

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF LOUISIANA
LAFAYETTE DIVISION

IN RE:

PICCADILLY RESTAURANTS, LLC,
ET AL.,

DEBTORS

* CASE NO. 12-51127
*
* (JOINT ADMINISTRATION)¹
*
* CHAPTER 11
*
* JUDGE ROBERT SUMMERHAYS

DEBTORS' MOTION FOR AN ORDER, PURSUANT TO SECTIONS 503(b)(9), 363(b), AND 105(a) OF THE BANKRUPTCY CODE, (1) GRANTING CRITICAL VENDOR STATUS, (2) AUTHORIZING DEBTORS TO ENTER INTO A DISTRIBUTION AGREEMENT WITH THE MERCHANTS COMPANY, D/B/A MERCHANTS FOODSERVICE, AND ITS AFFILIATES, (3) AUTHORIZING THE IMMEDIATE CASH PAYMENT OF A PORTION OF THE PRE-PETITION CLAIM OF MERCHANTS, (4) AUTHORIZING THE REAPPLICATION OF CERTAIN OF THE DEBTORS' POST-PETITION PAYMENTS TO CERTAIN PRE-PETITION INVOICES OF THE MERCHANTS COMPANY, (5) ALLOWING MERCHANTS' SECTION 503(b)(9) CLAIM AND PACA CLAIMS, AND (6) GRANTING RELATED RELIEF

NOW INTO COURT, through undersigned counsel, come the above-captioned debtors and debtors-in-possession (collectively, the "Debtors"),² and move the Court, for the entry of a final Order, substantially in the form of **Exhibit A**, pursuant to sections 503(b)(9), 363(b) and 105(a) of the chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"), (1) Granting Critical Vendor Status to The Merchants Company d/b/a Merchants Foodservice, and its Affiliates ("Merchants"),³ (2) Authorizing the Debtors to Enter into a Distribution Agreement with Merchants (the "Distribution Agreement"), substantially in the form of **Exhibit B**, (3)

¹ Jointly administered with *In re Piccadilly Food Service, LLC*, 12-51128 (Bankr. W.D. La. 2012), and *In re Piccadilly Investments, LLC*, 12-51129 (Bankr. W.D. La. 2012).

² The debtors in these Chapter 11 cases include Piccadilly Restaurants, LLC, Piccadilly Food Service, LLC, and Piccadilly Investments, LLC.

³ Merchants includes the divisions and affiliates of Merchants, including The Merchants Company, d/b/a Sunrise Fresh Produce (Jackson), and Sunrise Fresh Produce, LLC (Jacksonville).

Authorizing the Immediate Cash Payment of a Portion of the Pre-Petition Claim of Merchants, (4) Authorizing the Reapplication of Certain of the Debtors' Post-Petition Payments to Certain Pre-Petition Invoices of Merchants, (5) Allowing Merchants' Section 503(b)(9) Claim and PACA Claims, and (6) Granting Related Relief (the "Motion"). In support of the Motion, the Debtors respectfully state as follows:

JURISDICTION

1. This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334, and 11 U.S.C. § 503. This matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A), (B) and (O).

2. Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

3. The statutory bases for the relief requested herein are sections 105(a), 363(b) and 503(b)(9) of the Bankruptcy Code.

BACKGROUND

4. On September 11, 2012 (the "Petition Date"), each of the Debtors filed a petition with the Court under chapter 11 of the Bankruptcy Code. The Debtors are operating their businesses and managing their properties as debtors-in-possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

5. No request for the appointment of a trustee or examiner has been made in these procedurally consolidated bankruptcy cases (collectively, the "Chapter 11 Case").

6. An official committee of unsecured creditors (the "Unsecured Creditors' Committee") was appointed on October 23, 2012.

THE DEBTORS' BUSINESSES

7. The Debtors operate cafeteria-style restaurants and provide food services to schools and other organizations. More particularly, on the Petition Date, the Debtors operated seventy-eight (78) cafeterias, and employed approximately 3,400 employees. As of fiscal year ended January 3, 2012, the Debtors generated revenues of roughly \$165 million.

8. On October 2, 2012, the Debtors filed a Motion for an Order Approving the Rejection of Certain Unexpired Leases of Nonresidential Real Property for Certain Closed or Underperforming Cafeterias, and the Rejection of Certain Unexpired Leases of Personal Property, Executory Contracts and One Unexpired Sublease Related to those Closed or Underperforming Cafeterias (Docket #167) (the "Rejection Motion"). The Rejection Motion was granted at a hearing held on October 23, 2012 (Docket #243).

9. As a consequence of the Rejection Motion, nine (9) underperforming cafeterias were closed in October 2012. Piccadilly Restaurants, LLC ("Restaurants") currently operates sixty-nine (69) cafeterias in ten states. The Debtors estimate that they currently employ approximately 3,000 people.

