IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	
	)	Chapter 11
SUGARFINA INC., *et al.*,	)	
	)	Case No. 19-11973 (MFW)
Debtors.	)	(Jointly Administered)
	)	**Obj. Deadline: Oct. 21, 2019 @ 4:00 p.m.**
	)	**Hearing Date: Oct. 24, 2019 @ 10:30 a.m.**
	)	Ref. D.I. Nos. 20, 214, 257

THE TAUBMAN LANDLORDS' PRECAUTIONARY OBJECTION TO THE AMENDED NOTICE OF POSSIBLE ASSUMPTION OF CERTAIN EXECUTORY CONTRACTS AND UNEXPIRED LEASES, AND CURE CLAIM OBJECTION

The Taubman Landlords[1], by their attorneys, Susan E. Kaufman and Andrew S. Conway, for their precautionary[2] objection to the Debtors' (for ease of reference herein, "Debtor" in the singular) Amended Notice of Assumption of Lease/Executory Contract Notice of Assumption and Cure Cost with Respect to Executory Contracts or Unexpired Leases Potentially to be Assumed and Assigned in Connection With Sale of Debtors' Assets (the "Notice")(D.I. 257) and state as follows:

1. This is a contested matter, pursuant to Bankruptcy Rules 6006(b) and 9014.

2. Jurisdiction is based upon 28 U.S.C. §1334.

3. This is a core proceeding within the meaning of 28 U.S.C. §157(b).

4. On September 6, 2019 ("Filing Date"), the Debtor filed its petition for relief under Chapter 11 of the United States Bankruptcy Code ("Bankruptcy Code").

[1]The Taubman Landlords are the owners of certain regional retail shopping centers including TRG IMP LLC, a Delaware limited liability company, commonly known as International Market Place, located in Waikiki, Hawaii, and Short Hills Associates, L.L.C., a Delaware limited liability company, commonly known as The Mall at Short Hills, located in Short Hills, New Jersey, at which locations Debtor is a Tenant pursuant to written leases (the "Taubman Leases").

[2]The Taubman Landlords file this "precautionary" objection to the Debtors' notice of possible assumption and assignment of certain executory contracts and unexpired leases because of the relatively short period of time scheduled between the auction date and the hearing date on the approval of assumption and assignment of leases.

I. Assumption and Assignment

5. The Debtor proposes an extremely short period of time between the auction and a hearing to approve the assumption and assignment of leases. At this time, and presumably due to the proposed schedule, the Debtor will have failed to satisfy the requirements of Bankruptcy Code Section 365(b) for assumption of the Taubman Leases in that it has failed to cure existing defaults under the leases. In addition, inasmuch as the Taubman Leases require the Debtor's payment of the landlords' attorneys' fees under these circumstances, in order to meet the requirements of Section 365(b) the debtor must reimburse the landlord for its pecuniary losses. *In re: Tech Hifi, Inc.*, 49 B.R. 876 (Bankr. D. Mass. 1985) (reasonable attorneys' fees required to be paid in order to assume lease).

6. Furthermore, the proposed assignments to the as of yet unidentified assignee has yet to be shown to comply with the provisions of Bankruptcy Code Section 365(f) and, therefore, cannot be approved by this Court. Section 365(f) of the Bankruptcy Code provides, in pertinent part:

> (f)(2) The trustee may assign an executory contract or unexpired lease of the debtor only if--
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> (A) the trustee assumes such contract or lease in accordance with the provisions of this section; and
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> (B) adequate assurance of future performance by the assignee of such contract or lease is provided, whether or not there has been a default in such contract or lease. (Emphasis added.)

