UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re:	:	Chapter 11
MIDWAY GAMES, INC., *et al.*,	:	Case No. 09-10465 (KG)
	:	(Jointly Administered)
Debtors.	:	
	:	**Hearing Date: February 13, 2009 at 2:00 p.m.**

PRELIMINARY LIMITED OBJECTION OF CERTAIN INDIVIDUAL BENEFICIAL HOLDERS OF DEBTOR'S 6% SENIOR CONVERTIBLE NOTES DUE 2025 AND 7.125% SENIOR CONVERTIBLE NOTES DUE 2026 TO DEBTOR'S MOTION FOR ORDER AUTHORIZING USE OF CASH COLLATERAL

Certain firms that manage funds that are the beneficial holders (each, an "Objecting Noteholder")[1] of 7.125% Senior Convertible Notes due 2026 and/or 6% Senior Convertible Notes due 2025 (collectively, the "Notes"), issued by Midway Games, Inc. ("Midway"), a debtor and debtor-in-possession in the above-captioned chapter 11 cases (and, collectively with the other debtors and debtors-in-possession in the above-captioned chapter 11 cases, the "Debtors"), hereby file this Preliminary Objection to the Debtors' motion (the "Motion") for an order authorizing the use of cash that is purportedly the collateral ("Cash Collateral") of Acquisition Holdings Subsidiary I LLC ("AHS" or the "Controlling Shareholder"), and in support thereof, respectfully state as follows:

1. These cases, and the relief requested by the Debtors in the Motion, are tainted by highly unusual transactions by insiders of the Debtors (including AHS, which owns

[1] Each of the following institutions is an Objecting Noteholder: Highbridge International LLC, Tennenbaum Capital Partners, LLC, Magnetar Financial LLC and Lanphier Capital Management, Inc.

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87.2% of the outstanding shares of the Debtors) that, to put it charitably, require significant scrutiny. As a consequence, each Objecting Noteholder respectfully requests that this Court proceed with great caution and skepticism before granting any rights or benefits to the Controlling Shareholder at the expense of these estates and their creditors. Each Objecting Noteholder believes that AHS is substantially oversecured with respect to its alleged secured claim. Consequently, AHS should not receive as adequate protection anything more than replacement liens against the assets of the Debtors that were allegedly pledged as prepetition collateral, solely to the extent of any diminution in the value of its purported interest in such collateral and solely to the extent that the validity or priority of AHS's prepetition indebtedness and/or liens are not successfully challenged.

2. Notwithstanding the forgoing, based upon initial review, it would appear that the package of rights and protections now being offered to AHS goes well beyond what is necessary to adequately protect AHS's interests, if any, in its purported collateral. The rights and protections now offered are excessive and, under the circumstances, inappropriate. They unnecessarily provide the Controlling Shareholder with an undue level of control over the Debtors and their chapter 11 cases. They also effectively undercut the estates' ability to investigate and challenge Controlling Shareholder's purportedly secured claim.

BRIEF BACKGROUND

Redstone Former Ownership

3. Midway's common stock is publicly traded on the New York Stock Exchange (Symbol: MWY). But, notwithstanding Midway's status as a publicly traded company, it was dominated and controlled, until November 28, 2008, by Sumner Redstone ("Redstone"), who owned approximately 87.2% of Midway's outstanding shares. Redstone

owned Midway's shares directly and also indirectly through two companies owned and controlled by him: National Amusements, Inc. ("NAI") and Sumco, Inc. ("Sumco" and, collectively with Redstone and NAI, the "Redstone Parties"). Redstone used his controlling equity stake in Midway to control Midway's board of directors. Indeed, until her resignation in November, 2008, Redstone's daughter, Shari Redstone, chaired Midway's board of directors.

