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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re	**Chapter 11**
BORDERS GROUP, INC., *et al.*,[1]	**Case No. 11-_____ (___)**
Debtors.	**(Joint Administration Pending)**

DEBTORS' EMERGENCY MOTION FOR ENTRY OF ORDER (I) AUTHORIZING THE DEBTORS TO SELL CERTAIN ASSETS THROUGH STORE CLOSING SALES AND TO ENTER INTO AGENCY AGREEMENT WITH (A) JOINT VENTURE COMPOSED OF HILCO MERCHANT RESOURCES, LLC, SB CAPITAL GROUP, LLC, AND TIGER CAPITAL GROUP, LLC OR (B) OTHER SUCCESSFUL BIDDER AT THE AUCTION, (II) APPROVING STALKING HORSE FEE, (III) AUTHORIZING DEBTORS TO ABANDON UNSOLD PROPERTY, (IV) WAIVING COMPLIANCE WITH CONTRACTUAL STORE CLOSING SALE RESTRICTIONS, (V) EXEMPTING (A) STATE AND LOCAL "FAST PAY" LAWS AND (B) LAWS RESTRICTING STORE CLOSING SALES, AND (VI) GRANTING RELATED RELIEF

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

Borders Group, Inc. ("BGI") and its debtor affiliates, as debtors and debtors in possession (collectively, the "Debtors") submit this emergency motion (the "Motion") for an order (I) authorizing the Debtors to sell certain assets, consisting of merchandise (the "Merchandise") and

[1] The Debtors in these cases, along with the last four digits of each Debtor's federal tax identification number, are: Borders Group, Inc. (4588); Borders International Services, Inc. (5075); Borders, Inc. (4285); Borders Direct, LLC (0084); Borders Properties, Inc. (7978); Borders Online, Inc. (8425); Borders Online, LLC (8996); and BGP (UK) Limited.

owned furniture, fixtures and equipment ("Owned FF&E") located at approximately 200 of their stores (the "Closing Stores") identified in Exhibit A and, at the Debtors' option, up to 75 of 136 potential other stores (the "Put Option Stores")[2], through store closing sales (the "SCSs"), free and clear of all liens, claims or encumbrances and to enter into an Agency Agreement in substantially the form annexed hereto as Exhibit B, with a joint venture composed of Hilco Merchant Resources, LLC, SB Capital Group, LLC and Tiger Capital Group, LLC (the "Stalking Horse Bidder"), or alternatively with the successful bidder at the Auction (the "Successful Bidder"), (II) approving stalking horse fee in connection with the Debtors' auction (the "Auction") to select a liquidator to conduct the SCSs (the "Liquidating Agent"), (III) authorizing Debtors to abandon unsold Merchandise and Owned FF&E after conclusion of the SCSs, (IV) waiving compliance with provisions in the Debtors' agreements restricting store closing sales (the "Contractual Restrictions"), (V) exempting the Debtors from state and local rules, statutes or ordinances restricting store closing sales (the "Applicable Law Restrictions") and from state "fast pay" laws and regulations ("Fast Pay Laws"), and (VI) granting related relief. In support of this Motion, the Debtors respectfully represent as follows:

Preliminary Statement

The Debtors, in consultation with their key constituencies, have identified the immediate steps that are essential to ensuring the Debtors' continued and stabilized viability. Chief among them is the Debtors' need immediately to cut costs by closing highly unprofitable stores and restructuring around a core group of favorably-performing stores. The Debtors have determined

[2] Pursuant to the Agency Agreement, between 15 and 30 days of commencement of the SCSs, the Debtors may designate some or all of the Put Option Stores (the "Put Option") to be included in the SCSs. The Debtors will provide a written notice to the parties listed in the "Notice" section of this Motion and the landlord of each affected store identifying each Put Option Store the Debtors elect to include in the SCSs, which notice shall be given as soon as practicable upon notifying the Liquidating Agent of such election, but at least five (5) days prior to commencement of SCSs at such locations. As set forth below, the Debtors request authority to exercise the Put Option and execute an amendment to the Agency Agreement or a new agency agreement substantially similar to the Agency Agreement without further order of the court.

that closing at least 200 of their 642 stores is absolutely critical to any reorganization process and, to the extent the Debtors cannot negotiate favorable lease concessions from landlords, closing up to 75 more stores may be necessary. Indeed, prior to the Petition Date, the Debtors already implemented a program to close more than 260 stores. Importantly, the agents under the Debtors' proposed two debtor-in-possession financing facilities (the "DIP Facility Agents") agree and fully support the Debtors' proposed SCSs.

The Closing Stores are currently operational and stocked with quickly dwindling Merchandise that the Debtors are not replenishing, as well as furniture, fixtures and equipment. Closing the stores in a quick, efficient manner that maximizes value necessitates an orderly process and the assistance of experienced liquidators. Indeed, closing the stores right away is essential because the Debtors are losing approximately $2 million per week at the Closing Stores, the Debtors have ceased supplying Merchandise to the Closing Stores, and delays in the liquidation process will render the Closing Store's inventory to become less valuable, not only due to lack of replenishment, but also due to changes in the quality of the inventory mix.

As such, prior to the Petition Date, the Debtors and their advisors began contacting all of the nationally-recognized potential liquidators (the only parties that can effectuate a transaction of this magnitude) to solicit interest in bidding on the right to conduct the SCSs. They discussed the SCSs with five liquidator firms. The Debtors and their advisors then ran a process to identify the highest and best bid that would also be willing to serve as a stalking horse and be subject to an auction. The result of that process is the Stalking Horse Bidder's bid (the "Stalking Horse Bid") which would pay the Debtors (i) a guaranteed amount of 73% of the cost value of all Merchandise located at the Closing Stores and which the Debtors estimate will bring at least $131 million and as much as $148 million into the estates, plus (ii) a 50% share of any proceeds

received during the SCSs after a 5% fee and recovery of expenses.[3] Moreover, during the SCSs, the Stalking Horse Bidder would fund store level expenses as well as overhead expenses allocable to Closing Stores relieving the Debtors of such burdens.

The Stalking Horse Bid provides a baseline, knowable amount of recovery from the SCSs. The Stalking Horse Bidder agreed to subject its Stalking Horse Bid to the Auction, conditioned upon certain customary stalking horse protections including, without limitation, a minimal break-up fee of $1,000,000 payable if the Stalking Horse Bidder is not the successful bidder at the Auction (which is less than 1% of the guaranteed consideration). In exchange for this break-up fee, the Debtors were able to negotiate certain other valuable provisions including the sale of the periodicals inventory, cost to retail factors and a broader merchandise threshold. Importantly, the Agency Agreement, including explicitly the break-up fee, has been approved by the Debtors' key constituencies including the Debtors' two proposed DIP Facility Agents.

The Debtors believe it is critical that the winner of the Auction commence the SCSs by no later than Saturday, February 19, 2011. In addition to the enormous cash drain that the Closing Stores are on the Debtors' limited resources, the Presidents' Day long weekend is a valuable opportunity and, because every day that passes causes the Closing Stores to suffer dwindling inventory that the Debtors cannot replenish, each bidder would revise its offer downward if the SCSs do not commence immediately. Indeed, based on discussions with liquidators, the Debtors believe that delaying the sales until after Presidents' Day weekend will lower the sale price by as much as 1-2% off the guaranty percentage paid by the liquidators, equal to approximately $2 million to $4 million of value. Given these deadlines and the continued liquidity drain the Debtors suffer each day that the Closing Stores stay open -- which

[3] Proceeds of Merchandise will be used in accordance with the Debtors' cash collateral authority sought simultaneously herewith.

costs the Debtors approximately $2 million of losses per week -- the Debtors need to proceed quickly and shall conduct a final auction on Wednesday, February 16, 2011. The Debtors, therefore, respectfully request authority to enter into Agency Agreement with the Stalking Horse Bidder or with the Successful Bidder at the Auction.

Finally, as is customarily granted where Debtors effectuate store closing sales, the Debtors request certain related relief to obviate any contractual or state or local laws that could inhibit the SCSs. For the reasons set forth below, the Debtors should be authorized to engage in the SCSs as set forth herein.

