

1 JEFFER MANGELS BUTLER & MITCHELL LLP  
BENNETT G. YOUNG (Bar No. 106504)

2 *byoung@jmbm.com*

3 Two Embarcadero Center, 5th Floor  
San Francisco, California 94111-3813

4 Telephone: (415) 398-8080

Facsimile: (415) 398-5584

5 Attorneys for

ARADIGM CORPORATION

6 Debtor and Debtor-in-Possession

7  
8 UNITED STATES BANKRUPTCY COURT

9 NORTHERN DISTRICT OF CALIFORNIA, OAKLAND DIVISION

10 In re

CASE NO. 19-40363 WJL

11 ARADIGM CORPORATION,

Chapter 11

12  
13 Debtor

**MEMORANDUM OF POINTS AND  
AUTHORITIES IN SUPPORT OF  
MOTION OF DEBTOR PURSUANT TO  
11 U.S.C. §§ 105, 362, 363, 364, 503 AND  
507, AND FED. R. BANKR. P. 2002, 4001,  
6003, 6004 AND 9014 FOR ORDER (I)  
AUTHORIZING THE DEBTOR TO  
OBTAIN SENIOR SECURED,  
SUPERPRIORITY, POSTPETITION  
FINANCING, (II) GRANTING LIENS  
AND SUPERPRIORITY CLAIMS, (III)  
MODIFYING AUTOMATIC STAY, AND  
(IV) GRANTING RELATED RELIEF**

14  
15  
16  
17  
18  
19 Hearing Date: May 29, 2019

Time; 10:30 a.m.

20 Place: 1300 Clay Street, Room 220  
Oakland, CA

21 Judge: Hon. William J. Lafferty

## TABLE OF CONTENTS

	<u>Page</u>
I. JURISDICTION .....	1
II. BACKGROUND .....	1
III. OVERVIEW OF PROPOSED DIP LOANS .....	3
IV. THE DEBTOR'S PREPETITION FINANCING.....	10
V. BACKGROUND TO THE PROPOSED POSTPETITION FINANCING .....	10
A. The Debtor's Liquidity .....	10
B. The DIP Loans .....	11
VI. BASIS FOR RELIEF REQUESTED.....	12
A. The Court Should Approve the DIP Loans Under Section 364(c). ....	12
B. The DIP Lenders Should Be Deemed Good Faith Lenders under Section 364(e) .....	15
C. The Scope of The Carve-out Is Appropriate.....	15
D. The Automatic Stay Should Be Modified on a Limited Basis.....	16
E. Bankruptcy Rule 4001(a)(3) Should Be Waived .....	16

## TABLE OF AUTHORITIES

	<u>Page</u>
<b>CASES</b>	
<i>Blue Earth, Inc. et al.</i> , Case No. 16-30296 (Bankr. N.D. Cal. Apr. 29, 2016).....	14
<i>In re Aeropostale, Inc.</i> , Case No. 16-11275 (SHL) (Bankr. S.D.N.Y. May 06, 2016).....	16
<i>In re Ames Dep't Stores</i> , 115 B.R. 34 (Bankr. S.D.N.Y. 1990).....	13, 15
<i>In re Capitol Station 65</i> , LLC, No. 1723627-B-11, 2018 WL 333863 (Bankr. E.D. Cal. Jan. 8, 2018).....	13, 14
<i>In re Farmland Indus., Inc.</i> , 294 B.R. 855 (Bankr. W.D. Mo. 2003).....	12
<i>In re Fleetwood Enterprises, Inc., et al.</i> , Case No. 09-14254-MJ (Bankr. C.D. Cal. Apr. 1, 2009) .....	16
<i>In re Gardens Reg'l Hosp.</i> , No. 2:16-BK-17463-ER, 2017 WL 7101146 (Bankr. C.D. Cal. July 28, 2017) .....	12, 16
<i>In re Los Angeles Dodgers LLC</i> , 457 B.R. 308 (Bankr. D. Del. 2011) .....	13
<i>In re Newzoom, Inc.</i> , Case No. 15-31141 (Bankr. N.D. Cal. Oct. 15, 2015) .....	14
<i>In re Rdio, Inc.</i> , Case No. 15-31430 (Bankr. N.D. Cal. Dec. 10, 2015) .....	14
<i>In re Reading Tube Indus.</i> , 72 B.R. 329 (Bankr. E.D. Pa. 1987) .....	13
<i>In re Republic Airways Holdings Inc.</i> , No. 16-10429(SHL), 2016 WL 2616717 (Bankr. S.D.N.Y. May 4, 2016) .....	13
<i>In re Simasko Prod. Co.</i> , 47 B.R. 444 (D. Colo. 1985).....	13
<i>In re Snowshoe Co.</i> , 789 F.2d 1085 (4th Cir. 1986) .....	13
<i>In re Sterling Mining Co.</i> , No. 09-20178-TLM, 2009 WL 2514167 (Bankr. D. Idaho Aug. 14, 2009) .....	12

1	<i>In re SunEdison, Inc.,</i>	
2	Case No. 16-10992 (SMB) (Bankr. S.D.N.Y. Apr. 26, 2016) .....	16
3	<i>In re Toys “R” Us, Inc.,</i>	
4	Case No. 17-34665 (Bankr. E.D. Va. Sep. 20, 2017) .....	14
5	<b>STATUTES</b>	
6	28 U.S.C.	
7	§ 157.....	1
8	§ 157(b)(2) .....	1
9	§ 1334.....	1
10	§ 1408.....	1
11	§ 1409.....	1
12	§ 1930(a) .....	7
13	United States Bankruptcy Code	
14	Chapter 5 .....	7
15	§ 363(c)(2)(B) .....	9
16	§ 364(c) .....	12
17	§ 364(c)(1) .....	12
18	§ 364(c)(2) .....	12
19	§ 364(e) .....	15
20	§ 506(c) .....	8
21	§ 544.....	9
22	§ 545.....	9
23	§ 547.....	9
24	§ 548.....	9
25	§ 549.....	9
26	§ 552.....	8
27	§ 552(b).....	8
28	§ 553.....	9
	§ 723(a) .....	9
	§ 724(a) .....	9
	§ 726(b).....	7

