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**UNITED STATES BANKRUPTCY COURT
THE SOUTHERN DISTRICT OF NEW YORK**

In re:

JENNIFER CONVERTIBLES, INC.,¹

Debtors.

Chapter 11

Case No. 10-13779 (ALG)

(Motion for Joint Administration Pending)

**DEBTORS' MOTION PURSUANT TO SECTIONS 105(a), 363(c), AND 503(b)(1) THE
BANKRUPTCY CODE FOR AUTHORIZATION TO HONOR PREPETITION
OBLIGATIONS TO CUSTOMERS AND OTHERWISE CONTINUE
CUSTOMER PROGRAMS IN THE ORDINARY COURSE OF BUSINESS**

Jennifer Convertibles, Inc. (“Jennifer Convertibles”) and its affiliated debtors, as debtors in possession (together, the “Debtors”), hereby move this Court for an order authorizing the Debtors to honor prepetition obligations to customers and to otherwise continue customer practices and programs in the ordinary course of business. In support of this Motion, the Debtors respectfully state as follows:

¹ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor’s federal tax identification number, if applicable, are: (i) Jennifer Convertibles, Inc. (4646); (ii) Jennifer Convertibles Boylston MA, Inc. (7904); (iii) Jennifer Chicago Ltd. (0505); (iv) Elegant Living Management, Ltd. (5049); (v) Hartsdale Convertibles, Inc. (1681); (vi) Jennifer Management III Corp. (3552); (vii) Jennifer Purchasing Corp. (7319); (viii) Jennifer Management II Corp. (9177); (ix) Jennifer Management V Ltd. (9876); (x) Jennifer Convertibles Natick, Inc. (2227); (xi) Nicole Convertibles, Inc. (5985); (xii) Washington Heights Convertibles, Inc. (0783).

Background

1. On July 18, 2010 (the “Petition Date”), each of the Debtors commenced with the Bankruptcy Court a voluntary case pursuant to chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”). The Debtors continue to operate their businesses and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. No trustee, examiner or statutory creditors’ committee has been appointed in these chapter 11 cases.

2. Jennifer Convertibles, Inc. was organized as a Delaware corporation in 1986, and is currently the owner of (i) the largest group of sofabed specialty retail stores and leather specialty retail stores in the United States, with stores located throughout the Eastern seaboard, Midwest, West Coast and Southwest, and (ii) seven big box, full-line furniture stores operated under the Ashley Furniture HomeStore brand (the “Ashley Stores”) under a license from Ashley Furniture Industries, Inc.

3. In order to generate sales, the Debtors rely on aggressive pricing, the attractive image of its stores, extensive advertising and prompt delivery. Operations are classified into two operating segments organized by retail concept: Jennifer and Ashley. The Jennifer segment operates the sofabed specialty retail store concept. The Ashley segment is the big box, full line home furniture retail store concept. There are no inter-company sales between segments. The Ashley segment is highly profitable due to its unique sourcing model, whereby once most sales are executed, Ashley’s supplier manages the supply chain process. Under the Ashley sourcing model, the Debtors need for warehouse inventory is reduced, thereby limiting working capital needs and infrastructure requirements. The Debtors’ two operating segments

enable the Debtors to more effectively offer diverse home furnishings and accessories and expand to a broader consumer base.

4. As of the Petition Date, the Debtors' stores include 130 stores operated by the Jennifer segment. During fiscal 2007, the Debtors opened their first Ashley Store. As of the Petition Date, the Debtors operate seven Ashley Stores.

5. As of the Petition Date, the Debtors employ 497 people. There are 336 employees in the Jennifer segment, 114 employees in the Ashley segment and 47 corporate employees. None of the employees are represented by a collective bargaining unit.

6. For the fiscal year ended August 29, 2009, the Debtors' consolidated financial statements showed revenues from continuing operations of approximately \$94,177,000, compared with \$120,131,000 for the fiscal year ended August 30, 2008, and \$132,683,000 for the fiscal year ended August 25, 2007. For the thirty-nine weeks ended May 29, 2010, revenues from continuing operations were approximately \$70,036,000, with \$56,144,000 coming from the Jennifer segment stores, and \$13,892,000 from the Ashley segment stores.

