

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re:

SUGARFINA INC., *et al.*,

Debtors.

Chapter 11

Case No. 19-11973 (MFW)

(Jointly Administered)

Ref. No. 21

**OBJECTION AND RESERVATION OF RIGHTS
TO ENTRY OF A FINAL ORDER APPROVING DEBTORS' MOTION ORDER (I)
AUTHORIZING THE DEBTORS TO OBTAIN POSTPETITION SECURED
FINANCING, (II) GRANTING LIENS AND SUPERPRIORITY ADMINISTRATIVE
EXPENSE STATUS, (III) GRANTING ADEQUATE PROTECTION, (IV) MODIFYING
THE AUTOMATIC STAY, AND (V) AUTHORIZING THE DEBTORS' USE OF CASH
COLLATERAL AND (VI) SCHEDULING A FINAL HEARING**

Bristol Investment Fund, Ltd. ("Bristol") hereby submits this objection and reservation of rights to the *Debtors' Motion for Entry and Approval of Interim and Final Orders (i) Authorizing The Debtors To Obtain Postpetition Secured Financing, (ii) Granting Liens And Superpriority Administrative Expense Status, (iii) Granting Adequate Protection, (iv) Modifying The Automatic Stay, And (v) Authorizing The Debtors' Use Of Cash Collateral And (vi) Scheduling A Final Hearing* [D.I. 21] ("DIP Motion"). In support of this Objection, Bristol respectfully states as follows:

1. Bristol is a party in interest and creditor in the Debtors' cases, holding an unsecured claim in the amount of approximately \$105,095.89 against Sugarfina, Inc, plus other unliquidated damages Bristol may have in connection with the prepetition negotiation of a potential DIP and sale transaction with the Debtors.

2. Prior to the Petition Date and again prior to filing this Objection, Bristol attempted to engage the Debtors regarding the terms of a superior DIP financing and sale

proposal. Bristol's attempts were consistently rebuffed by the Debtors and their advisors. As set forth below, Bristol remains willing and able to fund this chapter 11 case and allow for a sale process that will maximize value.

3. The DIP Facility contains features which shock the conscience, including (i) an effective interest rate on the loan that exceeds 75%, (ii) a "success fee" arrangement which would allow the proposed staking horse buyer (a minority \$1 million participant in the DIP Facility) to credit bid the second lien lender's \$11 million second lien debt, in order to freeze out other bidders (and prior to the investigation period of any party in interest to challenge) and (iii) arbitrary deadlines and an expedited process to further chill bidding.

4. At the first day hearing, the Court properly questioned many of the DIP Facility's terms and denied interim approval of many aspects of the DIP Facility.

5. Fortunately, the Debtor can secure financing on far less onerous terms, which were offered in the past and which are now being offered again. See, In re Reading Tube Indus., 72 B.R. 329, 332 (Bankr. E.D. Pa. 1987) (Bankruptcy Code section 364(d) "requires the Debtor to demonstrate that less onerous postpetition financing was unavailable.")

The DIP Motion and Sale Process

6. On September 9, 2019 (the "Petition Date"), the Debtors commenced the above-captioned bankruptcy cases.

7. A formation meeting for the Official Committee of Unsecured Creditors is scheduled for September 17, 2019.

8. Under the DIP Motion, the Debtors seek final authority to obtain a senior secured, super-priority revolving credit facility in the aggregate amount of \$4.0 million, inclusive of a \$600,000 roll up of pre-petition debt (the "DIP Facility") from SFCC Loan Investors, LLC,

(“SFCC”) and Candy Cube Holdings, LLC (“Candy Cube”, and together with SFCC, individually and collectively, “DIP Lender”). SFCC is providing 75% of the DIP Facility and Candy Cube, the proposed stalking horse purchaser, is allegedly providing 25% of the DIP Facility.

9. The purported purpose of the DIP Facility is to finance the Debtors’ bankruptcy process. However, while cash appears to be necessary to fund the process, the egregious terms, milestones and undisclosed agreements are designed to ensure no auction ever occurs.

10. On September 11, 2019, the Debtors filed a motion [Dkt. 62,] seeking to approve, among other things, bidding procedures and a convoluted sale transaction to Candy Cube for a headline value of \$13 million (minus seven categories of price deductions). The DIP Facility requires a sale process to occur in approximately 30 days and contemplates a bid deadline on October 4, 2019 (10 days after the Bidding Procedures Hearing, and 25 days from Petition Date), an auction on October 8th (14 days after the Bidding Procedures Hearing, and 29 days from Petition Date), and a proposed sale hearing on October 10th (16 days after Bidding Procedures Hearing, and 31 days from Petition Date). As will be set forth in further pleadings, the Candy Cube APA is, like the DIP Facility, an overly complicated, smoke and mirrors transaction, that is not as advertised.

11. According to the Debtors, on September 28, 2018, they entered into a \$4.4 million Loan and Security Agreement with Avidbank, which was subsequently assigned to SFCC. The DIP Motion alleges that as of the Petition Date, approximately \$5.0 million remains outstanding under the SFCC Facility.