**RULES AND REGULATIONS**

**Federal Rules of Bankruptcy Procedure**

Rule 4001 .....	3
Rule 4001(a)(1) .....	16
Rule 4001(a)(3) .....	16
Rule 4001(c) .....	3
Rule 4001(c)(1)(B) .....	3, 5
Rule 4001(c)(1)(B)(i) .....	3, 7
Rule 4001(c)(1)(B)(iv) .....	7
Rule 4001(c)(1)(B)(vii) .....	7
Rule 4001(c)(1)(B)(ix) .....	6
Rule 4001(c)(1)(B)(xi) .....	7
Rule 4001(d) .....	3

**OTHER AUTHORITIES**

United States Bankruptcy Court, Northern District of California <i>Guidelines for Cash Collateral and Financing Stipulations</i> .....	7
The Wall Street Journal .....	4

1 The Debtor filed this Chapter 11 case in order to pursue a sale of its assets. Those assets  
2 consist of the Aradigm Technology, a portfolio of U.S. and foreign patents and associated know  
3 how for the formulation of inhaled antibiotics. The Debtor's assets are encumbered by the License  
4 and Collaboration Agreement (the "**Grifols License**") between the Debtor and Grifols, S. A.  
5 ("**Grifols**") pursuant to which the Debtor granted Grifols an exclusive worldwide license to  
6 commercialize the product while the Debtor retained the exclusive right to pursue regulatory  
7 approval and to manufacture the product.

8 As a result of the specialized nature of the Debtor's assets and the encumbrance posed by  
9 the Grifols License, a sale process is likely to take time. The Debtor, however, has limited revenue  
10 and relies on investor funding to fund its operations. At the time this Chapter 11 case was filed,  
11 the Debtor's cash resources were depleted, leaving the Debtor with a limited runway to pursue a  
12 sale.

13 In order to provide the Debtor with additional liquidity and therefore greater runway for a  
14 sales process, the DIP Lenders, which are managed by First Eagle Investment Management ("**First**  
15 **Eagle**"), the Debtor's second largest stakeholder, have agreed to lend the Debtor \$2 million  
16 secured by a lien on the Debtor's assets. These funds will enable the Debtor to retain an investment  
17 banker to assist the Debtor in the sale process and will extend the Debtor's runway for  
18 approximately seven to nine months, thereby substantially increasing the probability that the  
19 Debtor will successfully complete a sale of the Aradigm Technology for the benefit of all of its  
20 constituents.

21 Accordingly, the Debtor respectfully requests that the relief requested herein be granted.

22 **I. JURISDICTION**

23 The Court has jurisdiction to consider this matter pursuant to 28 U.S.C. §§ 157 and 1334.  
24 This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2). Venue is proper before the Court  
25 pursuant to 28 U.S.C. §§ 1408 and 1409.

26 **II. BACKGROUND**

27 The Debtor is a publicly traded emerging specialty pharmaceutical company focused on  
28 the development and commercialization of products for the treatment and prevention of severe

1 respiratory diseases. The Debtor has concentrated on the development of drug delivery  
2 technologies, particularly the development of respiratory drug delivery. The Debtor's lead product  
3 candidates are proprietary formulations of the potent antibiotic ciprofloxacin that are delivered by  
4 inhalation for the management of infections associated with the severe respiratory diseases of  
5 cystic fibrosis, non-cystic fibrosis bronchiectasis ("**NCFBE**") or infections with non-tuberculous  
6 mycobacteria.

7 The Debtor's inhaled ciprofloxacin formulation ("**Ciprofloxacin DI**") for the treatment of  
8 NCFBE patients with chronic lung infection with *P. aeruginosa* recently completed two Phase 3  
9 trials. In July 2017, the Debtor submitted a New Drug Application ("**NDA**") to the Federal Drug  
10 Administration ("**FDA**") for Ciprofloxacin DI. In January 2018, the FDA sent a Complete  
11 Response Letter ("**CRL**") stating that it cannot approve the NDA in its present form.

12 During the course of 2018 the Debtor had a meeting with the FDA to understand if a new  
13 submission under the Limited Pathway for Antimicrobial Drugs would be possible. The Debtor  
14 addressed all issues stated in the CRL and requested another meeting with the FDA. That meeting  
15 was held on January 25, 2019. At that meeting, the FDA reiterated the position taken in the CRL  
16 requesting that the Debtor conduct an additional Phase 3 trial. The Debtor estimates that a Phase 3  
17 trial will cost approximately \$75 million. The Debtor remains confident in the efficacy, safety and  
18 quality of Ciprofloxacin DI and is committed to continue working on the approval of  
19 Ciprofloxacin DI in the US for NCFBE patients who have very severe disease with high morbidity  
20 and mortality and no available treatment options.

21 In March 2018, the Debtor submitted a marketing authorization application ("**MAA**") to  
22 the European Medicines Agency ("**EMA**"), seeking approval for Ciprofloxacin DI for the  
23 treatment of NCFBE patients with chronic lung infection with *P. aeruginosa*. The EMA is  
24 currently reviewing the MAA for Ciprofloxacin DI according to standard timelines.