Redstone Loans

4. As recently as February 29, 2008, the Debtors' balance sheet was far less encumbered by debt. The Debtors' long term debt then consisted primarily of (i) Midway's $150 million in aggregate principal obligations under the Notes and (ii) approximately $15 million in loan obligations due under a June 29, 2007 secured loan agreement between the Debtors as borrowers (or guarantors) and Wells Fargo Foothill, Inc. ("Wells Fargo"), as arranger and administrative agent.[2]

5. On February 29, 2008, the Debtors replaced and supplanted the Wells Fargo loan facility with $90 million in loans made under three separate loan facilities issued by the Redstone-owned and controlled NAI, as follows:

a. a $30 million loan facility (consisting of a term loan and a revolving credit facility) secured by substantially all of the Debtors' assets (the "Insider Secured Facility");

b. a $40 million unsecured loan facility to Midway (the "Insider Unsecured Facility"); and

[2] Although only approximately $15 million was drawn under the Wells Fargo credit facility as of February 29, 2008, the facility consisted initially of a $20,000,000 term loan and a $10,000,000 revolving credit facility (the "Wells Fargo Loan"). The facility was not set to mature until 2012.

c. a $20 million unsecured subordinated loan facility to Midway (the "Insider Subordinated Facility" and, collectively with the Insider Secured Loan Facility and the Insider Unsecured Loan Facility, the "Insider Loans").

6. Based upon the Debtors' public filings, it appears that all of the Insider Loans were fully drawn in relatively short order, and, just like that, the Debtors' $15 million in outstanding loan indebtedness to Wells Fargo ballooned to $90 million in outstanding loan indebtedness to the Debtors' controlling stakeholder.

The Redstone-Thomas Transaction

7. After the consummation of these Insider Loans, on November 28, 2008, the Redstone Parties sold for an aggregate purchase price of $100,000 (i) all of their approximate 87% equity stake in the Midway, (ii) a 100% participation interest in the Insider Secured Facility, and (iii) a 100% participation interest in the Insider Unsecured Facility to certain shell companies formed and owned by a very secretive individual named Mark Thomas ("Thomas" and, together with the aforementioned acquisition companies, including AHS, the "Thomas Parties"), a person virtually unknown in the video game industry (the transactions described in (i), (ii) and (iii) above, collectively, the "Redstone-Thomas Transaction").[3]

Irreparable Harm Caused by the Redstone-Thomas Transaction

8. As evidenced by the Thomas Parties' $100,000 purchase price over $70 million of debt and substantially all of the equity of Midway, as of November 28, 2008, the $90 million in Insider Loans had left the Debtors highly leveraged and insolvent. Redstone's orchestration and implementation of the Redstone-Thomas Transaction substantially

[3] The Objecting Noteholders are informed and believe that since the initial transaction, AHS was fully assigned NAI's rights, title and interest in the Secured Loan and Unsecured Loans.

compounded that injury. First and foremost, it triggered a "change in ownership" for the Debtors under Internal Revenue Code § 382. As a consequence of this "change in ownership" it appears that the Debtors immediately and irretrievably lost their ability to utilize tens of millions, and, perhaps, even hundreds of millions, of dollars in favorable tax attributes owned by the Debtors, including, without limitation, net operating loss carry forwards, capital loss carry forwards and built-in losses (collectively, "Tax Attributes").[4] But for the Redstone-Thomas Transaction, the Debtors would have been able to utilize the Tax Attributes in connection with any restructuring or transactions contemplated in these chapter 11 cases. The Redstone-Thomas Transaction also had other immediate adverse consequences, including, among others, the triggering of (i) redemption obligations under each of the indentures (each an "Indenture" and, collectively, "Indentures") governing the Notes that the Debtors were unable to and, in fact, failed to satisfy (resulting in defaults under the Indentures) and (ii) defaults under the Insider Loans, two of which are now owned by the Thomas Parties.

9. No formal disclosures ever have been made regarding the bases for the Redstone-Thomas Transaction. No disclosures ever have been made regarding Thomas or what, if any, relationship Thomas or his companies have with any Redstone Party.[5] To the best of the each Objecting Noteholder's knowledge, little or no meaningful diligence has been done by the Company in connection with the Redstone-Thomas Transaction. But it is safe to assume that

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[4] It is believed that, as a consequence of the Redstone-Thomas Transaction, the Redstone Parties were able to capture the benefit of substantial tax losses that would otherwise have been available to the Debtors.

[5] The Objecting Noteholders are informed and believe that Thomas is a partner of Georgetown Partners, LLC, a small private equity company. Beyond that, they have little information about the Thomas Parties. Requests for additional information from Thomas' attorney were denied.

there must be a connection between Redstone and Thomas given that Redstone essentially gifted his rights in the Debtors to Thomas.

