IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	Chapter 11
BUILDING MATERIALS HOLDING CORPORATION, et al. [1]	)	Case No. 09-12074 (KJC)
	)	Jointly Administered
Debtors	)	**Re: Docket No. 1667**

OBJECTION BY ROBERT R. THOMAS AND THE RESTATED THOMAS TRUST DATED APRIL 14, 2009 TO DEBTOR'S MOTION FOR ENTRY OF IMPLEMENTATION ORDER WITH RESPECT TO PARAGRAPH 44 OF CONFIRMATION ORDER (RELATING TO ROBERT R. THOMAS AND THE RESTATED THOMAS TRUST)

Robert R. Thomas ("Mr. Thomas") and The Restated Thomas Trust Dated April 14, 2009 (the "Thomas Trust") (collectively, the "Thomas Parties") hereby file this objection ("Objection") to the Debtor's Motion For Entry of Implementation Order With Respect to Paragraph 44 Of Confirmation Order [D.I. 1667] (the "Motion"). In support of this Objection, the Thomas Parties respectfully represent as follows:

I. INTRODUCTION.

1. The Motion seeks to interpret and enforce language inserted into the Plan Confirmation Order to resolve the Thomas Parties' objection to confirmation (D.I. 1008 - the "Plan Objection"). The Plan Objection related specifically to the assumption under the Plan of two contracts referred to collectively in the Confirmation Order as the "Acquisition Agreement."

[1] The Reorganized Debtors, along with the last four digits of each Reorganized Debtor's tax identification number, are as follows: Building Materials Holding Corporation (4269), BMC West Corporation (0454), SelectBuild Construction, Inc. (1340), SelectBuild Northern California, Inc. (7579), Illinois Framing, Inc. (4451), C Construction, Inc. (8206), TWF Construction, Inc. (3334), H.N.R. Framing Systems, Inc. (4329), SelectBuild Southern California, Inc. (9378), SelectBuild Nevada, Inc. (8912), SelectBuild Arizona, LLC (0036), and SelectBuild Illinois, LLC (0792). The mailing address for the Reorganized Debtors is 720 Park Boulevard, Suite 200, Boise, Idaho 83712.

2. The Plan Objection briefed in detail the Thomas Parties' contention that the cure claim must be determined under the ADR provisions set forth in the Acquisition Agreement, which provides for mediation and then binding arbitration.

3. The Debtors did not comply with the procedures included within their own Plan, in that the Debtors did not file or serve a proposed cure claim on the Thomas Parties prior to confirmation. ***Instead, the issue of the cure claim was committed to the arbitration process under the following paragraph of the Confirmation Order:***

> 44. Robert R. Thomas and The Restated Thomas Trust. Notwithstanding anything that may be construed to the contrary in the Plan or this Confirmation Order, ***the Cure Claims, if any, of Robert R. Thomas or The Restated Thomas Trust*** Dated April 14, 2009 under the Acquisition Agreement (as defined in the Objection By Robert R. Thomas and The Restated Thomas Trust Dated April 14, 2009 to Confirmation of Joint Plan of Reorganization as Amended October 22, 2009 [D.L 1008]) ***shall be resolved by proceedings consistent with the Alternative Dispute Resolution provisions of the Acquisition Agreement.***

4. Throughout this bankruptcy case, including in their Plan Objection, the Thomas Parties asserted in filings with the Court that under the doctrine of recoupment and other theories they were entitled to recover as part of their cure claim the damages they suffered due to the breach by the Debtors of two related leases (the Gregg Street Lease and the Ralph Road Lease, referred to in the Acquisition Agreement as the "New Shareholder Leases").

5. Now that the parties are finally preparing to pursue the ADR procedures required under the Acquisition Agreement, the Debtors want this Court to intercede in the ADR process and decide issues relating to the cure claims. The Debtors cannot point to any express waivers of their recoupment rights by the Thomas Parties, nor to any waiver of their arbitration rights.

6. If this Court were to grant the Debtor's Motion, it would be deciding matters expressly reserved to arbitration under the Acquisition Agreement. For that reason, the Motion must be denied.

II. STATEMENT OF THE CASE.

7. The Acquisition Agreement consists of two related pre-petition contracts for the Debtors' acquisition of businesses owned by the Thomas Parties. The sale closed on about October 17, 2005.

8. The businesses sold were conducted on specially designed and built facilities owned by the Thomas Parties. These facilities were essential to the operation of the business and but were specialized in design such that they could not easily be leased for other purposes. As a part of the Acquisition Agreement, certain of the Debtor Affiliates agreed to lease these facilities from the Thomas Parties. These leases were attached as exhibits to the Acquisition Agreement and referred to as the "New Shareholder Leases." In turn, the New Shareholder Leases themselves refer to the Acquisition Agreement. The rent under the New Shareholder Leases was set at an above-market rate and functioned as a component of the purchase price for business.

9. The Acquisition Agreement includes among other things a continuing obligation on the part of the Thomas Parties to defend and indemnify certain of the Debtors against construction defect claims. In filings with this Court prior to confirmation, the Thomas Parties consistently asserted three things:

9.1 That the Debtors had breached their duty to cooperate in defending the construction defect claims, resulting in damages to the Thomas Parties.

9.2 That the Acquisition Agreement was related to the New Shareholder Leases, such that (under the doctrine of recoupment among other theories) the Acquisition Agreement could not be assumed without also compensating the Thomas Parties for the Debtors' breaches of the New Shareholder Leases.

9.3 That the ADR provisions of the Acquisition Agreement required that all issues relating to assumption and "cure claims" under the Acquisition Agreement be submitted first to mediation and then to binding arbitration.

