UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re	:	Chapter 11
	:	Case No. 09-10713-KG
G.I. JOE'S HOLDING CORPORATION, *et al.*,	:	Jointly Administered
	:	
Debtors.	:	
	:	
	:	**Related to Docket No. 13**

LIMITED OBJECTION OF WORLDWIDE DISTRIBUTORS TO PROPOSED FORM OF FINAL ORDER GRANTING MOTION OF THE DEBTORS FOR ENTRY OF INTERIM AND FINAL ORDERS: (A) AUTHORIZING THE DEBTORS TO OBTAIN POSTPETITION FINANCING, (B) GRANTING LIENS AND SUPERIORITY CLAIMS, (C) AUTHORIZING USE OF CASH COLLATERAL, (D) GRANTING ADEQUATE PROTECTION TO PRE-PETITION SENIOR LENDERS AND (E) SCHEDULING A FINAL HEARING

Worldwide Distributors ("Worldwide"), by and through its undersigned counsel, files this limited objection (the "Limited Objection") to the proposed form of final order granting Motion of the Debtors for Entry of Interim and Final Orders: (A) Authorizing the Debtors to Obtain Postpetition Financing, (B) Granting Liens and Superiority Claims, (C) Authorizing Use of Cash Collateral, (D) Granting Adequate Protection to Pre-Petition Senior Lenders and (E) Scheduling a Final Hearing (the "DIP Motion") that has been provided to the undersigned. This Limited Objection addresses only the proposal – first raised after the deadline to object to the DIP Motion – by other, subordinate secured parties to strip from the final order an important protection afforded to Worldwide in the first and second interim orders granting the DIP Motion. In short, Worldwide asks only that the final order preserve the protections for Worldwide to which the other parties agreed in the interim orders, recognizing that the Court will determine the nature and extent of Worldwide's claim through a separate declaratory judgment adversary proceeding Worldwide will commence, which it expects to file this week. In support of its Limited Objection, Worldwide states as follows:

Background

1. The above-captioned debtors (the "Debtors") commenced these chapter 11 cases on March 4, 2009 (the "Petition Date"), by filing separate voluntary petitions with this Court. Since the Petition Date, the Debtors have been operating their respective businesses as debtors in possession pursuant to sections 1107 and 1108 of title 11 of the United States Code (the "Bankruptcy Code").

2. On the Petition Date, the Debtors also filed the DIP Motion, seeking approval of debtor in possession financing. In response to concerns raised by Worldwide, the two interim orders granting the DIP Motion included particular protections for Worldwide, primarily in Section 22 of the interim orders. The Court entered the interim order on March 9 and 23, 2009 (Docket Nos. 48 and 106).

3. In the second interim order, the Court set an objection deadline of March 23, 2009 for objections to the DIP Motion and scheduled a final hearing for April 2, 2009, at 10:00 a.m. (EST).

Worldwide's Structure and Relationship to G.I. Opco

4. Worldwide Distributors is a Washington State cooperative corporation based in Kent, Washington. Worldwide's members are retailers. Worldwide operates as a buying cooperative that increases the buying power of its retailer members.

5. Worldwide has two classes of members, Classes A and B. Debtor G.I. Joe's, Inc. (referred to in the DIP Motion as "G.I. Opco"), is a Class A member of Worldwide. Worldwide permits Class A members to order goods directly from approved vendors. A Class A member's purchase order to the vendor requests that the vendor ship the goods to the member, but it

identifies Worldwide as the obligor who will pay the invoice and as the entity to whom the vendor should send the invoice.

6. Worldwide classifies vendors in two classes, also referred to as Classes A and B. If a Class A member orders goods from a Class A vendor, the vendor sends the invoice to Worldwide. From time to time, a vendor may send an invoice to the member, in which case the member will redirect the invoice to Worldwide. But even though the invoice comes to Worldwide and identifies Worldwide as the obligor, the member is obligated to pay the vendor directly, and if the member does so, Worldwide makes no payment. If the member fails to pay the invoice, the vendor requests that Worldwide make payment (Worldwide may not previously have received the invoice), and Worldwide is obligated to pay on behalf of the member.

