

# At Bat in Bankruptcy Court

An avid baseball fan  
— and veteran  
Delaware bankruptcy  
lawyer — shares  
insights on the battle  
over control of  
the LA Dodgers.

I have seen a full array of issues put before the Delaware Bankruptcy Judges. Companies of various shapes, sizes and notoriety including Marvel Entertainment,<sup>1</sup> Napster, Zenith, Smith Corona, Montgomery Ward, Washington Mutual, Tribune, TWA, Continental Airlines, Phoenix Steel, Tower Records and Solyndra have filed here. However, as a sports fan, and most particularly a devout follower of Major League Baseball and the Philadelphia Phillies, there has not been a case more fascinating than the LA Dodgers' bankruptcy filing during the 2011 baseball season.

Shortly after that filing, I was retained as Delaware counsel to the Commissioner of Baseball, Bud Selig. Our legal team was immediately preparing for a court hearing to object to proposed bankruptcy financing negotiated by the Dodgers' beleaguered owner, Frank McCourt. Soon I was welcoming top MLB executives at our offices prior to that hearing. During breaks at the hearing I listened as Mr. Selig's top lieutenants called him to discuss strategy.

That first hearing was a precursor of things to come. It was important for the Dodgers to immediately obtain "debtor-in-possession" financing. The team was low on liquidity and had various payroll obligations coming due at the time it filed, including amounts due to former players including Manny Ramirez.<sup>2</sup> At the hearing the team did obtain interim approval for \$60 million in financing from Highbridge, a Goldman Sachs affiliate.

MLB ended up not pressing its ob-

jection but fully reserved its rights regarding final approval. The proceeding was a warm-up for the final hearing on approval of \$150 million in total financing several weeks later. Before delving into that fight, some background on McCourt's deteriorating relationship with the League will be helpful.

The Dodgers were a proud franchise. As recently as the 2008 and 2009 seasons, the team experienced success, reaching the National League Championship Series both seasons (but losing to my beloved Phillies!). By most accounts the team's situation began to unravel when McCourt and his wife Jamie separated after the 2009 season and subsequently commenced divorce proceedings.

As the McCourts' marriage unraveled, so did the Dodgers' performance, as they failed to make the playoffs the following season. The divorce proceeding languished. The media frenzy in LA worsened over time. Stories came out about the McCourts' lavish lifestyle and an alleged affair involving Jamie that led to the divorce. But what really sensationalized the divorce was the revelation that Jamie was claiming she owned 50% of the team. More on that later, but the cumulative effect of all this was instability for the team.

As the on- and off-the-field distractions from the divorce continued into the offseason after 2010, the team's finances worsened. What surfaced in press reports was a strategy by McCourt to address that issue. One potential source of liquidity was leveraging an increasingly valuable asset of professional sports franchises – so-called “media rights.” The Dodgers had negotiations with Fox Sports Net West2, LLC (“Fox”), the regional television network broadcasting most of its games. The Dodgers would agree to an amendment of their existing agreement whereby Fox would advance \$25 million in fees payable for the 2011 season.

MLB had concerns with this transaction (besides that it had not been submitted for its approval). The advance represented a large share of the Dodgers' telecast rights fees for the 2011 season (greater than 70%), thereby reduc-

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ing revenues available for 2011. Disputes with the League regarding the team's media rights would continue.

MLB also asserted that during that offseason McCourt caused the Dodgers to pay rent four months in advance to an entity of his which owned the stadium parking lots in order to fund McCourt's marital support obligations. MLB believed that McCourt personally had relatively modest personal assets outside of his Dodgers ownership in relation to his personal expenses and marital obligations.<sup>3</sup> Purportedly his “only” source of income was \$5 million per year obtained through lease payments made by the Dodgers.

There was not much optimism among the Dodgers faithful as the 2011 season got underway, and matters only worsened. On Opening Day at Dodgers Stadium, Giants fan Brian Stow was brutally attacked by Dodgers fans in the stadium parking lot. Very negative publicity followed this incident. The team was accused of having lax security and poor lighting in their parking lots.<sup>4</sup> Criticism of McCourt as communicated in the media reached a new low.<sup>5</sup>

Relations with the League were reaching a tipping point at this time. MLB had already commenced an investigation of the Dodgers' management. In early 2011, MLB had raised

specific issues with McCourt relating to his 2004 acquisition of the team, undisclosed transactions that followed involving team assets, and deficiencies in team operations. The League had an overriding concern that McCourt apparently did not have any independent source of wealth or income other than the Dodgers and the team's related real estate assets.