7. Net sales from continuing operations were \$88,845,000 and \$113,073,000 for the fiscal years ended August 29, 2009 and August 30, 2008, respectively. Net sales from continuing operations decreased by 21.4%, or \$24,228,000 for the fiscal year ended August 29, 2009 compared to the fiscal year ended August 30, 2008. The decrease in net sales is attributable to a decline in overall demand within the furniture industry sector due to a poor housing market and an overall weak U.S. economy. Consolidated same store sales from continuing operations (sales at those stores open for the entire current and prior comparable periods) decreased 19.6% for the thirteen weeks ended May 29, 2010, compared to the same period ended May 30, 2009.

8. Specifically, in the Ashley segment, net sales from continuing operations were \$5,106,000 and \$3,363,000 for the thirteen-week periods ended May 29, 2010 and May 30, 2009, respectively. Net sales from continuing operations increased by 51.8%, or \$1,743,000 for the thirteen-week period ended May 29, 2010 compared to the thirteen-week period ended May 30, 2009. The increase is largely attributable to four new Ashley locations open during the thirteen-week period ended May 29, 2010, that were not open during the same thirteen week period last year.

9. In the Jennifer segment, net sales from continuing operations were \$16,375,000 and \$16,987,000 for the thirteen-week periods ended May 29, 2010 and May 30, 2009, respectively. Net sales from continuing operations decreased by 3.6%, or \$612,000 for the thirteen-week period ended May 29, 2010 compared to the thirteen-week period ended May 30, 2009. The decrease is attributable to the decline in overall demand within the furniture industry sector due to the prevailing conditions of the U.S. economy, the current housing market, store closings, and delays in receipt of merchandise from the Debtors' Chinese supplier, all as discussed in greater detail in the other first day motions, filed concurrently herewith.

10. The factual background relating to the Debtors' commencement of these chapter 11 cases is set forth in additional detail in the Declaration of Rami Abada in Support of First Day Motions (the "Abada Declaration") filed contemporaneously with this Motion and incorporated herein by reference.

Jurisdiction

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

12. The statutory predicates for the relief requested herein are sections 105(a), 363, and 503(b)(1) of chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”) and Rules 6003 and 6004 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”).

Relief Requested

13. Prior to the commencement of these chapter 11 cases, in the ordinary course of business and as is customary in the retail industry, the Debtors instituted and engaged in certain activities to develop and sustain a positive reputation and relationship with their customers. To that end, the Debtors implemented various customer programs and policies (collectively, the “Customer Programs”) designed to ensure customer satisfaction, develop and sustain customer relationships and loyalty, improve profitability, and generate goodwill for the Debtors and their products and services. By this Motion, the Debtors request, pursuant to sections 105(a), 363(b), and 503(b)(1) of the Bankruptcy Code, authorization to continue, replace, implement new, and/or terminate the Customer Programs in the ordinary course of business and as the Debtors deem appropriate in their business judgment, and to perform and honor, at the Debtors’ sole discretion, their prepetition obligations thereunder.

14. As part of their cash management system, the Debtors maintain disbursement accounts at certain banks and other financial institutions (the “Banks”).² The Debtors draw upon funds in their disbursement accounts to satisfy their obligations arising from the Customer Programs. The Debtors request that the Court authorize the Banks to receive, honor, process, and pay any and all checks drawn, or electronic fund transfers requested or to be

² The Debtors’ cash management system is discussed in more detail in the Motion for an Order Authorizing Debtors (A) to Continue Existing Cash Management System, (B) to Maintain Existing Bank Accounts and Business Forms, (C) to Continue Intercompany Arrangements, and (D) to Extend the Time to Comply with the Requirements of Section 345(b) of the Bankruptcy Code, filed concurrently herewith.

requested, on the disbursement accounts to the extent that such checks or electronic fund transfers relate to any Customer Programs.