10. These issues were first raised by the Thomas Parties in relation to the Debtors' first day motions to reject the New Shareholder Leases. At that time the Thomas Parties filed a "Reservation of Rights and Limited Response" (D.I. 156 – the "Limited Response") which stated in pertinent part:

> ***The Debtors' breach of the New Shareholder Leases would give rise to a recoupment defense to continuing liability under the indemnity provisions of the Securities Purchase Agreement, among other things.***
>
> . . . .
>
> In this case, by abandoning the leased premises, defaulting in rents due prior to the bankruptcy filing, and by filing their First Omnibus Motion the Debtors have announced their intent to breach the New Shareholder Leases. ***The Thomas Parties wish to make clear what they believe the consequences of such a decision will be, and to state that they do not intend to waive their right to arbitrate as to any claim, defense or right which may spring from the breach. If the Debtors make any demand or take any post-rejection action to enforce the Securities Purchase Agreement or Asset Purchase Agreement, the Thomas Parties' defenses would be subject to arbitration.***
>
> ***This pleading is simply a statement of position to notify the Debtors on the record that a breach of the leases, which were an inextricable part of the consideration agreed to be paid by the Debtors in the acquisition, will give rise to defenses to the Trust's liabilities under the Securities Purchase Agreement and Asset Purchase Agreement. If the Debtors conclude in their business judgment to proceed with their breach of the leases in spite of the legal consequences, the Thomas Parties will not***

> ***attempt to carry the burden of challenging the Debtors' business judgment.*** The Thomas Parties do, however, reserve all of their rights, claims and defenses which arise from the breach, all of which are subject to arbitration under the dispute resolution provisions of the Securities Purchase Agreement and Asset Purchase Agreement. [***italics*** added]

11. The Debtors filed a Reply (D.I. 173) to the Limited Response, which disputed the recoupment theory, did not dispute the ADR issue, and basically agreed that the issues regarding the relationship of the New Shareholder Leases and the Acquisition Agreement were not before the Court, stating:

> ***While the Debtors are filing this limited Reply to the Response, the Debtors reserve all rights to dispute, in the proper forum, any allegation that the rejection of the Leases gives rise to a recoupment defense or constitutes the breach of any agreement other than the Leases being rejected,*** and to dispute all other factual allegations and conclusions of law asserted in the Response. [***italics*** added]

12. Later, the Thomas Parties filed proofs of claim based on the Acquisition Agreement (the "Proofs of Claim," copy attached to Declaration of Paul S. Street in Support of Reorgainzed Debtor's Motion, etc. D.I. 1668[2] Exh. K). The Proofs of Claim each seek $400,000 in damages, according to proof, arising out of the Debtor's breaches of its duty to cooperate in defending the claims. The Proofs of Claim also state in part:

> Claimant contends that the Securities Purchase Agreement, Asset Purchase Agreement and New Shareholder Leases were part of the same transaction such that rejection of the New Shareholder Leases precludes assumption of the Securities Purchase Agreement and Asset Purchase Agreement.
>
> . . . .
>
> ***Claimant reserves the right to file a cure claim at such time as the Debtor seeks to assume the Securities Purchase Agreement and/or the Asset Purchase Agreement.***
>
> . . . .
>
> The Securities Purchase Agreement, Asset Purchase Agreement and New Shareholder Leases each require that all disputes arising under or relating

[2] Hereinafter referred to as the "Street Declaration"

> to them be subject to alternative dispute resolution . . . ***In submitting proofs of claim in this bankruptcy case, Claimant does not waiver [sic] such dispute resolution provisions and demands that any objection to the within claim be submitted to mediation and if necessary to binding arbitration.*** [*italics* added]

13. After the expiration of the claims bar date, the Debtors filed and sought to confirm their joint Plan. The Plan contains the following provisions:

> **6.1** ***Assumption and Rejection of Contracts and Unexpired Leases.*** Except as otherwise provided herein or pursuant to the Confirmation Order, all Executory Contracts and Unexpired Leases . . . shall be assumed pursuant to section 365(a) of the Bankruptcy Code as of the Effective Date, except for any such contract or lease (i) that has been assumed or rejected, or renegotiated and either assumed or rejected on renegotiated terms, pursuant to an order of the Bankruptcy Court entered prior to the Effective Date . . . or (iv) that is identified on the Rejected Executory Contract and Unexpired Lease List.

> ***6.4*** ***Cure of Defaults.*** Any monetary defaults under each Executory Contract and Unexpired Lease to be assumed pursuant to the Plan shall be satisfied, pursuant to section 365(b)(1) of the Bankruptcy Code, by payment of the Cure Claim in Cash on the Effective Date . . . . In the event of a dispute regarding (i) the Cure Claim . . . or (iii) any other matter pertaining to assumption, the payments required by section 365(b)(1) of the Bankruptcy Code in respect of Cure Claims shall be made following the entry of a Final Order or orders resolving the dispute and approving the assumption. ***At least 20 days prior to the Confirmation Hearing, the Debtors shall provide for notices of proposed assumption and proposed Cure Claims to be sent to applicable third parties. . . .*** . Any counterparty to an Executory Contract or Unexpired Lease that fails to object timely to the proposed assumption or Cure Claim will be deemed to have assented to such assumption and Cure Claim. ***If an objection to a proposed Cure Claim is sustained by the Bankruptcy Court, the Reorganized Debtors may elect to reject such Executory Contract or Unexpired Lease in lieu of assuming it.*** [*italics* added]

14. The Acquisition Agreement was never listed in the "Rejected Executory Contracts and Unexpired Lease List" referred to in the Plan. By operation of the above-quoted provisions of the Plan, the Debtors have assumed the Acquisition Agreement. However, ***the Debtors failed to file or serve any notice of a proposed cure claim relating to the Acquisition Agreement, and the Thomas Parties were never required to submit their cure claim.*** Had they been required to

do so, the Thomas Parties would obviously have timely filed a cure claim which included the recoupment claims and defenses and contended that payment of damages for breach of the New Shareholder Leases was required.