25 The Debtor continues to seek regulatory approval of Ciprofloxacin DI formulation to treat  
26 NCFBE patients. However, the Debtor has limited operating income and relies on investor capital  
27 to fund its operations and its research, development and regulatory effort. Addressing the delays  
28 the Debtor has experienced obtaining regulatory approval and the FDA's request for an additional

Phase 3 trial will require significant expenditures by the Debtor on additional research and development and regulatory activities, but the Debtor lacks the capital to fund these expenditures. The Debtor's principal funding partner, Grifols, indicated that it was unwilling to fund the new Phase 3 trial requested by the FDA and was unwilling to continue to fund the Debtor. The Debtor therefore determined to seek a buyer for its assets and filed this Chapter 11 case in order to conserve its cash resources and to pursue a sale of its assets.

### III. OVERVIEW OF PROPOSED DIP LOANS

The Debtor propose to enter into the DIP Loans to fund its operations, the administration of the Debtor's Chapter 11 Case and the Debtor's sale process. The DIP Loans preserve the Debtor's operations and provides the Debtor with sufficient liquidity to fund the administration of these cases and to pursue and consummate a successful sale of the Debtor's assets. The DIP Loans were negotiated in good faith and at arm's length. As discussed below and in the Thomas Declaration, the DIP Loans are the best postpetition financing option available to the Debtor and should be approved.

In accordance with Bankruptcy Rules 4001(c) and (d), the following table summarizes the material terms of the Order and the DIP Loans.<sup>1</sup>

Material Terms	Summary	Citation
<b>Borrower</b> Fed. R. Bankr. P. 4001(c)(1)(B)	Aradigm Corporation (the " <b>Borrower</b> ").	See DIP Credit Agreement; Order (preamble)
<b>DIP Lenders</b> Fed. R. Bankr. P. 4001(c)(1)(B)	<b>21 APRIL FUND, LTD.</b> , an exempted company organized under the laws of the Cayman Islands, and <b>21 APRIL FUND, L.P.</b> , a Delaware limited partnership.	See DIP Credit Agreement; Order (preamble)
<b>DIP Loans</b> Fed. R. Bankr. P. 4001(c)(1)(B)	The DIP Loans provide for (a) a first lien superpriority revolving credit facility in an aggregate principal amount of \$2.0 million.	See DIP Credit Agreement (§ 3.1); Order (preamble)
<b>Borrowing Limits</b>	\$2.0 million.	See DIP Credit

<sup>1</sup> As noted above, *see* note 1 *supra*, all capitalized terms listed in this table but not otherwise defined herein shall have the meaning ascribed to such terms in the DIP Credit Agreement. Any summary of the terms of the Order and DIP Loans contained in this Motion is qualified in its entirety by reference to the provisions of the actual Order and DIP Credit Agreement, as applicable. To the extent the Motion and the Order or DIP Credit Agreement are inconsistent, the Order or DIP Credit Agreement, as applicable, shall control. The Debtor reserves the right to supplement the statements made pursuant to Bankruptcy Rule 4001 herein.



1	<b>Material Terms</b>	<b>Summary</b>	<b>Citation</b>
2	Fed. R. Bankr. P. 4001(c)(1)(B)		Agreement (§ 3.1); Order (preamble and ¶ 2)
3			
4	<b>3-Month Forecasts</b> Fed. R. Bankr. P. 4001(c)(1)(B)	The Debtor will provide the DIP Lenders three month cash flow forecasts monthly on a rolling basis and monthly variance reports.	See DIP Credit Agreement (§ 8.1)
5			
6	<b>Use of DIP Proceeds</b> Fed. R. Bankr. P. 4001(c)(1)(B)	The DIP Loans proceeds shall be used (i) for working capital and general corporate purposes and (ii) to pay fees, costs and expenses incurred in connection with DIP Loans and professional and other fees and costs of administration incurred in connection with the Chapter 11 Cases.	See DIP Credit Agreement (§ 3.2); Order ¶ 6
7			
8			
9	<b>Interest Rates</b> Fed. R. Bankr. P. 4001(c)(1)(B)	Interest shall accrue at the Base Rate plus 3% per annum. The <b>Base Rate</b> will be the highest of (a) 1% and (b) the prime rate as published in the Money Rates Section or column of The Wall Street Journal; however, if such rate is, at any time while the obligations under the DIP Facility remain outstanding, no longer published, the Base Rate will be the average of the prime interest rates that are announced, from time to time, by the three (3) largest banks (by assets) headquartered in the United States that publish a prime, base or reference rate. Default interest shall equal an additional 3% per annum.	See DIP Credit Agreement (§ 1.1)
10			
11			
12			
13			
14			
15	<b>Expenses and Fees</b> Fed. R. Bankr. P. 4001(c)(1)(B)	Facility Fee of 2% of the Aggregate Commitment.	See DIP Credit Agreement (§ 4.6)
16			
17	<b>Maturity Date</b> Fed. R. Bankr. P. 4001(c)(1)(B)	The earlier of: January 31, 2020; the 363 Sale closing date, the effective date of any chapter 11 plan of Borrower; and the acceleration of the DIP Facility as a result of the occurrence of an Event of Default; provided, that the Maturity Date may be extended by Lender in Lender's sole and absolute discretion.	See DIP Credit Agreement (§§ 1.1, 3.1)
18			
19			
20			
21	<b>Mandatory Prepayments</b>	Upon the consummation of any Asset Sale or upon receipt of any proceeds arising from the incurrence of any Indebtedness, Borrower shall make a mandatory prepayment .	See DIP Credit Agreement (§ 3.3(a))
22			
23			
24	<b>Collateral and Priority</b> Fed. R. Bankr. P. 4001(c)(1)(B)(i)	<b>Collateral</b> – substantially all owned or hereafter acquired assets and property of the Borrower (the “Collateral”).  <b>Priority</b> - the DIP Lenders shall be granted the following on the Collateral:  <b>a) <u>First Priority Liens</u></b> - a perfected first priority security interest and lien on the Collateral to the extent such Collateral is not subject to valid.	See DIP Credit Agreement (§§ 3.4); Order, ¶¶ 3, 4
25			
26			
27			
28			

