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Former Special Litigation Counsel to
SONICblue, Inc., *et al.*,
Debtors and Debtors in Possession

UNITED STATES BANKRUPTCY COURT FOR

THE NORTHERN DISTRICT OF CALIFORNIA

SAN JOSE DIVISION

In re

SONICblue Inc., *et al.*,

Debtors and Debtors in Possession.

Case No. 03-51775 MSJ

Chapter 11
(Jointly Administered)

OPENING BRIEF IN SUPPORT OF O'MELVENY & MYERS LLP'S FIFTH AND FINAL FEE APPLICATION

Date: October 13, 2009
Time: 10:00 a.m.
Place: Courtroom 3070
Judge: Hon. Marilyn Morgan

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I. INTRODUCTION

In July 2003, SONICblue, Inc. ("SONICblue" or the "Debtor") and its affiliated debtors-in-possession (collectively, the "Debtors") retained O'Melveny & Myers LLP ("O'Melveny") as special litigation counsel under Bankruptcy Code §327(e).[1] On November 4, 2008, O'Melveny filed its Fifth and Final Fee Application (the "Fee Application"). The Post-Confirmation Creditors' Committee (the "PCC") and SB Claims Holder, LLC[2] ("SB Claims", and collectively with the PCC, the "Objectors") filed objections to O'Melveny's Fee Application.

At a hearing held on May 5, 2009, the Court overruled objections related to the adequacy of O'Melveny's disclosures under Federal Rule of Bankruptcy Procedure ("FRBP") 2014, but ordered an evidentiary hearing on certain issues relating to the "senior debt" provisions of the settlement reached between the Estates, Intel Corporation ("Intel") and VIA Technologies, Inc. ("VIA") on which O'Melveny worked in 2004 and 2005. In particular, the Court identified three areas that it wanted to probe:

1. What steps O'Melveny, acting through Suzzanne Uhland, undertook to independently investigate the assertion that VIA's claim against the Debtors should not properly be treated as senior debt pursuant to the Indenture Dated As Of April 22, 2002 for the 7-3/4% Senior Subordinated Convertible Debentures Due 2005 (the "Indenture") governing the 7-3/4% Senior Subordinated Convertible Debentures Due 2005 (the "2002 Notes").
2. Why the parties did not try to negotiate a lower dollar claim with VIA in return for

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[1] 11 U.S.C. §327(e).

[2] A Claim Transfer Agreement was entered into on or around April 24, 2007 among VIA, S3 Graphics Co., Ltd. and SonicBlue Claims, LLC. [Docket Number 2274] Plaintiff's Exh. 166, attached to the Johnson Decl. as Exh. A. The VIA claims subsequently were transferred to the following entities, all of which O'Melveny understands were owned, directly or indirectly, in whole or in part, by Mr. McGrane and/or members of his family: Ferry Claims, LLC, [Docket Number 3385] Plaintiff's Exh. 167, attached to the Johnson Decl. as Exh. B; Freefall Claims I, LLC, [Docket Number 3388] Plaintiff's Exh.168, attached to the Johnson Decl. as Exh. C; Freefall Manager, LLC, [Docket Number 3698] Plaintiff's Exh. 169, attached to the Johnson Decl. as Exh. D; and SB Claims Holder, LLC, [Docket Number 3717] Plaintiff's Exh. 170, attached to the Johnson Decl. as Exh. E. O'Melveny understands that SB Claims Holder, LLC is the entity that currently holds the VIA claims and purports to act on its behalf. For ease of reference, these entities are referred to collectively herein as "SB Claims."

VIA's claim being treated as "senior debt" under the Indenture for the 2002 Notes, since lowering the amount of VIA's claim would have benefited other unsecured creditors at the expense of the holders of the 2002 Notes (the "2002 Noteholders").

3. What role O'Melveny played in preparing the FRBP 9019 motion filed with the Court to approve the settlement with VIA and Intel, in particular with respect to the fact that the motion did not flag the senior debt issue.

The evidence will show that there is no basis for criticizing Ms. Uhland or O'Melveny for having failed to investigate or challenge a conclusion regarding senior debt treatment that was no longer questioned by any party with knowledge or an economic interest. With respect to the 9019 Motion, O'Melveny had no real opportunity or any reason to attempt to insert a discussion of what was perceived not to be an issue.

II. OVERVIEW

The record, to be augmented by evidence at the hearing, will demonstrate that the following key facts are not in dispute.

- O'Melveny was retained as special litigation counsel under Bankruptcy Code §327(e) to help defend the Debtors in their opposition to Intel's motion to lift the stay, because the Debtors' general bankruptcy counsel, Pillsbury Winthrop Shaw Pittman LLP ("Pillsbury"), was prevented by a conflict from being adverse to Intel. Since Pillsbury had no such conflict with VIA and, indeed, had a long history of representing the Debtors in matters involving VIA, except to the extent that the Intel License was implicated. Pillsbury continued to take the lead role in connection with the Debtors' disputes with VIA. The relationship between the Intel and VIA disputes necessitated O'Melveny coordinating with Pillsbury and the other parties to the extent that the Intel dispute affected the resolution of the VIA claim, and issues involving VIA potentially implicated or affected the Debtors' dispute with Intel. Nevertheless, during the entire time that O'Melveny represented the Debtors, Pillsbury, rather than O'Melveny, served as the Debtors' lead counsel for matters involving VIA.

- Because O'Melveny's mandate was to focus on Intel and Intel-related issues, the bulk of time spent by O'Melveny lawyers involved Intel. This work included protracted and difficult litigation, discovery and negotiations with Intel, which is well-known for being a ferocious litigant that jealously safeguards the confidentiality of its technical information and licensing arrangements.
- It was important to the Debtors to resolve the Intel dispute in a manner that would eliminate, or at least reduce to the minimum extent possible, any resulting claim that VIA could assert under the Amended and Restated Investment Agreement, dated August 28, 2000 ("Investment Agreement"), entered into between VIA and the Debtors. That investment agreement resulted in the formation of a joint venture entity known as S3 Graphics Co., Ltd.[3] ("S3 Graphics" or the "Joint Venture"). The Joint Venture entity was intended to make products that would be licensed under a 1998 patent cross-license, entered into between Intel and the Debtor. O'Melveny formulated innovative arguments that succeeded in preventing Intel from obtaining relief from the stay to allow it to terminate its cross-license—thereby preventing VIA from being able to assert massive claims against the Debtors under the Investment Agreement. Intel took the position that the Joint Venture structure constituted a "sham" transaction from the outset, designed to inappropriately expand the intended scope of the license. Despite the vehemence of Intel's views, O'Melveny explored possible creative licensing arrangements with Intel that might have avoided any VIA claim and fought to obtain discovery with respect to the 2003 "global" settlement between Intel and VIA which these two litigants attempted to withhold and which ultimately paved the way for a settlement with each of them that was highly beneficial for these estates (the "Estates").
- VIA was the first to settle, reaching an agreement in principle in early fall 2005. O'Melveny's primary role in this first stage of the settlement was: (a) to speak out

[3] At the time of the agreement, SONICblue was known as S3.

against a proposal by other parties to settle with VIA for a claim in a dollar amount ($27 million) that O'Melveny believed would be overly generous to VIA and (b) to strive to structure the VIA portion of the settlement to maximize the Debtors' prospects for reaching a resolution with Intel and without the Estates needing to pay significant sums to Intel, for without an agreement with Intel (or a total litigation victory, with its attendant costs), the VIA settlement would have been illusory.

- After the parties reached an agreement in principle with VIA in fall 2005, O'Melveny proceeded to achieve a successful resolution with Intel that, against all odds, resulted in the Estates obtaining, at no cost, the releases from Intel that were a condition to the VIA portion of the settlement without needing to pay Intel anything.
- O'Melveny achieved exceptional results for the Estates. Defeating Intel's argument that the cross-license agreements could not be assumed by S3 Graphics, the joint venture formed by SONICblue and VIA, required O'Melveny to develop legal and factual arguments that dealt with the Ninth Circuit's decisions in *In re Catapult Entertainment, Inc.*, 165 F.3d 747 (9th Cir. 1999), and *In re CFLC, Inc.*, 89 F.3d 673 (9th Cir. 1996). These obstacles were so daunting that Pillsbury had earlier advocated not resisting Intel's efforts to terminate the cross-license but to concentrate on litigating with VIA. O'Melveny faced an adversary— Intel—with virtually unlimited litigation resources and an overwhelming need to avoid a negative precedent in an area of the law crucial to its business. Indeed, as an intellectual property-intensive business, Intel carefully controls its license and cross-license arrangements, and does not tolerate any use of its intellectual property beyond its intent. Intel vigorously fought O'Melveny's efforts to obtain discovery into such matters as Intel's recent global and highly confidential settlement with VIA. Through sheer tenacity and creative lawyering, O'Melveny was able to achieve a remarkable result vis-à-vis Intel. No one has ever challenged this fact or that the novelty and difficulty of the questions involved and the skill required to achieve these results more than satisfy the test for fee awards formulated by the Ninth Circuit in *Kerr v. Screen Extras Guild*, 526 F.2d

67 (9th Cir. 1975), *cert. denied*, 425 U.S. 95 (1976). Even with respect to the VIA portion of the settlement, where O'Melveny's role was more limited, there is no question that reducing the VIA claim from over $100 million to $12.5 million was viewed at the time by the Debtors' business principals, the Official Committee of Unsecured Creditors (the "Committee") and all other major participants in these cases, as an exceptionally positive result for the Estates.

- In achieving these results, Ms. Uhland had frequent interaction with many of the major players in these cases, including: (i) Pillsbury, which represented the Debtors generally as well as with respect to the VIA litigation; (ii) Levene, Neale, Bender, Rankin & Brill LLP ("Levene Neale"), the Committee's general bankruptcy counsel; (iii) Kreig, Keller, Sloan Reilley & Roman ("KKSRR"), engaged by the Committee as its IP counsel; (iv) counsel for Intel, including lawyers at Gibson Dunn & Crutcher ("Gibson Dunn"); (v) counsel for VIA, including Pachulski, Stang, Ziehl, Young & Jones LLP ("Pachulski"), Heller Ehrman LLP ("Heller") and Wilson Sonsini Goodrich & Rosati ("Wilson Sonsini"); and (vi) Bruce Bennett and other lawyers at Hennigan, Bennett & Dorman LLP ("HBD") representing the three 2002 Noteholders, each of whom sat on the Committee.
- Despite the intimation by the Objectors that frequent communications between O'Melveny and Mr. Bennett are *ipso facto* proof of misconduct (as if to substitute a theory of "guilt by frequency of association" for evidence), O'Melveny's communications with Mr. Bennett arose naturally in the context of dealing with essential aspects of these cases. Moreover, (i) the team of O'Melveny lawyers had far more frequent contact with many other constituents to this dispute; (ii) Intel insisted that creditors on the Committee participate directly in negotiations with them and the Committee nominated Mr. Bennett for this role; (iii) Mr. Bennett's clients had been appointed to the Committee by the Office of the United States Trustee and held three of the seats on the Committee; and (iv) Mr. Bennett's clients held the most substantial unsecured claims in the case so that they necessarily had a significant voice in most

matters, including resolution of the Intel and VIA issues. Far from suggesting anything sinister, these communications were an inevitable part of the job O'Melveny had to perform in order to resolve a difficult and potentially costly dispute.