MLB believed that during his tenure as owner, McCourt had “siphoned off” more than \$180 million in direct and indirect cash distributions from team revenues.<sup>6</sup> The League was concerned about the cumulative effect of that. Other major areas of concern included the Club's ability to fund planned capital expenditures, including \$360 million in planned renovations of Dodger Stadium.<sup>7</sup>

In April 2011, the first month of the new season, MLB concluded its initial investigation and announced the appointment of a monitor, Ambassador J. Thomas Schieffer. The League viewed the Club's situation as serious. Fan and media scrutiny of team ownership was at its peak, while the team's on-the-field performance and attendance were in further decline.

Notwithstanding the Monitor's presence at team headquarters, he was excluded from critical decisions. First, a deal was announced in which a McCourt entity would receive a substantial \$385-million advance in exchange for Fox's broadcasting rights being extended for 17 years. The Commissioner's Office reviewed this new deal, and on June 20, denied approval.<sup>8</sup>

Additionally, while negotiations with Fox took place and as the Dodgers were waiting for MLB's decision, unbeknownst to the Monitor the team was making preparations for a momentous back-up plan – a chapter 11 filing – and McCourt was negotiating bankruptcy financing.<sup>9</sup> The team did file in Delaware one week after the League denied approval, becoming the second team in a year to file for chapter 11 (the Texas Rangers being the other).

With this backdrop, it would be an understatement to say relations were strained between McCourt and the

League as the battle over final approval of bankruptcy financing ensued. McCourt had a choice of two lenders. MLB was willing to provide financing as an alternative to Highbridge, McCourt's preferred lender. MLB's terms were clearly more favorable.<sup>10</sup> The League argued the Dodgers would not be properly exercising business judgment by refusing to accept their better offer. The Dodgers argued the League was seeking control. Expedited discovery followed.

A one-day trial was held before Chief Judge Kevin Gross. While generally approval of debtor financing is subject to a business judgment standard, MLB argued that the Dodgers were not entitled to that protection. Since McCourt was personally subject to a \$5-million fee – not previously disclosed to the Court – payable to Highbridge if that financing was not approved, his personal interests rather than the debtor's best interests were driving the decision. MLB pointed out that the Dodgers were seeking approval of financing on clearly less favorable terms and were refusing to negotiate with the League. MLB also argued that McCourt could not use bankruptcy to avoid the MLB Constitution and various other contractual obligations entered into when buying the team in 2004. The Dodgers disagreed.<sup>11</sup>

At the conclusion of the trial, Judge Gross announced he was taking the matter under advisement and would issue a prompt decision, which he did.<sup>12</sup> The Court's Opinion was short and direct. Judge Gross began his decision in gracious fashion by noting the Dodgers' "rich and successful history is of mythical proportions."<sup>13</sup> In acknowledging the "underlying feud" between the Commissioner and McCourt, the Judge added: "It is clear that Baseball needs and wants the Dodgers to succeed and the Debtors are best served by maintaining Baseball's good will and contributing to the important and profitable franchise group under the Commissioner's leadership."<sup>14</sup>

The Judge then cut to the chase and compared the terms of the Debtors' financing with MLB's proposed terms, finding the "substantial economic superiority" of the latter. The Court found:

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"Debtors not only failed to attempt to obtain unsecured financing [as required by statute], they refused to engage Baseball in negotiations because, they explained, Baseball has been hostile to Debtors."<sup>15</sup>

The Judge could have stopped there, but went on to address the Dodgers' view that courts typically apply a business judgment standard to a debtor's selection of its lender. The Court agreed that deference is given to the business decisions of directors of Delaware corporations, but then pointed to the exceptions to that rule, including when directors are not disinterested. Since McCourt had a personal stake in seeing that the Highbridge loan was approved the Dodgers' decision was not protected by the business judgment rule. Therefore, the Court applied the entire fairness standard, which it found was not met. In concluding his opinion, Judge Gross directed the team to negotiate with MLB in good faith.<sup>16</sup>

This had been an epic battle and the Commissioner's Office was pleased with the result. However, disagreements between McCourt and MLB were not limited to financing. McCourt had purchased the team in 2004 from Fox Entertainment Group, a subsidiary of News Corp., for approximately \$421 million. From all accounts, the MLB

approval process for the sale was not contentious.

