

GIBSON, DUNN & CRUTCHER LLP

Michael A. Rosenthal (MR-7006)
Craig H. Millet (admitted *pro hac vice*)
Matthew K. Kelsey (MK-3137)
200 Park Avenue
New York, New York 10166-0193
Telephone: (212) 351-4000
Facsimile: (212) 351-4035

Attorneys for the Debtors in Possession and Defendant
FALCON GAS STORAGE COMPANY, INC.

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK**

-----X	
IN RE:	: Chapter 11
ARCAPITA BANK B.S.C.(c), <i>et al.</i> ,	: Case No. 12-11076 (SHL)
Debtors.	: Jointly Administered
-----X	

**STATUS REPORT RE: (1) HOPPER *et al.* v. FALCON GAS STORAGE
COMPANY, INC. AND (2) TIDE’S MOTION TO LIFT STAY**

Arcapita Bank B.S.C.(c) (“*Arcapita Bank*”) and its affiliated Debtors (the “*Debtors*”) including Falcon Gas Storage Company, Inc. (“*Falcon*”) hereby submit this Status Report on: (1) the Adversary Action filed by the Hopper Parties against Falcon (the “*Hopper Adversary Proceeding*”), and (2) the related Motion for an Order Lifting the Automatic Stay ... to Allow Continuance of District Court Action filed by Tide (defined below) [Docket No. 279] (the “*Lift Stay Motion*”).

A. RELEVANT BACKGROUND

1. Since July 2005, the stock of Falcon is 80% owned by Arcapita Bank affiliate GA Storage Funding Inc. and 20% owned by John Hopper and other related parties (the “*Hopper Parties*”).

2. As of early 2010, Falcon's primary asset was the stock of NorTex Gas Storage Company, LLC ("**NorTex**"), a company that owns and operates two large underground natural gas storage facilities and associated equipment near Fort Worth, Texas.

3. On March 15, 2010, Falcon entered into a purchase agreement (the "**Purchase Agreement**") to sell 100% of its stock in NorTex (the "**NorTex Sale**") to Tide Natural Gas Storage I, LP and Tide Natural Gas Storage II, LP (together, "**Tide**") for \$515 million.

4. Prior to closing the NorTex Sale, the Hopper Parties filed actions in state court in Texas against Tide, Falcon, certain of its directors and NorTex, seeking damages and to enjoin the NorTex Sale to Tide (collectively, the "**Hopper Litigation**") because Falcon's board of directors had allegedly breached their fiduciary duties by agreeing to a sales price for the NorTex stock purportedly below fair value.

5. The Texas Courts refused to enjoin the sale; however, as a result of the pending Hopper Texas Litigation and as a condition to closing imposed by Tide, Falcon agreed to (1) indemnify Tide for any liability Tide might suffer as a result of the Hopper Litigation, and (2) place approximately \$70 million of the total sales proceeds from the NorTex sale in escrow (the "**Escrowed Money**") with HSBC Bank USA, National Association ("**HSBC**") to be available to satisfy those specific indemnification obligations.

6. After the NorTex Sale closed, on July 27, 2010, Falcon and the Hopper Parties settled the Hopper Litigation in exchange for (1) an immediate cash payment of \$6.5 million and (2) the agreement that, when the Escrowed Money were released to Falcon, Falcon would then pay the Hopper Parties an additional \$8.25 million. Because the settlement of the Hopper Litigation fully resolved the contingent indemnification obligations of Falcon to Tide, the dismissal of the Hopper Litigation resulted in the occurrence of an "**Escrow Breakage Trigger**" under the terms of the Purchase Agreement and Escrow Agreement.

7. Despite the occurrence of an Escrow Breakage Trigger, Tide refused to provide release instructions to HSBC, claimed title to the full amount of the Escrowed Money and filed an action in the Southern District of New York against Falcon, Arcapita Bank and Arcapita Inc., alleging “fraud in the inducement” and intentional misrepresentations in connection with the purchase and sale of securities, among other things. *Tide Natural Gas Storage I, L.P. v. Falcon Gas Storage Co., Inc.*, Case No. 10-cv-05821-KMW (S.D.N.Y.) (the “**District Court Action**”). The District Court Action has been stayed by Arcapita Bank’s and Falcon’s bankruptcy filings.