- During the time that O'Melveny represented the Debtors, O'Melveny had no knowledge of or involvement in: (a) the attempted use by the 2002 Noteholders of an opinion letter issued by Pillsbury related to those notes; (b) any of the issues related to the objections to unaccreted original issue discount ("OID") on the 2002 Notes initially filed by Pillsbury and later handled by Levene Neale; (c) the prepetition history of payments received by Pillsbury; or (d) the allocation of preference litigation and objections to the 2002 Noteholders between Pillsbury and Levene Neale.

While these facts are undisputed, the Court is obviously concerned that the settlement among VIA, Intel and the Estates that it approved on October 27, 2006 included a waiver of any prospect that VIA could assert that its claim was senior to the 2002 Notes. The Objectors have asserted that O'Melveny's undeniable successes on behalf of the Debtors are diminished in value by the suspicion that O'Melveny acted deficiently, unprofessionally or even fraudulently in carrying out its representation of the Debtors. These allegations are squarely contradicted by the facts. O'Melveny welcomes this opportunity to set the record straight.

Each of the issues highlighted by the Court at the May 5, 2009 is discussed in detail, and in context, in section III of this Opening Brief. The essential facts related to the three issues highlighted by the Court, detailed in Section III below, can be summarized as follows[4]:

- Ms. Uhland did not purport to conduct an extensive investigation of the Indenture or whether VIA's claims might constitute senior debt under the Indenture. This was appropriate and proper given a number of facts, including:
  - o Prior to O'Melveny having any familiarity with this issue, the Debtors' financial advisor, Houlihan Lokey Howard & Zukin ("Houlihan"), had flagged the issue for the Debtors and the Committee. The issue had been identified and analyzed before

[4] References to the record support for these facts are set forth in Section III below.

O'Melveny was engaged. Moreover, this issue was not within O'Melveny's scope of work.

- In 2003, representatives of the Debtors had advised Mr. Bennett that the key language in the Indenture related to a loan that had been proposed to be extended to the Debtors by VIA but which never closed and, therefore, any claims that VIA had under the Investment Agreement were not senior debt. No one from O'Melveny was involved in these discussions, which predated O'Melveny dealing, even peripherally, with matters involving VIA.
- Prior to a June 2004 settlement meeting with Intel and VIA, Ms. Uhland was given a copy of a 2003 Houlihan recovery analysis that indicated that the first $15 million of VIA's claims would be senior to the 2002 Notes. But this analysis was inconsistent with (i) VIA's proofs of claim, which Ms. Uhland reviewed prior to the June 2004 meeting; (ii) the Investment Agreement; (iii) much of the language in the Indenture, which used terminology that would not normally be applied to a claim like the liquidated damages provisions of the Investment Agreement; and (iv) Ms. Uhland's experience, which indicated that it would be highly abnormal for a claim such as VIA's asserted claim to be afforded seniority. At a meeting held on June 15, 2004, David Gershon of SONICblue informed Ms. Uhland that at one point VIA had proposed making a $15 million loan to SONICblue, but that this financing never closed. This was not news to SONICblue or to Pillsbury, which had negotiated this transaction. Nor was it news to Mr. Bennett, who was previously aware of this fact.
- At the time, Ms. Uhland did not have any reason to delve into this history in any greater detail. Rather, the parties concluded that she should battle with Intel in order to prevent the Joint Venture from losing the license, thereby eliminating the prospect that VIA might have a substantial claim against the Debtors that would result if the Joint Venture lost the Intel license.

- From O'Melveny's perspective, this issue next surfaced in September 2005 when the parties were close to reaching an agreement in principle with VIA, contingent on later bringing home a settlement with Intel. VIA started this process by offering to enter into a global settlement for an allowed $42.5 million claim. Negotiations over the next month—driven largely by facts developed by O'Melveny in the Intel litigation—resulted in a proposed settlement for an allowed claim for VIA of $12.5 million. This was viewed as a great victory by Pillsbury and the Committee, both of whom had earlier indicated that they would be willing to accept any claim for VIA equal to or less than $25 million.
- Shortly before the final term sheet was developed, Al Boro of Pillsbury learned from one of his colleagues at his firm of the Indenture and the senior debt issue. Mr. Boro's partners at Pillsbury, including Tom Loran, had been made aware of this issue earlier as were members of Levene Neale, as counsel for the Committee. After having raised the issue, Mr. Boro conducted an investigation of the issue, including reviewing correspondence with VIA from 2002 and the documents surrounding the proposed $15 million loan that was never made. Based on his investigation, he concluded that the Indenture, which his firm had negotiated, could not be interpreted to provide that any claim by VIA was senior to the 2002 Notes.
- It was also problematic as to whether any of the "VIA" claims were, in fact, claims held by VIA, as opposed to S3 Graphics. The Investment Agreement provided that any payments owed under it were to be paid to S3 Graphics, including any liquidated damage claims related to the Intel license and any "Books and Records" claims. But only VIA, not S3 Graphics, was mentioned in the Indenture as a potential holder of "senior debt."
- Ms. Uhland's role on the VIA portion of this matter was limited. She understandably wanted to ensure that the 2002 Noteholders and VIA had a meeting of the minds as to whether the $12.5 million VIA claim was senior to the

2002 Notes, for unless those parties agreed on this issue, there would be no deal, at least not in the near term and probably not without further litigation. In addition, once the amount of the VIA claim was arrived at—$12.5 million—the Estates were indifferent as to whether the VIA claim was senior to the 2002 Notes. Seniority, or lack thereof, was purely a matter between VIA and the 2002 Noteholders ***if*** they were in disagreement on this issue.

- Pillsbury, Heller Ehrman (VIA's counsel) and O'Melveny were all involved in turning drafts of the term sheet that the parties ultimately signed in September 2005. This term sheet provided that VIA would have an allowed $12.5 million general unsecured claim that would be neither senior nor junior to other claims. At one point, Henry Kevane of the Pachulski firm (VIA's primary bankruptcy counsel) asked Ms. Uhland to explain the "neither senior nor junior" language. She recounted that it had been inserted at the request of the 2002 Noteholders. She also explained her understanding of the proposed $15 million loan and how it was dealt with in the Indenture. But Ms. Uhland was clear that this language was the 2002 Noteholders' proposal, rather than the Debtors'. She expected that Mr. Kevane would check with his client on this issue and if there was any dispute he would raise it, since VIA had every incentive to do so if there was a serious issue. Mr. Kevane understood this, investigated the matter with his client and reported that VIA had no disagreement with this language.
- In sum, Ms. Uhland never purported to conduct a detailed investigation of the senior debt issue and had no reason to do so. Others who were more centrally involved in matters related to VIA (*e.g.*, Mr. Boro) have testified that they did so. And the parties who were most directly adverse on this issue and who had a direct economic interest in it—the 2002 Noteholders and VIA—were in total agreement. After SB Claims entered the picture, it argued strenuously that the VIA claim should be senior to the 2002 Notes. Without regard to who is right on this issue,

the parties with an economic interest in this issue during the time that O'Melveny was involved were in total agreement.

- The Court also questioned why the parties did not bargain for a lower VIA claim by offering to agree that VIA had seniority. No one suggested this at the time. The reasons why include:
  - Reducing VIA's claim to $12.5 million was viewed as a home run. Pillsbury, in particular, was extremely strong in advocating that this offer be accepted and accepted quickly. It resulted in substantial benefits for the Estates, including all unsecured creditors, by reducing VIA's claim to about 12% of what VIA had asserted and exactly one-half of a result that the Committee had indicated would be acceptable.
  - After VIA's counsel checked with its client and conducted diligence, VIA accepted the language that made clear that VIA's claim would not be senior debt under the Indenture. Throughout the negotiations, VIA never asserted that it might even have a colorable argument to the contrary.
  - ***If*** VIA had insisted that its claim be senior debt under the Indenture, undoubtedly a battle royale would have erupted with the 2002 Noteholders, for the benefits of VIA seniority would have come directly from the pockets of the 2002 Noteholders. But, in fact, VIA did not raise this issue and there was no reason or basis to engage in that battle.
- With respect to the Debtors' Motion to Approve the Settlement filed under FRBP 9019 on October 7, 2006 (after O'Melveny succeeded in bringing Intel into the fold at no cost to the Estates), O'Melveny's response is simple—the portions of this motion and memorandum of points and authorities that dealt with VIA and its claim were prepared by Pillsbury. O'Melveny was asked—on a rush basis and with very little notice—to comment only on the portions of these pleadings that dealt with Intel. O'Melveny did so.

- The language in the memorandum of points and authorities that dealt with the VIA claim was drafted by Pillsbury and included a statement that VIA would have a general unsecured claim and that this would likely result in a recovery of approximately $4 million. ***If*** one were focused on the senior debt issue, this would indicate that VIA's claim would not be senior.
- The parties with the greatest interest in this issue—VIA and the 2002 Noteholders—were well aware of the fact that the settlement waived any right of VIA to claim that it was entitled to seniority. Since the parties directly involved had agreed, this did not seem like a major issue. Of course, several months after the settlement was approved, SB Claims acquired certain of VIA's rights and sought to reopen the settlement even though SB Claims was aware that VIA had waived any right to assert seniority before SB Claims acquired VIA's position.
- Several months earlier, when the motion was filed, O'Melveny had no reason to think that it should intervene in an area that was not within O'Melveny's assignment and where O'Melveny had no reason to believe that controversy would later erupt since the parties with an economic interest had agreed. But in any event, the language in the motion and the memorandum of points and authorities addressing this issue was prepared by Pillsbury and Pillsbury did not ask for O'Melveny's assistance with respect to it.

Over the balance of this Opening Brief, O'Melveny reviews the factual record in greater detail. We welcome the opportunity to address the Court's concerns and appreciate the opportunity to set the record straight.

III. FACTS AND ARGUMENT

A. Background of Intel-VIA Dispute and Intel's Stay Motion

S3 Graphics was formed pursuant to an Amended and Restated Investment Agreement dated August 28, 2000 (the "Investment Agreement"), between SONICblue and VIA for the purpose of operating SONICblue's graphics chip business. Plaintiff's Exh. 176, attached to the

October 2, 2009 Declaration of Aaron M. Johnson ("Johnson Decl.") as Exh. F.[5] SONICblue was issued voting stock in the Joint Venture that provided it with control, but the economic benefits of the Joint Venture flowed almost exclusively to VIA. The graphics chip business relied upon patents owned by Intel that were licensed to SONICblue under a 1998 patent cross license agreement (the "Cross License Agreement") with Intel, which license could be used by SONICblue's subsidiaries, including S3 Graphics.[6] The Investment Agreement provided that if S3 Graphics were deprived of the benefit of the Cross License Agreement, then VIA and/or S3 Graphics may be entitled to liquidated damages from SONICblue—arguably up to $70 million.[7] VIA was not entitled to any damages, however, if the Cross License Agreement terminated or ceased to cover S3 Graphics's products due to an act or omission by S3 Graphics or VIA. Because of the structure of the transaction, which allocated most of the economic benefit to VIA, not SONICblue, Intel took the position that the entire structure was inconsistent with the spirit, if not the letter, of the Cross License Agreement. Prior to the Debtors' chapter 11 filing, Intel informed SONICblue that it considered the joint venture structure a "sham transaction."

