UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re	:	Chapter 11
	:	
Friendly Ice Cream Corporation, *et al.*,	:	Case No. 11-13167-KG
	:	
	:	Jointly Administered
	:	
Debtors.	:	**Hearing Date: October 24, 2011 at 3:00 p.m.**
	:	**Objections Due: October 18, 2011 @ 4:00 p.m**
	:	**Extended by agreement for the U. S. Trustee**

UNITED STATES TRUSTEE'S OBJECTION TO THE DEBTORS MOTION FOR ENTRY OF (A) AN ORDER APPROVING BIDDING PROCEDURES AND NOTICE PROCEDURES AND (B) AN ORDER (I) APPROVING THE ASSET PURCHASE AGREEMENT, INCLUDING EXPENSE REIMBURSEMENT; (II) AUTHORIZING THE SALE OF ALL OR SUBSTANTIALLY ALL OF THE ASSETS OF THE DEBTORS FREE AND CLEAR OF ALL LIENS, CLAIMS, ENCUMBRANCES AND OTHER INTERESTS; (III) AUTHORIZING THE ASSUMPTION AND ASSIGNMENT OF CERTAIN EXECUTORY CONTRACTS AND UNEXPIRED LEASES; AND (IV) GRANTING RELATED RELIEF (D. E. 15, 90)

In support of her Objection to the Debtors Motion for Entry of (A) an Order Approving Bidding Procedures and Notice Procedures and (B) an Order (I) Approving the Asset Purchase Agreement, Including Expense Reimbursement; (II) Authorizing the Sale of all or Substantially all of the Assets of the Debtors Free and Clear of all Liens, Claims, Encumbrances and Other Interests; (III) Authorizing the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases; and (IV) Granting Related Relief (D. E. 15, 90) (the "Motion"), Roberta A. DeAngelis, United States Trustee for Region 3 ("U.S. Trustee"), by and through her undersigned counsel, states as follows:

Introduction

1. This Court has jurisdiction to hear and determine this Objection.

2. Pursuant to 28 U.S.C. § 586(a)(3), the U.S. Trustee is charged with administrative oversight of the bankruptcy system in this District. Such oversight is part of the U.S. Trustee's overarching responsibility to enforce the laws as written by Congress and interpreted by the courts. *See United States Trustee v. Columbia Gas Systems, Inc. (In re Columbia Gas Systems, Inc.)*, 33 F.3d 294, 295-96 (3d Cir. 1994) (noting that U.S. Trustee has "public interest standing" under 11 U.S.C. § 307 which goes beyond mere pecuniary interest); *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498, 500 (6th Cir. 1990) (describing the U.S. Trustee as a "watchdog").

3. Under 11 U.S.C. § 307, the U.S. Trustee has standing to be heard on the issues raised by this Objection.

Statement of Relevant Facts

4. On October 5, 2011 (the "Petition Date"), the Debtors filed voluntary petitions for relief under Chapter 11 of 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.

5. The U.S. Trustee appointed an official committee of unsecured creditors on October 12, 2011 (D. E. 117).

6. The Debtors in these chapter 11 cases are Friendly Ice Cream Corporation ("FICC") along with its wholly-owned subsidiaries Friendly's Restaurants Franchise, LLC, Friendly's Realty I, LLC, Friendly's Realty II, LLC and Friendly's Realty III, LLC (together "Friendly's" or "the Debtors").

7. The Debtors are a family-oriented restaurant chain and provider of ice cream

products in the Eastern United States. As of the Petition Date, Friendly's operations encompasses approximately 490 restaurants located in 16 states. In addition to its restaurant operations, Friendly's manufactures a complete line of premium ice cream products distributed to more than 7,000 supermarkets and other third party retail locations in 48 states. The Debtors have over 10,000 employees.

8. The Debtors' operations are segmented into four key business units: Company-Owned Restaurants, Franchising, Foodservice, and Retail and Custom Packing.

9. As of the Petition Date, the Debtors have outstanding debt obligations in the aggregate principal amount of approximately $297.0 million (excluding approximately $14.9 million in issued and unfunded letters of credit), consisting primarily of approximately (a) $21.5 million in secured debt under the first lien senior secured credit facility, (b) $267.7 million in a subordinated secured promissory note, and (c) $7.8 million in principal amount of 8.375% unsecured notes.

10. Relevant to the Motion, the ICC is obligated to Sundae Group Holdings I, LLC (the "PIK Noteholder") pursuant to a Subordinated Secured Promissory Note. It should be noted that the PIK Noteholder is majority owned, indirectly, by one or more affiliates of Sun Capital Partners, Inc. Certain co-investors, including the Debtors' Chief Executive Officer, are minority owners of the PIK Noteholder. The Debtors' ultimate majority equity holders are also affiliates of Sun Capital Partners, Inc.