McCourt, however, funded the purchase by incurring a significant amount of debt, much of it borne by the team itself. MLB anticipated this debt load would be reduced over time, which did not happen. Additionally, after the sale, assets were transferred away from the team to affiliates of McCourt. One example was the Dodgers' parking lots being transferred to a McCourt entity and then leased back.<sup>17</sup> Another example was the rights to sales of Dodgers tickets being transferred to a McCourt entity named Dodgers Tickets LLC. MLB contended that these transactions had not been disclosed to the league at the time and required its approval.

These issues were percolating in the years following McCourt's acquisition of the team, but as described above his relationship with the League started unraveling during his divorce from his wife Jamie.<sup>18</sup> Things got even more interesting when it was learned Jamie claimed a 50% ownership interest in the Dodgers. When the team was purchased in 2004 the McCourts entered into a post nuptial agreement which, unlike other marital assets to be divided 50/50 (at least clearly in McCourt's view), provided that Frank McCourt owned 100% of the team.

During the divorce proceeding, however, it came to light that there was a second version of the post nuptial agreement with slightly different wording which suggested that Jamie owned half the team.<sup>19</sup> The dispute was approaching a trial in 2011, soon after the bankruptcy filing, when it was announced that the couple had reached a settlement. Frank agreed to pay Jamie \$130 million by April 30, 2012 in exchange for her release of any interest in the team. That agreement created a substantial financial commitment for Frank, however, which caused MLB even greater concern that McCourt's governance of the Dodgers was driven by his personal financial situation.

Given the relationship between MLB and McCourt, questions about the Dodgers' financial stability, and the sustained negative media coverage, the

Commissioner's position was clear: McCourt must sell the Dodgers. Accordingly, the skirmish over financing was just the beginning. Everyone knew this, including Judge Gross.

The public war between MLB and McCourt would worsen before peace broke out. As anticipated, the Dodgers filed a motion for approval of "procedures" for the marketing of their media rights. The team wanted the Court to approve essentially modifying the contract between Fox and the Dodgers by moving up by a year the 45-day period in which the team was required to exclusively negotiate with Fox over an extension of their agreement. Fox did not consent to this.

MLB filed a motion to terminate the Dodgers' exclusive period to file a chapter 11 plan or alternatively compel the Club to assume all MLB-related agreements (which in the view of MLB, could not be done because the previous breaches thereof by McCourt could not be cured).

Judge Gross scheduled the matters

for a mid-October trial and in an Order set forth the specific issues to be tried.

There had been a new development in the case during that summer which at first was not public knowledge. Former Delaware District Court Chief Judge Joseph Farnan was asked by Judge Gross to serve as a mediator of disputes between MLB and the Dodgers.<sup>20</sup> Judge Farnan's involvement as a mediator "behind the scenes" would pay off.<sup>21</sup>

On November 1, 2011 MLB announced it had reached a global settlement with the Dodgers. Most critically, McCourt agreed to sell the Dodgers in an auction process. But there was a time constraint: under his settlement with his ex-wife, McCourt had to make a \$130-million payment by April 30, 2012. He would need a sale of the team to be approved by MLB and the Court and then close by that time. More on the sale later; the Dodgers still had issues with Fox.

The Dodgers' skirmishes with Fox began with the MLB settlement. Since bankruptcy requires court approval of

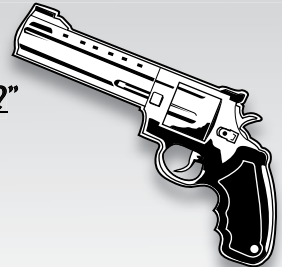
settlements, the Dodgers filed a motion which Fox challenged. The settlement terms described in the motion referenced the Dodgers' media rights as potentially part of a sale. Fox objected because, among other reasons, there were separate confidential terms between MLB and the Dodgers which by agreement were not part of the record and not to be disclosed to other parties including Fox. Judge Gross approved the MLB settlement, overruling the objection. The larger battle between the team and Fox would be over the Dodgers' proposed media rights procedures.

