UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MONTANA

In re **YELLOWSTONE MOUNTAIN CLUB, LLC**, Debtor.	Case No. **08-61570-11**
CREDIT SUISSE and **TIMOTHY L BLIXSETH**, Plaintiffs. -vs- **OFFICIAL COMMITTEE OF UNSECURED CREDITORS**, **YELLOWSTONE MOUNTAIN CLUB, LLC**, **YELLOWSTONE DEVELOPMENT LLC**, **BIG SKY RIDGE, LLC**, and **YELLOWSTONE CLUB CONSTRUCTION COMPANY LLC**, Defendants.	Adv No. **09-00014**

RECEIVED
By Jim Cossitt at 2:44 pm, May 12, 2009

Partial & Interim
ORDER

At Butte in said District this 13th day of May, 2009.

In this Adversary Proceeding, trial was originally scheduled to commence at 09:00 a.m.

on Wednesday, April 22, 2009. However, after considering Timothy L. Blixseth's ("Blixseth") Expedited Motion to Bifurcate and Continue Trial of Claims Regarding Blixseth filed April 21, 2009, at Docket Entry No. 203, the Court continued the trial date to Wednesday, April 29, 2009. The Debtors were represented at the trial in this Adversary Proceeding by Tom Hutchinson, Troy Greenfield, Connie Sue Martin and David A. Ernst of Seattle, Washington, and James A. Patten of Billings, Montana; Credit Suisse was represented by Mark S. Chehi, Robert S. Saunders and Joseph O. Larkin of Wilmington, Delaware, George A. Zimmerman, Evan R. Levy and Jeremy M. Falcone of New York, New York, Edward J. Meehan of Washington, D.C. and Shane Coleman of Billings, Montana; the Official Committee of Unsecured Creditors was represented by J. Thomas Beckett, Chris P. Wangsgard, Derek Langton, Sean D. Reyes and Mark W. Dykes of Salt Lake City, Utah, and James P. Cossitt of Kalispell, Montana; and Blixseth was represented by Michael J. Flynn of Boston, Massachusetts, Joseph M. Grant of Houston, Texas, and Joel E. Guthals of Billings, Montana. The Court heard expert testimony from David Abshier, John Hekman, Kent Mordy, and Christopher Donaldson. The Court heard fact testimony from Blixseth, Michael W. Doyle, Stephen R. Brown, Moses Moore, Brad Foster, Samuel T. Byrne, Edra Blixseth, Steve Yankauer, and Robert Sumpter. The testimony of the following witnesses was submitted through deposition transcript:[1] Jeff Barcy, Dean R. Paauw and William G. Griffon. Exhibit A

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[1] Blixseth listed George Mack as a trial witness in his Amended List of Witnesses filed April 27, 2009. Blixseth testified at trial that George Mack was in Missoula at the time of trial and available to testify. However, Blixseth did not call George Mack as a witness. After trial, a question arose regarding the admission into evidence of George Mack's deposition. Because George Mack was available to testify, but was not called, the Court declines to consider George Mack's deposition under Fed.R.Civ.P. 32(a), made applicable to this proceeding by F.R.B.P. 7032. For the reasons just stated, and because Stephen R. Brown testified, the Court will

attached hereto identifies the Exhibits that were offered and admitted into evidence.

Prior to commencement of trial on April 29, 2009, the Official Committee of Unsecured Creditors ("Committee"), the Debtors and Credit Suisse filed a proposed Final Pretrial Order on April 27, 2009, at Docket Entry No. 238. Blixseth participated in drafting the aforementioned proposed Final Pretrial Order but then proposed additional changes that could not be timely reviewed and approved by the Committee, Debtors and Credit Suisse. Thus, Blixseth instead filed his own proposed Final Pretrial Order on April 27, 2009, at Docket Entry No. 241. After hearing comments from counsel and after considering both proposed Final Pretrial Orders, the Court made some of Blixseth's proposed adjustments to the proposed Final Pretrial Order submitted by the Committee, Debtors and Credit Suisse and entered a Final Pretrial Order on April 29, 2009, at Docket Entry No. 257. The Final Pretrial Order approved by the Court supercedes the pleadings filed by the parties and governed the course of the trial.[2]

This Order is abbreviated and limited, and serves only as an interim ruling for purposes of facilitating the upcoming auction of the Debtors' assets. This Order will be followed by a subsequent detailed Memorandum of Decision and Order that will decide all matters heard at trial.