10. Each Objecting Noteholder believes that substantial claims may exist against the Redstone Parties, the Thomas Parties and others arising out of the facts set forth above.

Preliminary Objections to The Debtors' Cash Collateral Request

11. In addition to doing more than simply adequately protecting the Controlling Shareholder against the diminution of collateral, the protections and rights that the Debtors now offer the Controlling Shareholder would permit the Controlling Shareholder excessive control over the Debtors and their cases. Although the Controlling Shareholder is not being asked to, and is not, advancing any new monies to the Debtors, the proposed form of interim cash collateral order (the "Cash Collateral Order") effectively treats the Controlling Shareholder as if it were a debtor-in-possession lender. The Cash Collateral Order places a clear emphasis on insiders getting paid before and, potentially, at the expense of the estates and their creditors. Among other objectionable provisions, the Cash Collateral Order:[6]

a. prohibits and otherwise hamstrings any party's ability to investigate or challenge the Controlling Shareholder's claims by, among other restrictions:

> (i) cross-defaulting the Cash Collateral Order to Section 8.14 of the Insider Secured Credit Facility loan agreement which prohibits the "Company" from contesting or commencing any proceeding against Controlling Shareholder seeking to establish the invalidity or unenforceability of any of the related loan documents or any liability or

[6] Each Objecting Noteholder fully reserves and preserves its right to raise further objections to the Motion at the interim hearing on the Motion and in connection with any final hearing on the Motion.

obligation purported to be created thereunder (Cash Collateral Order ¶ 34(k));[7]

(ii) defaulting the Cash Collateral Order upon commencement of any litigation or proceeding challenging the validity of the Controlling Shareholder's prepetition claims or liens or upon initiation of discovery against the Controlling Shareholder, NAI or the Debtors regarding same that the "Debtors fail to timely take all actions necessary and appropriate to oppose the relief requested through such challenge (Cash Collateral Order ¶ 34(j));"

(iii) limiting to $25,000 the carve-out for investigation of what will be a very fact intensive inquiry of the Insider Secured Facility and the highly unusual circumstances surrounding the creation and transfer of that facility to the Controlling Shareholder (Cash Collateral Order ¶ 30);

(iv) defaulting the Cash Collateral Order in the event that the Committee's professional fees and expenses through May 10, 2009 exceed 15% of the $85,000 and $50,000 budgeted for Committee counsel and financial advisors, respectively (Cash Collateral Order ¶ 34(e));

(v) restricts the post-default Carve-Out for all estate professionals to $150,000 (Cash Collateral Order ¶ 29); and

(vi) subordinates to Controlling Shareholder's superpriority administrative expense claim any professional fees in excess of the amounts set forth in the Budget attached to the Motion (the "Budget")(Cash Collateral Order ¶ 29);

b. contains waivers of the estates' right to surcharge the collateral pursuant to Bankruptcy Code §§ 506(c) and 552(b)(Cash Collateral Order ¶ 36);

c. stipulates to the validity, extent and priority of the claims and liens of the Controlling Shareholder ((Cash Collateral Order ¶ 9);

d. contains the good faith protections of Bankruptcy Code § 363(m) (Cash Collateral Order ¶ 13); and

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[7] The Cash Collateral Order at Paragraphs 18 and 34(r), contains numerous cross-default references making for a very difficult read and interpretation of the Cash Collateral Order. The Cash Collateral Order should stand on its own. There should be no cross-default references back to the underlying loan documents.

e. concedes that the Controlling Shareholder is not in control of the Debtors or their assets (Cash Collateral Order ¶ 40).

12. In addition to the foregoing, the Cash Collateral Order does not appear to contain a definitive statement that the rights and protections being granted to the Controlling Shareholder are completely subject to there being no successful challenge to the validity, priority and extent of the Controlling Shareholder's prepetition claims and liens.

13. As noted above, the Controlling Shareholder has gone to extraordinary lengths to limit the Committee professionals' ability to recover fees and expenses from these estates. This effort is equaled only by the effort that it has undertaken to make sure that the Debtors pay the Controlling Shareholder interest and fees during the 90-day period covered by the Budget. In addition to the Controlling Shareholder's right to receive interest payments of approximately $551,000, the Controlling Shareholder will also be entitled to recover legal fees of $500,000 during the budgeted period. Another $125,000 is budgeted for payment of "Lenders" professionals. The Budget also permits the payment of $1,950,000 in incentive bonuses to key employees to be paid subject to Court approval. These dollars stand in stark contrast to what has been budgeted for Committee professionals.