15. The Plan Objection filed by the Thomas Parties referred back to the Limited Response, and repeated (at p. 5 ¶ 10) the argument that ***"the New Shareholder Leases were part of a unified acquisition transaction . . . [and] that rejection of the New Shareholder Leases would give rise to a defense, based on a right of recoupment, to the Debtors' indemnity claims under the Securities Purchase Agreement."*** The Plan Objection then went on (at p. 11 ¶ 27) to "object to confirmation of the Amended Plan on the grounds that it provides for the resolution of its claims and defenses under the Acquisition Agreement in a manner which is not consistent with the ADR provisions contained in the Acquisition Agreement."

16. The Plan Objection was resolved at the eleventh hour by the insertion of the above-quoted paragraph 44 of the Confirmation Order. This language contains no waiver of any legal rights of the Thomas Parties with respect to the cure claim or the right to arbitrate.

17. Counsel for the Debtors has not submitted in support of the Motion any written communication, email or other communication, even testimony concerning oral discussions, which support the interpretation that the language of paragraph 44 was intended as a waiver of any legal claim or defense, or a waiver of the right to arbitrate.

III. THE CURE CLAIM IS REQUIRED TO BE RESOLVED BY ARBITRATION

17. The Federal Arbitration Act ("FAA") provides at 9 U.S.C. § 2:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof . . . . shall be valid, irrevocable, and

> enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

18. 9 U.S.C. § 1 states that "'commerce,' as herein defined, means commerce among the several States . . . ." Given both the interstate operations of the businesses involved and the fact that the parties to the Acquisition Agreement were residents of different states, the Acquisition Agreement clearly constitutes a contract "evidencing a transaction involving commerce" such that the FAA applies to the ADR provisions of these contracts. See generally, *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, 55-56, 123 S.Ct. 2037, 156 L.Ed.2d 46 (2003).

19. 9 U.S.C. § 3 provides:

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

20. In opposing confirmation, the Thomas Parties only objected to the Plan's provisions for determining their cure claims, because the Plan did not require resolution of claims and defenses relating to the Acquisition Agreement according to the ADR provisions.

23. The Acquisition Agreement provides in part:

> (a) With the exception of disputes arising pursuant to Sections 10 and 22.6, any dispute, controversy or claim arising out of or relating to this Agreement or any transaction contemplated hereby, whether based on contract, tort, statute or other legal or equitable theory (including without limitation, any claim of fraud, misrepresentation or fraudulent inducement or any question of validity or effect of this Agreement including this clause) or the breach or termination thereof ("Dispute"), shall be resolved in accordance with this Section . . . .
>
> (b) The parties shall first use their reasonable and good faith efforts to settle any Dispute through non-binding mediation to be held in Orange County, California ("Mediation"), prior to initiating binding arbitration as

> set forth below. . . . If for any reason the parties are unable to resolve the Dispute within thirty (30) days following the date of the Notice of Dispute, such Dispute shall be resolved by binding arbitration to be conducted before the American Arbitration Association ("AAA") in accordance with the Commercial Arbitration rules and regulations promulgated by AAA as in effect at the time of the arbitration, and as follows . . . .

24. A good portion of the Debtors' Motion is taken up with an analysis of the merits of the position of the Thomas Parties, that damages for breach of the lease must be paid by the Debtors if they assume the Acquisition Agreement. The merits of the argument are discussed in the final section of this Objection. However, the Court should bear in mind that the merits of these claims must be resolved under the ADR provisions of the Acquisition Agreement. The scope of this particular arbitration clause, which specifically includes "statutory claims" is extraordinarily broad. The Debtor's Motion contains no assertion that these issues are not subject to arbitration under the ADR provisions. The Motion is based entirely on the idea that the right to arbitrate these issues was waived in the plan confirmation process.

25. There is no question that confirmation of a chapter 11 plan, as well as the allowance and disallowance of claims against the bankruptcy estate, including cure claims, are "core matters" as to which this Court has the jurisdiction to make a final determination. 28 U.S.C. § 157(b)(2)(B) & (L). However, whether any matter is or is not within the Bankruptcy Court's core jurisdiction "does not affect whether the Bankruptcy Court [has] the discretion to deny arbitration . . . ." *In re Mintze*, 434 F.3d 222, 229 (3d Cir. 2006).

26. *Mintze* was a chapter 13 case filed by a debtor who had, prepetition, notified her home mortgage lender of her intent to rescind for alleged violation of the Truth in Lending Act ("TILA" 15 U.S.C. §§ 1601-1667f). The Debtor commenced an adversary proceeding to enforce the rescission, then opposed the lender's motion to compel arbitration. The bankruptcy court

found that both the confirmation of the chapter 13 plan and the allowance of the lender's claim were core matters, and "decided that the matter was best resolved in the bankruptcy court system because the outcome of Mintze's rescission claim would affect her bankruptcy plan and the distribution of monies to her other creditors." *In re Mintze*, 434 F.3d 222, 227 (3d Cir. 2006). The United States District Court for the District of Delaware affirmed, but the Third Circuit reversed.

27. The Third Circuit held that the abuse of discretion standard of review did not apply to the appeal in *Mintze*, supra., because the above-quoted provisions of the FAA are mandatory in their requirement that courts must enforce contractual arbitration. In determining whether FAA applied, the Third Circuit applied the test articulated in *Shearson/Am. Exp., Inc. v. McMahon*, 482 U.S. 220, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987) and applied in *Hays & Co. v. Merrill Lynch Pierce, Fenner & Smith, Inc.*, 885 F.2d 1149, 1156 (3d Cir. 1989). As recapitulated in *Mintze*, supra., 434 F.3d at 229, the standard is as follows:

> By itself, the FAA mandates enforcement of applicable arbitration agreements even for federal statutory claims. See *McMahon,* 482 U.S. at 226, 107 S.Ct. 2332.
>
> The FAA's mandate can, however, be overridden. If a party opposing arbitration can demonstrate that "Congress intended to preclude a waiver of judicial remedies for the statutory rights at issue," the FAA will not compel courts to enforce an otherwise applicable arbitration agreement. *McMahon,* 482 U.S. at 227, 107 S.Ct. 2332. To overcome enforcement of arbitration, a party must establish congressional intent to create an exception to the FAA's mandate with respect to the party's statutory claims. Congressional intent can be discerned in one of three ways: (1) the statute's text, (2) the statute's legislative history, or (3) "an inherent conflict between arbitration and the statute's underlying purposes." *McMahon,* 482 U.S. at 227, 107 S.Ct. 2332.

