The Intersection of Bankruptcy Law With Other Areas of the Law

Presented by the February Pupilage Team
Led by Ray Lemisch and Leslie Heilman

Delaware Bankruptcy American Inn of Court
February 21, 2012 at 5:30 p.m.
United States Bankruptcy Court for the District of Delaware
824 Market Street, 5th Floor, Courtroom No. 5
Wilmington, Delaware 19801

DELAWARE BANKRUPTCY INN OF COURT

FEBRUARY 21, 2012 PUPILAGE PROGRAM:
INTERSECTION OF BANKRUPTCY LAW WITH OTHER AREAS OF THE LAW

Team Leaders: Ray Lemisch and Leslie Heilman

Moderator: Johnna Darby

I. Bankruptcy Law and Employment Law (Group Leader: Bill Burnett) (Judges: Victoria Counihan; Bill Burnett; Dan DeFranceschi) (Research and Support: Margaret England; Mark Hurford; Damien Tancredi; Scott Stewart; Charles McCauley)

A. WARN Act: Contours of a Single Employer

1. Arguments: Colin Robinson; Scott Leonhardt

2. Q&A by Judges

B. Pension Plan Termination

1. Arguments: Tyler Semmelman; Joe McMahon

2. Q&A by Judges

II. Bankruptcy Law and Property Law (Group Leader: Mark Degrosseilliers)

A. Reclamation: Procedures; Relevance; Remedy Requirements

1. Group Members: Mark Minuti; Luke Murley; Kurt Gwynne; Tori Guilfoyle; Doug Herrmann

2. Q&A

B. Intellectual Property

1. Group Members: Ericka Johnson; Mark Degrosseilliers; Jack Shrum; Eric Schnabel

2. Q&A

C. Insurance: SIR requirements; Property of the Estate; Duty to Cooperate; D&O Issues

1. Group Members: Zeke Allinson; Greg Hauswirth; Michael Lastowski; Patrick Reilly

2. Q&A

III. Bankruptcy Law and Criminal Law (Group Leader: Natalie Ramsey)

A. Ponzi Scheme/5th Amendment/Effect on Discharge and Confirmation

1. Group members: Jeff Drobish; Nella Bloom; Jeff Carbino

2. Q&A by Judge

B. Committee Litigation: Crime/Fraud exception and *in pari delicto*

1. Group members: Natalie Ramsey; Leigh-Anne Raport; Chad Toms

2. Q&A by Judge

The Intersection of Bankruptcy Law With Employment Law

PENSION MATERIALS

UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re	:	Chapter 11
HARRY & DAVID HOLDINGS, INC, *et al.*,[1]	:	Case No. 11-10884 (MFW)
Debtors.	:	(Jointly Administered)
		Hearing Date: To be determined.
		Obj. Deadline: To be determined.

NOTICE OF MOTION AND HEARING

PLEASE TAKE NOTICE that, on May 9, 2011, the above-captioned debtors (collectively, the "Debtors") filed the *Motion of the Debtors for an Order (A) Determining that the Financial Requirements for a Distress Termination of Their Defined Benefit Pension Plan Are Satisfied; and (B) Approving a Distress Termination of the Pension Plan* (the "Motion") with the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court").

PLEASE TAKE FURTHER NOTICE that any responses or objections to the Motion must be in writing, filed with the Clerk of the Bankruptcy Court, 824 North Market Street, 3rd Floor, Wilmington, Delaware 19801, and served upon and received by the undersigned attorneys for the Debtors. **As of the date hereof, no objection deadline for the Motion has been set** (the "Objection Deadline"). Once set, parties in interest will receive separate notice of Objection Deadline.

[1] The Debtors are the following four entities (the last four digits of their respective taxpayer identification numbers, if any, follow in parentheses): Harry & David Holdings, Inc. (4389); Harry and David (1765); Harry & David Operations, Inc. (1427); Bear Creek Orchards, Inc. (7216). The address of each of the Debtors is 2500 South Pacific Highway, Medford, OR 97501.

PLEASE TAKE FURTHER NOTICE that a hearing to consider the Motion will be held before The Honorable Mary F. Walrath, United States Bankruptcy Judge for the District of Delaware, at the Bankruptcy Court, 824 North Market Street, 5th Floor, Courtroom 4, Wilmington, Delaware 19801. **As of the date hereof, no hearing on the Motion has been scheduled** (the "Hearing"). Once scheduled, parties in interest will receive separate notice of the Hearing.

Dated: May 9, 2011
Wilmington, Delaware

Respectfully submitted,

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ATTORNEYS FOR DEBTORS

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re	:	Chapter 11
HARRY & DAVID HOLDINGS, INC, *et al.*,[1]	:	Case No. 11-10884 (MFW)
Debtors.	:	(Jointly Administered)
		Hearing Date: To be determined. **Objection Deadline: To be determined.**

MOTION OF THE DEBTORS FOR AN ORDER (A) DETERMINING THAT THE FINANCIAL REQUIREMENTS FOR A DISTRESS TERMINATION OF THEIR DEFINED BENEFIT PENSION PLAN ARE SATISFIED; AND (B) APPROVING A DISTRESS TERMINATION OF THE PENSION PLAN

The above-captioned debtors (collectively, the "Debtors") hereby move the Court for the entry of an order pursuant to Section 363(b) of the Bankruptcy Code: (i) determining that the financial requirements for a "distress termination" of their defined benefit pension plan, the Harry and David Employees' Pension Plan (the "Pension Plan") are satisfied under section 4041(c)(2)(B) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), 29 U.S.C § 1341(c)(2)(B) and (ii) approving the termination of the Pension Plan (as such term is defined below). In support of this Motion, the Debtors respectfully state as follows:

Introduction

1. The Debtors must terminate the Pension Plan to obtain the exit equity financing necessary to allow the Debtors to reorganize and emerge as viable entities. After extensive efforts to preserve and enhance liquidity and improve their operations – including closing unprofitable store locations and rejecting related leases, beginning the process of

1 The Debtors are the following four entities (the last four digits of their respective taxpayer identification numbers, if any, follow in parentheses): Harry & David Holdings, Inc. (4389); Harry and David (1765); Harry & David Operations, Inc. (1427); Bear Creek Orchards, Inc. (7216). The address of each of the Debtors is 2500 South Pacific Highway, Medford, Oregon 97501.

consolidating vendors and implementing purchasing best practices, and implementing targeted headcount reductions – the Debtors' businesses remain significantly cash flow constrained. As such, the Debtors require equity capital, and, absent the relief sought in this Motion, the Debtors will be unable to obtain the equity infusion they need to emerge from chapter 11 as viable entities.

2. The Pension Plan is one of the Debtors' largest debt obligations and must be eliminated for the Debtors to emerge from these chapter 11 cases. Absent the relief sought in this Motion, the Debtors will be unable to obtain the $55 million in equity exit financing that is necessary for the Debtors to confirm *any* chapter 11 plan. As described in more detail below, if the Pension Plan is not terminated, the Debtors' Noteholders will not provide the $55 million in exit equity financing. Furthermore, if the Debtors are unable to obtain such exit equity financing, the ABL Lenders will not provide $100 million in exit debt financing (the "ABL Exit Facility"). In light of the risk that a post-emergence termination of the Pension Plan would pose to the Noteholders' equity investment, it would be unreasonable to expect the Noteholders, or any investor, to commit $55 million in new equity absent a termination of the Pension Plan. As a result, the Debtors' must terminate the Pension Plan to emerge from these chapter 11 cases.

General Background

3. On March 28, 2011 (the "Petition Date"), each of the Debtors commenced a case under chapter 11 of the Bankruptcy Code.[2] The Debtors are operating their businesses and managing their properties as debtors-in-possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. The Debtors' chapter 11 cases have been consolidated for procedural purposes only and are administered jointly.

[2] This Court has jurisdiction to consider this matter pursuant to 28 U.S.C. §§ 157 and 1334 and 29 U.S.C. § 1341 (ERISA § 4041). This is a core proceeding pursuant to 28 U.S.C. § 157(b). Venue for this matter is proper in this district pursuant to 28 U.S.C. § 1409.

4. The Debtors are a vertically integrated, multi-channel specialty retailer and producer of branded premium gift-quality fruit, food products, and gifts marketed under the Harry and David®, Wolferman's®, and Cushman's® brands. The Debtors market their products through catalogs distributed through the mail, the Internet, business-to-business, consumer telemarketing, Harry and David Stores, Cushman's seasonal stores, and wholesale distribution to other retailers. For the twelve months ending December 25, 2010, the Debtors generated approximately $416 million in revenue.

5. On April 7, 2011, the United States Trustee for the District of Delaware (the "U.S. Trustee") appointed an official committee of unsecured creditors (the "Creditors' Committee") in these chapter 11 cases, pursuant to section 1102 of the Bankruptcy Code.

Events Leading to the Commencement of the Chapter 11 Cases

6. Over the course of the last several years, various external market factors have diminished the Debtors' historical competitive advantages and, correspondingly, revenues and profitability. In addition, consumers have become extremely price conscious following the beginning of the 2008 recession, and this consciousness continues to materially impact the Debtors' profitability. The Debtors' financial performance over the past three years is a reflection of this trend, as consumer price consciousness caused the Debtors to discount their products more significantly than they had expected. In particular, during the 2010 holiday season, the Debtors expected a significant improvement in sales performance, which ultimately did not materialize. In order to clear inventory purchases, the Debtors were forced to discount even more heavily than anticipated. See Declaration of Kay Hong in Support of First-Day Pleadings (Docket No. 3) attached hereto as Exhibit A (the "Hong Declaration"), ¶¶ 23-26.

7. As a result, the Debtors failed to generate enough cash flow during the 2010 holiday season to satisfy the minimum available cash covenant contained in the Debtors'

Prepetition Revolving Credit Facility (as defined below), and the Debtors were unable to continue borrowing under the Prepetition Revolving Credit Facility. Hong Declaration, ¶ 27.

8. After losing the ability to borrow under the Prepetition Revolving Credit Facility and facing a significant liquidity shortfall as a result of their 2010 holiday season results, the commencement of these cases became necessary to (a) address the Debtors' liquidity needs and (b) provide a single forum to restructure the Debtor's primary prepetition liabilities. Hong Declaration, ¶ 28.

The Debtors' Prepetition Liabilities

9. As of the Petition Date, the Debtors' primary liabilities consisted of: (a) two series of senior unsecured notes; (b) pension obligations; (c) unsecured trade debt; and (d) lease obligations.[3] Hong Declaration, ¶ 16. The Debtors cannot confirm a chapter 11 plan and continue to operate outside of these chapter 11 cases without the restructuring of each of these significant prepetition liabilities. In particular, as described in more detail below, the Debtors cannot obtain the exit financing necessary to confirm a chapter 11 plan and operate their businesses outside of these cases without the termination of the Pension Plan. The Debtors significant prepetition liabilities, including their liabilities under the Pension Plan, are described in more detail below.

Senior Unsecured Notes

10. The Debtors had approximately $58 million of Senior Floating Rate Notes due March 1, 2012 and $140 million of Senior Fixed Rate Notes due March 1, 2013

3 The Debtors are party to a Credit Agreement, dated March 20, 2006 (as amended) with GMAC Commercial Finance LLC, as Collateral Agent and Documentation Agent, UBS Securities LLC, as Arranger, UBS AG Stamford Branch, as Issuing Bank, Administrative Collateral Agent and Administrative Agent, and UBS Finance LLC, as Swingline Lender, that provided the Debtors with a $105 million revolving credit facility (the "Prepetition Revolving Credit Facility"). Borrowings under the Prepetition Revolving Credit Facility are secured by substantially all of the Debtors' assets. As of the Petition Date, the Debtors had no outstanding borrowings under the Prepetition Revolving Credit Facility.

(collectively, the "Senior Notes") outstanding as of the Petition Date. A single indenture, dated February 25, 2005, governs both series of Senior Notes and Wells Fargo Bank, N.A. is the indenture trustee. The Senior Notes represent senior unsecured obligations of Harry and David and are guaranteed by the other Debtors. Hong Declaration, ¶¶ 17-18.

Unsecured Trade Debt

11. In the ordinary course of operating their direct marketing and retail business, the Debtors have historically purchased raw materials and other goods and services from over 1400 vendors. As of the Petition Date, the Debtors estimated that they owed approximately $37 million for raw materials and other unsecured obligations for goods and services. Hong Declaration, ¶ 21.

Lease Obligations

12. The Debtors operate approximately 70 stores in leading outlet and lifestyle centers, specialty malls and other high traffic shopping areas throughout the United States. In addition, the Debtors were responsible for lease payments with respect to 52 other store locations where the Debtors' ceased operations prior to the Petition Date. The Debtors rejected the leases for these store locations effective as of the Petition Date. The Debtors also lease storage or warehouse space at approximately 12 locations. Prior to the Petition Date, the Debtors approximate annual expense for leased properties was approximately $19 million. Hong Declaration, ¶ 22.

The Pension Plan

13. Debtor Harry and David, an Oregon corporation, sponsors the Pension Plan, covering certain employees of the Debtors. As of January 1, 2011, the total unfunded liability for the Pension Plan on an actuarial basis is estimated to be $23,600,000. To preserve liquidity, the Debtors did not make their minimum required contribution to the Pension Plan due

on April 15, 2011 in the amount of $704,000 and in respect of the 2011 plan year. The Debtors project that minimum required contributions to the Pension Plan totaling approximately $420,300 and $4,739,200 remain to be paid in respect to the 2010 and 2011 plan years, respectively, but, with the exception of the April 15, 2011 payment, are not yet due and owing. For the five year period 2011-2015, the minimum total required contributions to the Pension Plan under the Code and ERISA is estimated to be $24,228,200. See Declaration of Karen M. Mack in Support of Motion of the Debtors for an Order (A) Determining that the Financial Requirements for a Distress Termination of Their Defined Benefit Pension Plan Are Satisfied; and (B) Approving a Distress Termination of the Pension Plan attached hereto as Exhibit B (the "Mack Declaration"), ¶¶ 8-9.

14. If the Pension Plan is terminated, the PBGC likely will assert a claim against the Debtors, on a joint and several basis, for the Pension Plan's unfunded liabilities. Based on the PBGC's method for calculating claims for unfunded pension liabilities, the PBGC has advised the Debtors that it will file a claim for termination liability against the Debtors in the amount of approximately $45 million.[4] In the event that the Pension Plan is terminated prior to the confirmation of the Plan, such a claim would generally be an unsecured obligation in the chapter 11 case and, aside from any premium the reorganized Debtors may be obligated to pay to the PBGC under 29 U.S.C. § 1396(a) as a result of such termination, the reorganized Debtors would be relieved of any further liability on account of the Pension Plan.

The Plan Support Agreement

15. Prior to the Petition Date, the Debtors executed a plan support agreement (the "Plan Support Agreement") with approximately 81% of the holders (the "Noteholders") of the Debtors' Senior Notes. The Plan Support Agreement contemplates the reorganization of the

[4] The Debtors reserve the right to dispute the amount of any such claims.

Debtors through a chapter 11 plan, the term sheet for which is attached to the Plan Support Agreement (the "Plan"). The Plan Support Agreement (a) will facilitate the confirmation of a Plan that provides for the significant restructuring of the Debtors' primary prepetition liabilities and (b) ensures that the Debtors' will have sufficient exit financing to allow the Debtors to emerge from these cases on an expedited basis and continue to operate their businesses. Hong Declaration ¶¶ 32-36.

16. The Debtor's exit from these chapter 11 cases will be funded with (a) the proceeds of a rights offering (the "Rights Offering") to purchase stock of the reorganized Debtors in connection with their emergence from chapter 11 and (b) the $100 million ABL Exit Facility. The proceeds of the Rights Offering will repay the Debtors' second lien, $55 million debtor-in-possession financing facility (the "Noteholder DIP Facility"), and the $100 million ABL Exit Facility will be used to (a) refinance any draws under the ABL DIP Facility (as defined below) and (b) fund the Debtors' post-emergence operations, permitting the Debtors to exit chapter 11. See Declaration of Neil A. Augustine in Support of Motion of the Debtors for an Order (A) Determining that the Financial Requirements for a Distress Termination of Their Defined Benefit Pension Plan Are Satisfied; and (B) Approving a Distress Termination of the Pension Plan attached hereto as Exhibit C (the "Augustine Declaration"), ¶ 13.

17. In connection with the anticipated Plan, eligible holders of the Senior Notes will be entitled, as part of the Rights Offering, to purchase stock in the reorganized Debtors at the price specified in the Plan, which will be at a discount to the assumed "plan value" for such stock under the Plan. Under the anticipated Plan, however, holders of the Senior Notes are not required to purchase such stock. As such, to ensure that the Debtors will have at confirmation the full $55 million to repay amounts owing under the Noteholder DIP Facility and

exit these chapter 11 cases, the Debtors prior to the Petition Date also entered into the Backstop Agreement with the Noteholders. Subject to, and on the terms of, the Backstop Agreement, the Noteholders have committed to purchase, at the same purchase price, stock in the reorganized Debtors to the extent that the Rights Offering does not raise the full $55 million to repay amounts owing under the Noteholder DIP Facility. In addition, under the proposed Plan, the Noteholders have agreed to convert all of the Senior Notes to equity in the reorganized Debtors. Augustine Declaration, ¶ 14.