HISTORICAL BACKGROUND

Various pleadings introduced in this Adversary Proceeding and in the main bankruptcy case state that in 1992, Plum Creek Timber Co., a subsidiary of Northern Pacific Railroad

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similarly not consider the deposition testimony of Stephen R. Brown.

[2] The Court noted that the Final Pretrial Order could be subsequently modified to prevent manifest injustice.

Company sold its land in the Gallatin National Forest to Blixseth and the McDougal brothers, foresters from Oregon. Blixseth consolidated his land holdings with three deals with the federal government to swap 100,000 acres he had just bought for the acreage that now encompasses the Debtors' real estate holdings known as the Yellowstone Club located in Madison County, Montana. The deal with the government also included additional land in several other Montana counties, plus 250 million feet of salable timber. The land swaps required two separate acts of Congress. The first, known as the Gallatin Preservation Act of 1993, covered 38,000 acres and was President Clinton's first major piece of environmental legislation. The second act, in 1998, is known as Gallatin II and involved another 54,000-acre swap. The public acquired another 8,100 acres in a third swap that was not subject to Congressional approval. Soon after the assemblage was completed, Blixseth and the McDougals dissolved their partnership. The timberland was distributed to the McDougal brothers and Blixseth retained the acreage that could be developed.

Blixseth and his former wife, Edra Blixseth ("Edra"), formed the Debtor corporations and on the land that Blixseth retained from his partnership with the McDougal brothers, began development in late 1999 of the world's only private ski and golf community, commonly referred to as the Yellowstone Club.[3] The Yellowstone Club is a membership only master-

[3] Cushman & Wakefield's appraisal as of July 1, 2005, states that the Yellowstone Club "appeals to ultra-wealthy families as a second-home (or third-home) location for its private recreational facilities (particularly the ski area), views, and proximity to winter and summer recreation. Prospective buyers are required to have a net worth of over $3 million, but based on the costs of membership and housing, we would expect nearly all buyers to have investable assets of at least $5 million, if not $10 million. The membership price for residents is $250,000 for a 30-year refundable deposit. The price is expected to be increased during the sell-out period. Annual dues . . . were recently raised from $10,600 to $16,000 per year. Property owners association (POA) dues are currently $5,100 per year."

planned unit development, situated on 13,500 acres of private land in Madison County, Montana near the northwest corner of Yellowstone National Park.

The Blixseths originally contemplated that the Yellowstone Club would consist of seven planned residential areas or neighborhoods comprised of roughly 864 fee dwelling units in 2,700 acres of development pods. To get the Yellowstone Club off the ground, the Blixseths sold equity interests in the Yellowstone Club to various persons, who were referred to as Pioneer and Frontier Members. The 25 Pioneer and 15 Frontier memberships were sold at substantially reduced prices.

FACTS

On September 30, 2005, the Debtors were controlled by Blixseth as the sole Class A Shareholder through his holding company, Blixseth Group, Inc. ("BGI"). Approximately 13% of the Club was owned by Class B Members who were referred to as the Class B Shareholders or the "Bs" in this litigation. BGI was an Oregon sub-S corporation, which was solely owned by Blixseth as President and CEO from 1999 to mid-August of 2008.

In or around December of 2004, Jeffrey Barcy ("Barcy"), a Director in Credit Suisse's Investment Banking Division, made several attempts to send Blixseth and his secretary or assistant emails that contained a two to three-page teaser, providing Blixseth with a brief overview of Credit Suisse and its new loan product referred to as a syndicated term loan, which was described to Blixseth as something akin to a "home-equity loan." Blixseth eventually responded to Barcy's emails by calling Barcy on the telephone. Blixseth and Barcy had a brief phone conversation and following the telephone conversation, the "next marketing step [for Barcy and his team] was a trip up to the Yellowstone Club[.]" Following the initial meeting at

the Yellowstone Club, Barcy testified that although he could not remember exact details, he and Blixseth "had a number of phone conversations and probably emails back and forth as to why it would be interesting for [Blixseth] to potentially do a loan on the Club."