The Dodgers filed a motion for approval of amended procedures for marketing their media rights which included a modification of Fox's exclusive negotiating rights. Due to the accelerated sale process, driven by McCourt's obligations due on April 30, this proceeding had to be expedited. Interestingly, MLB had agreed in its settlement to be neutral, although it would still get caught in the fray with discovery.<sup>22</sup> As Fox and the Dodgers prepared for trial, Judge



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Farnan continued to attempt to broker another deal.

A two-day trial was held in December, 2011. Fox had two expert witnesses.<sup>23</sup> After closing argument, the Judge announced that he was going to issue a written decision but then explained he was going to rule in the Dodgers' favor. The litigation quickly shifted to the District Court after Fox filed an expedited appeal. Remember that the Dodgers and Blackstone, their investment bankers, were working feverishly on the sale of the team, aiming to complete the process in a matter of weeks.

Soon the complexion of this litigation would change. District Court Judge Leonard Stark granted Fox's motion for a stay pending appeal and established an accelerated briefing schedule. The Judge, who was relatively new to the bench, demonstrated he was more than capable of keeping up with the bankruptcy lawyers' fast-paced ways by issuing an oral decision and then keeping his promise to issue a written opinion a few days later. The Dodgers were going to be perilously near the end of their marketing process while the appeal was pending. It was not surprising when days before appellate argument the Dodgers announced a settlement with Fox.

Heading into the late innings of its bankruptcy, the Dodgers still had to select a high bidder for the team, obtain MLB approval and consummate a sale through a chapter 11 plan. Under the settlement with the League, a sale could include assets not owned by the Dodgers (including the parking lots), but did not have to. In addition, the settlement with Fox meant that bidders could discuss media rights (but the bankruptcy could not be used to reject the existing telecast agreement).

Interested bidders mentioned in the media included Steve Cohen of SAC, former Dodgers and Yankees manager Joe Torre, former Dodgers owner Peter O'Malley, former Dodgers players Orel Hershiser and Steve Garvey, Dallas Mavericks owner Mark Cuban and investor Ron Burkle.

Eventually, in March 2012, the earth-shattering winning bid was announced.

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A group led by former NBA great Magic Johnson (an LA fan favorite), seasoned MLB executive Stan Kasten and hedge fund Guggenheim Partners would buy the team for an astonishing \$2.15 billion. The purchase price was record setting for a U.S. professional sports franchise.<sup>24</sup> The price was a reflection of how valuable media rights had become in professional sports (the new owners did not negotiate a new media rights deal in connection with their acquisition, but the contract with Fox expires after the 2013 season).<sup>25</sup>

Now that the team had a buyer, court approval through confirmation of a chapter 11 plan was necessary.<sup>26</sup> Confirmation is a two-step process. First, a disclosure statement must be approved. A disclosure statement provides information necessary for a creditor or equity holder entitled to vote on a chapter 11 plan to decide to accept or reject it. Here, the proceeds from the sale of the team would be so large that all creditors would be paid in full and equity in the debtor "LA Holdco LLC" – Frank McCourt – would receive a substantial distribution.<sup>27</sup> As such, the only party needing to vote on the Plan was McCourt himself.

Under this scenario this process would seemingly proceed smoothly, but nothing was easy in this bankruptcy. For instance, the creditor who had potentially a very large claim – Brian Stow, the Giants fan severely injured on Opening Day – raised issues with the Plan.

His personal injury claim would have to be liquidated outside of the Bankruptcy Court in the California state court litigation commenced before the bankruptcy, which was stayed by the filing.<sup>28</sup> Nevertheless, the Dodgers attempted procedurally in the bankruptcy to disallow a proof of claim filed on behalf of Stow and his children. Stow, who retained a highly regarded firm specializing in bankruptcy, opposed this procedural move, and also argued that the Plan improperly granted releases of third parties and questioned the adequacy of reserves for creditor claims. Matters with Stow in the bankruptcy did get resolved, and the confirmation hearing was scheduled on April 13, 2012. Again, timing was important – McCourt's deadline for payment of \$130 million to his ex-wife was April 30. The team's objective was to remain on schedule for confirmation.<sup>29</sup>

On the eve of the confirmation hearing, there was still much to accomplish. One very significant hurdle was obtaining League approval of all aspects of the purchase of the team. Since MLB had open issues as of the deadline for opposing the plan, it filed an objection. On the morning of the hearing, MLB's legal team headed over to Young Conaway's Delaware office for discussions with the Dodgers and Guggenheim and the mediator, Judge Farnan.