Jurisdiction

1. This Court has subject matter jurisdiction to consider and determine this matter pursuant to 28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b). Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

Relief Requested

2. By this Motion, the Debtors seek entry of an order pursuant to sections 105(a), 363(b) and 554(a) of the Bankruptcy Code in substantially the form annexed hereto as Exhibit C, (i) approving stalking horse protections, (ii) authorizing the Debtors to sell the Merchandise and Owned FF&E at the Closing Stores through the SCSs free and clear of all liens, claims and encumbrances, (iii) authorizing the Debtors to enter into the Agency Agreement with the Stalking Horse Bidder or with the Successful Bidder at the Auction, (iv) authorizing the Debtors to abandon unsold Merchandise or Owned FF&E at the Closing Stores following conclusion of the SCSs, (v) waiving compliance with Contractual Restrictions, (vi) exempting Applicable Laws Restrictions and Fast Pay Laws, and (vii) granting related relief.

Background

3. On the date hereof (the "Commencement Date" or the "Petition Date"), each of the Debtors commenced a voluntary case under chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code"). The Debtors continue to operate their business and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. Contemporaneously herewith, the Debtors filed a motion seeking joint administration of their chapter 11 cases pursuant to Rule 1015(b) of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

4. The Debtors are a leading operator of book, music and movie superstores and mall-based bookstores. At January 29, 2011, the Debtors operated 642 stores, under the Borders, Waldenbooks, Borders Express and Borders Outlet names, as well as Borders-branded airport stores in the United States, of which 639 stores are located in the United States and 3 in Puerto Rico. Two of Borders' flagship stores (along with other less prominent stores) are located in Manhattan. In addition, the Debtors operate a proprietary e-commerce web site, www.Borders.com, launched in May 2008, which includes both in-store and online e-commerce components.

5. As of February 11, 2011, the Debtors employed a total of approximately 6,100 full-time employees, approximately 11,400 part-time employees, and approximately 600 contingent employees (who are required to work one shift per month, and usually do so at special events), all of whom are located in the United States and Puerto Rico.

6. For the fiscal year ended January 29, 2011, the Debtors recorded net sales of approximately $2.3 billion. As of December 25, 2010, the Debtors had incurred net year-to-date losses of approximately $168.2 million.

7. Additional information regarding the Debtors' business, capital structure, and the circumstances leading to these chapter 11 cases is contained in the *Declaration of Scott Henry Pursuant to Local Bankruptcy Rule 1007-2 in Support of First Day Motions* (the "First Day Decl.") filed contemporaneously herewith. Additional information regarding the Debtors' solicitation efforts that resulted in the Stalking Horse Bid is contained in the *Declaration of Holly Felder Etlin in Support of Store Closing Sale Motion* (the "Etlin Decl.") also filed contemporaneously herewith.

The Closing Stores

8. Historically, the Debtors, in the ordinary course of their business, have continually reviewed their store portfolio to close underperforming or otherwise unprofitable stores. The Debtors have endeavored to renegotiate leases and obtain landlord concessions wherever possible, and particularly in their least profitable stores. Where the Debtors cannot obtain necessary rent concessions at unprofitable stores, or if a lease expired on its own terms and the landlord desired to retake the premises, the Debtors have regularly closed stores and conducted closing sales for the efficient self-liquidation of inventory and Owned FF&E.

9. In some instances, when conducting such closing sales, the Debtors have retained liquidation firms to consult and advise the Debtors regarding the liquidation process. For example, in early 2009, the Debtors retained Hilco Merchant Resources, LLC ("Hilco") to consult with regard to several store closing sales. Currently Hilco acts as consultant with respect to nineteen (19) closing sales the Debtors commenced pre-petition. In this regard, conducting store closing sales with the assistance of liquidators (and in particular Hilco) is part of the Debtors' ordinary course operations. Hilco's consulting services are provided pursuant to certain consulting agreements annexed hereto as Exhibit D (the "Hilco Consulting Agreements"). As

discussed below, the Debtors herein seek to assume the Hilco Consulting Agreements (in addition to approval of the Agency Agreement).

10. Prior to the Petition Date, the Debtors, in consultation with their advisors and their key constituents, concluded that it was in the best interests of the Debtors and their stakeholders to close and liquidate the inventory at the Closing Stores because those stores could not sustain continued operations and were not saleable as going concerns. First Day Decl. at ¶ 105; Etlin Decl. at ¶ 7. The Debtors, with input from financial advisors, determined that SCSs conducted by one or more experienced and reputable liquidator(s) would achieve the maximum values for the assets located in the Closing Stores and would minimize administrative expenses. First Day Decl. at ¶ 105; Etlin Decl. at ¶ 8. Indeed, given the breadth of the SCSs, it would be impossible for the Debtors to self-administer the SCSs without outside liquidator assistance. Etlin Decl. at ¶ 8.

11. The Debtors also determined that it is critical to commence the SCSs as soon as possible for several important reasons, including the following:

- First, the Closing Stores are operating at a significant loss and represent a drain on the Debtors' liquidity. Indeed, the Debtors estimate that each week the Closing Stores remain open causes the Debtors to suffer approximately $2 million of losses. Thus, the sooner the Debtors can liquidate the assets at the Closing Stores and reject the corresponding leases, the sooner and better the Debtors can mitigate the strain on their liquidity.

- Second, the Debtors have ceased supplying the Closing Stores, and delays in the liquidation process could cause portions of the Closing Stores' inventory to become less valuable, not only due to lack of replenishment, but also due to changes in the quality of the inventory mix due to ongoing sales, thus, of diminished value.

- Third, the guaranteed amount liquidators are willing to pay to conduct the SCSs would drop substantially if the sales cannot commence during Presidents' Day weekend. Indeed, based on discussions with liquidators, the Debtors believe that delaying the sales until after Presidents' Day weekend will lower the sale price by as much as 1-2% of the Guaranty Percentage, resulting in approximately $2 million to $4 million less in proceeds.

- Fourth, continuing to operate the Closing Stores would distract the Debtors' management team from properly focusing their attention and resource on operating the Chapter 11 cases and restructuring around a core group of profitable stores.

Etlin Decl. at ¶ 27.

The Solicitation Process

12. Prior to the Petition Date, the Debtors and their advisors engaged in a strategic process to solicit bids to select the stalking horse and conduct the SCSs. *Id.* at ¶¶ 9-22.

13. On February 3, 2011, the Debtors through their advisors began contacting the nation's largest liquidation firms to gauge interest in a process to solicit bids for SCSs. First Day Decl. at ¶ 106; Etlin Decl. at ¶ 9. At that time, the Debtors' advisors informally contacted representatives of each of those liquidation firms and learned shortly thereafter -- as is customary of transactions of this size -- that the nation's largest liquidation firms would form two groups for purposes of bidding on the SCSs. First Day Decl. at ¶ 106; Etlin Decl. at ¶ 9. One group consists of Great American Group LLC and Gordon Brothers Retail Partners LLC (collectively, the "GB Group") and the other consists of Hilco Merchant Resources, LLC, Tiger Capital, and SB Capital Group (collectively, the "Hilco Group"). First Day Decl. at ¶ 106; Etlin Decl. at ¶ 10.[4] Based on those discussions, and the small universe of liquidation firms that could handle a liquidation of this size and breadth and the limited time such firms require for diligence, the Debtors' advisors concluded that a quick solicitation process would provide optimal returns, while ensuring adequate notice to all possible participants. First Day Decl. at ¶ 106.

14. On February 7, 2011, the Debtors through their advisors transmitted bid solicitation packages (the "Bid Solicitation Packages") containing: (a) a form non-disclosure agreement, and (b) a bid solicitation letter (the "Bid Solicitation Letter") informing the parties of

[4] While the Debtors were contacted by two other potential bidders that executed confidentiality agreements with the Debtors, they never participated in the stalking horse bidding. Etlin Decl. at ¶ 13.

the Debtors' intentions to conduct SCSs and setting forth clear procedures for parties to request more information and to submit bids. First Day Decl. at ¶ 107; Etlin Delc. at ¶ 11., Ex. 1. The Bid Solicitation Letter specifically instructed interested parties to complete the non-disclosure agreement, at which time the parties would be provided diligence materials and a draft form agency agreement. *Id.* The Bid Solicitation Packages were transmitted to the GB Group and the Hilco Group. First Day Decl. at ¶ 107; Etlin Delc. at ¶ 12.