18. The Noteholders have required, as a condition to their commitment under the Backstop Agreement, and as a condition to their support of the Plan, that the Debtors terminate the Pension Plan. As described in more detail below, the Debtors (a) cannot obtain sufficient exit financing, and cannot emerge from these chapter 11 cases, without the commitment of the Noteholders to provide $55 million in new equity financing and (b) cannot obtain the commitment of the Noteholders without terminating the Pension Plan. Without the Noteholders' commitment to providing up to $55 million in exit equity financing, the Debtors also would be unable to secure the $100 million ABL Exit Facility. The Debtors also cannot realistically emerge from chapter 11 without a conversion of their Senior Notes to equity. Augustine Declaration, ¶ 15.

Relief Requested

19. By this Motion, the Debtors seek an order (i) determining that the financial requirements for a "distress termination" of the Pension Plan under 29 U.S.C. § 1341(c)(2)(B)(ii)(IV) are satisfied; (ii) authorizing the Debtors to terminate the Pension Plan under 29 U.S.C. § 1341(c)(2)(B) and section 363(b) of the Bankruptcy Code; and (iii) for certain related relief. Based upon the actuarial determinations of the future minimum funding

requirements of the Pension Plan and the Debtors' projected cash flow in any viable reorganization scenario, the distress termination of the Pension Plan is required.

Legal Basis for Relief Requested

20. A plan sponsor may voluntarily terminate a pension plan in one of two ways: (1) it may terminate the plan under a "standard termination" if there are sufficient plan assets to pay all plan benefits, or (2) it may terminate the plan under a "distress termination" if, among other requirements, there are not sufficient plan assets to pay all plan benefits. There is no dispute that the Pension Plan's assets are insufficient to pay all plan benefits. As a result, the Debtors are seeking a distress termination of their Pension Plan. An underfunded plan may be terminated under a distress termination if (a) the plan administrator (i.e., here, Debtor Harry and David) provides plan participants, their beneficiaries and the PBGC required notice of plan termination, (b) the plan administrator provides certain information to the PBGC and (c) the plan sponsor and each member of its controlled group of trades and businesses meets any of the tests for a "distress termination" set forth in section 4041(c) of ERISA.

21. To satisfy the notice requirements set forth in section 4041(c) of ERISA, the plan administrator must also provide a written Notice of Intent to Terminate (a "NOIT") to each person who is an affected person at least 60, but not more than 90, days prior to the proposed termination date.[5] The plan administrator also must file with the PBGC a Form 600, which serves as notice to the PBGC in its status as an affected person.

22. The test[6] to determine whether a chapter 11 debtor satisfies the requirements for a "distress termination" is referred to as the "Reorganization Test" and requires the following:

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5 See 29 U.S.C. § 1301(a)(21); PBGC Reg. § 4041.43(a)(1).

6 The other tests for Distress Termination are as follows:

> (a) The entity has filed, or had filed against it, as of the proposed termination date, a petition seeking reorganization in a case under the Bankruptcy Code;
>
> (b) Such entity's chapter 11 case has not, as of the proposed termination date, been dismissed;
>
> (c) Such entity timely submits a copy of any requests for the approval of the bankruptcy court of the plan termination to the PBGC at the time the request is made; and
>
> (d) The bankruptcy court determines that, unless the plan is terminated, such entity will be unable to (i) pay all of its debts pursuant to a plan of reorganization and (ii) continue in business outside the chapter 11 reorganization process and approves the termination.[7]

23. By this Motion, the Debtors seek a determination under the Reorganization Test that, unless the Pension Plan is terminated, the Debtors will be unable to (i) pay all of their debts pursuant to a plan of reorganization and (ii) continue in business outside the chapter 11 reorganization process. As described in more detail below, the Debtors satisfy the Reorganization Test because (a) termination of the Pension Plan is a condition to the Debtors' obtaining $55 million in necessary exit equity financing pursuant to the terms of the Backstop Agreement, (b) the Debtors would not be able to obtain sufficient exit financing from the Noteholders or another source without the termination of the Pension Plan, (c) absent the

(continued…)

(a) The Liquidation Test: (i) an entity has filed, or had filed against it, as of the proposed termination date, a petition seeking liquidation in a case under the Bankruptcy Code and such case has not, as of the proposed termination date, been dismissed; or (ii) a reorganization case is converted to a liquidation case as of the proposed termination date. See ERISA § 4041(c)(2)(B)(i).

(b) the Business Continuation Test: an entity demonstrates to the satisfaction of the PBGC that, unless a distress termination occurs, such entity will be unable to pay its debts when due and will be unable to continue in business; See ERISA § 4041(c)(2)(B)(iii)(I).and

(c) the Pension Costs Test: an entity demonstrates to the satisfaction of the PBGC that the costs of providing pension coverage have become unreasonably burdensome to such entity, solely as a result of a decline of its workforce covered as participants under all single-employer pension plans for which it is a contributing sponsor. See ERISA § 4041(c)(2)(B)(iii)(II).

[7] See 29 U.S.C. § 1341(c)(2)(B)(ii); ERISA § 4041(c)(2)(b)(ii)(I).

commitment of the Noteholders to provide $55 million in exit equity financing, the Debtors would be unable to secure the $100 million ABL Exit Facility, and likely would be required to obtain both replacement exit and DIP financing, (d) the Debtors likely would not be able to obtain replacement DIP or exit debt financing without the Noteholders' commitment to $55 million in exit equity financing and (e) termination of the Pension Plan is a condition to the Plan Support Agreement. As a result, absent termination of the Pension Plan, the Debtors cannot confirm a chapter 11 plan.

24. Like the current situation, courts have frequently found that a debtor satisfies the Reorganization Test where the debtor is unable to secure financing necessary to exit its chapter 11 cases without terminating its pension plans. See In re Falcon Prods., Inc., 354 B.R. 889 (E.D. Mo. 2006) (standard for distress termination was satisfied where exit financing was conditioned on termination of the debtor's pension plan); In re Delta Air Lines Inc., Case No. 05-17923 (ASH) (Bankr. S.D.N.Y. Sept. 5, 2006) (same); In re Oneida Ltd., Case No. 06-10489 (Bankr. S.D.N.Y. May 6, 2006) (same); In re U.S. Airways Group, Inc., 296 B.R. 734 (Bankr. E.D. Va. 2003) (same); In re Wire Rope Corp. of America, Inc., 287 B.R. 771 (Bankr. W.D. Mo. 2002) (same); In re Sewell Mfg. Co., Inc., 195 B.R. 180 (Bankr. N.D. Ga. 1996) (same).

25. In In re Falcon Prods., Inc., 497 F.3d 838 (8th Cir. 2007), the Eighth Circuit upheld a distress termination based on facts very similar to the facts in this case. There, the debtors argued and the bankruptcy court found that (a) the debtors could not achieve their plan projections without $50 million in equity exit financing, (b) the debtor could not secure the commitment for the necessary exit financing if their pension plans were not terminated and (c) the plan equity investors' decision to require termination of the pension plans as a condition

to their equity investment was reasonable. In upholding the bankruptcy court's distress termination order, the Eighth Circuit held that:

> "Based on the bankruptcy court's factual findings that Falcon cannot survive outside of Chapter 11 bankruptcy without the $50 million investment which is conditioned on termination of the pension plans, the bankruptcy court correctly decided that under section 1341 termination of all three Falcon pension plans is warranted."

26. The bankruptcy court in In re Sewell Manufacturing Company, Inc., 195 B.R. 180 (Bankr. N.D. Ga. 1996), approved a distress termination based on findings that (a) the reorganized debtor was expected to suffer negative cash flow in its current fiscal year and (b) neither its lender nor any other buyer or lender was willing to finance the required minimum pension plan funding contributions.[8] The debtor established that the only means for it to meet its upcoming pension obligations, as well as pay current debts, aside from finding a willing lender or buyer, was for the debtor to increase its sales by seventy percent over the next six months.[9] The court considered this concept an impossibility given current industry conditions and concluded that the standards required by section 4041(c)(2)(B)(ii)(IV) of ERISA (as described in paragraph 22 (d), above) had been satisfied and approved the termination.[10]

27. Similarly, the court in In re Wire Rope Corporation of America, Incorporated, 287 B.R. 771 (Bankr. W.D. Mo. 2002), also approved a distress termination based on the court's finding that the debtor's unfunded pension liabilities would prevent the debtor from securing financing necessary to allow the debtor to exit its chapter 11 case. In that case the court concluded that the debtor had two options, either (a) terminate its pension plan and attempt to obtain exit financing necessary to continue its business under a plan of reorganization, or

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8 Sewell Mfg., 195 B.R. at 185-86.

9 See id. at 186.

10 Id.

(b) attempt to retain its pension plans "and most likely go out of business." The court's ruling relied upon the finding that the debtor would not be able to obtain the requisite debt and equity financing it needed to confirm a plan and emerge from chapter 11 without terminating its pension plan. Therefore, based on its finding that the debtor could not obtain exit financing necessary to emerge from chapter 11, the court concluded that the debtor had shown that absent termination it "cannot pay all of its debts under a plan of reorganization and continue in business."

<u>Need for Termination of the Pension Plan</u>

28. Here, as in the cases cited above, if the Debtors do not terminate the Pension Plan, the Debtors will be unable to obtain the exit financing necessary to allow the Debtors to reorganize and emerge as viable entities. Despite the Debtors' efforts to preserve and enhance liquidity and improve their operations – including closing unprofitable store locations and rejecting related leases, beginning the process of consolidating vendors and implementing purchasing best practices, and implementing targeted headcount reductions – the Debtors' businesses remain cash flow constrained, even though the Debtors are not currently servicing their prepetition obligations. The Debtors cannot emerge from chapter 11 unless (a) the Debtors obtain $55 million in exit financing through the Rights Offering and the Backstop Agreement; (b) the Debtors' $198 million in Senior Notes are converted to equity; (c) the Debtors' estimated $37 million in prepetition general unsecured claims are restructured; (d) the Debtors reject 52 store leases and (e) the Pension Plan is terminated. The Pension Plan is one of the Debtors' significant liabilities that must be eliminated for the Debtors to emerge from these chapter 11 cases as a viable going concern.

29. If the Pension Plan is not terminated, the Debtors would owe approximately $420,300 and $4,739,200 in contributions in respect of the Pension Plan for plan

years 2010 and 2011, respectively. Absent termination of the Pension Plan, for the plan years 2011-2015, the Debtors would be required to make minimum contributions to such plans in the aggregate amount of more than $24 million. Mack Declaration, ¶ 8.

30. The Debtors understand the hardship that the termination of the Pension Plan might create for certain of their current employees and retirees, but note that persons already receiving a pension or eligible to receive a pension in the future will receive such pension after the termination of the Pension Plan, subject to any PBGC-imposed limitations thereon. The Pension Plan, however, is frozen both to new participants and for future accruals for existing participants. As a result, the contribution obligations relate entirely to prepetition periods and do not compensate any current employees for current service. As employees are not currently accruing benefits under the Pension Plan, and benefits accrued previously are insured by the PBGC (subject to statutory-imposed limits), the Debtors believe that the hardship on employees and retirees will be very limited.

31. The Debtors, in conjunction with their professionals, have sought other ways to reduce their pension funding obligations short of terminating the Pension Plan. The Debtors have (a) "frozen" the Pension Plan (i.e., eliminated future benefit accruals) as of June 30, 2007; and (b) considered whether funding waivers from the Internal Revenue Service would be sufficient to relieve the financial burden imposed by continuing contributions to the Pension Plan. These alternatives, however, do not provide the reduction in pension funding obligations that the Debtors require.

32. First, using normal, ongoing assumptions, "freezing" the Pension Plan has resulted in an insufficient reduction of the funding obligation. Irrespective of the ultimate configuration of the reorganized entity, the reorganized entity could not possibly obtain the

necessary exit financing to emerge from these chapter 11 cases without the actual termination of the Pension Plan. Second, funding waivers would just "borrow" from the Pension Plan, and increase future contributions with interest. Kicking the problem down the road does not solve the problem and is unacceptable to the providers of the Debtors' exit equity financing.

The Debtors Must Terminate the Pension Plan
To Obtain Exit Financing and Confirm a Chapter 11 Plan

33. To emerge from these chapter 11 cases and continue to operate as a going concern, the Debtors require $55 million in equity exit financing (a) to repay the Debtors' $55 million Noteholder DIP Facility and (b) to obtain the $100 million ABL Exit Facility. The proceeds of the ABL Exit Facility are necessary to (i) repay any draws under the ABL DIP Facility and (ii) fund the Debtors' post-emergence operations. As the result of an extensive DIP financing marketing process, the Debtors were able to secure a commitment of up to $100 million in debtor in possession financing (the "ABL DIP Facility") and the $100 million ABL Exit Facility from UBS Securities LLC, as lead arranger, UBS Loan Finance LLC, as a lender and as a swingline lender, UBS AG, Stamford Branch, as issuing bank, administrative collateral agent and administrative agent (collectively, "UBS" and Ally Commercial Finance LLC (together with UBS, the "ABL Lenders"). The commitment letter from the ABL Lenders provides for $100 million first lien ABL DIP Facility converts to the $100 million first lien ABL Exit Facility upon confirmation of the Plan. Augustine Declaration, ¶¶ 9-11.

34. Through the Debtors' investment banker Rothschild, Inc. ("Rothschild"), the Debtors aggressively sought debtor in possession and exit loan financing from a broad range of potential lenders and other providers of financing. The parties contacted included (a) traditional lenders such as asset-based lenders and banks and (b) non-traditional lenders such as hedge funds and private equity firms. In total, Rothschild contacted 47 such potential lenders

consisting of 26 traditional lenders and 21 non-traditional lenders. Rothschild sent confidentiality agreements to 39 of these potential lenders and 23 potential lenders signed confidentiality agreements allowing them to receive confidential information about the Debtors. Among these potential lenders, 15 attended meetings with the Debtors' management, and ultimately 3 potential lenders provided the Debtors with financing commitment letters. As a result of this process, the Debtors were able to obtain a commitment for $100 million in first lien debtor in possession and exit financing from the DIP ABL Lenders and a commitment for the $55 million Noteholder DIP Facility. Augustine Declaration, ¶¶ 10, 11.

35. None of the potential lenders provided the Debtors with a commitment for $155 million in exit debt financing. In any case, the Debtors do not believe that the proper capital structure emerging from chapter 11 should include that much debt. To secure the necessary capital to emerge from these chapter 11 cases, the Debtors obtained an additional $55 million in exit equity financing to repay the $55 million Noteholder DIP Facility. As discussed above, the Debtors expect to secure this additional $55 million in exit financing through the Rights Offering. To ensure that the Debtors will have at confirmation the full $55 million in Rights Offering proceeds, the Debtors entered into the Backstop Agreement pursuant to which the Debtors are obligated to terminate the Pension Plan to protect the viability of the business post-confirmation. Augustine Declaration, ¶¶ 10-14.

36. Currently, the claims of the Noteholders are *parri passu* with the claims of the PBGC. If the Debtors were to retain the Pension Plan post-emergence, however, the Noteholders' claims that are being converted to equity under the Plan would be subordinated to the claims of the PBGC, whose contingent claims would essentially be left unimpaired if the Pension Plan is not terminated. The overhang of the Pension Plan liability, would, therefore,

impair the equity of the Noteholders. In a liquidity event, such as a sale, capital raise or subsequent bankruptcy filing (a "Liquidity Event"), the Debtors would face a substantial PBGC obligation overhang that would significantly reduce, or potentially eliminate, the equity returns and recoveries to the Noteholders, whose equity commitment is critically necessary to the Debtors' ability to confirm *any* chapter 11 plan and emerge from these chapter 11 cases. Augustine Declaration, ¶ 19.

37. As a result, absent termination of the Pension Plan, the Noteholders were not willing to provide the Debtors with the $55 million equity commitment necessary to allow the Debtors to emerge from these chapter 11 cases, nor, without such termination, are the Noteholders willing to support the Plan. Without the Debtors' agreement to terminate the Pension Plan, and eliminate any overhang on the reorganized Debtors' equity, the Noteholders would not agree to provide the Debtors with equity financing, nor would the Noteholders agree to convert their notes to equity. In fact, the commitment of the Noteholders to provide $55 million in exit financing to the Debtors, and the Noteholders' plan support agreement, is conditioned on the termination of the Pension Plan. Augustine Declaration. ¶ 20.

