to fit the markets they serve. Incredibly, after the proposed cuts, there will be fewer Domestic than Import dealers, approximately 9,600 Domestics, 9,900 Imports (some are duals.) (See Attachment 2) These terminations are closing the door for a Domestic comeback on the East and West coasts (See Attachments

3&4), while opening the door to Imports rising across the center of the country. This is why many knowledgeable experts now believe that GM and Chrysler will fail. In addition, losing over 100,000 jobs unnecessarily at this time is an outrage.

One of the more egregious mistakes committed by the Auto Task Force was believing the GM and Chrysler management when they said that they could select dealers for termination using fundamentally flawed dealer sales performance criteria and Customer Satisfaction Index (CSI) data. For example, some of the sales performance data rely on how a dealer performs compared to his/her state average. But, this can be very misleading due to the many differences between rural and metropolitan markets (See Attachment 5.) They are not valid indicators of effectiveness in new auto sales. The use of CSI scores should not have been a major factor in determining whether our dealerships should continue. The Auto Task Force was misled into believing that CSI is an accurate predictor of future success and viability. I am hopeful that the Subcommittee will recognize that it is well-documented that GM and Chrysler CSI scores have been manipulated by factory and dealer employees to the extent that they are meaningless. It is outrageous to use this data as termination criteria. (See Attachment 6)

It is even more outrageous that any dealers were terminated because as Mr. Press said (Automotive News, October 26, 2009), "Fewer dealers mean fewer sales." People with experience in auto manufacturing and retailing would not have made these mistakes and they would not have appointed a Chairman and board of directors at GM and Chrysler with no automotive manufacturing experience. If this is not fatal the failure to provide a captive finance company might indeed be fatal. No manufacturer in the last 50 years has been successful in the US market without a captive finance company to support its dealers. The GMAC bank might be good for Cerberus but its independence will not be good for Chrysler or GM. Keep in mind, dealer floor plan providers have to advance 95% to 99% of sticker price (MSRP) on new cars that will eventually only sell for 80% to 90% of sticker price. How will Treasury feel about that? The bottom line is that we should have listened to Mom when she told us, "experience is the best teacher."

**Questions from the Honorable Trent Franks, Ranking Member**

1. **Have any of you been able to discern any logical business principle upon which Chrysler, GM or the Auto Task Force determined which dealers to keep and which to let go?**

We believe the business plan used in the bankruptcy court regarding dealers was a sophistry.

We have been unable to discern any logical business principle upon which Chrysler, GM, or the Auto Task Force determined which dealers to keep and which to let go. As noted in my testimony and answers provided to the Subcommittee, the companies relied on fundamentally flawed criteria in many cases and the Task Force was misled as to whether dealers actually cost money to the manufacturers. Finally, Mr. Press has admitted publicly that he did not want to terminate dealers but the Task Force demanded the cuts.

**2. If the termination of dealers was not based on any legal or economic principle, wasn't it simply based on politics?**

In my opinion the terminations were the result of awful advice and the decisions of leaders that lacked the experience to know they were getting awful advice. However, I do know that profitable and economically viable dealers throughout the Nation were terminated in violation of state franchise laws and this represented a misguided decision by the companies and the Auto Task Force. I am not in a position to offer an opinion as to whether the dealer terminations were "simply based on politics" as you use politics but certain GM and Chrysler Field Managers disposed of certain dealers they did not like. We are grateful that both HB2743 and S1304 have received by partisan support.

**3. Is it true that Chrysler asked for debtor-in-possession financing to help repurchase inventory from terminated dealers, in light of the fact that the dealers were forced to close in such a short time period?**

I do not know.

**4. Is it true that the Treasury Department objected to such assistance?**

I do not know.

**5. If so, do you know why Treasury objected to helping the dealers?**

See above.

**6. Couldn't the Obama Administration have used some of the billions of dollars in federal loans it forgave these companies to help terminated dealers with their economic hardships?**

As a representative of the Committee to Restore Dealer Rights, it is important to me to stress that our legislative effort has been predicated on the notion that it would cost nothing to the taxpayer to reinstate the terminated Chrysler and GM dealers. Note that H.R. 2743 and S. 1304 are silent on compensation. Bringing our dealerships back on line would come at no cost and would generate substantial new revenues for federal, state, and local coffers. In any event, it is clear that if the Obama Administration wanted to find funding to support the dealers whose economic rights and property rights were eviscerated by the Bankruptcy Court and the Auto Task Force, it could do so.

**7. Wouldn't that have been a case of the Administration actually helping Main Street instead of Wall Street and other Big Money interests?**

If dealers received compensation, it would have helped Main Street. But I must repeat that the CRDR legislation does not seek compensation or a bailout of any kind. Restoring dealers would not cost the taxpayer or GM and Chrysler anything and would improve their chances of returning to independent profitability.



**8. Wouldn't that have helped to preserve or "transition" small business jobs, instead of just wiping them out?**

I am not in a position to know how hypothetical compensation would have been structured or spent. It is clear, though, that reinstatement (which costs nothing) would have been and still is the best way to preserve 169,000 jobs.

**9. Is it true that many dealers are being left with millions of dollars of debt in inventory, infrastructure, and single-use facilities that can result in personal bankruptcy?**

I have heard anecdotes suggesting that many dealers are, in fact, being left with millions of dollars of debt in inventory, facilities, real estate, and personal guarantees and that they face personal bankruptcy.

**10. What is the Auto Task Force doing to make sure that these hard-working small business people do no worse in their cases than the GM, Chrysler and the UAW did in the auto company bankruptcies?**

I do not know of any decision or action taken by the Task Force that has benefited dealers. However, the Auto Task Force is a complete mystery to me. Your question is better aimed at them. I would be interested to know more about what the Task Force is doing. Sunlight is the best disinfectant.