10. Additionally, after the Petition Date, the Debtors continue to be active in the food service line of business, which separates the Debtors from other restaurant companies in the industry. These contracts involve schools and governmental agencies. Shortly after the Petition Date, the Debtors served 131,000 meals and 100,000 snacks to Hurricane Isaac victims throughout South Louisiana.

DEBTORS' BUSINESS WITH MERCHANTS BEFORE THE PETITION DATE

11. Merchants is a privately owned business with over \$500 million in annual sales, and ranked #1 in national sales growth among food service companies by Institutional

Distribution Magazine. Merchants is a major seller and distributor to restaurant chains, such as Ryan's and Kentucky Fried Chicken.

12. Merchants offers its customers four full-scale distribution centers that ensure accurate next-day deliveries, with convenient voice-activated order selection systems, and a 165-unit fleet of multi-temperature food service delivery trucks and delivery drivers.

13. Since 2009, Merchants has been the Debtors' primary source of food and supplies (collectively, the "Food and Supplies"), both in terms of the Debtors' cafeterias and food services lines of businesses. The Food and Supplies include, but is not limited to, dry groceries, refrigerated products, frozen foods, and a wide variety of paper products. The Debtors estimate that thirty percent (30%) of its annual expenses are spent on food and ten percent (10%) of its annual expenses are spent on supplies, such as paper and soaps.

14. As of the Petition Date, the Debtors estimate that Merchants sells and delivers approximately ninety percent (90%) of the Debtors' Food and Supplies, and operates without a written agreement with the Debtors.

15. In 2012, before the Petition Date, the Debtors paid Merchants \$29,825,577 for Food and Supplies. In 2011, the Debtors paid Merchants \$44,416,332 for Food and Supplies.

16. In the ordinary course of business, each day, the Debtors rely on Food and Supplies provided by various suppliers to Restaurants' sixty-nine (69) cafeterias, as well as the Debtors' food service line of businesses. As stated previously, the Debtors estimate that Merchants sells and delivers approximately ninety percent (90%) of the Debtors' Food and Supplies. Generally, deliveries are made to each of Restaurants' cafeteria by Merchants on a day-to-day basis. Merchants is the pivotal link, therefore, in the Debtors ability to operate its businesses.

RELIEF SOUGHT IN THIS MOTION

17. By this Motion, the Debtors seek an Order that authorizes the relief sought in this Motion as to Merchants, based on (a) its status as a critical vendor, (b) section 503(b)(9), and (c) the Perishable Agricultural Commodities Act, 7 U.S.C. § 499(a), *et seq.* (“PACA”). Each of these issues is more fully discussed below in this Motion.

18. The following chart summarizes Merchants’ claims⁴ and the relief sought in the Motion with respect to those claims.

MERCHANTS’ CLAIM	PROPOSAL
PACA Claim (\$159,486)	Allowed; previously paid under Court’s PACA Order.
§503(b)(9) Administrative Claim for goods within 20 days (\$2,323,585)	Allowed; paid at the earliest time that any other allowed administrative claim under 11 U.S.C. §503(b)(9) is paid to any creditor by any of the Debtors
Unsecured Claim (\$1,740,492)	Allowed; immediately paid as follows: (i) credit against “Margin Differential Credit” of at least \$700,886 (which is a credit to be given by Merchants for the difference between the actual prices the Debtors paid post-petition for Food and Supplies and the lower prices to be paid under a new Distribution Agreement); (ii) 50% of the remaining amount thereafter will be paid by the Debtors in cash; and (iii) the remaining 50% balance will be satisfied by re-applying and re-classifying, on a dollar-for-dollar basis, the post-petition payments previously made by the Debtors to Merchants for Food and Supplies. Merchants to deliver a Distribution Agreement that extends up to \$1.4 million in post-petition credit terms to the Debtors.

19. By this Motion, the Debtors seek the entry of an Order, substantially in the form of **Exhibit A**, as follows:

⁴ For a summary of Merchants’ claims, see **Exhibit C**.

(a) An Order that finds that Merchants is a Critical Vendor of the Debtors and that authorizes the Debtors to enter into the Distribution Agreement with Merchants by which Merchants will agree to extend up to \$1.4 million in post-petition credit terms to the Debtors and sets the margins by which Merchants will sell Food and Supplies to the Debtors. The Debtors must provide Merchants with the information and documentation set forth on Exhibit A to the Distribution Agreement (Exhibit B to this Motion), which is also Exhibit 2 to the proposed Order (Exhibit A to this Motion), within the time periods set forth therein.