The Customer Programs

15. The Customer Programs are integral to ensure the smooth functioning of the Debtors' businesses. The Debtors believe that they must promptly assure customers of their continued ability to satisfy prepetition and postpetition obligations under the Customer Programs to maintain their valuable customer base, and myriad other important benefits derived therefrom, following the commencement of these chapter 11 cases. Any inability of the Debtors to promptly honor these obligations would be disastrous to the survival of the Debtors as a going concern because of the resulting destruction of goodwill and loss of customer patronage.

16. Refunds. As part of their normal and customary retail operations, and indeed as is customary in retail business generally, from time to time the Debtors issue refunds on items purchased at their stores. These refunds are either in cash, if an item was purchased in cash, or by store creditor or credit card. Refunds total approximately \$14,000 per week, and the Debtors anticipate that subsequent to the Petition Date, these credits and cash refunds will continue at or about the same level.

17. Credit Card Purchases. Many customers purchase merchandise and services from the Debtors using major credit cards (including, among others, American Express, MasterCard, Visa, Discovery and other secondary credit card programs). In connection with this process, the Debtors are parties to certain agreements with credit card companies and processors to which the Debtors pay certain fees in exchange for the Debtors' ability to accept credit card purchases in their stores, subject to certain adjustments, returns and refunds.

18. The Debtors' continued ability to honor and process credit card transactions is essential to the chapter 11 cases, in order to preserve the Debtors' value and maintain customer loyalty. Credit card purchases account for a significant portion of the sales at any given retail store location. If the Debtors were unable to continue to honor credit card transactions, they would lose a major avenue for conducting sales in the ordinary course of their business.

19. Under the terms of their agreements, the Debtors are required to pay the credit card companies and processors fees ranging from one percent (1%) to five percent (5%) of sales for their services, certain of which may have accrued but remain unpaid as of the Petition Date. The fees are generally paid monthly, however, some are paid more frequently depending upon the provider. The Debtors estimate that there will be significant fees owed to the credit card companies on account of prepetition charges. As such, the Debtors request the authority to continue to pay these fees in the ordinary course of their business in order to avoid interruption of these vital credit card processing services in the approximate amount of \$25-50,000.

20. Customer Deposits. The Jennifer segment typically requires a minimum cash, check or credit card deposit of 50% of the purchase price when a sales order is given, with the balance, if any, payable in cash or by bank check, certified or official check, upon delivery of the merchandise. The Ashley segment requires a deposit of 100% of the purchase price when the sale order is given.

21. It is vital that the Debtors be able honor these customer deposits and fill customers' orders. The customers are the lifeblood of the Debtors' operations, and without customer confidence, the Debtors' businesses would have no value. If the Debtors are unable to honor the deposits, the corresponding effect would be disastrous to the ability of the Debtors to

reorganize. As of the Petition Date, the Debtors had approximately \$8.3 million in customer deposits and thus the Debtors request the authority to continue to honor the customer deposits in the ordinary course of their business. Most deposits are within the statutory amount set forth in Bankruptcy Code section 507(a)(7).

22. The Supplemental Program. The Debtors also offer to customers a hybrid lease/purchase supplemental program. Under this program, a finance company purchase the merchandise from the Debtors, and the customer then leases it from the finance company with monthly payments at no interest. All lease/purchase agreements are for twelve months. The finance company charges a 6% discount on all transactions to the Debtors. Because this is a true lease/purchase agreement, the customer may return the merchandise at any time with no recourse to the Debtors. The Debtors are not obligated to take the merchandise back, or give any refunds.

23. This supplemental program is very important to the Debtors' business, as it gives customers the option to finance their purchases. Without this program in place, the Debtors' sales volume would dramatically drop. As such, the Debtors request the authority to continue to offer customers the lease/purchase option.

Basis for Relief

24. As an initial matter, sections 1107(a) and 1108 of the Bankruptcy Code authorize a debtor in possession to continue to operate its business. Section 363(c) of the Bankruptcy Code allows a debtor in possession operating its business pursuant to section 1108 of the Bankruptcy Code to use property of the estate in the ordinary course of business without notice or a hearing. The Debtors respectfully submit that their continuing, renewing, replacing, initiating and terminating their Customer Programs is in the ordinary course of their business and is permitted by Bankruptcy Code sections 1107(a), 1108 and 363(c), without further application

to the Court. However, out of an abundance of caution, the Debtors seek authority to continue, renew, replace, implement, modify, and/or terminate the Customer Programs as they deem appropriate, and to honor their undisputed prepetition obligations in respect thereof, in the ordinary course of business, without interruption, in accordance with prepetition practices.

