

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF DELAWARE**

In re:	)	Chapter 11
	)	
FLEMING COMPANIES, INC., et al.,	)	Case No. 03-10945 (MFW)
	)	(Jointly Administered)
Debtors.	)	
	)	Related Docket No's.: 12, 16

**DEBTORS' OMNIBUS REPLY TO (i) OBJECTIONS BY CERTAIN PARTIES TO THE DEBTORS' MOTION FOR AUTHORITY TO PAY PREPETITION CLAIMS UNDER THE PERISHABLE AGRICULTURAL COMMODITIES ACT AND THE PACKERS AND STOCKYARD ACT AND (ii) THE OBJECTIONS BY CERTAIN PARTIES HOLDING PACA AND/OR PASA CLAIMS TO THE DEBTORS' EMERGENCY MOTION FOR AN ORDER AUTHORIZING THE USE OF CASH COLLATERAL AND APPROVING POSTPETITION FINANCING**

The above-captioned debtors and debtors in possession (the "Debtors" or "Fleming") hereby submit this omnibus reply (the "Reply") to (i) objections by certain parties to the Debtors' Motion for Authority to Pay Prepetition Claims Under the Perishable Agricultural Commodities Act ("PACA") and the Packers and Stockyard Act ("PASA") and (ii) the objections by certain parties holding claims under PACA or PASA (the "PACA/PASA Claims") to the Debtors' Emergency Motion for an Order Authorizing the Use of Cash Collateral and Approving Postpetition Financing (the "Financing Motion"). In support of this Reply, the Debtors respectfully state as follows:

**INTRODUCTION**

1. On April 2, 2003, the Debtors filed their Motion for Authority to Pay Prepetition Claims Under the Perishable Agricultural Commodities Act and the Packers and Stockyard Act (the "PACA/PASA Procedures Motion") in which the Debtors sought to establish the following procedures (the "PACA/PASA Procedures") for the review and payment of valid PACA/PASA Claims:

- a. The Debtors will file a report, on notice to parties in interest, listing those PACA and PASA claims, if any, which they deem to be valid;
- b. Absent further order of the Court, such report shall be filed by the Debtors within 90 days of the day any order granting this Motion becomes final;
- c. If the Debtors fail to file such a report within the required period of time, any holder of an alleged PACA or PASA claim may bring a motion on its own behalf, but may not bring such a motion or an adversary proceeding seeking similar relief (including declaratory relief) earlier than 90 days after the day any order granting the Motion becomes final;
- d. All parties in interest shall have the right and opportunity to object to the inclusion or omission of any asserted PACA or PASA claim in connection with such report; and
- e. The Debtors will be authorized to pay all valid PACA or PASA claims pursuant to the above-described report.

2. Various parties (the “Objecting Parties”) have filed objections (the “Objections”) to the PACA/PASA Procedures Motion and/or the Financing Motion. The principal arguments raised by the Objecting Parties are: (a) a PACA/PASA Trust is automatically created when applicable fruits and/or vegetables are supplied; (b) that PACA/PASA funds must be transferred to a segregated PACA/PASA Trust; (c) that PACA/PASA Trust assets are not estate assets and may not be pledged to support the use of cash collateral or to obtain post-petition financing; (d) that PACA/PASA requires immediate payment of the PACA/PASA Trust assets to PACA/PASA Claimants; and (e) that the time requested by the Debtors to review PACA/PASA Claims is unnecessary.

3. As more fully described in the PACA/PASA Procedures Motion, the Debtors do not contest that, where an applicable seller complies with the terms of the PACA and/or PASA statutes, a trust is created and that, in such situation, the assets covered by the trust are not estate assets. However, the Debtors contest the assertion that immediate payment is required under either PACA or PASA, or that PACA/PASA funds must be moved to a

segregated trust. Additionally, the Debtors, as more fully described below, have not had sufficient time to properly analyze the asserted PACA/PASA Claims in these cases.

4. Several Objecting Parties have also argued that, since the trust assets are not assets of the estates, such assets (a) may not be pledged to obtain postpetition financing and (b) do not constitute cash collateral. In the proposed final order approving the Financing Motion (the “Financing Order”), the Debtors make clear, notwithstanding entry of the Financing Order, that PACA/PASA Claimants reserve any trust rights with respect to any assets, including any PACA Trust (as defined therein) interests against non-Debtor third parties under applicable law.

