

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

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In re

SUGARFINA, INC., *et al.*,

Debtors.¹
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:
: Chapter 11
:

: Case No. 19-11973 (MFW)
:

: (Jointly Administered)
:

: Hrg. Date: Oct. 3, 2019 at 2:00 p.m. (ET)
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: Obj. Due: Sept. 23, 2019 at 4:00 p.m. (ET)
:

: Related to D.I. No. 62
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**LIMITED OBJECTION OF FEDERAL REALTY INVESTMENT TRUST, THE
FORBES COMPANY, THE MACERICH COMPANY, AND THE RELATED
COMPANIES TO DEBTORS' MOTION FOR ENTRY OF AN ORDER: (I)(A)
APPROVING BIDDING PROCEDURES AND PROTECTIONS IN CONNECTION
WITH A SALE OF SUBSTANTIALLY ALL OF THE DEBTORS ASSETS FREE AND
CLEAR OF LIENS, CLAIMS, ENCUMBRANCES, AND INTERESTS; (B)
SCHEDULING AN AUCTION AND SALE HEARING; (C) APPROVING THE FORM
AND MANNER OF NOTICE THEREOF; (D) APPROVING PROCEDURES FOR THE
ASSUMPTION AND ASSIGNMENT OF CONTRACTS AND LEASES; AND (E)
GRANTING RELATED RELIEF AND (II)(A) AUTHORIZING AND APPROVING THE
SALE OF SUBSTANTIALLY ALL OF THE DEBTORS' ASSETS FREE AND CLEAR
OF ALL CLAIMS, LIENS, INTERESTS, AND ENCUMBRANCES; (B) AUTHORIZING
AND APPROVING THE ASSUMPTION AND ASSIGNMENT OF CERTAIN
CONTRACTS AND LEASES; AND (C) GRANTING RELATED RELIEF**

Federal Realty Investment Trust, The Forbes Company, The Macerich Company, and the Related Companies (the "Landlords") hereby file this objection (the "Objection") to Debtors' Motion For Entry Of An Order: (I)(A) Approving Bidding Procedures and Protections in Connection With a Sale of Substantially All of the Debtors Assets Free and Clear of Liens, Claims, Encumbrances, and Interests; (B) Scheduling an Auction and Sale Hearing; (C) Approving the Form and Manner of Notice Thereof; (D) Approving Procedures for the Assumption and Assignment of Contracts and Leases; and (E) Granting Related Relief and (II)(A) Authorizing And Approving The Sale Of Substantially All of the Debtors' Assets Free

¹ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number or Canadian Revenue Agency, as applicable are (1) Sugarfina, Inc., a Delaware corporation (4356), (2) Sugarfina Interntaional, LLC, a Delaware limited liability company (1254) and (3) Sugarfina (Canada), Ltd. (4480). The location of the Debtors' corporate headquarters is 1700 E. Walnut Ave., 5th Floor, El Segundo, California 90245.

and Clear of All Claims, Liens, Interests, and Encumbrances; (B) Authorizing and Approving the Assumption and Assignment of Certain Contracts and Leases; and (C) Granting Related Relief (the “Sale Motion”),² and respectfully represent as follows:

I. BACKGROUND FACTS

1. Sugarfina, Inc., and affiliated co-debtors (collectively, the “Debtors”), filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Code on September 6, 2019 (the “Petition Date”). Debtors continue to operate their business and manage their properties as debtors-in-possession pursuant to 11 U.S.C. §§ 1107(a) and 1108.³

2. The Debtors lease retail space (the “Premises”) from the Landlords pursuant to unexpired leases of nonresidential real property (individually, a “Lease,” and collectively, the “Leases”) at the locations (the “Centers”) set forth in detail on the attached Schedule A. The Leases are leases “of real property in a shopping center” as that term is used in Section 365(b)(3). *See In re Joshua Slocum, Ltd.*, 922 F.2d 1081, 1086-87 (3d Cir. 1990).