**11. Is it true that the Auto Task Force has argued that having more dealers causes pressure for price-cutting vehicles, and that it used that as a rationale for terminating dealers?**

It is unclear to me whether the Task Force has made that argument, primarily because the Task Force would not meet with our Committee other than an abrupt 12-minute meeting with Mr. Bloom, who spoke for 10 minutes of the 12 minutes. I believe competition is good for America. It is the American way. The dealers and their people that were cut are great competitors because they had to be to survive the worst recession since the Great Depression.

**12. What do you think of that theory?**

I think reliance on that theory reflects the Task Force's inexperience.

If, in fact, the Task Force has argued that having more dealers causes pressure for price cutting vehicles and used that as a rationale for terminating dealers, it would reflect a fundamental misunderstanding of the dealer's role in supporting the manufacturers. Further, if that is the case, it is scary that so much power could be given to such inexperienced individuals.

As I noted in an answer to Chairman Cohen's Question for the Record #2, dealers are critical to servicing the existing cars on the road and play an important role in whether a consumer will purchase from the same manufacturer again. By inconveniencing millions

of consumers, putting aside pricing, the Task Force's reductions will have lessened the demand for GM and Chrysler vehicles and opened the door for the imports to take further hold.

Manufacturers through the manipulation of rebates and incentives determine the retail pricing of cars. (Please see attachments 7 and 8.) Keep in mind that dealers pay 95% to 99% of sticker price to the manufacturer before the car is even shipped from the factory. Cars actually sell for much less than that, after rebates and incentives are deducted from the sticker price to arrive at the transaction price. Currently, the manufacturer keeps almost all of the revenue from the sale of a new car.

In 2008, GM paid \$2,266 more per car than Toyota in incentives to reduce transaction prices to levels that would sell cars. This is because so few of GM's cars are recommended by Consumer Reports while nearly all of Toyota's cars receive Consumer Report's recommendation. Troy Clark, then President of GM, told the Washington Post last summer that the new Chevrolet Malibu brought \$3,500 more revenue to GM than the previous Malibu. The difference was from \$16,500 to \$20,000. The new Malibu is recommended in Consumer Reports while the previous model was not. Improving product quality is the only way GM can increase the price of its cars. Ford has increased prices over \$1 billion this year because so many of their cars are recommended in Consumer Reports. Product quality has a much greater effect on transaction prices than dealer price competition (See Attachment 9&10.)

13. **Do you think it was the Administration's role to help GM and Chrysler charge more for their cars than to assure that consumers could pay the lowest possible price for cars during this recession?**

No.

Facts the Task Force didn't consider?

# Fact – Nearly two-thirds of U.S. Parc are GM, Ford, or Chrysler Models

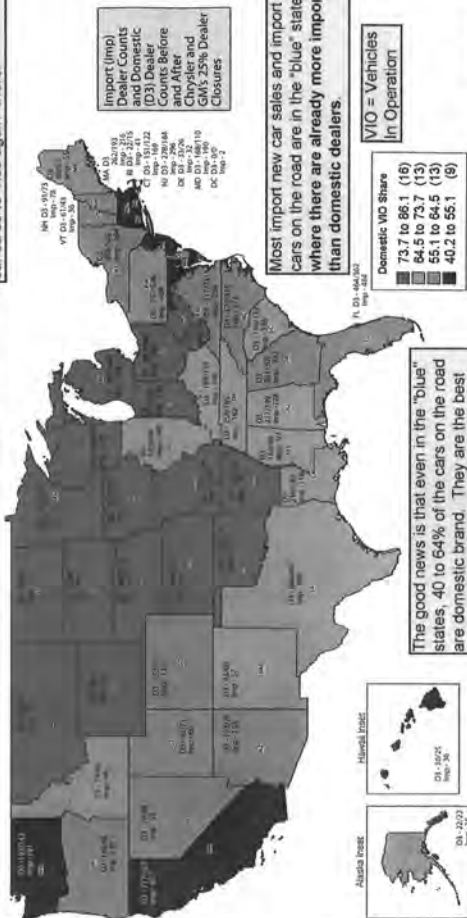
Therefore, at least two-thirds of all dealers should be domestic dealers. But, with the proposed cuts, there will be more import than domestic dealers and Chrysler and GM may not "rise again", they may fail.

The proposed dealer cuts in the "red" states will severely inconvenience customers (up to 86% of the cars on the road there) and open the door for imports to move into the abandoned locations.

Domestic Share of Lt. Vehicles in Operation

Today, where there are more domestic dealers, there are more domestic sales, where more import dealers, more import sales.

The proposed dealer cuts in the "blue" states will inconvenience customers and make it all but impossible for domestic car sales to "rise again" there.



Alaska Inset: 04-12-07 Imp: 14  
Hawaii Inset: HI-19-05 Imp: 36  
Puerto Rico Inset: PR-01-04-03 Imp: 7

The good news is that even in the "blue" states, 40 to 64% of the cars on the road are domestic brand. They are the best prospects for new domestic cars.

Most import new car sales and import cars on the road are in the "blue" states where there are already more import than domestic dealers.