Material Terms	Summary	Citation
	<p>perfected and non-avoidable liens (“<b>First Priority Liens</b>”), subject to the Carve-Out and any Senior Permitted Liens;</p> <p>b) <b>Junior Liens</b> – a junior perfected security interest and lien on the Collateral to the extent such Collateral is subject to valid, perfected and non-avoidable liens in favor of third parties that were in existence on the Petition Date, or to valid and unavoidable liens in favor of third parties that were in existence on the Petition Date that were perfected subsequent to the Petition Date (“<b>Junior Liens</b>”, collectively with the First Priority Liens, the “<b>DIP Liens</b>”), subject to such valid liens, the Carve-Out and any Senior Permitted Liens; and</p> <p>d) <b>Superpriority Expense Claims</b> – superpriority administrative expense claims in the Chapter 11 Case of the Debtor (“<b>Superpriority Expense Claims</b>”), subject to the Carve-Out.</p>	
<b>Conditions to Closing</b> Fed. R. Bankr. P. 4001(c)(1)(B)	<p>Material closing conditions include:</p> <ul style="list-style-type: none"> <li>• Execution of DIP Credit Agreement</li> <li>• The payment of fees and expenses set forth in the DIP Loan Documents (which will be withheld from the initial Advance)</li> <li>• The accuracy of all representations and warranties and the absence of a default or event of default</li> <li>• Receipt of a valid and perfected security interest in the Collateral</li> <li>• Receipt of a three month cash flow forecast</li> <li>• Entry of the Order authorizing DIP Loans</li> <li>• No change has occurred that results in a Material Adverse Effect; provided, however, that any changes attributable solely to the commencement of the Chapter 11 Case shall not constitute a Material Adverse Effect.</li> </ul>	See DIP Credit Agreement (§ 6.1)
<b>Events of Default</b> Fed. R. Bankr. P. 4001(c)(1)(B)	Material events of default include:	See DIP Credit Agreement (§ 10.1)

1	Material Terms	Summary	Citation
2		<ul style="list-style-type: none"> <li>• Default in payment obligations;</li> </ul>	
3		<ul style="list-style-type: none"> <li>• Inaccuracy of representations and warranties when made or deemed made or breach of covenant;</li> </ul>	
4			
5		<ul style="list-style-type: none"> <li>• Entry of unstayed judgments;</li> </ul>	
6		<ul style="list-style-type: none"> <li>• Invalidity of loan documents, or security interests;</li> </ul>	
7			
8		<ul style="list-style-type: none"> <li>• Dismissal or conversion of cases to a case under chapter 7;</li> </ul>	
9		<ul style="list-style-type: none"> <li>• Appointment of a trustee or an examiner;</li> </ul>	
10		<ul style="list-style-type: none"> <li>• Entry of an order (1) staying, reversing, vacating, modifying or amending the Order, (2) granting relief from stay, (3) authorizing financing or sale of substantially all assets without the repayment of DIP Loans or (4) except as permitted by the DIP Loan Documents, granting senior or pari passu liens or superpriority claims;</li> </ul>	
11			
12			
13			
14			
15		<ul style="list-style-type: none"> <li>• Filing by the Debtor or any other party of a reorganization plan that does not require the repayment of the DIP Loans;</li> </ul>	
16			
17		<ul style="list-style-type: none"> <li>• Borrower fails to comply with the terms of the Orders or any other Bankruptcy Court order in any material respect; and</li> </ul>	
18			
19		<ul style="list-style-type: none"> <li>• Borrower seeks to, or supports (in any such case by way of any motion or other pleading filed with the Bankruptcy Court or any other writing to another party in interest executed by or on behalf of Borrower), any other Person's motion to disallow, in whole or in part, Lender's claim in respect of the Obligations or to challenge the validity, perfection, priority, non-avoidability or enforceability of the Liens in favor of Lender;</li> </ul>	
20			
21			
22			
23			
24			
25	<b>The Indemnification of Any Entity</b> Fed. R. Bankr. P. 4001(c)(1)(B)(ix)	Borrower shall indemnify and hold harmless the DIP Lenders and their Affiliates, officers, directors, employees, agents, advisors, attorneys, and representatives from and against any and all claims, damages, losses, liabilities and expenses (including reasonable fees of counsel and disbursements), joint or several, that may be incurred by or asserted or	See DIP Credit Agreement (§ 4.5)
26			
27			
28			