(b) An Order that (i) allows Merchants' unsecured administrative claim under section 503(b)(9) of the Bankruptcy Code in the amount of \$2,323,585 (the "Allowed 503(b)(9) Claim") for the value of goods that Merchants delivered to Restaurants within twenty (20) days of the Petition Date, and (ii) provides that the Allowed 503(b)(9) Claim will be paid at the earliest time that any other allowed administrative claim under 11 U.S.C. §503(b)(9) is paid to any creditor by any of the Debtors.⁵

(b) An Order that allows the previously paid PACA claims of Merchants (collectively, the "Allowed PACA Claims"), for a total of \$159,487.⁶

(c) An Order that (i) allows Merchants' unsecured claim in the amount of \$1,740,492 (the "Allowed Unsecured Claim"), and (ii) authorizes the Debtors to pay the Allowed Unsecured Claim, within two (2) business days from the date of the entry of the Order granting this Motion, as follows:

A. First, a credit (the "Margin Differential Credit")⁷ will be given by Merchants to Restaurants against the Allowed Unsecured Claim of Merchants for the margin differential charged for Food and Supplies after the Petition Date when compared to the more favorable contract terms subsequently negotiated between Restaurants and Merchants (as reflected in the Distribution Agreement), which Margin Differential Credit will continue to accrue until the entry of an Order granting this Motion. The Margin Differential Credit will be no less than \$700,886, the value of the Margin Differential Credit as of November 30, 2012.

B. Second, the Debtors will pay Merchants cash in an amount equal to fifty percent (50%) of the remaining amount of the Allowed Unsecured Claim (the "Critical Vendor Cash Payment"); and

C. Third, fifty percent (50%) of the remaining amount of the Allowed Unsecured Claim will be satisfied by re-applying and re-classifying, on a dollar-

⁵ The Allowed 503(b)(9) Claim is discussed at Paragraphs 21 through 24 of this Motion, and Exhibit D. For a summary of Merchants claims, see Exhibit C.

⁶ The Allowed PACA Claims are discussed at Paragraphs 25 through 27 of this Motion. For a summary of Merchants claims, see Exhibit C.

⁷ See Exhibit E for a more detail concerning the Margin Differential Credit, and Paragraphs 32 and 32 of this Motion.

for-dollar basis, post-petition payments previously made by Restaurants to Merchants for the purchase of Food and Supplies (the “Critical Vendor Reclassified Payment”). The intent of the Vendor Reclassified Payment is to convert a sufficient amount of such paid-in-advance payments made for post-petition purchases of Food and Supplies to be able to satisfy the balance of Allowed Unsecured Claim, thereby minimizing the amount the Debtors are required to draw under its DIP Financing.⁸

(d) After the payments and credits required of the Debtors herein are made to Merchants, and as consideration for the payments required herein, Merchants will enter into and deliver to Restaurants an executed Distribution Agreement, dated effective on the date that an Order is entered that grants this Motion, (substantially in the form of Exhibit B). The Distribution Agreement will govern the future sale and delivery of Food and Supplies at prices and a margin that are generally equal to or lower than the pre-petition prices charged by Merchants to Restaurants,⁹ as well as (i) giving the Debtors’ credit terms of up to \$1.4 million (the “Credit Terms”), (ii) for a term of two years, and (ii) terminable by Restaurants on 120-days’ notice to Merchants.¹⁰

(e) All of the payments by the Debtors to Merchants, including the Allowed PACA Claims, the applications of the Margin Differential Credit, the Critical Vendor Cash Payment and the Critical Vendor Reclassified Payment, as well as the allowance of the Allowed 503(b)(9) Claims and the Allowed Unsecured Claim, are absolute and final and are without any right of the Debtors or any successor thereto, including but not limited to a Chapter 11 trustee, a Chapter 7 trustee, or any Liquidation Agent or Liquidation Trust created or appointed pursuant to any confirmed Chapter 11 Plan, or the Unsecured Creditors’ Committee, or any of the DIP Lenders,¹¹ to avoid, recover or recoup either under chapter 5 of the Bankruptcy Code or otherwise, any transfers or payments made by any of the Debtors to Merchants.

⁸ The Debtors filed an Emergency Motion for an Order (I) Authorizing the Debtors to Obtain Post-Petition Financing Pursuant to 11 U.S.C. §§ 364(c) and 364(d), (II) Authorizing the Debtors’ Use of Case Collateral Pursuant to 11 U.S.C. § 363(c); (III) Granting Adequate Protection Pursuant to 11 U.S.C. § 361; and (IV) Scheduling a Final Hearing Pursuant to Bankruptcy Rule 4001(c) (Docket #15) (the “Financing Motion”). On September 18, 2012, the Bankruptcy Court entered an Order (Docket #84) that granted, on an interim basis, the Financing Motion, as modified by the Stipulation and Order, and (a) Authorizing Post-Petition Financing, (b) Authorizing Use of Cash Collateral, (c) Granting Superpriority Security Interests and Administrative Claims Pursuant to 11 U.S.C. § 364, (d) Granting Adequate Protection to Pre-Petition Lenders, (e) Granting Limited Relief from the Automatic Stay and (f) Granting Related Relief (the “Stipulation”) (Docket #83). A Final Hearing on the Stipulation is currently scheduled on the Stipulation on December 4, 2012.