28. The Court in *Mintze,* supra, found nothing in the Bankruptcy Code that evidenced a Congressional intent to make an exception to the FAA's mandate to enforce the arbitration clause contained in the loan documents. The Court concluded that "[i]f arbitration is enforced in this case, we likewise cannot perceive of a sufficiently adverse effect on the underlying purposes of the Bankruptcy Code." *In re Mintze*, 434 F.3d 222, 232 (3d Cir. 2006).

29. The Debtor in *Mintze* presumably argued that the ability to rescind her home mortgage loan was pivotal to her ability to confirm a chapter 13 plan. In contrast, in this case rights under the Acquisition Agreement and the New Shareholder Leases are not life or death matters for the Reorganized Debtors. As set forth in the two proofs of claim filed on behalf Gregg Street, LLC and Ralph Road, LLC (Street Decl. Exhs I and J) term of the two leases had only 15 months to run after the petition date, such that the amount of the claim even if not limited under Bankruptcy Code section 502(b)(6), would not have exceeded about $500,000 under each lease. A portion of that amount will be paid in any event on account of the Thomas Parties' lease rejection claims. In contrast, the projected 2009 financial statements of the reorganized Debtors, attached as Exhibit F to the Disclosure Statement, show total assets of $401,200,000, current assets of $234,800,000, and 2009 gross revenue of $693,000,000.

30. Under *Mintz,* the Bankruptcy Court is without discretion to deny arbitration of claims within the scope of the ADR provisions of the Acquisition Agreement. The only way that this Court can now adjudicate any aspect of those claims is to find that the Thomas Parties waived their right to arbitrate them by withdrawing their objection to confirmation after the Debtors agreed to include paragraph 44 in the Confirmation Order.

IV. THE THOMAS PARTIES DID NOT WAIVE THEIR ARBITRATION RIGHTS

31. Other than the Debtor's strained interpretation of paragraph 44 of the Confirmation Order, the Motion cites no statement or behavior by the Thomas Parties which would indicate an intention to waive the right to arbitrate all issues relating to the assumption of the Acquisition Agreement, including the cure claim. A finding of waiver of the right to arbitrate is not favored. See, *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25, 103 S.Ct. 927, 941-42, 74 L.Ed.2d 765 (1983).

32. In this case the right to arbitrate the issue of recoupment and the cure claim under the Acquisition Agreement was asserted by the Thomas Parties at the earliest possible moment in the chapter 11 case, in their Limited Response. This filing, quoted at greater length above, says in part that "[t]he Thomas Parties wish to make clear what they believe the consequences of [rejection of the New Shareholder Leases] will be, and to state that they do not intend to waive their right to arbitrate as to any claim, defense or right which may spring from the breach."

33. After the Debtors were advised of the Thomas Parties' position, almost one year ensued prior to Plan confirmation. Up to and including Plan confirmation, the Debtors took no steps, either in this Court or under the ADR provisions, to clarify whether they would be required to pay damages for breaching the New Shareholder Leases as part of the cure claim should they assume the Acquisition Agreement.

34. There was never a motion by the Debtors to assume the Acquisition Agreement. The Plan did not mention the Acquisition Agreement. It just generally provided for the assumption of all executory contracts not expressly rejected, and required the Debtors to serve a proposed cure claim on counterparties. As explained above, ***the Debtors failed to follow the***

procedures set forth in their own Plan, because they never filed or served a proposed cure claim on the Thomas Parties in relation to the Acquisition Agreement.

35. Notwithstanding that the amount of the cure claim still had not been placed in issue by the Debtors and wasn't before the Bankruptcy Court, the Thomas Parties filed their Plan Objection, quoted at length above, which reminded the Court of their position regarding recoupment and asked the Court to compel arbitration.

36. The Third Circuit has "consistently emphasized that 'prejudice is the touchstone for determining whether the right to arbitrate has been waived by litigation conduct.'" *Nino v. Jewelry Exchange, Inc.*, 609 F.3d 191, 209 (3d Cir. 2010) quoting *Ehleiter v. Grapetree Shores, Inc.*, 482 F.3d 207, 222 (3d Cir. 2007). By stating their position at the earliest moment in the case, the Thomas Parties avoided any alleged prejudice to the Debtors due to surprise.

37. Even if the Debtors mistakenly believed that the Thomas Parties had agreed to limit their claims and defenses, they have not been prejudiced by that misunderstanding. The Debtors have no appreciable affirmative duties post-closing under the Acquisition Agreement other than to cooperate in the defense of the construction defect claims (a duty that they continue to breach). The Debtors have not been burdened by their assumption of the Acquisition Agreement so far. They have only benefitted.

38. Under the Plan, the Debtors also have a second bite at the decision to assume or reject the Acquisition Agreement depending upon the resolution of the cure claim issue. The Plan provides at section 6.4, that "if an objection to a proposed Cure Claim is sustained by the Bankruptcy Court, the Reorganized Debtors may elect to reject such Executory Contract or Unexpired Lease in lieu of assuming it." The Debtor's Motion recognizes this when it states that "The Thomas Parties' argument is simply a belated effort to force the Reorganized Debtors to

reject the Acquisition Agreement, and thereby free the Thomas Parties from their substantial indemnity obligations . . . ."

