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NAVIGATING THE NEXT.

Retail Apocalypse: Lessons Learned and Outlook for the Industry

Speakers:

Holly Etlin, Managing Director, AlixPartners

Ray Edwards, Executive Vice President, Retailer Services, Kimco Realty

Mike Edwards, Independent Board Director & Chairman, Retail and Ecommerce Operations

Jennifer Feldsher, Partner, Morgan Lewis

Craig Wolfe, Partner, Morgan Lewis

Christina Melendi, Partner, Morgan Lewis

April 29, 2021

Presenters



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Topics to Be Covered

- **Current State of Retail and Lessons Learned from Past Restructurings**
 - Impact of the pandemic on the industry
 - Acceleration of omnichannel consumers
 - Increased need for a more seamless experience and BOPUS technology
 - Changes in consumer behavior patterns – some temporary, many more permanent
- **Outlook For the Post–COVID-19 Marketplace**
 - Liquidity levels
 - Commercial real estate issues continue
 - Section 365(d)(3) constraints on continued nonpayment of rent
 - Assumption and rejection deadlines
 - State of the law – force majeure and frustration of purpose
 - Changes in Paycheck Protection Program (PPP) eligibility rules allow some debtors to benefit
 - Subchapter 5 – A new lifeline for some businesses
- **Industry Winners and Losers**

Current State of Retail and Lessons Learned from Past Restructurings

Impact of the Pandemic

- Expansion to omnichannel
- But that causes a “2% degradation”
- Potential Solutions?

Consumer Behavior Patterns Have Changed

- Buy Online/Pick Up In Store (BOPUS) technology needs
- Which trends are likely to be permanent and which are likely to return to prepandemic levels (e.g., all online, curbside pickup)
- Industry differences (e.g., grocers vs. apparel)

Current State of Retail and Lessons Learned from Past Restructurings (cont'd)

Lessons Learned from Past Restructurings

- Bankruptcies likely to continue
- COVID-19 hardships will be an opportunity to rebalance and retool
- Uptick in restructurings, liquidations to continue
 - As will litigation with respect to nonpayment of rent
 - Section 365(d)(3) will need to be addressed in the absence of shutdown/suspension relief
- M&A activity will increase as players are looking for value on the cheap

Outlook for the Post–COVID-19 Marketplace

- **Liquidity Levels in the Sector**
- **Commercial Real Estate**
 - Status of brick and mortar – big malls vs. open-air – why it makes a difference now more than ever
 - Shift to higher-quality centers
 - Geography – how migration patterns have impacted the bottom line
 - Legal: Noteworthy lease term changes

Legal Issues – Need to Address COVID-19 Period and Future Rent Obligations

Section 365(d)(3) gives the debtor up to 60 days to perform postpetition obligations under a nonresidential lease. The debtor's obligation to make postpetition payments is reinstated on the 61st day.

- During COVID-19, extraordinary relief was available to suspend rent payments, usually with support of landlords

Legal Issues – Need to Address COVID-19 Period and Future Rent Obligations (*cont'd*)

See, e.g.,

- *In re Modell's Sporting Goods* (Case No. 20-14179, Bankr. D.N.J.) – court granted the “extra-ordinary” remedy of suspending a debtor’s obligation to pay postpetition rent due to complications caused by COVID-19 executive orders. The court granted the suspension twice.
- *In re Pier 1 Imports* (Case No. 20-30805, Bankr. E.D. Va.) – court held that section 365(d)(3) does not give landlords the right to compel payment of postpetition obligations (rent); landlords would have priority administrative-expense claims that had to be paid upon confirmation.
- *In re JC Penney Co., Inc. et al.*, No. 20-20182 (DRJ) (Bankr. S.D. Tex. May 28, 2020) (Dkt. No. 338); *In re CraftWorks Parent, LLC*, No. 20-10475 (BLS) (Bankr. D. Del. May 20, 2020) (Dkt. No. 174); *In re Chinos Holdings, Inc.*, No. 20-32181 (KLP) (Bankr. E.D. Va. May 4, 2020); *In re True Religion Apparel, Inc.*, No. 20-10941 (CSS) (Bankr. D. Del. Apr. 13, 2020)

**Going forward –
various
Bankruptcy Code
amendments
under the
Consolidated
Appropriations Act
may impact the
landlord-tenant**

1

Section 365(d)(3) allows small businesses to defer rent up to 120 days, provided that they satisfy hardship tests

2

Section 365(d)(4) extends the assumption and rejection period from 120 days to 210 days, and maintains the single 90-day extension provision before landlord consent is required