**Domestic V/S Share**

- 73.7 to 86.1 (16)
- 54.5 to 73.7 (13)
- 55.1 to 64.5 (13)
- 40.2 to 55.1 (9)

**V/S = Vehicles In Operation**



mailto:po@oknightimpact.com

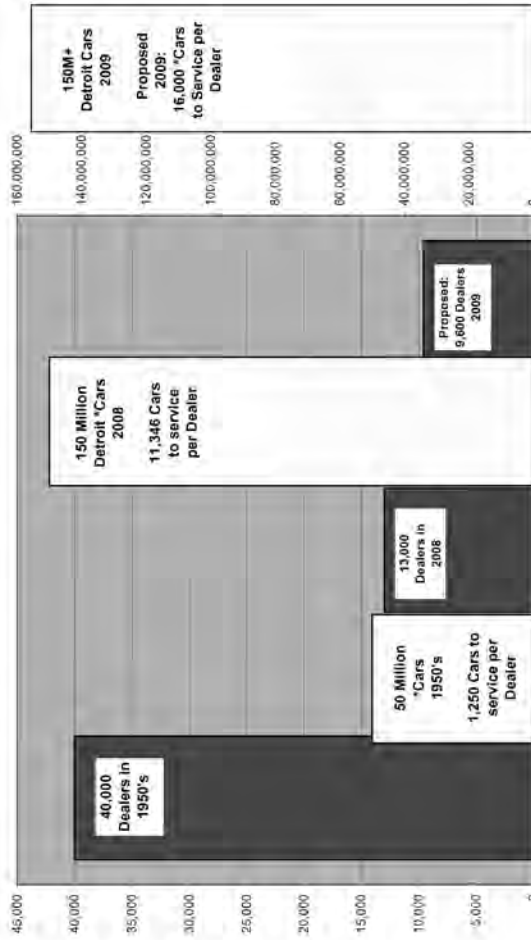
R.L. Pook provided this information to me at no charge. I assume they want to help the government make better decisions. All boxed commenting by Jakob Fritzsche. jacob@fritzsche.com

**Facts The Task Force Didn't Consider?**  
 Source: NADA DATA from Autodata - May 2008. Chrysler Dealer Closures Ltd. GM Dealer Closures - Wash Post  
 \* Includes Estimated 2009 Domestic/Import Dealer Closures (U.S.) - Source: Paul Taylor NADA

STATE	TOTAL New Car Dealerships	Exclusive Import Dealerships	Exclusive Domestic and Domestic Import Dealers	Chrysler Closures	GM Announced Closures	GM Proposed Closures	TOTAL Closures	Remaining Exclusive Domestic and Domestic Import Dealers	Percent Reduction D3	TOTAL Dealership Employment	Estimated Job Loss From Chrysler and GM Dealer Closures
Arkansas	297	74	193	3	17	18	41	192	21.5%	4,811	1,388
Indiana	521	132	389	22	48	49	119	270	30.7%	21,882	5,912
Iowa	369	77	292	22	46	44	112	180	38.5%	12,177	3,709
Kansas	258	69	189	17	28	29	74	115	39.1%	10,062	2,869
Michigan	759	158	601	30	58	50	138	448	35.5%	38,433	7,243
Minnesota	438	101	337	18	36	38	92	242	38.1%	19,710	4,252
Missouri	494	123	371	27	14	14	55	216	14.7%	21,738	3,399
Montana	132	40	92	4	18	13	35	57	39.5%	4,224	1,154
Nebraska	213	45	168	6	21	20	47	119	29.3%	6,623	1,927
North Dakota	98	18	79	8	6	6	20	56	28.4%	3,168	853
Ohio	553	296	257	47	75	78	200	496	30.0%	30,023	3,042
Oklahoma	299	78	221	12	17	18	47	179	20.5%	11,194	8,697
South Dakota	117	19	98	7	16	18	38	80	39.2%	3,110	1,152
West Virginia	169	58	111	17	25	24	66	53	56.9%	6,253	2,447
Wisconsin	597	129	468	18	32	48	118	352	24.6%	21,462	4,185
Wyoming	70	31	40	5	6	6	17	32	34.3%	2,450	588
<b>73.7 - 88.1 % D3 UO</b>	<b>8,787</b>	<b>1,430</b>	<b>4,327</b>	<b>282</b>	<b>487</b>	<b>479</b>	<b>1,239</b>	<b>3,088</b>	<b>28.9%</b>	<b>238,737</b>	<b>50,461</b>
Alabama	345	128	217	12	33	32	77	140	35.4%	16,552	3,629
Alaska	38	9	29	0	0	0	0	22	0.0%	2,260	0
Arizona	123	44	79	3	6	9	19	60	33.7%	5,731	880
Illinois	934	302	632	44	68	64	174	459	27.9%	42,964	7,990
Kentucky	298	109	189	9	23	22	54	135	29.7%	13,112	2,385
Louisiana	327	118	210	16	10	10	36	183	18.3%	18,198	1,925
Maine	144	55	89	4	14	14	32	57	35.4%	5,328	1,169
Massachusetts	242	92	150	6	38	37	81	409	35.8%	9,436	3,146
New Mexico	140	37	103	3	10	10	23	160	27.9%	7,426	1,201
Pennsylvania	1,181	404	777	54	90	87	231	528	30.9%	51,084	10,158
South Carolina	328	120	208	11	24	23	58	132	30.9%	14,996	2,676
Tennessee	420	162	258	14	30	29	73	185	28.3%	28,263	3,987
Texas	1,346	490	856	51	55	53	159	697	18.0%	87,450	10,341
<b>4.8 - 73.7 % D3 UO</b>	<b>5,854</b>	<b>2,113</b>	<b>3,741</b>	<b>227</b>	<b>481</b>	<b>387</b>	<b>1,018</b>	<b>3,726</b>	<b>27.1%</b>	<b>296,911</b>	<b>49,424</b>
Arizona	298	153	145	5	11	11	27	76	25.8%	29,184	3,054
Colorado	284	131	153	13	13	14	40	111	27.8%	17,040	2,549
Delaware	65	32	33	3	2	2	7	28	21.0%	4,032	430
Florida	948	484	464	27	35	34	102	362	21.9%	19,788	6,244
Georgia	603	242	361	13	24	23	60	301	15.7%	33,768	3,859
Nevada	118	59	59	5	3	3	11	48	18.3%	10,974	1,913
New Hampshire	169	78	91	0	0	0	0	78	18.9%	7,098	747
New York	1,112	464	648	28	60	58	146	392	22.3%	48,928	8,420
North Carolina	892	272	620	14	36	35	85	335	20.2%	32,624	3,963
Oregon	274	129	145	9	21	20	50	88	34.7%	13,974	2,564
Utah	153	60	93	10	6	6	22	71	25.4%	9,333	1,329
Vermont	37	38	0	2	8	8	18	63	39.1%	2,813	1,414
Virginia	351	234	117	25	26	25	76	241	24.0%	33,060	4,598
<b>58.1 - 64.5% D3 UO</b>	<b>5,322</b>	<b>2,374</b>	<b>2,948</b>	<b>166</b>	<b>253</b>	<b>244</b>	<b>663</b>	<b>2,285</b>	<b>22.8%</b>	<b>318,614</b>	<b>38,783</b>
California	1,894	877	1,017	32	65	63	160	587	22.3%	123,898	13,412
Connecticut	320	169	151	7	11	11	29	122	19.0%	14,400	1,288
DC	2	2	0	0	0	0	0	0	0.0%	84	0
Hawaii	66	36	30	1	1	1	3	23	16.4%	5,062	360
Maryland	358	190	168	17	21	20	58	110	34.7%	23,988	3,604
Massachusetts	478	216	262	12	29	28	69	193	35.3%	23,422	3,381
New Jersey	574	289	285	28	33	32	94	184	33.8%	32,144	5,558
Rhode Island	63	41	22	1	3	3	7	13	31.3%	3,338	355
Washington	383	191	192	15	18	17	50	142	28.2%	23,363	3,073
<b>49.2 - 69.1% D3 UO</b>	<b>3,858</b>	<b>2,018</b>	<b>1,820</b>	<b>114</b>	<b>182</b>	<b>178</b>	<b>474</b>	<b>1,348</b>	<b>28.9%</b>	<b>259,688</b>	<b>31,064</b>
<b>Total</b>	<b>36,771</b>	<b>7,935</b>	<b>12,836</b>	<b>789</b>	<b>1,323</b>	<b>1,277</b>	<b>3,389</b>	<b>9,447</b>	<b>26.4%</b>	<b>1,118,888</b>	<b>189,852</b>