39. If the Debtors are permitted to abide the outcome of the cure claim issues, and may then decide to reject based on an unfavorable outcome, they cannot claim prejudice based on any misunderstanding about the cure claim. In the meantime, the Debtors have not suffered any prejudice from having assumed the Acquisition Agreement. They have only received the benefit of the Thomas Parties' continuing obligation to indemnify.

V. THE CURE CLAIM IS NOT BARRED BY RES JUDICATA OR COLLATERAL ESTOPPEL

40. The Debtors argue that the Thomas Parties are now barred by res judicata and by collateral estoppel to argue before the arbitrator that defaults under the New Shareholder Leases should be compensated as part of the cure claim under the Acquisition Agreement.

> Res judicata "requires a showing that there has been (1) a final judgment on the merits in a prior suit involving (2) the same claim and (3) the same parties or their privies." *EEOC v. United States Steel Corp.*, 921 F.2d 489, 493 (3d Cir.1990). Collateral estoppel, on the other hand, requires of a previous determination that "(1) the identical issue was previously adjudicated; (2) the issue was actually litigated; (3) the previous determination was necessary to the decision; and (4) the party being precluded from relitigating the issue was fully represented in the prior action." *Jean Alexander Cosmetics, Inc. v. L'Oreal USA, Inc.*, 458 F.3d 244, 249 (3d Cir.2006) (citing *Henglein v. Colt Indus. Operating Corp.*, 260 F.3d 201, 209 (3d Cir.2001)).
>
> *U.S. v. 5 Unlabeled Boxes,* 572 F.3d 169 (3d Cir. 2009).

41. It is first of all questionable that the Confirmation Order is a "final judgment" with respect to the assumption of the Acquisition Agreement. Paragraph 44 specifically refers the matter of the cure claim to arbitration. The Plan provides that the Debtors may change their mind and reject the Acquisition Agreement depending upon the results of the arbitration.

42. It is also not the case that the Confirmation Order resolved the "identical" issue that the Debtors are now concerned about. The amount and nature of the cure claim was not before the Court at the time of the confirmation hearing, because the Debtors failed to follow the procedure called for in the Plan with respect to cure claims. The Plan placed the burden on the Debtors to file and serve a proposed cure claim on counterparties, and set a deadline for those counterparties to object. Had the Debtors done so the Thomas Parties would have, for the third time, stated their position that damages for abandonment of the New Shareholder Leases were part of the cure claim, and that issue would then have been before the Bankruptcy Court.

43. The issue of the cure claim was not before the Bankruptcy Court under the Plan procedures, and instead was deferred to arbitration as it was required to be. There is no language in the Confirmation Order that specifically addresses "the identical issue" to be arbitrated, i.e., the nature and amount of the cure claim. The Thomas Parties did not hide the ball with respect to these arguments in their Plan Objection. The Plan Objection referred back to the Limited Response, and repeated the argument that "***the New Shareholder Leases were part of a unified acquisition transaction. [and] that rejection of the New Shareholder Leases would give rise to a defense, based on a right of recoupment, to the Debtors' indemnity claims under the Securities Purchase Agreement.***"

44. If the Debtors wished to draft confirmation order language that specifically barred the arguments regarding the issues of recoupment and defenses arising from breach of the New Shareholder Leases, they could have done so. In that case, the Thomas Parties would have continued to oppose confirmation. Apparently, they decided instead to "finesse" the issue. The Debtors are now reduced to making complex arguments and strained interpretations which cannot establish a waiver on the part of the Thomas Parties.

VI. THE MERITS OF THE CURE CLAIM

45. The Debtors' Motion states, and the Thomas Parties agree, that the issue of whether the Debtors' breach of the New Shareholder Leases is a defense to enforcement of the Acquisition Agreement is a question of state law. It is also a question that depends on the intent of the parties to the contract. *In re Pollock,* 139, B.R. 938, 940 (Bankr. App. 9th Cir. 1992)(citing *Keen v. Harling,* 61 Cal.2d 318, 320, 38 Cal.Rptr. 513, 515, 392 P.2d 273 (1964). The issue must be decided on a case by case basis. *In re Plitt Amusement Co. of Washington, Inc.,* 233 B.R. 837, 843 (Bankr. C.D. Cal. 1999)(citing *Pilcher v. Wheeler,* 2 Cal.App.4th 352, 3 Cal.Rptr.2d 533 (1992)). Under California law, "it is not necessary that the instruments be considered as one contract for all purposes." *In re Plitt Amusement Co. of Washington, Inc.,* 233 B.R. at 843 (Bankr. C.D. Cal. 1999)(citing *Malmstedt v. Stillwell,* 110 Cal.App. 393, 294 P.41 (1930)).

46. All of the Debtor's arguments on this point overlook the fundamental fact that the application of California law to the Acquisition Agreement, the determination of the intent of the parties, and the decision "on a case by case basis" as to whether the breach of one contract affects rights or duties under another, ***are all matters for the arbitrator to determine.*** Unless this Court finds that the Thomas Parties have waived the right to arbitrate these issues, it must defer the resolution of these matters to the arbitrator, regardless of its view of the merits.

47. The Debtor's Motion cites the following factors listed in *In re Gardiner,* 831 F.2d 974, 976 (11th Cir. 1987)(applying Florida law) cited with approval by *In re Pollock,* 139, B.R. 938, 940-41 (Bankr. App. 9th Cir. 1992): (1) Whether the nature and purpose of the obligations are different; (2) whether the consideration for the obligations is separate and distinct; and (3)

whether obligations of the parties are interrelated. The Thomas Parties contend that each of these factors mitigate in favor of their position.

