MCLE Information

The Handout. Participants must download the PowerPoint as the handout for this webinar to comply with MCLE requirements. Click on "File" in order to "Save As" to your computer.

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Questions. Direct MCLE questions and forms to Jeanine McKeown (her contact information is found on all MCLE forms provided):

Jeanine McKeown at 213-229-7140 or
jmckeown@gibsondunn.com

GIBSON DUNN

SHM Corporate Navigators™

From Distressed to Dressed: Overcoming the Challenges and Realizing Opportunities for Fashion, Retail, and Consumer Businesses in the Current Environment

December 9, 2015

Introduction

GIBSON DUNN

Gibson Dunn is a full-service global law firm, renowned for excellent legal service and commitment to our clients. Gibson Dunn's Fashion, Retail and Consumer Products practice includes attorneys from our corporate, litigation, intellectual property, tax, real estate and business reorganization groups.

SHM Corporate Navigators™

SHM Corporate Navigators™ is a global strategic advisory and merchant banking firm that has completed over $2.5 billion in growth and transactions by integrating and enhancing financial, marketing, operational, and channel performance in collaboration with their middle market clients, consistently maximizing value.

Current Financial Environment

- Despite plummeting energy prices, consumer spending is soft
- Consumer perceptions of value have changed
- Middle market stores are the hardest hit
- Auto loans and mortgages make up a greater percentage of consumer debt than historically

Trends in Retail and Fashion Industry

- On-line sales is the fastest growing distribution channel
- “Fast fashion” and flash sales are growing
- Retailers are focusing on “mobile first” strategies
- Traditional retail chains are expanding on-line channels by acquiring existing outlets
- Retailers are reducing foot print by closing larger stores with negative “four wall” EBITDA

Navigating Successful Turnaround

- Define realistic goals and determine the optimal operational, marketing, legal and financial strategies to reach those goals
- Operational strategies and integrated business planning address challenges with design, product development and production processes, sales, operations, and commercial calendars

Navigating Successful Turnaround (cont.)

- Marketing strategies increase top line sales, identify potential changes to the business model and develop new distribution channels
- Legal strategies can effect store closings, exit non-core markets or dispose of non-core assets
- Financial strategies can address balance sheet and capital structure challenges through debt reduction or financial restructuring

Navigating Successful Turnaround – Advance Planning is Critical

- Because a successful turnaround typically includes navigating significant legal issues, General Counsels play a vital role in developing and implementing the restructuring strategy
- Negotiations take time and must be commenced prior to occurrence of events of default
- Suppliers will often give concessions if they believe the company will remain a customer
- Once a company experiences critical cash shortages, it may be too late to negotiate with creditors

Navigating Successful Turnaround: Understanding Creditors' Bankruptcy Treatment is Critical

- Understanding creditors' treatment in bankruptcy is critical to avoid filing
- Bankruptcy treatment constitutes the floor for a consensual deal
- High liquidation value of inventory creates special hurdles for reorganizing fashion and retail companies

Navigating Successful Turnaround: Debt Reduction

- 100% consensus is required to reduce principal obligations
- In court only ½ in number of creditors and 2/3 in dollar amount of those **that vote** are required
- Case studies show most successful strategy is to negotiate restructuring out of court, but implement it in court

Navigating Successful Turnaround: Credit Negotiation

- Disputed claims are not entitled to vote
- Debt trading will likely consolidate debt holders
- Depending on debt holdings, restructuring may be accomplished by negotiating with a few key holders

M&A Opportunities in the Distressed Retail Environment

- Distressed fashion and retail companies will be forced to acquire new investments, sell non-core assets, exit certain markets or liquidate
- To take advantage of opportunities, it is important to understand creditors' rights that may affect the purchase assets from distressed companies.
- Creditors with liens or security interests may have rights to the assets after the sale
- Unpaid, unsecured creditor may have assert fraudulent transfer or successor liability claims

M&A Opportunities in the Distressed Retail Environment (cont.)

- Buyers of distressed assets may wish to adopt one or more structural approaches to address creditors rights claims
  - Asset purchases
  - UCC foreclosures
  - Assignments for the benefit of creditors or receiverships
  - Bankruptcy

Special Considerations for Acquisitions of Fashion and Retail Companies: Gift Cards

- Purchasers may find it necessary to honor outstanding gift cards
- Therefore, an acquirer must determine its strategy with respect to gift cards before an acquisition
- Experience shows that retailers that have not honored gift cards have faced litigation and ended up honoring them

Special Considerations for Fashion and Retail Companies: Intellectual Property

- Brand names and copyrights may be valuable assets
- If properly structured, inventory liquidation can proceed separately from intellectual property sales
- If debtor is licensor of intellectual property, licensee can continue to use IP even if licensor rejects IP license, except if the IP is a trademark license

Special Considerations for Fashion and Retail Companies: Intellectual Property (cont.)