12. On November 28, 2018, SGRI entered into a Note Purchase Agreement with Goldman Sachs (the “Goldman Sachs Facility”) for a principal amount of \$10.0 million, subject to a Lien Subordination Agreement with Avidbank (now SFCC).

13. Upon information and belief, one or both of the foregoing loans may have insider personal guarantees associated with them.

14. Among its more offensive terms, the DIP Lender/Stalking Horse Buyer requested the following fees:

- (a) Origination Fee. On the Closing Date, a fully earned, non-refundable origination fee of an amount equal to two percent (2.0%) of the DIP Facility Commitments, payable out of the *first* Advance made under the DIP Agreement;
- (b) Repayment Premium. On the Maturity Date (including upon any acceleration by the DIP Lender of the DIP Obligations under the DIP Agreement), the Debtors agree to pay a premium to the DIP Lender equal to (i) 1.125 times the amount of the DIP Facility Commitments, less (ii) the aggregate amount of (A) the fee set forth in Section 2.6(a), and (B) interest actually paid to the DIP Lender by such date in accordance with the terms of the DIP Agreement...
- (c) Success Fee. Upon the occurrence of the Maturity Date, seven percent (7%) of the greater of (i) the aggregate amount of cash proceeds in excess of two million dollars (\$2,000,000) that Goldman Sachs actually receives ... and (ii) if Candy Cube is the successful purchaser of the Debtors’ assets, the sum of (x) the amount of any indebtedness assigned by Goldman Sachs to Candy Cube that is used by Candy Cube to credit bid, plus (y) the amount of cash proceeds in excess of two million dollars (\$2,000,000) that Goldman Sachs actually receives on account of obligations arising under the Goldman Sachs Facility... (the “**Success Fee**”), to be paid by Debtors out of distributions that would have otherwise been payable to Goldman Sachs. (emphasis added)

15. These fees are unconscionable, not customary or market, and are particularly troublesome given the Debtors’ fiduciary duties and the better financing alternatives

available. The Success Fee structure is anti-competitive in nature and possibly the result of a collusive agreement. Bristol will seek expedited discovery to address these issues.

16. Notably, at the first day hearing, counsel for the parties did not defend the Success Fee and the Repayment Premium as “fair” and “reasonable.” Instead, adjectives like “creative,” “multifaceted” and “funky” were used.

17. Properly, the court questioned the nature and extent of the fees the reasoning behind the “Success Fee”, under which Candy Cube, as a minority participant in the DIP Facility, allegedly a \$1 million participant, could chill bidding by (i) receiving approximately \$11 million of Goldman Sachs credit bid rights at the auction and (ii) the DIP Lender could be repaid 7% of its bid after an auction, a right granted to no other bidder.

18. The “Success Fee” of the DIP Facility is designed to eliminate two key protections to the estate. First, if approved, the DIP Facility will permit a credit bid well in advance of the expiration of the “challenge period” under the Local Rules. Courts in this District typically do not allow for a DIP financing to eliminate the challenge periods under the guise of an expedited sale, and the Court should not allow for it in this case. Second, the Success Fee does not comport with the plain terms of Bankruptcy Code section 363(k), which only permits the “holder” of the secured debt to “bid at such sale, and, . . . offset such claim against the purchase price of such property.” Candy Cube cannot satisfy these statutory requirements, and as a result, the Success Fee cannot be approved, as it violates the clear terms of section 363(k).

19. At the first day hearing, after the Court’s questions about how the extraordinary fees were arrived at and why Goldman would ever agree to such terms, one of the explanations was that Goldman was willing to accept such terms to “lock in” a recovery of \$2 million. It appears that Goldman Sachs, perhaps unwittingly or by being misled, was induced to

agree to these terms because they were told there were no alternatives. As explained below, it appears Goldman will earn far more if this DIP Facility is not approved and a cash auction is allowed. To protect Goldman Sachs, Bristol is prepared to offer the replacement DIP that will advance to Goldman \$3 million in adequate protection payments (\$1 million more than the current DIP Facility), and allow it to also obtain the upside from proceeds of a fair and competitive auction.

Bristol's Efforts to Become a Replacement or Additional DIP Lender

20. Bristol initially approached the Debtors months ago, with a proposal to offer DIP financing for the Debtors operations and purchase the assets for \$30 million. After diligence, the proposal was reduced to \$20 million. On or around August 9, 2019, Bristol was told that unless its bid was at least \$20 million and had no priming associated with it, the estate had a "better deal" and discussions were halted. Bristol was also told not to contact Avid or Goldman Sachs. It appears that Bristol was misled, as the current DIP Facility both contains priming and is also for far less than \$20 million.