On March 21, 2003, SONICblue and its related debtors filed for protection under chapter 11 of the Bankruptcy Code. [Docket Number 1] Plaintiff's Exh. 159, attached to Johnson Decl. as Exh. G. On June 6, 2003, Intel filed a motion seeking relief from the automatic stay (the "Stay Motion") to permit it to terminate the Cross License Agreement. Citing the Ninth Circuit's holdings in *In re CFLC, Inc.*, 89 F.3d 673 (9th Cir. 1996), and *Catapult Entertainment, Inc. v. Perlman* (*In re Catapult*), 165 F.3d 747 (9th Cir. 1999), both of which involved the denial of motions by a debtor in possession to assume or assume and assign a contract under §365(c) of the Bankruptcy Code, Intel asked this Court to make the logical leap that even absent a motion to

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[5] The instant hearing is on O'Melveny's Fifth and Final Fee Application, and thus O'Melveny is more properly referred to as the "moving party," rather than the "plaintiff." However, for the purposes of marking exhibits, and consistent with the Court's convention, O'Melveny's exhibits will be marked "Plaintiff's" exhibits.

[6] Pursuant to the Investment Agreement, VIA delivered 13 million shares of SONICblue common stock to SONICblue, SONICblue and VIA formed S3 Graphics, and SONICblue contributed the assets of its graphic chip business to S3 Graphics.

[7] *See* Plaintiff's Exh. 176 at §§ 5, 9.

assume or to assume and assign, it was entitled to ***terminate*** the Cross License Agreement by virtue of *ipso facto* clause.

Pillsbury had been the Debtors' primary outside counsel for many years. When the Debtors' financial prospects began to sink, the Debtors turned to Pillsbury to serve as their primary insolvency counsel. As the Debtors' general in-house counsel explained, Pillsbury was selected "given the complexity of the number of issues—in particular, the VIA issues" with which Pillsbury had long-standing familiarity. Gershon Dep. at 80:2-23, attached to Johnson Decl. as Exh. H. But Pillsbury also had a conflict of interest that prevented it from being adverse to Intel. Gershon Dep. at 83:14-19, attached to Johnson Decl. as Exh. H. Thus, the Debtors approached O'Melveny to serve as special litigation counsel under Bankruptcy Code §327(e). As the Debtors' general counsel explained, O'Melveny was to handle the "Intel and IP-related aspects of the VIA dispute." Gershon Dep. at 83:5-13, attached to Johnson Decl. as Exh. H. The Debtors filed their application to retain O'Melveny as special litigation counsel on or around July 14, 2003 and the Court approved this application on July 25, 2003. [Docket Numbers 335, 365] Plaintiff's Exhs. 160, 161, attached to Johnson Decl. as Exhs. I, J.

Before O'Melveny was engaged, Pillsbury had recommended that the Debtors stipulate to relief from the automatic stay in favor of Intel, based on Pillsbury's reading of the *Catapult* and *CFLC* decisions. Such a stipulation almost certainly would have triggered the liquidated damages provisions in the Investment Agreement and would have exposed the Debtors to a claim of $70 million from VIA. The Committee was not willing to agree to this approach. O'Melveny also disagreed with Pillsbury's legal analysis and believed factual issues existed as to whether Intel had pre-consented to an assignment of the Cross License Agreement

In addition, shortly after the Debtors filed their bankruptcy cases, Intel and VIA settled and dismissed worldwide patent infringement lawsuits against one another. This was documented in an undisclosed and carefully guarded settlement agreement (the "2003 Intel-VIA Settlement Agreement"). The 2003 Intel-VIA Settlement Agreement was not filed with any court and its terms are not publicly available. Consistent with Intel's view of the joint venture structure, Intel also had filed patent infringement suits against S3 Graphics, despite the fact that, since its

formation, S3 Graphics was licensed to use Intel's patents pursuant to the Cross License Agreement as a "subsidiary" of SONICblue.[8] As part of the 2003 Intel-VIA Settlement, Intel also dismissed its lawsuits against S3 Graphics, albeit without prejudice, although S3 Graphics was not a party to the 2003 Intel-VIA Settlement Agreement and although Intel and S3 Graphics apparently did not enter into a separate settlement agreement. Accordingly, O'Melveny believed that Intel may have consented to an assignment by the Estates, either in the 2003 Intel-VIA Settlement Agreement, as a result of certain provisions in the Cross License Agreement itself, or otherwise. If O'Melveny could prevail on these arguments, Intel could not terminate the cross-license and VIA's claims for liquidated damages would be eliminated.[9]

O'Melveny's efforts to oppose Intel's initial Stay Motion were successful. On July 30, 2003, this Court denied Intel's request for relief from the automatic stay, citing cases holding that a request for relief from the stay is a summary proceeding and not a forum for litigating underlying disputes. *See* Tr. of July 30, 2003 Hearing, Plaintiff's Exh. 138. The Court's ruling was without prejudice to Intel's right to renew its Stay Motion after November 30, 2003, and the Court strongly suggested that the parties participate in voluntary discovery prior to any such renewal.

B. The VIA Claim Objection

VIA and S3 Graphics had filed duplicate $105 million proofs of claim against SONICblue, for, among other things, liquidated damages under the Investment Agreement and claims arising out of the formation of S3 Graphics (the "VIA Claims"). Plaintiff's Exhs. 122,

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[8] In December 1998, debtor SONICblue—then known as S3 Inc.—and Intel entered into the Cross License Agreement, whereby SONICblue received a non-exclusive license to use certain of Intel's patents and Intel received a non-exclusive license to use certain of SONICblue's patents. (Intel filed a copy of the Cross License Agreement under seal and attached a redacted version of the Cross License Agreement to its Stay Motion.) Pursuant to section 3.6(a) of the Cross License Agreement, the rights of SONICblue and Intel thereunder extend to the parties' respective "Subsidiaries," defined to include any entity, such as S3 Graphics, in which at least a fifty percent (50%) ownership interest and control is maintained.

[9] VIA's claims were generally discussed as falling into two broad categories—the license claims, which were asserted to be about $70 million, and the so-called "books and records" claims that related to certain other aspects of the Investment Agreement and which were asserted to be about $30 million.

123, attached to Johnson Decl. as Exhs. K, L. In December 2004, Pillsbury filed an adversary proceeding on behalf of the Debtors and an objection to VIA's and S3 Graphics's claims (the "VIA Claim Objection"), thereby formalizing through litigation before the Bankruptcy Court an adversarial relationship between the Debtors and VIA that dated essentially to the signing of the Investment Agreement. [Docket Number 1090] Plaintiff's Exh. 165, attached to Johnson Decl. as Exh. M. Certain aspects of the VIA Claim Objection related to a variety of post-closing disputes between VIA and SONICblue, including matters related to accounting and delivery of certain assets (the "Books and Records Claims"). Pillsbury, on behalf of the Debtors, also brought claims against VIA and S3 Graphics for breach of fiduciary duty in an effort to defend against the possible liquidated damages claim brought by VIA.

Given its conflicts with Intel, Pillsbury's approach focused on possible defenses to VIA's claims, even if the Intel license were lost. O'Melveny had no role in this litigation with VIA other than to caution against taking positions that might enhance Intel's arguments to terminate the cross-license, and to the extent permitted by the protective orders, providing information that might assist Pillsbury in its efforts.

C. 2003-2004: Disputes over Access to Intel and VIA Materials

Access to the 2003 Intel-VIA Settlement Agreement (and related materials) was a critical part of O'Melveny's strategy with respect to Intel. At the Court's suggestion, O'Melveny worked with the Debtors to attempt to resolve the discovery disputes with Intel and VIA informally. VIA's initial production of documents, however, was extremely limited and disappointing.

Given the difficulty and attendant expense of the discovery and litigation processes, the Debtors endeavored to pursue settlement with the limited information available to them, while continuing to litigate the discovery issues with VIA and Intel. O'Melveny assisted the Debtors in creating and presenting a good-faith written settlement offer to Intel in January 2004. The initial settlement structure advanced by the Debtors contemplated a cash payment to Intel for a license that would remain in place through the conclusion of the liquidated damages period under the Investment Agreement, thereby undercutting any claim that VIA might assert based on a termination of this license. Although O'Melveny and Intel maintained informal communications

in the interim, Intel did not formally respond to this settlement offer until April 2004, when it refused the offer without making a counter. And on May 13, 2004, Intel renewed its Stay Motion. [Docket Number 788] Plaintiff's Exh. 162, attached to Johnson Decl. as Exh. N.[10] It then was clear that the Intel dispute would need to move to a litigation mode.

In May 2004, O'Melveny prepared and filed a motion to compel Intel and VIA to respond to the Debtors' first set of document requests—which had themselves been pending for nearly a year ("Motion to Compel"). [Docket Number 805] Plaintiff's Exh. 163, attached to Johnson Decl. as Exh. O.[11] In its opposition, VIA insisted that its documents were not relevant to the patent dispute with Intel. But when heavily redacted versions of the 2003 VIA-Intel Settlement Agreement finally were produced by Intel, O'Melveny's analysis of these materials revealed curious references to VIA and SONICblue's joint venture, S3 Graphics, which strongly suggested that production of the unredacted versions of the 2003 Intel-VIA Settlement Agreement and related documents could reveal evidence that was highly relevant to the consent arguments O'Melveny was pursuing.

D. The June 15, 2004 Three-Way Settlement Meeting

After filing the Motion to Compel, O'Melveny continued to attempt to advance settlement discussions among the Debtors, Intel and VIA (who hoped to resolve the matter without producing the documents sought by O'Melveny), including at an in-person, three-way meeting at Intel's Silicon Valley offices held in June 2004.[12]

Intel insisted that representatives of the creditors on the Committee attend so that they would not just be dealing with estate professionals and the Debtors. Ms. Uhland contacted

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[10] The motion and supporting papers were filed under seal pursuant to Court order and thus are not attached or otherwise filed in connection with the instant brief.

[11] This motion and supporting papers also were filed under seal and for the same reasons are not attached or otherwise filed in connection with the instant brief.

[12] The litigation with Intel involved extremely technical legal and factual issues that touched on complex areas of both intellectual property and bankruptcy law. Accordingly, because of that overlap, on many occasions the participation of both Ms. Uhland (an O'Melveny partner with extensive bankruptcy experience) and David Eberhart (an O'Melveny partner with extensive intellectual property litigation experience) was required at events such as settlement conferences as well as conferences with creditors and with the Debtors' former officers and employees.

Levene Neale, counsel to the Committee, and strongly urged that some representatives of the Committee attend. Levene Neale extended this invitation to all Committee members. Ultimately, only Mr. Bennett, on behalf of the three 2002 Noteholders who sat on the Committee, attended. Bennett Dep. at 140:13-142:5; 142:7-13, attached to Johnson Decl. as Exh. P. These three noteholders were the largest unsecured creditors in the chapter 11 cases, so their participation made sense to all concerned, including Intel and the Committee. In fact, not long after O'Melveny became involved in the case, Ms. Uhland consulted with the Committee's representatives, who, prior to this time, had regularly and consistently invited Mr. Bennett (or other lawyers from the HBD firm) to participate in meetings and calls to discuss the status of the case. The 2002 Noteholders, through Mr. Bennett, continued to fill this role until resolution of the Intel and VIA disputes.