Credit Suisse was specifically trying to "break new ground with a product by doing real estate loans in the corporate bank loan market." Through its new syndicated term loans, Credit Suisse was able to offer a loan product the size of which had previously been unavailable to borrowers. Barcy testified that Credit Suisse's syndicated loan product had previously been marketed to other master-planned residential and recreational communities such as Tamarack Resort, Promontory, Ginn, Turtle Bay, and Lake Las Vegas. Each of the above entities received a syndicated loan from Credit Suisse's Cayman Islands branch, which allowed the equity holders in said entities to take sizeable distributions from all or part of the Credit Suisse loan proceeds. According to Steve Yankauer ("Yankauer"), a Managing Director at Credit Suisse, Credit Suisse's Cayman Islands branch was created in 2005 to facilitate the syndicated loan product and to Yaunkauer's knowledge, Credit Suisse never had a physical presence in the Cayman Islands.

Blixseth originally declined Credit Suisse's loan offer, but then contacted Barcy a couple months later and "said that he might have a use of the proceeds for the loan and would be interested in talking again." Following Blixseth's call, Barcy and another person from Credit Suisse met Blixseth at Blixseth's home in Palm Springs, California. Blixseth initially agreed to take a loan of only $150 million. After several months of negotiations between Credit Suisse First Boston and Blixseth, the proposed amount of the loan grew from $150 million to $375 million.

Credit Suisse, Cayman Islands Branch, and Blixseth, on behalf of the Debtors, eventually entered into a credit agreement dated September 30, 2005 ("Credit Agreement"). In the time leading up to September 20, 2005, Barcy testified that Credit Suisse did “a fair amount of due diligence.” Such due diligence included doing a background check on Blixseth and hiring an appraisal firm to provide an “independent assessment” of the Yellowstone Club's cash flows and a law firm to “do a separate legal investigation into the Club to make sure that the entities we were financing against truly held the assets that we believed we were financing.”

Curiously, Credit Suisse never requested audited financial statements from the Debtors and in fact, appears to have relied exclusively on the historical and future projections provided by Blixseth and the Debtors. Credit Suisse's financial due diligence instead consisted, as stated above, of commissioning Cushman & Wakefield to do an analysis of the Debtors' cash flows. Cushman & Wakefield was originally hired to do a fair market appraisal of the Debtors. However, the terms of engagement were eventually altered to provide that Cushman & Wakefield would perform a total net value analysis of the Debtors. Barcy explained that Credit Suisse's capital market group suggested and then developed, in conjunction with Cushman & Wakefield, a new form of appraisal methodology, which Credit Suisse termed “total net value”. The Total Net Value methodology was first developed when Credit Suisse was selling its syndicated loan product to Lake Las Vegas. Credit Suisse's Total Net Value methodology does not comply with the Financial Institutions Recovery Reform Act of 1989 (“FIRREA”), but that was not important to Credit Suisse because Credit Suisse was seeking to sell its syndicated loans “to non bank institutions.”

Barcy also testified that he was aware of a prior limited appraisal of the Debtors'

property that Cushman & Wakefield did on behalf of American Bank. In that limited appraisal, as of September 21, 2004, Cushman & Wakefield determined that the "as-is market value" of those assets that later served as collateral for Credit Suisse's $375 million loan was $420 million. The $420 million as-is valuation was based on a discount rate of 18.5 percent. Barcy and Credit Suisse apparently gave little, if any, regard to Cushman & Wakefield's September 21, 2004, appraisal and instead placed their reliance solely on Credit Suisse's newly created Total Net Value valuation.

Similar to the syndicated loans to Tamarack Resort, Promontory, Ginn, Turtle Bay and Lake Las Vegas, the Yellowstone Club Credit Agreement was originally drafted to provide that the proceeds of the loan would be used, in part, for "distributions" to members of the Borrower for purposes unrelated to the Yellowstone Development. During the same period of time that Blixseth was negotiating with Credit Suisse for his loan, Blixseth was also attempting to buy the interests of the B shareholders under the guise that Blixseth wanted to repurchase the "B" shares for estate planning purposes and to involve his children in ownership of the Yellowstone Club. Not all the B shareholders agreed to Blixseth's proposed purchase and thus, Blixseth purchased none of the B shareholders' interests because his offer was an all or nothing deal.

Coincidentally, in late August of 2005 or early September of 2005, about the same time that Blixseth was unsuccessful in buying the B shareholders' interests, Blixseth was allegedly advised by his attorneys and accountants that he would have to take the Credit Suisse loan proceeds as a loan rather than a distribution. The reasoning was two-fold. First, Blixseth would have tax consequences on a distribution. Second, recording such a large distribution on the Debtors' books would result in negative owners' equity accounts.