38. It would be unreasonable to expect the Noteholders, or any investor, to commit $55 million in new equity absent a termination of the Pension Plan. For the same reasons, it is unlikely that an alternative equity investor would agree to provide $55 million in exit equity financing to the Debtors without conditioning such investment on termination of the Pension Plan. Augustine Declaration, ¶ 21.

39. As a result, it is reasonable that the Noteholders would condition their commitment to invest $55 million in the Debtors on termination of the Pension Plan. In light of (a) the risk of incurring a significant pension liability in a Liquidity Event that could wipe out all

or a significant portion of the Noteholders' new equity investment and (b) the burden of a long term liability that provides no corresponding benefit to equity or to the reorganized Debtors, it would be unreasonable to expect the Noteholders to agree to retain the Pension Plan. Augustine Declaration, ¶ 22.

40. Accordingly, the Debtors have determined that termination of the Pension Plan is required to obtain the exit financing necessary to confirm a chapter 11 plan, and therefore, is the best and only alternative available to emerge from bankruptcy. Without the termination of the existing pension benefit obligations, there is simply no chapter 11 plan that will produce viable emerging entities.

<u>Satisfaction of Applicable Legal Standards</u>

41. The Debtors satisfy each of the prongs of the Reorganization Test. First, each of them is currently a debtor under chapter 11 of the Bankruptcy Code, which is currently pending. Second, the PBGC will be served with a copy of this Motion. Finally, the Debtors meet the financial necessity prong of the test for the reasons set forth.

42. To comply with the requirement that the plan administrator provide a NOIT to each person who is an affected person at least 60, but not more than 90, days prior to the proposed termination date, the Debtors will timely send a NOIT to all affected parties, including filing the Form 600 with the PBGC.

43. Therefore, for the reasons stated herein, the Debtors submit that the relief requested in the Motion can and should be approved.

<u>Request that Order be Made Immediately Applicable</u>

44. The Debtors request that any order entered approving this Motion be made immediately applicable. Bankruptcy Rule 6004(g) provides that "[a]n order authorizing the use, sale, or lease of property . . . is stayed until the expiration of 10 days after entry of the order,

unless the court orders otherwise." Because the Debtors and the Pension Plan participants require certainty as to the termination of such plans and due to the number of actions and communications to affected parties, including plan participants and the PBGC that must precede the termination and creation of the Pension Plan, the Debtors request that any order granting some or all of the relief requested in this Motion be made immediately applicable, pursuant to Bankruptcy Rule 6004(g).

Notice

45. Notice of this Motion shall be provided to: (a) the Office of the United States Trustee for the District of Delaware; (b) counsel to the Creditors' Committee; (c) counsel to the Debtors' postpetition secured lenders; (d) the PBGC; and (e) the parties that have requested notice pursuant to Bankruptcy Rule 2002. In light of the nature of the relief requested herein, the Debtors respectfully submit that no other or further notice is required.

No Prior Request

46. No prior request for the relief sought in this Motion has been made to this or any other court in connection with these chapter 11 cases.

WHEREFORE, the Debtors respectfully request that the Court enter an order, substantially in the form attached hereto as Exhibit D: (i) determining that the financial requirements for a "distress termination" of the Pension Plan under 29 U.S. C. § 1341(c)(2)(B) are satisfied; (ii) approving the termination of the Pension Plan under 29 U.S.C. § 1341(c)(2)(B) and section 363(b) of the Bankruptcy Code; and (iv) granting such other and further relief as the Court may deem proper.

Dated: May 9, 2011
Wilmington, Delaware

Respectfully submitted,

/s/ Zachary I. Shapiro

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ATTORNEYS FOR THE DEBTORS

EXHIBIT A

UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re	:	Chapter 11
HARRY & DAVID HOLDINGS, INC, *et al.*,[1]	:	Case No. 11-______ (____)
Debtors.	:	(Joint Administration Pending)

DECLARATION OF KAY HONG IN SUPPORT OF FIRST-DAY PLEADINGS

1. I am a Managing Director at Alvarez & Marsal in its North America Commercial Restructuring Group and currently serve as the Interim Chief Executive Officer and Chief Restructuring Officer of Harry & David Holdings, Inc. ("Parent"), a Delaware corporation, Harry and David, an Oregon corporation, Harry & David Operations, Inc., a Delaware corporation, and Bear Creek Orchards, Inc., a Delaware corporation (collectively, the "Debtors"). I have held these positions with the Debtors since February 18, 2011.

2. In my prior engagements at Alvarez & Marsal, I have served as an officer at Spiegel, Inc. and Movie Gallery, Inc. and as a financial adviser to Eddie Bauer Holdings, Inc. and the secured lenders of Legacy Estates Group and Oriental Trading Company, among others. Prior to joining Alvarez & Marsal, I served as Director of Finance at Teledesic LLC, a satellite telecommunications company, worked in the Equity Research Division of Goldman Sachs & Co. and served as a Management Consultant with the San Francisco Consulting Group (acquired by KPMG Consulting). I earned a bachelor's degree from Stanford University and a master's degree

1 The Debtors are the following four entities (the last four digits of their respective taxpayer identification numbers, if any, follow in parentheses): Harry & David Holdings, Inc. (4389); Harry and David (1765); Harry & David Operations, Inc. (1427); Bear Creek Orchards, Inc. (7216). The address of each of the Debtors is 2500 South Pacific Highway, Medford, Oregon 97501.

in business administration from Harvard Business School. I am a member of the Turnaround Management Association and the Association of Insolvency and Restructuring Advisors and am a Certified Insolvency and Restructuring Advisor.

3. On the date hereof (the "Petition Date"), each of the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"), as well as certain motions and other pleadings (the "First Day Pleadings") with this Court. I am authorized by the Debtors to submit this Declaration on their behalf in support of the First Day Pleadings.

4. The First Day Pleadings are intended to enable the Debtors to operate effectively and efficiently within these chapter 11 cases, as well as avoid certain adverse consequences that might otherwise result from the commencement of such cases. Among other things, the First Day Pleadings seek relief aimed at maintaining: (a) the loyalty of the Debtors' customers; (b) the confidence of the Debtors' various stakeholders; and (c) the morale of the Debtors' employees. Gaining and retaining the support of these key constituencies is critical to the Debtors' efforts to successfully reorganize. I have reviewed the First Day Pleadings, and it is my belief that the relief sought therein is necessary to: (a) avoid immediate and irreparable harm to, and ensure the uninterrupted operation of, the Debtors' business; and (b) maximize and preserve the value of the Debtors' chapter 11 estates.

5. In accordance with these objectives, the Debtors entered into a plan support agreement (the "Plan Support Agreement") just prior to the Petition Date with certain holders of the Debtors' Senior Notes (as defined below). The Plan Support Agreement includes an agreement with those holders to backstop a rights offering that will provide the necessary capital for the Debtors to exit these cases. In addition, the Debtors' existing lenders under their

Prepetition Revolving Credit Facility have agreed to provide similar financing to the Debtors upon their emergence from bankruptcy. In sum, the Debtors have all of the necessary pieces in place to confirm a chapter 11 plan and exit bankruptcy in an expedited manner.

6. In my capacity as Interim Chief Executive Officer and Chief Restructuring Officer, I am familiar with the Debtors' day-to-day operations, financial condition, business affairs and books and records. Except as otherwise indicated, all facts set forth in this Declaration are based upon: (a) my personal knowledge; (b) my review of relevant documents; (c) information supplied to me by other members of the Debtors' management team or professionals retained by the Debtors; or (d) my opinion based upon my experience and knowledge of the Debtors' operations and financial condition. If I were called upon to testify, I could and would testify competently to the facts set forth herein.

7. Part I of this Declaration provides an overview of the Debtors' business. Part II provides a description of the Debtors' corporate and capital structures. Part III provides a discussion of the events that compelled the commencement of these chapter 11 cases. Part IV sets forth the Debtors' plan for these cases, including details regarding a plan of reorganization support agreement the Debtors entered into with certain of their public noteholders and the financing arrangements the Debtors have finalized to meet their capital needs during these cases and after the Debtors exit from bankruptcy. Part V affirms and incorporates the facts that support the relief requested in the First Day Pleadings.

Part I

Overview of the Debtors' Business

8. The Debtors are a leading multi-channel specialty retailer and producer of branded premium gift-quality fruit, gourmet food products and other gifts marketed under the

Harry & David®, Wolferman's® and Cushman's® brands. Signature products and offerings marketed under the Harry & David name include Royal Riviera® pears, Fruit-of-the-Month Club® products, Tower of Treats® gifts and Moose Munch® caramel and chocolate popcorn snacks. Products marketed under the Wolferman's brand include specialty English muffins and other breakfast products, and the Cushman's product line includes Cushman HoneyBells® citrus, among other products. The Debtors' marketing channels include direct marketing (via catalog, phone, Internet, mail/fax and telemarketing), business-to-business, Harry and David stores, seasonal Cushman's stores, and wholesale distribution through select retailers.

9. The Debtors grow, manufacture, design and package products that account for the significant majority of their annual sales revenue. The Debtors own approximately 3,400 acres of land in Oregon, of which approximately 1,900 acres are planted orchards geographically dispersed throughout the Rogue Valley of Southern Oregon at varying elevations and micro-climates. Also included in the 3,400 acres is the Debtors' 93 acre campus in Medford, Oregon, which houses: (a) a 54,000 square foot bakery, confectionery and chocolate complex dedicated to the production of baked goods, chocolates and confections; (b) a 646,000 square foot fruit packing and gift assembly complex, including cold storage; (c) a 72,000 square foot year-round call center and various other distribution and storage facilities. The Debtors owned acreage in Rogue Valley further includes housing for their seasonal agricultural workforce. The Debtors also own a 51-acre campus in Hebron, Ohio that houses a 275,000 square foot fruit packing and gift assembly complex, including cold storage and a 55,000 square foot call center and office space.

10. The Debtors' owned real property and other manufacturing related assets have enabled them to create a substantial and scalable infrastructure in their production,

fulfillment and distribution capabilities, information technology systems and retail stores network. The Debtors maintain vertically integrated operations that allow them to efficiently monitor costs, quality and manufacturing processes and inventory. This vertical integration further allows the Debtors to maintain a high degree of control over product quality compared with that of the Debtors' competitors, as the Debtors rely less heavily on third-party suppliers.

11. The Debtors sell their products primarily through direct marketing and retail stores. The Debtors direct marketing consists of the distribution of various catalogs, other direct mail and the Internet. The Debtors also operate approximately 70 permanent retail stores. The Debtors' stores are located generally in leading outlet and lifestyle centers, specialty malls and other high traffic shopping areas throughout the United States. In addition, the Debtors operate a single flagship Country Village store in Medford, Oregon, which offers the full selection of Harry and David retail products as well as expanded offerings consisting of fresh fruit, vegetables and produce, gourmet specialty foods and wine selections.

12. A significant portion of the Debtors' net sales, earnings and cash flows are generated during the holiday season from October through December. Accordingly, the Debtors' annual operating results and their liquidity are materially impacted by the holiday season. For example, in fiscal 2010, as is typical for their businesses, over 60 percent of the Debtors' revenues were generated during the holiday season and that was the only fiscal quarter during which the Debtors generated positive cash flows or operating income.

13. The Debtors employ approximately 1,950 full-time employees. The Debtors also typically employ thousands of seasonal employees. For the twelve months ending December 25, 2010, the Debtors generated approximately $416 million in revenue. As of

December 25, 2010, the Debtors had approximately $304 million in assets and approximately $361 million in liabilities.

Part II

Corporate and Capital Structure of the Debtors

Corporate Structure

14. The Parent is a holding company that owns, directly or indirectly, each of the other Debtors. In general, Wasserstein & Company, LP, or affiliates thereof ("Wasserstein"), own approximately 63 percent of the Parent's outstanding shares. Affiliates of funds sponsored by Highfields Capital Management LP own approximately 34 percent of the Parent's outstanding shares. Employees or former employees of the Debtors own the remaining outstanding shares of the Parent.

15. The Parent holds 100 percent of the outstanding shares of Harry and David. In turn, Harry and David owns 100 percent of the outstanding shares of Harry & David Operations, Inc. and Bear Creek Orchards, Inc. Harry and David functions as the Debtors' primary marketer and seller of products. Harry and David Operations, Inc. is responsible primarily for the manufacture of goods sold by the Debtors. Bear Creek Orchards, Inc. holds legal title to the Debtors' orchards.

Prepetition Capital Structure

16. As of the Petition Date, the Debtors' primary liabilities consisted of: (a) two series of senior unsecured notes; (b) pension obligations; (c) unsecured trade debt; and (d) lease obligations.[2] These liabilities are described in more detail below.

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[2] The Debtors are party to a Credit Agreement, dated March 20, 2006 (as amended) with GMAC Commercial Finance LLC, as Collateral Agent and Documentation Agent, UBS Securities LLC, as Arranger, UBS AG Stamford Branch, as Issuing Bank, Administrative Collateral Agent and Administrative Agent, and UBS Finance LLC, as Swingline Lender, that provided the Debtors with a $105 million

Senior Unsecured Notes

17. The Debtors had approximately $58 million of Senior Floating Rate Notes due March 1, 2012 and $140 million of Senior Fixed Rate Notes due March 1, 2013 (collectively, the "Senior Notes") outstanding as of the Petition Date. A single indenture (the "Indenture"), dated February 25, 2005, governs both series of Senior Notes and Wells Fargo Bank, N.A. is the indenture trustee.

18. The Senior Notes represent senior unsecured obligations of Harry and David and are guaranteed by the other Debtors. The Senior Floating Rate Notes accrue interest at a rate per annum equal to LIBOR plus 5 percent calculated and paid quarterly. The Senior Fixed Rate Notes accrue interest at an annual fixed rate of 9 percent, with seminannual interest payments.

19. In fiscal 2008 and fiscal 2009, the Debtors repurchased approximately $34.8 million of then outstanding Senior Fixed Rate Notes and $11.8 million of the then outstanding Senior Floating Rate Notes. The Debtors offically cancelled $22.2 million of the repurchased Senior Fixed Rate Notes and $2 million of the repurchased Senior Floating Rate Notes, and the Debtors hold the remaining repurchased notes. The amounts listed in this paragraph are in addition to the $198 million of outstanding Senior Notes described above.

(continued...)

revolving credit facility (the "Prepetition Revolving Credit Facility"). Borrowings under the Prepetition Revolving Credit Facility are secured by substantially all of the Debtors' assets. As of the Petition Date, the Debtors had no outstanding borrowings under the Prepetition Revolving Credit Facility.

Pension Obligations

20. As of June 26, 2010, the Debtors had listed in their books and records approximately $30 million in obligations relating to the underfunding of the Harry and David Employees' Pension Plan (the "Pension Plan"). Effective June 30, 2007, the Debtors froze benefit accruals under the Pension Plan. The Debtors fund the Pension Plan in accordance with statutory funding requirements; as such, the timing of any future payments is subject to a number of factors and uncertainties and could change. For instance, the Debtors' required level of funding of the Pension Plan changes each year depending on the funded status of the pension plan, applicable interest rates and actuarial factors applied by the Debtors' actuaries.

Unsecured Trade Debt

21. In the ordinary course of operating their direct marketing and retail business, the Debtors have historically purchased raw materials and other goods and services from over 1400 vendors. Significant raw materials the Debtors purchase from third party vendors include paper for the Debtors' catalogs, corrugated paper for delivery needs, and chocolate, butter, cheese and certain fruit that the Debtors do not produce or grow themselves. In addition, the Debtors outsource some of their products, including selected fresh produce, meats, certain confections, snacks, condiments and tabletop, entertaining and home décor accessories. As of the Petition Date, the Debtors estimate that they owe approximately $37 million for raw materials and other unsecured obligations for goods and services.

Lease Obligations

22. The Debtors operate approximately 70 stores in leading outlet and lifestyle centers, specialty malls and other high traffic shopping areas throughout the United States. In addition, the Debtors are responsible for lease payments with respect to 52 other store locations where the Debtors' ceased operations prior to the Petition Date. The Debtors are seeking to

reject the leases for these store locations as of the Petition Date. The Debtors also lease storage or warehouse space at approximately 12 locations. Prior to the Petition Date, the Debtors approximate annual expense for leased properties was approximately $19 million.

Part III

Events Leading to the Commencement of These Cases

23. For nearly 75 years, the Debtors thrived as an industry leading catalog retailer. Over the course of this time, the Debtors developed significant brand equity, high customer awareness and distinctive ownership of fruit gifting. The Debtors further benefited from the high barriers of entry for potential competitors that resulted from the expenses associated with printing and mailing catalogs and the length of time necessary to develop a profitable customer base. Over the course of the last several years, however, various external market factors have diminished the Debtors' competitive advantages and, correspondingly, revenues and profitability.

