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UNITED STATES BANKRUPTCY COURT
THE SOUTHERN DISTRICT OF NEW YORK

In re:	Chapter 11
JENNIFER CONVERTIBLES, INC.,[1]	Case No. 10-13779 (ALG)
Debtors.	(Jointly Administered)

DEBTORS' REPLY TO THE OBJECTION OF ASHLEY HOMESTORES, LTD. TO DEBTORS' MOTION PURSUANT TO 11 U.S.C. § 365 FOR APPROVAL OF THE ASSUMPTION OF EXECUTORY CONTRACTS WITH LICENSOR, EFFECTIVE AS OF THE EFFECTIVE DATE OF A PLAN OF REORGANIZATION

The debtors and debtors in possession in the above-captioned cases (collectively, the "Debtors") submit this reply (the "Reply") in opposition to the objection (the "Objection") of Ashley HomeStores, Ltd. ("Ashley") to the Debtors' motion pursuant to 11 U.S.C. § 365 for approval of the assumption of executory contracts with licensor, effective as of the effective date of a plan of reorganization (the "Motion"). In support of this Reply, 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).

PRELIMINARY STATEMENT[2]

1. Neither the law nor the facts support Ashley's assertions in the Objection. Because Ashley does not have the facts or the law on their side, they have tried to confuse this Court with a variety of red herrings and inapplicable case law. Indeed, many of the authorities Ashley cites do not stand for the propositions for which they are cited and ignore this Court's position on assumption in accordance with section 365 of the Bankruptcy Code; other cases cited by Ashley are contradicted by more recent and relevant authorities.

2. As set forth more fully below and in the Motion, the Debtors are simply seeking to assume six (6) executory contracts, referred to as trademark usage agreements (the "TUAs"), with Ashley, pursuant to 11 U.S.C. § 365, as of the effective date of a chapter 11 plan of reorganization (the "Plan"). Section 365 of the Bankruptcy Code authorizes a debtor to assume, reject, or assume and assign executory contracts, as discussed more fully in the Motion. The Debtors are not seeking to assign the TUAs. Ashley nevertheless insists that this Court adopt an interpretation of 365(c) based on case law in which the relevant agreement is being both assumed *and* assigned. Despite Ashley's assertions to the contrary, the Southern District of New York does not follow the "hypothetical" test utilized by other jurisdictions, and the Debtors cannot be prohibited from assuming the TUAs based upon a hypothetical inability to assign.

3. The Objection is nothing more than Ashley's attempt to muddle what is actually a very straightforward issue and what the law permits. The Debtors are seeking to assume, not assign, the TUAs in accordance with unambiguous case law in the Southern District of New York. While it is true that the Motion was filed on behalf of the "Debtors", the Debtors do not dispute that Hartsdale Convertibles, Inc. ("Hartsdale") will be the entity assuming the TUAs, and Jennifer Convertibles, Inc., as the parent company, will continue to act as the guarantor as it has

[2] Capitalized terms used but not defined herein shall have the meanings set forth in the Motion.

from the inception of each TUA. This aspect of the arrangement is not new, and Ashley bargained hard for the terms of the TUAs. The Ashley Objection creates the illusion that they are surprised by this relationship, and ignores the fact that it was disclosed on every application that was furnished to Ashley by the Debtors. Through the Objection, Ashley is attempting to impose restrictions that go well beyond the scope of the TUAs. The Debtors see through this illusion, and expect so will this Court.

4. Moreover, the Debtors' operations, including the cash management system, will remain unchanged after the effective date of the Debtors' Plan ("Post-Effective Date"). Ashley's rights and remedies will be unaffected. In addition, the Debtors' financial projections indicate that they will not be receiving credit from Ashley to purchase inventory, but will rather be doing business with Ashley on a cash-on-delivery ("COD") basis.[3] If anything, Ashley will be in a better position than pre-bankruptcy, because thirty day payment terms that existed prepetition have been modified.

5. Ashley's Objection, if taken at face value, argues that section 365(c)(1) authorizes Ashley to terminate the TUAs, thereby rendering chapter 11 a mandatory forfeiture statute. This cannot be true. The Debtors have not defaulted under the TUAs. Nor have they ever been notified by Ashley that they were ever in default. The Debtors are willing provide both a timely cure payment and adequate assurance of future performance. Accordingly, the Debtors should be entitled to assume the TUAs, subject only to later proof of the cure amount.

[3] The Ashley model prides itself on the fast delivery of purchased goods to its customers. Because this is of utmost importance to Ashley, the Debtors believe Ashley should be willing to extend normalized credit terms to the Debtors Post-Effective Date, like they provide for their other licensees.