1	Material Terms	Summary	Citation
2		awarded, in each case arising out of or in connection with or relating to any investigation, litigation or proceeding, or the preparation of any defense with respect thereto, arising out of or in connection with or relating to the DIP Loan Documents, or the transactions contemplated thereby, or any use made or proposed to be made with the proceeds of the DIP Loans.	
6	<b>Waiver or Modification of the Automatic Stay</b> Fed. R. Bankr. P. 4001(c)(1)(B)(iv)	The automatic stay shall be modified as necessary to permit the granting of DIP Liens and to incur all DIP Obligations under the DIP Loan Documents and to authorize the DIP Lenders to retain and apply payments and to exercise the rights and remedies set forth in the Order.	See Order ¶ 14.
10	<b>Waiver or Modification of Applicability of Non-Bankruptcy Law Relating to the Perfection or Enforcement of a Lien</b> Fed. R. Bankr. P. 4001(c)(1)(B)(vii)	The Order is sufficient and conclusive evidence of the validity, perfection and priority of the DIP Liens without the necessity of filing or recording any financing statement, deed of trust, mortgage, or other instrument or document which may otherwise be required under the law of any jurisdiction or the taking of any other action to validate or perfect the DIP Liens or to entitle the DIP Liens to the priorities granted in the Order.	See Order ¶ 6.
15	<b>Carve-Out</b> Fed. R. Bankr. P. 4001(c)(1)(B)(i)	The DIP Liens and the DIP Superpriority Claim shall be subject and subordinate to a carve-out (the " <b>Carve-Out</b> ") that consists of: (a) all fees required to be paid to the Clerk of the Bankruptcy Court and the Office of the U.S. Trustee pursuant to 28 U.S.C. § 1930(a) in the Bankruptcy Case; (b) all reasonable and documented fees and expenses, not to exceed \$50,000.00 in the aggregate, incurred by a trustee under Bankruptcy Code section 726(b); (c) the aggregate amount of the fees and expense of Professionals to the extent reflected in the Budget through and including the Carve-Out Date; <i>provided, however,</i> that the Carve-Out may only be used for the payment of fees and expenses of Professionals to the extent allowed by order of the Bankruptcy Court in the Bankruptcy Case. Following the Carve-Out Date, amounts payable from the Carve-Out to Professionals for fees and expenses first incurred after such date shall not exceed \$250,000.00.	See Order ¶ 10_
25	<b>Liens on Avoidance Actions</b> Fed. R. Bankr. P. 4001(c)(1)(B)(xi)	Collateral will not include proceeds of causes of action arising under Chapter 5 of the Bankruptcy Code.	See Order ¶ 3_

Certain of the terms of the DIP Loans are terms that are identified in the Court's *Guidelines for Cash Collateral and Financing Stipulations* (the "**Guidelines**") as provisions that the Court will not ordinarily approve. For the reasons set forth herein, the Debtor submits that such terms are necessary and appropriate in the circumstances of this case.

Guidelines Provision		DIP Loans Description
1	Cross-collateralization clauses, <i>i.e.</i> , clauses that secure prepetition debt by postpetition assets in which the secured party would not otherwise have a security interest by virtue of its prepetition security agreement or applicable law. <i>See</i> Bankruptcy Code § 552.	None.
2	"Roll-ups," <i>i.e.</i> , such as provisions deeming prepetition debt to be post-petition debt or using post-petition loans from a pre-petition secured creditor to pay part or all of that secured creditor's pre-petition debt, other than as provided in Bankruptcy Code § 552(b), which deals with security interests in proceeds and profits.	None.
3	Provisions or findings of fact that bind the estate or all parties-in-interest with respect to the validity, perfection or amount of the prepetition secured party's lien or debt.	None.
4	Provisions or findings of fact that bind the estate or all parties-in-interest with respect to the relative priorities of the secured party's lien and liens held by persons who are not party to the stipulation (This would include, for example, an order approving a stipulation providing that the secured party's lien is a "first priority" lien).	None.
5	Waivers of, or grants of lien on, rights under Bankruptcy Code §506(c), unless the waiver or grant is effective only during the period in which the debtor is authorized to use cash collateral or borrow funds. (Otherwise a future trustee might be faced with a duty to care for and preserve collateral in the trustee's possession and no financial means for discharging that duty).	Paragraph 23 of the Order provides that the Debtor will waive its right to surcharge the DIP Secured Parties for administrative costs or expenses during the period that Borrower is authorized to borrow under the DIP Loans.
6	Provisions that operate, as a practical matter, to divest the debtor in possession or trustee of any discretion in the formulation of a plan or administration of the estate or limit access to the court to seek any relief under other applicable provisions of law.	Section 10.1(t) of the DIP Credit Agreement provides that it is an "Event of Default" under the DIP Credit Agreement if the Debtor or any other person files a Chapter 11 Plan that does not provide for the indefeasible payment in full in cash of the DIP Obligations.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

Guidelines Provision		DIP Loans Description
7	Releases of, or limitations on, liability for the creditor's alleged prepetition torts or breaches of contract.	None.
8	Waivers of, or liens on any of the estate's rights arising under Bankruptcy Code §§ 544, 545, 547, 548, 549, 553, 723(a), or 724(a), or the proceeds of any such rights.	None.
9	Automatic relief from the automatic stay upon default, conversion to Chapter 7, or appointment of a trustee.	Paragraph 14 of the Order provides for shortened notice to seek a lifting of the automatic stay to permit the enforcement of Lender's remedies under the Loan Documents.
10	Waivers and modifications of the procedural requirements for foreclosure mandated under applicable non-bankruptcy law.	None.
11	Waivers or limitations, effective on default or expiration, of the debtor in possession's or trustee's right to move for a court order pursuant to Bankruptcy Code § 363(c)(2)(B) authorizing the use of cash collateral in the absence of the secured party's consent.	None.
12	Findings of fact on matters extraneous to the approval process. (For example, in connection with an application to borrow on a secured basis, a finding that the debtor cannot obtain unsecured credit would be acceptable if supported by competent evidence, whereas a "finding" that the lender acted in good faith in declaring the prepetition loan in default would not be acceptable).	None.
13	Provisions providing unreasonable treatment with respect to fees or professionals retained by a creditors' committee compared to any carve-outs provided for professionals retained by the debtor in possession or trustee.	None.
14	Provisions that provide an inadequate carve-out for a subsequently appointed trustee in the case, whether before or after conversion.	The DIP Credit Agreement provides for a carve-out of \$50,000 for a subsequently appointed trustee.
15	Indemnification of any entity	Section 4.5 of the DIP Credit Agreement provides that Borrower shall indemnify and hold harmless the DIP Lenders and their Affiliates, officers, directors, employees, agents, advisors,