⁹ For a summary of the impact of the claims and the credit line, see Exhibit C.

¹⁰ For a summary of the impact of the claims and the credit line, see Exhibit C.

¹¹ The DIP Lenders are defined in the Stipulation as Atalaya Special Opportunities Fund IV LP (Tranche B), any other Person that is a signatory as “Lender” to this Stipulation, and any Person that is a permitted assignee of any DIP Lender.

MERCHANTS' PRE-PETITION CLAIM IN THIS CHAPTER 11 CASE

(a) Merchants Pre-Petition Claim

20. As of the Petition Date, the Debtors have determined that Merchants had a claim in this Chapter 11 Case in the amount of \$4,223,564, representing money owed for Food and Supplies (collectively, the "Merchants Pre-Petition Claim"). The Merchants Pre-Petition Claim includes (a) an unsecured, non-priority claim, (b) an administrative claim under section 503(b)(9) of the Bankruptcy Code, and (c) PACA claims, each as discussed below.¹²

(b) The Allowed 503(b)(9) Claim

21. Of the total Merchants' Pre-Petition Claim, Merchants holds a valid claim under section 503(b)(9) of the Bankruptcy Code¹³ in the amount of \$2,323,585, representing the value of goods (Food and Supplies) that Merchants sold in the ordinary course of business to Restaurants within twenty (20) days of the Petition Date. Attached as Exhibit D is a schedule that lists, by invoice and delivery date, the Food and Supplies sold and delivered to Restaurants.

22. The Debtors have reconciled the invoices and confirmed that the Food and Supplies on Exhibit D were delivered within twenty (20) days of the Petition Date. The Debtors do not contest that the value of the Food and Supplies was the price listed on the invoices, as set forth on Exhibit D.

¹² For a summary of Merchants claims, see Exhibit C.

¹³ For a summary of Merchants claims, see Exhibit C. Bankruptcy Code § 503(b)(9) provides for the allowance, as an administrative expense, of the value of any good sold to Restaurants in the ordinary course of its business and received by Restaurants within twenty (20) days before the Petition Date. That section provides as follows:

After notice and a hearing, there shall be allowed, administrative expenses . . . including –

(9) the value of any goods received by the debtor within 20 days before the date of the commencement of a case under [title 11] in which the goods have been sold to the debtor in the ordinary course of such debtor's business.

23. For these reasons, the Debtors seek entry of a final Order that allows the Allowed 503(b)(9) Claim in the amount of \$2,323,585.

24. By this Motion, the Debtors do not seek authority to pay the Allowed 503(b)(9) Claim.¹⁴ Instead, the Allowed 503(b)(9) Claim will be paid at the earliest time that any other allowed administrative claim under 11 U.S.C. §503(b)(9) is paid to any creditor by any of the Debtors.

(c) *The Allowed PACA Claims*

25. The Debtors have paid PACA claims to Merchants before filing this Motion, in accordance the Order entered by this Court on September 21, 2012 (Docket #110) that granted the Debtors' Motion for Authority to Pay Potential Claims under PACA.

26. More particularly, after reviewing Merchants' submissions, on October 17, 2012, the Debtors paid The Merchants Company the amount of \$133,491.69 for its PACA claim. On November 9, 2012, the Debtors also paid the following PACA claims: (i) The Merchants Company, d/b/a Sunrise Fresh Produce (Jackson) the amount of \$10,692.65; and (ii) Sunrise Fresh Produce, LLC (Jacksonville) the amount of \$15,302.32.

27. Merchants' Allowed PACA Claims aggregate \$159,487. By this Motion, the Debtors seek a final Order allowing the Merchants' Allowed PACA Claims in the aggregate amount of \$159,487.¹⁵

¹⁴ The Debtors filed a Motion for an Order Establishing Procedures for the Assertion, Resolution, and Satisfaction of the Claims Asserted Pursuant to Bankruptcy Code Section 503(b)(9) (Docket #165), and an Order approving that Motion was entered on November 2, 2012 (Docket #275).

¹⁵ For a summary of Merchants claims, see **Exhibit C**.

**BUSINESS WITH MERCHANTS AFTER THE PETITION DATE
AND THE PROPOSED DISTRIBUTION AGREEMENT**

(a) Business with Merchants after the Petition Date

28. Although Merchants has continued to do business with the Debtors after the Petition Date on a prepayment basis, at increased prices, Merchants has repeatedly warned the Debtors that it will not continue to do so after December, 2012, unless it is given the “critical vendor” relief sought in this Motion.

29. After the Petition Date, because of the size of the Merchants Pre-Petition Claim, and because the Debtors and Merchants do not have a contract that obligates Merchants to sell to the Debtors on credit, Merchants required the Debtors to pay in advance for the purchase of any Food and Supplies (collectively, the “Post-Petition Payments”).