Section 365(b)(3) defines adequate assurance of future performance as follows:

> (3) For the purposes of paragraph (1) of this subsection and paragraph (2)(B) of subsection (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance--
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> (A) of the source of rent and other consideration due under such lease, and in the case of an assignment, that the

> financial condition and operating performance of the proposed assignee and its guarantors, if any, shall be similar to the financial condition and operating performance of the debtor and its guarantors, if any, as of the time the debtor became the lessee under the lease;
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> (B) that any percentage rent due under such lease will not decline substantially;
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> (C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other lease, financing agreement, or master agreement relating to such shopping center; and
>
> (D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center. (Emphasis added.)

7. To date, the Taubman Landlords have not received any adequate assurance information from either Sugarfina Acquisition Corp., (the "Stalking Horse") or any potential bidder. Moreover, from a review of the Asset Purchase Agreement for the Stalking Horse filed on October 6, 2019, D.I. 214, the Stalking Horse may designate certain leases no later than 3 days before Closing (after the sale hearing), which leases will be retained by the Debtor for a period of up to 90 days after Closing and may later be designated for assumption or rejection (the "Retained Contracts"). See, Stalking Horse APA § 5.10.

8. The Stalking Horse APA further provides that the Stalking Horse shall be solely responsible for and directly pay for all costs related to the "continuation, operation or holding" of the Retained Contracts. Thus, it appears that this is an attempt to have the Court sanction a defacto assumption and assignment of leases without requiring the payment of cure to the Landlords. See, Stalking Horse APA § 5.10(a)(vi).

9. The Taubman Landlords reserve all rights in connection with these Retained Contracts, including requiring that all rent be escrowed for the entire Retained Contracts Period and that any ultimate assignee of the Taubman Leases comply with all requirements of § 365 as set forth above.

10. Since the Debtor's leases with the Taubman Landlords are of real property in a shopping center, the Debtor has the burden of proof to establish that assumption and assignment will not affect the "use," will not disrupt the tenant mix or balance in the shopping center affected, will not substantially affect future performance of non-monetary obligations of the lessee, and will insure the performance of all monetary obligations under the lease. *In re: Lafayette Radio Electronics Corp.*, 12 B.R. 302 (Bankr. E.D.N.Y. 1981).

11. The Debtor's Notice has failed to establish these requirements and meet its burden of proof. Nowhere in the Debtor's Notice is there a showing that all provisions of the leases including the use and radius clauses will be complied with. Nowhere in the Debtor's Notice is there a showing of any history of an operating performance by the assignee or that the assignee's operating performance will be similar to the operating performance of the Debtor as of the time the Debtor became the lessee under the leases. Finally, nowhere in the Debtor's Notice or any supporting documents is there a showing that the financial condition of the proposed assignee is similar to the financial condition of the Debtor as of the time the Debtor became the lessee under the lease as required by Section 365(b)(3)(A).

In 1984, Congress amended Section 365(b)(3) to stop the assumption and assignment of shopping center leases which would violate the use clause of the lease and disrupt the tenant mix. 130 Cong. Rec. S-8895 (June 29, 1984; Statement of Sen. Hatch). To further protect shopping centers, Congress also amended Section 365(b)(3)(A) to require the debtor to provide adequate assurance that

an assignee has a financial condition and operating performance similar to that of the original tenant when the lease was executed. The legislative history indicates that the purpose of this language was "to insure that the assignee itself will not soon go into bankruptcy and will provide operating and advertising benefits to the other tenants similar to those provided by the original tenant when its lease was executed." 130 Cong. Rec. S-8895 (June 29, 1984), reprinted in App. Pt. 6 Collier on Bankruptcy (16th ed. 2019). *See also, In re: The Casual Male*, 1990 Bankr. Lexis 2277 (Bankr. D. Mass., October 3, 1990). Furthermore, the "party moving to assume [and assign] a lease has the ultimate burden of persuasion that . . . all requirements for assumption [and assignment] have been met." *In re: Rachels Industries, Inc.*, 109 B.R. 797, 802 (Bankr. W.D. Tenn. 1990).