	Guidelines Provision	DIP Loans Description
		attorneys, and representatives from and against any and all claims, damages, losses, liabilities and expenses (including reasonable fees of counsel and disbursements), joint or several, that may be incurred by or asserted or awarded, in each case arising out of or in connection with or relating to any investigation, litigation or proceeding, or the preparation of any defense with respect thereto, arising out of or in connection with or relating to the DIP Loan Documents, or the transactions contemplated thereby, or any use made or proposed to be made with the proceeds of the DIP Loans

**IV. THE DEBTOR'S PREPETITION FINANCING**

The Debtor's prepetition financing consists entirely of unsecured debt. The Debtor's unsecured debt consists of promissory notes, convertible notes, and trade payables. The Debtor's promissory notes and convertible notes are held by Grifols and by First Eagle and its affiliates, including 21 April Fund, Ltd., one of the DIP Lenders. The aggregate amount outstanding is approximately \$37.2 million. As of the Petition Date, the Debtor's outstanding trade payables, including certain disputed claims, totaled approximately \$1.5 million. Thomas Decl. ¶ 7.

**V. BACKGROUND TO THE PROPOSED POSTPETITION FINANCING**

**A. The Debtor's Liquidity**

The Debtor has limited operating income and relies on investor capital to fund its operations and its research, development and regulatory effort. As such, the Debtor has limited liquidity. The Debtor has therefore downsized its operations. As of April 26, 2019, the Debtor had approximately \$949,00 cash on hand in its US accounts and approximately \$104,000 in accounts receivable. Prior to the filing of its Chapter 11 case, the Debtor substantially reduced its workforce to 13 persons. In an effort to give itself the most runway possible to effectuate a sale the Debtor converted all of its employees to part-time, rejected its expensive office lease and moved to cheaper quarters. Even with these cost savings measures, the Debtor projects that, absent the

1 proposed postpetition financing, it will run out of cash in or about the end of June 2019. Thomas  
2 Decl. ¶ 8.

3 Prior to filing its Chapter 11 case, the Debtor discussed with Grifols whether Grifols would  
4 continue to fund the Debtor. Grifols is the Debtor's largest shareholder, holding approximately  
5 48% of the Debtor's stock, and its largest creditor, with a claim based on promissory notes and  
6 convertible notes of approximately \$32 million. In addition, Grifols and the Debtor are parties to  
7 the Grifols License pursuant to which the Debtor granted to Grifols an exclusive worldwide  
8 license to commercialize the product as well as all liposomal ciprofloxacin products for various  
9 indications, in return for certain milestone payments and a royalty stream once the product was  
10 commercialized, while the Debtor retained the exclusive right to pursue regulatory approval and to  
11 manufacture the product. Grifols declined to continue to fund the Debtor. Thomas Decl. ¶ 9.

12 After filing the Chapter 11 case, the Debtor entered into discussions with First Eagle  
13 regarding First Eagle's willingness to fund the Debtor. First Eagle is the Debtor's second largest  
14 shareholder, holding approximately 26% of the Debtor's stock, and its second largest creditor, with  
15 a claim based on notes and convertible notes of approximately \$4.4 million. First Eagle indicated  
16 that it was willing to fund the Debtor postposition, but only on a senior secured, superpriority  
17 basis. Thomas Decl. ¶ 10.

18 **B. The DIP Loans**

19 Summaries of the material terms of the DIP Loans are set forth above and in the  
20 accompanying Thomas declaration. Thomas Decl. ¶ 11. The Debtors may use the DIP Loans for  
21 working capital and general corporate purposes, and to pay fees, costs and expenses incurred in  
22 connection with the administration of the chapter 11 case. *Id.*

23 The DIP Loans provide additional runway to the Debtor to market and sell its assets.  
24 Without the DIP Loans, the Debtor will run out of cash in or about June 2019. The DIP Loans will  
25 extend this runway for roughly seven to nine months. Thomas Decl. ¶ 12.

26 Furthermore, by extending the Debtor's runway to pursue a sale, the DIP Loans make  
27 feasible the retention by the Debtor of an investment banker to aid in the sale process. The Debtor  
28 believes that the process of selling its assets will be complicated as a result of the Grifols License



1 and therefore is not likely to be quick. In the Debtor's business judgment, the cost of an investment  
2 banker was not warranted with the short sale runway the Debtor would otherwise have. The DIP  
3 Loans afford the Debtor seven to nine months of additional time for a sales process. The longer  
4 runway will give an investment banker more time to have a positive impact on the process and, in  
5 the Debtor's judgment, justifies incurring the expense. Thomas Decl. ¶ 13.

6 **VI. BASIS FOR RELIEF REQUESTED**

7 **A. The Court Should Approve the DIP Loans Under Section 364(c).**

8 The Debtor requests authorization under section 364(c) of the Bankruptcy Code to grant  
9 the DIP Lenders three types of protections: (a) superpriority administrative claims pursuant to  
10 section 364(c)(1) (*See* DIP Credit Agreement § 2.19(a)); (b) senior liens on the Debtor's  
11 unencumbered assets pursuant to section 364(c)(2) (*id.* § 2.19(b)); and (c) junior liens on the  
12 Debtor's assets that are subject to a lien pursuant to section 364(c)(3) (*id.* § 2.19(c)). The Debtor  
13 has satisfied the requirements to obtain credit on these terms.

