IN THE UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

In re:	§	Chapter 11
	§	
CROSSROADS SYSTEMS, INC.	§	Case No. 17-51926
	§	
Debtor.	§	
	§	

DEBTOR'S MOTION FOR AN ORDER (I) AUTHORIZING THE DEBTOR TO REJECT PURCHASE AND ASSIGNMENT AGREEMENT WITH SDSI AND (II) ESTIMATING REJECTION CLAIM

Crossroads Systems, Inc., a Delaware corporation, as debtor-in-possession in the above-captioned chapter 11 case (the "Debtor"), files this *Debtor's Motion for an Order (i) Authorizing the Debtor to Reject Purchase and Assignment Agreement with SDSI and (ii) Estimating Rejection Claim* (the "Motion"), and respectfully represents as follows:

Jurisdiction and Venue

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

Background

A. General Background

2. On August 13, 2017 (the "Petition Date"), the Debtor commenced the above captioned case (the "Chapter 11 Case") by filing a voluntary petition for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). The Debtor continues to manage and operate its business as a debtor-in-possession pursuant to sections 1107 and 1108 of the

Bankruptcy Code. No request for the appointment of a trustee or examiner has been made in the Chapter 11 Case, and no committees have been appointed or designated.

3. A detailed description of the Debtor and its business, and the facts and circumstances supporting the Motion and the Debtor's Chapter 11 Case is set forth in the *Statement of Background Information and Declaration of Jennifer Crane, Chief Financial Officer of Crossroads Systems, Inc., in Support of Debtor's Chapter 11 Petition and First Day Motions*, filed on August 13, 2017.

4. Contemporaneously with the filing of the Chapter 11 Case, the Debtor filed its Prepackaged Chapter 11 Plan of Reorganization (the "Prepackaged Plan") and related Disclosure Statement. Solicitation on the Prepackaged Plan began prior to the filing of the Chapter 11 Case, and, prior to the Petition Date, the Debtor had received acceptances to the Prepackaged Plan from holders of more than two-thirds of equity interests in the only class impaired by the Prepackaged Plan. On the Petition Date, the Debtor also filed a motion seeking assumption of its obligations under the Restructuring Support Agreements (the "RSAs") that forms the basis for the Prepackaged Plan, including the investment by 210/CRDS Investment LLC ("210") that provides funding for the Prepackaged Plan transactions and for operation of the Debtor after the effective date of the Plan. On August 30, 2017, the Court entered the final order approving assumption of the RSAs.

B. Purchase and Assignment Agreement With SDSI

5. The Debtor is a party to that certain Purchase and Assignment Agreement with StrongBox Data Solutions, Inc. ("SDSI") dated March 22, 2016 (the "P&A Agreement"). A true and correct copy of the P&A Agreement is attached hereto as **Exhibit A** and incorporated herein by reference.

6. Pursuant to the P&A Agreement, the Debtor entered into a transaction to sell all of its right, title and interest in and to certain assets related to the Debtor's product and support services division, including the Strongbox product line and all rights therein and thereto, to SDSI on March 22, 2016.

7. The P&A Agreement provides that the Debtor shall have certain continuing obligations including indemnity obligations.[1]

8. At this time, the Debtor is not aware of any claims against the Debtor pursuant to the P&A Agreement.

9. Any claim against the Debtor under the P&A Agreement is contingent and unliquidated.

10. The RSA with 210 may be terminated if Liabilities (as defined in the RSA), other than those contemplated by the RSA with 210, as of the Effective Date, exceed $50,000. Accordingly, the Debtor must minimize rejection damage claims. Further, the Debtor is required to reject the P&A Agreement pursuant to the RSA with 210 because 210 designated the P&A Agreement to be rejected.

Relief Requested

11. The Debtor seeks the entry of an order, substantially in the form attached hereto as **Exhibit B** (the "Proposed Order"), under sections 105(a), 365, and 502(c) of the Bankruptcy Code and Rules 6004 and 6006 of the Federal Rules of Bankruptcy Procedure (i) authorizing the Debtor to reject the P&A Agreement and (ii) estimating the rejection claim of SDSI (the "Rejection Claim") for all purposes, including distribution, at zero.

[1] The P&A Agreement contains certain confidentiality obligations. The Debtor intends to continue to honor these confidentiality obligations.