12. The current version of Section 365 differs significantly from the prior version of this section, which provided as follows:

> (C) that assumption or assignment of such lease will not breach *substantially* any provision, such as a radius, location, use, or exclusivity provision, in any other lease, financing agreement, or master agreement relating to such shopping center. . . .

11 U.S.C. § 365(b)(3)(C) (Law. Co-op. 1985), at pp. 225-236. (repealed October 10, 1984) ("the 1978 Version").

Close inspection of these two provisions reveals that the difference between the two versions lies primarily in the deletion of a single, but important, word. The 1978 Version required that the assignment of the lease not "substantially" breach any use clause. In 1984, Congress amended this section by removing the word substantially, in order to overrule certain decisions authored by bankruptcy courts seeking to stretch the language of the section in order to allow debtors' estates to profit by assignments to non-conforming users. This intent is clearly revealed in the legislative history to the 1984 version, which provides, in part:

> The [1982] bankruptcy code currently provides that when a shopping center lease is assumed or assigned, assurances must be given that the lease provisions will not be substantially breached and that the tenant mix will not be substantially disrupted. Unfortunately, courts have misapplied these provisions in ways which have deprived shopping centers and their tenants of the protections which Congress intended to provide them.
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> This bill would delete the word "substantially" from [§365(b)(C)] thus requiring that any clause in the lease be adhered to. It is especially important that any use clause in the lease be strictly adhered to and that the tenant mix not be disrupted. The bankruptcy courts will still retain the flexibility to determine whether or not a proposed new use for the premises falls within any use clause of the lease and whether or not the new use would disrupt the tenant mix. This amendment requires strict compliance with the provisions of the use clauses in shopping center leases and prohibits any changes in the use of the tenant's space not permitted by the use clause. *This amendment is intended to stop courts from creating new leases by changing essential lease terms to facilitate assignments. It is intended to stop the practice of some courts to determine whether there has been a disruption by reference to the amount of space to be assigned as a percentage of the total area in the shopping center.* This amendment is not intended to enforce requirements to operate under a specified trade name.
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> Approximately half of all U.S. retail trade is conducted in shopping centers. Retail merchants in shopping centers depend upon the operation of a carefully chosen mix of stores, all shopping center tenants . . . are using their space in ways not provided for in the lease and which disrupt the tenant mix, the financial health of all of the other merchants and of the shopping center itself can be threatened. This bill will reduce the likelihood that provisions of the bankruptcy code will themselves add to the economic distress of retail merchants in shopping centers.

130 Cong. Rec., §8891 (daily ed. June 29, 1984) (statement of Sen. Hatch) (emphasis supplied).

In other words, Bankruptcy Code Section 365(b)(3)(C) was amended in order to mandate that assignees strictly comply with existing use clauses. *See also* L. Cherkis, *Collier Real Estate Transactions and the Bankruptcy Code* para. 3.01 [6] (1987) ("The amendments to 365(b)(3) were intended to require a prospective assignee of a shopping center lease from a trustee of a debtor-tenant

to adhere to a use clause which reflects the landlord's judgment of the proper tenant mix and synergy in the shopping center, and does not permit a court to change the use prescribed in the lease in order to facilitate an assignment.").

13. The requirement that the use clause provision of the lease must be complied with has been emphasized by the recent bankruptcy code amendments. The ability of the debtor to assign a shopping center lease under section 365(b)(3) is subject to the right of a shopping center lessor to enforce use, radius, exclusivity, tenant mix and similar provisions in its leases. See the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"). The legislative history supports the clear intent of Congress and states:

> "Section 404(b) [of BAPCPA] amends section 365(f)(1) to assure that section 365(f) does not override any part of section 365(b). Thus, section 404(b) makes a trustee's authority to assign an executory contract or unexpired lease subject not only to section 365(c), but also to section 365(b), which is given full effect. Therefore, for example, assumption or assignment of a lease of real property in a shopping center must be subject to the provisions of the lease, such as use clauses."