BACKGROUND[4]

6. The Debtors, in accordance with the TUAs, are the owner and operator of six Ashley stores (the "Ashley Stores"). The TUAs are license agreements between Ashley Homestores, Ltd. and Hartsdale, one of the Debtor subsidiaries in these chapter 11 cases. The Debtors' parent entity, Jennifer Convertibles, Inc., is a guarantor under the TUAs.

7. Prior to the commencement of these chapter 11 cases, the Debtors operated seven Ashley Stores. Post-petition, the Debtors closed one Ashley Store. All six of the remaining Ashley Stores operated by Hartsdale are located in New York.

8. Pursuant to the Plan, the Debtors will (i) assume the remaining six TUAs effective as of the effective date of the Plan, and (ii) cure any outstanding monetary obligations under the TUAs.

RESPONSE

A. Section 365(c) of the Bankruptcy Code Allows The Debtors To Assume The TUAs Without The Consent Of Ashley.

9. The Debtors' Motion provides ample authority demonstrating that (i) the TUAs are executory contracts as contemplated by section 365 of the Bankruptcy Code; and (ii) the Southern District of New York utilizes and favors an "actual test", commonly known as the "Footstar Approach," pursuant to which the New York bankruptcy courts hold that a debtor may assume an otherwise non-assignable agreement, provided that the debtor does not intend to assign such agreement.

10. In arguing that, contrary to unambiguous case law, the TUAs *cannot* be assumed under New York law, Ashley cites to a single Southern District of New York case, Tap Publs. v. Chinese Yellow Pages, 925 F. Supp. 212, 218 (S.D.N.Y. 1996), which was decided almost ten

[4] For a more detailed background, please see the Debtors' Motion at ¶¶ 11-14.

years prior to Footstar, supra. Even assuming Chinese Yellow Pages would be upheld over Footstar, Chinese Yellow Pages cites a single treatise discussing *assignment* of a trademark. As the Motion makes abundantly clear, the Debtors are not seeking to *assign* the Ashley TUAs, but only to *assume* them. See Motion at ¶¶ 22 - 25 ("the Debtors are seeking only to assume, and not to assign, the TUAs"). Thus, the treatise cited by the court in Chinese Yellow Pages is immaterial to the facts at issue herein, and the more relevant Footstar is applicable law.

11. Ashley also cites to a number of courts that have utilized the "hypothetical test" when determining whether or not an executory contract may be assumed pursuant to section 365 of the Bankruptcy Code. Ashley conveniently omits to mention that this test is overtly disregarded by the Southern District of New York. It is undisputed that a majority of courts outside of this District do not follow the "Footstar" approach; a number of cases cited by Ashley in the Objection were also cited by the Debtors in the Motion as examples of jurisdictions where the Debtors would not be allowed to assume the TUAs, regardless of whether the Debtors have actually attempted or intend to assign the TUAs to a third party. See Motion at n. 2. Yet, Ashley attempts to rely on these decisions, which clearly are not precedential in the Southern District of New York. In addition, Ashley cites to In Adelphia Communications Corp., 359 B.R. 65, 72 (Bankr. S.D.N.Y. 2007) as support for their propositions, despite the fact that Adelphia unambiguously supports the "Footstar" approach:

> As the Court advised the parties at the outset of oral argument, though the [objectants'] ability to object to assignment of their franchise agreements without their consent presents a close issue, the law in this district, and by far the better view, is that where the assumption is to be effected by a debtor in possession (as contrasted to a trustee), the right to object to assignment does not by itself affect the right to assume.
>
> That is the clear holding of the decisions of Judge Hardin of this Court in the Footstar cases, which this Court believes it should follow. The Footstar decisions also are consistent in outcome with the decisions of the First Circuit and the Fifth Circuit, and the great majority of the lower courts, which in this Court's view

> reach the proper result. Cases to the contrary, including some Circuit Court decisions that apply a species of "plain meaning" analysis to section 365(c)(1), are in this Court's view incorrectly decided. They give insufficient attention to other provisions of section 365, link concepts that have no relation to each other, and yield results demonstrably at odds with the purposes of the statute.

Id. Ashley has no support for its position in this jurisdiction, as case law from the Southern District of New York is abundantly clear: the Debtors may assume, but not assign, the TUAs.

12. In addition, Ashley argues that because the TUAs were entered into by Hartsdale and Ashley, the "Debtors" may not assume the TUAs. As noted above, the Debtors do not dispute that Hartsdale will be the entity assuming the TUAs. Because these chapter 11 cases have been procedurally consolidated, the Motion was made by the "Debtors," however, the Debtors and Ashley are in agreement that Hartsdale alone will be the entity assuming the TUAs, effective upon the effective date of the Plan.