25. Pursuant to section 503(b)(1) of the Bankruptcy Code, a debtor may incur, and the court, after notice and a hearing, shall allow as administrative expenses “the actual, necessary costs and expenses of preserving the estate.” 11 U.S.C. § 503(b)(1). In addition, pursuant to section 363(c) of the Bankruptcy Code, a debtor may, in the exercise of its sound business judgment and after notice and a hearing, use property of the estate outside of the ordinary course of business. The Debtors believe the use of estate funds to continue the Customer Programs is permitted by sections 503(b)(1) and 363(b) as necessary costs of preserving the Debtors’ estates. Honoring the Customer Programs will enable the Debtors to retain, maintain, and create valuable customer relationships which, will strengthen the Debtors’ business and prospects for a successful reorganization.

26. The Debtors submit that, generally, honoring the terms of Customer Programs, such as customer deposits, are ordinary course transactions for which the Debtors do not need court approval. *See* 11 U.S.C. §363(c). However, to the extent that the customer programs do not represent “ordinary course” transactions, the Court may authorize the continued honoring of the customer programs under 363(b) of the Bankruptcy Code. Section 363(b) of the Bankruptcy Code provides, in relevant part, that “[t]he trustee, after notice and a hearing, may use, sell or lease, other than in the ordinary course of business, property of the estate.” 11 U.S.C. §363(b)(1). Under this section, a court may authorize a debtor to pay certain prepetition claims. *See Ionosphere Clubs*, 98 B.R., 174, 175 (Bankr. S.D.N.Y. 1989) (authorizing payment of

prepetition claims where the debtors articulate “some business justification, other than the mere appeasement of major creditors”); *In re James A. Phillips, Inc.*, 29 B.R. 391, 397 (S.D.N.Y. 1983) (authorizing, pursuant to section 363, a contractor to pay petition claims of some suppliers who were potential lien claimants, because the payments were necessary for the general contractors to release funds owed to the debtors).

27. Further, to supplement the explicit powers described above, section 105(a) 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 this title.” 11 U.S.C. § 105(a). A bankruptcy court’s use of its equitable powers to “authorize the payment of prepetition debt when such payment is needed to facilitate the rehabilitation of the debtor is not a novel concept.” *In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989). “Under 11 U.S.C. § 105, the court can permit pre-plan payment of a pre-petition obligation when essential to the continued operation of the debtor.” *In re NVR L.P.*, 147 B.R. 126, 127 (Bankr. E.D. Va. 1992) (citing *Ionosphere Clubs*, 98 B.R. at 177). The Debtors submit that honoring their prepetition obligations under the Customer Programs, and the continuation of such programs, is imperative to the ongoing operations and viability of the Debtors.

28. The prepetition obligations owed by the Debtors pursuant to their Customer Programs qualify for postpetition payment because if the Debtors do not honor these obligations, the Debtors’ goodwill and going concern value will be severely and irreparably harmed. *See In re Coserv, L.L.C.*, 273 B.R. 487, 497 (Bankr. N.D. Tex. 2002) (noting that one example where the debtor-in-possession can only fulfill its fiduciary duty by pre-plan satisfaction of a prepetition claim are “prepetition ... claims of . . . a customer which, if not honored, could so harm the debtor’s good will as to destroy its going concern value”); *In re Equalnet*

Communications Corp., 258 B.R. 368, 370 (Bankr. S.D. Tex. 2000) (holding that “such a failure to pay and its consequent loss of customer base would impair value of the business on either a going concern or liquidation basis”).

29. The continuity, viability, and revitalization of the Debtors’ businesses is dependent upon the development and maintenance of the loyalty of their customers. The Debtors must be permitted to continue the Customer Programs and honor their prepetition obligations thereunder so as to ensure customer loyalty. The Debtors expect to have sufficient resources available to maintain all of their Customer Programs, to the extent described herein. Considering the potential loss of competitiveness, goodwill, and relationships, and the resulting negative impact on the Debtors’ business and reorganization efforts, the Debtors submit that the requested relief is in the best interest of the Debtors, their estates, and their creditors, and the Motion should be approved in all respects.