ARGUMENT

To the Extent the Controlling Shareholder Holds a Valid, Secured Claim, it is Oversecured and Not Entitled to the Adequate Protection Sought By the Debtors

14. Section 363(p)(l) establishes that the Debtors have the burden of proof on the issue of adequate protection. See 11 U.S.C. 363(p)(l); In re Pursuit Athletic Footwear, Inc., 193 B.R. 713, 716 (Bankr. D. Del. 1996); In re Donato, 170 B.R. 247, 254-55 (Bankr. D. N.J. 1994).

15. This burden is, however, satisfied by the existence of an equity cushion. Periodic payments to an oversecured are not required. See In re Continental Airlines, Inc., 146 B.R. 536, 539 (Bankr. D. Del. 1992); Donato, 170 B.R. at 254-55; In re Sharon Steel Corp., 159 B.R. 165, 169 (Bankr. W.D. Pa. 1993) ("The existence of an equity cushion alone may constitute adequate protection."); In re Shaw Indus., Inc., 300 B.R. 861, 865 (Bankr. W.D. Pa. 2003) (same); In re Reading Tube Indus., 72 B.R. 329, 333 (Bankr. E.D. Pa. 1987) ("A debtor may demonstrate adequate protection by proving the existence of... an equity cushion"); see also Dunes, 69 B.R. at 793-95 (where prepetition debt against the subject property was $17.5 million and the collateral was valued at $26.2 million, the equity cushion was more than adequate under the circumstances).

16. Indeed, even where an equity cushion is decreasing in size as a result of the accrual of postpetition interest under Section 506(b), an oversecured creditor is nevertheless not entitled to receive periodic postpetition interest payments in order to preserve the value of this cushion. See In re Delta Resources, Inc., 54 F.3d 722, 728 (11th Cir. 1995). The oversecured creditor's interest in property that must be adequately protected encompasses only any decline in the value of the collateral, "rather than perpetuating the ratio of the collateral to the debt." See id. at 730; see also In re Gallegos Research Group, Corp., 193 B.R. 577, 584 (Bankr. D. Colo. 1995) ("Oversecured creditors may not be entitled to cash payments or postpetition liens because they are adequately protected through the existence of a value cushion.").

17. Each Objecting Noteholder disputes the validity of the liens and security interests alleged by the Controlling Shareholder. Nonetheless, even assuming, for the sake of argument, that those liens and security interests are valid, the Controlling Shareholder is

substantially oversecured. The Company will continue to operate in chapter 11 and will generate replacement receivables in collateral and cash for the Cash Collateral that is to be consumed by the Debtors.

18. The Cash Collateral alone now totals no less than $16.5 million. In addition, the Controlling Shareholder asserts blanket liens against the Debtors' assets. Each Objecting Noteholder believes that the value of the Debtors' ongoing business could range in the tens of millions of dollars. Thus, to the extent the liens securing the Insider Secured Facility are valid, then the total value of the Controlling Shareholder's purported collateral substantially exceeds the amount the Controlling Shareholder's secured claim.

Insider Transactions Should Be Closely Scrutinized

19. "[I]nsider transactions are subjected to rigorous scrutiny and when challenged, the burden is on the insider not only to prove the good faith of a transaction but also to show the inherent fairness from the viewpoints of the Corporation and those with interests therein." Citcorp Venture Capital, Ltd. v. Comm. of Creditors Holding Unsecured Claims (In re Papercraft Corp.), 211 B.R. 813, 823 (W.D. Pa. 1997); see also, In re Lafayette Hotel Partnership, 227 B.R. 445, 454 (S.D.N.Y. 1998) ("[S]ince there is an incentive and opportunity to take advantage, dominant shareholders' and other insiders' loans in a bankruptcy must be subject to rigorous scrutiny."). The adequate protection package now being offered to the Controlling Shareholder should be subjected to the same heightened scrutiny that the Court would apply to any transaction between a debtor and its insider. Here, at the outset of these chapter 11 cases, there has been no meaningful scrutiny by an independent party regarding (i) the Redstone-Thomas Transaction, (ii) the relationship of the parties thereto, (iii) the identity of Thomas, the new 87% shareholder of the Debtors, (iv) the $90 million in insider loans made

within the year preceding the bankruptcy petition date, (v) the fiduciary duties that may have been owed by various insiders to the Debtors and their creditors and (vi) the fiduciary duties that may have been breached as a consequence of the insider transactions.