In preparation for the meeting, Ms. Uhland attempted to gain an understanding of the issues with VIA, although she never intended nor purported to supplant the much more substantial knowledge of these issues held by Pillsbury and others.

Several months earlier, Ms. Uhland had received recovery analyses that had been prepared in 2003 by Houlihan, the Debtors' financial advisor, which showed that the first $15 million of any VIA claim would be senior to the 2002 Notes. Plaintiff's Exh. 4, attached to Johnson Decl. as Exh. Q. Such analyses had been shared with all the members of the Committee since the outset of the chapter 11 cases. Bennett Dep. at 340:21-341:10, attached to Johnson Decl. as Exh. P; Plaintiff's Exhs. 1, 2, 3, attached to Johnson Decl. as Exhs. R, S, T. In preparation for these meetings, Ms. Uhland also obtained copies of the proofs of claim filed by VIA. Curiously, the VIA proofs of claim did not assert that these claims would be senior, although such an assertion would have been standard if in fact VIA thought it was entitled to seniority. Ms. Uhland also reviewed the Investment Agreement. Yet the Investment Agreement contained no covenants or other reference to a ***requirement*** that some portion of the liquidated damages claim be treated in a particular manner under future financing documents and in fact stated that the liquidated damages were payable to S3 Graphics, not Via, and, further, the $15 million amount had no connection to any of the amounts referenced in the liquidated damages or other provisions of the Investment

Agreement. Ms. Uhland also obtained a copy of the Indenture for the 2002 Notes and found it curious that the Indenture did not refer to the Investment Agreement and used the word "indebtedness" rather than damages. Finally, Ms. Uhland thought that it was counterintuitive that lenders to a company (*i.e.*, the 2002 Noteholders) would agree to provide any benefit to a potential damage claim by a third party, because in her experience such benefits generally flowed to financing sources rather than liquidated damage provisions in a contract.

On the morning of June 15, 2004, O'Melveny hosted a pre-meeting at its offices in Menlo Park, California. Attending that pre-meeting were Ms. Uhland and Mr. Eberhart from O'Melveny; Mr. Loran from Pillsbury; Mr. Bennett from HBD; and Mr. Gershon, one of the SONICblue client representatives. During the pre-meeting, Ms. Uhland asked Mr. Gershon about the language in the Indenture and whether he knew about a $15 million VIA claim. Mr. Gershon explained that at one point SONICblue and VIA had contemplated a settlement of their dispute pursuant to which VIA would lend SONICblue $15 million, but that this contemplated loan had never materialized. The fact that the proposed loan amount was $15 million and that it was to be a loan (fitting with the terms "principal" and "indebtedness" used in the Indenture) led Ms. Uhland to conclude that the language in the Indenture was ***likely*** intended to apply to this contemplated loan as opposed to a liquidated damages claim under the Investment Agreement.

Although this was news to Ms. Uhland, it was not news to the others, including Mr. Bennett. For over one year at this point, Levene Neale, Mr. Bennett and other members of the Committee had been in possession of the Houlihan analyses that showed that a $15 million portion of VIA's claim would be senior. And at least six months earlier, Mr. Bennett had participated on a conference call, during which the Debtors discussed the $15 million VIA loan that never materialized. Bennett Dep. at 253:6-15; 253:23-254:4, attached to Johnson Decl. as Exh. P. Thus, neither Mr. Bennett nor Mr. Loran reacted at all to what was a revelation to Ms. Uhland—it was old hat for them.

During the in-person settlement meeting with Intel and VIA later that day, VIA indicated that it wanted a continued license from Intel as part of a resolution of the matter. Intel and VIA concluded that it would be fruitful for those two parties to have discussions outside the presence

of SONICblue and they did so for a few hours while the SONICblue representatives waited. At the conclusion of those discussions, Intel and VIA informed SONICblue that as the next step in the process, VIA was to provide information to Intel about its intended use of the license so Intel could evaluate this request for a license.

At this point, the settlement discussions were focused on the possibility that Intel would license the patents to VIA—presumably with SONICblue contributing cash to Intel as consideration for the license. If that came to fruition, VIA's liquidated damages claim against the Estates would likely be eliminated. Ms. Uhland did not consider what she had learned to be the definitive word on whether a VIA claim would be senior, but it did seem to her that the conclusions in the Houlihan analysis were dubious. This topic was not within O'Melveny's scope of work and was not even relevant to the path down which the parties were headed. So for a variety of reasons, Ms. Uhland had no reason to, and did not, investigate this point further.

E. Mid-2004 to Mid-2005: The Settlement Talks Deteriorate and O'Melveny Leads Extensive Discovery Battles

Soon after the June 15, 2004 settlement meeting, Intel and VIA advised the Debtors that further settlement discussions no longer would be fruitful. At that point, O'Melveny renewed its efforts to establish that Intel had consented to an assignment of the license by S3 Graphics or had granted a license to VIA that would cover the products of S3 Graphics, either of which would eliminate VIA's liquidated damages claim entirely. O'Melveny returned to the pending discovery war and fought to gain access to materials related to the 2003 Intel-VIA Settlement Agreement in hopes of finding further evidence supporting the Debtors' consent defense to Intel's renewed Stay Motion. VIA vigorously resisted that discovery. O'Melveny presented evidence to the Court of the likely relevance of the unredacted settlement documents. After submitting detailed reply papers on the Motion to Compel, O'Melveny again contacted Intel and VIA to seek a consensual resolution of at least the outstanding discovery issues. After significant negotiation, and only on the eve of the hearing on the Motion to Compel, the parties reached resolution, and at the hearing the parties presented to the Court a further agreed protective order (the "September 2004 Protective Order") pursuant to which Intel and VIA agreed to respond more completely to the

Debtors' document requests. Plaintiff's Exh. 134, attached to Johnson Decl. as Exh. U. The September 2004 Protective Order severely limited the total number of outside attorneys who could access or even discuss the purportedly confidential information.[13] This stipulation was put on the record and the parties agreed to a tentative discovery schedule.

Since settlement discussions had broken down, O'Melveny led the Debtors' efforts to pursue offensive and defensive strategies with respect to the Cross License Agreement and related matters. A key part of that strategy involved O'Melveny's preparation and filing on December 17, 2004 of a motion seeking to assume the Cross License Agreement pursuant to §365(a) of the Bankruptcy Code (the "Assumption Motion"). [Docket Number 1084] Plaintiff's Exh. 164, attached to Johnson Decl. as Exh. V. The Debtors, in consultation with the Committee, determined to pursue this strategy, for if the Debtors were able to assume the Cross License Agreement, VIA's $70 million contingent proof of claim for liquidated damages would be defeated.

In the Assumption Motion, O'Melveny argued that Bankruptcy Code §365(c)(1) as interpreted in *Catapult* did ***not*** prevent assumption by a debtor when the licensor had agreed, in the license itself, to assignment provisions that were not tied to the identity of the licensee. O'Melveny argued that Intel had, in effect, "pre-consented" to assignment by way of certain provisions of the Cross License Agreement. The Assumption Motion raised the stakes substantially for Intel—if the cross-license could be assumed it could thereafter be assigned to VIA or another entity, a result that that would be cataclysmic for Intel.

Not surprisingly, Intel fought back and served broad discovery demands seeking support for its argument that SONICblue had breached the cross-license by virtue of the joint venture transaction.

While expensive, this discovery was fruitful for the Estates. Over the summer of 2005 O'Melveny developed key evidence regarding the negotiation of the Cross License Agreement

[13] Mr. Bennett was included, given that his clients had volunteered when Intel asked for representatives of the creditors on the Committee to participate directly in this process. Bennett Dep. at 371:1-372:4, attached to Johnson Decl. as Exh. P.

helpful to O'Melveny's interpretation of certain provisions that supported the Assumption Motion, as well as evidence regarding VIA's conduct in the 2003 VIA-Intel settlement that supported arguments that VIA may have effectively waived (or should be bound from asserting) its liquidated damages claim. In early August 2005, O'Melveny deposed two Intel witnesses (Messrs. Blumberg and Snodgrass) and discovered key evidence related to the 2003 Intel-VIA Settlement that significantly strengthened the case O'Melveny was building.

F. August 2005 Settlement Negotiations

Lawyers from Heller Ehrman (representing VIA) and Pillsbury attended an August 11, 2005 settlement meeting, the stated purpose of which was to discuss a possible settlement of the VIA Books and Records Claim. Pillsbury was surprised when VIA made a settlement proposal that would have resolved all of VIA's claims, including the liquidated damages claim premised on the Intel license. That day, Mr. Boro of Pillsbury contacted Ms. Uhland of O'Melveny and reported that VIA had made a settlement proposal pursuant to which VIA would have a $42.5 million allowed claim and would be assigned the Estates' position in the Intel litigation, including the pending Assumption Motion. According to the Pillsbury attorneys, the proposed claim and assignment of the Intel litigation were two legs in what they called the "five-legged stool" settlement proposal advanced by VIA.

While the fact that VIA was interested in discussing settlement was encouraging, Ms. Uhland argued that the VIA offer was not attractive for several reasons. To begin with, and perhaps most basically, Ms. Uhland was very concerned about the proposal to assign the Estates' claims against Intel to VIA. Intel and VIA had a long history of acrimony and assigning the Estates' rights to VIA would entail a substantial risk that VIA's litigation tactics against Intel may create exposure for the Estates to Intel, perhaps including administrative priority claims in favor of Intel. And while the dollar amount of VIA's claim was more in Pillsbury's purview than O'Melveny's, Ms. Uhland expressed the view that a $42.5 million claim for VIA seemed excessive given a variety of factors, including: (i) Pillsbury's assessment of the Books and Records Claim was that the Estates' exposure was relatively small—probably a claim of around $2 - 3 million; (ii) VIA's best case with respect to the Intel license was likely a $35 million claim;

and (iii) the testimony of Intel's witnesses in recent depositions conducted by O'Melveny (each of which VIA attended) indicated that VIA's liquidated damages claim had serious fact problems.

The next day, Pillsbury convened a call with the Committee. Messrs. Boro and Loran participated as did Ms. Uhland, Anne Wells of Levene Neale (bankruptcy counsel to the Committee), Anne Kearns of KKSRR (IP counsel to the Committee) and Mr. Bennett, who had been participating in negotiations with Intel after having been nominated by the Committee for this role. Given that O'Melveny had focused almost exclusively on the aspects of the dispute relating to the Intel litigation, Ms. Uhland concentrated primarily on (a) the economic risks to the Estates associated with assigning the Intel litigation to VIA and (b) the risks associated with Intel learning that SONICblue was engaging in settlement negotiations with VIA.

The Committee was pleased that VIA had shown movement, but thought that a $42.5 million claim for VIA was excessive. After discussing the matter, the Committee reported that they would support a settlement of VIA's claim at anything less than $25 million and supported Pillsbury's proposal to counter at $6 million so that there would be room for movement. Boro Decl., Plaintiff's Exh. 149 at ¶¶ 10, 11, attached to Johnson Decl. as Exh. W.