30. Accordingly, the Debtors request that they be authorized but not directed, in their business judgment and at their discretion, to (a) perform and honor their prepetition obligations under the Customer Programs as they deems appropriate, and (b) continue, renew, replace, implement new and terminate such of the Customer Programs as they deem appropriate, in the ordinary course of business, without further application to the Court. Any delay in the relief sought indeed, even being forced to advise customers that further judicial relief is necessary, could result in the Debtors' losing a substantial portion of their customer base, diminish the value of their assets, and severely harm their prospects for a successful sale of their assets.

31. Nothing herein is intended or should be construed as an admission as to the validity of any claim against any of the Debtors, a waiver of any of the Debtors' rights to

dispute any claim, or an approval or assumption of any agreement, contract, or lease. If the Court grants the relief sought herein, any payment made pursuant to the Court's order is not intended and should not be construed as an admission as to the validity of any claim or a waiver of any of the Debtors' rights to subsequently dispute such claim and recover such payments.

The Debtors Satisfy Bankruptcy Rules 6003 and 6004

32. Bankruptcy Rule 6003 provides that to the extent relief is necessary to avoid immediate and irreparable harm, a bankruptcy court may approve a motion to “pay all or part of a claim that arose before the filing of the petition” prior to twenty (20) days after the Petition Date. Fed. R. Bankr. P. 6003. As described above, the Debtors’ Customer Programs are essential to the Debtors’ business operations and the maintenance of goodwill with their customers. The Debtors submit that the relief requested in this Motion is necessary to avoid immediate and irreparable harm to the Debtors, as described herein, and that Bankruptcy Rule 6003 has been satisfied. To implement the foregoing successfully and insure the Debtors' operations are not disrupted, the Debtors seek a waiver of the notice requirements under Bankruptcy Rule 6004(a) and the ten-day stay of an order authorizing the use, sale, or lease of property under Bankruptcy Rule 6004(h), to the extent these rules are applicable.

Notice

33. No trustee, examiner or statutory creditors’ committee has been appointed in these chapter 11 cases. Notice of this Motion has been provided to: (i) Office of the United States Trustee for the Southern District of New York; (ii) those creditors holding the thirty (30) largest unsecured claims against the Debtors’ estate (on a consolidated basis); (iii) counsel to Haining Mengnu Group Co. Ltd.; (iv) the SEC; (v) the IRS; (vi) all taxing authorities in relevant jurisdictions; (vii) all attorneys general in relevant jurisdictions; and (viii) any other party

directly affected by this Motion. The Debtors submit that such notice is sufficient under the circumstances.

No Previous Request

34. No previous request for the relief sought herein has been made to this or any other Court.

WHEREFORE the Debtors respectfully request entry of the Proposed Order granting the relief requested herein and such other and further relief as the Court may deem just and appropriate.

Dated: New York, New York
July 19, 2010

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*Proposed Attorneys for the Debtors and
Debtors in Possession*

Exhibit A

Proposed Order

**UNITED STATES BANKRUPTCY COURT
THE SOUTHERN DISTRICT OF NEW YORK**

In re:

JENNIFER CONVERTIBLES, INC.,¹

Debtors.

Chapter 11

Case No. 10-13779 (ALG)

(Motion for Joint Administration Pending)

**ORDER PURSUANT TO SECTIONS 105(a), 363(c), AND 503(b)(1) OF THE
BANKRUPTCY CODE AUTHORIZING THE DEBTORS TO HONOR PREPETITION
OBLIGATIONS TO CUSTOMERS AND OTHERWISE CONTINUE
CUSTOMER PROGRAMS IN THE ORDINARY COURSE OF BUSINESS**