24. Specifically, the Internet has allowed numerous additional direct competitors to enter the Debtors' market. Unlike the Debtors, who manufacture approximately 85 percent of their own products in house, these new entrants typically outsource non-proprietary products from cost-advantaged manufacturers. As such, these new entrants generally possess lower overhead costs than the Debtors.

25. "Big box" retailers also have begun to sell products that compete with those of the Debtors. Similar to the Debtors' new direct competitors, the "big box" retailers possess certain cost advantages over the Debtors, and the addition of the "big box" retailers have further increased competition for the Debtors, placing more downward pressure on pricing.

26. Recognizing the existence of an emerging number of low cost competitors, the Debtors focused on the quality of their products. However, consumers have

become extremely price conscious following the beginning of the 2008 recession, and this consciousness continues to materially impact the Debtors' ability to maintain higher selling prices. The Debtors' financial performance over the past three years is a reflection of this trend, as consumer price consciousness caused the Debtors to discount their products more significantly than they had expected previously. Additionally, during the 2010 holiday season, the Debtors expected a significant improvement in sales performance, which ultimately did not materialize. In order to clear inventory purchases, the Debtors were forced to discount even more heavily than anticipated.

27. As a result, the Debtors failed to generate enough cash flow during the 2010 holiday season to satisfy the minimum available cash covenant contained in the Prepetition Revolving Credit Facility, and the Debtors were unable to continue borrowing under the Prepetition Revolving Credit Facility. [3]

28. After losing the ability to borrow under the Prepetition Revolving Credit Facility and facing a significant liquidity shortfall as a result of their 2010 holiday season results, the commencement of these cases became necessary to (a) address the Debtors' liquidity needs and (b) provide the opportunity to, among other things, right-size the Debtors' business though (i) structural improvements and (ii) the evaluation and elimination of liabilities that only serve as a drain on the Debtors' profitability. In accordance with these objectives, the Debtors closed 52 unprofitable stores just prior to the Petition Date. The Debtors have filed a motion to reject each of the closed stores' leases, effective as of the Petition Date. The closing of unprofitable stores and rejection of the associated leases will result in immediate cost savings in respect of overhead,

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3 Specifically, the Prepetition Revolving Credit Facility required that the Debtors maintain an available net cash balance (defined as cash, cash equivalents and short-term investments, minus accounts payable) of at least $50 million as of December 31 of each year.

rent and other payments and represents one step in the Debtors' efforts to streamline their operations.

Part IV

The DIP Credit Facilities and Restructuring Support Agreement

29. After determining that the commencement of these cases was necessary, the Debtors, with the assistance of their professional advisors, explored various options with respect to postpetition financing. After engaging in productive discussions with potential investors and lenders, the Debtors determined that financing proposals by the existing lenders under their Prepetition Revolving Credit Facility and a proposal by an ad hoc committee of holders of the Senior Notes (the "Ad Hoc Committee") and Wasserstein, also a holder of Senior Notes, provided the Debtors with the best opportunity to emerge from these cases in a timely manner and maximize the value of their estates. In combination, these proposals provide the Debtors with the necessary access to working capital during these case as well as financing to exit these cases. In addition, the Debtors have obtained the agreement of a significant number of their public noteholders for the structure of a chapter 11 plan, as set forth in the Plan Support Agreement with the Ad Hoc Committee, to exit these chapter 11 cases.

Postpetition Financing

30. The Debtors' proposed postpetition financing consists of a first lien and a separate second lien credit facility. The first lien credit facility (the "First Lien DIP Credit Facility") is a $100 million revolving credit facility provided by the Debtors' existing lenders under the Prepetition Revolving Credit Facility (the "First Lien DIP Lenders"). Borrowings under the First Lien DIP Credit Facility will be secured by a first priority lien on substantially all of the Debtors' assets, with the exception of funds held in a single bank account that holds proceeds from the Second Lien DIP Credit Facility (as defined below). The First Lien DIP

Credit Facility will enable the Debtors to purchase necessary inventory later in the year as they work towards the 2011 holiday season. In addition, the First Lien Revolving Credit Facility essentially will act as the Debtors' exit facility, as the First Lien DIP Lenders have provided a commitment to provide a similar revolving credit facility to the Debtors upon their emergence from these chapter 11 cases.

31. In addition to the First Lien DIP Credit Facility, members of the Ad Hoc Committee (the "Second Lien DIP Lenders") and Wasserstein, also a holder of Senior Notes, will provide a $55 million second lien term loan (the "Second Lien DIP Credit Facility") to the Debtors. Borrowings under the Second Lien DIP Credit Facility will be secured by a lien on substantially all of the Debtors' assets, and such lien will be subordinate only to the lien granted under the First Lien DIP Credit Facility. The Second Lien DIP Credit Facility will provide the Debtors with the necessary working capital to operate during the course of these cases as they work towards the confirmation of a plan of reorganization.

The Plan Support Agreement

32. The Debtors, the Ad Hoc Committee and Wasserstein, also a holder of Senior Notes, entered into a plan support agreement (the "Plan Support Agreement") just prior to the Petition Date that sets forth the structure for a plan of reorganization that will allow the Debtors to emerge from these cases on an expedited basis. A copy of the Plan Support Agreement is attached hereto as Exhibit A.

33. The Plan Support Agreement contemplates that the holders of the Senior Notes will receive a pro rata share of approximately 166,667 shares of the reorganized Debtors' common stock. Unsecured creditors, other than holders of the Senior Notes, may elect to receive: (i) the same pro rata share of the reorganized Debtors' common stock as the holders of Senior Notes; (ii) subject to the availibility of necessary cash, a cash distribution, equal to 75

percent of the plan value of the unsecured creditors' pro rata share of the reorganized Debtors' common stock; or (iii) a promissory note that would (a) equal the value of the unsecured creditors' pro rata share of the reorganized Debtors' common stock (based on the plan value thereof), (b) accrue interest at 6 percent per annum and (c) mature on the date that is 7 years after the effective date of the Debtors' chapter 11 plan.

34. The Plan Support Agreement also contemplates a $55 million rights offering with a backstop commitment from the Ad Hoc Committee and Wasserstein of $55 million. Wasserstein has agreed to backstop 40 percent of the rights offering and to provide management services to the reorganized Debtors. The rights offering will provide the Debtors with the required equity financing to emerge from chapter 11 under the plan of reorganization contemplated by the Plan Support Agreement and is intended to be conducted in connection with the solicitation of votes in connection with such plan. All of the Debtors' creditors that qualify as accredited investors under applicable SEC law and possess an allowed claim will have the opportunity to participate in this rights offering.

35. In summary, the Debtors believe that confirming a chapter 11 plan in the form contemplated under the Plan Support Agreement is in the best interests of the Debtors' estates and their creditors. The Plan Support Agreement, however, does not restrict the Debtors from fulfilling their fiduciary duties. Accordingly, the Debtors may terminate the Plan Support Agreement in the event that supporting the plan contemplated under the Plan Support Agreement no longer is in the best interests of the Debtors' estates.

Part IV

Facts Relevant to the First Day Pleadings

36. Concurrently with the filing of these chapter 11 cases, the Debtors filed the First Day Pleadings requesting various forms of relief. Generally, the First Day Pleadings

have been designed to meet the Debtors' goals of: (a) continuing their operations in chapter 11 with as little disruption and loss of productivity as possible; (b) maintaining the confidence and support of their customers, employees, vendors, suppliers and service providers during the Debtors' reorganization process; and (c) establishing procedures for the smooth and efficient administration of these chapter 11 cases.

37. I have reviewed each of the First Day Pleadings filed contemporaneously herewith (including the exhibits thereto and supporting memoranda) and incorporate by reference the factual statements set forth in the First Day Pleadings. It is my belief that the relief sought in each of the First Day Pleadings is tailored to meet the goals described above and, ultimately, will be critical to the Debtors' ability to achieve a successful reorganization.

38. It is my further belief that, with respect to those First-Day Pleadings requesting the authority to pay discrete prepetition claims or continue selected prepetition programs (e.g., those First-Day Pleadings seeking relief related to the Debtors' obligations to their vendors, employees, customers, shippers and other distribution network providers, potential PACA[4] claimants, foreign vendors, reclamation claimants, taxing authorities and insurers), the relief requested is essential to the Debtors' reorganization and necessary to avoid immediate and irreparable harm to the Debtors and their employees, customers and affected vendors.

39. Impairment of the Debtors' business operations, or of their relationships with their employees, customers or vendors — at the very time when the smooth operation of those operations and the dedication, confidence and/or cooperation of those constituencies is most critical — would clearly imperil the Debtors' chances of a successful reorganization. The Debtors operate in a highly competitive sector of the domestic economy. Any diminution in the

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4 The Perishable Agricultural Commodities Act of 1930, as amended, 7 U.S.C. §§ 499a et seq.

Debtors' ability to maintain their operations in the ordinary course will have an immediate and irreparable harmful impact upon the going concern value of the estates to the detriment of all of the Debtors' stakeholder constituencies. The Debtors believe that payment of those selected prepetition claims identified in the First Day Pleadings will forestall such irreparable harm and that all creditors of the Debtors will ultimately benefit from the relief requested therein.

40. The Debtors' reorganization depends in large part on restoring vendor, customer and employee confidence and maintaining the operation of their business as they restructure. Accordingly, the Debtors have an immediate need to continue the orderly operation of their business by securing goods and paying employees in the normal course of business. The Debtors' continued operations will enable the Debtors to preserve the going concern value of their estates and re-establish any lost vendor and customer confidence, thereby maximizing recoveries for the Debtors' stakeholders. Further, the Debtors believe that such relief will enable them to stabilize operations and ultimately, in conjunction with a reorganization, restore their profitability.

Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge, information and belief.

Dated: March 28, 2011
Medford, Oregon

Kay Hong

EXHIBIT B

UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re	:	Chapter 11
HARRY & DAVID HOLDINGS, INC, *et al.*,[1]	:	Case No. 11-10884 (MFW)
Debtors.	:	(Jointly Administered)

DECLARATION OF KAREN M. MACK IN SUPPORT OF MOTION OF THE DEBTORS FOR AN ORDER (A) DETERMINING THAT THE FINANCIAL REQUIREMENTS FOR A DISTRESS TERMINATION OF THEIR DEFINED BENEFIT PENSION PLAN ARE SATISFIED; AND (B) APPROVING A DISTRESS TERMINATION OF THE PENSION PLAN

I, Karen M. Mack, declare as follows:

1. I am an actuary employed by the firm Altman & Cronin Benefit Consultants, LLC ("Altman & Cronin"), which is the actuary for the above-captioned debtors' (collectively, the "Debtors") defined benefit pension plan, the Harry and David Employees' Pension Plan (the "Pension Plan"). I submit this declaration in support of the Motion of the Debtors for an Order (A) Determining that the Financial Requirements for a Distress Termination of Their Defined Benefit Pension Plan are Satisfied; and (B) Approving a Distress Termination of the Pension Plan (the "Pension Motion").[2] Except as otherwise noted,[3] I have personal knowledge of the matters set forth herein.

1 The Debtors are the following four entities (the last four digits of their respective taxpayer identification numbers, if any, follow in parentheses): Harry & David Holdings, Inc. (4389); Harry and David (1765); Harry & David Operations, Inc. (1427); Bear Creek Orchards, Inc. (7216). The address of each of the Debtors is 2500 South Pacific Highway, Medford, Oregon 97501.

2 Unless otherwise defined herein, capitalized terms shall have the meaning ascribed to such terms in the Pension Motion.

2. My educational background includes a Bachelor of Arts degree in mathematics, with honors, from the University of Notre Dame. I am a Fellow of the Society of Actuaries and an Enrolled Actuary under ERISA. Furthermore, I am a Member of the American Academy of Actuaries and a Fellow of the Conference of Consulting Actuaries. I have worked as a consulting actuary in the retirement field for over eighteen years and have worked at Altman & Cronin for approximately eight months. In this capacity, I have obtained first-hand knowledge of the Pension Plan that is the subject of the Pension Motion.

3. Harry and David, an Oregon corporation and one of the Debtors, sponsors the Pension Plan covering certain employees of the Debtors. As of January 1, 2010 the Pension Plan had 2,516 plan participants, of which 1,627 were active participants, 229 were retirees in pay status, and the remaining 660 were terminated participants entitled to future vested benefits. The normal retirement age under the plan is 65. Certain employees entitled to "bridge benefits" from a prior plan may commence unreduced retirement benefits at age 62. Benefits earned prior to January 1, 2002 for the non-bridge group are subject to different early retirement and other actuarial conversion factors. The Pension Plan was frozen with respect to all future benefit accruals effective June 30, 2007.

4. The Pension Plan began experiencing significant funding problems with the investment experience of 2008, in which the Pension Plan's investment return was negative (-) 39%. This investment loss, coupled with benefit payments and administrative expenses

(. . . continued)

[3] Certain of the disclosures herein relate to matters within the personal knowledge of other professionals at Altman & Cronin and are based on information provided by them.

during the year, caused the Pension Plan's fair market value to fall from $31,074,000 as of January 1, 2008 to $18,290,000 as of January 1, 2009. This reduction in asset levels is shown after reflecting contributions in the amount of $3,822,000 during 2008 for the 2007 and 2008 plan years. As a result of this asset loss, the Pension Plan's funded status fell dramatically. The funding target attainment percentage ("FTAP") measures the Pension Plan's funded status under the Pension Protection Act of 2006 (the "PPA") and compares the ratio of plan assets to liabilities. The FTAP at January 1, 2008 (before the investment loss) was 73.8% and fell to 47.5% as of January 1, 2009. The FTAP is based on the actuarial value of assets, which was equal to the market value of assets as of January 1, 2008 and utilized a smoothing method as of January 1, 2009 to recognize asset losses over a two year period within a corridor of 10% of the market value of assets. The discount rate for both measurement periods was based on the January segmented yield curve in effect for the valuation year. Changes in the yield curve during that time resulted in an effective interest rate increase from 6.10% to 6.43%, resulting in a decrease in liabilities, which mitigated the asset loss to some degree. The drop below 60% funded status subjected the Pension Plan to benefit restrictions as required under the PPA, as outlined in the Internal Revenue Code Section 436, and the Pension Plan was amended in March 2009 to eliminate the payment of lump sums other than for small benefit cashouts.

5. In 2008 through 2010, the Pension Plan has complied with the funding requirements under the PPA which are designed to bring plans back to a fully funded status over (essentially) a seven year period. As of January 1, 2010 the Pension Plan's FTAP was 53.14%. As of January 1, 2011 it is estimated to be approximately 49% primarily because the decline in interest rates outpaced the investment earnings and contributions to the Pension Plan during 2010.

6. The plan sponsor availed itself of the PPA funding relief for the 2009 plan year, which allowed for delayed amortization of the 2009 unfunded liability. In addition, funding projections were prepared which assumed that Harry and David would also take advantage of funding relief for the 2011 plan year. The Pension Plan has no credit balance and measures assets for funding using a two-year smoothing of gains and losses.

7. Minimum required funding projections were prepared for the five plan years 2011 to 2015. These projections reflected a baseline assumption set assuming that the future discount rate environment remains the same (February 2011 segmented yield rates) and that plan assets are expected to earn 8% per year before offsets for administrative expenses (assumed to remain at 2010 levels) and PBGC premiums. Furthermore, the projections were based on the January 1, 2010 census and fair market value of assets as of January 1, 2011. In projecting future assets, all contributions were expected to be made in a timely manner.

8. Using the baseline assumptions summarized above, the projected contributions under the IRC and ERISA are expected to be $24,228,200 for the five plan years 2011-2015. These are broken down by year as follows:

Plan Year	**Minimum Required Contribution for Plan Year**
2011	$4,739,200
2012	$5,068,600
2013	$5,658,100
2014	$5,637,500
2015	$3,124,800
Total 2011-2015	**$24,228,200**

The minimum required contributions shown above are subject to the timing requirements of the PPA and may be contributed over two calendar years, depending on the quarterly contribution requirements, which are due on April 15th, July 15th, October 15th of the current plan year and

January 15th of the following plan year. The final contribution for the plan year is due by September 15th of the following plan year. The plan year for the Pension Plan is the calendar year. The actual cash contributions to be paid during the calendar years 2011-2015 is $24,859,700. The reason for the difference is timing of the required contributions.

9. The contribution projections listed above are provided on an ongoing basis and assume that all contributions are made to the Pension Plan on the required due dates. For 2011, to preserve liquidity, the Debtors did not make their minimum required quarterly contribution to the Pension Plan due on April 15, 2011 in the amount of $704,000 and in respect of the 2011 plan year. The minimum required contributions to the Pension Plan totaling $420,300 (final contribution for the 2010 plan year) and $4,739,200 (estimated 2011 minimum required contribution) remain to be paid in respect to the 2010 and 2011 plan years, but, with the exception of the April 15, 2011 quarterly installment attributable to the 2011 plan year, are not yet due and owing.