13. Post-Effective Date, Mengnu will own a majority of the common stock of Jennifer Convertibles, Inc. Post-Effective Date, Jennifer Convertibles, Inc. will remain the guarantor under the TUAs, and will continue in its role as such. Significantly, and notably absent from Ashley's Objection is a claim that there is a change of control provision in any of the TUAs. The simple reason is because no such provision exists. Jennifer Convertibles, Inc. was a public company prior to the filing and will remain one Post-Effective Date. Thus, there was no expectation or requirement as to who would own the publicly held shares of Jennifer Convertibles, Inc. As discussed in greater detail in the Motion, there is no language in the TUAs providing that that a change of ownership or control is deemed to be an assignment or is in any way prohibited. See Motion at ¶ 24 ("Consistent with the notion that Ashley was not concerned about the control of Hartsdale is the statement in the Acknowledgement and Addendum to the TUA 'that the relationship between the Licensor (Ashley) and Licensee (Hartsdale) is not a fiduciary or similar special relationship, but rather is an ordinary commercial relationship

between independent business people with arms length dealings'."). Thus, even *assuming arguendo* that Mengnu's ownership of Jennifer Convertibles, Inc. is deemed to be more than merely a change in Jennifer Convertibles, Inc.'s common stock ownership, such transaction would not affect Hartsdale as licensor. The relief requested by Ashley -- to prohibit the assumption of the TUAs because of a change in ownership of the Jennifer Convertibles, Inc. common stock -- is outside of what they bargained for with the Debtors pre-bankruptcy, and should not be allowed by this Court. The Debtors should not be deprived of their valuable contracts solely by reason of having filed for protection with this Court.

14. In addition, the case cited by Ashley as support for the above, In re Alltech Plastics, Inc., 71 B.R. 686 (Bankr. W.D. Tenn. 1987) was, by Ashley's own admission, based on totally different facts. See Objection at ¶ 16. Specifically, Alltech is a Tennessee case from almost twenty-five years ago in which a chapter 7 trustee was moving to assume and assign a patent license. Unlike in Alltech, here the Debtors are (i) acting as debtors-in-possession, and (ii) seeking only to assume, and not to assign, the TUAs. In accordance with Footstar, supra, and other applicable cases, the law is straightforward and unambiguous: section 365(c)(1) is inapplicable to a debtor in possession which seeks to assume, but not assign, its non-assignable contract. Id. at 569. The court in Footstar was very clear that "no provision of the Bankruptcy Code states in words or substance that references in the Code to 'trustee' are to be construed to mean 'debtor' or 'debtor in possession,'" and "nothing in the Bankruptcy Code prohibits the debtors from assuming the Agreements." Id. at 570-1. The Alltech case is wholly irrelevant to the facts at hand.

15. Finally, while ¶¶ 13 - 14 of the Objection argue that substantive consolidation unjustly saddles Hartsdale with the debt of the other Debtor entities, the issue of a commingled

cash management system, under which the Debtors have always and will continue to operate, has already been addressed by the Court. See Transcript of August 4, 2010 Hearing at 46:8-14 ("The businesspeople obviously want to be comforted that Ashley isn't, to its disadvantage, carrying the entire company. But I have no evidence that that is the case; no evidence that your concerns about use of the trademarks are in any way damaged by the fact that the debtor's continuing to use a prepetition cash management system, that prior to the petition date, the client had no apparent concern about"). Even Ashley has acknowledged the Debtors' commingled operations, as evidenced by the letter from Jennifer Convertibles, Inc. to Ashley, dated February 18, 2010, in which the address of the proposed licensee to the TUAs is listed as Jennifer Convertibles, Inc. The letter has been attached as **Exhibit A**. Additionally, there is nothing in the TUAs that prevents the Debtors from placing liens on the inventory purchased from Ashley. Ashley's concerns are unfounded, and merely another way Ashley is attempting to manipulate the bankruptcy process for their own benefit.

B. The Debtors Have Demonstrated Their Ability to Satisfy Their Cure Obligations Under Section 365(b)(1)(A)&(B) Of The Bankruptcy Code.