\* There are 2,000 import franchises (dealt with domestic brands) so the total import count is actually 9,558

Only Detroit could go from 40,000 Dealers serving 50 Million Detroit Cars to 13,000 Dealers serving 150 Million Detroit Cars. Who cares about Customer Service?



Now, in a new law, even for Detroit, they propose an additional 26% dealer reduction... to improve profits... Nevermind that this results in dramatically less service for Detroit customers than imports offer, or that Detroit dealers will have more than twice the cars to service. Will this kill their recovery?

If's obvious Detroit doesn't care about service, but why doesn't the Task Force care? An Experienced automotive retailer would advise the Task Force, that without offering more service and reaching out to Detroit brand customers, Chrysler & GM may fail.

Analysis of Detroit Brand/Dealers

Source: RL Post Automotive News "Cars" is passenger vehicles including 4 Trucks 207,000,000 in 2008  
 4000 Import: 150M Domestic RL Post  
 4th Dealers: 1850's: 13,200 Domestic Dealers Automotive News  
 Contact Jack@FHZMail.com 5/23/2009

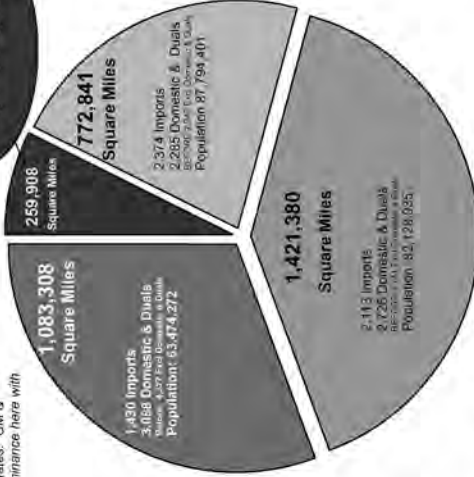
Attachment 2

**Too few Domestic Dealers may cause GM & Chrysler to fail.  
After closures there are fewer Domestic dealers than Imports, even though there are nearly twice as many Domestic cars\* on the road.**

Domestics are strongest in the red states. Closing dealers here will diminish current market dominance. This area has only 12 million fewer people, but the land area is 2.12 times larger than the blue states. GM & Chrysler will lose dominance here with fewer dealers.

\*87 Million Imports 150 Million Domestic  
9,935 Total Import Dealers (2,000 dealer units on average)  
9,447 Total Domestic Dealers  
Obviously too few to provide competitive service. They may fail, why take the risk? Put the dealers and 169,000 people back to work to compete and help Detroit rise again.  
That's the American way.

2,018 Imports  
1,348 Domestic & Duels  
as a % of total cars  
Population: 70,552,486



Domestics have already lost market share on the East and West coasts (blue states) and will continue to lose as they close more dealerships.



**"The last buyer of a GM car is the most likely buyer of a new GM Car."  
Mr. Ron Bloom 7/21/2009 Senior Advisor, U.S. Treasury**

Sources: RL Polk, Washington Post, US Census Data, Info please.