In the days after August 17, 2005, Ms. Uhland had a series of discussions with Mr. Bennett in which they worked through an analysis of the claims Intel potentially could have against SONICblue and concluded that ***if*** SONICblue were to consider seriously VIA's proposal that it be assigned the right to pursue the Estates' litigation with Intel, such an arrangement should be conditioned on VIA indemnifying the Estates against Intel. Of course, Mr. Bennett's clients had been the only members of the Committee who were willing to heed Intel's request for creditors to participate in this dialogue and given the size of their claims, the consensus belief—among O'Melveny, Pillsbury and the SONICblue client representatives—was that opposition by the 2002 Noteholders would present a significant impediment to any potential settlement. In contrast, building and maintaining creditor support would be an important aspect of any successful settlement.

Over the following weeks, the parties analyzed the prospects for settlement and refined their positions. When VIA indicated that it was ready for another settlement meeting, the parties

prepared for a meeting ultimately held on September 15, 2005.

G. Negotiating the September 2005 Term Sheet

A few days before the September 15, 2005 in-person settlement meeting, Mr. Loran forwarded to Ms. Uhland, Mr. Eberhart and Mr. Bennett a counter-offer and draft term sheet that Mr. Loran had received the day before from VIA's attorneys at Heller Ehrman. Plaintiff's Exh. 21, attached to Johnson Decl. as Exh. X. Mr. Loran described VIA's settlement proposal as involving a $27.5 million allowed claim and the assignment of the Intel litigation to VIA. Plaintiff's Exh. 21, attached to Johnson Decl. as Exh. X. Obviously, this was an encouraging sign and close to the $25 million limit that the Committee had earlier indicated would be acceptable.

Ms. Uhland explained to Messrs. Boro and Loran of Pillsbury and to Mr. Bennett of HBD that she still considered VIA's demand to be excessive. By this point Ms. Uhland had pointed out that $27.5 million was close to VIA's best case recovery on its liquidated damages claim, because not only would the liquidated damages be capped at $35 million in an Intel deal, but also because the Estates had a right to put their shares in the joint venture to VIA for $10 million, ***if*** the liquidated damages were ever triggered, and that amount could be offset against the damages.[14] Moreover, if the put claim was not subject to offset—i.e. was a separate contractual right—the situation for the Estates would be better still. She also spent considerable time analyzing the terms of an indemnity from VIA and the collateral to secure that indemnity if VIA insisted on acquiring the Estates' rights against Intel.

On September 15, 2005, many of the parties involved in the litigation with VIA met at Pillsbury's San Francisco offices. Messrs. Loran and Mr. Boro from Pillsbury hosted. VIA was represented by Ed Slizewski from Heller and Mr. Kevane from Pachulski. S3 Graphics was represented by Luther Orton from Snyder Miller & Orton. Ms. Uhland and Mr. Eberhart of O'Melveny also attended.

At the September 15 meeting, there were several "breakout sessions," during which the sides conferred to discuss certain proposals and then regrouped for further negotiations. To argue

[14] *See* Class A Shares Option Agreement, attached to Plaintiff's Exh. 176, attached to Johnson Decl.

for a lower VIA claim, Ms. Uhland asserted that the Class A shares could be put to VIA for cash and that VIA would be entitled to no liquidated damages claims in light of its prior consents in connection with the 2003 Intel-VIA Settlement Agreement. In contrast, VIA argued that the liquidated damages provision did not impose a cap and further that VIA's damages may include an administrative claim portion.

The parties reached a total impasse over the proposed assignment to VIA of the Estates' rights against Intel and the corresponding right to a solid indemnification by VIA in favor of the Estates. VIA acknowledged that its primary purpose in seeking assignment of the Intel litigation would be to use the Assumption Motion and the facts developed by O'Melveny as leverage to get a broader release from Intel than VIA had negotiated in the 2003 Intel-VIA Settlement Agreement. Accordingly, the parties concluded that they could not complete a two-party settlement that would meet all of VIA's objectives and instead shifted focus to a three-party settlement where any agreement with VIA would be conditioned on SONICblue obtaining for VIA a release of both claims at issue in the 2003 action as well as actions accruing during the pendency of the bankruptcy cases.

Even this approach was very problematic for those focused on the Intel piece of the puzzle, including Ms. Uhland and Mr. Eberhart—for if not correctly crafted, the Estates could be obligated to expend substantial resources, including cash, in order to obtain a release from Intel. This release, moreover, was needed to cover products of the Joint Venture as to which Intel had previously sued for patent infringement. Intel had dismissed that litigation ***without prejudice*** in 2003. Ms. Uhland and Mr. Eberhart were, moreover, concerned that if Intel learned that a binding agreement had been reached with VIA, Intel might perceive that its bargaining position had improved and take a harder line in settlement negotiations. Without that release, O'Melveny's job was not done.

Toward the end of the settlement meeting, Mr. Kevane made a proposal that he termed a "mediator's proposal"—*i.e.*, not a proposal that his client had authorized, but what he thought a mediator would have proposed as a fair compromise and one that, if the professionals agreed, they each could advocate to their clients. He proposed that VIA have an allowed claim of

$12.5 million, which was roughly halfway between the amounts that the parties had been advocating.

Before the SONICblue attorneys left the September 15 meeting, Messrs. Loran, Boro and Eberhart and Ms. Uhland had breakout sessions during which they placed a call to Marcus Smith of SONICblue. Mr. Smith agreed that resolution of the litigation for $12.5 million was a very good result, ***provided*** that SONICblue could obtain the necessary releases from Intel.

Mr. Slizewski called Messrs. Boro and Loran of Pillsbury the next day to report that VIA had agreed to the $12.5 million figure and pressed for a response from the Debtors. Messrs. Boro and Loran informed Mr. Slizewski that SONICblue was in agreement with this settlement but that they also needed to get clearance from the major creditors to ensure that the settlement would be something that the Debtors could deliver. Boro Decl., Plaintiff's Exh. 149 at ¶ 16, attached to Johnson Decl. as Exh. W. Mr. Slizewski reacted negatively to this comment and reported that until and unless the Debtors and the creditors agreed to the $12.5 million figure, VIA would not proceed with negotiating a term sheet, and unless this happened quickly, VIA might withdraw from settlement discussions. *Id.* At this point, Messrs. Boro and Loran became quite anxious to accept the VIA offer and to accept it quickly.

Ms. Uhland and Mr. Eberhart, however, were not as enamored of the proposal. While they believed that the dollar amount of the proposed claim—$12.5 million—represented a reasonable discount off VIA's best (and reasonable) cases, the proposed settlement structure boded poorly for consummation since (i) it required obtaining a release from Intel and (ii) VIA appeared to want to place a substantial burden on the Debtors to deliver that release, even if it required the Estates to make a substantial payment to Intel. They also were not as concerned about VIA walking away from the settlement as were Messrs. Boro and Loran, for they knew that the recent evidence developed in discovery showed that VIA had a real down side risk that it would have no claim whatsoever on the license issue if the Estates were willing to litigate fully with Intel. This was a daunting and expensive prospect for the Estates, but VIA was well aware of the fact that discovery had turned up information that could be very damaging to its claims. In contrast, Pillsbury, necessarily, was not involved in this aspect of the litigation given its Intel

conflict.

Logistics over the next few days were frustrating for many of the major parties. Messrs. Boro and Loran had informed Mr. Slizewski that VIA could expect an answer promptly, and no later than early on Monday morning, September 19, 2005. But Ms. Uhland was tied up in all-day meetings on Friday, September 16 and on other matters on Monday September 19, and Mr. Bennett was in New York on other business. Ms. Uhland and Mr. Eberhart also thought that the process should be slowed down slightly until Ms. Uhland had a chance to vet with Mr. Smith of SONICblue the difficulties inherent in the Intel part of the settlement proposal. Messrs. Boro and Loran understandably were not sensitive to these issues, since Pillsbury's conflict with Intel precluded them from being privy to these matters. But Mr. Bennett was, given that he had been commissioned as the Committee's envoy to the Intel negotiations. And Mr. Bennett shared the concern that an attractive deal with VIA not be agreed to too quickly if the result was an extremely difficult road ahead with Intel that could render any agreement with VIA more costly to the Estate than anticipated. Bennett Dep. at 195:12-196:18; 206:3-8, attached to Johnson Decl. as Exh. P.

As it turned out, on the morning of September 15, 2005, Mr. Boro (whose specialty is commercial litigation rather than bankruptcy law) had contacted Matthew Walker, a Pillsbury bankruptcy attorney, to gain a better understanding of the distinctions Ms. Uhland was drawing between a put right that the Estates had against VIA that might be netted via offset and such a claim that might be collected at 100 cents on the dollar if there was no mutuality. These were concepts that were outside Mr. Boro's expertise. Boro Dep. at 160:11-161:10, attached to Johnson Decl. as Exh. Y. During the call, Mr. Walker told Mr. Boro that there was a provision in the Indenture for the 2002 Notes that provided VIA with $15 million in senior indebtedness. Boro Dep. at 160:25-161:6, attached to Johnson Decl. as Exh. Y; *see also* Plaintiff's Exh. 26, attached to Johnson Decl. as Exh. Z. This was the first time that Mr. Boro had heard of the senior indebtedness provision in the Indenture. Boro Dep. at 161:16-19, attached to Johnson Decl. as Exh. Y. At the end of the call, Mr. Boro asked Mr. Walker to fax him a copy of the Indenture, which Mr. Walker did, along with sections of an internal Pillsbury memorandum that

summarized, but did not analyze, various provisions in the Indenture. Plaintiff's Exh. 27, attached to Johnson Decl. as Exh. AA.

The next day, Mr. Boro called Ms. Uhland. Ms. Uhland remembers that Mr. Boro asked her if Mr. Bennett was aware that $15 million of VIA's claim would be senior to the 2002 Notes under the terms of the Indenture. Ms. Uhland was surprised that Mr. Boro considered the existence of the Indenture to be a revelation, for she was aware that this issue had been addressed far earlier, including in the 2003 Houlihan analyses that had been shared with Levene Neale and the June 2004 discussion with Mr. Gershon, where he explained that VIA had considered making a $15 million loan but that it never had closed. Mr. Loran of Pillsbury had participated in the June 2004 discussion, but his partner Mr. Boro had not. Thus, Ms. Uhland recounted for Mr. Boro the conversation she had with Mr. Gershon on June 15, 2004 regarding the contemplated $15 million loan from VIA to SONICblue that never materialized. Although Ms. Uhland did not have a copy of the Indenture readily available, she paraphrased for Mr. Boro her understanding, based on her June 2004 discussion with Mr. Gershon, of the definitions of "indebtedness" and "principal" from the Indenture.