15. On February 8 and 9, 2011, the entities in the GB Group and the Hilco Group signed non-disclosure agreements. First Day Decl. at ¶ 108; Etlin Delc. at ¶ 13. Also on February 8, 2011, the Debtors' advisors provided each of those parties copies of a draft form agency agreement (which is customary for transactions of this type) and began providing them diligence materials, including (a) detailed information regarding the Closing Stores including, as to each Closing Store: (i) the address, (ii) a schedule of Occupancy Expenses (as defined in the Agency Agreement) to be paid by the liquidators, (iii) 2010 P&Ls, (iv) historical weekly sales by SKU, and (v) inventory by SKU; (b) a summary of the Debtors' perpetual inventory; (c) promotional calendars for the first and second quarters of 2011; (d) a detailed listing of certain inventory contained in the debtors distribution center to be included in the sale; and (e) employee manuals and benefits plan summary (collectively, the "Diligence Information"). First Day Decl. at ¶ 107; Etlin Delc. at ¶ 14. The Debtors and their advisors held numerous calls and discussions with representatives of both groups.

16. The Bid Solicitation Letter originally set February 10, 2011 as the deadline for parties to submit bids (consisting of a marked-up agency agreement reflecting proposed deal terms). Etlin Decl. at ¶ 15. On February 9, 2011, at the request of one of the groups, the

Debtors' advisors informed the GB Group and the Hilco Group that the Debtors would extend the bid deadline to February 11, 2011. *Id.*

17. On February 11, 2011, the GB Group and the Hilco Group each submitted bids. *Id.* at ¶ 17. The Debtors then contacted each group to discuss the terms of each bid and proceeded to engage in extensive negotiations as to specific terms related to their offers. *Id.* In particular, the Debtors and their advisors had numerous discussions with both groups regarding critical economic issues like the merchandise threshold, cost factor, and general economics of each bid. *Id.* The Debtors also provided additional diligence to the bidders including with respect to the Debtors' roll forward inventory. *Id.*

18. All day on Saturday, February 12 and in the morning of Sunday, February 13, 2011, the Debtors had frequent discussions with each group in an effort to improve the terms of the bids. *Id.* at ¶ 18. The Debtors' advisors estimate they spoke to each bidder group at least four times during this period. *Id.* The discussions were successful in improving both bids. *Id.* For example, after extensive negotiations, the Hilco Group agreed to reduce its merchandise threshold requirement from $184 million to $180 million, and increased its guaranteed amount from 71% of cost to 73%. *Id.*

19. By mid-day on Sunday, February 13, 2011, the Hilco Group emerged as the party with the higher and better bid. *Id.* at ¶ 19. Compared to the GB Group's bid, the Hilco Group's bid provides a guaranty percentage that is 2% higher, which equates to almost $4M more in proceeds for the Debtors. *Id.*. In addition, the Hilco Group's terms on inventory thresholds, cost-to-retail adjustments and expense reimbursement are more favorable to the Debtors, decreasing the Debtors' potential exposure to excess expenses or inventory adjustments. *Id.* The Debtors thus selected the bid proposed by the joint venture composed of Hilco Merchant

Resources, LLC, SB Capital Group, and Tiger Capital Group, LLC Hilco Group's bid as the Stalking Horse Bid. First Day Decl. at ¶ 111; Etlin Decl. at ¶ 19. The Hilco Group agreed to have their bid subject to an auction on the condition they be afforded a break-up fee if their bid was not the winning bid at the Auction. Etlin Decl. at ¶ 19.

20. The Stalking Horse Bid would pay the Debtors (i) a guaranteed amount of 73% of the cost value of all Merchandise located at the Closing Stores and which the Debtors estimate will bring at least $131 million and as much as $148 million into the estates, plus (ii) a 50% share of any proceeds received during the SCSs after a 5% fee and recovery of expenses. *Id.* at ¶ 20.

21. On February 14, 2011, the Debtors informed the GB Group that the Hilco Group's bid was selected as the Stalking Horse Bid. *Id.* at ¶ 21. The Debtors' advisors then worked with the Hilco Group and its professionals to revise the draft form agency agreement, which resulted in the Agency Agreement executed by the Debtors on February 15, 2011 and which is subject to Court approval. First Day Decl. at ¶ 111; Etlin Decl. at ¶ 21.

22. The Agency Agreement has been shared with the Debtors' key constituencies including (a) certain large publishers holding a substantial portion of the Debtors' trade debts that individually decided to jointly retain the same professionals at Lowenstein Sandler and Alvarez & Marsal and (b) the Debtors' two proposed DIP Facility Agents. Each group provided comments to the agreement, which the Debtors and their advisors considered carefully and, where acceptable, revised the agreement to reflect. Moreover, each of those constituencies has been fully informed of the Debtors' solicitation efforts and the economics of the agency agreement and, indeed, representatives of each constituency expressed satisfaction with the amount of consideration the Debtors and their bankruptcy estates will receive under the agency

agreement and its terms. Finally, counsel representing many of the Debtors' most significant landlords was also consulted regarding landlord specific issues reflected in the sale guidelines.

Bases for Relief

23. Section 363(b) of the Bankruptcy Code provides, in relevant part, that "[t]he trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate . . ." *See* 11 U.S.C. § 363(b)(1); *see also In re Ames Dept. Stores, Inc.* (Ames I), 136 B.R. 357, 359 (Bankr. S.D.N.Y. 1992) (noting that "going-out-of-business" sales are governed by section 363(b)); Fed. R. Bankr. P. 6004(f)(1) ("All sales not in the ordinary course of business may be by private sale or by public auction."). Moreover, section 105(a) of the Bankruptcy Code provides that "[t]he Court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a).

24. The decision to sell assets outside the ordinary course of business is based upon the sound business judgment of the debtor. *See, e.g.*, *In re Chateaugay Corp.*, 973 F.2d 141, 145 (2d Cir. 1992); *Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.2d 1063, 1071 (2d Cir. 1983) ("The rule we adopt requires that a judge determining a § 363(b) application expressly find from the evidence presented before him at the hearing a good business reason to grant such an application."); see *also Official Comm. of Subordinated Bondholders v. Integrated Res., Inc. (In re Integrated Res., Inc.)*, 147 B.R. 650, 656 (S.D.N.Y. 1992) (stating "the business judgment rule is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action was in the best interests of the company," and has continued applicability in bankruptcy) (quoting *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985)), *appeal dismissed*, 3 F.3d 49 (2d Cir. 1993).

I. AUTHORITY TO SELL ASSETS THROUGH STORE CLOSING SALES

25. The Debtors, exercising their business judgment and in consultation with their advisors and key constituents, have determined that it is in the best interests of their estates and creditors to conduct SCSs at the Closing Stores immediately. Based on applicable precedent, the Court should authorize the Debtors to do so as set forth herein to stem the losses resulting from continued operations at the Closing Stores and to enable the estates to recover as much as possible from the such liquidations.

A. Approval of Store Closing Sales Under Section 363 is Warranted

26. Prior to the Petition Date, the Debtors extensively reviewed the performance of their retail store locations, including a review of the profitability of each store on a stand-alone basis. As a result, during 2009 the Debtors closed 219 stores, primarily Waldenbooks Specialty Retail stores, and in 2010 the Debtors closed and additional 45 retail stores.

27. The Debtors also have identified the Closing Stores as underperforming and/or unprofitable stores that should be closed as part of the Debtors' overall business strategy. The Debtors further determined that conducting SCSs prior to their closing would provide the best opportunity for maximizing the value of the inventory located within those stores. The Debtors believe that any attempt to restore the profitability of the Closing Stores would not only prove to be futile, but perhaps more significantly, would distract management from critical efforts to restructure the Debtors' ongoing operations and burden the estates with additional carrying costs.

28. The Closing Stores are operating at a significant loss and represent a drain on the Debtors' liquidity. Indeed, the Debtors estimate that each week the Closing Stores remain open causes the Debtors to suffer approximately $2 million of additional losses. Thus, the sooner the Debtors can liquidate the assets at the Closing Stores and reject the corresponding leases, the sooner and better the Debtors can mitigate the strain on their liquidity. Moreover, the Debtors

have ceased supplying the Closing Stores, and delays in the liquidation process could cause portions of the Closing Stores' inventory to become less valuable, not only due to lack of replenishment, but also due to changes in the quality of the inventory mix due to ongoing sales, thus, of diminished value. The realization of fair value for the assets as promptly as possible will inure to the benefit of all parties' in interest. Thus, time is of the essence to preserve and maximize the value of the Debtors' assets before the Merchandise declines in value, and to reduce ongoing administrative expenses. Therefore, the Debtors propose to conduct SCSs at the Closing Stores, by and through the Liquidating Agent, immediately upon entry of an order by this Court granting the relief requested in this Motion.