30. From the Petition Date through November 30, 2012, the Debtors have made a total of \$10,104,758 in Post-Petition Payments.

(b) The Proposed Distribution Agreement

31. The negotiation process with Merchants has resulted in a two-year contract that would give the Debtors binding contract terms for the purchase of Food and Supplies that are far more favorable to the Debtors than the non-binding conditions that currently exist.

32. To be clear, pricing is the key factor for the Debtors. Since the Petition Date alone, the aggregate amount of the Margin Differential (or the more favorable contract terms under the proposed Distribution Agreement compared to the prices charged after the Petition Date) totals \$700,886, as of November 30, 2012.¹⁶ As part of the relief sought in this Motion, Merchants has agreed to apply the Margin Differential Credit against its Allowed Unsecured

¹⁶ The Margin Differential is more fully detailed on **Exhibit D** to this Motion.

Claim. Additionally, Merchants has agreed to continue to accrue the Margin Differential Credit until the entry of an Order granting this Motion, and that the entire accrued Margin Differential Credit will be applied against the Allowed Unsecured Claim.

33. Under the proposed Distribution Agreement, Merchants will sell Food and Supplies at a margin of 8.5%. Before the Petition Date, Merchants operated on a 9.5% markup of cost, which is the equivalent of an 8.7% margin. Merchants has agreed that the margin under the Distribution Agreement will be 8.0% from and after of the Allowed 503(b)(9) Claim of Merchants is paid in full. (**Exhibit B**, at page 5.)

34. In addition, Restaurants alone can terminate the Distribution Agreement without cause, upon giving 120-days' notice to Merchants. (**Exhibit B**, at page 7.) This termination provision gives flexibility to Restaurants, while giving Merchants an opportunity to liquidate \$3,000,000 in Piccadilly proprietary products inventory that Merchants is expected to purchase in order to fulfill its obligations under the Distribution Agreement. This cancellation provision was required by Merchants because the Distribution Agreement permits Restaurants to direct a significant amount of purchases from specific vendors selected by Restaurants, as well as specific proprietary products that may even include Piccadilly logo products that could not be sold to other customers. Because it is beneficial to Restaurants for Merchants to invest heavily in this proprietary inventory, the Debtors had to give Merchants the 120-day notice of cancellation in order to have the ability to continue this directed purchase process.

35. Because the Credit Terms under the Distribution Agreement are up to \$1,400,000, the days within which the Debtors have to repay Merchants will vary depending on the Debtors' volume. This is beneficial to the Debtors in months where they have less customer volume, such

as January and February. As such, the Debtors estimate that the days outstanding under the Credit Terms could range from 14 to 18 days.

36. Because Merchants is providing Credit Terms, the Debtors must provide Merchants with the information and documentation set forth on Exhibit A to the Distribution Agreement (Exhibit B to this Motion), which is also Exhibit 2 to the proposed Order (Exhibit A to this Motion), within the time periods set forth therein.

37. In sum, the Distribution Agreement is binding on Merchants, and insures that the Debtors will have uninterrupted access to roughly ninety percent (90%) of its Food and Supplies, and will have Credit Terms of up to \$1.4 million.

38. Moreover, the terms and conditions of the relief sought in this Motion are the result of strenuous and protracted negotiations that began on the Petition Date. The Debtors believe that the relief sought in this Motion represents the most favorable terms and conditions that it can negotiate under the circumstances, and that Merchants is the best and by far the most economical source for its Food and Supplies.

39. To verify that Merchants is offering the best price for its Food and Supplies, the Debtors undertook an exhaustive solicitation process with other vendors, as described below.

**THE SOLICITATION PROCESS AND THE BUSINESS JUSTIFICATION
FOR THE CRITICAL VENDOR PAYMENTS TO MERCHANTS**

40. Since the commencement of this Chapter 11 Case, the Debtors have sought competitive offers from other vendors who could sell and deliver Food and Supplies to the Debtors in lieu of Merchants. More particularly, the Debtors solicited competitive bids from five (5) other suppliers and distributors. Thereafter, where appropriate, the Debtors entered into further negotiations in an attempt to improve on initial and, in some cases, subsequent bids.

41. At the conclusion of this process, the Debtors determined that Merchants' current offer remains, by far, the Debtors' best available option. This is true even after taking into account the critical vendor relief sought in this Motion, including the payment of the Critical Vendor Cash Payment and the Critical Vendor Reclassified Payment (collectively, the "Critical Vendor Payments").