Upon the motion, dated July 19, 2010 (the “Motion”)² of Jennifer Convertibles, Inc. and its affiliated debtors, as debtors in possession (collectively, the “Debtors”), for an order authorizing the Debtors, pursuant to sections 105(a), 363(c), and 503(b)(1) of title 11 of the United States Code (the “Bankruptcy Code”), for an order authorizing the Debtors to honor certain prepetition obligations to customers and otherwise continue Customer Programs, in the ordinary course of business, all as more fully set forth in the Motion; and. upon consideration of the Declaration of Rami Abada in Support of the Debtors’ Chapter 11 Petitions and Request for First Day Relief; and the Court having jurisdiction to consider the Motion and the relief requested therein pursuant to 28 U.S.C. §§ 157 and 1334; and consideration of the Motion and the requested relief being a core proceeding pursuant to 28 U.S.C. § 157(b); and venue being proper before this Court pursuant to 28 U.S.C. §§ 1408 and 1409; and due and proper notice of

¹ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor’s federal tax identification number, if applicable, are: (i) Jennifer Convertibles, Inc. (4646); (ii) Jennifer Convertibles Boylston MA, Inc. (7904); (iii) Jennifer Chicago Ltd. (0505); (iv) Elegant Living Management, Ltd. (5049); (v) Hartsdale Convertibles, Inc. (1681); (vi) Jennifer Management III Corp. (3552); (vii) Jennifer Purchasing Corp. (7319); (viii) Jennifer Management II Corp. (9177); (ix) Jennifer Management V Ltd. (9876); (x) Jennifer Convertibles Natick, Inc. (2227); (xi) Nicole Convertibles, Inc. (5985); (xii) Washington Heights Convertibles, Inc. (0783).

² All Capitalized terms not otherwise defined herein shall have the meanings ascribed to them in the Motion.

the Motion having been provided to the parties listed therein, and it appearing that no other or further notice need be provided; and the Court having determined that the legal and factual bases set forth in the Motion establish just cause for the relief granted herein; and it appearing that the relief requested in the Motion is in the best interests of the Debtors, their estates, and creditors; and upon all of the proceedings had before the Court and after due deliberation and sufficient cause appearing therefor,

IT IS HEREBY ORDERED THAT:

1. The Motion is GRANTED.
2. The Debtors are authorized and empowered in their sole discretion, but not directed, pursuant to sections 105(a), 363, and 503(b) of the Bankruptcy Code, to continue, renew, replace, implement, modify, and/or terminate the Customer Programs, as they deem appropriate, in the ordinary course of business and without further application of the Court.
3. The Debtors are authorized in their sole discretion, but not directed, to honor all prepetition obligations relating to the Customer Programs, in the ordinary course of business, in the same manner and on the same basis as the Debtors honored such obligations prior to commencement of these chapter 11 cases; provided, however, that the relief granted herein shall not constitute an approval or assumption of any Customer Program or related agreement or policy pursuant to section 365 of the Bankruptcy Code.
4. Nothing in this Order or the Motion shall be construed as prejudicing or waiving any rights the Debtors may have to contest the amount or basis of any prepetition or postpetition obligations relating to the Customer Programs.
5. The Debtors' Banks are authorized, when requested by the Debtors in the Debtors' sole discretion, to receive, process, honor and pay all checks drawn on or direct deposit

and funds transfer instructions relating to the Debtors' accounts and any other transfers that are related to the Customer Programs and the costs and expenses incident thereto; provided, however, that sufficient funds are available in the accounts to make such payments; provided further, however, that the Banks may rely on the representations of the Debtors regarding which checks that were drawn or instructions that were issued by the Debtors before the Commencement Date should be honored postpetition pursuant to an Order of this Court and the Banks shall not have any liability to any party for relying on the representations of the Debtors as provided herein.

6. Bankruptcy Rule 6003 has been satisfied.
7. The requirements of Bankruptcy Rule 6004(a) are waived.
8. Notwithstanding any applicability of Bankruptcy Rule 6004(h), the terms and conditions of this Order shall be immediately effective and enforceable upon entry of this Order.
9. The Debtors are authorized to take all steps necessary to carry out this Order.
10. This Court retains jurisdiction to interpret and enforce this Order.

Dated: July __, 2010
New York, New York

UNITED STATES BANKRUPTCY JUDGE