29. Store closing or liquidation sales are a routine occurrence in chapter 11 cases involving retail debtors. *See Ames Dept. Stores, Inc.* (Ames I), 136 B.R. at 359) (holding that "going-out-of-business" sales are an important part of "overriding federal policy requiring [a] Debtor to maximize estate assets"); *see also In re Ames Dept. Stores, Inc.* (Ames II), Ch 11 Case No. 01-42217 (REG) (Bankr. S.D.N.Y. Aug. 20, 2001) (approving store closing sales and agency agreement on first day). Bankruptcy Courts have approved similar requests by debtors to conduct store closing sales, finding the debtors' requested relief consistent with applicable provisions of the Bankruptcy Code. *See, e.g.*, *In re Blockbuster Inc.*, Ch. 11 Case No. 10-14997 (BRL) (Bankr. S.D.N.Y. Jan. 20, 2011) (authorizing debtors to continue self-administered going out of business sales); *In re Movie Gallery, Inc.*, Ch. 11 Case No. 10-30696 (Bankr. E.D. Va. Feb. 4, 2010); *In re Finlay Enters., Inc.*, Ch. 11 Case No. 09-14873 (JMP) (Bankr. S.D.N.Y. Sept. 25, 2009); *In re Goody's LLC*, Ch. 11 Case No. 09-10124 (Bankr. D. Del. Jan. 21, 2009) (authorizing debtors' assumption of prepetition agency agreement and to conduct store closing sales); *In re Circuit City Stores, Inc.*, Ch. 11 Case No. 08-35653 (KRH) (Bankr. E.D. Va. Nov.

10, 2008); *In re Linens Holding Co.,* Ch 11 Case No. 08-10832 (Bankr. D. Del. May 30, 2008) (approving store closing sales of certain closing locations), (Bankr. Del. Oct. 16, 2008) (approving store closing sales for all remaining store locations); *In re Sharper Image Corp.*, Ch. 11 Case No. 08-10322 (Bankr. D. Del. Mar. 14, 2008); *In re Steve & Barry's Manhattan LLC,* Ch. 11 Case No. 08-12579 (ALG) (Bankr. S.D.N.Y. Aug. 22, 2008).

B. To the Extent Applicable, Assets Should be Sold Free and Clear of Liens, Claims and Encumbrances

30. The Debtors request approval to sell assets subject to the Agency Agreement on a final "as is" basis, free and clear of any and all liens, claims and encumbrances in accordance with section 363(f) of the Bankruptcy Code. A debtor in possession may sell property under sections 363(b) and 363(f) "free and clear of any interest in such property of an entity other than the estate" if anyone of the following conditions is satisfied:

- applicable non-bankruptcy law permits sale of such property free and clear of such interest;
- such entity consents;
- such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
- such interest is a *bona fide* dispute; or
- such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

11 U.S.C. § 363(f)(1)-(5); *Citicorp Homeowners Servs., Inc. v. Elliot (In re Elliot)*, 94 B.R. 343, 345 (E.D. Pa. 1988) (noting that since Section 363(f) is written in the disjunctive, the court may approve a sale free and clear if anyone subsection is met).

31. As an initial matter, the Debtors' two proposed DIP Facility Agents have consented to the SCSs and, particularly, to the sale of the Merchandise and Owned FF&E free and clear of their liens, claims and encumbrances, with all such obligations to attach to the

proceeds of the SCSs with the same validity and priority that such liens, claims, encumbrances, or interests had against the assets.

32. With respect to any other party asserting a lien, claim, or encumbrance against the Merchandise or the Owned FF&E, the Debtors anticipate that they will be able to satisfy one or more of the conditions set forth in section 363(f). In connection with the sale of the assets pursuant to the terms and conditions of the Agency Agreement, the Debtors propose that any liens, claims, and encumbrances asserted against the Merchandise be transferred to and attach to the amounts payable to the Debtors under the Agency Agreement, in the same order of priority and subject to the rights, claims, defenses, and objections, if any, of all parties with respect thereto.

33. Accordingly, the Debtors submit that, to the extent applicable, the Court should authorize the Debtors to sell the Merchandise and other SCSs assets free and clear of any liens, claims, encumbrances, or other interests that may exist, with any of the same to be transferred and attached to the net proceeds of the sale, with the same validity and priority that such liens, claims, encumbrances, or interests had against the assets.

C. The Auction Process

34. In addition to the extensive discussions and negotiations that the Debtors already conducted to arrive at the Stalking Horse Bid, the Debtors have determined, in an exercise of their business judgment that conducting a final auction to select the Liquidating Agent for the SCSs is in the best interests of their estates. As such, the Debtors will conduct the Auction on Wednesday, February 16, 2011 beginning at 10:00 AM (EST) at the offices of Kasowitz, Benson, Torres & Friedman LLP, 1633 Broadway, New York, New York, 10019. The Debtors are providing notice of the Auction to all key constituencies.

35. The Debtors and their advisors, in consultation with their key constituents, will establish the terms and conditions of the Auction, which will include that (a) the initial overbid must exceeds the Stalking Horse Bid by at least the sum of (i) 0.5% of the Cost Value of Merchandise (as defined in the Agency Agreement) plus (ii) the Break-Up Fee (defined below), (b) any subsequent overbid must exceed the prior bid by at least 0.25% of the Cost Value of Merchandise, and (c) that any successful bidder must execute an agency agreement in substantially the form of the Agency Agreement, with only the terms and form of consideration changed. The successful bidder at the Auction will be deemed the Liquidating Agent.

36. The Debtors submit that the forgoing procedures are fair, transparent and will derive the highest and best bids for the Closing Store assets. The Debtors also believe that going forward on an expedited basis will in no way impair recoveries because (a) all of the nationally-recognized potential liquidators (the only parties that can effectuate a transaction of this magnitude) have been directly involved in the process, (b) those parties were provided all necessary diligence and have expertise in quickly formulating and executing such bids, (c) the solicitation process run by the Debtors' advisors was routine for such situations and the form of agency agreement used is mostly customary, and (d) the Debtors' proposed DIP Facility Agent as well as representatives of unsecured creditor constituencies have had direct input in the process. Etlin Decl. at ¶ 28.

37. Moreover, the Debtors believe that the procedures used provide sufficient notice and opportunity to participate as the key parties already have been provided diligence materials and have been given access to the Debtors and the Closing Stores. Critically, the Debtors' key constituents including the Debtors' two proposed DIP Facility Agents have consented to and support the manner in which the Debtors are proceeding.

II. AUTHORITY TO RETAIN THE STALKING HORSE BIDDER OR THE SUCCESSFUL BIDDER AT THE AUCTION AS LIQUIDATING AGENT

A. Need to Retain a Liquidator

38. The Debtors seek authority to dispose of the assets under the terms of the Agency Agreement with the Liquidating Agent selected at the Auction. Proceeding in this fashion will provide the Debtors with several benefits. First, allowing a professional liquidator to liquidate the assets will enable the Debtors to maximize sale proceeds while minimizing distraction from the restructuring effort. Second, it is more cost effective for the Debtors to allow a Liquidation Agent to conduct the SCSs than to conduct such sales on their own because, among other reasons, the Liquidating Agent will reimburse the Debtors for expenses of the SCSs. Moreover, liquidation agents generally have extensive knowledge, expertise and experience in conducting store closing sales. Therefore, the Debtors' decision to retain a liquidating agent to conduct the SCSs is an exercise of sound business judgment.

39. The Debtors submit, and will demonstrate at the hearing on this Motion, that any such prevailing bidder is entitled to the protections of section 363(m) of the Bankruptcy Code, as the Agency Agreement is the product of a good faith, arm's-length transaction.

40. Pursuant to the arrangement proposed herein, the Liquidating Agent will have the right to use the Closing Stores and the Debtors' related services, FF&E and other assets located in the Closing Stores in conducting the SCSs. In addition, pursuant to the Agency Agreement, the Liquidating Agent will also have a right to establish and implement advertising, signage and promotion programs consistent with "store closing" or similar theme (but not "going out business" or any similar theme). As mentioned above, counsel representing many of the Debtors' most significant landlords was consulted regarding landlord specific issues reflected in the sale guidelines governing the conduct of the SCSs.