Ms. Uhland was concerned that if Mr. Boro thought that a settlement with VIA for a $12.5 million claim would result in VIA having a claim that was senior to the 2002 Notes, there was no basis for a settlement, for she also knew that Mr. Bennett did not share this view. Although Ms. Uhland had not even considered the senior debt issue since June 2004, she clearly remembered that prior discussion with Mr. Gershon, Mr. Loran and Mr. Bennett. In order to make sure that there really was a meeting of the minds among those adverse to VIA, on Saturday, September 17, 2005, she sent Mr. Bennett an e-mail in which she reported a "weird call from Al Boro" the prior day in which Mr. Boro had asked if Mr. Bennett was aware that the VIA settlement claim would be senior debt. Plaintiff's Exh. 35, attached to Johnson Decl. as Exh. BB. In this e-mail, Ms. Uhland reported that she had advised Mr. Boro of the June 2004 discussion with Messrs. Gershon, Bennett and Loran and referred him to some of the terminology in the Indenture that rendered it unlikely that the sort of settlement being proposed would qualify as senior debt. Plaintiff's Exh. 35, attached to Johnson Decl. as Exh. BB. Unless this issue was

surfaced and dealt with before advancing discussions with VIA, it was possible that settlement discussions might appear to make progress only to screech to a halt when this issue was joined.

Mr. Bennett expressed incredulity that the litigation team from Pillsbury was not apparently in communication with the Pillsbury bankruptcy lawyers who had looked at this issue previously. Mr. Bennett also expressed concern that VIA's term sheet allowed VIA to allocate the $12.5 million claim among VIA Technologies and S3 Graphics. Mr. Bennett found this potentially quite troubling since he asserted that only S3 Graphics, not VIA, had any potential for asserting claims under the Investment Agreement, whereas, only VIA, not S3 Graphics, was even mentioned in the Indenture. Thus, he thought that this requested ability to allocate claims to VIA that rightfully belonged to S3 Graphics might be an attempt by VIA to inappropriately shoehorn the $12.5 million claim into the senior debt definition of the Indenture. Bennett Dep. at 322:19-324:11, attached to Johnson Decl. as Exh. P.

Ms. Uhland did not represent to Mr. Boro that she had conducted a detailed investigation of the Indenture. She had not, for this was not part of O'Melveny's assignment. This Indenture had been negotiated by Pillsbury and Mr. Boro decided to dig further. He later investigated the history of the prior settlement discussions and the negotiation of the Indenture and reviewed documents dating to 2002. His investigation "confirmed that this provision was included in the definition of 'Senior Indebtedness' as a placeholder for a loan of $15 million that VIA was to have made" that never closed. Boro Decl., Plaintiff's Exh. 149 at ¶ 20, attached to Johnson Decl. as Exh. W. Indeed, in his deposition, Mr. Boro testified that when he raised this issue with Ms. Uhland on September 16, 2005, it was not to express the view that the first $15 million of a VIA claim would, in fact, be senior debt under the Indenture. Instead, he merely raised a question about the issue and after having floated it and having investigated it further, was persuaded that a settled VIA claim ***would not*** be senior under the Indenture. Boro Dep. at 195:20-197:4; 206:18-208:5; 634:2-23; 644:25-645:16, attached to Johnson Decl. as Exh. Y.

On Monday, September 19, Ms. Uhland was tied up almost the entire day in meetings unrelated to SONICblue. She remained concerned that the SONICblue team resolve the language in the term sheet ***regarding the Intel release*** so that SONICblue would not be trapped in an

untenable position vis-à-vis Intel.

Mr. Bennett also was unavailable for much of the day on September 19, 2005, as he was in New York on another matter. During the day, he managed to confirm to both Ms. Uhland and Mr. Boro that his clients would support a settlement of the VIA claim at $12.5 million if it were "clear that claim is not for borrowed money or anything else that might constitute senior debt." Plaintiff's Exh. 41, attached to Johnson Decl. as Exh. CC. But he remained concerned with VIA's demand that it get a release from Intel for the past two years and wanted to discuss some thoughts he had on how best to deal with the Intel issues. Plaintiff's Exh. 41, attached to Johnson Decl. as Exh. CC.

On the morning of Tuesday, September 20, Ms. Uhland sent a revised draft term sheet to Mr. Bennett. The revised term sheet attempted to incorporate the language proposed by Mr. Bennett regarding the senior debt issue as well as deal with the Intel release. Thus, this version of the term sheet provided that the $12.5 million VIA claim would "constitute a claim for damages against SONICblue, not a claim for indebtedness or borrowed money." Plaintiff's Exh. 45, attached to Johnson Decl. as Exh. DD. And with respect to the Intel piece, it provided that the release SONICblue was required to obtain from Intel would be obtained "without the payment of additional consideration to Intel . . . ." *Id.* Otherwise, VIA could have insisted that SONICblue spend whatever it took to obtain a release from Intel and Intel could have held SONICblue hostage.

Later that morning, Mr. Loran sent Ms. Uhland, Mr. Eberhart and Mr. Smith an e-mail indicating that he had called Mr. Slizewski (VIA's counsel at Heller) to accept the $12.5 million proposal. Plaintiff's Exh. 47, attached to Johnson Decl. as Exh. EE. Mr. Loran did not consult with the O'Melveny attorneys before unilaterally calling to accept the settlement figure. Ms. Uhland was disappointed, because she felt that SONICblue had lost negotiating leverage without first vetting the Intel issues. Nonetheless, O'Melveny scheduled time later that morning to participate in a team call with Messrs. Loran, Boro and Smith. The purpose of the call was to gain agreement among the parties, including Mr. Smith, regarding the strategy for the call with the VIA attorneys later that day, and the introduction of the additional terms regarding Intel.

On the SONICblue team call, Ms. Uhland was asked to circulate a revised term sheet. She sent this redraft later that day to the meeting participants ("September 20 Draft"). Plaintiff's Exh. 50, attached to Johnson Decl. as Exh. FF. This draft dealt with the senior debt issue by providing that the $12.5 million VIA claim would be "neither senior nor junior to any other general unsecured claim" and which claim "shall constitute a claim for damages against SONICblue, not a claim for indebtedness or borrowed money." *Id.*

Later that afternoon, the O'Melveny attorneys participated in a conference call with Mr. Boro and Mr. Loran representing the Debtors; Mr. Slizewski and Mr. Kevane representing VIA; and Mr. Orton and Ms. Rees representing the Joint Venture. The attorneys from Pillsbury took the lead on the call, again reiterating that SONICblue and the bondholders had agreed to the $12.5 million figure. Boro Dep. at 266:18-267:3; 269:11-270:18, attached to Johnson Decl. as Exh. Y. Representatives from SONICblue also stated that the Estates should not be obligated to pay to obtain an Intel release and that the SONICblue attorneys would be adding clarifying language to that effect.

On the morning of September 21, 2005, Ms. Uhland sent an e-mail to Messrs. Boro, Loran and Eberhart, attaching a revised draft of the term sheet ("September 21 Draft"). Plaintiff's Exh. 53, attached to Johnson Decl. as Exh. GG. The draft incorporated comments from Ms. Uhland and Mr. Boro. Section 1 was revised to provide as follows:

> Claimants shall jointly hold a single, allowed, general unsecured claim in the Chapter 11 case of SONICblue Inc. in the amount of $12.5 million representing a compromise of the damages claims asserted by the Claimant (the "Allowed Claim"), which claim shall be neither senior nor junior to any other general unsecured claim.

Later that afternoon, Ms. Uhland circulated the September 21 Draft term sheet to Mr. Slizewski representing VIA and the SONICblue team. Plaintiff's Exh. 54, attached to Johnson Decl. as Exh. HH. The "neither senior nor junior" language in Section 1 remained unchanged from the draft she sent earlier that day.

Also on September 21, Ms. Uhland called Ms. Anne Wells of Levene Neale, who was O'Melveny's primary contact with the Committee about the Intel litigation. Ms. Uhland gave Ms. Wells background on the status of the settlement discussions in order to ensure that

Committee counsel was in the loop on these developments.

VIA responded by revising the term sheet the next day, in advance of a call that had been set up among the representatives of the Debtors and VIA ("September 22 Draft"). Plaintiff's Exh. 56, attached to Johnson Decl. as Exh. II. VIA struck the "neither senior nor junior" language and indicated on the call that they did so mainly because they did not understand what it was intended to accomplish. Plaintiff's Exh. 59, attached to Johnson Decl. as Exh. JJ.

Later that evening, VIA circulated a revised term sheet, which Mr. Eberhart forwarded to the rest of the SONICblue team and to Mr. Bennett. Plaintiff's Exh. 61, attached to Johnson Decl. as Exh. KK. In the cover e-mail, Mr. Eberhart asked Mr. Bennett for his "view on the elimination of the 'neither junior nor senior' language from [Section] 3.a." Plaintiff's Exh. 61, attached to Johnson Decl. as Exh. KK. Mr. Loran responded about an hour later, indicating that Mr. Boro had spoken to Mr. Bennett about the "neither junior nor senior" language and that it would be put back into the term sheet. Plaintiff's Exh. 62, attached to Johnson Decl. as Exh. LL. Neither Ms. Uhland nor Mr. Eberhart was involved in Mr. Boro's conversation with Mr. Bennett or otherwise consulted about re-inserting the language into the term sheet.

In the early afternoon on September 23, 2005, Mr. Loran sent an e-mail to Mr. Slizewski (with a copy to the O'Melveny attorneys and Mr. Boro), attaching a revised term sheet ("September 23 Draft"). Plaintiff's Exh. 63, attached to Johnson Decl. as Exh. MM. According to Mr. Loran's cover e-mail, this draft made modifications to VIA's September 22 Draft, consistent with the parties' discussion on the September 22 conference call. Section 3.a of the September 23 Draft provided as follows:

> Claimants shall jointly hold a single, allowed general unsecured claim in the Chapter 11 case of SONICblue, Inc., which claim shall be afforded the benefits and priority of SONICblue's other allowed general unsecured claims but shall be neither junior nor senior to any other allowed junior unsecured claim, in the amount of $12.5 million, representing a compromise of the claims that have been asserted by the Claimants for damages and other relief based on alleged breaches of the Amended and Restated Investment Agreement, including, without limitation, liquidated damages for the alleged breach of section 5.6 thereof (the "Allowed Claim").

On Monday, September 26, 2005, Ms. Uhland spoke to Mr. Kevane of Pachulski (counsel

to VIA) by phone. Ms. Uhland remembers that the call primarily was about the strategy for negotiating with Intel after the execution of the term sheet, VIA having negotiated for the right to be consulted regarding the Estates' efforts to compromise with Intel. She also recalls that Mr. Kevane wanted to discuss various issues that were raised during the September 22 VIA - SONICblue conference call, in which Ms. Uhland had been unable to participate. One of these issues was the inclusion of the "neither junior nor senior" language. Ms. Uhland explained that this language had been inserted at the request of the 2002 Noteholders and Mr. Kevane clearly understood that the 2002 Noteholders were the source of this language. Kevane Dep. at 45:4-46:1; 46:14-18, attached to Johnson Decl. as Exh. NN. Ms. Uhland described the language in the Indenture and that she understood that during 2002, VIA and SONICblue had discussed the possibility of VIA making a $15 million loan to SONICblue, but that those negotiations had taken another turn and this loan was never made. Thus, she explained that the "neither junior nor senior" language in the term sheet was requested by the 2002 Noteholders to provide them with assurances that VIA was not trying to convert a damages claim into a loan claim, which arguably would be entitled to seniority under the Indenture.