Judge Gross moved the hearing to 4 p.m. (on a Friday, which happened to be the 13th). Surely that would give the parties enough time to resolve open issues? Not quite. By the time the hearing began at 6 p.m., there was not a festive atmosphere. MLB expressed various concerns to the Judge over details of the sale.

Judge Gross, however, eventually decided to confirm the plan that evening, paving the way for the \$2+ billion sale to close. The League got its wish through McCourt's sale of the team, the transaction closed by April 30 and the McCourts each received their millions.<sup>30</sup> ♦

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*The end notes accompanying this article are posted on the Delaware Bar Foundation's website, [www.delawarebarfoundation.org](http://www.delawarebarfoundation.org).*

# At Bat In Bankruptcy Court

Jeffrey M. Schlerf

## FOOTNOTES

1. A book was written about the Marvel Entertainment case. D. Raviv, *Comic Wars*, 2002 (Broadway Books).
2. The top unsecured creditors listed on the chapter 11 petition included various notable MLB players: Manny Ramirez (\$21 million), Andruw Jones (\$11.1 million), Hiroki Kuroda (\$4.5 million), Rafael Furcal (\$3.7 million) and Ted Lilly (\$3.4 million), plus the Chicago White Sox and famed broadcaster Vince Sculley.
3. Motion of Major League Baseball to Terminate Exclusivity or, in the Alternative, to Compel the Debtors to Seek Assumption or Rejection of the Baseball Agreements, at para. 32.
4. On May 24, 2011, Mr. Stow commenced litigation in California state court against the Dodgers and affiliates and certain unnamed “Doe” defendants, asserting claims for negligence and seeking compensatory and punitive damages.
5. Michael Martinez & Stan Wilson, *What Has Happened to the Dodgers?*, CNN.COM (June 10, 2011), [http://www.cnn.com/2011/US/06/09/dodgers\\_fan.exodus/index.html](http://www.cnn.com/2011/US/06/09/dodgers_fan.exodus/index.html); Editorial, *True to the Dodgers: The storied franchise of Rickey and O’Malley must be owned by someone other than Frank McCourt*, L.A. Times (Jul. 2, 2011), <http://latimes.com/news/opinion/opinionla/la-ed-dodgers-20110702,0,1265931.story>; Larry Behrendt, *Frank McCourt Must Go*, IT’S ABOUT THE MONEY.NET (June 21, 2011), <http://itsaboutthemoney.net/archives/2011/06/21/commissioner-selig-frank-mccourt-must-go-a-petition>.
6. Motion of Major League Baseball to Terminate Exclusivity, *supra* note 3, at para. 30.
7. *Id.* at para 32.
8. Denial was for various reasons, including that McCourt did not shop for better offers for the team’s media rights, the advance payment would sacrifice the Dodgers’ future, the deal would separate a valuable asset from the team and nearly half of the advance would be used for McCourt’s marital obligations, and the deal was only a short-term fix and would prevent the Dodgers would re-valuing the asset for 17 years.
9. Motion of Major League Baseball to Terminate Exclusivity, *supra* note 3, at para. 37.
10. Among other things, MLB would lend on an unsecured basis (i.e., without taking any collateral).
11. Other parties to this proceeding included the unsecured creditors’ committee (consisting of Brian Stow; the Major League Baseball Players Association; KABC Radio; plus two trade creditors), the Office of the United States Trustee and Jamie McCourt.
12. In what can only be described as a “Delaware moment”, on the Friday afternoon when the opinion was issued, Bob Brady, Delaware counsel to the Dodgers and I crossed paths at –

of all places – the local Phillies summer baseball camp. We speculated when the Judge’s opinion would be released. The decision hit the docket while I was driving back to the office.