41. This Court, as well as others, in numerous chapter 11 cases, have approved the similar use of a liquidator to conduct store closing sales. *See, e.g., In re Goody's LLC*, Ch. 11 Case No. 09-10124 (Bankr. D. Del. Jan. 21, 2009); *In re Circuit City Stores, Inc.*, Ch. 11 Case No. 08-35653 (KRH) (Bankr. E.D. Va. Nov. 10, 2008); *In re Linens Holding Co.*, Ch. 11 Case No. 08-10832 (Bankr. Del. May 30, 2008 and Oct. 16, 2008) (order, respectively, approving liquidator's store closing sales of certain closing locations and approving liquidator's store closing sales for all remaining store locations); *In re Sharper Image Corp.*, Ch. 11 Case No. 08-10322 (Bankr. D. Del. Mar. 14, 2008); *In re Steve & Barry's Manhattan LLC,* Ch. 11 Case No. 08-12579 (ALG) (Bankr. S.D.N.Y. Aug. 22, 2008).

B. The Agency Agreement

42. The Debtors respectfully request approval of the Agency Agreement with the Stalking Horse Bidder or, in the event another bidder is the Successful Bidder at the Auction, then the Debtors request authority to enter into an agency agreement with such bidder containing materially the same provisions as the Agency Agreement.

43. Regardless of who is the Liquidating Agent, the salient terms of the Agency Agreement (outlined below) will not change, other than possible economic improvements favorable to the Debtors and their estates. Therefore, inasmuch as adequate notice of the material terms of the Agency Agreement is given by this Motion and already has been provided to the major constituents -- and as any other bids will only be more favorable to the Debtors and their estates -- the Debtors submit that no further hearing or notice should be necessary with respect to approval of either the Agency Agreement or any other, materially similar agency agreement with the Successful Bidder.

44. Although the Debtors respectfully refer the Court to the Agency Agreement in its entirety, certain of the material terms are set forth below[5]:

- Assets. All Merchandise at the Closing Stores as of the Sale Commencement Date plus Merchandise located in the distribution center as of the Sale Commencement date that is received in the Closing Stores as of the Inventory Receipt Deadline. Initially, the Closing Stores will consist of the 200 stores identified in Exhibit A hereto. At the Debtors' option, exercisable within 15 and 30 days of the Sale Commencement Date, up to 75 of 136 additional stores may be added to the Closing Stores.

- Guaranteed Amount. As a guaranty of the Liquidating Agent's performance under the Agency Agreement, the Liquidating Agent will guarantee the Debtors' receipt of a certain percentage of the Cost Value of the Merchandise included in the sale (the "Guaranty Percentage"). **The Stalking Horse Bidder has agreed to a Guaranty Percentage of 73%, which the Debtors estimate will bring at least $131 million and as much as $148 million into the estates.**

- Recovery Amount. To the extent that the proceeds realized from the sale of Merchandise exceed (i) the Guaranteed Amount and (ii) the expenses of the sale (discussed *infra*) (collectively, (the "Sharing Threshold"), the remaining proceeds will be allocated first to pay the Agent's Fee and next to be shared between the Debtors and the Liquidating Agent. **The Stalking Horse Bidder has agreed to an Agent's Fee of 5% of the Cost Value of Merchandise. The Stalking Horse Bidder also has agreed that proceeds in excess of the Sharing Threshold and the Agent's Fee will be shared 50% to the Debtors and 50% to the Stalking Horse Bidder.**

- Sale of Owned FF&E. The Liquidating Agent will sell the FF&E located at the Closing Stores (except excluded items identified by the Debtors, with lender consent), in exchange for providing the Liquidating Agent a fee, calculated as a percentage of the net proceeds from such sales. **The Stalking Horse Bidder has agreed to a fee of 20%.**

- Payment Timing. On the first business day following entry of an Order approving the SCSs, the Liquidating Agent will wire to the Debtors an amount certain as payment of a portion of the Guaranteed Amount (the "Guaranteed Amount Deposit"). **The Stalking Horse Bidder has agreed to pay 80% of the Guaranteed Amount as the Guaranteed Amount Deposit.** The Liquidating Agent will pay the remaining Guaranteed Amount and all other amounts due to the Debtors, pursuant to the timing in the Agency Agreement, as and when the parties reconcile the Guaranteed Amount.

[5] Capitalized terms used in this summary shall have the meanings ascribed to them in the Agency Agreement. This summary of the Agency Agreement is for summary purposes only and is qualified in its entirety by the terms and provision of the Agency agreement.

- Expenses of Sale. From the Sale Commencement Date through and including the Sale Termination Date, the Liquidating Agent will be unconditionally responsible for all Expenses enumerated in Section 4.1 of the Agency Agreement (including, without limitation, Occupancy Expenses, Payroll, benefits for Retained Employees, Agent's on-site supervision related costs, signs and banners, promotional costs, Sale supplies, telephone, postage/overnight or delivery/courier charges, utility charges, credit card and bank fees, costs related to moving, transferring or consolidating merchandise between Closing Stores, insurance costs, trash removal and cleaning costs, security and building alarm costs, cost of capital and letter of credit fees, and any Retention Bonuses for Retained Employees and an agreed percentage of the costs of the physical inventory taking), incurred in conducting the Sale during the Sale Term, which Expenses may be funded and paid from Proceeds of the Sale to the extent available, or directly by the Liquidating Agent.

- Employees. The Liquidating Agent shall have the right to use the Debtors' store-level employees during the Sale Term and will reimburse the Debtors for actual payroll, and Employee Benefits up to an agreed upon cap based upon a percentage of the aggregate base payroll. The Liquidating Agent may also elect to pay, as an expense, a retention bonus to certain retained employees. The employees will remain the Debtors' employees at all times.

- Cost Value / Inventory Taking. The Cost Value of Merchandise is the average landed actual cost for an item of Merchandise, as reflected in the Debtors' perpetual inventory file as of the Sale Commencement Date. The Debtors and Liquidating Agent will jointly conduct a physical inventory taking at forty (40) of the Closing Stores, for purposes of testing the Cost Value of the Merchandise in the Closing Stores. The Agency Agreement provides a procedure for adjusting the Cost Value used in the sale, based on results of the inventory taking.

- Sale Term. The Liquidating Agent has the right to conduct the Store Closing Sales commencing the day after entry of the Order approving the SCSs. **The Stalking Horse Bidder has conditioned its agreement, however, on entry of such Order by February 18, 2011**. The SCSs will continue until April 30, 2011; provided, however, that under certain circumstances, the Liquidating Agent may terminate the sales at certain Closing Stores prior to such date.

- Sale Guidelines. The SCSs shall be conducted in accordance with the Sale Guidelines attached to the Agency Agreement as Exhibit 8.1(a). The Liquidating Agent shall be authorized to advertise and promote the sales as a "store closing" or similar themed sale (but not "going out business" or any similar theme).

- Merchandise Returns/Gift Cards/Other Programs. Although sales of all items of Merchandise sold during the Sale Term shall be a "final sale", the Liquidating Agent will accept returns of Merchandise sold prior to the Sale Commencement Date provided that such return is accompanied by the original Store register receipt and is otherwise in compliance with Debtors' return and price adjustment

policy in effect as of the date such item was purchased. During the Sale Term, the Liquidating Agent will accept the Debtors' gift cards, Borders Rewards Plus Loyalty Program discounts, and Merchandise credits issued by the Debtors prior to the Sale Commencement Date, but solely to the extent that the Court authorizes the Debtors to honor such items in connection with the Debtors' customer programs motion, filed concurrently herewith. The Debtors shall reimburse the Liquidation Agent for such amounts during the weekly sale reconciliation. The Liquidating Agent shall not honor any employee discounts.

- Letter of Credit / Security Interests. To secure its obligations under the Agency Agreement, the Liquidating Agent will post a letter of credit for the benefit of the Debtors. The Liquidating Agent will be granted, upon issuance of the Letter of Credit and effective as of the Payment Date, a valid and perfected first priority security interest in and lien upon (x) the Merchandise, (y) proceeds realized from the disposition of the Agent Sale FF&E up to the amount of the Agent's disposition commission related to Agent Sale FF&E, and (z) the Proceeds, to secure all obligations of Merchant to Agent. Such security interest shall remain junior and subordinate in all respects to the Agent's Payment Obligations, and (b) the liens, security interests and claims of the GECC and the Lenders, to the extent of the unpaid portion of Agent's Payment Obligations. Upon entry of the Approval Order, and payment of the Guaranteed Amount Deposit, and the issuance of the Letter of Credit, the security interest granted to the Agent will be deemed properly perfected without the necessity of filing financing statements or other documentation.