3. The Debtors filed the Sale Motion [D.I. 62] on the September 10, 2019 and requested an expedited hearing to approve the bid procedures relating to the Sale Motion. The Sale Motion proposes the sale of substantially all of the Debtors’ assets to Candy Cube Holdings, LLC (the “Stalking Horse Bidder”), or to a successful overbidder pursuant to an auction of the Debtors’ assets. Landlords do not object to a fair sale process that provides the Debtors an opportunity to maximize the value of their assets. The schedule set forth in the Sale Motion and Bidding Procedures, however, and should be modified to protect the interests of counterparties to contracts and leases. Landlords’ primary objections may be summarized as follows:

- The Bidding Procedures do not specifically require that Landlords receive adequate assurance of future performance information (“Adequate Assurance Information”), much less receive such information prior to filing an objection;

² Terms not otherwise defined here shall have the meanings ascribed to them in the Sale Motion, Bid Procedures, and accompanying documents.

³ Unless otherwise specified, all statutory references to “Section” are to 11 U.S.C. §§ 101 et seq. (the “Bankruptcy Code”).

- The sale timeline does not provide Landlords with sufficient time to review and assess Adequate Assurance Information once it is received;
- To the extent the Debtors seek to move forward with a Backup Bidder, any approval of such Backup Bidder should only occur after a further hearing with an opportunity for parties to object;

4. Landlords request that the Debtors provide Adequate Assurance Information relating to the Stalking Horse Bidder (and any other bidders) far enough in advance of any objection deadline such that Landlords can make a meaningful assessment of such information prior to filing objections. Landlords also object to the proposed schedule for the sale of the Debtors' assets, and the Court should require a schedule that protects the rights of all parties. The current sale schedule is incapable of achieving that goal.

II. ARGUMENT

A. The auction schedule must protect Landlords' due process and Bankruptcy rights.

5. The Debtors propose the following auction and sale schedule:

- September 26, 2019 – Deadline to file and serve Cure Notice.
- October 4, 2019 – Bid deadline.
- October 4, 2019 – Deadline to object to Assumption/Assignment, Cure, and Sale.
- October 8, 2019 – Auction.
- October 10, 2019 – Deadline to object to adequate assurance if successful bidder is not Stalking Horse Bidder.
- October 10, 2019 – Sale Hearing.

6. As proposed, the schedule requires: (a) Landlords' objections to the sale and assumption and assignment to the Stalking Horse Bidder at the bid deadline (and prior to the auction and filing of a proposed sale order); and (b) Landlords' objection to successful bidders other than the Stalking Horse Bidder within a day of the conclusion of the Auction and at the time of the Sale Hearing (ensuring that there is no opportunity to resolve potential issues with such bidder). Pursuant to the Sale Motion, the Debtors seek to close on the sale by the end of October. As a result, the Debtors should move the Sale Hearing back at least a week to allow counterparties the opportunity to review the successful bidder, file more than just a general sale objection, and most importantly, provide time for the parties to informally resolve potential objections. Moving the Sale Hearing as proposed above will still provide the Debtors with two weeks after the Sale Hearing to close.

7. The proposed schedule requires Landlords to file multiple, and potentially unnecessary, objections. The proposed sales schedule renders Section 365(b) all but useless, and the Court should modify the sale process to better protect the rights of Landlords and other parties.

8. Fundamental due process requires that “notice must be reasonably calculated to apprise interested parties of the pendency of an action and to afford them an opportunity to present objections.” Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306, 314 (1950). *See also Sullivan v. Barnett*, 139 F.3d 158, 171 (3rd Cir. 1998) (due process requires notice and a meaningful opportunity to be heard). These due process considerations apply to bankruptcy proceedings. *See, e.g., Matter of Boomgarden*, 780 F.2d 657, 660-661 (7th Cir. 1985). A fair and open sale process must provide Landlords: (i) a meaningful opportunity to review Adequate Assurance Information to assess a successful bidder’s ability to perform under the Leases; and (ii) sufficient time to file a substantive objection and, if necessary, conduct discovery in advance of an evidentiary hearing on the proposed assumption and assignment of the Leases.⁴

B. The Debtors must provide Landlords with Adequate Assurance Information that satisfies Section 365(b)(1).

9. While the Bidding Procedures provides that each bid must contain adequate assurance of future performance information relating to the bidder’s ability to perform under the Debtors’ contracts and leases, the Sale Motion and the Bidding Procedures do not provide bidders with a specific list of the information to be provided. Moreover, the Sale Motion and the Bidding Procedures do not provide when (or if) the Debtors will provide the Adequate Assurance Information to Landlords. Adequate Assurance Information must address the ability of the proposed assignee to perform under the Leases in the future, and Landlords must receive, at a