21. On August 14, 2019, weeks before the filing, Bristol contacted the Debtors again, asking about the status, and again reiterating that it was interested in a transaction. Attached hereto as Exhibit A is a copy of the August 14, 2019 email. The Debtors did not respond nor engage in any discussions with Bristol. Had they responded, they would have learned that the Debtors were positioned to obtain DIP financing on far better economic terms and a purchase offer for more value.

22. Upon reading the DIP Motion, Bristol sent yet another term sheet offering an improved DIP Facility. Attached as Exhibit B is a copy of the term sheet that was sent to the Debtor on September 10, 2019. It provides for additional liquidity to conduct an appropriate sale

process, with a DIP Facility of \$5 million (versus \$4 million), at 6 % interest (versus 8%), **with none of the fees** and onerous terms the existing DIP Facility contains. Once again, the Debtors did not respond to this term sheet or engage in any discussions about an alternative DIP loan proposal.

23. Bristol remains interested in becoming the replacement postpetition lender on unquestionably better terms and on terms that will allow a fair auction process.

24. Based upon review of the transcripts in the case and pleadings filed, Bristol is willing provide an improved loan on the following terms (the “Replacement DIP Facility”):

- (i) **DIP Facility Amount:** \$12,000,000 term loan, which shall be used as follows:
 - \$4 million to fund the existing Budget and repay any DIP advances previously made to funds the Budget;
 - \$5 million plus accrued interest satisfy the SFCC pre-petition loan in full, in an amount to be determined by the Court; and
 - \$3 Million to pay adequate protection to Goldman Sachs (\$1 million more than Goldman has agreed to accept from SFCC for its entire obligations).
- (ii) **Interest Rate:** 6%
- (iii) **Origination Fee:** *NONE*
- (iv) **Repayment Premium:** *NONE*
- (v) **Success Fee:** *NONE*
- (vi) **Budget:** Borrower will comply with the terms of the existing debtor in possession budget (the “**DIP Budget**”) approved by the Bankruptcy Court in the Interim Order as may be amended.
- (vii) **DIP Collateral and Superpriority Claims:** The DIP Facility will be secured by a senior secured priming lien and security interest in all of the assets of the Debtors and non debtor affiliates whether consisting of real, personal, tangible or intangible property (collectively, the “**DIP Liens**”) (collectively, the “**Collateral**”),

subject only to the same carve out approved in the existing DIP Loan (the “**Carve Out**”)

The Purchaser will be granted an allowed superpriority administrative claim (the “**DIP Lender Superpriority Claims**”) in accordance with section 364(c)(1) of the Bankruptcy Code, having a priority in right of payment over any and all other obligations but shall be subject to the Carve Out.

- (viii) **Adequate Protection To Goldman Sachs**: As explained above, Goldman Sachs shall be paid \$3 million from the DIP Facility proceeds.
- (ix) **Maturity Date**: the earlier of (i) the date which is six (6) months following the Petition Date, (ii) the consummation of a sale of all or substantially all of the assets of the Debtors pursuant to section 363 of the Bankruptcy Code per the Milestones below.
- (x) **Milestones**: the existing DIP Facility milestones proposal are acceptable.
- (xi) **Credit Bid**: DIP Lender may credit bid its DIP Facility at the section 363 sale.
- (xii) **Offer to Purchase**: DIP Lender intends to submit an asset purchase agreement to acquire substantially all of the assets for a purchase price of not less than \$14 million.

25. The above terms are for superior to the existing DIP Facility and present significant benefits to the estate. First, the Replacement DIP Facility allows SFCC’s existing secured debt to be repaid in full. Second, it funds the entire Budget and repays any of the existing DIP lender’s advances to date. Third, it provides \$3 million to Goldman Sachs, \$1 million more than it will receive from the existing DIP Facility, with a potential of additional recovery if there is a competitive auction. Finally, and perhaps most importantly, it will not contain any terms that would allow credit bid rights to be high jacked by a bidder, thus leveling the playing field and ensuring a fair auction that will maximize value.

26. The Debtors have not satisfied their burden under Bankruptcy Code section 364 of demonstrating that less expensive and less restrictive financing is unavailable to

them. Bankruptcy Code section 364(d) “requires the Debtor to demonstrate that less onerous postpetition financing was unavailable.” In re Reading Tube Indus., 72 B.R. 329, 332 (Bankr. E.D. Pa. 1987). On this issue, “it is important for a bankruptcy court to make a qualitative assessment of the credit transaction in light of readily available alternatives before granting any [Bankruptcy Code section] 364 motion. Since such a qualitative analysis is necessary in considering every [Bankruptcy Code section] 364 motion, it should not be neglected in deciding whether to grant a [Bankruptcy Code section] 364(d) motion.” In re Aqua Assocs., 123 B.R.192, 196 (Bankr. E.D. Pa. 1991).

CONCLUSION

The DIP Loan is unconscionable and should not be granted the Court’s seal of approval. It is clear that the Debtors have not obtained financing on the most advantageous terms available and the DIP Motion should be denied.

Dated: September 16, 2019
Wilmington, Delaware

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