7. Worldwide's obligation to pay the invoice on behalf of the member arises at least from its historical representation to vendors, in writing and otherwise, that it guarantees all member purchases through Worldwide, and its practice of authorizing and instructing members, at least through the Worldwide member handbook, to make purchases through Worldwide by naming Worldwide as the "bill to" party on the member's purchase orders. Because Worldwide has guaranteed member purchases through Worldwide, members who make Class A purchases through Worldwide owe both an obligation to the vendor to pay the vendor and an obligation to Worldwide to pay the vendor. Both those obligations arise when the vendor extends credit to Worldwide. Thus, at the same time a vendor extends credit for a Class A purchase through Worldwide, the member becomes obligated to Worldwide to pay the vendor, and that obligation gives rise to a claim by Worldwide against the member that is part of the member's indebtedness to Worldwide.

8. If a Class A member orders goods from a Class B vendor, the vendor sends the invoice to Worldwide. Worldwide is obligated to and does pay the invoice. Worldwide then bills the member for the amount of the invoice, and the member is obligated to pay that amount to Worldwide. (On February 18, 2009, Worldwide informed all vendors that it would no longer process invoices to G.I. Opco unless Worldwide had pre-approved the purchase order.) Worldwide's obligation to pay the invoice and the member's obligation to reimburse Worldwide both arise when the vendor extends credit to Worldwide. Thus, at the same time a vendor extends credit for a Class B purchase through Worldwide, the member becomes obligated to reimburse Worldwide, and that obligation gives rise to a claim by Worldwide against the member that is part of the member's indebtedness to Worldwide.

9. In the case of a Class A member's purchases from either Class A or Class B vendors, Worldwide is entitled to and does mark up the amount due from the member by various percentages (which the parties refer to as an "upcharge") to compensate Worldwide for its services and risk.

Worldwide's Perfected, First-Priority Security Interest

10. On April 1, 1978, G.I. Opco executed and delivered to Worldwide a security agreement. In that security agreement, G.I. Opco granted to Worldwide a security interest in all inventory (not just inventory financed by Worldwide) and proceeds and accounts receivable to secure all direct and indirect indebtedness of G.I. Opco to Worldwide.

11. On June 15, 1978, Worldwide filed a UCC-1 financing statement with the Oregon Secretary of State. (G.I. Opco is an Oregon corporation.) The financing statement described inventory and proceeds and products of inventory. Worldwide has continued that financing statement each five years thereafter, and the current expiration date is April 1, 2013.

12. On February 3, 1998, G.I. Opco executed and delivered to Worldwide a second security agreement. In the second security agreement, G.I. Opco granted to Worldwide a security interest in all inventory and proceeds and all equipment and proceeds to secure all G.I. Opco direct and indirect indebtedness to Worldwide. On June 21, 2002, G.I. Opco executed and delivered to Worldwide a third security agreement. In the third security agreement, G.I. Opco granted to Worldwide a security interest in, among other things, all inventory and equipment.

13. Other than Worldwide's financing statement, no unexpired financing statement naming G.I. Opco as debtor predates March 5, 1998.

14. On September 19, 2003, Worldwide filed an amendment to its financing statement describing, among other things, all G.I. Opco equipment and other property, in addition to all inventory.

Measuring Worldwide's Secured Claim Against G.I. Opco

15. Due to the nature of the Class A vendor purchase and payment process, Worldwide can only estimate its claim against G.I. Opco arising from those transactions. On February 19, 2009, G.I. Opco informed Worldwide that its unpaid Class A vendor invoices totaled $3,460,545.37. Worldwide is aware of Class A invoices issued during the 90 days preceding the March 4, 2009, petition date totaling $7,017,706.57. On March 17, 2009, Patrick J. O'Malley, G.I. Opco's chief restructuring officer, orally informed Mark Williams, Worldwide's president, that G.I. Opco then estimated that the total amount of unpaid Class A invoices was $6.8 to $7 million.

16. By contrast to Worldwide's claim based on Class A vendor transactions, Worldwide can determine and has determined that the sum of all Class B vendor invoices that Worldwide has paid, and for which G.I. Opco owes reimbursement to Worldwide, plus charges

billed directly by Worldwide (for goods sold directly by Worldwide and for unpaid monthly member dues) is $1,698,424.36; that amount includes upcharges for all invoices. Even that amount could increase by the amount of invoices for goods shipped to G.I. Opco before the petition date for which Worldwide has not yet received the invoice.

17. Thus, the sum of Worldwide's claim against G.I. Opco is at least $8,498,424.36 (the sum of $6.8 million, the bottom end of the range of Class A invoice amounts according to O'Malley and $1,698,424.36, the amount of Class B vendor invoices paid by Worldwide for which G.I. Opco has not reimbursed Worldwide).