42. The Debtors estimate that the next closest offer to Merchants (the "Next Best Offer") would cost the Debtors approximately \$3.9 million over a 12-month period, or 10% more over a 12-month period, in increased costs for Food and Supplies **alone**. This also equates to an increase of \$76,000 weekly. Merchants' Allowed Unsecured Claim (\$1,740,492) minus the Margin Differential Credit (\$740,886 as of December 1, 2012, and increasing each day), leaves an Allowed Unsecured Claim of about \$1,000,000, half which would be paid with the Critical Vendor Cash Payment, and half would be satisfied with the Critical Vendor Reclassified Payment. The Debtors would prefer *not* to make any Critical Vendor Payments, and would rather only pay creditors under a confirmed Chapter 11 plan. But here, the cost savings under the Distribution Agreement provides the business justification for doing so. After roughly 14-weeks, the cost savings under the Distribution Agreement will have paid for the Critical Vendor Payments.

43. While these cost savings alone provide the business justification for the relief sought in this Motion, in soliciting competing offers, the Debtors also discovered that Merchants' competitors are simply unable to comprehensively stock the Debtors' proprietary products at the same low costs as Merchants offers. The inability to stock the Debtors' proprietary products, due to stocking restrictions at the competitors' warehouses, would cause significant

changes in the Debtors' restaurants operations and would impact Restaurants' ability to offer some of its customary and much-loved food offerings.

44. And this is only part of the business justification for the Debtors making the Critical Vendor Payments. The additional weekly cost for Food and Supplies does not take into account the immense disruption to the Debtors in terms of the management hours that would ensue if the Debtors attempted to replace Merchants at this point. It would be prohibitively difficult for the Debtors (a) to switch from Merchants' three (3) major warehouses to the ten (10) warehouses that are used by the supplier who submitted the Next Best Offer, (b) to cover the additional expenses caused by the reduction in proprietary products available to all to the Debtors' restaurants, and (c) other intangible factors that would become operational difficulties for the Debtors in changing from Merchants to another seller and distributor of the Food and Supplies.

45. Simply put, the Merchants' proposal pays for itself over a relatively short period of time, without management disruptions and substantial labor expenses that the Debtors would be forced to incur if they were forced to move from Merchants to another vendor or vendors. Under these circumstances, there is a clear business justification for making the Critical Vendor Payments. For all of these reasons, the Debtors believe that the relief sought in this Motion is vital to the Debtors' reorganization efforts.

BASIS FOR RELIEF

46. Multiple bases exist for the relief requested herein. The Court may: (a) authorize payment under section 363 of the Bankruptcy Code; (b) authorize payment under its equitable authority and consistent with the Doctrine of Necessity, and (c) authorize payment to allow the Debtors to comply with the fiduciary obligations to their estates generally imposed by the

Bankruptcy Code. The relief requested herein is also consistent with relief regularly granted by courts in this district and in other jurisdictions. *See, e.g., In re Compact Manifolds, Inc.*, Case No. 06-50341 (Bankr. W.D. La. Aug. 18, 2006); *In re Entergy New Orleans, Inc.*, Case No. 05-17697 (Bankr. E.D. La. Dec. 5, 2005); *see also In re SemCrude, L.P.*, Case No. 08-11525 (Bankr. D. Del. July 23, 2008); *In re Tropicana Entrn't, LLC*, Case No. 08-10856 (Bankr. D. Del. May 30, 2008); *In re Leiner Health Prods., Inc.*, Case No. 08-10446 (Bankr. D. Del. Mar. 12, 2008)).

A. The Court May Authorize the Relief Requested Regarding the Critical Vendor Payments under Section 363 of the Bankruptcy Code

47. The Court may grant the relief requested in this Motion regarding the critical vendor payments pursuant to section 363(b) of the Bankruptcy Code. Section 363 provides, in relevant part, that the “[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 . . .” 11 U.S.C. § 363(b)(1). Under this section, a court may authorize a debtor to pay certain prepetition claims. *See In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989). To do so, “the debtor must articulate some business justification, other than the mere appeasement of major creditors.” *Id.* at 175.

48. The relief requested herein is necessary to prevent substantial and immediate harm to the Debtors. The Debtors require a steady stream of the Food and Supplies to ensure their ability to keep the cafeterias and food services businesses operating. The expense of granting the relief sought in this Motion (i.e., the Critical Vendor Payments) will have paid for itself in a relatively short period of time because the Next Best Bid will cost more than \$76,000 weekly for the cost of Food and Supplies alone. (See Paragraph 42 of this Motion.)

49. In addition to the cost savings,¹⁷ the Debtors will have a Distribution Agreement with Merchants at prices or margins that are generally equal to or lower than the pre-petition prices or margins charged by Merchants. More particularly, the margin will be 8.5% under the Distribution Agreement, the Debtors operated on a 9.5% markup of cost before the Petition Date, which is the equivalent of an 8.7% margin of sale.