### **ARGUMENT**

#### **PACA/PASA do not require immediate payment**

5. While requiring “prompt payment,” see 7 U.S.C. 7 § 499(b) and 7 CFR §46.2(aa), neither PACA nor PASA speaks in the context of a bankrupt debtor and neither requires immediate payment. 7 U.S.C. § 499(b). As stated in In re Fresh Approach, Inc., 51 B.R. 412, 420 (Bankr. N.D. Texas 1985), when considering a PACA claimant’s request for payment “it is the Court’s task to balance the rights of various Claimants against the Bankruptcy Code’s bias in favor of efforts to reorganize a debtor.”

6. Those cases cited by the Objecting Parties for the proposition that PACA or PASA requires immediate payment are distinguishable as payment in those cases was not required until, at a minimum, several months after the petition date. For example, in Fresh Approach, 51 B.R. at 421-422, the court granted the PACA creditor’s motion for payment of its PACA claim, however, the court recognized that the motion was being heard five months after the petition date and explicitly recognized that the Creditors “repeatedly assured the Court that they do not seek the Debtors’ liquidation”); see also, W.L. Bradley, 75 B.R. at 513 (granting

relief from stay and ordering payment but only after the motion had “been under advisement for a few months.”).

7. As described in the PACA/PASA Procedures Motion, the Debtors intend to make prompt payment to the holders of valid PACA/PASA Claims; however, as more fully described in the Motion, the Debtors are seeking to establish procedures to allow the Debtors time to evaluate PACA/PASA Claims in a manner that will allow them to evaluate and pay valid PACA/PASA Claims while at the same time not interfere with their efforts to stabilize the Debtors’ operations at this critical time and otherwise jeopardize the likelihood of a successful reorganization for the benefit of all creditors.

8. As is more fully described in the Financing Motion and in the Affidavit of Peter S. Willmott, Interim President and Chief Executive Officer of Fleming Companies, Inc. in Support of First Day Motions, the Debtors are experiencing a significant liquidity crisis. Adoption of the proposed PACA/PASA Procedures will, while simultaneously protecting PACA/PASA creditors, minimize the risk of unnecessary litigation and afford the Debtors a much needed opportunity to address their liquidity issues.

**Neither PACA nor PASA requires the creation of a segregated trust**

9. While various courts have taken various approaches to protect the rights of valid PACA/PASA Claimants, the statute speaks of a “non-segregated floating” trust. W.L. Bradley, 75 B.R. at 509. There is no need for a segregated trust in these cases. In their various pleadings, the PACA/PASA Trust Claimants assert that unpaid PACA Trust creditors take priority over all other creditors, secured and unsecured, on the produce buyer’s assets to the full extent of their claim. See Notice of Joinder in Objection of Certain PACA Trust Creditors to Motion for Authority to Pay Prepetition PACA Claims and Supplemental Authorities in Support of Objection citing to Hiller Cranberry Products, Inc v. Koplovsky, 165 F.3d 1 (Mass. 1999). As

noted above, the PACA/PASA Claimants' right to assert this argument and the protection afforded thereby is preserved in the proposed Financing Order.

10. The PACA/PASA Procedures sought by the Debtors are similar to those that have been implemented and which proved very successful in protecting the interests of all parties in the AmeriServe cases. See In re AmeriServe Food Distribution, Inc., et al., Case No. 00-358 (PJW).<sup>1</sup>

11. In AmeriServe, (a) certain parties asserted claims against the debtors under PACA and PASA, (b) the debtors' pre-petition lenders asserted a perfected security interest in the debtors' pre-petition inventory, receivables and cash and (c) the debtors, facing a liquidity crisis, sought to sell the pre-petition inventory and to collect the pre-petition receivables in the ordinary course. The PACA/PASA creditors objected and Judge Walsh determined that the such claimants would be better served under the Debtors' proposed procedures than by filing adversary complaints that could only serve to extend the matter for many months as those adversaries proceeded.