14 Under section 364(c), a debtor may grant superpriority administrative claims and incur  
15 secured debt if the court determines that the debtor was "unable to obtain unsecured credit  
16 allowable under section 503(b)(1) . . . as an administrative expense". 11 U.S.C. § 364(c). Courts  
17 evaluating requests for financing under section 364(c) consider whether certain factors are met,  
18 including that: (1) the proposed financing is an exercise of the debtor's sound and reasonable  
19 business judgment; (2) the financing agreement was negotiated in good faith and at arm's length;  
20 (3) no alternative financing is available on any other basis; (4) the terms of the transaction are fair,  
21 reasonable, and adequate, given the circumstances of the borrower and the proposed lender; (5) the  
22 financing is necessary, essential, and appropriate for the continued operation of the Debtor's  
23 businesses and the preservation of their estates; and (6) the financing is in the best interests of the  
24 estate and its creditors. *See In re Gardens Reg'l Hosp.*, No. 2:16-BK-17463-ER, 2017 WL  
25 7101146, at \*4 (Bankr. C.D. Cal. July 28, 2017) (approving postpetition financing under § 364(c)  
26 based on these factors); *In re Sterling Mining Co.*, No. 09-20178-TLM, 2009 WL 2514167, at \*3  
27 (Bankr. D. Idaho Aug. 14, 2009); *see also In re Farmland Indus., Inc.*, 294 B.R. 855, 879-81  
28 (Bankr. W.D. Mo. 2003) (discussing factors applied by bankruptcy courts across jurisdictions).

Each of these factors is satisfied here.

**1. The DIP Loans Reflect the Debtor's Sound Business Judgment.**

In evaluating proposed DIP financing under Section 364(c), courts generally defer to the business judgment of the debtor. *See In re Republic Airways Holdings Inc.*, No. 16-10429(SHL), 2016 WL 2616717, at \*10–11 (Bankr. S.D.N.Y. May 4, 2016); *In re Ames Dep't Stores*, 115 B.R. 34, 40 (Bankr. S.D.N.Y. 1990). Courts presume that debtors make financing decisions “on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company.” *In re Los Angeles Dodgers LLC*, 457 B.R. 308, 313 (Bankr. D. Del. 2011); *see also In re Simasko Prod. Co.*, 47 B.R. 444, 449 (D. Colo. 1985) (“The discretion to act with regard to business planning activities is at the heart of the debtor’s power.”) Courts will not “second-guess a business decision, so long as corporate management exercised a minimum level of care in arriving of the decision”. *In re Los Angeles Dodgers LLC*, 457 B.R. at 313; *see also In re Simasko Prod. Co.*, 47 B.R. at 449 (“business judgments should be left to the board room and not to this Court”).

Here, the Debtor sought additional funding from Grifols, its principal funding partner and the Debtor's largest creditor and largest shareholder. Grifols declined to fund, leaving the Debtor no choice but to file a chapter 11 case. After filing, the Debtor sought financing from First Eagle, the Debtor's other per-petition lender, which agreed to fund. Accordingly, the Debtor submits that the decision to enter into the DIP Loans are the product of their sound business judgment.

**2. The DIP Loans Were Negotiated in Good Faith and at Arm's Length, Their Terms Are Fair, Reasonable and Adequate, and the Debtor Could Not Obtain Credit Available on More Favorable Terms.**

A debtor is not required to seek alternative financing from every possible lender before it may grant administrative expense claims or incur secured debt. *See In re Snowshoe Co.*, 789 F.2d 1085, 1088 (4th Cir. 1986) (more favorable credit unavailable where debtor contacted lenders in the “immediate geographic area” and they would not extend unsecured credit); *see also In re Reading Tube Indus.*, 72 B.R. 329, 332 (Bankr. E.D. Pa. 1987). Rather, the debtor need only demonstrate that it made a “reasonable effort” to obtain unsecured credit from other lenders. *In re Ames Dep't Stores, Inc.*, 115 B.R. 34, 40 (Bankr. S.D.N.Y. 1990) (citing cases); *In re Capitol*

1 *Station 65, LLC*, No. 1723627-B-11, 2018 WL 333863, at \*12 (Bankr. E.D. Cal. Jan. 8, 2018).

2 Here, the Debtor approached its two pre-petition lenders to obtain additional financing.  
3 First Eagle agreed to fund, and the Debtor's negotiations of the terms of the DIP Loans were  
4 carried out in good faith and at arm's length. Thomas Decl. ¶ 10

5 Finally, as described more fully above, the Debtor was unable to obtain financing without  
6 agreeing to provide the lenders with certain terms enumerated in the Guidelines. The Debtor  
7 submits that approving such terms is appropriate under the circumstances because (a) the DIP  
8 Lenders were unwilling to extend credit without such terms; and (b) the terms of the DIP Loans  
9 are otherwise favorable to the Debtor and its estate. Notably, the DIP Loans do not subject the  
10 Debtor to any milestones related to a sale or plan process, and it contains no financial covenants.  
11 Moreover, provisions similar to the enumerated terms at issue here are frequently approved in this  
12 district, *see, e.g., Blue Earth, Inc. et al.*, Case No. 16-30296 (Bankr. N.D. Cal. Apr. 29, 2016)  
13 [Docket No. 116]; *In re Newzoom, Inc.*, Case No. 15-31141 (Bankr. N.D. Cal. Oct. 15, 2015)  
14 [Docket No. 153]; *In re Rdio, Inc.*, Case No. 15-31430 (Bankr. N.D. Cal. Dec. 10, 2015) [Docket  
15 No. 122], and in large chapter 11 cases elsewhere, *see, e.g., In re Toys "R" Us, Inc.*, Case No. 17-  
16 34665 (Bankr. E.D. Va. Sep. 20, 2017) [Docket No. 98].

17 For the foregoing reasons, the Debtor submits that the DIP Loans were negotiated at arm's  
18 length and in good faith, that its terms are fair, reasonable and adequate, and that the DIP Loans  
19 represent the best financing available to the Debtor under the circumstances.