Barcy testified that Credit Suisse knew that “there were a number of minority investors in the Club.” However, Barcy was not concerned when Blixseth contacted Credit Suisse sometime between August 22, 2005, and September 4, 2005, and requested that the Credit Agreement be modified to provide that the loan proceeds could be used: “(I) for distribution *or loans* up to [$ ____] to affiliates of the borrower for purposes unrelated to the Yellowstone Development[.]” Between September 4, 2005, and September 30, 2005, the recitals were once again amended to finally provide that the proceeds of the loan would be used “(I) for distribution or loans up to $209,000,000 to members of the Borrower for purposes unrelated to the Yellowstone Development, (ii) for investments up to $142,000,000 into Unrestricted Subsidiaries for purposes unrelated to the Yellowstone Development, (iii) to pay the Transaction Costs, (iv) to refinance the Existing Indebtedness, (v) to finance a portion of the development and construction costs associated with the Yellowstone Development in accordance with the Financial Plan[.]” Barcy testified that it was Blixseth's “responsibility to figure out what he had to do internally to make those distributions or not make those distributions. And as a controlling shareholder of the Yellowstone Club, that was in his court.”

Nothing in the record suggests that the loan between Credit Suisse and Blixseth (disregarding, however, the minority shareholders) was not at arm’s length. For instance, Credit Suisse originally sought a transaction fee of 3 percent, but Blixseth wanted the transaction fee reduced to 2 percent. Credit Suisse, via Barcy, and Blixseth ultimately agreed to "flip a coin" to decide the rate. Credit Suisse lost the toss, and Blixseth was thus successful in reducing the transaction fee to 2 percent.

After several months of negotiations, Credit Suisse and Blixseth finally came to an

agreement on the terms of the Credit Agreement and executed the same. The Credit Agreement provided for the disbursement of $375 million in loan proceeds to be distributed in two significant ways after payment of $7.5 million in fees to Credit Suisse and other expenses attributable to the loan. First, the Credit Agreement designated up to $209 million of the loan proceeds to be used as "distributions or loans" for "purposes unrelated" to the Yellowstone Club. Additionally, up to $142 million was authorized to be used for investments into "unrestricted subsidiaries" for "purposes unrelated" to Yellowstone Club development. Thus, the bulk of the loan proceeds, up to $351 million, were designated to be used for purposes outside of, and unrelated to, the Yellowstone Club.

In the years leading up to the Credit Agreement, the Yellowstone Club carried a debt load ranging from a low of approximately $4 to $5 million to a high of approximately $60 million on a revolving line of credit. The day before the Loan Transaction, the Yellowstone Club carried approximately $19 to $20 million in debt on its books, consisting of a combination of a revolving line of credit and a term loan with American Bank. The majority of this debt was related to the construction of the Warren Miller Lodge, which was already underway.

The Debtors had also experienced negative cash flows in several of the years leading up to the Credit Agreement with Credit Suisse. Several of the witnesses made reference to EDITDA, which is earnings before interest, taxes, depreciation and amortization.[4] Kent Mordy ("Mordy"), a certified public accountant and a certified insolvency and reorganization advisor,

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[4] From what the Court understands, EBITDA can be used to analyze and compare profitability between companies and industries because it eliminates the effects of financing and accounting decisions. However, this is a non-GAAP measure that allows a greater amount of discretion as to what is, and is not, included in the calculation. EBITDA is a good metric to evaluate profitability, but not cash flow.

calculated that the Debtors' Cash EBITDA was a negative $15,701,772 in 2002, a positive $20,369,766 in 2003, and a negative $45,910,598 in 2004. According to Mordy, the Debtors projected Cash EBITDA of $83,500,000 in 2005 but realized Cash EBITDA of only $19 million. Dr. John S. Hekman ("Hekman"), who has a Ph.D in economics and is employed by LECG to provide expert witness testimony in the area of real estate and real estate finance, also did an EBITDA calculation. Hekman's EBITDA calculation for 2005 was $39 million. Mordy explained that his Cash EBITDA numbers were different from Hekman's EBITDA calculations, which were positive for 2003, 2004 and 2005, because Hekman did not subtract capital expenditures and development costs. Yankauer disputed Hekman's and Mordy's EBITDA calculations for 2005, arguing that such figure was closer to $55,610,953. Whatever the accurate number, it is clear that even though the Debtors' had nine months of operations under their belt before the September 30, 2005, Credit Agreement, they missed their profitability projections by a substantial amount. Such numbers show that Debtors' projections for the future, upon which Credit Suisse relied without question, had no foundation in historical reality.