⁴ To the extent the Sale Motion contemplates the assumption and assignment of the Leases, it initiates a contested hearing subject to Rule 9014 of the Federal Rules of Bankruptcy Procedure (“FRBP”). *See* FRBP 6006(a). Any evidentiary hearing will include witness testimony, and under FRBP 9014, the Court should establish procedures to provide parties a reasonable time to schedule an evidentiary hearing where witnesses will testify. *See* FRBP 9014(e). Any final schedule must establish a reasonable time to deal with evidentiary hearings relating to the assumption and assignment of Leases.

minimum, the following information, and a reasonable timeframe to review such information, if Debtors are to satisfy this burden:

- (i) the specific name of the proposed bidder, the proposed tenant that will act as the assignee, and the proposed name under which the assignee intends to operate the store;
- (ii) the potential assignee's intended use for the space;
- (iii) audited financial statements and annual reports for the past three (3) years, including all supplements or amendments thereto;
- (iv) cash flow projections for the proposed assignee, the proposed assignee's most recent business plan, all cash flow projections for the Leases subject to the assignment request, and any financial projections, calculations and/or pro-formas prepared in contemplation of purchasing the Leases;
- (v) all documents and other evidence of the potential assignee's retail experience and experience operating stores in a shopping center; and
- (vi) a contact person for the proposed assignee that Landlords may directly contact in connection with the adequate assurance of future performance.

10. The Stalking Horse Bidder, and any other party that makes a bid for the Debtors' assets that includes the assumption and assignment of any of the Leases, must provide basic information on their ability to perform under the Leases, the intended use for the Premises, the name of the proposed tenant, a contact person, and their experience operating in a retail shopping center environment. The above is a non-exclusive list of the minimum information that should be included in any bid package that Landlords will need to assess a potential assignee's viability. Landlords reserve the right to request further information that they may deem necessary to make an informed decision as to the ability of the Stalking Horse Bidder, or any other potential assignee of the Leases, to satisfy the requirements of Section 365.

11. The Debtors may not assume and assign the Leases unless there is adequate assurance of future performance under the Leases. 11 U.S.C. § 365(b)(1)(C); *see also* 11 U.S.C. § 365(f)(2). The provision of adequate assurance of future performance is an affirmative duty of the Debtors, and the Debtors bear the ultimate burden of persuasion as to issues under Section 365. *See In re Rachels Industries, Inc.*, 109 B.R. 797, 802 (Bankr. W.D. Tenn. 1990); *see also Richmond Leasing Co. v. Capital Bank, N.A.*, 762 F.2d 1303, 1309 (5th Cir. 1985). The obligation to comply with Section 365(b) and Section 365(f) is unaffected by maneuvering the assumption and assignment process through a sale process.

12. Courts require a specific factual showing through competent evidence to determine whether a debtor demonstrates adequate assurance of future performance. *See e.g., Matter of Haute Cuisine, Inc.*, 58 B.R. 390 (Bankr. M.D. Fla. 1986) (even though experts presented cash flow projections, the court found that insufficient documentary evidence had been presented). To determine whether a party provides adequate assurance of future performance under Section 365(b), courts have looked to sufficient economic backing, economic conditions, certificates, credit reports, escrow deposits or other similar forms of security or guarantee. *In re Belize Airways*, 5 B.R. 152 (Bankr. S.D. Fla. 1980); *In re Lafayette Radio Electronics Corp.*, 9 B.R. 993 (Bankr. E.D.N.Y. 1981). Courts also look to the operating experience of the proposed assignee. *In re Bygaph, Inc.*, 56 B.R. 596 (Bankr. S.D.N.Y. 1986).

13. Section 365 requires that the Debtors provide adequate assurance of future performance information to carry their burden under Section 365, and without receipt of such information, the Landlords cannot assess the *bona fides* of any proposed assignee.⁵ Landlords must receive Adequate Assurance Information prior to any objection deadline for Section 365(b) to have any meaning, and Landlords request that any final schedule require that the Debtors deliver Adequate Assurance Information to Landlords at least seven (7) days before any objection deadline.

C. The Debtors must provide heightened Adequate Assurance Information required by Section 365(b)(3) for shopping center leases.