Basis for Relief Requested

A. Rejection of the P&A Agreement Is an Exercise of the Debtor's Sound Business Judgment

12. Section 365 of the Bankruptcy Code provides that a debtor, subject to court approval, may assume or reject an executory contract. 11 U.S.C. § 365(a); *see also In re Univ. Med. Ctr.*, 973 F.2d 1065, 1075 (3d Cir. 1992) ("This provision allows a trustee to relieve the bankruptcy estate of burdensome agreements which have not been completely performed."). A decision to assume or reject an executory contact pursuant to section 365 must be based on the debtor's business judgment. *See Richmond Leasing Co. v. Capital Bank, N.A.*, 762 F.2d 1303, 1309 (5th Cir. 1985); *In re Taylor*, 913 F.2d 102 (3d Cir. 1990); *Sharon Steel Corp. v. Nat'l Fuel Gas Distribution Corp.*, 872 F.2d 36 (3d Cir. 1989); *In re Gardinier, Inc.*, 831 F.2d 974, 975 n.2 (11th Cir. 1987). The business judgment test is not a strict standard and merely requires a showing that either assumption or rejection of the contract at issue will benefit the debtor's estate. *See In re Bildisco*, 682 F.2d 72, 79 (3d Cir. 1982), *aff'd sub nom*, *NLRB v. Bildisco & Bildisco*, 465 U.S. 513 (1984).

13. Upon a finding that a debtor has exercised its sound business judgment in determining that rejection will benefit the estate, a court should approve rejection. *See Comput. Sales Int'l, Inc. v. Fed. Mogul (In re Fed. Mogul Glob., Inc.)*, 293 B.R. 124, 126 (D. Del. 2003) ("a court should approve a debtor's decision to reject a contract unless that decision is the product of bad faith or a gross abuse of discretion"); *Commercial Fin. Ltd. v. Haw. Dimensions, Inc. (In re Haw. Dimensions, Inc.)*, 47 B.R. 425, 427 (D. Haw. 1985) ("Under the business judgment test, a court should approve a debtor's proposed rejection if such rejection will benefit the estate."); *Summit Land Co. v. Allen (In re Summit Land Co.)*, 13 B.R. 310, 315 (Bankr. D.

Utah 1981) ("court approval under Section 365(a), if required, except in extraordinary situations, should be granted as a matter of course").

14. The P&A Agreement is an executory contract and subject to rejection under section 365(a) of the Bankruptcy Code.

15. Under the circumstances, the P&A Agreement is a burdensome executory contract. The Debtor's decision to reject the P&A Agreement is in the best interest of the Debtor and is a sound exercise of its business judgment. As stated above, rejection of the P&A Agreement is required under the RSA. Through the RSA, the Debtor will obtain much-needed equity capital and access to a future financing source that will allow the Debtor to continue executing on its current patent monetization strategy and to continue to pursue other opportunities for the benefit of the Debtor, its creditors, and shareholders. The new capital and access to financing under the RSA will benefit the Debtor and its entire estate.

16. Absent rejection of the P&A Agreement and estimation of the Rejection Claim at zero, 210 has the right to terminate the RSA and refuse to support the Debtor's proposed restructuring, which may irreparably harm the Debtor's estate.

17. Therefore, the Court should approve the Debtor's rejection of the P&A Agreement.

B. Estimation of the Rejection Claim

(i) The Rejection Claim Is Unliquidated and Subject to Estimation

18. Section 502(c) of the Bankruptcy Code **requires** a court to estimate "any contingent or unliquidated claim, the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case." 11 U.S.C. § 502(c); *see also in re A.H. Robbins Co.*, 788 F.2d 994, 1011-1012 (the "duty of estimation in a proper case under section 502(c) is not a permissive one; it is a mandatory obligation of the bankruptcy court"). "Estimation of

unliquidated and contingent claims is essential prior to the hearing on confirmation of a plan, in order for the court to evaluate the feasibility of the plan without delaying the confirmation process." *In re Nat'l Gypsum Co.*, 139 B.R. 397, 405 n.19 (N.D. Tex. 1992) (citation omitted).

19. Courts generally recognize that a claim is unliquidated, and therefore subject to estimation, if the amount of the claim or the date that it is due is not readily "ascertainable by reference to (1) an agreement or (2) to [sic] a simple mathematical formula." *In re Horne*, 277 B.R. 320, 322 (Bankr. E.D. Tex. 2002).

20. With respect to the P&A Agreement, there is no "amount due" to any party to the P&A Agreement. Instead, the Debtor has certain continuing obligations if certain events occur. No events have occurred that give rise to a claim. The Debtor believes that the events that would give rise to a claim are remote. The amount of any claim and the date it may be due is not readily ascertainable.

21. Estimation of the Rejection Claim, as requested in the Motion, will expedite administration of the Debtor's estate and confirm that the condition precedent under the RSA will be satisfied. On the other hand, failure to estimate the Rejection Claim will delay administration of the Debtor's estate and potentially provide 210 with a right to terminate the RSA and refuse to support the Debtor's proposed restructuring. In the Debtor's view, this would not only necessarily frustrate and prolong the Debtor's reorganization efforts but destroy enterprise value which is maximized as a result of the Prepackaged Plan. Therefore, the Court should estimate the Rejection Claim under section 502(c) of the Bankruptcy Code.