18. Worldwide members are periodically entitled to certain dividends. In the second interim order, the Court authorized Worldwide to offset against its claim a calendar year 2008 dividend of $20,953.00 to G.I. Opco.

The Proposed Final Order

19. As the Court may recall from the March 6, 2009, initial hearing on the DIP Motion, Worldwide objected to the DIP Motion because it requests that the Court permit G.I. Opco to pay the proceeds of the sale of inventory – on which Worldwide has the first-priority security interest – to subordinate secured parties without restriction, creating the risk that the remaining collateral will not suffice to pay Worldwide's secured claim. In return for withdrawing its objection, the Debtors and the subordinate secured parties agreed in the first interim order, among other things, that any amounts they received would be subject to disgorgement to the extent Worldwide's claim exceeds the amount of the escrow the Court establishes for Worldwide's benefit from the collateral sale proceeds. That provision was carried forward in the second interim order without objection by the Debtors, the subordinate secured parties, or any other party.

20. On March 26, 2009, three days after the DIP Motion objection deadline specified in the second interim order, Worldwide received a draft final order that entirely eliminated the disgorgement requirement. Worldwide objected to that deletion and requested that the language from the second interim order be restored. On March 31, 2009, Worldwide received a revised draft final order, which also eliminated the disgorgement right granted by the interim orders, but in its place it added a sentence permitting Worldwide to request at the sale hearing set for April 9, 2009, that the court order that the sale proceeds be subject to disgorgement. The following excerpt is a marked comparison of Section 22(c) of the revised proposed final order against the second interim order:

> (c) For avoidance of doubt, the Debtors, the Pre-Petition Secured Parties and the Term Loan B Secured Parties expressly reserve all rights to object to the validity, priority, enforceability or amount of Worldwide's claims, rights and interests and to assert any defenses thereto, and Worldwide reserves all of its claims, rights and interests. Unless otherwise agreed to by the parties or ordered by this Court, at least the first $5.0 million of net proceeds of a going concern sale, a going out of business sale, any other sale of Collateral after the Commitment Termination Date, or a chapter 7 liquidation shall be held in escrow for potential payment to Worldwide to the extent of its allowed secured claims as determined by final order of this Court to have priority over the Pre-Petition Liens and Term Loan B Pre-Petition Liens, which escrowed funds shall be released only upon further order of this Court. The Pre-Petition Secured Parties, Term Loan B Secured Parties and the Debtors acknowledge that Worldwide asserts that its potential secured claim may be more than $8.5 million and even though the Debtors, Pre-Petition Secured Parties an Term Loan B Secured Parties dispute such assertion, each of such parties and Worldwide shall work with each other in good faith prior to the ~~Final Hearing~~**hearing on the sale of substantially all of the Debtors' assets currently scheduled for April 9, 2008 ("Sale Hearing")** to attempt to reach agreement on the appropriate amount of an escrow for Worldwide's claims up to the full amount of its asserted claim; provided, however, that in the event that they are not able to so agree, **at the Sale Hearing, (i)** notwithstanding the amount of the escrowed sale funds as required by this Order, Worldwide shall retain the right to seek to require the establishment of an escrow of more than $5.0 million, up to the full amount of its asserted claim, ~~and to establish a lien, claim or other payment right in excess of $5.0 million, and the rights of all parties in interest to challenge any such additional escrow, lien, claim or payment right are expressly reserved. Notwithstanding anything to the contrary set forth herein,~~**(ii) Worldwide may also request that** any funds

> received by the Pre-Petition Secured Parties or the Term Loan B Secured Parties shall ~~remain~~**be** subject to disgorgement in the event that the Court determines by Final Order that Worldwide's claim exceeds the amount of the escrow established by order of the Court, even if the full unpaid balance of the DIP Facility, Pre-Petition Facility or Term Loan B Facilities have not been paid as of such date~~. Without limitation, the grounds on which this Court may determine that Worldwide is entitled to receipt of such funds may include a determination that the funds are proceeds of collateral in which Worldwide had as of the petition date, a valid, duly perfected, enforceable and non-avoidable security interest or Lien with priority over that of the~~**, and (iii) the Debtors, Committee,** Pre-Petition Secured Parties~~ and the~~**,** Term Loan B Secured Parties and ~~that such claim, including interest and attorney fees (to the extent allowed pursuant to Bankruptcy Code §506(b)), can not be paid in full from the escrow established by the Court.~~**any other party in interest shall retain all rights to challenge the amount of any escrow, lien, claim or payment or disgorgement right in favor of Worldwide.**

Worldwide again objected to the removal of the disgorgement right, but it offered to agree to entry of the order if the phrase "Worldwide may also request that any funds received by the Pre-Petition Secured Parties or the Term Loan B Secured Parties shall be subject to disgorgement" were changed to "The Pre-Petition Secured Parties or the Term Loan B Secured Parties may request that any funds received by them not be subject to disgorgement," but that request was rejected.