C. The SCSs Do Not Require Appointment of A Consumer Privacy Ombudsman

45. Section 363(b)(1) of the Bankruptcy Code provides that a debtor may not sell or lease personally identifiable information unless such sale or lease is consistent with its policies or upon appointment of a consumer privacy ombudsman pursuant to section 332 of the Bankruptcy Code.

46. Pursuant to the Agency Agreement, the Liquidating Agent will *not* have access to the Debtors' customer lists and the Debtors will not disclose any personally identifiable information regarding the Debtors' customers. Therefore, appointment of a consumer privacy ombudsman is unnecessary.

D. The Break-Up Fee

47. The Agency Agreement contemplates that if the Stalking Horse Bidder is not the successful bidder at the Auction, then in consideration of the Stalking Horse Agent conducting its due diligence, entering into the Agency Agreement, and agreeing to subject its Stalking Horse Bid to the Auction, the Stalking Horse Bidder will receive a break-up fee of $1,000,000 (the "Break-Up Fee"). The Stalking Horse Bidder has agreed that it will not be permitted to apply the Break-Up Fee to offset amounts it is required to bid pursuant to set bidding increments. The Debtors hereby respectfully request that the Court approve the Break-Up Fee.

48. Courts in the Second Circuit analyze the appropriateness of bidding incentives such as the Bid Protections under the "business judgment rule" standard, and it is well established in this district that courts consider whether (a) the relationship of the parties who negotiated the break-up fee is devoid of taint by self-dealing or manipulation, (b) the fee encourages, rather than hampers, bidding, and (c) the amount of the fee is reasonable relative to the proposed purchase price. *See Integrated Res.*, 147 B.R. at 657-8 (to evaluate bid protections, courts should employ the business judgment rule, which proscribes judicial second-guessing of the corporate debtor's actions taken in good faith, absent self-dealing, and in the exercise of honest judgment); *see also In re Metaldyne Corp.*, 409 B.R. 661, 670 (Bankr. S.D.N.Y. 2009) (approving bid protections because, among other factors, "the stalking horse bid brings value to the estate by setting a floor on the price and providing a structure for potential competing bids . . . [and] would provide comfort to the Debtors' employees and customers that the company was entering the auction with a locked-in bid.").

49. The Debtors, in their business judgment, have concluded that the Break-Up Fee is reasonable and appropriate under the circumstances. Etlin Decl. at ¶ 24. It is the result of good

faith, arms-length negotiations, and provides a price floor and bidding structure for potential competing bids. *Id.* The Debtors believe the Break-Up Fee will incentivize competitive bidding thereby maximizing recovery to the Debtors and their estates in the SCSs. *Id.* Indeed, the Break-Up Fee – which equates to approximately less than 1% of the consideration guaranteed by the Stalking Horse Bidder -- will not be paid unless the Auction results in approximately $940,000 more in consideration to the Debtors, net of the Break-Up Fee. *Id.*

50. The Debtors and the Hilco Group extensively negotiated the inclusion of the Break-Up Fee and its amount, which negotiations resulted in the Hilco Group's agreement to reduce the fee to its current level by $950,000. *Id.* at ¶ 25. In exchange for this break-up fee, the Debtors were able to negotiate certain other valuable provisions including the sale of the periodicals inventory, cost to retail factors and a broader merchandise threshold. *Id*. Based on those discussions, the Debtors believe that the Stalking Horse Bidder would not proceed with the sale without the Break-Up Fee. (Indeed, GB Group, the competing bidder, also requested a break-up fee). *Id.*

51. Accordingly, the Break-Up Fee is well below the range of break-up fees and expense reimbursements approved by courts in this district.[6]

[6] *See e.g., In re BearingPoint, Inc.*, No. 09-10691 (REG) (Bankr. S.D.N.Y. Apr. 7, 2009) [Docket No. 369] (approving a break-up fee of approximately 3% of the purchase price and expense reimbursement up to $5,000,000); *In re Silicon Graphics, Inc.*, No. 09-11701 (MG) (Bankr. S.D.N.Y. Apr. 3, 2009) [Docket No. 55] (approving break-up fee of approximately 2.8% of the purchase price and expense reimbursement up to $750,000); *In re Steve & Barry's Manhattan LLC*, No. 08-12579 (ALG) (Bankr. S.D.N.Y. Aug. 5, 2008) [Docket No. 369] (approving break-up fee of 2% of the purchase price and expense reimbursement up to $2 million); *In re Fortunoff Fine Jewelry and Silverware, LLC*, No. 08-10353 (JMP) (Bankr. S.D.N.Y. Feb. 22, 2008) [Docket No. 190] (approving break-up fee of approximately 2.8% of the purchase price); *In re Bally Total Fitness of Greater New York, Inc.*, No. 07-12395 (BRL) (Bankr. S.D.N.Y. Aug. 21, 2007) [Docket No. 269] (approving break-up fee of 4.3% of the purchase price and expense reimbursement of up to 2.1% of the purchase price); *In re Solutia Inc.*, No. 03-17949 (PCB) (Bankr. S.D.N.Y. Oct. 19, 2005) [Docket No. 2611] (approving break-up fee of approximately 2.9% of the purchase price and expense reimbursement up to $2 million).

52. Finally, and importantly, the Break-Up Fee has been approved in writing by the Debtors' key constituencies, including, within the Agency Agreement, by the Debtors' two proposed DIP Facility Agents.

53. Accordingly, the Debtors respectfully request that the Court approve the Break-Up Fee and authorize the Debtors to pay it immediately if the Stalking Horse Bidder does not prevail at the Auction.

* * *

54. The Debtors believe that the terms of the Agency Agreement are typical, customary and reasonable under the circumstances in the exercise of their prudent business judgment. Accordingly, the Debtors respectfully request that the Court approve the Agency Agreement with the Stalking Horse Bidder, or authorize the Debtors to enter into a substantially similar agreement with the Successful Bidder. Additionally, the Debtors request authority to exercise the Put Option and execute an amendment to the Agency Agreement or a new agency agreement substantially similar to the Agency Agreement without further order of the court.[7]

III. WAIVER OF CONTRACTUAL RESTRICTIONS AND EXEMPTION OF FAST PAY LAWS AND LAWS RESTRICTING STORE CLOSING SALES

55. The Debtors respectfully request waiver of certain contractual or applicable law restrictions that could otherwise inhibit or prevent the Debtors' ability to maximize recovery through the SCSs, and which are customarily waived in sales such as these.

A. Waiver of Contractual Restrictions

56. The Debtors request that the Court override or invalidate any Contractual Restrictions that may impair the Debtors' ability to close stores and conduct the SCSs. The stores subject to the SCSs are located on properties that are leased by the Debtors. In certain

[7] *See* note 2, *supra.*

cases, the contemplated SCSs may be inconsistent with certain provisions of such leases, subleases, or other documents with respect to any such leased premises, including (without limitation) reciprocal easement agreements, agreements containing covenants, conditions and restrictions (including, without limitation, "go-dark" provisions and landlord recapture rights), or other similar documents or provisions.