3

Section 547 protects landlords that enter into lease amendments with tenants on or after March 13, 2020, as deferral of rent and subsequent repayment are protected from claims of preferential transfers

4

Sunsets 12/27/22

Legal Issues – Need to Address COVID-19 Period and Future Rent Obligations (*cont'd*)

- **Force Majeure**

- During the pandemic, efforts to escape rent liability based on force majeure grounds were mostly unsuccessful.
- Nonpayment of rent largely governed by the terms of the lease agreements.
- *But see JN Contemporary Art LLC v. Phillips Auctioneers, LLC*, No. 1:20-cv-04370-DLC (S.D.N.Y. 2020) – court found that the pandemic was a triggering event under the contract's force majeure clause (circumstance beyond the parties' reasonable control; natural disaster) to excuse defendant's nonperformance under the contract to sell plaintiff's artwork at an in-person event in May 2020.

- **Frustration of purpose and impossibility – discharges a party's duty to perform under a contract where a wholly unforeseeable event hinders the contract's purpose**

- Mixed results in pandemic litigation.
- Recently, *UMNV 205-207 Newbury LLC v. Caffé Nero Americas Inc.* (Mass. Super. Ct., Feb. 8, 2021, 2084CV01493-BLS2) has breathed new life into the argument. In that case; the court held that rent was not due if the restaurant couldn't operate, as the purpose of the contract — to serve customers food and coffee *inside* the café — had been frustrated.

Legal Issues – Need to Address COVID-19 Period and Future Rent Obligations (*cont'd*)

- *In re Cinemex USA Real Estate Holdings, Inc., et al.*, 2021 WL 564486 (Bankr. S.D. Fla., Jan. 27, 2021) – purposes of movie theater lease were frustrated by a government order to shut down theaters; relief from paying rent granted only for those periods when theater was legally prohibited from opening.
- ***But see***
 - *In re CEC Entertainment Inc.*, 2020 WL 7356380 (Bankr. S.D. Tex., Dec. 14, 2020) – since leases had contemplated the risk of disruption by governmental regulations and allocated such risks via the force majeure clauses, the clauses, which did not allow the debtor to withhold or abate rent during the pandemic, superseded the frustration-of-purpose doctrine.
 - *The Gap Inc. v. Ponte Gadea New York LLC*, 2021 WL 861121 (S.D.N.Y. Mar. 8, 2021) – request for rescission and reformation of a lease based on frustration-of-purpose doctrine was denied; the lease’s force majeure clause contemplated the government-mandated shutdown, and was therefore not “wholly unforeseeable.”

Expansion of Subchapter V (Small Business Reorganizations)

Historically intended for very small businesses with \$2.725 million debt threshold

Cares Act increased debt ceiling to \$7.5 million, excluding insider and contingent debt

Expanded ceiling expires on March 27, 2022

Expansion of Subchapter V (Small Business Reorganizations) (*cont'd*)

Key Features

Typically, no creditors' committee

Fast track process

No consenting impaired class required to confirm a plan

Absolute priority rule is relaxed so equity can maintain ownership without creditors being paid in full

Commitment to pay all disposable income for three to five years

Subchapter V Trustee is appointed

Expansion of Subchapter V (Small Business Reorganizations) (*cont'd*)

- New case law held that PPP money and lease rejection damages claims are excluded from debt ceiling. *In re Parking Mgmt., Inc.*, 620 B.R. 544 (Bankr. D. Md. 2020) (Judge Thomas J. Catliota).
- Therefore, much larger cases have been filed:
 - Furla (USA), Inc. (Bankr. S.D.N.Y. 20-12604) (14 retail stores)
 - NTS W. USA Corp. (Desigual) (Bankr. S.D.N.Y. 20-35769) (12 retail stores)
 - Solstice Sunglasses (Bankr. S.D.N.Y. 21-10306) (66 retail stores)

PPP Eligibility Clarified

- Since the first round of PPP loans, there has been confusion regarding eligibility for debtors
 - Small Business Administration (SBA) argued that any applicant in Chapter 11 bankruptcy was not eligible for a PPP loan
 - Generally prevailed
 - Impacted Chapter 11 filings
- In the second round of PPP funding, Congress skirted the issue by leaving it to the SBA to determine if a debtor could access PPP loans (SBA said no)

PPP Eligibility Clarified (*cont'd*)

- Finally, on April 6, 2021, the SBA provided additional guidance for when a debtor could access PPP funds by issuing FAQ 67. The SBA determined what conditions terminate involvement of a business in a bankruptcy case.
- For debtors under Chapter 11, 12, or 13, the FAQ provides that they are no longer “presently involved in any bankruptcy” upon two occasions:
 - once a plan confirmation order has been entered, and
 - once an order dismissing the case is entered.
- In each of the circumstances, however, the SBA indicates that the order must be entered before the filing of the PPP application.