10. If the Pension Plan is terminated, the Pension Benefit Guaranty Corporation (the "PBGC") likely will assert a claim against the Debtors, for the Pension Plan's unfunded liabilities. As of April 30, 2011, the estimated value of the plan liabilities using the assumptions and methodology as set forth under ERISA Section 4044 is $59,045,000. This estimate is based on the most recent PBGC rates available for May 2011 which are 3.96% for the first 20 years following the date of plan termination and 4.32% thereafter and the 2011 PBGC mortality table and mandated retirement ages under 4044 (XRAs). The estimate is based on the January 1, 2010 census. All plan benefits were valued and were not limited to the PBGC maximum or allocated to priority categories.

11. As of April 27, 2011 (the most current date available), the market value of plan assets was $24,601,000. This implies that the unfunded PBGC 4044 liability is $34,444,000. However, since both the asset value and liability values will fluctuate in the future, this is an estimate at the point in time given and not a guarantee of the unfunded obligation in the future. This estimate does not include any termination premium under ERISA Section 4006, nor does the estimate allocate liabilities to priority categories and apply the maximum guaranteed benefit limits. Finally, this is not intended to be the estimate of the entirety of the PBGC claim, which could be based on additional factors including unpaid contributions and upcoming PBGC premium payments.

Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing is true and correct.

Karen M. Mack

Karen M. Mack, FSA, EA, MAAA
Altman & Cronin Benefit Consultants, LLC
100 Pine Street, Suite 1500
San Francisco, CA 94111

EXHIBIT C

UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re	:	Chapter 11
HARRY & DAVID HOLDINGS, INC, *et al.*,[1]	:	Case No. 11-10884 (MFW)
Debtors.	:	(Jointly Administered)

DECLARATION OF NEIL A. AUGUSTINE IN SUPPORT OF MOTION OF THE DEBTORS FOR AN ORDER (A) DETERMINING THAT THE FINANCIAL REQUIREMENTS FOR A DISTRESS TERMINATION OF THEIR DEFINED BENEFIT PENSION PLAN ARE SATISFIED; AND (B) APPROVING A DISTRESS TERMINATION OF THE PENSION PLAN

I, Neil A. Augustine, declare as follows:

1. I am a Senior Managing Director and Co-Head of the North America Debt Advisory and Restructuring Group of the firm Rothschild, Inc. ("Rothschild" or the "Firm"), which has its principal office at 1251 Avenue of the Americas, New York, New York 10020. I submit this declaration (the "Declaration") in support of the Motion of the Debtors for an Order (A) Determining that the Financial Requirements for a Distress Termination of Their Defined Benefit Pension Plan are Satisfied; and (B) Approving a Distress Termination of the Pension

1 The Debtors are the following four entities (the last four digits of their respective taxpayer identification numbers, if any, follow in parentheses): Harry & David Holdings, Inc. (4389); Harry and David (1765); Harry & David Operations, Inc. (1427); Bear Creek Orchards, Inc. (7216). The address of each of the Debtors is 2500 South Pacific Highway, Medford, Oregon 97501.

Plan (the "Pension Motion").[2] Unless otherwise stated in this declaration, I have personal knowledge of the facts set forth herein.[3]

Qualifications

2. Rothschild has extensive experience in providing financial advice and investment banking services to debtors in chapter 11 cases and other corporate financial restructurings.

3. Rothschild is a member of one of the world's leading independent financial advisor and investment banking groups, with more than forty (40) offices in more than thirty (30) countries, including an office located at 1251 Avenue of the Americas, New York, New York 10020. Rothschild has expertise in domestic and cross-border restructurings, mergers and acquisitions, privatization advice, and other financial advisory and investment banking services. A private firm with approximately 220 employees in the United States and offices in New York and Washington, D.C., Rothschild is experienced in providing high quality financial advisory and investment banking services to financially troubled companies. Rothschild is an experienced bankruptcy and restructuring advisor to debtors in a variety of industries. Rothschild is highly qualified to advise on strategic alternatives and its professionals have extensive experience in deals involving complex financial and operational restructurings. Moreover, Rothschild is a member of the Financial Industry Regulatory Authority and the Securities Investor Protection Corporation.

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2 Unless otherwise defined herein, capitalized terms shall have the meaning ascribed to such terms in the Pension Motion.

3 Certain of the statements made herein relate to matters within the personal knowledge of other professionals at Rothschild or the Debtors' employees or advisors and are based on information provided by them.

4. Rothschild and its professionals have extensive experience working with financially troubled companies from a variety of industries in complex financial restructurings, both out-of-court and in chapter 11 cases. Rothschild's business reorganization professionals have served as financial advisor and investment banker in numerous cases, including, among others: Atlantic Express Transportation Group, Barney's, Inc., Bedford Fair Industries, BHM Technologies Holdings, Inc., Blockbuster, Inc., Bradlees', Inc., Cadence Innovation LLC, Circuit City Stores, Inc., Comdisco, Inc., Crown Vantage, Inc., Delphi Corporation, Edison Brothers Stores, Inc., Fairpoint Communications, Inc., Federal Mogul Corp., Friedman's, Inc., Geneva Steel Company, Globe Manufacturing, Guilford Mills, Inc., Heartland Steel, HomePlace, Inc., Hilex Poly Co. LLC, International Wire Group, James River Coal Company, Key Plastics LLC, La Roche Industries, Inc., Leiner Health Products, Inc., Metromedia International Group, Inc., Milacron Inc., Motor Coach Industries, Inc., Mpower Holdings Corp., Neenah Enterprises, Inc., New World Pasta Company, Northwest Airlines, Inc., Oxford Automotive, Inc., Pacific Gas & Electric Company, PPI Holdings, Inc., Penton Business Media Holdings, Inc., Recycled Paper Greetings, Inc., Remy Worldwide Holdings, Inc., Sbarro, Inc., Sea Launch Co., LLC, Service Merchandise Corp., Special Metals Corporation, Solutia, Inc., Superior Telecom Inc., Sun-Times Media Group, Inc., The FINOVA Group Inc., Thermadyne Holdings Corp., Thorn Apple Valley, Inc., Tower Automotive, Trans World Airlines, Trident Resources Corp., Today's Man, Inc., Tronox Inc., UAL Corporation, VeraSun Energy Corporation, Viasystems Group, Inc., Visteon Corp., WestPoint Stevens, Inc., Werner Holding Company, Wilcox & Gibbs, Inc. and Zenith Electronics, Inc.

5. I hold a Bachelor of Arts degree and a Masters of Business Administration from the University of Rochester. I began my career at Chemical Bank where I was actively

involved in advising both debtors and creditors as well as providing debtor-in-possession financing. Thereafter, I became one of the founding members of The Blackstone Group's Restructuring and Reorganization Financial Advisory Department. After leaving the Blackstone Group, I held positions as the Director of Distressed Debt Research at Lehman Brothers, Inc. and as the Director of Research at Whippoorwill Associates, Inc., a $600 million money management firm specializing in purchasing claims in financially troubled companies. Prior to joining Rothschild in April 2001, I was the Group Portfolio Manager for the Distressed Debt Group of Morgens, Waterfall, Vintiadis & Company Inc., a New York-based, S.E.C.-registered investment advisor with approximately $1 billion of capital under management. I have previously served on the boards of United Artists Theatre Company, Safeguard Business Systems, Inc., The Grand Union Company and American Blind and Wallpaper Factory, Inc., and am currently on the board of Cotton Holdings, Inc.

6. I have more than twenty-one years experience in investing in and advising distressed companies and their creditors. I have substantial experience marketing, structuring and evaluating debtor-in-possession financings, secured debt, exit financing, unsecured debt, rights offerings and preferred and common stock.

7. I have been involved in out-of-court and in-court restructurings in the United States, Europe, Canada and Mexico. The bankruptcy-related matters in which I have testified at deposition and/or at trial include, but are not limited to, cases involving the following debtors: Blockbuster, Inc., Trump Entertainment Resorts, Inc., FairPoint Communications, Inc., Atlantic Express Transportation Group, New World Pasta Corp., VeraSun Energy, Innovative Communications Corp., Werner Ladder Co., Motor Coach Industries, Milacron Inc. and WestPoint Stevens, Inc.

8. Since its retention on December 17, 2010, Rothschild has provided extensive investment banking services to the Debtors in preparation for the Debtors' restructuring efforts. As a result of the work performed on behalf of the Debtors, Rothschild has acquired significant knowledge of the Debtors and its businesses and is intimately familiar with the Debtors' financial affairs, operations and related matters.

The DIP and Exit Financing

9. During the month leading up to the Petition Date, it became clear that Harry & David required a significant capital infusion to continue to operate. Due to the Debtors' seasonal working capital requirements, the Debtors' asset based lending facility did not provide a sufficient borrowing base to fund the operations from the end of the holiday selling season to the beginning of the next investment in inventory (typically August). The Debtors' business plan projected a liquidity shortfall, and the Debtors determined that approximately $155 million of financing would be required to operate their business from the Petition Date to the end of the holiday selling season with the requisite financial flexibility. Following this determination, Rothschild began a process to solicit proposals for debtor-in-possession and exit financing.

10. Rothschild aggressively sought debtor-in-possession and exit loan financing for the Debtors from a broad range of potential lenders and other providers of financing. The parties contacted included (a) traditional lenders such as asset-based lenders and banks and (b) non-traditional lenders such as hedge funds and private equity firms. In total, Rothschild and the Debtors solicited indications of interest from approximately 47 sophisticated financial institutions, hedge funds and alternative lenders active in the DIP market in an effort to obtain proposals for debtor in possession and exit financing. The Debtors executed confidentiality agreements with 23 of these parties and provided a management presentation to 15 of these parties. Additionally, the Debtors signed confidentiality agreements with and

provided the management presentation to four prepetition noteholders. However, Rothschild received only three commitment letters for financing, which reflected the Debtors' challenging operating environment. More significantly, only two of the commitment letters contained committed exit financing. None of the other parties expressed interest in exit financing.

11. As the result of the marketing process, the Debtors were able to secure a commitment of up to $100 million in debtor in possession and exit financing (the "ABL Facility") from UBS Securities LLC, as lead arranger, UBS Loan Finance LLC, as a lender and as a swingline lender, UBS AG, Stamford Branch, as issuing bank, administrative collateral agent and administrative agent (collectively, "UBS" and Ally Commercial Finance LLC ("Ally" and together with UBS, the "ABL Lenders"). The Debtors also were able to secure $55 million in second lien debtor-in-possession financing facility (the "Noteholder DIP Facility") from approximately 81% of the holders of the Debtors' Senior Notes (the "Noteholders").

12. The ABL Facility contained the following express conditions: (i) the confirmation of a plan of reorganization reasonably acceptable to the Lenders and the occurrence of the effective date of such plan of reorganization, (ii) *the repayment in full of the Noteholder DIP Facility pursuant to an equity rights offering or the conversion to equity of any claims outstanding pursuant to the Noteholder DIP Facility*, (iii) *the conversion to equity of any claims outstanding on account of the Senior Floating Rate Notes due 2012 and the 9% Senior Fixed Rate Notes due 2013*, (iv) completion of review of capital and corporate structures of reorganized Borrowers, which structures shall be reasonably satisfactory to the Administrative Agent and the Collateral Agent (and which shall not include a "diligence out"), and (v) such other reasonable and customary conditions as may be required by the Lenders.

13. In order to secure the $100 million DIP financing and exit financing ABL Facility commitments the Debtors must raise $55 million and convert the outstanding Senior Notes to equity. The Debtors intend to raise the required $55 million in equity in the form of a rights offering (the "Rights Offering"). The proceeds of the Rights Offering will repay the Debtors' second lien, $55 million Noteholder DIP Facility. The $100 million ABL Exit Facility will be used to (a) refinance any draws under the ABL DIP Facility (as defined below) and (b) fund the Debtors' post-emergence operations, permitting the Debtors to exit chapter 11.

14. In connection with the anticipated Plan, eligible holders of the Senior Notes will be entitled, as part of the Rights Offering, to purchase stock in the reorganized Debtors at the price specified in the Plan, which will be at a discount to the assumed "plan value" for such stock under the Plan. There is no guaranty, however, that all eligible holders of the Senior notes will choose to participate in the Rights Offering. As such, to ensure that the Debtors will have at confirmation the full $55 million to repay amounts owing under the Noteholder DIP Facility, and exit these chapter 11 cases, the Debtors also entered into the Backstop Agreement with the Noteholders. Subject to, and on the terms of, the Backstop Agreement, the Noteholders have committed to purchase, at the same purchase price, stock in the reorganized Debtors to the extent that the Rights Offering does not raise the full $55 million to repay amounts owing under the Noteholder DIP Facility.

The Debtors Must Terminate the Pension Plan
To Obtain Exit Financing and Confirm a Chapter 11 Plan

15. The Noteholders have required, as a condition to their commitment under the Backstop Agreement and as a condition to their support of the Plan, that the Debtors terminate the Pension Plan. The Noteholders are the only parties willing to provide the Debtors with the necessary equity exit financing. To ensure that the Debtors will have at confirmation

the full $55 million in Rights Offering proceeds, the Debtors entered into the Backstop Agreement pursuant to which the Debtors are obligated to terminate the Pension Plan to protect the viability of the business post-confirmation. As a result, the Debtors (a) cannot obtain sufficient exit financing, and cannot emerge from these chapter 11 cases, without the commitment of the Noteholders to provide $55 million in new equity financing, (b) cannot obtain the commitment of the Noteholders without terminating the Pension Plan and (c) cannot secure from the ABL Lenders $100 million in exit debt financing (the "ABL Exit Facility") without obtaining $55 million in exit equity financing.

16. The Debtors' projections do not support the Debtors' continuing as a going concern absent a significant capital infusion and, therefore, the Debtors must terminate the Pension Plan to reorganize and emerge from chapter 11. Without the ABL Facility and the Noteholder DIP Facility, the Debtors would not have sufficient liquidity to continue as a going concern. Furthermore, without the Rights Offering and Backstop Agreement, the Debtors would not be able to obtain the $100 million ABL Exit Facility to fund post-emergence operations and cannot repay the Noteholder DIP Facility and emerge from these chapter 11 cases.

17. It is unlikely that alternative sources of equity exit financing would be willing to invest with the significant overhang of the underfunded pension liability. The Debtors have stabilized their operations within chapter 11, however, there remains uncertainty about the performance of the business and risk in the upcoming holiday season and business plan. Specifically, after the Debtors emerge from chapter 11 uncertainty could cause negative performance relative to Debtors' business plan. In the event the Debtors significantly underperform relative to their business plan, the Debtors likely will lack sufficient liquidity to continue as a going concern. In such a scenario, the equity investors, and the Noteholders whose

claims will be converted to equity under the Plan, would be subordinated to any future pension claims for underfunding of the Pension Plan, likely resulting in a full loss of the equity investors' investment.

18. Furthermore, new debt financing would likely leave the Debtors over-levered relative to their peers. Even if the Debtors could raise $55 million in new incremental debt financing it is not likely that the ABL Lenders would provide the $100 million ABL Exit Facility commitment with an additional $55 million of debt in the reorganized Debtors' capital structure. The Debtors' comparable companies have negligible leverage, and an additional $55 million of debt, to the extent it could be raised, would leave the Debtors over-levered and likely prevent the Debtors' emergence from chapter 11. Specifically, several of the Debtors' comparable companies including: Blyth, Inc., Rocky Mountain Chocolate Factory, Inc., Build-A-Bear Workshop Inc. and Lancaster Colony Corp. have negative net leverage (i.e. more cash than debt). United Online and 1-800 Flowers Inc. have net leverage ratios of 0.8x and 1.0x, respectively. As the table below illustrates, significant debt burden would leave Harry & David over-levered relative to comparable companies.