16. The Debtors and Ashley are in agreement that the Debtors need to satisfy their cure obligations under section 365(b)(1) before the TUAs can be assumed. See Objection at ¶ 19; Motion at ¶ 35. As set forth in the Motion and in the Financial Projections, the Debtors intend to do so, and will pay Ashley in full for amounts owed on account of the TUAs. The amounts the Debtors believe will satisfy the monetary defaults under the TUAs will be set forth on the Cure Schedule, to be filed with this Court on or prior to January 13, 2011. If Ashley does not agree with the proposed cure amount, procedures for objecting to such amounts are set forth in Article XI of the Debtors' Plan.

17. As to the non-monetary defaults under the TUAs, the Debtors believe it is important to note that prior to the Petition Date, Ashley never expressed issue or concern that the Debtors were not in compliance with the provision in the TUAs requiring financial reporting, and never moved to declare the Debtors in default of the agreements. The Debtors will provide such reports to Ashley on a go forward basis, however, the Debtors do not believe this section of the TUAs needs to be cured prior to assumption. The first and only time Ashley requested such financial reports occurred after the chapter 11 filing, in their letter to the Debtors dated August 17, 2010. Significantly, this letter came after the hearing on August 4, 2010, during which this court stated that "if after a reasonable period of time, your client is seeking some specific information that it has not received that is material, and that can't be worked out by the businesspeople, then you're free to come back and seek some specific relief." See Transcript of August 4, 2010 Hearing at 44:21-25. Ashley never approached the Bankruptcy Court to enforce the financial reporting requirement, and the Debtors do not believe it would be just to compel them to reject these valuable executory contracts simply because of a provision Ashley is only choosing to enforce post-petition. The Debtors therefore request that this Court disallow Ashley's attempt to utilize the bankruptcy process to expand the rights and remedies they already contracted for under each of the seven (7) TUAs.

18. The Objection also goes into great detail about the "Manhattan HomeStore" (as defined in the Objection). Ashley's alleged concerns regarding the Manhattan HomeStore are nothing more than a red herring.

19. Ashley argues that because the Debtors closed the Manhattan HomeStore and will be rejecting the Manhattan HomeStore TUA, the Debtors defaulted under the TUA, and, oddly, that this also caused a default under the six (6) remaining TUAs as well. Ashley offers no basis

for this statement, and there are no cross-default provisions in any of the TUAs that would support this contention. While Ashley may believe that the Manhattan HomeStore was "the most visible location operated by Hartsdale," this simply is not true. The location for the Manhattan HomeStore was a Jennifer Leather store for fifteen years. The Jennifer Leather store was underperforming, so the Debtors decided to close the Jennifer Leather store and instead utilize the facility as a location for one of the Ashley Stores (the Manhattan HomeStore) on a trial basis, despite the fact that the facility had less than 6,000 useable square feet (significantly less selling space than other Ashley store locations). The Manhattan HomeStore was only open for three months, and also failed to perform satisfactorily. Moreover, during this time period the Debtors sought permission of Ashley to open an additional Ashley Store in Astoria, Queens, as Astoria had proven to be a profitable location for one of the Debtors' Jennifer Convertibles stores. Ashley originally approved the Debtors' request, but after the chapter 11 filing Ashley rescinded their approval, thus preventing the expansion into a lucrative location. It is disingenuous of Ashley to complain about shutting down a sub-par store location, while at the same time acting to prevent the Debtors from expanding and opening another store in a location that has proven to be profitable. The Debtors believe they are fully within their rights to reject the underlying TUA for the Manhattan HomeStore, and that doing so does not cause a default of the six remaining TUAs.

C. The Debtors Have Provided The Adequate Assurance Of Future Performance Required Under Section 365(b)(1)(C) Of the Bankruptcy Code.

20. Contrary to what is stated in the Objection, the Debtors can and will provide assurance that they will be able to perform under the TUAs Post-Effective Date. As discussed above, Post-Effective Date the Debtors' financial projections indicate that they will not be receiving credit from Ashley to purchase inventory, but will rather be doing business with

Ashley on a COD basis. Thus, there is zero credit being extended by Ashley, and no reason given for why the Debtors would be unable to perform under the TUAs, and no need for the Debtors to provide any additional adequate assurance. See In re Docktor Pet Center, Inc., 144 B.R. 14, 16 (Bankr. D. Mass. 1992) ("the Court finds that adequate assurance of future performance ... will be provided by shipment to AEP's assignee only on C.O.D. terms").

21. Ashley is also concerned with the commingled cash management system, but as set forth above, the Debtors have always and will continue to operate in such a manner, and the Debtors' operations have already been approved by this Court and acknowledged by Ashley. See Transcript of August 4, 2010 Hearing at 46:8-14, supra; Exhibit A attached hereto. In addition, as discussed in greater detail in subsection "B" above, the Debtors will comply with the terms of the TUAs and provide financial reports to Ashley on a go forward basis, however, their failure to do so in the past should not constitute a default.