House Report No. 109-31, Pt. 1, 109th Cong., 1st Sess. 87 (2005).

14. Courts have interpreted Section 365(b)(3)(C) as being a strict requirement that the bankruptcy courts not alter use clauses by approving assignments which effect changes of use. In *In re Rose's Stores, Inc.*, 1995 U.S. App. Lexis 8090 (Decided April 12, 1995) (4th Cir.), the Court rejected a proposed assignee who wished to operate a grocery store in what had been a department store. In addition, two cases interpreting the 1978 version have clearly indicated that the future course of interpreting this section, under the 1984 version, would be governed by an entirely different mandate. One such case is *In re Tech Hifi, Inc.*, 49 Bankr. 876 (Bankr. D. Mass. 1985). In *Tech Hifi*, the landlord was attempting to prevent the debtor, an electronics retail and service store, from assigning its lease to a leather goods retailer. After determining that the 1978 version of

§365(b)(3)(C) does not require a showing that assignment will not breach the lease to be assigned, but only a showing that the assignment will not substantially breach other agreements relating to the shopping center, *Id*. at 879-880, the Court remarked:

> The recent amendment to §365(b)(3)(C) by the Bankruptcy Amendments and Federal Judgeship Act of 1984 require strict adherence to use clauses. Assignment is subject to all use and exclusivity provisions in the particular lease to be assigned . . .

Id. at 879, n. 2. Thus, the Court clearly indicated that it would not allow any deviations from or modifications to a use clause when a trustee assigns a lease under the 1984 version.

An identical view was expressed in *In re Bricker*, 43 Bankr. 344 (Bankr. D. Ariz. 1984). The court in *Bricker* held that the debtor had no rights to an automatic stay pursuant to 11 U.S.C. §362. *Id*. With respect to the 1978 version of §365(b)(3)(C), the court noted that a new rule would apply to future changes in use:

> Apparently feeling this provision has been misapplied to deprive shopping centers of use restriction protections, Congress deleted the word "substantially" from §365(b)(3)(C) in the Bankruptcy Amendments and Federal Judgeship Act of 1984. H.R. 5174, Title III, Subtitle C. 130 Cong. Red. H. 7480 (June 29, 1984). Thus, strict adherence to use restrictions is mandated for future cases.

Id. at 347, n. 4. Again, this language indicates that the slightest deviation from a lease's use clause will not be permitted in order to effect an assignment.

15. The debtor has the burden of proof under Section 365(b)(1) of the Bankruptcy Code. *In re Memphis-Friday's Associates*, 88 Bankr. 830, 840-841 (Bankr. W.D. Tenn. 1988); *In re Lafayette Radio Electronics Corp.*, 12 Bankr. 302, 307 (Bankr. E.D.N.Y. 1981). *See also In re TSW Stores of Nanuet, Inc.*, 34 B.R. 299, 308 (Bankr. S.D.N.Y. 1983) (The court denied the application to assign the lease where the debtor had "failed to establish that the assumption and assignment of its shopping center lease [would] not disrupt substantially any tenant mix or balance in the shopping

center.")

16. The Taubman Landlords entered into the Taubman Leases with a known entity which at the time exhibited a strong financial position and demonstrated a tradition of effective and experienced management. Without a showing that the assignee has a similar financial capacity, has a similar track record with regard to managerial experience with this type of operation, and plans to continue to operate the enterprise in a manner consistent with the restrictions of the leases, it is patently unfair and violative of the requirements of Bankruptcy Code Section 365 to permit the Debtor to assume and assign the Taubman Leases pursuant to the motion currently on file.

17. Further, no evidence of adequate assurance has been offered by the Debtor to date and it is unclear whether the purchasers will be a new or established entity. Section 365(l) provides as follows:

> (l) If an unexpired lease under which the debtor is the lessee is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the debtor's obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.