Hekman also testified that the Federal Reserve aggressively lowered interest rates in 2001 to counteract the 2001 recession. As a result of the low interest rates, Hekman characterized 2003 and 2004 as the peak years for real estate. However, due to concerns about the housing bubble, the Federal Reserve began raising interest rates in 2005, which caused the beginning of a slowdown in the real estate markets.

Despite all the red flags, the Credit Agreement was consummated and $342,110,262.53 was wired to the Yellowstone Club. This amount reflected the total loan amount of $375 million less fees, administrative costs, and a $24,241,910.98 takeout to payoff preexisting debt.

On the same date that $342,110,262.53 was transferred to the Debtors, approximately $209 million was transferred out of the Yellowstone Club by Blixseth to BGI. As previously noted, the transfer of loan proceeds out of the Yellowstone Club was a key feature of the product that Credit Suisse used to sell the loan. Yankauer testified that the cornerstone of this loan product was that it allowed preferred resort owners, such as Blixseth, to capitalize on the value of their asset.

The immediate transfer of funds out of the Yellowstone Club to BGI and then to Blixseth was not memorialized in any contemporaneous loan documents but was simply reflected on the Debtors' books with a journal entry. Blixseth, right around the time the B shareholders were threatening suit against Blixseth and the Yellowstone Club, drafted a two-page promissory note in the amount of $209 million. The $209 million unsecured demand note, payable by BGI to the Debtors, was created in May 2006, and backdated to September 30, 2005.

Roughly all of the $209 million proceeds that were transferred to BGI were then disbursed to various personal accounts and payoffs benefitting Tim and Edra Blixseth personally. Blixseth testified that the Debtors had no interest in any of these accounts or payoffs. The Debtors, under Blixseth' direction, never made demand of BGI on the demand notes, even when the Yellowstone Club needed cash.

From 2005 through the filing of the bankruptcy, the Yellowstone Club was persistently behind in its accounts payable. When the need for cash would become imperative, Moses Moore ("Moore"), who worked as a Senior Accountant and then later Comptroller for the Yellowstone Club, would request money from George Mack ("Mack"), who served at that time

as the Yellowstone Club's outside accountant. Mack was a go-between between Blixseth and Moore when Moore needed money to pay the bills at the Yellowstone Club. After Moore would make a request for funds, Moore testified that money may or may not appear in the Yellowstone Club's accounts. Moore testified that it was not uncommon to have to shuffle the Yellowstone Club's accounts payables due to a lack of money, and creditor and vendor invoices would often go unpaid for 90 days or more.

When funds were tight, rather than make a demand on the BGI promissory note, Blixseth would instead seek to obtain operating funds from various members of the Yellowstone Club. One such member that Blixseth approached was Samuel T. Byrne ("Byrne"). Byrne, the founder and managing partner of CrossHarbor, first visited the Yellowstone Club in 2004 or 2005 as a guest of another Yellowstone Club member. As a result of his visit, Byrne purchased two Yellowstone Club lots in 2005. Blixseth approached Byrne and asked whether he would be interested in making a bulk purchase of Yellowstone Club lots at a substantially reduced price. Byrne made his first bulk purchase in 2006 by taking over the 58 unit Sunrise Ridge Condominium Development for a price of $60 million. In August of 2007, Blixseth again approached Byrne to purchase 31 lots on the golf course. That sale was consummated in August of 2007 at a price of $54 million.

The foregoing facts form the basis for the Court's decision regarding the Debtors' and the Committee's equitable subordination claim. The Court has carefully reviewed the case law under 11 U.S.C. § 510(c), and concludes that equitable subordination is an appropriate remedy in this case. Under § 510(c), a court may, based upon equitable considerations, subordinate for purposes of distribution all or a part of a claim or interest to all or part of another. 11 U.S.C. §

510(c). This Court's decision to grant the Debtors and the Committee equitable relief is reviewed for an abuse of discretion. *See Grosz-Salomon v. Paul Revere Life Ins. Co.*, 237 F.3d 1154, 1163 (9th Cir.2001).