(ii) The Court Should Estimate the Rejection Claim at No More Than the Value of Any Claim Under the P&A Agreement as of the Petition Date

22. Bankruptcy courts have broad discretion in determining the method to estimate a claim, and the court may use "whatever method is best suited to the circumstances." *In re Brints*

Cotton Mktg., Inc., 737 F.2d at 1341; *see also In re Adelphia Bus. Sol., Inc.*, 341 B.R. 415, 422-23 (Bankr. S.D.N.Y. 2003) (courts have discretion to use "whatever method is best suited to the contingencies of the case, so long as the procedure is consistent with the fundamental policy of chapter 11 that a reorganization must be accomplished quickly and efficiently") (citation omitted). A claim arising from a rejected agreement is valued as of the date of the bankruptcy filing. *See* 11 U.S.C. § 365(g).

23. The Debtor believes the value of the contingent, unliquidated claim pursuant to the P&A Agreement is zero.

24. The Debtor could only be liable based on a limited set of events as stated in the P&A Agreement, which have not happened, and in all probability, will not happen. As of the Petition Date (and as of the date of filing this Motion), there were no liquidated or undisputed claims under the P&A Agreement, and there has been no assertion by any party of any claim under the P&A Agreement even though it was signed over seventeen (17) months ago.

25. Thus, the Debtor believes there are no amounts owed under the P&A Agreement, and the Court should enter an order valuing the Rejection Claim of SDSI at zero.

(iii) 502(e) Requires Disallowance of Any Contingent Indemnity Claim

26. An additional justification for valuing the Rejection Claim at zero is that, in theory, there may be a contingent claim that is subject to mandatory disallowance by section 502(e) of the Bankruptcy Code.

27. Three elements must be established to disallow a claim pursuant to section 502(e)(1)(B). "First, the claim must be for reimbursement or contribution. Second, the party asserting the claim must be 'liable with the debtor' on the claim. Third, the claim must be

contingent at the time of its allowance or disallowance." *In re GCO, LLC*, 324 B.R. 459, 465 (Bankr. S.D.N.Y. 2005).

28. First, courts have consistently held that "the concept of reimbursement includes indemnity." *In re Wedtech Corp.,* 85 B.R. 285, 289 (Bankr. S.D.N.Y 1988). Second, it is generally agreed that a claim is contingent "if the debtor's legal duty to pay does not come into existence until triggered by the occurrence of a future event." *Pearl-Phil GMT (Far East) Ltd. v. Caldor Corp.*, 266 B.R. 575, 580 (S.D.N.Y. 2001) (citing *Mazzeo v. United States (In re Mazzeo),* 131 F.3d 295, 303 (2d Cir. 1997)). Third, "[t]he co-liability factor is determined by reference to the underlying third party action. If the causes of action in the underlying lawsuit assert claims upon which, if proven, the debtor could be liable but for the automatic stay, then the co-liability factor is present." *In re Drexel Burnham Lambert Group, Inc.* ("Drexel I"), 146 B.R. 92, 102 (S.D.N.Y. 1992) (internal quotations omitted).

29. Again, in theory, a claim could be asserted in the future (although remote), for infringement or product warranty for example, asserting liability against the Debtor and SDSI. SDSI, arguably therefore, has a contingent, disputed claim for indemnification against the Debtor based on this theoretical future claim.

30. This "so contingent" claim is subject to mandatory disallowance. *See In re GCO,* 324 B.R. at 466-67 ("The purpose of § 502(e)(1)(B) is to prevent contingent, unresolved indemnification or contribution claims from delaying the consummation of a plan of reorganization or a final distribution in a liquidating case.").

31. Accordingly, the Rejection Claim should be valued at zero.

Debtor's Reservation of Rights

32. Nothing contained herein is intended or should be construed as an admission as to the validity or priority of any claim against the Debtor or a waiver of the Debtor's rights to dispute any claim. The Debtor expressly reserves its rights to contest any claim and to withdraw the Motion at any time prior to approval by the Bankruptcy Court in the event that the parties are unable to reach an agreement on any objections to the Motion.

WHEREFORE, the Debtor respectfully requests that the Court (i) grant the Motion and (ii) grant such other and further relief as is just and proper.

RESPECTFULLY SUBMITTED this 5th day of September, 2017.

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PROPOSED ATTORNEY FOR THE DEBTOR-IN-POSSESSION

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of this document (without Exhibit A, the P&A Agreement) was served via on September 5, 2017, via U.S. First Class Mail, postage paid, (or via the Court's ECF System, where applicable), and via email/fax if known, to the parties on the attached service list which includes counsel for Fujifilm and SDSI (with both exhibits to SDSI). If a party wants a copy of Exhibit A, please contact the undersigned.

/s/ Eric Terry