14. The Leases are shopping center leases and require a heightened demonstration of adequate assurance of future performance than is required by the general provision of Section 365(b)(1)(C). *In re Sun TV and Appliances, Inc.*, 234 B.R. 356, 359 (Bankr. D. Del. 1999). In order to assume and assign shopping center leases, the Debtors must satisfy the heightened requirements set forth in 11 U.S.C. § 365(b)(3)(A) - (D). *See Joshua Slocum*, 922 F.2d at 1086;

⁵ If the Landlords do not have sufficient information (or time) to make a determination as to a proposed assignee, or if the proposed assignee is unacceptable, the Landlords must object to the proposed sale and prepare for an evidentiary hearing. In preparation of such evidentiary hearing, Landlords must conduct expedited discovery, arrange for expert testimony, and file supplemental objections based upon the information gleaned from whatever information the Debtors, or any successful bidder, actually produces.

see also L.R.S.C. Co. v. Rickel Home Centers, Inc. (In re Rickel Home Centers, Inc.), 209 F.3d 291, 299 (3rd Cir. 2000). The heightened adequate assurance requirements that Debtors must satisfy under Section 365(b)(3) include the following:

- the source of rent and that the financial condition and operating performance of the proposed assignee and its guarantors, if any, must be similar to the financial condition and operating performance of the debtor and its guarantor(s), if any, as of the time the debtor became the lessee. *See* 11 U.S.C. § 365(b)(3)(A);
- that any percentage rent due under the lease will not decline substantially. *See* 11 U.S.C. § 365(b)(3)(B);
- that assumption and assignment of the lease is subject to all provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach of any such provision in any other lease, financing agreement, or master agreement relating to such shopping center. *See* 11 U.S.C. § 365(b)(3)(C); and
- that assumption and assignment of the lease will not disrupt the tenant mix or balance in the shopping center. *See* 11 U.S.C. § 365(b)(3)(D).

15. These heightened requirements must be satisfied in connection with an assumption and assignment under Section 365(f)(2)(B). Sun TV and Appliances, Inc., 234 B.R. at 370. Courts also require a specific factual showing through competent evidence to determine whether the Debtors can satisfy Section 365(b)(3)'s heightened adequate assurance of future performance requirements. Matter of Haute Cuisine, Inc., 58 B.R. at 394. The Sale Motion fails to address this heightened standard, and the Bidding Procedures should advise bidders that they must satisfy this heightened standard in order to be eligible to take an assignment of the Leases.

D. Any assumption and assignment must comply with the terms of the Leases.

16. Through the BAPCPA⁶ amendments, "Section 365(f)(1) is amended to make sure that all of the provisions of Section 365(b) are adhered to and that 365(f) of the code does not override Section 365(b)." Floor Statement of Senator Orrin Hatch, 151 Cong. Rec. S. 2459, 2461-62 (daily ed. March 10, 2005). The BAPCPA clarified Section 365 to reflect the Congressional intent that the language of Section 365(f), and any ability to assume and assign the Leases, is subject to the protections of Section 365(b)(1) and (3). It does not modify Section 365(b). Trak Auto Corp. v. West Town Ctr. LLC (In re Trak Auto Corp.), 367 F.3d 237, 243-44

⁶ On October 17, 2005, the Bankruptcy Abuse Prevention And Consumer Protection Act of 2005 (the "BAPCPA") went into effect, clarifying, *inter alia*, the protections that Landlords are entitled to under 11 U.S.C. § 365.

(4th Cir. 2004) (bankruptcy courts could not use the general anti-assignment provision of Section 365(f)(1) to trump the specific protections granted to landlords in Section 365(b)(3)(C)). Therefore, any assignment must remain subject to all provisions of the Leases, including but not limited to those provisions concerning use, radius, exclusivity, and tenant mix and balance.

17. The revisions to Section 365 make it clear that the Debtors cannot use Section 365(f) to render lease provisions unenforceable. While certain provisions may indirectly limit the assignment of the Leases, Section 365(b) specifically protects these provisions. Provisions governing use, radius and the permitted conduct upon the Premises, therefore, are not anti-assignment provisions and Section 365(f) does not render them unenforceable. These are provisions negotiated in good faith that legitimately preserve the Landlords' control over their shopping centers. Section 365(b)(3) no longer permits even insubstantial breaches of provisions such as use, radius, location or exclusivity. These critical lease terms are enforceable under Section 365(b), and this Court should deny any attempted assignment that fails to strictly comply with such provisions, and strike any language in an order that prospectively renders such lease provisions unenforceable.

E. Any sale must not be free and clear of obligations to pay all charges due under the Leases, including unbilled year-end adjustments and reconciliations.