**Example of Import Impact on Metro Markets:  
Suburb of Washington, DC**

**Rockville Pike (Rt. 355)  
Dealerships**



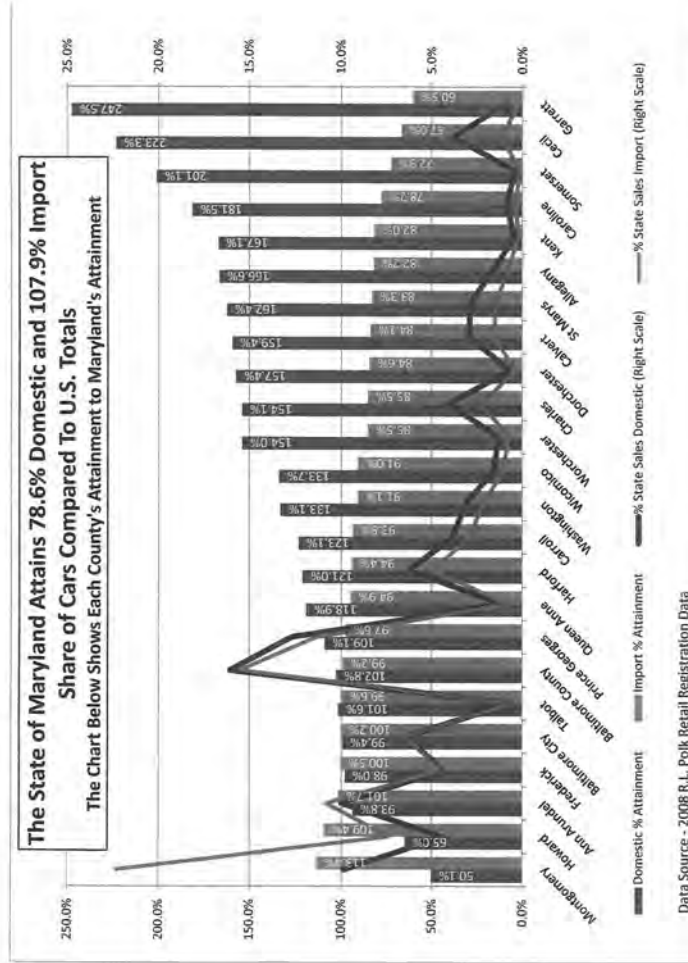
**No. of Dealerships (After Closures)**

**Where there was once a cluster of 64 dealerships, the  
Domestics are outnumbered by a ratio of 6:1**

**What chance do they have?**

Attachment 4

For More Information: [Jack@FitzMall.com](mailto:Jack@FitzMall.com)





## GM WANTS IT BOTH WAYS WITH BILL HEARD

**JAMES B. TREECE**  
 AUTOMOTIVE NEWS  
 OCTOBER 1, 2008 - 11:01 AM ET  
**UPDATED: 10/3/08 11:30 A.M. EDT**

The case of Bill Heard Enterprises Inc. shows that General Motors' customer-satisfaction ratings are a sham.

In the wake of the collapse of the world's largest, by unit volume, Chevrolet dealership company, the dirt is coming out. Former employees, rivals, vendors and customers are saying out loud what Better Business Bureaus and state regulators have known for years: Bill Heard Enterprises ran a sleazy sales operation. It was the sort of operation that gives good, ethical dealers a bad name by association.

At this point, we cannot assert that the company's failure was a case of chickens coming home to roost. The collapse of the \$2.13 billion-sales-a-year enterprise appears to be due mainly to a combination of tighter credit that killed sales to subprime customers, tumbling truck sales and the company's overextension.

Could it be that the same questionable ethical culture that winked at fake recall notices and bogus travel sweepstakes also led to financial shenanigans? We don't know that.

What we do know is that GM was happy to cozy up to Bill Heard when the metal was moving.

In 2004, GM gave Heard a Dealer of the Year award and the Jack Smith Leadership Award. The Smith award recognizes dealers who have attained the highest levels of sales and customer satisfaction in their region.

Today, though, GM is singing a different tune.

A GM spokesperson told one of our reporters that Bill Heard Enterprises' legal and financial troubles do not reflect poorly on Chevrolet, GM or the company's other dealers.

"It's just individual people owning individual businesses, and it's separate from the General Motors name," the spokesperson said. "What happens at one dealership should not reflect on the entire network."

Read that quote again. What horseradish! I've heard some slinkers from PR people, but this sets a new low.

A dealership can do whatever it wants, and that doesn't reflect on the network? Chevy's network — its brand, its image and those of its other dealers — isn't affected by a bad apple in the barrel?

If that's true, then why does GM bother tracking CSI scores, and supposedly rewarding dealers with the better scores? If a bad dealer doesn't reflect on the network, then neither does a good one. It doesn't matter.

Maybe some people at GM believe CSI results are bunk. But there are a few people in the industry who disagree with them. Unfortunately, everything about the Bill Heard tale supports the "bunk."

You can reach James B. Treece at [jtreece@crain.com](mailto:jtreece@crain.com).

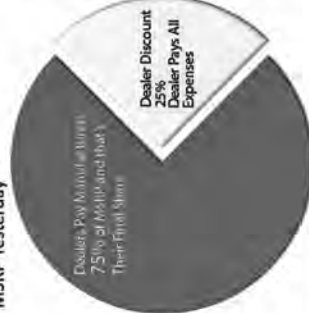
**Saving Money by Reducing Dealers is Impossible: "Dealers Cost Zero! Zero! Zero!"** ... Majority Leader Harry Hoyt, June 6, 2009  
**Manufacturers Keep More \$ Than Ever**  
 "It simply doesn't cost the factory anything to have too many dealers; it costs the dealers"

Edmunds.com, National Bureau of Economic Research, Automobile News, 1/13/2009

All manufacturers, including GM/Chrysler are getting more of what the consumer pays than ever before. The dealers, of course, are getting less, a lot less!!!