50. In addition, the Distribution Agreement can be terminated on 120-days' notice only by the Debtors. The Distribution Agreement is binding on Merchants, and insures that roughly ninety percent (90%) of the Debtors' Food and Supplies will not be disrupted. Without the relief sought in this Motion, the outcome could significantly impair the Debtors' businesses and frustrate the primary goals of chapter 11: the preservation of going concerns and the maximization of estates values. *See Bank of Am. Nat'l. Trust & Savs. Assoc. v. 203 N. LaSalle P'ship*, 526 U.S. 434, 453 (1999)

51. In order to meet its obligations under the Distribution Agreement, Merchants estimates that it will invest \$3,000,000 in Piccadilly proprietary products inventory. Having the proprietary products in inventory is beneficial to the Debtors for a number of reasons, including the cost savings to the Debtors in having its products and the importance of having special made products on hand when needed.

52. Despite protracted efforts after the Petition Date, the Debtors have been unable to secure an alternative source of Food and Supplies at prices that are at or near comparable prices. The Debtors estimate that the Next Best Offer alternative to Merchants would cost the Debtors between \$3.9 million to \$7 million annually.

¹⁷ See Paragraphs 42 through 45 of this Motion.

B. The Court May Authorize the Relief Requested Herein Under Its Equitable Authority and the Doctrine of Necessity

53. The Court may rely on its general equitable powers to grant the relief requested in tills Motion. Section 105 of the Bankruptcy Code empowers the Court to “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code].” A bankruptcy court’s use of its equitable powers under the doctrine of necessity to “authorize the payment of pre-petition debt when such payment is needed to facilitate the rehabilitation of the debtor is not a novel concept.” *Ionosphere Clubs*. 98 B.R. at 175-76.

54. The doctrine of necessity is an equitable doctrine that has existed in bankruptcy law for over 125 years. *See Miltenbergerv. Loansport C. & S.W.R. Co.*, 106 U.S. 311-12 (1882). The doctrine of necessity authorizes payment of a prepetition obligation where such payment is essential to the continued operation of the debtor’s business. *See In re Columbia Gas Sys., Inc.*, 136 B.R. 930, 939 (Bankr. D. Del. 1992). In so doing, the doctrine of necessity “endeavors to reconcile two otherwise irreconcilable objectives of chapter 11: the reorganization of otherwise viable entities that have fallen upon hard times . . . and, at the same time, the equal treatment of all creditors.” *In re United Am., Inc.*, 327 B.R. 776, 781 (Bankr. E.D. Va. 2005).

55. Although the doctrine of necessity is not explicitly codified within the Bankruptcy Code, this equitable doctrine remains a vital component of bankruptcy jurisprudence. *See Midlantic Nat’l Bank v. New Jersey Dep’t of Env’tl. Prot.*, 474 U.S. 494, 501 (1986) (“The normal rule of statutory construction is that if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific.”). “The Supreme Court, the Third Circuit and the District of Delaware all recognize the court’s power to authorize payment of pre-petition claims when such payment is necessary for the debtor’s survival during

chapter 11.” *In re Just for Feet, Inc.*, 242 B.R. 821, 825 (D. Del. 1999); *see also In re Lehigh & New England Rv. Co.*, 657 F.2d 570, 581 (3d Cir. 1981).

56. The doctrine of necessity authorizes the Debtors to satisfy a portion of the Merchants Pre-Petition Claim because such payments are necessary to preserve the value of the Debtors’ estates. The Debtors’ relationships with Merchants is not governed by a contract, and the Debtors have no means to compel future performance by Merchants. Absent the relief sought in this Motion, the Debtors could be denied economic and reasonable access to Food and Supplies or be forced to accept substantially less favorable terms with other food distributors.

C. The Court May Authorize the Relief Requested Herein to Permit the Debtors to Comply with Their Fiduciary Obligations

57. Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, debtors in possession are fiduciaries “holding the bankruptcy estate[s] and operating the business[es] for the benefit of [their] creditors and (if the value justifies) equity owners.” *In re CoServ. L.L.C.*, 273 B.R. 487, 497 (Bankr. N.D. Tex. 2002). Implicit in the fiduciary duties of any debtor in possession is the obligation to “protect and preserve the estate, including an operating business’s going-concern value.” *Id.* There are instances in which a debtor can fulfill this fiduciary duty “only . . . by the preplan satisfaction of a prepetition claim.” *Id.* The *CoServ* court specifically noted the pre-confirmation satisfaction of prepetition claims would be a valid exercise of the debtor’s fiduciary duty when the payment “is the only means to effect a substantial enhancement of the estate . . .” *Id.*

58. As discussed above, the Debtors believe the relief requested in this Motion is vitally necessary to preserve the value of their estates for the benefit of all stakeholders in this Chapter 11 Case. The Debtors’ failure to pay pre-petition claims held Merchants (a) would cost the estates a substantial amount of money by driving up the expense on post-petition Food and

Supplies, and (b) prevent significant disruptions to the Debtors' business operations. *Cf. Just for Feet*, 242 B.R. at 825 (“The Debtors need a continuous supply of inventory . . . Therefore, the court finds that payment of the pre-petition claims of certain trade vendors . . . is essential to the survival of the debtor during the chapter 11 reorganization.”). The Debtors' inability to purchase Food and Supplies at competitive prices, without substantial disruption of their operations, could jeopardize its operations. Clearly, the Debtors' fiduciary obligations would be better served by authorizing the limited relief requested herein, thereby ensuring the Debtors' access to reasonably priced Food and Supplies, and proprietary products, during this Chapter 11 Case.