Outlook of a Post-COVID-19 Marketplace

- **Segment winners and losers**
 - Health and wellness
 - Creature comfort providers
 - Furniture
 - Home goods
 - Environmental, social, and corporate governance
- **Challenges**
 - Supply chain
 - Excess inventory
 - Work from home

Coronavirus/ COVID-19 Resources

We have formed a multidisciplinary **Coronavirus/COVID-19 Task Force** to help guide clients through the broad scope of legal issues brought on by this public health challenge.

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To help keep you on top of developments as they unfold, we also have launched a resource page on our website at

[www.morganlewis.com/
topics/coronavirus-
covid-19](http://www.morganlewis.com/topics/coronavirus-covid-19).

If you would like to receive a daily digest of all updates to the page, please visit the resource page to [subscribe](#) using the purple “Stay Up to Date” button.



Biography



Holly Etlin

Managing Director

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Holly joined AlixPartners as Managing Director in 2007. She has over 30 years of experience in providing turnaround services for companies in the retail, distribution, consumer products, financial services, media, and hospitality industries. Holly is a Certified Turnaround Professional and is admitted to the American College of Bankruptcy and the International Insolvency Institute. In 2007, the Turnaround Management Association (TMA) recognized Holly with its Turnaround of the Year Award for the successful turnaround of Winn-Dixie Stores; in 2011, TMA recognized Holly with its Transaction of the Year Award for the successful refinancing of Neff Rental; and in 2017 she won the TMA Turnaround of the Year award for her work at BCBG MaxAzria. Holly studied Economics at UCLA.

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Ray Edwards

Executive Vice President, Retailer Services
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Ray joined Kimco Realty in 2001 and is EVP of Retailer Services. He is focused on strengthening Kimco's relationship with its national retailers and is a voting member of the company's investment committee, approving all new investments, development projects, and property dispositions. He develops opportunities for real estate rich retailers through investments, lending, and providing real estate solutions. Ray worked on the 2006 transaction that acquired the 650-store Albertson's grocery chain, and in 2013 they subsequently acquired the remaining stores which led to the 2015 merger with Safeway to create the second largest grocery chain in the country with over 2,300 stores. Ray received his JD from St. John's University Law School.

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Mike is a strategic retail and eCommerce executive with 35 years of experience leading publicly traded and privately held retailers through major, billion-dollar transformations. Mike is skilled in driving optimization across digital marketing, merchandising, sales and technology and he has repeatedly aided in the sale and repositioning of companies falling victim to slow topline growth, major profit losses, over-leveraged balance sheets, and under-utilization of technology, even amid cybersecurity crises and a global pandemic. He has served as President and CEO of an international children's lifestyle brand and online luggage and travel accessories business and led global merchandising and operations at Staples, Borders Group, Lucy Activewear, and Jo-Ann Stores. Michael holds a Bachelor of Science in Business and Marketing from Drexel University.

Mike Edwards

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Jennifer focuses her practice on corporate restructuring and insolvency law. She represents interested parties in bankruptcy proceedings and complex corporate debt restructurings with an emphasis on the representation of secured creditors, special situations investment funds, ad hoc groups, and acquirers of assets in all aspects of distressed situations. Jennifer also has experience representing troubled corporate debtors in in-court and out-of-court reorganizations, asset sales, loan restructurings, and commercial loan transactions.

Jennifer has directed all aspects of the bankruptcy process for debtors and creditors, including contested plan confirmation hearings, contested relief from stay and cash collateral hearings, and DIP loan negotiations and related hearings. In addition, Jennifer is routinely called on to advise directors, managers, creditors, and institutional investors on zone of insolvency issues and fiduciary duties.

She has acted as counsel to companies involved in many of the largest restructurings, including in the energy, retail, telecommunications, technology, healthcare, airline, automotive, gaming, and financial services industries.

Before joining Morgan Lewis, Jennifer was a partner at a major international law firm.

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Craig A. Wolfe

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Craig has more than 20 years of experience counseling clients facing financial distress. Craig also represents sellers and purchasers of specific assets and entire businesses in the context of Chapter 11 bankruptcy cases. His clients span a wide range of industries and sectors, including retail, apparel, food and beverage, packaging, technology, ocean shipping, shipbuilding, petroleum trading, offshore oil, pipeline, transportation and logistics, entertainment, telecommunications, chemical, aircraft, steel, publishing, manufacturing, and printing.