48. ***Nature and Purpose of the Obligations.*** The Debtors argue that one obligation is to pay rent under a lease while the other obligation is to indemnify the buyer of a business against future claims to the extent not covered by insurance. In fact, the relationship between the parties was to be synergistic. In addition of course to the payment of rent, both the Gregg Street Lease and the Ralph Road Lease require in section 1.1 that the leased premises must be used "only for roofing truss, floor and wall frame manufacturing operations . . . and related uses consistent with applicable law." The Acquisition Agreement on the other hand provides for the sale to the Debtors of that specific type of business.

49. The Acquisition Agreement requires a continuing relationship between the parties in relation to the handling of construction defect claims which arise from that exact type of business. The Thomas Parties did not want to be obligated to indemnify the Debtors if they had abandoned that business or the location, and became in effect a pile of unattended banker's boxes full of old records. The obligation to indemnify an ongoing manufacturing business operating in your back yard, with local personnel available and obligated to assist in the defense, is different and less burdensome than the obligation to indemnify an absentee company that has ceased those operations. Yet this is precisely the situation that developed when the Debtor's chose to abandon their business conducted at the Gregg Street and Ralph Road facilities.

50. The object of the Acquisition Agreement was to sell an integrated business, and the object of the New Shareholder Leases was to continue to operate that business in the same location for the same purposes. The New Shareholder Leases and the indemnity relationship are in that way closely related in nature and purpose.

51. ***Separate and Distinct Consideration.*** Mr. Thomas has testified, and is prepared to prove, that the rent under the New Shareholder Leases was made above market as the result of calculations intended to build a portion of the purchase price for the business into the rent. It is therefore not the case that the "consideration" for the payment of rent under the New Shareholder Leases was only the occupancy of the real property. It is also not true that the only "consideration" for the continuing indemnity obligation of the Thomas Parties under the Acquisition Agreement was payment of the purchase price. The Thomas Parties had a right to expect continuing rental income under the New Shareholder Leases, at a level negotiated as part of the purchase price, in exchange for their continuing obligation to indemnify the Debtors.

52. ***The Obligations Are Interrelated.*** Were this a case in which a Debtor affiliate had purchased a business from the Thomas Parties on the one hand, and then another Debtor affiliate, in a separate non-contemporaneous transaction, had leased space unrelated to the business on the other, the affiliate relationship between the tenant on the one hand and the business purchaser on the other would not be sufficient to render the obligations interrelated. Here however, the Debtors consist of a group of twelve affiliates who continued to engage in a complex series of mergers, acquisitions and name changes before and after the Acquisition Agreement. No Debtor party to the New Shareholder Leases or Acquisition Agreement appears to have the same name or corporate identity as it did when the bankruptcy petition was filed.

53. The Thomas Parties are prepared to prove to the arbitrator that the rent under the New Shareholder Leases was computed by the parties to be part of the consideration for the purchase of the business. The obligation of the Thomas Parties to indemnify the Debtors against claims was to have been bought and paid for, in part, by the performance of the Debtors under the New Shareholder Leases. It is unfair for the Thomas Parties to be stripped of part of the

bargained for purchase price while at the same time held to their obligations as sellers under the Acquisition Agreement.

54. ***Recoupment to Recover Failed Consideration Under the Acquisition Agreement.*** The leases entered into by the Debtors are referred to by the Asset Purchase Agreement as the "New Shareholder Leases." The description is an acknowledgement of the unity of interest between the landlord LLCs, Mr. Thomas and the Trust, as indemnitors under the Securities Purchase Agreement. The New Shareholder Leases in turn refer in their recitals to the Acquisition Agreement. The New Shareholder Leases are attached as exhibits to the Acquisition Agreement, and these exhibits are made a part of the Acquisition Agreement under the integration clauses. (Street Decl. Exh A at p. 39 ¶ 22.1).

55. The Debtors' breach of the New Shareholder Leases gives rise to a recoupment defense to continuing liability under the indemnity provisions of the Acquisition Agreement. "Recoupment is an equitable remedy which permits the offset of mutual debts when the respective obligations are based on the same transaction or occurrence. See, e.g., *Anes v. Dehart (In re Anes),* 195 F.3d 177, 182 (3d Cir.1999); *University Med. Ctr. v. Sullivan (In re University Med. Ctr.),* 973 F.2d 1065, 1081 (3d Cir.1992)." *In re HQ Global Holdings, Inc.,* 290 B.R. 78, 82 (Bankr. D. Del. 2003).

56. The Debtors in their Motion cite the fact that the Acquisition Agreement and New Shareholder Leases involve different parties, i.e., the Thomas Parties on the one hand and various Debtor affiliates on the other. While this issue might be fatal to claims based on setoff, strict mutuality of claims is not required under the doctrine of recoupment. "The Bankruptcy Code does not contain a recoupment provision. ***The common law doctrine of recoupment provides an exception to setoff in bankruptcy cases. . . . This doctrine is justified on the***

grounds that 'where the creditor's claim against the debtor arises from the same transaction as the debtor's claim, it is essentially a defense to the debtor's claim against the creditor rather than a mutual obligation, and application of the limitations on setoff in bankruptcy would be inequitable.' [***italics*** added] [quoting *Lee v. Schweiker,* 739 F.2d 870, 875 (3d Cir. 1984)]." *In re University Medical Center,* 973 F.2d 1065, 1079-80 (3d Cir. 1992).

57. In this case, the liability of the Debtors under the New Shareholder Leases did arise out of the same transaction as the Acquisition Agreement. To allow the Debtors to intentionally breach their obligation to pay rent under the New Shareholder Leases while continuing to reap the ongoing benefits of the Acquisition Agreement would be an injustice for which (the arbitrator should conclude) the doctrine of recoupment offers a remedy.