- Originally dealers received a 25% discount from MSRP, paid all expenses, and negotiated the retail sales transaction with consumers, keeping as much of the 25% as possible. Manufacturers were limited to a maximum 75% share of MSRP.
- Today all manufacturers are reducing Dealer discounts dramatically, but dealers get most of the expenses. Manufacturers do pay some expenses and they manage the transaction with consumers, though they limit the amount of rebates and incentives.
- Edmunds data shows that in 2008 the consumer discount from MSRP averaged 16.7% for GM, 18.5% for Chrysler, and only 9.6% for Toyota.

**MSRP Yesterday**



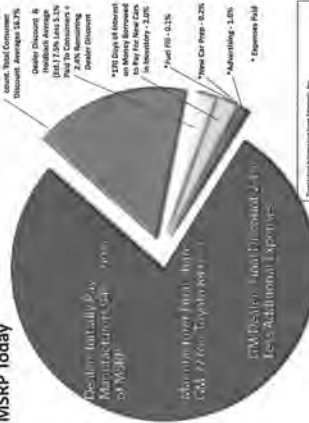
The Edmunds data also shows that the 16.7% average GM consumer discount from MSRP consists of 11.6% rebate/incentives and 5.1% dealer discount. This reduces the dealer discount to approximately 2.4%, from which it must pay most of the expenses of the sale.

The chart to the right shows the few expenses GM pays which it misleadfully claims it will save with fewer dealers.

Note that dealers fund all of the expenditures by paying almost MSRP for the car before it leaves the factory -- 75% Yesterday.

Also, all of the "savings" are expenses related to the sale of the car, not the dealer. The only way to reduce any of these expenses without selling fewer cars is to improve GM's management and product quality.

**MSRP Today**



- Vehicle Reservations (2%)
- By After After March 2009
- 11.6% and 1.5% Dealer Dis-
- Discount Average 13.7%
- Dealer Discount & Rebate/Average
- 11.6% and 1.5% Dealer Dis-
- 7.2% Rebate/Average
- 2.4% Remaining Dealer Discount
- \*15% Only if amount on Money Borrowed in February 2.2%
- \*Fuel 0% - 1.5%
- \*Tire Car Price 0.2%
- \*Advertising - 1.5%
- \*Expenses Paid

**Conclusion: Dealers Subsidize Manufacturers, Not the Other Way Around**

Category	Value
MSRP	100.00%
Dealer Discount	25.00%
Rebate/Incentive	11.60%
Finance	1.50%
Additional Expenses	1.50%
GM Share	77.60%

Category	Value
MSRP	100.00%
Dealer Discount	13.70%
Rebate/Incentive	11.60%
Finance	1.50%
Additional Expenses	1.50%
GM Share	83.70%

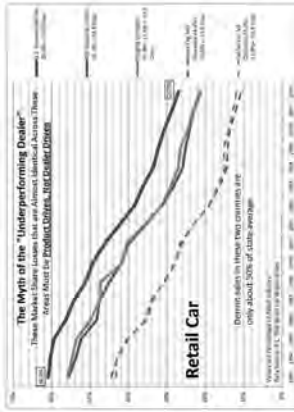
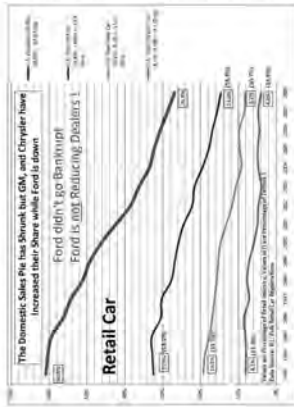
Attachment 7



**The Product is Underperforming, Not The Dealers !  
GM and Chrysler's Accusation of Under Performing Dealers Will Not Pass Examination**

**Detroit management is adept at blaming others for their loss of market share. But clearly, as Consumer Reports says, it is the product.**

The charts show a 16 year steady decline by all 3 Detroit manufacturers with Ford actually losing more market share than GM and Chrysler. We use a chart on car sales only because car sales are critical for the future as MPG requirements increase.



Although Ford has lost more market share, it has accepted responsibility and improved its products and Consumer Reports has recommended more Ford models in 2009 than GM and Chrysler combined.

Today Ford sales are increasing while GM and Chrysler sales are decreasing.

A review of the chart on the right indicates GM and Chrysler must have used "contrived data" to create "underperforming dealers" in Virginia and Maryland.

Fairfax (VA) and Montgomery (MD) counties are and have been for 16 years, almost identical in terms of Detroit share of sales. Yet Chrysler canceled 5 out of 7 Montgomery County dealers while keeping 5 out of 7 Fairfax County dealers. Using state averages they could easily show any dealer as underperforming because both counties only achieve about 50% of the state sales rate. To be "average" a dealer in these counties would have to sell at twice the "state average" just to meet "state average". Using "state averages" as a benchmark almost always over assigns domestic dealer's sales quotas in large metro markets. It's also easy to over assign responsibilities by moving census tracts into or out of a dealer's market area or simply increasing or decreasing the sales objectives or altering the mix of models supplied to the dealer. Only the manufacturers employees would know how they created underperforming dealers.



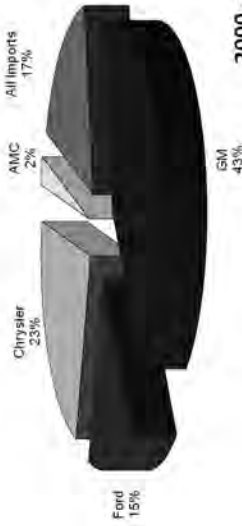
Chrysler & GM failed because of poor products. Consumer Reports ranked them last. Because GM puts one dealer employee out of work, they should match Toyota, Honda, or at least Hyundai ratings in Consumer Reports.

In the 60's and 70's GM & Chrysler had 66% of all the recommended vehicles in Consumer Reports. In 2000-2009, GM & Chrysler had only 14%.