22. Finally, should the Court determine that additional adequate assurance of future performance by the Debtors is necessary, the Debtors' Motion provides several examples of what other courts have deemed to be adequate assurance, including the debtor's payment history, presence of a guarantee, presence of a security deposit, evidence of profitability, a plan which would earmark money exclusively for the counterparty, the general outlook in the debtor's industry, and the willingness and ability of a debtor to fund the cure payments. Motion at ¶ 37. The Debtors believe they are able to provide the necessary and appropriate forms of adequate assurance, should Ashley find it necessary, in particular:

- The Debtors have always made timely payments to Ashley in accordance with the 30 day credit terms prepetition, and the COD terms in place post-petition;
- There is a guarantor already in place (Jennifer Convertibles, Inc.);

- The Debtors have provided evidence of profitability in their Financial Projections;
- Ashley is specifically provided for in the Plan;
- The Debtors' Financial Projections show continued operations, increased sales and profitability; and
- The Debtors are willing and able to pay cure amounts to Ashley.

Thus, the Debtors are able to provide sufficient adequate assurance to Ashley, and should accordingly be allowed to assume the TUAs.

CONCLUSION

For all of the above reasons, the Debtors respectfully submit that there is ample authority to support the relief requested in the Motion. Accordingly, the Debtors request that the Court approve the Motion and disallow Ashley's Objection in its entirety.

Dated: New York, New York
January 11, 2011

OLSHAN GRUNDMAN FROME
ROSENZWEIG & WOLOSKY LLP

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EXHIBIT A

JENNIFER CONVERTIBLES

Jennifer Convertibles, Inc., 417 Crossways Park Drive, Woodbury, NY 11797 516/496-1900

February 18, 2010

Mr. Norman L. Blemaster
Ashley HomeStores, Ltd.
One Ashley Way
Arcadia, WI 54612

RE: Proposed Ashley Furniture HomeStore Development at 552-572 86th Street, Brooklyn, NY 11209

Dear Mr. Blemaster:

Per your request, the following is the information you require to go forward in the application process:

1. The complete name of the proposed Licensee. If the name of the Licensee will be your corporation, please send or fax to me a copy of the Articles of Incorporation. If the name of the Licensee will be a limited liability company, please send or fax to me a copy of the Articles of Organization. Please remember that the name of the Licensee may not contain the word " Ashley ", "HomeStore," or " Millennium". Whether the Licensee is a corporation or limited liability company, please forward to me verification that the state has registered the name of the Licensee.

   Hartsdale Convertibles, Inc.
   Articles of Incorporation (already on file)

2. The street address, city and zip code of the proposed Licensee.

   417 Crossways Park Drive
   Woodbury, NY 11797

3. The square footage of the retail floor space of the proposed Ashley Furniture HomeStore location.

   17,600 square feet

4. The street address, city and zip code of the proposed Ashley Furniture HomeStore location and the anticipated month in which you expect the proposed location to soft open.

552-572 86th Street
Brooklyn, NY 11209

Soft opening May 1, 2010

5. The address of the proposed Licensee to which we will send all notices called for in the Trademark Usage Agreement. This may be a post office box if you desire.
   Jennifer Convertibles, Inc.
   Attn: Rami Abada
   417 Crossways Park Drive
   Woodbury, NY 11797

6. The complete name and title of the person who will sign the Trademark Usage Agreement and the Addendum, if applicable.
   Harley Greenfield, Chief Executive Officer

7. The complete name (middle initials required), home address and home telephone number of every person and entity that owns the proposed Licensee and the percentage ownership of each.
   N/A . Hartsdale Convertibles, Inc. is a 100% wholly owned subsidiary of Jennifer Convertibles, Inc., a public corporation (AMEX: JEN)

8. The street address, city and zip code of the corporate bill to location.
   Hartsdale Convertibles, Inc.
   Attn: Accounts Payable Department
   417 Crossways Park Drive
   Woodbury, NY 11797

9. The complete address, size, and number of dock doors of the warehouse to serve the Ashley Furniture HomeStore.
   1 Industrial Road-Suite 141, Dayton, NJ 08810
   79,306 square Feet
   6 Dock Doors

10. The account number(s) for any accounts with Ashley Furniture Industries, Inc.
    Account Number 9972500

Should you have any additional questions, or if you need any additional information, please do not hesitate to contact me.

Sincerely,
JENNIFER CONVERTIBLES, INC.

Harley J. Greenfield
Chairman and CEO