11. On September 9, 2011, Freeze, LLC (as successor to the original lender under the Secured Promissory Note, Freeze Group Holding Corp.) assigned its right, title, and interest in the Secured Promissory Note to the PIK Noteholder in exchange for, among other things, the

agreement by the PIK Noteholder to lend an additional $2 million under the P1K Note to fund the Debtors' operations and a commitment to lend certain additional amounts. Pursuant to this commitment, the PIK Noteholder subsequently lent an additional $2 million on September 26, 2011, and a further $2 million on September 30, 2011, for an aggregate of $6 million since the assignment. Under the Secured Promissory Note, FICC issued a secured promissory note due January 11, 2013 in the original principal amount of $100 million, with interest paid in-kind at a floating rate tied to an EBITDA grid which was subsequently amended to a flat rate of 12 percent (the "PIK Note"). On March 11, 2008 and June 5, 2008, the principal amount of the P1K Note was increased by $26.5 million and $19.5 million, respectively. The current amount outstanding under the PIK Note is approximately $267.7 million.

12. The PIK Note is junior in interest to the Prepetition Secured Credit Agreement, pursuant to an Intercreditor and Subordination Agreement between and among Wells Fargo Capital Finance and Freeze Group Holding Corp. The Secured Promissory Note is guaranteed by Freeze Operations Holding Corp. and Friendly's Restaurant Franchise, LLC, and is secured by substantially all of the assets of FICC, Freeze Operations Holding Corp., and Friendly's Restaurant Franchise, LLC.

13. On the Petition Date, the Debtors filed the Motion, which seeks, among other things, approval of certain bid procedures and protections for the sale of substantially all of the Debtors' assets (referred to as the "Sale"). As noted in more detail in the Motion, the Debtors seek to sell substantially all of their assets through a bidding and auction process.

14. As set forth in the Motion, the Purchaser will attempt to acquire the Debtors' assets through a credit bid (by way of an assignment from the PIK Noteholder) of the secured

debt holdings under the Secured Promissory Note. To facilitate an orderly sale process, an affiliate of Purchaser also agreed to fund the Debtors' post-petition financing needs through a 100% participation in the Debtors' senior secured debtor-in-possession credit agreement (the "DIP Credit Agreement") which provides the Debtors with post-petition revolving loans and letter of credit capacity in a principal amount not to exceed approximately $50.6 million on an interim basis and approximately $71.3 million on a final basis. Motion at Paragraph 9.

15. Although the Asset Purchase Agreement does not provide for any break-up fee, the Assets Purchase Agreement does provide for an expense reimbursement of $1,000,000 (the "Expense Reimbursement") if the parties close an alternative transaction but in the instance of, among other things, the issuance of a final and nonappealable order, decree, or ruling or any other action by a Governmental Authority to restrain, enjoin or otherwise prohibit the transfer of the Acquired Assets; the Auction has not concluded within 60 days after the Petition Date, unless agreed to in writing by Purchaser; a Sale Order has not been entered by December 23, 2011 (or such later date as Purchaser may have designated in writing to Sellers); or if, prior to the Closing Date, Sellers' Bankruptcy Cases shall be converted into a case under Chapter 7 of the Bankruptcy Code or dismissed, or if a trustee or examiner with expanded powers is appointed in the Bankruptcy Cases. Asset Purchase Agreement at Paragraphs 11.1 (b) and 11.1 (c).

16. The U. S. Trustee objects to the Motion on the following basis: (a) the Expense Reimbursement is not appropriate under relevant Third Circuit law; and (b) the sale appears to include the sale and/or disclosure of customer lists and other assets that can be defined as "personably identifiable information", which implicates Bankruptcy Code sections 363(b)(1) and 332 which may necessitate the appointment of a consumer privacy ombudsman.

APPLICABLE LAW AND ANALYSIS

A. The Expense Reimbursement is not appropriate under relevant Third Circuit law

17. First, the U.S. Trustee objects to the Expense Reimbursement to be paid to the Purchaser. As the Court knows, to award a break-up fee (or expense reimbursement) to a potential bidder, the court must determine that the fee was an actual and necessary cost and expense of preserving the estate. *See Calpine Corp. v. O'Brien Environmental Energy, Inc. (In re O'Brien Environmental Energy, Inc.),* 181 F.3d 527 (3d Cir. 1999).

18. In *O'Brien*, the Third Circuit Court of Appeals stated that ". . . the allowability of break-up fees, like that of other administrative expenses, depends upon the requesting party's ability to show that the fees were actually necessary to preserve the value of the estate." *O'Brien*, 181 F.3d at 535. The burden is on the Debtors to prove the necessity of, and benefit to the estate from, the proposed breakup fee or expense reimbursement. Moreover, although "the considerations that underlie the debtor's judgment may be relevant to the bankruptcy court's determination on a request for break-up fees and expenses," "the business judgment rule should not be applied as such in the bankruptcy context." *O'Brien*, 181 F.3d at 535.