Then & Now

1967 - 1979 Consumer Reports  
Recommendations as Percent of Total



2000 - 2009 Consumer Reports  
Recommendations as Percent of Total



- Chrysler
- Ford
- Saturn
- GM
- All Imports

RESPONSE TO POST-HEARING QUESTIONS FROM JIM TARBOX, PRESIDENT,  
TARBOX MOTORS, INC.

Questions for the Record  
Subcommittee on Commercial and Administrative Law  
Hearing on the Ramifications of Auto Industry Bankruptcies, Part III  
July 22, 2009

Jim Tarbox, President, Tarbox Motors, Inc.

Questions from the Honorable Trent Franks, Ranking Member

1. **Have any of you been able to discern any logical business principle upon which Chrysler, GM or the Auto Task Force determined which dealers to keep and which to let go?**

None- whatsoever

2. **If the termination of dealers was not based on any legal or economic principle, wasn't it simply based on politics?**

Politics, personalities & retribution

3. **Is it true that Chrysler asked for debtor-in-possession financing to help repurchase inventory from terminated dealers, in light of the fact that the dealers were forced to close in such a short time period?**

I understand it this way, only with what I read

4. **Is it true that the Treasury Department objected to such assistance?**

I understand it this way, only with what I read

5. **If so, do you know why Treasury objected to helping the dealers?**

I have no idea whatsoever

6. **Couldn't the Obama Administration have used some of the billions of dollars in federal loans it forgave these companies to help terminated dealers with their economic hardships?**

Most definitely

7. **Wouldn't that have been a case of the Administration actually helping Main Street instead of Wall Street and other Big Money interests?**

Most definitely

- 8. Wouldn't that have helped to preserve or "transition" small business jobs, instead of just wiping them out?**

Absolutely

- 9. Is it true that many dealers are being left with millions of dollars of debt in inventory, infrastructure, and single-use facilities that can result in personal bankruptcy?**

Yes

- 10. What is the Auto Task Force doing to make sure that these hard-working small business people do no worse in their cases than the GM, Chrysler and the UAW did in the auto company bankruptcies?**

Nothing, absolutely nothing

- 11. Is it true that the Auto Task Force has argued that having more dealers causes pressure for price-cutting vehicles, and that it used that as a rationale for terminating dealers?**

Yes

- 12. What do you think of that theory?**

I think it is flawed.

- 13. Do you think it was the Administration's role to help GM and Chrysler charge more for their cars than to assure that consumers could pay the lowest possible price for cars during this recession?**

No, but that is exactly what happened.



RESPONSE TO POST-HEARING QUESTIONS FROM GREG WILLIAMS, PRESIDENT,  
HUNTINGTON CHEVROLET, INC.

Questions for the Record  
Subcommittee on Commercial and Administrative Law  
Hearing on the Ramifications of Auto Industry Bankruptcies, Part III  
July 22, 2009

Greg Williams, President, Huntington Chevrolet, Inc.

Questions from the Honorable Steve Cohen, Chairman

**1. Have you or other minority automobile dealers had any further interactions with General Motors or Chrysler concerning the specific concerns of minority dealers with respect to dealership termination? If so, what was the result of these interactions?**

I have been to Capitol Hill on numerous occasions and as a result we have been able to have several Senators and Congressmen write letters to GM expressing that they come to the table and negotiate some sort of settlement with us, the result is that GM and Chrysler is negotiating with our representatives. There is a gag order on those negotiations so we don't know what's going on. I would very much appreciate if you would keep the pressure on them to make this right by us.

**2. If there are any additional points you wish to make—by way of elaborating upon your hearing testimony or responding to the testimony of the other witnesses — please do so.**

GMAC is coming back to congress for more money (5B) they should know that they should not ask for any additional money unless they consider releasing the personal guarantees on the minority dealers who borrowed money from them when they were a part of GM to buy out General Motors stock. Now those dealers have no way to pay this money back, but are still being held liable by GMAC.

Questions from the Honorable Trent Frauks, Ranking Member

**1. Have any of you been able to discern any logical business principle upon which Chrysler, GM or the Auto Task Force determined which dealers to keep and which to let go?**

I have not been able to discern any logical business principle upon which GM or Chrysler, or the Task force determined which dealers to let go. I feel that in GM's case they knew that they had an overabundance of dealers, and used this Bankruptcy to do what they would not have been able to do otherwise. They used this moment to also rid themselves of anyone who may have been outspoken or questioned them.



- 2. If the termination of dealers was not based on any legal or economic principle, wasn't it simply based on politics?**

Yes, the Administration could have used a miniscule amount of the funds to help these dealers rather than allowing us to die a horrific death for no reason.

- 3. Is it true that Chrysler asked for debtor-in-possession financing to help repurchase inventory from terminated dealers, in light of the fact that the dealers were forced to close in such a short time period?**

Most of the Dealers are being left with Millions of dollars of Debt along with the possibility of financial ruin or bankruptcy.