57. Store closing or liquidation sales are a routine part of chapter 11 cases involving retail debtors. Such sales are consistently approved by courts despite provisions of recorded documents or agreements purporting to forbid such sales. Indeed, other such restrictive provisions in contracts have been deemed unenforceable in other chapter 11 cases as impermissible restraints on a debtor's ability to maximize the value of its assets under section 363 of the Bankruptcy Code. *See In re Blockbuster Inc.*, Ch. 11 Case No. 10-14997 (BRL) (Bankr. S.D.N.Y. Jan. 20, 2011) at ¶¶ 7, 8; *In re Finlay Enters., Inc.*, Ch. 11 Case No. 09-14873 (JMP) (Bankr. S.D.N.Y. Sept. 25, 2009) at ¶ 14; *In re Steve & Barry's Manhattan LLC*, Ch. 11 Case No. 08-12579 (ALG) (Bankr. S.D.N.Y. Aug. 22, 2008) at ¶¶ 32, 33; *In re Bradlees Stores, Inc.*, Case No. 00-16035 (BRL) (Bankr. S.D.N.Y. Jan. 4, 2001) (authorizing Debtors to conduct GOB sales notwithstanding state rules or statutes governing closing, liquidation, or "going-out-of-business" sales and notwithstanding provision in leases restricting Debtor's ability to conduct such sales); *In re R.H. Macy & Co.*, 170 B.R. 69, 77 (Bankr. S.D.N.Y. 1994) (holding restrictive lease provision unenforceable against debtor that sought to conduct going-out-of-business sale "because it conflicts with the Debtor's fiduciary duty to maximize estate assets"); *Ames Dep't Stores, Inc.* (Ames I), 136 B.R. at 359 (finding that "to enforce the anti-GOB sale clause of the [l]ease would contravene overriding federal policy requiring Debtors to maximize estate assets by imposing additional constraints never envisioned by Congress"); *see also In re Tobago Bay*

Trading Co., 112 B.R. 463, 467 (Bankr. N.D. Ga. 1990) (finding anti-going-out-of-business sales clause in lease unenforceable).

58. The Court should ensure that no Contractual Restriction is an impediment to the SCSs, closures of Closing Stores, or the activities in connection therewith. To the extent such Contractual Restrictions exist, they should not be permitted to interfere with, or otherwise restrict the Debtors from conducting the SCSs or the closing of any Closing Stores.

B. Exemption From Applicable Law Restrictions

59. Certain states in which the Closing Stores are located have or may have licensing and other requirements governing the conduct of store closing, liquidation, or other inventory clearance sales, including (but not limited to) state, and local laws, statutes, rules, regulations, and ordinances related to store closing and liquidation sales, establishing licensing, permitting, or bonding requirements, waiting periods, time limits, bulk sale restrictions, augmentation limitations that would otherwise apply to the SCSs, or consumer fraud laws, with the exception of deceptive advertising laws (the "Liquidation Sale Laws"). Typical statutes and regulations provide that if a liquidation or bankruptcy sale is court authorized, however, then a company need not comply with these Liquidation Sale Laws.

60. The Debtors, therefore, request that the Court authorize the Debtors to conduct the SCSs without the necessity of, and the delay associated with, complying with the Liquidation Sale Laws. Because the Debtors and their assets are subject to this Court's jurisdiction, *see* 28 U.S.C. § 1334, this Court will be able to supervise the SCSs. The SCSs are legitimate methods by which the Debtors can maximize the return from the sale of the Merchandise for the benefit of their estates and creditors. Moreover, creditors and the public interest are adequately protected by the jurisdiction and supervision of this Court.

61. Even if a state or local law does not expressly except bankruptcy sales from its ambit, the Debtors submit that, to the extent that such state or local law conflicts with federal bankruptcy laws, it is preempted by the Supremacy Clause of the United States Constitution. To hold otherwise would severely impair the relief otherwise available under section 363 of the Bankruptcy Code. In concert with this premise, bankruptcy courts have consistently recognized that federal bankruptcy law preempts state and local laws that contravene the underlying policies of the Bankruptcy Code. *See, e.g.*, *Aloe v. Shenango Inc. (In re Shenango Group, Inc.)*, 186 B.R. 623, 628 (Bankr. W.D. Pa. 1995) ("Trustees and debtors-in-possession have unique fiduciary and legal obligations pursuant to the bankruptcy code. . . . [A] state statute [ ] cannot place burdens on them where the result would contradict the priorities established by the federal bankruptcy code."). While preemption of state law is not always appropriate, as when the protection of public health and safety is involved, *see Baker & Drake, Inc. v. Pub. Serv. Comm'n of Nev. (In re Baker &Drake, Inc.)*, 35 F.3d 1348, 1353-54 (9th Cir. 1994) (finding no preemption when state law prohibiting taxicab leasing was promulgated in part as a public safety measure), it is appropriate when, as here, the only state laws involved concern economic regulation. *Id.* at 1353 (finding that "federal bankruptcy preemption is more likely . . . where a state statute is concerned with economic regulation rather than with protecting the public health and safety"). Moreover, pursuant to section 105 of the Bankruptcy Code, the Court has the authority to permit the SCSs to proceed notwithstanding contrary Liquidation Sale Laws. *See* 11 U .S.C. § 105(a).

62. Here, section 363 of the Bankruptcy Code, which requires the Debtors to operate their businesses in a way that maximizes recoveries for creditors, will be undermined if the Court does not provide for the waiver of the Liquidation Sale Laws because the Liquidation Sale Laws

constrain the Debtors' ability to marshal and maximize assets for the benefit of creditors. Similar relief has been granted in this and other bankruptcy cases in other jurisdictions. *See*, *e.g.*, *In re Blockbuster Inc.*, Ch. 11 Case No. 10-14997 (BRL) (Bankr. S.D.N.Y. Jan. 20, 2011) at ¶¶ 9, 10; *In re Finlay Enters., Inc.*, Ch. 11 Case No. 09-14873 (JMP) (Bankr. S.D.N.Y. Sept. 25, 2009) at ¶ 11; *In re Steve & Barry's Manhattan LLC,* Ch 11 Case No. 08-12579 (ALG) (Bankr. S.D.N.Y. Aug. 22, 2008) at ¶ 36.

63. Importantly, given the supervision of this Court, the requested waiver will not unduly undermine state and local requirements that would otherwise apply to the SCSs. The Debtors only request that this Court authorize the Debtors to conduct the SCSs without the necessity of, and the delay associated with, obtaining various state licenses or permits, observing state and local waiting periods or time limits, and/or satisfying any additional requirements with respect to advertising, conducting the SCSs as store closings or similar type sales, or transferring merchandise from the distribution centers to the Closing Stores. The Debtors fully intend to be bound by and comply with remaining statutes and regulations, such as health and safety laws.

64. The Debtors also request that no other person or entity, including (but not limited to) any lessor or federal, state, or local agency, department, or governmental authority, be allowed to take any action to prevent, interfere with, or otherwise hinder consummation of the SCSs, or the advertising and promotion (including through the posting of signs) of SCSs, in the manner set forth in the proposed Order.

C. Exemption From State "Fast Pay" Laws and Regulations

65. Many states in which the Debtors operate have laws and regulations that require the Debtors to pay an employee substantially contemporaneously with his or her termination.[8] In

[8] For example, California Labor Code § 201(a) provides, in pertinent part, that "[i]f an employer discharges an employee, the wages earned and unpaid at the time of discharge are due and payable immediately."

many cases, these laws require the payment to occur either immediately or within a period of only a few days from the date such employee is terminated. The sweeping nature of the SCSs contemplated by this Motion will result in a substantial numbers of employees being terminated during the SCSs. The Debtors' payroll systems will simply be unable to process the payroll information associated with these terminations in a manner that will be compliant with these state laws and regulations.

66. As set forth above, the Bankruptcy Code preempts state and local laws that conflict with its underlying policies. *See* (¶ 61, *supra*). Preemption is appropriate where, as here, the only state laws involved concern economic regulation rather than the protection of public health and safety.

67. Under ordinary circumstances, the Debtors were often able to pay individual store-level employees from the register at a store location upon termination and reconcile the payment amount after-the-fact. However, given the number of employees that will be terminated during the SCSs, this will be impossible. Thus, it will be necessary to have the Debtors payroll department calculate individual termination payments, prepare each termination payment check, obtain authorization for each such check and then prepare each such check for mailing. With employee terminations on the scale necessitated by the SCSs, this process could easily take several days.

68. To be clear, the Debtors intend to pay their terminated employees as expeditiously as possible and under normal payment procedures. However, the requirements imposed by these state laws and regulations are unworkable in these extraordinary circumstances. If the Debtors are required to comply with these state laws and regulations, their efforts to wind down their operations and stem unnecessary payroll costs will be hampered tremendously. Indeed, if forced

to comply, the Debtors will face the choice of (a) having to incur the costs of keeping employees "employed" after the conclusion of a Sale while payroll is prepared or (b) staging terminations to the detriment of the Debtors' estates. Both of these choices will provide no benefit to the Debtors' estates and will only increase the administrative costs of conducting the SCSs.