Comparable Company Leverage [1]	LTM Total Leverage	LTM Net Leverage	CY 2012 Total Leverage	CY 2012 Net Leverage
1-800 Flowers	1.5 x	1.0 x	1.0 x	0.7 x
Blyth	1.6 x	--	--	--
Rocky Mountain	--	--	--	--
United Online	1.3 x	0.8 x	1.5 x	0.9 x
Build-a-bear	--	--	--	--
Lancaster Colony	--	--	--	--
Harry & David "as is" w/ Pension [2], [3]	n.m.	n.m.	13.2 x	13.2 x
Harry & David pro forma w/ Pension [3], [4]	n.m.	n.m.	1.8 x	1.8 x
Harry & David pro forma w/o Pension [3], [4]	n.m.	n.m.	1.1 x	1.1 x

(1) Assumes constant total and net debt balances for the comparable companies, as projections are not available

(2) LTM as of 12/31/2010; Harry & David's LTM EBITDA was negative and leverage statistics are not meaningful

(3) Harry & David's operating cash balance at CY2012 is required for operations; therefore, net leverage equals total leverage. Harry & David's "as is" debt balance includes the average revolver ($20 million), General Unsecured Creditors ($35 million), existing notes ($206.5 million), 2nd Lien DIP ($55 million) and pension liability ($24.1 million). The Harry & David's CY2012 debt includes the average revolver balance ($20 million), GUC note ($2.4 million) and the pension liability (see amounts below). Leverage multiples are based on Harry & David's CY2012 projected EBITDA of $25.9 million

(4) The pension liability equals the projected CY2012 pension shortfall of $24.1 million; in the pension termination scenario, it includes a $6 million PBGC note

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It Is Unreasonable to Expect the Noteholders, or Any Investor
<u>to Commit $55 Million in New Equity Absent Termination of the Pension Plan</u>

19. Currently, the claims of the Noteholders are *parri passu* with the claims of the PBGC. If the Debtors were to retain the Pension Plan post-emergence, however, the Noteholders' claims that are being converted to equity under the Plan would be subordinated to the claims of the PBGC, whose contingent claims would essentially be left unimpaired if the Pension Plan is not terminated. The overhang of the Pension Plan liability, would, therefore, impair the equity of the Noteholders. In a liquidity event, such as a sale, capital raise or subsequent bankruptcy filing (a "<u>Liquidity Event</u>"), the Debtors would face a substantial PBGC obligation overhang that would significantly reduce, or potentially eliminate, the equity returns

and recoveries to the Noteholders, whose equity commitment is critically necessary to the Debtors' ability to confirm any chapter 11 plan and emerge from these chapter 11 cases.

20. As a result, absent termination of the Pension Plan, the Noteholders were not willing to provide the Debtors with the $55 million equity commitment necessary to allow the Debtors emerge from these chapter 11 cases, nor, without such termination, are the Noteholders willing to support the Plan. Without the Debtors' agreement to terminate the Pension Plan, and eliminate the overhang on the reorganized Debtors' equity that would result if the Pension Plan were retained, the Noteholders would not agree to provide the Debtors with equity financing, nor would the Noteholders agree to convert their notes to equity. In fact, the commitment of the Noteholders to provide $55 million in exit financing to the Debtors, and the Noteholders' plan support agreement, is expressly conditioned on the termination of the Pension Plan. The providers of the Debtors' exit equity financing reasonably require that the reorganized Debtors' free cash be available to fund the Debtors' post-emergence operations, not the Debtors' pre-petition liabilities under the Pension Plan.

21. In light of the risk that retention of the Pension Plan would pose to the reorganized Debtors' equity value, it would be unreasonable to expect the Noteholders, or any investor, to commit $55 million in new equity absent a termination of the Pension Plan. Absent termination during these chapter 11 cases, the diversion of the reorganized Debtors' cash flow to service ongoing Pension Plan liabilities and the potential for loss in a Liquidity Event, would significantly reduce, and potentially eliminate the expected return on such equity investment, making it too risky for any equity investor to consider acceptable. Based on my professional experience, it is unlikely that an alternative equity investor would agree to provide $55 million in

exit equity financing to the Debtors without conditioning such investment on termination of the Pension Plan.

22. In light of the effect of the Pension Plan liability on the potential returns on equity, it is reasonable that the Noteholders would condition their commitment to investing $55 million in the Debtors on termination of the Pension Plan. Furthermore, in light of (a) the risk of incurring a significant pension liability that could wipe out all or a significant portion of the Noteholders' equity investment and (b) the burden of a significant long term liability that provides no corresponding benefit to equity or to the reorganized Debtors, no equity investor or other provider of financing has agreed or likely would agree to provide $55 million in exit equity financing to the Debtors without conditioning such investment on termination of the Pension Plan.

23. To the extent any new party proposes a new financing that includes the assumption of the Pension Plan, the Debtors will evaluate that proposal within the context of maximizing value to the estate. To date, however, no proposals have emerged.

24. Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing is true and correct.

Dated: May 9, 2011
New York, New York

/s/ Neil A. Augustine
Neil A. Augustine
Managing Director
Rothschild Inc.
1251 Avenue of the Americas,
New York, New York 10020

EXHIBIT D

UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re	:	Chapter 11
HARRY & DAVID HOLDINGS, INC, *et al.*,[1]	:	Case No. 11-10884 (MFW)
Debtors.	:	(Jointly Administered)

ORDER GRANTING MOTION OF THE DEBTORS FOR AN ORDER (A) DETERMINING THAT THE FINANCIAL REQUIREMENTS FOR A DISTRESS TERMINATION OF THEIR DEFINED BENEFIT PENSION PLAN ARE SATISFIED; AND (B) APPROVING A DISTRESS TERMINATION OF THE PENSION PLAN

This matter coming before the Court on the Motion of the Debtors for an Order (A) Determining That the Financial Requirements for a Distress Termination of Their Defined Benefit Pension Plan is Satisfied; and (B) Approving a Distress Termination of the Pension Plan (the "Motion")[2] of the above-captioned debtors and debtors in possession (collectively, the "Debtors"), pursuant to section 363(b) of the Bankruptcy Code; the Court having reviewed the Motion and all related pleadings and evidence presented at a hearing before the Court (the "Hearing") and having heard the statements of counsel at the Hearing regarding the relief requested in the Motion; and the Court having determined that the legal and factual bases set forth in the Motion and at the Hearing establish just cause for the relief granted herein;

1 The Debtors are the following four entities (the last four digits of their respective taxpayer identification numbers, if any, follow in parentheses): Harry & David Holdings, Inc. (4389); Harry and David (1765); Harry & David Operations, Inc. (1427); Bear Creek Orchards, Inc. (7216). The address of each of the Debtors is 2500 South Pacific Highway, Medford, Oregon 97501.

2 Capitalized terms not otherwise defined herein shall have the meanings given to them in the Motion.

THE COURT HEREBY FINDS AND CONCLUDES THAT:

1. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2).

2. Notice of the Hearing and the relief requested in the Motion was proper, timely, adequate and sufficient under the circumstances. No other or further notice of the Motion or the Hearing or the relief requested in the Motion and at the Hearing is necessary. A reasonable opportunity to object or be heard regarding the relief requested in the Motion and at the Hearing has been afforded to the parties affected by the relief requested in the Motion.

3. Based on the findings the Court set forth on the record at the Hearing, the Debtors satisfy the "Reorganization Test" of section 4041(c)(2)(B)(ii)(IV) of ERISA, 29 U.S.C. § 1341(c)(2)(B)(ii)(IV), with respect to the Pension Plan.

NOW, THEREFORE, IT IS HEREBY ORDERED THAT:

1. The Motion is GRANTED to the extent set forth herein.

2. Termination of the Pension Plan is hereby approved pursuant to section 4041(c)(2)(B)(ii)(IV) of ERISA and section 363(b) of the Bankruptcy Code.

3. The Debtors are authorized to take any other action necessary or appropriate to give effect to this Order.

Dated: ___________________, 2011
Wilmington, Delaware

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THE HONORABLE MARY F. WALRATH
UNITED STATES BANKRUPTCY JUDGE

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	
	:	**Case No. 02-10429 (JKF)**
KAISER ALUMINUM CORPORATION,	:	**Jointly Administered**
a Delaware Corporation, et al.,	:	
	:	**Chapter 11**
Debtors.	:	
	:	**Hearing Date: To Be Determined.**
	:	**Response Date: To Be Determined.**

MOTION OF DEBTORS KAISER ALUMINUM & CHEMICAL CORPORATION AND KAISER CENTER INC. FOR AN ORDER (A) DETERMINING THAT THE FINANCIAL REQUIREMENTS FOR A DISTRESS TERMINATION OF THEIR DEFINED BENEFIT PENSION PLANS ARE SATISFIED; (B) APPROVING A DISTRESS TERMINATION OF THE PENSION PLANS; (C) AUTHORIZING IMPLEMENTATION OF A REPLACEMENT DEFINED CONTRIBUTION PLAN; AND (D) FOR CERTAIN RELATED RELIEF

Debtors Kaiser Aluminum & Chemical Corporation ("KACC") and Kaiser Center Inc. ("KCI" and collectively with KACC, the "Moving Debtors") hereby move the Court for the entry of an order pursuant to Section 363(b) of the Bankruptcy Code: (i) determining that the financial requirements for a "distress termination" of their defined benefit pension plans are satisfied under section 4041(c)(2)(B) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), 29 U.S.C. § 1341(c)(2)(B); (ii) approving the termination of the Pension Plans (as such term is defined below), effective upon the entry of an order by this Court rejecting the applicable collective bargaining agreements ("CBAs") or as provided in any agreements reached with the affected unions; (iii) authorizing implementation of a replacement benefit plan under a defined contribution arrangement (or other acceptable arrangement); and (iv) for certain related relief. In support of this Motion, the Moving Debtors respectfully represent as follows:

Jurisdiction

1. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2).

Background

2. On February 12, 2002 (the "Petition Date"), the Moving Debtors and 13 affiliates commenced their respective reorganization cases by filing voluntary petitions for relief under chapter 11 of the Bankruptcy Code. On March 15, 2002, two additional affiliates commenced their voluntary chapter 11 cases Nine other affiliates filed their chapter 11 petitions on January 14, 2003. The 26 chapter 11 cases commenced by the Debtors have been consolidated for procedural purposes only and are being administered jointly.

3. The Debtors are continuing in possession of their respective properties and are operating and managing their businesses, as debtors in possession, pursuant to sections 1107 and 1108 of the Bankruptcy Code

4. On February 25, 2002, the United States Trustee for the District of Delaware (the "U.S. Trustee") appointed an official committee of unsecured creditors (the "Creditors' Committee") and a statutory committee of asbestos claimants (the "Asbestos Committee") in these chapter 11 cases, pursuant to section 1102 of the Bankruptcy Code. On January 27, 2003, the Court entered an order appointing Martin J. Murphy as the legal representative for future asbestos claimants (the "Future Claimants' Representative") (D.I. 1685).

5. On July 24, 2003, the Debtors filed a motion (the "1114 Committee Motion") (D.I. 2626) requesting that the Court appoint a committee to act as the authorized representative of salaried and certain union-represented retirees in the event the unions declined to represent retirees who were former members of the union.[1] On August 26, 2003, the Court entered an Order appointing the 1114 Committee (D.I. 2824).

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[1] On July 23, 2002, the Court had entered an order appointing a retirees' committee (D.I. 855) for the limited purpose of "assisting the Debtors' salaried retirees with benefits they may be entitled to under COBRA and any elections thereunder required to obtain such benefits." Pursuant to that order, the retirees' committee was appointed for a limited period, through September 30, 2002, subject to reactivation by the committee on twenty days' notice.

Kaiser Aluminum Corporation

6. Debtor Kaiser Aluminum Corporation, a Delaware corporation, is the direct parent of KACC and the indirect parent of the other Debtors.

7. The Debtors operate in all principal aspects of the aluminum industry - the mining of bauxite, the refining of bauxite into alumina, the production of primary aluminum from alumina and the manufacture of both fabricated and semi-fabricated aluminum products. These operations are conducted through three business units: Bauxite and Alumina, Primary Aluminum and Fabricated Products.

8. The Bauxite and Alumina business unit mines and purchases bauxite and refines it into alumina, a portion of which is used by the Debtors and the remainder of which is sold to third parties. Debtor Kaiser Bauxite Company ("KBC") has a mining lease with the Government of Jamaica that provides bauxite sufficient to meet the requirements of KACC's Gramercy, Louisiana alumina refinery. Kaiser Jamaica Bauxite Company ("KJBC"), a Jamaican partnership in which KBC owns a 49% interest, mines the bauxite from the land, which is subject to the mining lease, as an agent for KBC. Although KBC owns 49% of KJBC, it is entitled to, and generally takes and must pay for, all of KJBC's estimated annual bauxite output. The bauxite mined by KJBC that is not refined into alumina at the Gramercy refinery is sold to a third party.

9. Debtors Kaiser Jamaica Corporation ("KJC") and Alpart Jamaica Inc. ("AJI") also produce alumina. KJC and AJI collectively own a 65% interest in Alumina Partners of Jamaica ("Alpart"), a Delaware general partnership that owns a bauxite mining operation and an alumina plant located in Jamaica. The Government of Jamaica has granted a mining lease to, and entered into other agreements with, Alpart that provide sufficient bauxite for the Alpart refinery. Finally, Debtor Kaiser Alumina Australia Corporation ("KAAC") owns a 20% percent

interest in Queensland Alumina Limited ("QAL"), a Queensland corporation located in Queensland, Australia. QAL owns an alumina refinery that refines bauxite into alumina for the account of QAL's owners.

10. The Primary Aluminum business unit converts alumina into primary aluminum. Prior to the Petition Date, alumina was converted into primary aluminum at two smelters owned by KACC in the State of Washington and two smelters operated through joint venture arrangements with certain third parties, one in Ghana and the other in Wales, the United Kingdom. The two smelters in Washington state were temporarily curtailed in 2002 because of adverse market conditions that made the operations uneconomic for the Debtors. The Tacoma, Washington smelter was never restarted and was later sold to the Port of Tacoma, pursuant to a transaction approved by this Court in February 2003. The Mead, Washington smelter was indefinitely curtailed in January 2003 and no restart is anticipated in the near future in view of continuing adverse market conditions. The smelter in Ghana is owned by Volta Aluminium Company Limited ("Valco"), a Ghanaian corporation of which KACC owns 90%. The Ghana smelter was progressively curtailed during 2002-2003 and ultimately idled in May 2003 due to a dispute over power allocation and pricing with the Government of Ghana. The Wales smelter is owned and operated by Anglesey Aluminium Limited ("Anglesey"), a United Kingdom corporation. KACC owns a 49% interest in Anglesey.

11. The Fabricated Products business unit operates a rolling mill in Trentwood, Washington where heat-treat sheet and plate and other flat-rolled products are manufactured for the aerospace, transportation and industrial markets. KACC owns the rolling mill. Prior to the Petition Date, the mill also produced materials sold to manufacturers of beverage cans, but that aspect of the operation was discontinued and sold during the chapter 11 cases.

12. The Fabricated Products business unit in general operates ten plants engaged in extrusion, drawing, and forging in the United States and Canada. All the plants are owned by KACC with the exception of a plant in London, Ontario, which is owned by Kaiser Aluminum & Chemical Canada Limited and a plant in Richmond, Virginia owned by Kaiser Bellwood Corporation ("Bellwood"). These facilities manufacture extruded products and forged parts for a variety of industrial markets, including ground transportation, distribution, durable goods, defense, building and construction, electrical and general aviation markets.

13. As of January 1, 2003, the Moving Debtors employed approximately 3,000 employees domestically, approximately 2,100 of whom were hourly and 900 of whom were salaried. The majority of the hourly employees are represented for collective bargaining purposes by the USWA. In contrast to the current number of hourly and salaried employees, the Moving Debtors had, as of the same date, approximately 2,411 salaried retired employees and beneficiaries receiving pension benefits[2], and 8,657 hourly retired employees and beneficiaries receiving pension benefits.

Filing of Chapter 11 Cases

14. The Debtors commenced their chapter 11 cases in February 2002 because of liquidity and cash flow constraints that arose in late 2001 and early 2002. At that time, the Debtors faced significant imminent debt maturities, including the maturities of certain note obligations on February 15, 2002 and additional note obligations on February 1, 2003. In addition, aluminum industry business conditions, including prices, were unusually weak at that time and the general economy had significantly deteriorated. Weak industry and economic conditions were further exacerbated by the events of September 11, 2001. The Debtors had also

2 Effective December 17, 2003, the Pension Benefit Guaranty Corporation ("PBGC") terminated the Kaiser Aluminum Salaried Employees Retirement Plan (the "Salaried Plan") pursuant to section 4042(c) of ERISA, 29 U.S.C. § 1342(c), based upon its determination that termination was necessary to protect the interests of the Salaried Plan's participants.

become increasingly burdened by asbestos litigation and growing legacy obligations for future retiree medical and pension costs. The retiree medical obligations were particularly burdensome because healthcare costs for retirees had increased significantly and the Debtors had implemented operations efficiency initiatives that reduced the workforce and substantially increased the number of retirees. The confluence of all these factors created the prospect of continued operating losses and negative cash flow, resulting in lower credit ratings and an inability to access capital markets. As a result, the Debtors were unable to restructure their obligations outside of bankruptcy, and the chapter 11 filings became necessary.

Efforts to Preserve Liquidity

15. Since the outset of these reorganization cases, the Debtors have engaged in a variety of activities to preserve and enhance liquidity. The Debtors were successful at the outset of the chapter 11 cases in obtaining a $300 million post petition credit facility (the "DIP Facility") from Bank of America, N.A. ("BofA") and other financial institutions that was approved by the Court by final order entered on March 21, 2002. The facility provides for a secured, revolving line of credit subject to a borrowing base that can be used for advances and/or for the issuance of up to $125 million of letters of credit in the aggregate. In August 2003, the Debtors negotiated amendments to the DIP Facility that increased availability in a continuing adverse economic environment highlighted by low metal prices and high natural gas and fuel oil prices. Among other things, the amendments increased the borrowing base and modified certain covenants to decrease the risk of a default notwithstanding adverse business conditions and anticipated reductions in operating performance.