VII. CONCLUSION

58. Under the broad ADR provisions of the Acquisition Agreement, this Court was required under the Federal Arbitration Act to allow arbitration of all claims and defenses arising from the Debtors' assumption of that contract. The Thomas Parties asserted their right to arbitrate the cure claim at every opportunity, and also asserted at the same time their legal position that the doctrine of recoupment requires cure of defaults under the related New Shareholder Leases. Any waiver of the right to raise these issues before the arbitrator was required to be clear and specific. The language of paragraph 44 of the Confirmation Order did not constitute a waiver of those rights.

59. As the arbitration proceeds, the Debtors will suffer no prejudice if all of these issues are decided by the arbitrator. The Debtors will have the right to make all of the arguments on the merits which are presented in their Motion. In the meantime, pending completion of the arbitration, the Debtor suffers no burdens but only benefits from having tentatively assumed the

Acquisition Agreement, because the Thomas Parties' indemnity obligations are still in effect. The Plan provides the Debtor with a second opportunity to reject if the results of the arbitration are not satisfactory. The Debtors' motion should simply be denied, and the arbitration should be permitted to go forward.

DATE: September 17, 2010

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Attorneys for Robert R. Thomas
and The Restated Robert R. Thomas
Trust dated April 14, 2009

IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF DELAWARE

In re:	)	Chapter 11
	)	Case No. 09-12074 (KJC)
BUILDING MATERIALS HOLDING CORPORATION, et al. [1]	)	Jointly Administered
Debtors	)	**Re: Docket No. 1667**

DECLARATION OF ROBERT R. THOMAS IN SUPPORT OF OBJECTION BY ROBERT R. THOMAS AND THE RESTATED THOMAS TRUST DATED APRIL 14, 2009 TO DEBTOR'S MOTION FOR ENTRY OF IMPLEMENTATION ORDER WITH RESPECT TO PARAGRAPH 44 OF CONFIRMATION ORDER (RELATING TO ROBERT R. THOMAS AND THE RESTATED THOMAS TRUST)

I, Robert R. Thomas, declare:

1. I am the Trustee of the Restated Robert R. Thomas Trust Dated April 14, 1999 (the "Trust"). The term "Thomas Parties" as used in this Declaration refers to me individually and in my capacity as Trustee of the Trust. The Trust is the sole member of Ralph Road, LLC. I am also Co-Trustee of the Robert R. Thomas and Jane L. Thomas Declaration of Trust dated May 14, 1999 (the "Family Trust"). The Family Trust is the sole member of Gregg Street, LLC. The two trusts are referred to collectively in this Declaration as the "Thomas Trusts."

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[1] The Reorganized Debtors, along with the last four digits of each Reorganized Debtor's tax identification number are as follows: Building Materials Holding Corporation (4269), BMC West Corporation (0454), SelectBuild Construction, Inc. (1340), SelectBuild Northern California, Inc. (7579), Illinois Framing, Inc. (4451), C Construction, Inc. (8206), TWF Construction, Inc. (3334), H.N.R. Framing Systems, Inc. (4329), SelectBuild Southern California, Inc. (9378), SelectBuild Nevada, Inc. (8912), SelectBuild Arizona, LLC (0036), and SelectBuild Illinois, LLC (0792). The mailing address for the Reorganized Debtors is 720 Park Boulevard, Suite 200, Boise, Idaho 83712.

2. In my capacity as Trustee (as explained below) I am the managing member of Gregg Street, LLC and of Ralph Road, LLC, the landlords under two Shareholder Leases referred to below. I have personal knowledge of the facts stated herein and I could and would competently testify thereto if called as a witness.

3. In about 1988, I started HNR Framing Systems, Inc. ("HNR"). Prior to October, 2005, the Trust was the 100% shareholder of HNR.

4. In about 1997, I opened a roof truss yard in Poway, California under the name of Protruss Corporation. Protruss Corporation was an affiliate of HNR. The name was later changed to Home Building Components, Inc. ("HBC"). Prior to October, 2005, the Trust was also the 100% shareholder of HBC.

5. HBC manufactured roof trusses, which are large component parts installed as part of the framing of a roof on a home. HNR, on the other hand, actually performed framing on residential housing projects, including the use of trusses manufactured by HBC. The business enjoyed growth and great success as we acquired the capability to build floor systems and walls as well as roof systems.

6. HNR was the only framing company to have its own truss yard. This "control" over the truss fabrication and proper delivery times set us apart from the competition and allowed for continued growth. The existence of both the manufacturing company, HBC, and the framing company, HNR, created an important business synergy which gave HNR a substantial competitive advantage.

7. This competitive advantage was enhanced by the purchase and development of highly adapted and specialized business facilities. These included the following properties: (i) 13465 & 13495 Gregg Street, Poway, CA owed by Gregg Street LLC (Street Decl. Exh. C); (ii)

12345 Crosthwaite Circle, Poway, CA; and (iii) 340 West Ralph Road, Imperial CA, owned by Ralph Road, LLC (Attached to the Proof of Claim (Street Decl. Exh. J).

8. A portion of the leased premises (including the Crosthwaite facility and 13495 Gregg Street) were surrendered by later agreements with the Debtors (Street Decl. Exhs C, D, E & G) However, the Debtor retained, and continued to occupy (until about the date of its bankruptcy) the most highly specialized facilities specially adapted to synergized component manufacturing and framing businesses.

8.1 The facility at 13465 Gregg Street, Poway, CA, for example, included specially designed facilities for use and storage of plans and documents, IT facilities, dust recovery and soundproofing. The warehouse was designed to build floor trusses. Also, unlike normal tilt-up buildings, the doors of this building were specially constructed so that roof trusses could be removed and loaded onto trucks. The outside area included a 35,000 sq. ft. area in which trucks could be loaded.

8.2 The facility at 340 West Ralph Road was custom built to my specifications. It is the largest yard of its kind in the country. For example, it included an 8 car rail spur designed specifically for 80' "center beam" cars, used to haul lumber. The facility included two new 25,000 square foot buildings, seven older buildings, for office buildings and two maintenance buildings.