13. The Judge noted the team was “[f]ormerly the Brooklyn Dodgers, the team name is derived from the fans who used to “dodge” that city’s trolleys.” Memorandum Order, at 1 n. 1 (July 22, 2011).
14. *Id.* at 4.
15. *Id.* at 5.
16. *Id.* at 7. The Court also advised that he expected the League to propose a “short form credit agreement” which was “uncoupled” from MLB’s oversight and governance of the Dodgers. Soon thereafter the Dodgers and MLB agreed to such a contract.
17. McCourt had been a commercial developer in New England at the time he purchased the Dodgers in 2004. There was some media speculation at that time that McCourt’s motivation for buying the team included a desire to develop what was perceived as valuable land surrounding the stadium at Chavez Ravine in Los Angeles. The subject of McCourt’s intentions regarding these non-debtor assets would surface again during the bankruptcy when the team was finally put up for sale.
18. One obvious complication arose from the fact that after the team was purchased, Jamie played a significant role in the operations of the team.
19. What is alleged to have happened is the firm drafting the agreement had created six originals, three of which were what Frank had intended (100% ownership) and three of which reflected that the marital property included the Dodgers.
20. Judge Farnan served as a United States District Court Judge for 25 years, until 2010, in the District of Delaware. He was Chief Judge from 1997 to 2001, during a time when due to the workload of Delaware Bankruptcy Judges (there were only two), the Delaware District Court Judges presided over bankruptcy cases. After his retirement from the bench in 2010, Judge Farnan started his own law firm and, in addition to practicing in the area of patent litigation (in which he had vast experience as a trial judge), he has served as an arbitrator and mediator.
21. There were rumors that reaching a settlement required at least one visit to Wilmington by the Commissioner and McCourt.
22. In an interesting twist, previously Fox had not filed a formal objection to the Debtors’ first media rights motion but rather a joinder to MLB’s objection. Additionally, Fox had not served discovery earlier. The Dodgers took the position that Fox was not entitled to take any discovery in connection with the upcoming trial on the team’s amended motion for approval of marketing procedures. Fox disagreed, serving discovery on, among others, MLB. On December, 22, 2011, Judge Gross ruled that Fox was entitled to discovery from

the Debtors related to its motion to dismiss the Debtors’ chapter 11 cases.

23. Fox hired a new law firm shortly before trial, which resulted in its Delaware counsel taking a lead role at trial.
24. The Miami Dolphins football team sold for approximately \$1 billion in 2009.
25. On January 28, 2013 the Dodgers announced they had reached a 25 year deal with Time Warner involving the team launching its own network beginning in 2014. The deal was estimated to be worth between \$7 billion to \$8 billion. Bill Shaikin, *Dodgers, Time Warner Cable announce new channel: SportsNet LA*, LATimes.com (Jan. 28, 2013), <http://www.latimes.com/sports/dodgersnow/la-sp-dn-dodgers-time-warner-cable-sportsnet-la-20130128,0,1454054.story>
26. In a chapter 11 case, the sale of a debtor’s assets outside of the ordinary course of business can occur pursuant to Section 363 of the Bankruptcy Code or under a chapter 11 plan. 11 U.S.C. § 363(b)(1). 11 U.S.C. § 1123(a)(5) (D) allows for a chapter 11 plan to include the “sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate. . . .” In contrast to the Dodgers’ sale, the sale of the Texas Rangers in their bankruptcy was originally attempted through a § 363 sale. Ultimately, however, due to numerous objections raised by creditors, it was accomplished pursuant to a confirmed plan.
27. It was estimated that McCourt would receive almost \$1 billion from the sale, even after payment of taxes, legal fees and other obligations, including \$131 million paid towards his settlement with his ex-wife.
28. The Bankruptcy Code precludes the Bankruptcy Court from conducting a trial on a personal injury claim without the claimant’s consent.
29. The Dodgers had very experienced bankruptcy professionals representing them during the case: Dewey LaBoeuf as lead counsel, Young Conaway Stargatt & Taylor as Delaware counsel and The Blackstone Group as investment bankers. These professionals were worthy adversaries. In addition to the challenge of getting the sale under the plan consummated by April 30, the lawyers at Dewey LaBoeuf faced daily stories in the financial press about partner attrition at their firm and its financial instability. There was increasing speculation that the firm itself would soon file for chapter 11. Dewey LaBoeuf eventually did file for bankruptcy.
30. The bankruptcy may have come to an end after the plan was confirmed, but the McCourts’ divorce proceeding continued to make the headlines. In September, 2012, Jamie McCourt filed a motion to set aside the couple’s divorce settlement, claiming that Frank McCourt fraudulently misrepresented the value of the Dodgers’ franchise.