If the proposed assignee is a newly-formed company, the Taubman Landlords assert that the Court should at the very least require a security deposit in the amount of six (6) months' rent and other charges and a two-year guaranty from a solvent parent corporation.

II. Cure Claims Objection

18. Bankruptcy Code Section 365(b)(2), governs the financial obligations of a debtor which wishes to assume and assign a lease. Section 365(b) provides in pertinent part as follows:

> (b)(1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee—

> (A) cures, or provides adequate assurance that the trustee will promptly cure, such default;
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> (B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and
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> (C) provides adequate assurance of future performance under such contract or lease.

(Emphasis added).

19. The Taubman Landlords assert that the requirements of Section 365(b)(1)(B) include compensation to the landlord for sums incurred for attorneys' fees in connection with the bankruptcy case. *See, In re: F&N Acquisition Corp.*, 152 B.R. 304 (W.D.Wash. 1993); *In re: Westworld Community Healthcare, Inc.*, 95 B.R. 730 (C.D.Cal. 1989); *In re: Ryan's Subs, Inc.*, 25 Bankr. Ct. Dec. 649 (W.D.Md. 1994); and *In re: Child World, Inc.*, 161 B.R. 349 (S.D.N.Y. 1993) (Section 365(b)(1)(B) allows for recovery of attorneys' fees if based upon the language of the lease). The Taubman Leases require the reimbursement of attorneys' fees in connection with proceedings of this kind.

20. Pursuant to the terms of section 365 of the Bankruptcy Code, the Debtor can only assume and assign what rights it has under the Taubman Leases.

21. The cure amounts necessary to assume the Taubman Leases with the Debtor through October 11, 2019, not including pecuniary losses incurred by the Landlords, additional amounts due after October 11, 2019, and year-end adjustments for common area maintenance, taxes, and percentage rent are as follows:

Center	Debtors' Proposed Cure Amount	Taubman Landlords' Proposed Cure Amount	Taubman Landlords' Attorneys' Fees	Taubman Landlords' Total Cure Amount
International Market Place	$27,585.18	$37,345.12	$2,500.00	$39,845.12
The Mall at Short Hills	$21,014.36	$31,401.97	$2,500.00	$33,901.97

Copies of Account Status Reports showing all amounts due and owing are attached hereto as "Exhibit 1."

22. The Taubman Landlords reserve their rights to amend and supplement this Precautionary Objection to the Amended Notice of Possible Assumption and Assignment of Certain Executory Contracts and Unexpired Leases, and Cure Claim Objection (the "Cure Claim Objection"), as additional amounts become due under the Taubman Leases with Debtor.

23. Further, in addition to the cure amounts listed above, the Debtor or Buyer, as applicable, must be liable for, among other things, post-petition rent and other charges under the Taubman Leases through closing or assumption or rejection of the Taubman Leases, and Buyer must be liable for, among other things: (a) certain amounts due and owing under the Taubman Leases, but which may be unbilled as of the date hereof, including but not limited to year-end adjustments for common area maintenance, taxes and similar charges; (b) any regular or periodic adjustment of charges under the Taubman Leases which were not due or had not been determined as of the date of this objection; (c) any percentage rent that may be due under the Leases; (d) any non-monetary defaults; and/or (e) insurance and indemnification obligations under the Taubman Leases.

WHEREFORE, the Taubman Landlords request that the Debtor's motion to sell all leases, assume and assign the Taubman Leases and establish cure amounts be denied, and in the event of assumption of the leases that the Debtor be required to cure all outstanding defaults, that the cure

amounts be established in the amounts set forth above, that the assignee post security deposits as requested herein, and provide for an acceptable guaranty, that the order approving the assignments make clear, that the leases are being assumed and assigned as is, that the Taubman Landlords be awarded their costs and attorneys' fees incurred in connection with this objection, and granting such other and further relief as may be appropriate in the circumstances.

Respectfully submitted,

Dated: October 15, 2019

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