8. On April 30, 2012, Falcon filed its chapter 11 petition. On May 21, 2012, the Hopper Parties filed the Hopper Adversary Proceeding solely against Falcon and requested a declaration that prepetition the Hopper Parties acquired all right, title and interest of \$8.25 million of the Escrowed Money and, therefore, the \$8.25 million was not property of the Falcon estate. Despite their claim to the same Escrowed Money, neither Tide nor HSBC were named in the complaint.

9. On June 25, 2012, Tide filed Tide’s Motion for an Order Lifting the Automatic Stay Pursuant to 11 U.S.C. Section 362(d) to Allow Continuance of District Court Action [Docket No. 279] (the “**Lift Stay Motion**”) in which it claim titles to the Escrowed Money.

10. At the August 1, 2012, hearing on the Lift Stay Motion, Falcon, Tide and the Hopper Parties agreed to mediate the disputes, and the Court adjourned the hearing on the Lift Stay Motion so that the parties could pursue mediation.

11. The Court set a further status conference on both the Lift Stay Motion and the Hopper Adversary Proceeding for December 13, 2012, both of which were continued to December 18, 2012 by order of the Court.

B. RECENT DEVELOPMENTS

12. On December 4, 2012, counsel and principals for the Hopper Parties, Tide and Falcon met for a full day in New York City before Judge John S. Martin (Ret) (the “*Mediation*”) in an attempt to resolve disputes. Despite the parties’ efforts, the parties were unable to resolve the dispute through the Mediation.

13. Whether the Escrowed Money is property of the Falcon estate is a key threshold issue preventing any real progress toward settlement and is also central to the administration of Falcon’s bankruptcy case. Further, because Tide’s claim is based on “damages arising from the purchase or sale of a security of the debtor or an affiliate of the debtor,” Tide’s claim should be subordinated to the claims of the Hopper Parties and others pursuant to section 510(b) of the Bankruptcy Code. Additionally, HSBC claims to hold a secured claim based on the Escrow Agreement. Tide, HSBC and the Hopper Parties have all filed proofs of claims. The adjudication of these threshold “core” legal issues is necessary before the claims may be resolved and Falcon’s plan may be confirmed.

14. Tide and HSBC are indispensable to the issue pending in the Hopper Adversary Proceeding and, if Tide and HSBC are joined in the Hopper Adversary Proceeding, then all of these threshold core issues may be resolved in a single proceeding already pending before this Court. Accordingly, Falcon has filed a motion for leave to file counter and third-party claims in the Hopper Adversary Proceeding to join Tide and HSBC. The motion is scheduled to be heard by the Court at the next omnibus hearing on January 16, 2013 at 11:00 a.m.

15. The Debtors believe that there are no disputes of material facts and that only the legal effect of those facts is at issue. Therefore, if the counter and third party claims are allowed by the Court, Falcon intends to file a motion for summary judgment when it is proper to do so under the Federal Rules of Bankruptcy Procedure.

C. REQUESTED ACTION

16. Based on the foregoing, Falcon requests that the Court not rule on the Lift Stay Motion or set it for final hearing at this point. Instead, Falcon requests that the Court set a further status conference on *both* the Lift Stay Motion and the Hopper Adversary Proceeding to occur after (1) the Court has first ruled on Falcon's Motion for leave to file a counterclaim and third-party claims, and (2) the Court has adjudicated the core legal issues in response to a Motion for Summary Judgment to be filed by Falcon.

Dated: New York, New York
December 13, 2012

Respectfully submitted,

/s/ Craig H. Millet
Michael A. Rosenthal (MR-7006)
Craig H. Millet (admitted *pro hac vice*)
Matthew K. Kelsey (MK-3137)
GIBSON, DUNN & CRUTCHER LLP
200 Park Avenue
New York, New York 10166-0193
Telephone: (212) 351-4000
Facsimile: (212) 351-4035

ATTORNEYS FOR THE DEBTORS
AND DEBTORS IN POSSESSION