In the Ninth Circuit:

> The subordination of claims based on equitable considerations generally requires three findings: "(1) that the claimant engaged in some type of inequitable conduct, (2) that the misconduct injured creditors or conferred unfair advantage on the claimant, and (3) that subordination would not be inconsistent with the Bankruptcy Code." *Feder v. Lazar (In re Lazar)*, 83 F.3d 306, 309 (9th Cir.1996) (citing *Benjamin v. Diamond (In re Mobile Steel Co.)*, 563 F.2d 692, 699-700 (5th Cir.1977)).

In re First Alliance Mortg. Co., 497 F.3d 977, 1006 (9th Cir. 2006). When the remedy of equitable subordination involves a non-insider, non-fiduciary, "the level of pleading and proof is elevated: gross and egregious conduct will be required before a court [can] equitably subordinate a claim." *Id.*

The court in *Waslow v. MNC Commercial Corp. (In re Paolella & Sons, Inc.)*, 161 B.R. 107, 119 (E.D. Pa. 1993), recognized that equitable subordination is seldom used in a non-insider, non-fiduciary scenario because,

> [a]s Judge Easterbrook pointed out in *Kham & Nate's Shoes No. 2, Inc. v. First Bank*, 908 F.2d 1351, 1356 (7th Cir.1990), "[c]ases subordinating the claims of creditors that dealt at arm's length with the debtor are few and far between." The dearth of cases subordinating the claims of non-insiders is readily explained by the high threshold of misconduct that must be established by the objectant in non-insider cases. In *In re Osborne*, 42 B.R. 988, 996 (W.D.Wis.1984), the court discussed the conduct required for equitable subordination in non-insider cases:
>
> > [The degree of misconduct] has been variously described as "very substantial" misconduct involving "moral turpitude or some breach of duty or some misrepresentation whereby other creditors were deceived to their damage" or as gross misconduct amounting to fraud, overreaching or spoliation.

> Accord *In re Mayo*, 112 B.R. 607, 650 (Bankr.D.Vt.1990) ("There are few cases in which gross misconduct has actually been applied to non-insiders, and even fewer where inequitable misconduct has caused a claim to be subordinated."); *In re Dry Wall Supply, Inc.*, 111 B.R. 933, 938 (D.Colo.1990) (noting that "when [the fiduciary] relationship is absent, the party seeking equitable subordination of a claim must demonstrate even more egregious conduct by the creditor"). Although courts have struggled to articulate the misconduct that must be established to subordinate non-insider claims, it is clear that the non-insider's misconduct must be "gross or egregious." *See* Benjamin Weintraub & Alan N. Resnick, BANKRUPTCY LAW MANUAL ¶ 5.15 at 5-96 (3d ed. 1992); see also In re Osborne, 42 B.R. at 997 (stating that "plaintiffs are required to make a showing of gross or egregious misconduct"). Thus, "[a] mere statement that the creditor is guilty of 'inequitable conduct' will not suffice." *In re W.T. Grant*, 4 B.R. 53, 75-76 (Bankr.S.D.N.Y.1980), *aff'd*, 699 F.2d 599 (2d Cir.1983). Rather, the plaintiff must prove gross misconduct tantamount to "fraud, overreaching or spoliation." *Id.*; *see also In re Fabricators, Inc.*, 926 F.2d 1458, 1465 (5th Cir.1991) ("If a claimant is not an insider, then evidence of more egregious conduct such as fraud, spoliation or overreaching is necessary."); *In re Dry Wall Supply, Inc.*, 111 B.R. 933, 938 (D.Colo.1990) ("The degree of misconduct which the plaintiff must show in the case of a noninsider has been variously described as gross misconduct tantamount to fraud, misrepresentation, overreaching or spoliation."); *In re Teltronics*, 29 B.R. at 173 (holding that "it is incumbent upon the [objectant] to demonstrate that [the non-insider] engaged in very substantial misconduct tantamount to fraud, overreaching or spoliation, which caused other creditors of [the debtor] to suffer damages"); *In re Pinetree Partners, Ltd.*, 87 B.R. 481, 488 (Bankr.N.D.Ohio 1988) ("Where the claimant is a non-insider, egregious conduct must be proven with particularity. It is insufficient for the objectant in such cases merely to establish sharp dealings; rather, he must prove that the claimant is guilty of gross misconduct tantamount to fraud, overreaching or spoliation to the detriment of others."). In summary, the "gross or egregious misconduct" needed to subordinate claims of non-insiders is much greater than the "inequitable conduct" that warrants subordination of insiders and fiduciaries.