12. On March 17, 2000, Judge Walsh signed the global AmeriServe PACA Order which provided generally that:

- a. The Debtors were required to file a PACA report detailing their analysis of the PACA claims within 50 days of the order (thus the initial report was not required until 96 days after the petition date).
- b. PACA claimants would have 20 days to respond to the Report.
- c. For those claims listed in the Report but not disputed, such claims were deemed to be valid PACA claims.

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<sup>1</sup> Similar procedures were also implemented in the Kmart proceedings. See In re Kmart Corporation, Case No. 02-B-02474 (Sonderby). A copy of both the AmeriServe and Kmart Orders are attached hereto as Exhibit A.

- d. The Debtors were ordered to "use reasonable efforts to pay valid Claims as promptly as possible," but not out of cash collateral without the consent of lenders.
- e. A procedure was established whereby the Debtors and the PACA claimants held weekly conferences to discuss the Debtor's efforts to determine a source of payment of valid claims.
- f. If a claim was disputed, the claimant could file a motion or commence an adversary proceeding to determine such dispute.
- g. If the Report was timely filed, claimants were precluded from filing any motion or adversary proceeding against debtors and debtors' Directors and Officers.

13. On June 8, 2000, four months after the cases were filed, the Court signed a further order approving a claims payment procedure that had been consensually worked out to the agreement of all parties, including the debtors' lenders. It is the Debtors' belief that, if given additional time, the Debtors will be able to address the concerns of PACA/PASA Claimants in a similar manner. This result is one favored by other courts as well.<sup>2</sup> The alternative of requiring immediate segregation of funds and immediate payment would severely impact the Debtors' liquidity and could jeopardize the Debtors' efforts to reorganize and could force a liquidation. This result is not in the best interest of creditors, including PACA/PASA creditors, many of which continue to do business with the post-petition Debtors.

#### **The Debtors Require More Time to review PACA/PASA Claims**

14. The Debtors are the largest multi-tier distributor of consumable package goods in the United States. The Debtors supply products to nearly 50,000 retail locations such as grocery stores, drug stores, discount stores, convenience stores, casinos and gift shops throughout the United States, Canada, the Caribbean and the South Pacific. For the twelve

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<sup>2</sup> See also Fresh Approach, 51 B.R. at 422 (The Court urges [PACA creditors] to accommodate [the] Debtor to the extent possible to arrive at a mutually agreeable pay out plan that would not preclude [the] Debtor's efforts to successfully reorganize.").

months ended December 31, 2002, the Debtors generated total net sales of \$17.6 billion and employed approximately 20,000 workers.

15. Fleming's distribution business involves purchasing, receiving, warehousing, marketing, selecting, loading, delivering and distributing a wide variety of consumable items including groceries, meat, dairy, delicatessen products and packaged goods, as well a variety of general merchandise such as health and beauty care items. Generally, the product mix of the goods the Debtors distributed was approximately 61% groceries, 33% perishables, and 6% general merchandise.

16. These products are purchased from a diverse range of vendors and agricultural growers. Last year, the average number of stock-keeping units, or SKUs, carried in the Debtors' distribution centers ranged from 6,000 to 19,000 based on the size and focus of the specific distribution center.

17. The Debtors' distribution network operates through 50 distribution centers that have a combined total of approximately 20 million square feet of warehouse space. The nationwide scope of the Debtors' distribution facilities combined with the economies of scale offered by centralized procurement and volume pricing make it possible for the Debtors to offer attractive values to large retailers as well as the Debtors' traditional customer base of smaller, independent retailers.

18. In addition to purchasing goods from outside vendors for resale to retailers, the Debtors also offer products under private Fleming brands, including the BestYet®, Comida Sabrosa™, Exceptional Value™, and Nature's Finest® labels. The Debtors also offer products under controlled labels associated with the IGA® and Piggly Wiggly™ brands.

19. Largely independent of its distribution segment, certain of the Debtor entities also maintain retail operations. The retail segment currently operates 100 stores under the Food 4 Less, Rainbow and yes!LESS® trade names, serving primarily middle and lower income consumers.

20. In February 2003, Kmart Corporation, the largest customer of the Debtors' distribution segment, moved in its bankruptcy case currently pending in the Northern District of Illinois to reject its supply agreement with Fleming. In 2002, Kmart accounted for 23% of Fleming's net sales, and Kmart listed Fleming as its single largest supplier of food and consumable products in its bankruptcy pleadings, accounting for \$4.2 billion of total sales per annum.