19. The Expense Reimbursement is not appropriate in this context where the Purchaser is the assignee of the PIK Noteholder which is majority owned, indirectly, by one or more affiliates of Sun Capital Partners, an affiliate of the Debtors' ultimate majority equity holders, and the Debtors' CEO is a minority owner of the PIK Noteholder and the Purchaser seeks to purchase the Debtors' assets through a credit bid. The considerations applied by courts in determining the allowability of a break-up fee or expense reimbursement weigh against the approval of expenses where an insider or affiliate of an insider is the stalking horse bidder.

20. For instance, although breakup fees and reimbursement of expenses are sometimes approved to compensate an initial bidder for the time and expense of negotiating an agreement and conducting due diligence in connection therewith, the Expense Reimbursement in this case is inappropriate because the Purchaser have no apparent need for this protection. The justification that the Purchaser has spent considerable time in connection with identifying and quantifying the assets and negotiating the purchase agreement does not seem to ring true. The Purchaser should be intimately familiar with the Debtors and its assets. It is hard to believe that there are real significant due diligence costs here because of the Purchaser's close relationship with the Debtors.

21. Another consideration in determining the allowability of a break-up fee or expense reimbursement is that the protection is needed to induce a bid. Despite the indications in the Motion to the contrary, the U.S. Trustee takes issue with any assertion that the Purchaser would not bid for the Debtors' assets if the Expense Reimbursement is not provided. It seems rather implausible that the Purchaser would not submit its bid without the approval of the Expense Reimbursement.

B. Under Sections 363(b)(1) and 332 of the Bankruptcy Code, a consumer privacy ombudsman may be required

22. Finally, the U.S. Trustee notes that the Debtors propose to either sell its membership lists and other personally identifiable information of its customers, or make such information available to potential bidders in this bid process. As a result, a consumer privacy ombudsman must be appointed to protect the information. 11 U.S.C. § 363(b)(1) provides:

> (b)(1) The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the

> estate, except that if the debtor in connection with offering a product or a service discloses to an individual a policy prohibiting the transfer of personally identifiable information about individuals to persons that are not affiliated with the debtor and if such policy is in effect on the date of the commencement of the case, then the trustee may not sell
> or lease personally identifiable information[1] to any person unless –
>
> (A) such sale or lease is consistent with such policy; or
>
> (B) after appointment of a consumer privacy ombudsman in accordance with section 332, and after notice and a hearing, the court approves such sale or such lease –
>
> (I) giving due consideration to the facts, circumstances, and conditions of such sale or such lease; and
> (ii) finding that no showing was made that such sale or such lease would violate applicable nonbankruptcy law.

23. The Debtors privacy policy is posted on its website and a copy of that privacy policy is annexed hereto and made a part hereof as Exhibt "A". (See also, the Friendly's webiste

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[1] "Personally identifiable information" is defined in 11 U.S.C. § 101(41A) as meaning

> (A) if provided by an individual to the debtor in connection with obtaining a product or a service from the debtor primarily for personal, family, or household purposes –
> (i) the first name (or initial) and last name of such individual, whether given at birth or time of adoption, or resulting from a lawful change of name;
> (ii) the geographical address of a physical place of residence of such individual;
> (iii) an electronic address (including an e-mail address) of such individual;
> (iv) a telephone number dedicated to contacting such individual at such physical place of residence;
> (v) a social security account number issued to such individual; or
> (vi) the account number of a credit card issued to such individual; or
>
> (B) if identified in connection with 1 or more of the items of information specified in subparagraph (A) --
> (i) a birth date, the number of a certificate of birth or adoption, or a place of birth; or
> (ii) any other information concerning an identified individual that, if disclosed, will result in contacting or identifying such individual physically or electronically.

at http://www.friendlys.com/privacy/ and http://www.friendlys.com/privacy/kids/).

24. Nevertheless, it remains unclear if the sale of personally identifiable information to third parties is allowed under the privacy policy, but in any event, the Debtors have not ensured that the Sale is consistent with the privacy policy.

25. In sum, if the Debtors intend to sell the personally identifiable information of its customers (or assets containing personally identifiable information), a consumer privacy ombudsman must be appointed under 11 U.S.C. §§ 363(b)(1)(B) and 332(a), given that the sale of such information is not consistent with the Debtors' privacy policy.

26. The U.S. Trustee reserves any and all rights, remedies and obligations to, *inter alia*, complement, supplement, augment, alter and/or modify this Objection and to conduct any and all discovery as may be deemed necessary or as may be required and to assert such other grounds as may become apparent upon further factual discovery and to take whatever other actions are deemed necessary and appropriate.

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WHEREFORE, the United States Trustee respectfully requests this Court to issue a ruling denying the Motion as stated herein, and award such other relief as this Court deems appropriate and just under the circumstances.

Respectfully submitted,

ROBERTA A. DEANGELIS
UNITED STATES TRUSTEE

By: /s/Richard L. Schepacarter
Richard L. Schepacarter, Esquire
Trial Attorney
United States Department of Justice
Office of the United States Trustee
J. Caleb Boggs Federal Building
844 King Street, Room 2207, Lockbox 35
Wilmington, DE 19801
(302) 573-6491
(302) 573-6497 (Fax)

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