Credit Suisse's actions in the case were so far overreaching and self-serving that they shocked the conscience of the Court.

In Cushman & Wakefield's July 1, 2005, appraisal, the Debtors had purportedly sold 243 lots or units, and another 42 lots were listed under contract. The lot sales for 2000 through 2005 are summarized by closing date, lot number, price and type in Addendum B to the

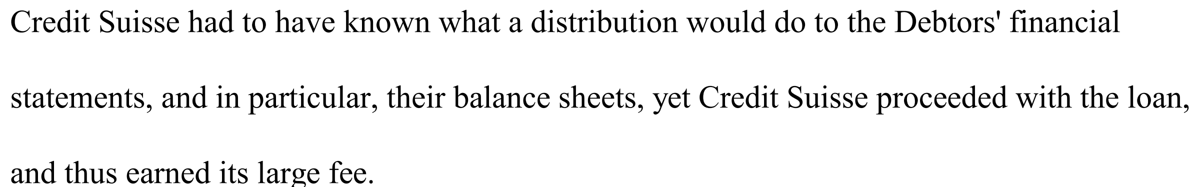
appraisal. Dean R. Paauw ("Paauw"), a certified Member of the Appraisal Institute ("MAI") who prepared Cushman & Wakefield's July 1, 2005, appraisal of the Yellowstone Club, states on page 65, in discussing an overview of the Yellowstone Club's current and recent real estate pricing, that there were five remaining lots in inventory in Pine Ridge, a subdivision at the Yellowstone Club. The five remaining Pine Ridge Lots were listed for sale at asking prices ranging from $1,950,000 to $4,000,000. Paauw went on to state that "[t]he developer typically achieves his asking price on his inventory, and [the Pine Ridge] lots are expected to be sold within the next 12 months." Paauw's July 1, 2005, appraisal also concludes that "[a]bsorption in Yellowstone Club has historically been hurt by limited availability in product."

In 2005, Credit Suisse was offering a new financial product for sale. It was offering the owners of luxury second-home developments the opportunity to take their profits up front by mortgaging their development projects to the hilt. Credit Suisse would loan the money on a non-recourse basis, earn a substantial fee, and sell off most of the credit to loan participants. The development owners would take most of the money out as a profit dividend, leaving their developments saddled with enormous debt. Credit Suisse and the development owners would benefit, while their developments – and especially the creditors of their developments – bore all the risk of loss. This newly developed syndicated loan product enriched Credit Suisse, its employees and more than one luxury development owner, but it left the developments too thinly capitalized to survive. Numerous entities that received Credit Suisse's syndicated loan product have failed financially, including Tamarack Resort, Promontory, Lake Las Vegas, Turtle Bay and Ginn. If the foregoing developments were anything like this case, they were doomed to failure once they received their loans from Credit Suisse.

Credit Suisse, Barcy, Yankauer and others on the Credit Suisse team only earned fees if they sold loans. Credit Suisse thus devised a loan scheme whereby it encouraged developers of high-end residential resorts, such as Blixseth, to take unnecessary loans. The higher the loan amount, the fatter the fee to Credit Suisse. This program essentially puts the fox in charge of the hen house and was clearly self-serving for Credit Suisse.

The fee structure was undoubtedly the catalyst that led to the most shocking aspect of Credit Suisse's newly developed loan product. As noted earlier, Credit Suisse's new loan product was marketed to developers on grounds that developers were authorized to take a substantial portion of their Credit Suisse loan proceeds as a distribution, or as Blixseth argues, a loan. In this case, Credit Suisse had not a single care how Blixseth used a majority of the loan proceeds, and in fact authorized Blixseth to take $209 million and use it for any purpose unrelated to the Yellowstone Club. Blixseth, however, had a problem in this case because he was not the sole owner of the Yellowstone Club and he did not want to share the loan proceeds with the B shareholders. Thus, Blixseth booked the $209 proceeds that he took from the Yellowstone Club as a loan months after he actually took the proceeds. Blixseth claims he always intended to repay the $209 million BGI note, but Blixseth's former wife Edra testified to the contrary.