69. Accordingly, the Debtors respectfully submit that in this instance, Fast Pay Laws are at odds with the underlying policies of the Bankruptcy Code and as such, the Debtors should be granted relief from their requirements. *See In re Linens Holding Co.*, Ch. 11, Case No. 08-10832 (Bankr. D. Del. Oct. 28, 2008) (waiving "fast pay" laws and regulations in connection with approval of store closing sales).

IV. AUTHORITY TO ABANDON UNSOLD PROPERTY FOLLOWING STORE CLOSING SALES

70. Section 554(a) of the Bankruptcy Code provides that after notice and a hearing, the trustee, and therefore the debtor in possession, "may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate." *See Hanover Ins. Co. v. Tyco Indus., Inc.*, 500 F.2d 654, 657 (3d Cir. 1974) (a trustee "may abandon his claim to any asset, including a cause of action, he deems less valuable than the cost of asserting that claim"); *In re Grossinger's Assoc.*, 184 B.R. 429, 432 (Bankr. S.D.N.Y. 1995). *See also Midlantic Nat'l Bank v. New Jersey Dep't of Envtl. Protection*, 474 U.S. 494, 507, n.9 (1986) ("[A] trustee [in bankruptcy] may not abandon property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards . . . This exception to the abandonment power . . . is a narrow one."); *In re Bryson*, 53 B.R. 3, 4-5 (Bankr. M.D. Tenn. 1985) ("The effect of the abandonment is to remove the asset from the jurisdiction of the bankruptcy court.").

71. Under the Agency Agreement, any Merchandise remaining at the Closing Stores following the SCSs can be sold by the Liquidating Agent, with the proceeds thereof treated as Proceeds for purposes of compensation computation. To the extent, however, that the Liquidating Agent does not sell any Merchandise or Owned FF&E, the Debtors request that they be authorized upon the conclusion of the SCSs to abandon same without incurring liability to any person or entity. The Debtors submit that if they are unable to sell or dispose of any such assets following the SCSs, it would be costly and burdensome to the estate to retain them.

72. In the event of such abandonment, the Debtors request that the applicable landlord be authorized to dispose of such property without any liability to any individual or entity that may claim an interest in such abandoned property and that such abandonment be without prejudice to any landlord's right to assert any claims based on such abandonment and without prejudice to the Debtors or other party-in-interest to object thereto.

73. Notwithstanding the foregoing, the Debtors and the Liquidating Agent will utilize all commercially reasonable efforts to remove or cause to be removed any confidential or personal identifying information (which means information which alone or in conjunction with other information identifies an individual, including, but not limited to, an individual's name, social security number, date of birth, government-issued identification number, account number, and .credit or debit card number) in any of the Debtors' hardware, software, computers or cash registers or similar equipment that are to be sold or abandoned.

V. ASSUMPTION OF HILCO CONSULTING AGREEMENTS

74. Section 365(a) of the Bankruptcy Code provides that a debtor may assume executory contracts. 11 U.S.C. § 365. The decision to assume or reject is governed by the business judgment rule. *See Orion Pictures Corp. v. Showtime Networks, Inc. (In re Orion*

Pictures Corp.), 4 F.3d 1095, 1099 (2d Cir. 1993) (stating that section 365 of the Bankruptcy Code "permits the trustee or debtor-in-possession, subject to the approval of the bankruptcy court, to go through the inventory of executor contracts of the debtor and decide which ones it would be beneficial to adhere to and which ones it would be beneficial to reject."); *see also NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 523 (1984) (stating that the traditional standard applied by courts to authorize the rejection of an executory contract is that of "business judgment"); *In re Gucci*, 193 B.R. 411, 415 (S.D.N.Y. 1996) ("A bankruptcy court reviewing a trustee's decision to assume or reject an executory contract should apply its 'business judgment' to determine if it would be beneficial or burdensome to the estate to assume it.").

75. The Debtors entered into the Hilco Consulting Agreements prior to the Petition Date to obtain Hilco's consulting services with respect to store closing sales run by the Debtors at 19 locations. Each agreement entitles Hilco to reimbursement of its expenses for conducing such sales. With respect to Waldenbooks locations, that is Hilco's only compensation. At Border SuperStore locations, Hilco also receives a commission of 1.25% of gross proceeds. As of the Petition Date, the Debtors has paid all obligations due to Hilco regarding the agreements.

76. Inasmuch as the Debtors continue running store closing sales at these 19 locations, they need Hilco's continued consulting services post-petition. Accordingly, the Debtors, in their business judgment, have concluded that assuming the Hilco Consulting Agreements is in the best interest of the Debtors and their estates, especially where doing so will not require the Debtors to pay any cure obligations.[9]

[9] Assumption of the Hilco Consulting Agreements is not a condition precedent to effectiveness of the Agency Agreement or the parties' rights and obligations thereunder.

VI. WAIVER OF STAY UNDER BANKRUPTCY RULES 6004(H) AND 6006(D)

77. Pursuant to Bankrupt*cy* Rule 6004(h), unless a court orders otherwise, all orders authorizing the sale of property pursuant to section 363 of the Bankruptcy Code are automatically stayed for 14 days after entry of the order. Fed. R. Bankr. P. 6004(h). The purpose of Bankruptcy Rule 6004(h) is to provide sufficient time for an objecting party to appeal before the order is implemented. *See* Fed. R. Bankr. P. 6004(h) advisory committee note.

78. In order to maximize value from the SCSs, the Debtors request that any order approving the Motion be effective immediately by providing that the 14-day stay under Bankruptcy Rules 6004(h) is waived. As discussed above and set forth in the Etlin Delc., the Liquidating Agent requires the ability to commence the SCSs right away and no later than February 19, 2011. Moreover, the Debtors face severe prejudice each day that the Closing Stores continue to operate, as those locations are unprofitable, drain liquidity, and are being quickly depleted of inventory which will not be replenished.

VII. COMPLIANCE WITH LOCAL RULE 6004-1

79. The Debtors submit that, given the description of the SCSs provided herein, the requirements of Rule 6004-1 of the Local Bankruptcy Rules for the Southern District of New York (the "Local Bankruptcy Rules") have been satisfied. Alternatively, to the extent the Court finds that the Debtors have not met any applicable provisions of Local Bankruptcy Rule 6004-1, the Debtors respectfully request that the Court waive such requirements with respect to this Motion.

NOTICE

80. Under Bankruptcy Rule 2002(a) and (c), the Debtors are required to notify their creditors of the SCSs, including (i) the terms and conditions of the SCSs; (ii) the date, time, and place of the hearing, and (ii) the deadline for filing any objections to the relief requested herein

(the "SCS Notice"). The Debtors respectfully submit that the form of the SCS Notice, attached hereto as Exhibit E complies with applicable rules. Copies of the SCS Notice have been served on: (i) the Office of the United States Trustee for the Southern District of New York (Attn: Tracy Davis, Esq. and Linda Riffkin, Esq.); (ii) those creditors holding the thirty largest unsecured claims against the Debtors' estates; (iii) counsel for the DIP Agents: (x) Morgan, Lewis & Bockius LLP (Attn: Wendy Walker, Esq. and Sandra Vrejan, Esq.), counsel for the Working Capital Agent, (y) Riemer & Braunstein LLP (Attn: Donald E. Rothman, Esq.), counsel for GA Capital LLC; (iv) Kelley Drye & Warren LLP, attorneys for certain landlords (Attn: James S. Carr, Esq., Robert L. LeHane, Esq., and Benjamin D. Feder, Esq.); (v) Lowenstein Sandler PC, attorneys for certain trade vendors (Attn: Kenneth A. Rosen, Esq., Bruce D. Buechler, Esq., Bruce S. Nathan, Esq., and Paul Kizel, Esq.); (vi) Fried, Frank, Harris, Shriver & Jacobson LLP, attorneys for General Growth Properties, Inc. (Attn: Brad Eric Scheler, Esq.); (vii) Bingham McCutchen LLP, attorneys for Bank of America, N.A. (Attn: Julia Frost-Davies, Esq. and Andrew Gallo, Esq.); (viii) offices of attorneys general for each state in which the Debtors operate; (ix) landlords for the Closing Stores; and (x) municipalities in which the Closing Stores are located. The Debtors submit that no other or further notice need be provided.

81. No previous request for the relief sought herein has been made by the Debtors to this or any other court.

WHEREFORE the Debtors respectfully request that the Court grant the relief requested herein and such other and further relief as it deems just and proper.

Dated: February 16, 2011
New York, New York

KASOWITZ, BENSON, TORRES
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