16. Additionally, the Debtors in June 2003 were able to facilitate QAL's access to $215 million of additional third party financing of which the Debtors' share was $43 million. This additional financing became available to QAL after the Debtors successfully

completed protracted negotiations with BofA and the nondebtor participants in QAL regarding a variety of issues associated with the financing.

17 At the same time that the Debtors were pursuing additional financing for their operations, they also were conducting a review of their assets with the objective of identifying and selling non-strategic assets. As a result of this process, a number of assets have been sold during the course of these cases. During 2002, the Debtors sold their Oxnard, California aluminum forging facility, certain equipment in their Trentwood facility previously associated with their lid and tab stock product lines and other real estate and equipment. The aggregate proceeds received from these asset sales were approximately $31 million. In 2003, the Debtors sold their Tacoma facility, their interests in the Kaiser Center office building and related real estate and other assets in Oakland, California, certain additional equipment at their Trentwood rolling mill, and other real estate and equipment. The aggregate proceeds received from these asset sales were approximately $86 million.

18. The Debtors also have been engaged since the inception of these chapter 11 cases in an extensive cost reduction program that encompasses all their operations. Since 2001, the calendar year ending just prior to the Petition Date, the Debtors have reduced controllable costs by approximately $130 million as compared to 2001 and are currently operating at an annualized rate of reduced controllable costs of over $150 million as compared to 2001. As a result of these efforts, the Debtors have experienced record controllable cost performance throughout 2002 and 2003. Similarly, the Debtors have substantially reduced inventories during these cases generating significantly lower amounts of working capital and approximately $57 million in additional cash.

The Debtors' Current Financial Condition

19. While all of these efforts have enabled the Debtors to date to maintain adequate liquidity to operate, the Debtors' cash resources and liquidity continue to decline. Excluding asset sale proceeds and non-recurring insurance recoveries, during the eleven months ended November 30, 2003, the Debtors consumed approximately $146 million of cash. Adverse market conditions have negatively affected all of the Debtors' business units. Demand for fabricated aluminum product remains weak. Until recently, metal prices remained at low levels. In addition, natural gas and fuel oil prices have increased to near historically high levels and the U.S. dollar has weakened, particularly against the Australian dollar and the U.K. Pound Sterling, currencies in which the Debtors are exposed to substantial costs in respect to their interests in QAL and Anglesey. The Debtors' financial condition has been further impaired by the curtailment and ultimate idling of the Valco smelter. As a result of these adverse economic conditions, the Debtors have been required to obtain a number of amendments to the DIP Facility to address lower than projected operating performance.

20. The Debtors' cash disbursements are currently exceeding cash receipts by approximately $10 million per month. In addition, the Debtors project $25 million in negative EBITDA for 2003. The Debtors' cash flow is negative even though the Debtors are not servicing their prepetition obligations, including over $800 million in bond and other indebtedness, and are not making payments with respect to their pension and asbestos liabilities. Nonetheless, as required by section 1114 of the Bankruptcy Code, the Debtors are continuing to pay their retiree medical liabilities, which aggregate approximately $60 million per year and are continuing to escalate at a significant rate.

Strategic Plan

21 In September 2002, the Debtors prepared a strategic plan for their business operations. That plan envisioned that the Debtors would sell or otherwise dispose of some or all of their Bauxite and Alumina and Primary Aluminum assets (collectively, the "Commodities Assets") and reorganize their Fabricated Products business. Thereafter, the strategic plan was shared with the Creditors' Committee, the Asbestos Committee and the Future Claimants' Representative. After considerable due diligence was completed by these parties, the two committees and the Future Claimants' Representative indicated they did not oppose the Debtors' plan. Therefore, beginning in approximately March 2003, the Debtors initiated a process to explore the sale of some or all of their interests in Alpart and Anglesey as well as the Gramercy refinery in connection with their interests in KJBC. After extensive marketing to prospective purchasers around the world, bids were submitted in November 2003. For the most part, the bids proposed values for the assets that were substantially less than anticipated. At the present time, the Debtors have not entered into any agreement to sell one or more of the Commodities Assets.

The Pension Plans

22. Pursuant to the collective bargaining agreements with certain unions, including the United Steelworkers of America, AFL-CIO-CLC (the "USWA") and the International Association of Machinists & Aerospace Workers (the "IAM"), the Moving Debtors currently are obligated to provide various retiree medical benefits (the "Retiree Benefits") and pension benefits (the "Pension Benefits"), to certain current and former hourly employees, including their spouses, surviving spouses and eligible dependents (the "Hourly Retirees"). The substantial majority of the Moving Debtors' Hourly Retirees who are receiving Pension Benefits are doing so pursuant to collective bargaining agreements negotiated with the USWA.

23 The Moving Debtors sponsor the following pension plans, covering hourly and union employees: the Kaiser Aluminum Pension Plan, the Kaiser Aluminum Inactive Pension Plan, the Kaiser Aluminum Tulsa Pension Plan, the Kaiser Aluminum Los Angeles Extrusion Pension Plan, the Kaiser Aluminum Sherman Pension Plan, the Kaiser Aluminum Bellwood Pension Plan, and the Kaiser Center Garage Pension Plan (the "Hourly Plans" or the "Pension Plans").

24. Effective December 17, 2003, the Pension Benefit Guaranty Corporation ("PBGC") terminated the Kaiser Aluminum Salaried Employees Retirement Plan (the "Salaried Plan") pursuant to section 4042(c) of ERISA, 29 U.S.C. § 1342(c), based upon its determination that termination was necessary to protect the interests of the Salaried Plans' participants. The PBGC announcement regarding the termination of the Salaried Plan did not discuss the Debtors' remaining Hourly Plans.

25. As of January 1, 2003, the total unfunded liability for the Hourly Plans was approximately $97,865,000. The Moving Debtors have not made and will not make minimum contributions to the Hourly Plans totaling approximately $47,845,233 that were and will become due in respect to the 2003 plan year.

Discussions with the PBGC and the Unions

26. The Moving Debtors and their advisors met with the PBGC in November 2002, January 2003, and September 2003 to discuss the Debtors' financial status, the alternatives they considered other than termination of the Hourly Plans, and the ultimate need to terminate the Hourly Plans.

27. In addition, for the past several months, the Moving Debtors have been meeting with the USWA and the IAM to attempt to reach negotiated agreements reducing the Moving Debtors' Pension Benefits obligations under the Hourly Plans to a level that would allow

them to formulate a viable plan or plans of reorganization. During this time, the Moving Debtors also have been negotiating modifications to various retiree medical and other benefit plans with the USWA, the IAM, and the 1114 Committee, with the intent of engaging in similar negotiations with the International Union, United Automobile, Aerospace, and Agricultural Implement Workers of America (the "UAW"), the International Chemical Workers Union Council - United Food & Commercial Workers (the "ICWUC-UFCW"), and the Paper, Allied-Industrial, Chemical and Energy Workers Union (the "PACE") as soon as practicable.

28. The Moving Debtors met with the USWA initially in November 2002, and continued these meetings in 2003 on May 13, July 15-16 and August 20 in Pittsburgh, Pennsylvania, September 15-16 in Minneapolis, Minnesota, September 30-October 1 in Chicago, Illinois, October 30-31 and December 4 in New York, December 11 in Pittsburgh, and December 17-19 in Minneapolis. In 2004, the Moving Debtors resumed meetings with the USWA in Minneapolis on January 8 and 9.

29. In 2003, the Moving Debtors met with the IAM on July 30 and on December 15.

30 Despite the Moving Debtors' good faith negotiations and considerable efforts to reach negotiated agreements with the USWA, the Debtors have been unable to reach a negotiated agreement with the USWA, as of the date of this filing. Similarly, the Moving Debtors have met with the IAM in good faith, made a proposal and explained it, but have not received a counterproposal or reached agreement as of the date of this filing.

Relief Requested

31. By this Motion, the Debtors seek an order (i) determining that the financial requirements for a "distress termination" of the Pension Plans under 29 U.S.C. § 1341(c)(2)(B) are satisfied; (ii) approving the termination of the Pension Plans under 29 U.S.C.

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§ 1341(c)(2)(B) and section 363(b) of the Bankruptcy Code, effective upon the entry of an order by this Court rejecting the applicable collective bargaining agreements ("CBAs") or as provided in any agreements reached with the affected unions;[3] and (iii) authorizing implementation of a replacement benefit plan under a defined contribution arrangement (or other acceptable arrangement); and (iv) for certain related relief. Based upon the actuarial determinations of the future minimum funding requirements of the Pension Plans and the Debtors' projected cash flow in any viable reorganization scenario, the distress termination of the Pension Plans is required. The Replacement Plans will become effective following the distress termination of the Pension Plans or at such other date to which the Debtors and the USWA might agree or the Court may order.

32. The Debtors may terminate the Pension Plans if any of the tests for a distress termination set forth in section 4041(c) of ERISA is met by each contributing sponsor and each member of each contributing sponsor's controlled group. See 29 U.S.C. § 1341. The distress termination tests are summarized as follows:

> (a) *The Liquidation Test*: (i) an entity has filed, or had filed against it, as of the proposed termination date, a petition seeking liquidation in a case under the Bankruptcy Code and such case has not, as of the proposed termination date, been dismissed; or (i) a reorganization case is converted to a liquidation case as of the proposed termination date.[4]
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> (b) *The Reorganization Test*: an entity has filed, or had filed against it, as of the proposed termination date, a petition seeking reorganization in a case under the Bankruptcy Code; such case has not, as of the proposed termination date, been dismissed; such entity timely submits a copy of any requests for the approval of the bankruptcy court of the plan termination to the PBGC at the time the request is made; and the bankruptcy court determines that, unless the plan is terminated, such entity will be unable to (i) pay

[3] Simultaneously with the filing of this Motion, the Moving Debtors have filed a Motion for an Order Authorizing Rejection of Certain Collective Bargaining Agreements Pursuant to Section 1113 of the Bankruptcy Code.

[4] *See* 29 U.S.C. § 1341(c)(2)(b)(i)(I)&(II); ERISA § 4041(c)(2)(b)(i)(I)&(II)

all of its debts pursuant to a plan of reorganization and (ii) continue in business outside the chapter 11 reorganization process and approves the termination [5]

(c) *The Business Continuation Test*: an entity demonstrates to the satisfaction of the PBGC that, unless a distress termination occurs, such entity will be unable to pay its debts when due and will be unable to continue in business [6]

(d) *The Pension Costs Test*: an entity demonstrates to the satisfaction of the PBGC that the costs of providing pension coverage have become unreasonably burdensome to such entity, solely as a result of a decline of its workforce covered as participants under all single-employer pension plans for which it is a contributing sponsor [7]

The Debtors seek Court approval to terminate the Pension Plans under the "Reorganization Test" described above. Neither the statute nor the regulations, however, indicate the specific means by which the plan administrator or the contributing sponsor establishes the "financial necessity" prong of this test — *i.e.*, that, without terminating the Pension Plans, the sponsor will be unable to meet its obligations under the plan of reorganization and will be unable to continue the business. Similarly, there is sparse case law interpreting this prong. The few cases that provide some guidance are discussed below.

33. The bankruptcy court in *In re Sewell Manufacturing Company, Inc.*, 195 B.R. 180 (Bankr. N.D. Ga. 1996), approved a distress termination based on findings that (a) the reorganized debtor was expected to suffer negative cash flow of more than $250,000 in its current fiscal year and (b) neither its lender nor any other buyer or lender was willing to finance the required minimum pension plan funding contributions.[8] The debtor established that the only means for it to meet its upcoming pension obligations, as well as pay current debts, aside from finding a willing lender or buyer, was for the debtor to increase its sales by seventy percent over

[5] *See* 29 U.S.C. § 1341(c)(2)(b)(ii)(I); ERISA § 4041(c)(2)(b)(ii)(I).

[6] *See* 29 U.S.C. § 1341(c)(2)(b)(iii)(I); ERISA § 4041(c)(2)(b)(iii)(I).

[7] *See* 29 U.S.C. § 1341(c)(2)(b)(iii)(II); ERISA § 4041(c)(2)(b)(iii)(II).

[8] *Sewell Mfg.*, 195 B.R. at 185-86.

the next six months[9] The court considered this concept an impossibility given current industry conditions and concluded that the standards required by section 4041(c)(2)(B)(ii)(IV) of ERISA had been satisfied and approved the termination.[10]

34. Similarly, the court in *In re Wire Rope Corporation of America, Incorporated*, 287 B.R. 771 (Bankr. W.D. Mo. 2002), primarily focused upon the testimony of the debtor's chief restructuring officer ("CRO") who indicated that the debtor projected approximately $23 million available for debt service during the three year period 2004 through 2006. Through the same period and into 2006, the debtor projected minimum funding requirements of $20.7 million for its three pension plans. The court observed that, by using nearly all the projected cash flow to meet the minimum funding requirements, there would be little left to satisfy the debtor's "significant" secured creditors and none left for its unsecured creditors. This, the court concluded, left "little question that the debtor will not be able to remain in business for long."[11] Given the debtor's presentation and testimony regarding its projected earnings, amounts available for debt service and free cash flow, together with the impact of the minimum funding contributions, the court concluded that the debtor "would, most likely, be forced into liquidation if it is not allowed to terminate its Retirement Plans, because it cannot both pay its debts under a plan of reorganization *and* continue in business outside of the reorganization process of Chapter 11."[12]

35. In addition to meeting one of the four tests for a distress termination discussed above, the plan administrator must also provide a written Notice of Intent to Terminate

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9 *See id.* at 186.

10 *Id.*

11 *Wire Rope*, 287 B.R. at 779.

12 *Id.* at 781 (emphasis added).

(a "NOIT") to each person who is an affected person[13] at least 60, but not more than 90, days prior to the proposed termination date[14] This includes the filing of PBGC Form 600, which serves as notice to the PBGC in its status as an affected person.

36. Finally, for a plan termination to proceed, it may not violate the terms and conditions of any existing collective bargaining agreement under which the plan has been bargained.[15] In the recent decision by the bankruptcy court in *In re US Airways, Inc.*, 296 B.R. 734 (Bankr. E.D. Va. 2003), the court held that the financial requirements for a distress termination had been satisfied by the plan sponsor under section 4041(c)(2)(B)(ii)(IV) of ERISA but declined to make a ruling as to whether the termination of the plan would violate the CBA between the debtors and the Air Line Pilots Association. Instead, the court conditioned its approval of the distress termination upon the outcome of the arbitration procedures that were established by the CBA.

Need for Termination of the Pension Plans and Relevant Discussions

37. Irrespective of whether the Debtors retain or sell some or all of their Commodities Assets, the Debtors will not under any viable scenario be able to satisfy their pension benefits obligations. The Fabricated Products business, either alone or in combination with any or all of the Commodities Assets, would not generate cash flow even remotely sufficient to fund the Debtors' pension benefits obligations. Any viable reorganization plan requires the termination of the Pension Plans and the provision of replacement benefits under

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[13] Affected parties include (a) participants; (b) beneficiaries of deceased participants; (c) alternate payees under applicable qualified domestic relations orders; (d) employee organizations currently representing participants; (e) for any group of participants not currently represented by an employee organization, the employee organization, if any, that last represented the group within the five-year period preceding issuance of the NOIT; and (f) the PBGC. ERISA §4001(a)(21); PBGC, *Distress Termination Filing Instructions*, pg. 5 (2003).

[14] *See* 29 U.S.C. § 1301(a)(21); PBGC Reg. § 4041.43(a)(1).

[15] *See* 29 U.S.C. § 1341(a)(3); ERISA § 4041(a)(3).

defined contribution arrangements (or other acceptable arrangements) for current, active employees (collectively, the "Replacement Plans").

38. Here, if the Moving Debtors cannot terminate the existing pension funding obligations, the Debtors will be unable to reorganize and emerge as viable entities. As detailed above, despite the Debtors' exhaustive efforts to preserve and enhance liquidity and improve their operations – obtaining additional financing, including obtaining additional availability under existing financing, selling non-strategic assets, implementing over $130 million in cost-cutting measures – the Debtors' businesses remain significantly cash flow negative. The Debtors' cash disbursements currently exceed cash receipts by approximately $10 million per month.

39. For the year 2003 the Moving Debtors owe or will owe approximately $47,850,000 in contributions in respect of the Hourly Plans for plan year 2003. Absent termination of the Hourly Plans, for the years 2004-2009, the Moving Debtors will be required to make minimum contributions to such plans in annual amounts in excess of $230 million. In contrast, the cost of the proposed Replacement Plans is estimated to be approximately $20 million annually.