21. On April 1, 2009, just before finalizing and filing this limited objection, Worldwide received a further revision to the final order, which initially appears acceptable to Worldwide. Section 22(c) of the revised order that Worldwide received and finds acceptable states as follows:

> (c) For avoidance of doubt, the Debtors, the Pre-Petition Secured Parties and the Term Loan B Secured Parties expressly reserve all rights to object to the validity, priority, enforceability or amount of Worldwide's claims, rights and interests and to assert any defenses thereto, and Worldwide reserves all of its claims, rights and interests. Unless otherwise agreed to by the parties or ordered by this Court, at least the first $5.0 million of net proceeds of a going concern sale, a going out of business sale, any other sale of Collateral after the Commitment Termination Date, or a chapter 7 liquidation shall be held in escrow for potential payment to Worldwide to the extent of its allowed secured claims as determined by final order of this Court to have priority over the Pre-Petition Liens and Term Loan B Pre-Petition Liens, which escrowed funds shall

be released only upon further order of this Court. The Pre-Petition Secured Parties, Term Loan B Secured Parties and the Debtors acknowledge that Worldwide asserts that its potential secured claim may be more than $8.5 million and even though the Debtors, Pre-Petition Secured Parties an Term Loan B Secured Parties dispute such assertion, each of such parties and Worldwide shall work with each other in good faith prior to the hearing on the sale of substantially all of the Debtors' assets currently scheduled for April 9, 2008 ("**Sale Hearing**") to attempt to reach agreement on the appropriate amount of an escrow for Worldwide's claims up to the full amount of its asserted claim; provided, however, that in the event that they are not able to so agree, at the Sale Hearing, (i) notwithstanding the amount of the escrowed sale funds as required by this Order, Worldwide shall retain the right to seek to require the establishment of an escrow of more than $5.0 million, up to the full amount of its asserted claim, (ii) unless an order is otherwise entered by the Court at such Sale Hearing, any funds received by the Pre-Petition Secured Parties or the Term Loan B Secured Parties shall be subject to disgorgement in the event that the Court determines by Final Order that Worldwide's claim exceeds the amount of the escrow established by order of the Court, even if the full unpaid balance of the DIP Facility, Pre-Petition Facility or Term Loan B Facilities have not been paid as of such date, and (iii) the Debtors, Committee, Pre-Petition Secured Parties, Term Loan B Secured Parties and any other party in interest shall retain all rights to challenge the amount of any escrow, lien, claim or payment right in favor of Worldwide and to request that any funds received by them not be subject to disgorgement in favor of Worldwide.

Limited Objection

22. Worldwide objects to entry of any final order on the DIP Motion that does not contain the same disgorgement language that appears in the second interim order, which the Court entered without objection, or the language in the most recent draft final order Worldwide received on April 1, 2009, which is quoted in the paragraph above. That language, and the other protections for Worldwide in Section 22 of the second interim order, are modest protections for a first-priority secured creditor who is receiving no payments while all collateral proceeds are being paid to a subordinate secured party.

23. In any case, Worldwide has not received adequate notice of the proposed deletion of the disgorgement requirement. In effect, the March 26 draft final order deleting the disgorgement requirement constituted a motion for authority to use Worldwide's cash collateral

without the disgorgement requirement, as to which a final hearing may not be held earlier than 15 days after service of the motion. Fed. R. Bankr. P. 4001(b)(2).

24. Worldwide recognizes that resolution of its claim will require addressing the appropriate amount of an escrow of collateral sale proceeds to pay Worldwide's claim.

25. Worldwide remains available to all the interested parties to resolve this limited objection without Court intervention.

WHEREFORE, Worldwide respectfully requests that this (i) Court deny the DIP Motion unless and until it is modified in accordance with the language set forth in the revised final order received by Worldwide on April 1, 2009, the language of which is quoted in paragraph 21 above, and (ii) granting such other and further relief as may be just and proper under the circumstances.

Dated: April 1, 2009
Wilmington, Delaware

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By: *<u>/s/ Carl D. Neff</u>*

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