Blixseth testified that he always intended to take the $209 loan proceeds as a loan rather than a distribution because booking the transaction as a distribution would have caused his owner's equity account to have a negative balance. The negative owner's equity would have appeared as a qualification on the Debtors' audited financial statements and may have caused the Debtors' to be out of compliance with the Credit Agreement. A sophisticated lender such as



Credit Suisse had to have known what a distribution would do to the Debtors' financial statements, and in particular, their balance sheets, yet Credit Suisse proceeded with the loan, and thus earned its large fee.

In addition to turning a blind eye to Debtors' financial statements, Credit Suisse's due diligence with respect to the $375 million loan was almost all but non-existent. Credit Suisse spent a fair amount of money on legal bills to ascertain that the Debtors did in fact own the property at the Yellowstone Club, and Credit Suisse also spent a fair amount ensuring that it was not violating any laws with its loan product. Credit Suisse, however, did little financial due diligence. Barcy testified that Credit Suisse was aware that Cushman & Wakefield had appraised Debtors' assets in 2004 and thus either knew or should have known that the collateral that Blixseth proposed for the Credit Suisse loan had a fair market value of $420 million in 2004. The Court highly doubts that Credit Suisse could have successfully syndicated the Yellowstone Club loan if the loan to value ratio was 90 percent. Thus, Credit Suisse instead commissioned Cushman & Wakefield to employ its newly devised valuation methodology. In applying the new valuation methodology, Credit Suisse relied almost exclusively on the Debtors' future financial projections, even though such projections bore no relation to the Debtors' historical or present reality.

Moreover, the Debtors' past debt had bounced between $4 to $5 million on the low end to $60 million on the high end. Credit Suisse proposed to increase the Debtors' debt load by at least six times. Barcy, Yankauer and the rest of the Credit Suisse syndicated loan team could not have believed under any set of circumstances that the Debtors could service such an increased debt load, particularly when the Debtors had several years of net operating losses,

mixed with a couple years of net operating revenues.

The only plausible explanation for Credit Suisse's actions is that it was simply driven by the fees it was extracting from the loans it was selling, and letting the chips fall where they may. Unfortunately for Credit Suisse, those chips fell in this Court with respect to the Yellowstone Club loan. The naked greed in this case combined with Credit Suisse's complete disregard for the Debtors or any other person or entity who was subordinated to Credit Suisse's first lien position, shocks the conscience of this Court. While Credit Suisse's new loan product resulted in enormous fees to Credit Suisse in 2005, it resulted in financial ruin for several residential resort communities. Credit Suisse lined its pockets on the backs of the unsecured creditors. The only equitable remedy to compensate for Credit Suisse's overreaching and predatory lending practices in this instance is to subordinate Credit Suisse's first lien position to that of CrossHarbor's superpriority debtor-in-possession financing and to subordinate such lien to that of the allowed claims of unsecured creditors.

The Debtors have provided for the membership claims in their proposed Chapter 11 plan. Accordingly, the Court declines to equitably subordinate Credit Suisse's secured claim to those of the members, including members of the Ad Hoc Committee of Yellowstone Club Members or the Ad Hoc Group of Class B Unit Holders.

For purposes of the upcoming auction of Debtors' assets scheduled for May 13, 2009, Credit Suisse shall be allowed to submit a credit bid for the amount of its allowed secured claim of $232 million. However, because Credit Suisse's claim is equitably subordinated, Credit Suisse must provide, as a component of its credit bid, sufficient funds to pay the CrossHarbor debtor-in-possession financing, the administrative fees and costs of the Debtors' bankruptcy

estate and the allowed unsecured claims of non-member creditors. For the reasons discussed herein,

IT IS ORDERED that a separate and final memorandum of decision and judgment will follow this partial and interim order, wherein judgment will be entered in favor of the Debtors and the Committee and against Credit Suisse; and pursuant to 11 U.S.C. § 510(c), Credit Suisse's allowed secured claim of $232 million is equitably subordinated to: (1) CrossHarbor's debtor-in-possession financing; (2) approved administrative fees and costs of the bankruptcy estate; and (3) the allowed claims of unsecured creditors. Credit Suisse's $232 million secured claim is not subordinated with respect to the claims of members resulting from their membership agreements and is not subordinated to any claims of the Class "B" minority shareholder members.

BY THE COURT

HON. RALPH B. KIRSCHER
U.S. Bankruptcy Judge
United States Bankruptcy Court
District of Montana