9. These specialized facilities, together with the competitive advantage created by the synergy between our manufacturing and framing operations, gave our companies a substantial competitive advantage.

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10. During the period 2003-2004, Building Materials Holding Corporation (the Debtor and its affiliates) attempted unsuccessfully to enter the Riverside / San Diego market. This venture, which they called KBI - SoCal, did not grow or fulfill their stated goal to be a "one stop shop" to America's top builders. BMHC's attention then turned to an acquisition of my companies.

11. In about October, 2005, the Thomas Parties and HNR entered into the Securities Purchase Agreement (Street Decl. Exh A). Under the Securities Purchase Agreement, the Trust agreed to sell 100% of the stock of HNR to BMC Construction, Inc. I am informed and believe that BMC Construction is now Selectbuild Construction, Inc., one of the Debtors in this chapter 11 case.

12. Concurrently, on behalf of HBC, I entered into an "Asset Purchase Agreement" (Street Decl. Exh. B). Under the Asset Purchase Agreement, HBC agreed to sell substantially all of its assets to FSC Construction, Inc. I am informed and believe that FSC Construction was later merged into one of the Debtor entities. The Securities Purchase Agreement and Asset Purchase Agreement are referred to collectively in this Declaration as the "Acquisition Agreement."

13. At the time that the Acquisition Agreement was entered into, I was a resident of California. The Thomas Trusts were each established by me as co-trustor under the laws of the State of California. HNR and HBC were California corporations with their chief executive offices in California. To the best of my knowledge, BMC Construction was a Delaware corporation which had executive offices both in Boise, Idaho and in San Francisco, California,

and maintained operations nationwide. To the best of my knowledge, FSC Construction was a Delaware corporation which had executive offices in Boise and in San Francisco.

14. During negotiations, representatives of BMHC negotiated to acquire all four leased facilities. They indicated that acquisition of these specialized facilities was critical to their business plans. In conjunction with the Acquisition Agreements, BMHC affiliates agreed to lease these properties. These new leases were specifically referred to in the Acquisition Agreement as the "New Shareholder Leases." My entering into the New Shareholder Leases at the closing of the transaction was made one of the explicit conditions to BMHC's obligation to consummate the acquisition. See Section 17.8, Securities Purchase Agreement, (Street Decl. Exh A) and Section 17.7, Asset Purchase Agreement, (Street Decl. Exh. B). I had to deliver the fully executed New Shareholder Leases for the above described facilities to BMHC at the closing. See Section 19.5, Securities Purchase Agreement, (Street Decl. Exh A) and Section 19.7, Asset Purchase Agreement, (Street Decl. Exh. B). Although I was glad to lease the facilities to Buyer, I was unwilling to sell them as part of the deal. Thus, the New Shareholder Leases were essential to BMHC's ability to operate the business that they wished to purchase and the New Shareholder Leases became an integral part of the deal.

15. The rent under the new Shareholder Leases was negotiated above market, as a part of the total consideration paid by the BMHC group for this integrated business. The "above market rent" was mutually beneficial to Buyer and Seller. Buyer did not have to pay as much cash at the closing and would effectively pay a portion of the purchase price in installments over many years. On the other hand, Seller would enjoy a stream of income for as long as the leases' terms and extension options (if exercised) lasted. The leased facilities were special purpose, custom designed and constructed solely to support the framing business operations of HNR. I

sold BMHC a "turnkey" operation, which is exactly what they wanted for their overall business plan. However, by assuming the Acquisition Agreements without curing, among other things, the 'deferred' portion of the purchase price, I have been deprived the full consideration of what I bargained for but BMHC gets to keep what I sold them.

16. Article 13 of the Securities Purchase Agreement includes an obligation on the part of the Thomas Parties to indemnify the Buyer, BMC Construction (now Selectbuild) against among other things any "Construction Defect Liability" (a term defined in the Agreement) caused by HNR prior to closing. As a framing contractor, HNR has been routinely named in many construction defect suits filed in California.

17. HNR is insured against these losses under various policies. However, there are various per-claim deductibles under the policies, including a $75,000.00 "self-insured retention" under a policy issued by Lloyds of London. Most construction defect cases filed against HNR are not meritorious and result from the deplorable practice of simply naming as a defendant every subcontractor who worked on a home (a "shake down"). If properly and vigorously defended, these shake down claims may usually be dismissed or settled for relatively small amounts.

18. Since the acquisition, the Trust has been subjected to a series of requests for indemnity under the Securities Purchase Agreement, has responded to those requests and paid already in excess of $400,000.00 in construction defect claims. However, since the acquisition Selectbuild has failed to fulfill its responsibilities under sections 13.4 and 13.5 of the Securities Purchase Agreement to mitigate losses by cooperating in the defense of third party claims. In particular, Selectbuild has failed to cooperate in providing access to the plans, contracts and project files, making the claims needlessly difficult to defend. I have protested Selectbuild's

breaches in writing, but as of the date of filing of the bankruptcy petitions, the Trusts had not yet initiated the dispute resolution procedures (mediation and arbitration) provided for under the Securities Purchase Agreement.

19. The Thomas Parties are preparing to initiate the ADR process required under the Acquisition Agreements and will promptly do so after the Court rules on this motion.

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct and that this Declaration was executed on September 17, 2010 at Alpine, California.

ROBERT R. THOMAS

CERTIFICATE OF SERVICE

I hereby certify that on this the 17th day of September, 2010, a copy of the foregoing *Objection by Robert R. Thomas and the Restated Thomas Trust Dated April 14, 2009 to Debtor's Motion for Entry of Implementation Order with Respect to Paragraph 44 of Confirmation Order (Relating to Robert R. Thomas and the Restated Thomas Trust)* was caused to be served on the following, in the manner so indicated:

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