Ms. Uhland did not intend or expect Mr. Kevane to rely on her explanation, and he did not. Mr. Kevane independently checked with the VIA business people—including senior people at his client—and concluded that the proposed "neither senior nor junior" language was acceptable to VIA. Kevane Dep. at 47:1-15; 47:22-48:5, attached to Johnson Decl. as Exh. NN.

Later that day, Mr. Loran worked with Mr. Slizewski to refine some of the language in the term sheet. *See, e.g.*, Plaintiff's Exhs. 65, 66, attached to Johnson Decl. as Exhs. OO, PP.

At around noon on September 27, 2005, Ms. Uhland received an e-mail from Mr. Slizewski, attaching the final term sheet, signed by representatives of VIA and the Joint Venture. Plaintiff's Exh. 68, attached to Johnson Decl. as Exh. QQ.

That same day, Mr. Boro sent this term sheet to the lawyers at Levene Neale (including Mr. Rankin and Ms. Wells) and KKSRR (Anne Kearns) representing the Committee. It provided that VIA would have an allowed general unsecured claim of $12.5 million and would be neither junior nor senior to other creditors. Plaintiff's Exh. 69, attached to Johnson Decl. as Exh. RR.

Of course, the Committee had earlier received the Houlihan analyses that assumed that the first $15 million of any VIA claim would be senior to the 2002 Notes and was aware of the language in the Indenture. Accordingly, the Committee was aware (or should have been) that VIA was effectively waiving any right to assert that its $12.5 million claim would be senior. The allowed amount of the VIA claim—$12.5 million—was exactly half of the amount that the Committee had indicated that it would accept a few weeks earlier.

Pillsbury arranged a call for the afternoon of September 27, 2005, with representatives of the Committee. The attorneys from Pillsbury (Messrs. Boro and Loran) led the call. Mr. Rankin and Ms. Wells participated from Levene Neale, as did Messrs. Smith and Gershon from SONICblue, Mr. Eberhart from O'Melveny and Mr. Bennett of HBD. Almost all of the conversation was focused on the settlement number. The Committee members were ecstatic and highly complimentary of the "incredible result." Boro Dep. at 362:20-363:11, attached to Johnson Decl. as Exh. Y.

Several aspects of the efforts to resolve the VIA dispute during late summer and early fall 2005 warrant particular emphasis. First, settling with VIA was only the first step in resolving this matter. An agreement with VIA also required bringing home an agreement with Intel or prevailing in litigation with Intel that undoubtedly would have taken years to resolve and would have required the Estates to expend substantial additional resources. O'Melveny was particularly concerned about this aspect of the settlement and focused on ensuring that an agreement with VIA not focus just on this first aspect of a deal and put an untenable burden on the Estates to deliver a release from Intel or to give VIA unfettered authority to deal with Intel on behalf of the Estates. Particularly from September 16-21, 2005, Ms. Uhland and Mr. Eberhart were concerned that Pillsbury not rush to accept a settlement with VIA for an allowed claim that the Pillsbury team thought was a very good result, but that would create inappropriate burdens for the Intel piece in which Pillsbury was not involved and could not be involved given its Intel conflict. The resolution reached in late September 2005 left a substantial task for O'Melveny to deliver, but at least the VIA agreement in principle did not require the Estates to take positions that might disadvantage the Estates as O'Melveny returned to do battle with Intel.

Second, once the parties agreed on an amount for the VIA claim—$12.5 million—whether that claim was senior or *pari passu* with the 2002 Notes was purely an issue between VIA and the 2002 Noteholders. For example, if unsecured claims (including the VIA claim at $12.5 million) totaled $500 million and the Estates' distributable assets totaled about $125 million, other unsecured creditors would receive a 25% distribution ($125 million divided by $500 million) irrespective of whether the VIA claim was senior to the 2002 Notes or *pari passu* with them. If the VIA claim was *pari passu* with the 2002 Notes, it too would receive a 25% distribution—*i.e.*, $3.125 million. If, on the other hand, the VIA claim was senior to the 2002 Notes, VIA would likely receive a 100% distribution (*i.e.*, $12.5 million) with the extra $9.375 million ($12.5 million, minus $3.125 million) being turned over to VIA by the 2002 Noteholders from the distribution that otherwise would go to these noteholders. But, in either case, other unsecured creditors would receive 25 cents on the dollar. In other words, the Estates and the unsecured creditors were indifferent as to how this issue was resolved, but it mattered to VIA and the 2002 Notes. From discussions in June 2004, Ms. Uhland understood that Mr. Bennett believed strongly that no VIA claim would be senior to the claims of his clients. This was a topic that had been vetted by Pillsbury, Mr. Bennett and the Committee without any involvement from O'Melveny. Ms. Uhland was aware of the issue and knew that if Mr. Boro, who was new to this analysis, thought that the VIA claim was senior, this had to be revisited with Mr. Bennett or the parties would soon face a roadblock in reaching any sort of meeting of the minds. Mr. Boro did an investigation and concluded that VIA's claim was not senior. The term sheets negotiated with VIA reflected this position.

Third, since only VIA stood to gain if its $12.5 million claim were senior to the 2002 Notes, it was incumbent on VIA to raise this issue if it thought there was a credible case to do so. Ms. Uhland never represented to VIA that she had independently investigated this issue—she had not—and Mr. Kevane clearly understood that the language in the term sheet had been proposed by the 2002 Noteholders. As one would expect, Mr. Kevane checked with the business people at VIA. After he had completed this diligence, VIA did not push back at all. If there was any serious issue about the senior debt issue, one surely would expect that VIA, the party with money

at stake, would have raised it.

Fourth, Levene Neale was aware of these issues and was enthusiastic about the settlement.

The Objecting Parties have argued, in hindsight, that Pillsbury and O'Melveny should have negotiated with VIA and Mr. Bennett for a lower allowed VIA claim coupled with an agreement that the VIA claim was senior. ***If*** possible, they contend that this could have resulted in marginally less dilution for other unsecured creditors. This argument is purely hindsight, for no one suggested it at the time, including Pillsbury (which had negotiated the Indenture). It also ignores the fact that VIA, the party with the most to gain from such an approach, did not at the time contend that there was even a plausible argument that it was entitled to seniority. It further ignores the fact that going down this path would have required substantial bargaining with the Estates' largest creditors who were adamant that no VIA claim could be senior. If VIA had come back with an argument that whatever claim it was allowed was senior to the 2002 Notes, the parties necessarily would have gone down that path. But since VIA did not, no one will ever know whether such an approach could ever have reached closure. This argument also ignores that Pillsbury and the Committee, each of whom was fully aware of the senior debt issue, were very enthusiastic over settling the VIA claim at $12.5 million and Pillsbury in particular did not want to risk losing this deal by any delay at all.

To be clear, O'Melveny did not conduct an independent investigation of the 2002 Indenture and its relationship with the VIA claim. This was not O'Melveny's charge. Mr. Boro has testified that he did so, and was satisfied that the claim was not senior. O'Melveny did not delve into these matters and does not have a view as to whether he was correct. Rather, O'Melveny strived to ensure that both the 2002 Noteholders and VIA really reached a meeting of the minds on this issue. They did.

H. Negotiating and Documenting the Three-Way Settlement

Between the end of September 2005 and December 2005, the O'Melveny attorneys were focused on trying to persuade Intel to provide the releases for VIA that were conditions to any settlement. Most of these negotiations were with Steve Johnson of Gibson Dunn, which represented Intel. Given Intel's position throughout the case that the joint venture structure was a

"sham transaction," obtaining a release for VIA was a formidable task—Intel had in prior settlement discussions refused to provide any type of release or license for VIA even when the Estates offered to compensate Intel. O'Melveny, however, had built a strong case for its Assumption Motion—the success of which would have created extremely damaging precedent for Intel—and using the legal and factual analyses developed made a demand for a release ***and*** a cash settlement from Intel if SONICblue agreed to terminate the cross license. Despite substantial skepticism by the major parties in the case (who expected the Debtors to need to pay some cash as consideration for releases from Intel), this approach was a resounding success. By December 2005, Intel agreed to give SONICblue and VIA releases without the payment of additional consideration from the Estates.

Intel and SONICblue started to negotiate a term sheet, but soon concluded that it would be better to turn directly to a definitive settlement agreement, including incorporating the VIA term sheet into more formal documentation.

In January 2006, Austin Barron from O'Melveny circulated the first draft of the three-way settlement agreement to Pillsbury, the SONICblue client representatives, counsel for VIA and counsel for Intel. Plaintiff's Exh. 74, attached to Johnson Decl. as Exh. SS. From January through September 2006, the parties hashed out detailed language. Mr. Barron generally served as the scrivener for the SONICblue team, incorporating revisions (sometimes voluminous) from the various parties.

On April 21, 2006, Mr. Boro of Pillsbury sent Ms. Uhland a markup of the settlement agreement. Plaintiff's Exh. 76, attached to Johnson Decl. as Exh. TT. He proposed, for the first time, expressly referencing the Indenture, as follows:

> Claimants and the Debtor agree that the Allowed Claim is not, and shall not be treated as, "Senior Indebtedness" under the terms of the Debtor's Indenture, dated as of April 22, 2002, for the 7-3/4% Secured Senior Subordinated Convertible Debentures due 2005.

No one from Pillsbury consulted with Ms. Uhland or any attorney at O'Melveny concerning this language. It also was not intended as a substantive change, for the "neither junior nor senior" language had the same effect as a specific reference to the Indenture. Messrs. Boro

and Loran of Pillsbury thought that this was simply clearer and would avoid any subsequent disputes. Boro Decl., Plaintiff's Exh. 149 at ¶ 20, attached to Johnson Decl. as Exh. W.

After Mr. Barron sent this language to VIA, Mr. Kevane of Pachulski sent Mr. Barron an e-mail requesting a copy of the Indenture that was now specifically referred to in the draft settlement agreement. Plaintiff's Exh. 80, attached to Johnson Decl. as Exh. UU. Mr. Barron forwarded a copy of Mr. Kevane's e-mail to Mr. Boro, requesting a copy of the Indenture. Plaintiff's Exh. 80, attached to Johnson Decl. as Exh. UU.

On May 18, 2006, Mr. Boro forwarded portions of the 2002 Indenture to Mr. Barron (with a copy to Ms. Uhland and Mr. Loran). Plaintiff's Exh. 81, attached to Johnson Decl. as Exh. VV. Mr. Boro's cover e-mail stated:

> Barron [sic], per your request, attached is a PDF with relevant excerpts from the 7-3/4% secured subordinated debenture. The $15 million indebtedness to VIA referred to in clause (g) of the definition of senior indebtedness (Section 1.1, at page 7) was a $15 million loan that VIA and SONICblue were negotiating but which was never consummated. ***Please ask Henry to call me if he would like more background on the proposed loan or if he has other questions on this change***. (Emphasis added).

Mr. Barron sent Mr. Kevane the Indenture excerpts provided by Mr. Boro of Pillsbury. In the transmittal e-mail, Mr. Barron included Mr. Boro's explanation of the proposed VIA loan transaction (with attribution) and instructed Mr. Kevane to call Mr. Boro directly with any questions. Plaintiff's Exh. 83, attached to Johnson Decl. as Exh. WW.