D. The Requirements of Bankruptcy Rule 6003 Are Satisfied

59. Bankruptcy Rule 6003 authorizes this Court to allow the Debtors to authorize payments to Merchants as provided herein because such relief is necessary to avoid immediate and irreparable harm to the Debtors and their estates. See Fed. R. Bankr. P. 6003(b). Immediate and irreparable harm exists where the absence of relief would threaten the value of the Debtors' estates. *See In re Ames Dep't Stores, Inc.*, 115 B.R. 34, 36 n.2 (Bankr. S.D.N.Y. 1990) (discussing application of immediate and irreparable harm standard as applied to Bankruptcy Rule 4001); *see also In re First NLC Fin. Servs., LLC*, 382 B.R. 547, 549 (Bankr. S.D. Fla. 2008) (“The Advisory Committee commentary [to Bankruptcy Rule 6003] plainly suggests that courts rely on the procedures and advanced case law under Rule 4001(b)(2) and (c)(2) for implementation of new Rule 6003.”).

60. By their very nature, a critical vendor such as Merchants provides essential Food and Supplies upon which the Debtors rely to ensure the seamless delivery of food products to its customers. Absent the relief sought in this Motion, Merchants has indicated that it will withhold essential Food and Supplies entirely. This outcome could substantially reduce the chances for the successful conclusion of the Chapter 11 Case before they have even had a chance to begin.

NOTICE

61. Notice of this Motion has been given to (a) the secured creditor, through Atalaya Administrative, LLC, and its counsel of record, Brent R. McIlwain and David F. Waguespack, (b) the 30 largest unsecured creditors, the identity of which may be amended from time to time, (c) the twenty (20) additional random unsecured creditors, (d) all parties who have requested special notice pursuant to Bankruptcy Rule 2002, (e) counsel for the Unsecured Creditors' Committee, and (f) the Office of the United States Trustee. The Debtors submit that no further notice is necessary for this Court to enter an Order granting the relief requested herein.

WHEREFORE, the Debtors seek a final Order, substantially in the form of **Exhibit A**: (a) that finds that Merchants is a critical vendor of the Debtors; (b) that allows Merchants' Allowed 503(b)(9) Claim, for the value of goods delivered to the Debtors within twenty (20) days of the commencement of these bankruptcy cases, in the amount of \$2,323,585; (c) that allows the previously paid Allowed PACA Claims of Merchants under the Perishable Agricultural Commodities Act, 7 U.S.C. § 499(a) *et seq.*, in the amount of \$159,487; (d) that authorizes the Debtors to immediately pay Merchants' Allowed Unsecured Claim by (i) permitting the application of the Marginal Differential Credit (as described in the Motion), (ii) authorizes the Debtors' Critical Vendor Cash Payment (as described in the Motion), and (iii) the re-application and re-classification, on a dollar-for-dollar basis, of certain post-petition payments previously made by the Debtors to Merchants for purchases of Food and Supplies after the Petition Date (as described in the Motion as the Critical Vendor Reclassified Payment); (e) that provides that all of the payments by the Debtors to Merchants are absolute and final and are without any right of the Debtors or any other party to avoid, recover or recoup any of the payments to Merchants authorized or paid to Merchants by the Order granting this Motion, or to

avoid, recover or recoup, either under chapter 5 of the Bankruptcy Code or otherwise, any transfers or payments made by any of the Debtors to Merchants, (f) that requires Merchants to deliver to Piccadilly Restaurants, LLC an executed Distribution Agreement (substantially in the form of **Exhibit B**), after payment of, and as partial consideration for, the critical vendor cash payment and re-classification payment, and that authorizes Piccadilly Restaurants, LLC to enter into the Distribution Agreement. The Debtors seek other relief to which they may be entitled by law and equity.

Respectfully submitted,

/s/ Elizabeth J. Futrell

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EXHIBITS

EXHIBIT A PROPOSED FINAL ORDER

EXHIBIT B DISTRIBUTION AGREEMENT – TO BE SUPPLIED

EXHIBIT C SUMMARY OF CLAIMS AND CREDIT LINE

EXHIBIT D SUMMARY OF INVOICES COMPRISING SECTION 503(b)(9) CLAIM

EXHIBIT E MARGIN DIFFERENTIAL CREDIT SUMMARY