40. Under any viable reorganization scenario – reorganization of the Fabricated Products business only with sales of all the Commodities Assets or reorganization of the Fabricated Products business together with one or more of the Commodities Assets – the reorganized entity will not have sufficient cash flow to continue funding the Hourly Plans.

41. The Kaiser Proposals are based on a careful analysis of the Moving Debtors' financial situation and are narrowly designed to avoid liquidation. Specifically, the Kaiser Proposals provide for the termination of certain pension plans,[16] with the terminated plans

[16] The Kaiser-USWA Proposal contemplates either a PBGC involuntary termination of or distress termination of the following pension plans: (1) the Kaiser Aluminum Pension Plan; (2) the Kaiser Aluminum Tulsa Pension Plan; the Kaiser Aluminum Inactive Pension Plan; and the Kaiser Aluminum Bellwood Pension Plan (collectively, the "Kaiser/USWA Pension Plans") The IAM

to be assumed by the PBGC. Under the Kaiser Proposals, the Moving Debtors would then institute a follow-on defined contribution pension plan ("the Kaiser Aluminum Defined Contribution Plan") to cover affected employees, if any, continuing in their employment after emergence from bankruptcy with the emerging entity. The proposed Kaiser Aluminum Defined Contribution Plan provides for employee contributions with an employer match of 50% of all of employee contributions up to 4% of pay and an additional fixed employer contribution based on age and service.

42. The Moving Debtors, in conjunction with their financial advisors, have sought other ways to reduce their pension funding obligations short of terminating the Hourly Plans. The Moving Debtors have considered (a) "freezing" the Hourly Plans (*i.e.*, eliminating future benefit accruals) and instituting an alternative replacement plan for post-"freeze" periods; and (b) seeking funding waivers from the Internal Revenue Service for three successive years. Neither alternative provides the reduction in pension funding obligations that the Moving Debtors require.

43. First, using normal, ongoing assumptions, "freezing" the Hourly Plans and instituting a replacement plan such as the Kaiser Aluminum Defined Contribution Plan for post-"freeze" periods would result in an insufficient reduction of the funding obligation. Irrespective of the ultimate configuration of the reorganized entity, the reorganized entity could not possibly support the required payments.

44. Second, a waiver application should not be filed until after the beginning of the year for which the contributions sought to be waived are due, and there can be no

(continued)

Proposals contemplate either a PBGC involuntary termination of or distressed termination of the following pension plans: (1) the Kaiser Aluminum Bellwood Pension; and (2) the Kaiser Aluminum Inactive Pension Plan (collectively, "the Kaiser/IAM Bellwood Pension Plans"); and (3) the Kaiser Aluminum Sherman Pension Plan and the Kaiser Aluminum Inactive Pension Plan (herein, the Kaiser/IAM Sherman Pension Plan[s]).

assurance that a waiver would be granted in any given year. Moreover, waivers may only be granted for three of any 15 plan years. 29 U.S.C. § 1083(a). In addition, each waived funding deficiency must be amortized over a period of five plan years, with interest at 150% of the federal mid-term rate. *Id.* The result is that the massive Hourly Plan funding obligations that are projected for future periods would merely be deferred for a short time period, rendering the reorganized entity unable in the interim to obtain financing, unable to secure capital from the capital markets, and unable to fund the obligations once any short deferral period expires.

45. In contrast, the Moving Debtors estimate that the cost to their estates of terminating the Hourly Plans and implementing a replacement plan such as the proposed Kaiser Aluminum Defined Contribution Plan will approximate $20 million[17] over the five-year period from 2004 through 2009 — a reduction of approximately $210 million over the current Hourly Plan cost forecast.

46. Accordingly, the Moving Debtors have determined that this option is the best and only alternative available to avoid liquidation and emerge from bankruptcy. Under ERISA, a plan sponsor's only options with respect to pension plans it can no longer support are (a) freezing the plans, (b) seeking a funding waiver or waivers, and (c) terminating the plans. As indicated above, the first two options do not provide the relief necessary to permit a reorganization of the Debtors. Without the termination of the existing pension benefit obligations, there is simply no reorganization plan that will produce viable emerging entities.

Satisfaction of Applicable Legal Standards

47. The Debtors satisfy each of the prongs of the Reorganization Test. First, each of them is currently a debtor under chapter 11 of the Bankruptcy Code, which is currently

[17] The Debtors currently are engaged in discussions with the USWA and IAM regarding, among other things, the terms of the Kaiser Proposals. Accordingly, as a result of such discussions, this amount could change.

pending. Second, as noted above, the Debtors have previously met with the PBGC to discuss the proposed termination of the Pension Plans, and the PBGC will be served with a copy of this Motion. Finally, the Debtors and the members of their controlled group meet the financial necessity prong of the test.

48 Specifically, as detailed above, the Debtors and their affiliates (including their nondebtor affiliates) will not be able to (a) pay all of their debts pursuant to a plan of reorganization and (b) continue in business outside the reorganization process unless the Pension Plans are terminated. Accordingly, such members will be unable to generate cash to satisfy the Debtors' future funding requirements under the Pension Plans.

49 To comply with the requirement that the plan administrator provide a NOIT to each person who is an affected person at least 60, but not more than 90, days prior to the proposed termination date, the Debtors will timely send a NOIT to all affected parties, including filing the Form 600 with the PBGC.

50 Finally, the Debtors' current CBAs require the maintenance of the Pension Plans. The Debtors have filed concurrently with this Motion a Motion for an Order Authorizing Rejection of Certain Collective Bargaining Agreements Pursuant to Section 1113 of the Bankruptcy Code. At the same time, the Debtors are continuing to negotiate with the Unions regarding termination of the Pension Plans and implementation of the Replacement Plans. The future disposition of the Pension Plans, accordingly, will be determined by the Court's ruling on the Section 1113 motion or by an agreement or agreements reached with the Unions

<u>Implementation of the Replacement Plans</u>

51 By this Motion, the Debtors also seek authorization to implement the Replacement Plans, effective upon the termination date of the Pension Plans or at such other date

to which the Debtors and the Unions might agree or the Court orders, pursuant to section 363(b) of the Bankruptcy Code. 11 U.S.C. § 363(b).

52. Section 363(b) of the Bankruptcy Code provides that a debtor in possession "after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate." 11 U.S.C. § 363(b). In general, a debtor may use, sell, or lease property of the estate outside the ordinary course of its business where such use represents an exercise of the debtor's sound business judgment. *See, e.g., Stephens Indus., Inc. v. McClung*, 789 F.2d 386, 390 (6th Cir. 1986) (citing *Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.2d 1063, 1070 (2d Cir. 1983)); *see also In re Martin*, 91 F.3d 389, 395 (3d Cir. 1996) (citing *Fulton State Bank v. Schipper (In re Schipper)*, 933 F.2d 513, 515 (7th Cir. 1991)); *In re Abbotts Dairies of Pa., Inc.*, 788 F.2d 143, 145-47 (3d Cir. 1986) (implicitly adopting the articulated business judgment test of *Lionel Corp.*). The "use" of a debtor's funds to pay for expenses related to the operation of its business is considered a use that is governed by section 363 of the Bankruptcy Code. *See McLean Indus., Inc. v. Med. Lab. Automation, Inc. (In re McLean Indus., Inc.)*, 96 B.R. 440, 443 (Bankr. S.D.N.Y. 1989) (exercise of option to purchase property is a "use" of property of the estate subject to section 363(b) of the Bankruptcy Code); *Continental Air Lines, Inc. v. Hillblom (In re Continental Air Lines, Inc.)*, 61 B.R. 755, 783 (S.D. Texas 1986) (use of debtor's funds to purchase another corporation outside of ordinary course of business is a "use" governed by section 363).

53. The Debtors understand the hardship that the termination of the Pension Plans will create for their current employees.[18] Accordingly, they have determined to implement the Replacement Plans as an alternative benefit for their employees and believe that this action is both a cost-effective alternative and warranted under the circumstances in accordance with

[18] Persons already receiving a pension will continue to receive such pension after the termination of the Pension Plans, subject to any PBGC-imposed limitations thereon.

section 363(b) of the Bankruptcy Code. Implementation of the Replacement Plans will preserve employee morale and enhance the reorganized Debtors' ability to retain their employees over the long term. Accordingly, the Debtors believe that establishing and implementing the Replacement Plans is in the best interests of their estates and creditors

Request that Order be Made Immediately Applicable

54. In addition, the Debtors request that any order entered approving this Motion be made immediately applicable. Bankruptcy Rule 6004(g) provides that "[a]n order authorizing the use, sale, or lease of property . . . is stayed until the expiration of 10 days after entry of the order, unless the court orders otherwise." Because the Debtors and the pension plan participants require certainty as to the termination of such plans and the implementation of the Replacement Plans and due to the number of actions and communications to affected parties, including plan participants and the PBGC that must precede the termination and creation of such plans, the Debtors request that any order granting some or all of the relief requested in this Motion be made immediately applicable, pursuant to Bankruptcy Rule 6004(g).

Notice

55. No trustee or examiner has been appointed in these chapter 11 cases. Notice of this Motion has been given to: (a) the U.S. Trustee; (b) counsel to the Creditors' Committee; (c) counsel to the Asbestos Committee; (d) counsel to the Futures Representative; (e) counsel to the Debtors' postpetition lenders; (f) counsel to MAXXAM Inc., the Debtors' principal equity holder; (g) the USWA, UAW, IAM, PACE and ICWUC-UFCW; (h) counsel to the First Retirees' Committee; (i) the PBGC; and (j) the parties that have requested notice in these chapter 11 cases. In light of the nature of the relief requested herein, the Debtors submit that no other or further notice is required.

No Prior Request

56. No prior request for the relief sought in this Motion has been made to this or any other court in connection with these chapter 11 cases.

WHEREFORE, the Debtors respectfully request that the Court enter an order, substantially in the form attached hereto as Exhibit 1: (i) determining that the financial requirements for a "distress termination" of the Pension Plans under 29 U.S.C. § 1341(c)(2)(B) are satisfied; (ii) approving the termination of the Pension Plans under 29 U.S.C. § 1341(c)(2)(B) and section 363(b) of the Bankruptcy Code, effective upon the entry of an order by this Court rejecting the applicable collective bargaining agreements or as provided in any agreements reached with the affected unions; and (iii) authorizing implementation of a replacement benefit plan under a defined contribution arrangement (or other acceptable arrangement); and (iv) granting such other and further relief as the Court may deem proper.

Dated: January 11, 2004

Respectfully submitted,

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ATTORNEYS FOR DEBTORS
AND DEBTORS IN POSSESSION

The Intersection of Bankruptcy Law With Property Law

RECLAMATION MATERIALS

MEMORANDUM

To: Delaware Bankruptcy Inn of Court Members

From: February Pupilage Team – Reclamation Subgroup

Date: January 29, 2012

Subject: DBIC Presentation - Summary of Key Reclamation Cases

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In re Dana Corporation, 367 B,R, 409 (Bankr. S.D.N.Y. 2007) (Lifland, J.)

Facts: Debtors moved for value determination of zero for all reclamation claims filed in their cases. The debtors asserted that all of the reclamation claims were worthless because those claims were subject to the superior rights of a holder of a security interest in the reclaimed goods.

Key language:
"With the introduction of section 503(b)(9) priority, reclamation claims under amended section 546(c) have decreased importance because goods delivered to a debtor in the 20 days prior to the bankruptcy will have automatic priority. Thus, reclamation rights are not mainly beneficial for goods delivered in the 21 to 45 days prior to the filing."

"The reality is that, in most cases, asset-based financing provides a prior perfected lien on most goods such that the right of reclamation is rendered moot."

Holding: Reclamation is an in rem remedy and reclaiming sellers have no right to compel a lien holder to satisfy its claim from some other collateral. Accordingly, if the value of any given reclaiming suppliers goods does not exceed the amount of debt secured by the prior lien, that reclamation claim is valueless.

In re Advanced Marketing Services, Inc., 360 B.R. 421 (Bankr. D. Del. 2007) (Sontchi, J.)

Facts: Simon & Schuster (a publisher) brought adversary proceeding to reclaim goods and filed emergency application for TRO. The TRO application sought to prevent the debtor form selling the goods pending trial on its reclamation and other claims.

Pre-petition, the debtor's senior debt facility was secured by a floating lien on substantially all of the debtors' assets, including inventory and, specifically, books, the likes of which supplied by Simon & Schuster. The same lender agreed to provide a DIP loan on substantially identical terms. The lender's pre-petition liens were rolled into a senior post-petition lien on the debtor's pre- and post-petition obligations, and pursuant to the post-petition credit agreement the debtor was required to pay its pre-petition obligations to the lender before paying the debtor's post-petition obligations. The interim DIP financing order "ratified and confirmed" the lender's pre-petition security interests and liens in favor of the debtor's post-petition lender. At the time of the opinion, only a interim DIP order was in place. However, a final DIP order bearing the same orders was subsequently entered.

Holding: Because the goods that the publisher sought to reclaim were subject to prior secured liens, publisher was unable to establish a likelihood of success on the merits of its reclamation claim and the TRO was therefore denied.

In re Paramount Home Entertainment Inc. v. Circuit City Stores, Inc., 445 B.R. 521 (E.D. Va. 2010)

Facts: Seller made timely reclamation demand on debtors. The court then set procedures for resolving reclamation demands. Pursuant to these procedures, the debtors were to advise each reclamation claimant of the allowed amount, if any, of its reclamation demand. If no such notice was given, then the debtors were deemed to have rejected the reclamation demand. As the seller was not sent a notice setting forth an allowed reclamation claim, its demands were deemed rejected by the debtors. Subsequently, the court authorized the debtors to conduct going out of business sales. The seller did not object to the sale, never commenced an adversary proceeding, never filed a motion for relief from the stay or took any other action in pursuit of its reclamation claim.

Holding: Reclaiming seller must diligently assert its rights while bankruptcy proceedings progress. Having established the basic benefit of a right of reclamation, a seller must follow certain procedures to protect that right. Noting that the right of reclamation is not self-executing, the court remarked that at least one of the actions a seller must take in connection with a purchaser undergoing bankruptcy is to file a motion for relief from the automatic stay. A written demand or merely following the court's reclamation procedures is not enough to gain the protections of the right of reclamation.

Note: The bankruptcy court held that even if the seller had diligently pursued its reclamation claim, its claim would still fail because at the commencement of the bankruptcy, the pre-petition lenders had a floating blanket lien on all of the debtors' assets, including inventory. Under UCC § 2-702, a seller's right to reclaim is subject to the rights of a good faith purchaser, such as the pre-petition lenders. The district court did not address this argument because it already held that the seller did not diligently pursue its claim, thus rendering this argument moot.

INTELLECTUAL PROPERTY MATERIALS

BANKRUPTCY AND INTELLECTUAL PROPERTY LAW

DELAWARE BANKRUPTCY INN OF COURT
FEBRUARY 21, 2012

Intellectual Property and the Bankruptcy Code - Background

- The modern Bankruptcy Code was enacted in 1978 and for 10 years it lacked specific provisions focused on intellectual property
- Consequently, courts treated licensing for intellectual property in the same manner they treated other executory contracts
- In 1985, in Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 765 F.2d 1043 (4th Cir. 1985), the Fourth Circuit upheld the right of a debtor licensor's ability to reject an executory contract for the licensing of a metallurgical process. As a result, the debtor was relieved of affirmative obligations owes to the licensee, and importantly, the licensee's right to use the licensed intellectual property was terminated.

Intellectual Property Bankruptcy Protection Act of 1988

- As a result of the Lubrizol opinion, Congress passed the Intellectual Property Bankruptcy Protection Act ("IPBA") in 1988. IPBPA consists of two essential components:
  - A broad, but not all encompassing definition of "intellectual property"
  - A set of protections for licensees of the defined "intellectual property" in the event that their licensor should reject the license agreement
- Purpose of IPBPA was to amend Bankruptcy Code section 365 to clarify that the rights of an intellectual property licensee to use the licensed property cannot be unilaterally cut off as a result of the rejection of the licensee.
- IPBPA is now incorporated into Bankruptcy Code sections 101(A)(35A) (defines intellectual property) and 365(n) (provides special protections for licensees)

Bankruptcy Code Definition of Intellectual Property

- The Term "Intellectual Property" means –
  - A. Trade Secret;
  - B. Invention, Process, Design, or Plant Protected Under Title 35,
  - C. Patent Application;
  - D. Plant Variety;
  - E. Work of Authorship Protected Under Title 17; or
  - F. Mask Work Protected Under Chapter 9 of Title 17; to the Extent Protected by Applicable Non-Bankruptcy Law

  The United States Code defines "mask work" as "a series of related images, however fixed or encoded, having or representing the predetermined, three-dimensional pattern of metallic, insulating, or semiconductor material present or removed from the layers of a semiconductor chip product, and in which the relation of the images to one another is such that each image has the pattern of the surface of one form of the semiconductor chip product." 17 U.S.C. § 901(a) (2).