On June 1, Ms. Uhland attended an in-person settlement meeting, the purpose of which was to discuss comments to the draft settlement agreement. The other participants were Mr. Barron of O'Melveny, Mr. Loran of Pillsbury, Johnny Lee (a business person at VIA), Mr. Kevane and Ms. Bal of Pachulski on behalf of VIA; Mr. Orton on behalf of the Joint Venture; and Mr. Johnson of Gibson Dunn on behalf of Intel. During the meeting, Mr. Boro raised the issue of the Indenture and led this portion of the discussion. Boro Dep. at 516:24-517:4, attached to Johnson Decl. as Exh. Y. Mr. Kevane said that he was worried that the "neither junior nor senior" language might disadvantage VIA vis-à-vis other general unsecured creditors. Thus, Mr. Kevane requested that the parties include language to the effect that the VIA claim was "*pari*

passu," which language he suggested replace the "neither junior nor senior" language. Mr. Boro again reiterated that the senior indebtedness language in the Indenture was intended to apply to a specific $15 million loan from VIA to SONICblue, which loan never materialized. VIA agreed. Plaintiff's Exh. 88, attached to Johnson Decl. as Exh. XX.; Boro Dep. at 518:12-520:7, attached to Johnson Decl. as Exh. Y.

Throughout summer 2006, the parties continued to engage in extensive and at times heated settlement negotiations and drafting sessions. However, there was no controversy over the senior debt language. Because certain VIA issues negotiated by Pillsbury were the last issues to be resolved, Pillsbury prepared and circulated the final version of the settlement agreement on September 19, 2006. Plaintiff's Exh. 93, attached to Johnson Decl. as Exh. YY. The parties signed the settlement agreement by the first week in October 2006.

I. Motion to Approve the Settlement

Once there was a final settlement, Pillsbury was anxious to get it approved as soon as possible. Pillsbury—without consulting O'Melveny—determined that the Motion to Approve the Settlement under FRBP 9019 ("9019 Motion") should be filed in time to be heard on October 27, 2006 when the Court was hearing other matters in these cases. In order to be heard on regular notice on October 27, the motion needed to be filed no later than October 6. Plaintiff's Exh. 97, attached to Johnson Decl. as Exh. ZZ.

Matt Walker from Pillsbury prepared the first draft of the 9019 Motion and the supporting memorandum of points and authorities. Walker Dep. at 106:19-107:7, attached to Johnson Decl. as Exh. AAA. Mr. Walker considered whether he should include a discussion of the senior debt issue in the motion and supporting papers, but made a conscious decision not to. Walker Dep. at 227:25-228:6, attached to Johnson Decl. as Exh. AAA; *see also* Boro Dep. at 527:9-527:19, attached to Johnson Decl. as Exh. Y. According to Mr. Walker, it was a "non-issue," because VIA had never claimed it was entitled to priority under the Indenture, and, as he understood it, had affirmatively acknowledged that it had no intention of claiming priority over the 2002 Noteholders under the Indenture. Walker Dep. at 227:6-24, attached to Johnson Decl. as Exh. AAA. Moreover, Mr. Walker concluded that the senior indebtedness issue had no effect on the

Estates, "because if VIA had claimed priority under the senior note indenture, that money would have come out of the senior noteholders' pockets, not the estate's." Walker Dep. at 226:5-227:5, attached to Johnson Decl. as Exh. AAA. Mr. Boro's testimony is consistent with Mr. Walker's. According to Mr. Boro, "a decision was made" as to what should be highlighted in the memorandum of points and authorities and then to attach the settlement agreement for the Court's review in detail. Boro Dep. at 531:6-532:7, attached to Johnson Decl. as Exh. Y. At the time the 9019 Motion was filed, Mr. Boro did not think the senior indebtedness waiver was material and he did not give it much thought, because it had not been the subject of any negotiations for several months. Boro Dep. at 531:6-532:7, attached to Johnson Decl. as Exh. Y. Pillsbury had the lead role for the VIA portion of the settlement and saw no need to consult with O'Melveny regarding what should be included in this portion of the 9019 Motion. O'Melveny was simply not involved in this thinking.

Pillsbury did not circulate the initial draft of the 9019 Motion and memorandum of points and authorities to O'Melveny until the afternoon of October 5. Plaintiff's Exhs. 94, 95, attached to Johnson Decl. as Exhs. BBB, CCC. In the transmittal e-mails, Pillsbury asked O'Melveny to address the Intel issues, with which Pillsbury was not familiar. Plaintiff's Exh. 97, attached to Johnson Decl. as Exh. ZZ. O'Melveny was not asked to comment on or otherwise revise the motion or supporting papers in any respect.

The O'Melveny attorneys were forced to work under tremendous time pressure, given that Pillsbury required comments the following morning. Plaintiff's Exh. 97, attached to Johnson Decl. as Exh. ZZ. When Mr. Barron asked for additional time to review the documents, he was told by Mr. Loran that it was a firm deadline and was told again to address the Intel aspects of the pleading. *Id.*

Mr. Barron worked through the afternoon of October 5 and into the early morning of October 6 to edit and revise the moving papers. Plaintiff's Exh. 101, attached to Johnson Decl. as Exh. DDD. On the morning of October 6, Ms. Uhland sent revisions and a redline of the papers to Mr. Loran. Plaintiff's Exh. 102, attached to Johnson Decl. as Exh. EEE. As requested, O'Melveny's revisions focused on the Intel litigation and settlement, a full discussion of which

had not been included in the initial Pillsbury draft of the moving papers. Plaintiff's Exhs. 96, 102 attached to Johnson Decl. as Exhs. FFF, EEE. The O'Melveny revisions added nearly three pages of discussion of the Intel-VIA dispute and nearly two pages of discussion of the settlement of the Intel litigation. Plaintiff's Exh. 96, 102, attached to Johnson Decl. as Exhs. FFF, EEE.

Pillsbury also took responsibility for circulating drafts of the moving papers to the Committee and obtaining its approval. Plaintiff's Exhs. 94, 97, 98, attached to Johnson Decl. as Exhs. BBB, ZZ, GGG. Late in this process, Mr. Walker added some language to page one of the memorandum of points and authorities that indicated that VIA would have a general unsecured claim of $12.5 million, on which VIA was likely to recover approximately $4 million. Plaintiff's Exh. 107, attached to Johnson Decl. as Exh. HHH. This would have identified how the senior debt issue was resolved for any party who was familiar with the issue in the first place, but probably would not have flagged the issue for anyone who was not familiar with the issue.

From discovery in these cases, O'Melveny is now aware that this was not the first time that Pillsbury had addressed this issue. In July 2006, Mr. Walker was working on a draft of the disclosure statement that Pillsbury intended to file with the plan on which they were also working. Mr. Walker initially had drafted language discussing the senior debt issue in some detail. But Mr. Boro (his superior) decided to cut this disclosure. Mr. Boro instructed Mr. Walker to delete this language, stating: "I would not want VIA to start thinking that it has a pressure point here (when it does not). . . . I have added language that we do not believe that VIA contests our position on the subordination provision (because it has agreed to a settlement term to that effect)." Plaintiff's Exh. 132, attached to Johnson Decl. as Exh. III. O'Melveny was not copied on this exchange and was not involved in preparing or reviewing the disclosure statement.

Because Pillsbury had taken the lead in drafting the 9019 Motion and supporting papers, the initial plan was for them to handle the actual filing. Plaintiff's Exh. 99, attached to Johnson Decl. as Exh. JJJ. However, at the last minute, Intel's counsel argued that the settlement agreement contained confidential information and thus had to be filed under seal. Plaintiff's Exh. 100, attached to Johnson Decl. as Exh. KKK. Because O'Melveny had handled all of the Intel

litigation (almost all of which involved information subject to the various protective orders), O'Melveny was familiar with the Court's specific procedures for e-filing documents under seal and O'Melveny agreed to file the motion on behalf of the Debtors.

O'Melveny had urged, from the outset, that the ***entire*** settlement agreement be filed with the motion, unredacted and not under seal. Plaintiff's Exh. 99, attached to Johnson Decl. as Exh. JJJ. But at Intel's insistence, the Debtors agreed to file the motion, memorandum of points and authorities, and the settlement agreement under seal and did so on the evening of October 6, 2006. Plaintiff's Exh. 114, attached to Johnson Decl. as Exh. LLL. Of course, a complete, unredacted copy of the settlement agreement was filed with the Court.

O'Melveny thought it best to prepare a redacted version of the Motion that might pass muster with Intel and could be filed and publicly accessible. Like most such matters involving Intel's confidential information, this was not easy. On October 24, 2006, Mr. Barron sent Mr. Johnson of Gibson Dunn a copy of the proposed redacted version of the memorandum of points and authorities in support of the Rule 9019 motion. Plaintiff's Exh. 119, attached to Johnson Decl. as Exh. MMM. But Pillsbury and Levene Neale—particularly Mr. Rankin—urged against filing the redacted version of the memorandum of points and authorities and their view prevailed. Plaintiff's Exhs. 120, 121, attached to Johnson Decl. as Exhs. NNN, OOO.

The settlement was then approved by the Court at the October 27 hearing.

Controversies about the settlement surfaced in January 2007, when several creditors objected to the adequacy of the disclosure statement's discussion of the senior debt issue. SB Claims soon joined the fray. SB Claims had acquired VIA's and S3 Graphics's rights pursuant to a Claim Transfer Agreement dated April 24, 2007. Recital E of the Claim Transfer Agreement excerpts the senior indebtedness waiver provision in full. [Docket Number 2274] Plaintiff's Exh. 166, at 21, attached to Johnson Decl. as Exh. A. SB Claims had been advised of VIA's general release from the time SB Claims first expressed interest in acquiring VIA's rights in the case in December 2006. Plaintiff's Exh. 171, attached to Johnson Decl. as Exh. PPP. And, in January 2007, SB Claims had been forwarded emails written by Pillsbury that excerpted the senior indebtedness provision and explained its background at length. Plaintiff's Exh. 172,

attached to Johnson Decl. as Exh. QQQ.

O'Melveny was not involved in preparing the disclosure statement to which these parties objected and O'Melveny's active participation in these cases had concluded the prior October.

Subsequently, allegations were made that the 2002 Noteholders used a Pillsbury opinion letter to pressure Pillsbury to drop an objection to the amount of unaccreted original issue discount given to the 2002 Noteholders; that Pillsbury had not disclosed this conflict; that Pillsbury had received undisclosed preferences; and that Pillsbury and Levene Neale had reached a convenient arrangement regarding prosecuting preferences and objections to the 2002 Noteholders' claims. This Court ultimately appointed a chapter 11 trustee and significant litigation ensued. What O'Melveny knows about these issues it has read in public filings and in the press, for O'Melveny had no inkling of them at the time.

IV. CONCLUSION

As the SONICblue cases approach their conclusion, the troubled path they have taken cannot detract from the overwhelming evidence that O'Melveny delivered tremendous value to, and at all times acted in the best interests of, the Debtors and their Estates.

For the foregoing reasons, O'Melveny respectfully requests that the Court overrule all objections and grant O'Melveny's Fifth and Final Fee Application in full.

Dated: October 2, 2009

BEN H. LOGAN
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