18. The Sale Motion seeks authority for the sale the leases free and clear of liens, claims and encumbrances. See Sale Motion at ¶¶ 64 – 70. The Landlords object to any sale free and clear of the obligations to satisfy unbilled taxes, reconciliations, percentage rent, or other year-end adjustments or unbilled charges that may have accrued under the Leases prior to the assignment of the Leases, but which have not yet been billed. The Debtors continues to be responsible for all such unbilled charges as they come due under the Leases, and the Debtors, or an assignee, must continue to satisfy all charges due under the Leases, including charges which have not yet been billed, reconciled and/or adjusted from pre-petition (or even post-petition) periods. Any assumption and assignment of the Leases cannot cut off the Landlords' right to recover unbilled charges that have accrued, or are accruing, under the Leases. If the sale is not

subject to these reconciliation and adjustment claims, it is unlikely that these legitimate lease charges will ever be paid to the Landlords.

19. Finally, the Leases provide that the Debtors must indemnify and hold the Landlords harmless with respect to any existing claims which may not become known until after the assumption and assignment of the Leases, examples of which may include such claims as personal injuries at the Premises and damage to the Premises or Centers by the Debtors or their agents. Any order approving the assumption and assignment of the Leases must provide that the assumption and assignment is pursuant to the terms of the Leases, including that any assignee continues to be responsible for all such indemnification obligations, regardless of when they arose. In the alternative, the Debtors must provide (by insurance or otherwise) that it can satisfy the indemnification obligations under the Leases for any such claims that relate to the period prior to any assumption and assignment of the Leases.

F. The Court should hold a further hearing for any Backup Bidder.

20. The Sale Motion Bidding Procedures proposes that in the event the successful bidder does not close on the sale, then the sale to the Backup Bidder may be approved without further hearing or Bankruptcy Court order. *See* Sale Motion at Page 16; Bidding Procedures at Page 6. This is inappropriate, as it would require interested parties to file multiple objections in advance of the Sale Hearing that will likely prove unnecessary and irrelevant. To the extent there are objections to the Backup Bidder, it would also require the Court to also conduct likely unnecessary and irrelevant evidentiary hearing on the Backup Bidder. In the unlikely event that the successful bidder fails to close, the approval of a Backup Bidder should only occur after Landlords have had time to review the Backup Bidder's Adequate Assurance Information, and if necessary, object to the ability of the Backup Bidder to provide adequate assurance of future performance. In the event there are objections to the Backup Bidder, the Court should schedule a separate objection deadline and hearing to address any issues concerning the assumption and assignment of the Leases.

G. Landlords object to any waiver of Rules 6004(h) and 6006(d).

21. The Landlords object to any waiver of requirements of Federal Rule of Bankruptcy Procedure (“Rule”) 6004(h) and 6006(d), especially to the extent it adversely affects the Landlords’ appellate rights thereunder. Such a waiver is unnecessary and inequitable. These subsections were added to the Rules specifically to protect the rights of the objecting parties, and thus eliminate the “rush to the courthouse” to obtain stay orders by those parties adversely affected by entry of orders under Sections 363 or 365. Landlords should not have their appellate rights compromised by an unnecessary and advance waiver of these protections, especially where the Debtors seek such a truncated sale process and where Debtors have not established any cause for such a waiver.

III. RESERVATION OF RIGHTS TO RAISE FURTHER OBJECTIONS

22. The Landlords reserve the rights to amend or modify the Objection once the results of the auction become known. Additionally, this Objection is without prejudice to Landlord’s ability to raise further objections at the Sale Hearing and the Landlords reserve all rights to: (i) object to any request to assume and assign the Leases on any grounds, including objections based upon adequate assurance of future performance and the proposed use for any Premises; (ii) object to the form of any asset purchase agreement, form of sale order, or other document executed by the Debtors and the successful bidder; (iii) raise additional objections at any sale hearing; (iv) require any attempted assignment to comply with all terms of the Leases; and (v) seek to continue the Sale Hearing.

23. To the extent consistent with the objections expressed herein, Landlords join in the objections of other lessors and the Official Committee of Unsecured Creditors.

IV. CONCLUSION

The Court should modify the procedures to incorporate the objections raised herein and adequately protect the rights of Landlords, and grant such further relief it deems appropriate.

Dated: September 23, 2019
Wilmington, Delaware

Respectfully submitted,

/s/ Leslie C. Heilman

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