21. The subsequent termination of the Debtors' agreement with the Kmart Corporation, as well as the disputes over the amount of Fleming's claim for damages, exacerbated existing liquidity issues. Specifically, the negative marketplace perceptions which arose led to tightening of the credit terms offered to the Debtors by their suppliers which, in turn, directly led to decreased revenues for the Debtors. In response, over the past few days the Debtors have been inundated with reclamation notices by their trade vendors and vendors have further tightened credit terms.

22. As of the Petition Date, Fleming was in default under its Prepetition Credit Agreement and all of Fleming's outstanding obligations are immediately due and payable in the amount of \$604 million, together with interest accrued, plus costs, fees and expenses.

23. Furthermore, given the Debtors' recent financial difficulties, they were unable to meet a March 28, 2003 deadline for the filing of its 10-k Annual Report with the



Securities and Exchange Commission. This further triggered certain defaults under certain of Fleming's various indenture agreements.

24. On the Petition Date, Fleming was subject to a scheduled interest payment on the 10 1/8% senior notes in the amount of \$18 million which payment has not been made.

25. Given all of the above, the need for a rapid filing which did not allow the Debtors to adequately prepare prior to filing for many contingencies that must now be addressed post-filing and the Debtors' liquidity crisis, the Debtors do not have the time or the personnel to devote immediate or full-time attention to the evaluation of PACA/PASA Claims without such efforts distracting from the Debtors' reorganization efforts. However, the Debtors have already begun to work with Bankruptcy Management Corporation, the Debtors' Claims and Notice Agent, and AlixPartners, the Debtors' restructuring advisors, to catalog and establish a procedure for reviewing PACA/PASA Claims.

26. While the Debtors are cognizant of the concerns of those holding valid PACA/PASA claims, the Debtors must also fulfill their duties to all creditors as debtors-in-possession by operating their estates for the benefit of those creditors. Therefore, the Debtors require, in addition to the other relief outlined in the PACA/PASA Procedures, time to properly evaluate their PACA/PASA claims. Such additional time will also benefit PACA/PASA creditors as any payments on invalid PACA/PASA Claims improperly reduce the assets of any PACA/PASA Trust.

### **CONCLUSION**

27. The PACA/PASA Procedures when read in conjunction with the other orders and proposed orders in the cases, provide protection to the Objecting Parties while affording the Debtors the opportunity to properly evaluate PACA/PASA Claims and to make payment on such claims in a manner that will minimize the likelihood of such payments

exacerbating the Debtors' current liquidity crisis — all of which is in the best interest of creditors.

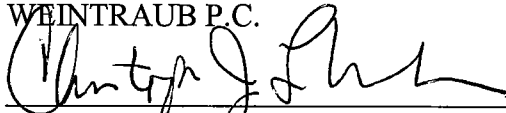
WHEREFORE, the Debtors respectfully request that the court deny the Objections, implement the PACA/PASA Procedures proposed by the Debtors herein, and grant such other and further relief as is just and proper.

Dated: April 17, 2003

KIRKLAND & ELLIS  
James H. M. Sprayregen, P.C. (ARDC No. 6190206)  
Richard L. Wynne (CA Bar No. 120349)  
Bennett L. Spiegel (CA Bar No. 129558)  
Shirley Cho (CA Bar No. 192619)  
Marjon Ghasemi (CA Bar No. 211551)  
777 South Figueroa Street  
Los Angeles, CA 90017  
(213) 680-8400 (Telephone)  
(213) 680-8500 (Facsimile)

and

PACHULSKI, STANG, ZIEHL, YOUNG, JONES &  
WEINTRAUB P.C.



---

Laura Davis Jones (DE No. 2436)  
Ira D. Kharasch (CA No. 109084)  
Scotta E. McFarland (DE No. 4184)  
Christopher J. Lhulier (DE No. 3850)  
Joseph S. Bolnick (CA No. 93542)  
919 North Market Street, 16<sup>th</sup> Floor  
P.O. Box 8705  
Wilmington, Delaware 19899-8705 (Courier No. 19801)  
(302) 652-4100 (Telephone)  
(302) 652-4400 (Facsimile)

[Proposed] Counsel for the Debtors and Debtors in  
Possession