- 4. Is it true that the Treasury Department objected to such assistance?**

*No response was submitted by the witness*

- 5. If so, do you know why Treasury objected to helping the dealers?**

*No response was submitted by the witness*

- 6. Couldn't the Obama Administration have used some of the billions of dollars in federal loans it forgave these companies to help terminated dealers with their economic hardships?**

*No response was submitted by the witness*

- 7. Wouldn't that have been a case of the Administration actually helping Main Street instead of Wall Street and other Big Money interests?**

*No response was submitted by the witness*

- 8. Wouldn't that have helped to preserve or "transition" small business jobs, instead of just wiping them out?**

*No response was submitted by the witness*

- 9. Is it true that many dealers are being left with millions of dollars of debt in inventory, infrastructure, and single-use facilities that can result in personal bankruptcy?**

*No response was submitted by the witness*

- 10. What is the Auto Task Force doing to make sure that these hard-working small business people do no worse in their cases than the GM, Chrysler and the UAW did in the auto company bankruptcies?**

*No response was submitted by the witness*

- 11. Is it true that the Auto Task Force has argued that having more dealers causes pressure for price-cutting vehicles, and that it used that as a rationale for terminating dealers?**

*No response was submitted by the witness*

- 12. What do you think of that theory?**

*No response was submitted by the witness*

- 13. Do you think it was the Administration's role to help GM and Chrysler charge more for their cars than to assure that consumers could pay the lowest possible price for cars during this recession?**

*No response was submitted by the witness*



POST-HEARING QUESTIONS SUBMITTED TO ROBERT G. KNAPP,  
PRESIDENT, KNAPP CHEVROLET\*

Questions for the Record  
Subcommittee on Commercial and Administrative Law  
Hearing on the Ramifications of Auto Industry Bankruptcies, Part III  
July 22, 2009

Robert G. Knapp, President, Knapp Chevrolet

Questions from the Honorable Trent Franks, Ranking Member

1. Have any of you been able to discern any logical business principle upon which Chrysler, GM or the Auto Task Force determined which dealers to keep and which to let go?
2. If the termination of dealers was not based on any legal or economic principle, wasn't it simply based on politics?
3. Is it true that Chrysler asked for debtor-in-possession financing to help repurchase inventory from terminated dealers, in light of the fact that the dealers were forced to close in such a short time period?
4. Is it true that the Treasury Department objected to such assistance?
5. If so, do you know why Treasury objected to helping the dealers?
6. Couldn't the Obama Administration have used some of the billions of dollars in federal loans it forgave these companies to help terminated dealers with their economic hardships?
7. Wouldn't that have been a case of the Administration actually helping Main Street instead of Wall Street and other Big Money interests?
8. Wouldn't that have helped to preserve or "transition" small business jobs, instead of just wiping them out?
9. Is it true that many dealers are being left with millions of dollars of debt in inventory, infrastructure, and single-use facilities that can result in personal bankruptcy?
10. What is the Auto Task Force doing to make sure that these hard-working small business people do no worse in their cases than the GM, Chrysler and the UAW did in the auto company bankruptcies?
11. Is it true that the Auto Task Force has argued that having more dealers causes pressure for price-cutting vehicles, and that it used that as a rationale for terminating dealers?
12. What do you think of that theory?
13. Do you think it was the Administration's role to help GM and Chrysler charge more for their cars than to assure that consumers could pay the lowest possible price for cars during this recession?

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\*The Subcommittee did not receive a response to their post-hearing questions from this witness before the printing of this hearing.



LETTER FROM MICHAEL J. ROBINSON, VICE PRESIDENT AND  
GENERAL COUNSEL OF NORTH AMERICA, GENERAL MOTORS COMPANY



MICHAEL J. ROBINSON  
GMNA Vice President & General Counsel

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General Motors Company  
Mail Code 482-C25-A36  
300 GM Renaissance Center  
P.O. Box 300  
Detroit, MI 48265-3000  
Tel 313-665-4874  
Fax 248-267-4365

July 30, 2009

AUG 10 2009

The Honorable Stephen I. Cohen  
Chairman, Subcommittee on Commercial and Administrative Law  
Committee on the Judiciary  
United States House of Representatives  
1005 Longworth House Office Building  
Washington, DC 20515

Dear Mr. Chairman:

During the hearing you chaired last week on the ramifications of auto industry bankruptcies, a number of the witnesses testifying on the second panel made incorrect statements about General Motors Company and our activities regarding our auto dealers. I would like to take the opportunity to correct the record regarding two of the statements.

The first statement concerns the number of African American auto dealers that will remain with General Motors Company after the restructuring of our dealer network. During your questioning, Gregory Williams, Dealer Operator of Huntington Chevrolet, stated that less than 20 African American dealers would remain at General Motors Company. He also implied that African American dealers were disproportionately affected by the restructuring. With due respect to Mr. Williams, he is wrong.

Throughout our network restructuring, GM worked to ensure that our minority dealer population was not unfairly impacted. In fact, the proportion of African American dealerships representing GM's continuing brands remains the same. The number of African American dealer operators who will remain with GM is 30, and they own 36 dealerships. In addition, another eight African American dealer operators are Saturn, Saab or HUMMER dealers who will continue to own and operate their 19 dealerships under new brand ownership. As you know, GM is attempting to sell these brands to another owner.

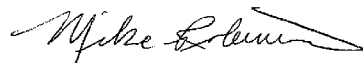
I can assure you that we recognize the contributions of our minority-owned dealerships as a vital part of our business. General Motors was the first U.S. automaker to initiate a structured minority dealer initiative in 1972. Although we have had some significant challenges with the changing automotive landscape since that time, one thing remains the same – and that is our commitment to the development, growth, and profitability of our minority dealers. That commitment is integrated in our Minority Dealer Development program and reinforced by the support from GM's leadership.

The Honorable Stephen I. Cohen  
July 30, 2009  
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The second statement was included in both the written and oral statement of Jack Fitzgerald, Owner/Dealer of Fitzgerald Auto Malls. Mr. Fitzgerald stated that "GM and Chrysler are leaving their dealers out to dry regarding product liability." The fact is GM is continuing to indemnify both our wind down and participation dealers regarding product liability claims concerning GM vehicles. GM continues to support our dealer partners, and our products and bankruptcy did not change this treatment.

Thank you for the opportunity to correct the record. We appreciate your interest in and support of African American dealers.

Regards,

A handwritten signature in cursive script, appearing to read "Mike Lamm". The signature is written in black ink and is positioned below the "Regards," text.

MJR:en