20. "It is especially clear, when claims in a bankruptcy accrue to the benefit of a corporate officer or director, that the court must reject any claim that would not be fair and equitable to other creditors." Manufacturers Trust Co. v. Becker, 338 U.S. 304, 310 (1949). Here, the Controlling Shareholder and its owner, Thomas, stand to reap an enormous, almost unprecedented windfall from the acquisition of the Insider Secured Facility. If paid in full on the claims arising from the Insider Secured Facility, the Thomas Parties will recover some 30,000% on their $100,000 investment within a matter of a few months. This extraordinary return does not include any additional recovery that the Thomas Parties could realize on the $40 million owed on the Insider Unsecured Facility. The Thomas Parties' return stands in stark contrast to the tens, or potentially even hundreds, of millions of dollars in Tax Attributes that the Redstone-Thomas Transaction may have stolen from these estates.

21. It is inexplicable that the Debtors would agree at the outset of these chapter 11 cases to provide the Controlling Shareholder adequate protection of the extent and nature set forth in the package now proposed. The Redstone-Thomas Transaction has done considerable harm to the Debtors and their estates. As a consequence, the estates may have substantial claims against each of the Redstone Parties and the Thomas Parties and those claims require meaningful investigation.

22. As the claims against the Controlling Shareholder will be at the very heart of these cases, the Controlling Shareholder should not receive at the very outset of these bankruptcy cases stipulations (i) blessing the extent, priority or validity of its claims, (ii)

enabling the Controlling Shareholder to use the Budget to dissuade Committee professionals from fulfilling their duties in these cases by restricting payment of their allowed fees and expenses to *de minimis* amounts, (iii) expressly prohibiting the commencement of any litigation against Controlling Shareholder, (iv) granting superpriority claims and other protections that are not (a) expressly subject to the validity and priority of the prepetition insider indebtedness and (b) void altogether if the validity and priority of that prepetition insider indebtedness is successfully challenged, (v) cross-defaulting the Cash Collateral Order to the Insider Secured Facility.

23. To the extent that the Controlling Shareholder is oversecured, it should not be entitled to draw cash from these estates unless and until such time as the Debtors successfully reorganize or sell substantially all of their assets and the Controlling Shareholder's claims are determined to be valid as to amount and priority.

24. The Controlling Shareholder also should not receive postpetition interest payments from the Debtors because there is no reasonable certainty that such payments can ever be recovered if the Court subsequently determines that the Controlling Shareholder was not, in fact, entitled to receive such payments. The Controlling Shareholder is not an established financial institution. If its sole assets consist of the Insider Loans and the Midway common stock, then it has no meaningful assets from which the estates could recover on a judgment or other ruling against it.

25. It is premature to award the Controlling Shareholder any protection greater than that which is absolutely necessary to ensure that its collateral, if any, is not diminished as a consequence of the Debtors' use of Cash Collateral, ongoing operation of their business or the imposition of the automatic stay.

RESERVATION OF RIGHTS

26. This Preliminary Objection is limited to the grounds stated herein and is without prejudice to the right of any of the Objecting Noteholders to object to any final or other adequate protection relief sought on any ground whatsoever. The Preliminary Objection is also without prejudice to the right of any of the Objecting Noteholders to make written or oral objections to the Debtors' other first day motions set for hearing on February 13, 2009. All such rights are fully reserved and preserved.

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CONCLUSION

WHEREFORE, each Objecting Noteholder respectfully requests that this Court (i) authorize the Debtors' use of Cash Collateral in return for the grant to the Controlling Shareholder of replacement liens against unencumbered assets of the Debtors acquired postpetition, but only to the extent there is true diminution in the value of the Controlling Shareholder's purported collateral as a consequence of the Debtors' use of Cash Collateral, the ongoing operation of the Debtors' businesses and the application of the automatic stay and (ii) that this Court grant such other and further relief as is just and proper.

Dated: February 13, 2009
Wilmington, Delaware

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