Craig has helped numerous companies avoid becoming Chapter 11 debtors, often on the eve of a potential filing and fully prepped for the “first day” hearing if bankruptcy became necessary. He also represents strategic financial and private equity clients in purchasing distressed businesses and specific assets, as well as creditors’ committees in the bankruptcies of companies across multiple industries.

Prior to joining Morgan Lewis, Craig was a partner in the finance and restructuring practice of another global law firm, resident in New York.

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Christina Melendi’s corporate and securities practice focuses on representing US and global public and private corporations and private equity sponsors and their portfolio companies in mergers and acquisitions (M&A), investments, divestitures, asset purchases, minority investments, joint ventures, private and public equity and debt financings, securities offerings, and other general corporate matters. She also advises institutional and mezzanine investors on equity rights for co-investment transactions with private equity sponsors and restructuring and workout transactions. Additionally, she currently serves as Morgan Lewis’s firmwide hiring partner, co-leader of the firm’s retail and eCommerce industry initiative, and deputy leader of the firm’s New York corporate and business transactions practice.

Christina assists companies to raise capital in the public markets, including initial public offerings and secondary offerings, and counsels clients on SEC reporting and securities law disclosure, annual meeting and proxy related issues, corporate governance matters, and stock exchange listing requirements.

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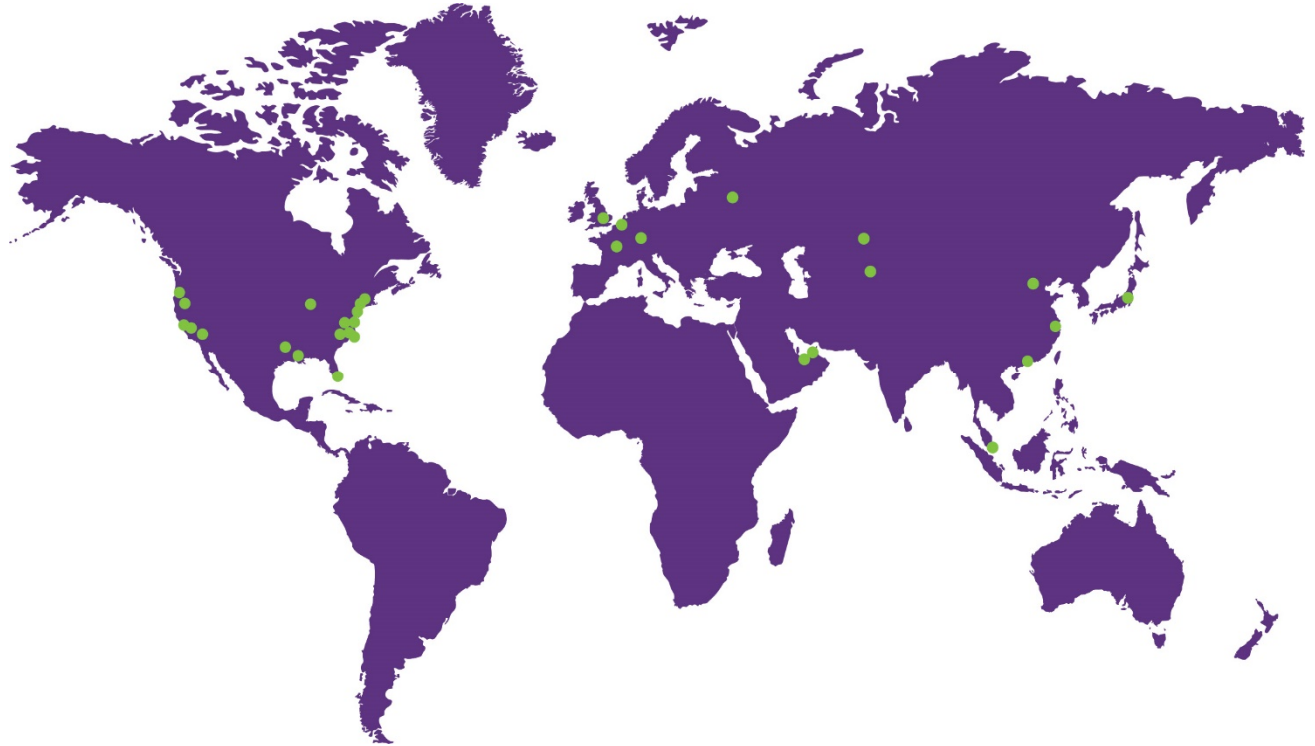
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