20 **3. The DIP Loans are Necessary, Essential and Appropriate for the**  
21 **Continued Operation of the Debtor's Businesses and the Preservation**  
**of its Estate and are in the Best Interest of the Estate and its Creditors.**

22 The DIP Loans are necessary for the continued operation of the Debtor's business and the  
23 preservation of its estate. Without access to this financing, the Debtor would soon lack sufficient  
24 liquidity to continue operating, putting at risk the assets of the Debtor's estate. Thomas Decl. ¶ 8.  
25 Accordingly, the DIP Loans preserve the Debtor's operations and is in the best interests of the  
26 estate and its creditors.

27 ///

28 ///

1           **B.       The DIP Lenders Should Be Deemed Good Faith Lenders under Section 364(e)**

2           Section 364(e) of the Bankruptcy Code protects a good faith lender's right to collect on  
3 loans extended to a debtor, and its right in any lien securing those loans, even if the authority of  
4 the debtor to obtain such loans or grant such liens is later reversed or modified on appeal. Section  
5 364(e) provides that:

6           The reversal or modification on appeal of an authorization under this section [364  
7 of the Bankruptcy Code] to obtain credit or incur debt, or of a grant under this  
8 section of a priority or a lien, does not affect the validity of any debt so incurred, or  
9 any priority or lien so granted, to an entity that extended such credit in good faith,  
whether or not such entity knew of the pendency of the appeal, unless such  
authorization and the incurring of such debt, or the granting of such priority or lien,  
were stayed pending appeal.

10          11 U.S.C. § 364(e).

11          The DIP Loans are the result of the Debtor's reasonable and informed determination that  
12 the DIP Lenders offered the most favorable terms pursuant to which the Debtor could obtain  
13 postpetition financing. All negotiations regarding the DIP Loans were conducted in good faith and  
14 on an arm's length basis. The terms and conditions of the DIP Loans are fair and reasonable, and  
15 the proceeds of the DIP Loans will be used only for purposes that are permissible under the  
16 Bankruptcy Code. Further, no consideration is being provided to any party to the DIP Loans other  
17 than as described herein. Accordingly, the Court should find that the DIP Lenders are "good faith"  
18 lenders within the meaning of section 364(e) of the Bankruptcy Code, and are entitled to all of the  
19 protections afforded by that section.

20           **C.       The Scope of The Carve-out Is Appropriate**

21          The DIP Liens are subject to the Carve-Out. Without the Carve-Out, the Debtor and other  
22 parties-in-interest may be deprived of certain rights and powers because the services for which  
23 professionals may be paid in these Chapter 11 Cases would be restricted. *See In re Ames Dep't*  
24 *Stores, Inc.*, 115 B.R. 34, 38 (Bankr. S.D.N.Y. 1990) (observing that courts insist on carve-outs  
25 for professionals representing parties in interest because "[a]bsent such protection, the collective  
26 rights and expectations of all parties-in-interest are sorely prejudiced"). The Carve-Out does not  
27 directly or indirectly deprive the Debtor's estate or other parties-in-interest of possible rights and  
28 powers. Additionally, the Carve-Out ensures that assets will be available for the payment of fees

of the Clerk of Court or the Office of the United States Trustee for the Northern District of California and professional fees of the Debtor.

**D. The Automatic Stay Should Be Modified on a Limited Basis**

The relief requested herein contemplates a modification of the automatic stay to permit the Debtor to grant the DIP Liens and, subject to a five Business Day notice period, permit the DIP Lenders to enforce their remedies under the DIP Credit Agreement as against the Debtor. Stay modifications of this kind are ordinary and standard features for DIP financing, and in the Debtor's business judgment, are reasonable and fair under the present circumstances. *See, e.g., In re Gardens Reg'l Hosp.*, No. 2:16-BK-17463-ER, 2017 WL 7101146 (Bankr. C.D. Cal. Jul. 28, 2016); *In re Fleetwood Enterprises, Inc., et al.*, Case No. 09-14254-MJ (Bankr. C.D. Cal. Apr. 1, 2009) [Docket No. 183]; *In re SunEdison, Inc.*, Case No. 16-10992 (SMB) (Bankr. S.D.N.Y. Apr. 26, 2016) [Docket No. 87]; *In re Aeropostale, Inc.*, Case No. 16-11275 (SHL) (Bankr. S.D.N.Y. May 06, 2016) [Docket No. 99].

**E. Bankruptcy Rule 4001(a)(3) Should Be Waived**

The Debtor requests a waiver of the stay of the effectiveness of the order approving this Motion under Bankruptcy Rule 4001(a)(3). Bankruptcy Rule 4001(a)(3) provides, "[a]n order granting a motion for relief from an automatic stay made in accordance with Rule 4001(a)(1) is stayed until the expiration of fourteen days after entry of the order, unless the court orders otherwise." As explained herein, access to the DIP Loans is essential to prevent irreparable damage to the Debtor's estate. Accordingly, ample cause exists to justify the waiver of the fourteen-day stay imposed by Bankruptcy Rule 4001(a)(3), to the extent such stay applies.

No previous request for the relief sought herein has been made by the Debtor to this or any other court.

///

///

///

///

///

1 WHEREFORE the Debtor respectfully requests entry of the Interim Order granting the  
2 relief requested herein and such other and further relief as the Court may deem just and  
3 appropriate.  
4

5 DATED: May 1, 2019

JEFFER MANGELS BUTLER & MITCHELL LLP  
BENNETT G. YOUNG, ESQ.

6  
7  
8 By: /s/ Bennett G. Young  
BENNETT G. YOUNG  
9 Attorney for ARADIGM CORPORATION  
10 Debtor and Debtor-in-Possession  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28