- Trademark licenses are not covered by the intellectual property provisions of the Bankruptcy Code
- Therefore, applicable state law continues to govern trademarks in a bankruptcy case
- However, courts differ whether rejection of trademark license terminates licensees' rights to use trademarks

Special Considerations for Fashion and Retail Companies: Intellectual Property (cont.)

- IP licenses are typically treated as executory contracts for purposes of Section 365, based on the fact that each side has material unperformed obligations
- Courts have found exceptions where licensee’s obligations were substantially performed

Special Considerations for Fashion and Retail Companies: Intellectual Property (cont.)

- Intellectual property licenses are treated as Executory Contracts subject to "Assumption", "Assumption and Assignment" or "Rejection"
- Generally there is a right to assume and assign executory contracts even where contract prohibits assignment
- Intellectual property licenses are also subject to rejection and exceptions to the general effect of rejection are created by Section 365(n)

Special Considerations for Fashion and Retail Companies: Intellectual Property (cont.)

- The application of Section 365(n) raises a variety of specific issues
- Trademarks are excluded from Section 365(n) because of the special concerns that are raised in a trademark context (these include an owner's obligation to monitor use of licensed trademarks and to enforce quality control standards)
- Unclear how election under Section 365(n) is to apply to license that includes both trademark rights and other intellectual property rights
- The effect of subsequent sale of licensed intellectual property poses certain challenges

Special Considerations for Fashion and Retail Companies: Intellectual Property (cont.)

- Due to the unique nature of intellectual property licenses, many parties employ a variety of risk mitigation devices
- Security interests can be used to back-stop the obligations under license agreement
- Intellectual property holding companies can be created to isolate the intellectual property from other business activities of licensor
- When dealing with a distressed entity, one should consider the type of license and the structure to mitigate fraudulent transfer risk

Special Considerations for Fashion and Retail Companies: Intellectual Property (cont.)

- A bankruptcy filing by an IP licensee presents other challenges
- A bankrupt licensee may have the ability to terminate license agreement following bankruptcy
- A bankrupt licensee may assume or assign intellectual property licenses

Special Considerations for Fashion and Retail Companies: Leases

- If store locations will be closed, it is critical to allow time to negotiate with landlords
- Due to treatment in bankruptcy, landlords may re-negotiate leases without a filing
- Leases can be rejected in a bankruptcy case, with a damages cap of 1 year's rent or 15% of the remaining lease term not to exceed 3 years
- Landlords are required to mitigate damages

Special Considerations for Fashion and Retail Companies: Leases (cont.)

- Leases can be assigned to third parties in certain circumstances, even if lease terms prevent assignments
- Monetary defaults must be cured before lease can be assumed or assigned
- Leases in bankruptcy must be assumed in 120 days, with one 90-day extension, upon court approval

Special Considerations for Fashion and Retail Companies: Leases (cont.)

- Thereafter, no extensions are allowed without landlord's prior written consent
- Landlords may be willing to negotiate regarding market leases, but not for below-market leases
- If inventory is liquidated, it is critical to negotiate with landlords for GOB sales and time to reject store leases

Key Take-Aways

- Operational, marketing, legal and financial approaches allow companies to navigate the complex, challenging environment they face
- Advance planning is required to successfully execute operational or financial restructurings of retail and fashion companies
- It is critical to be knowledgeable about bankruptcy treatment of creditors, even if no bankruptcy is ever filed

Key Take-Aways (cont.)

- Challenges faced by competitors and counterparties present opportunities for stronger businesses in the industry
- Dispositions of non-core assets, including intellectual property and real estate can provide buying opportunities

Harry J. Kobritz

Managing Director, SHM Corporate Navigators
260 Madison Avenue, 8th Floor, New York, New York 10016
Harry.Kobritz@shmcnglobal.com

In his 30 years as a senior financial, operating executive, and strategic advisor, Harry has primarily served middle market companies in enhancing financial and operational performance, due diligence, corporate and family governance. He has initiated and completed transactions with a combined value of $500 million and provided strategic advisory services for companies with enterprise values exceeding $1 billion. His extensive expertise includes retail, fashion and beauty, manufacturing, global import and distribution, cross border transactions, staffing, advertising and marketing. He has restructured legendary retail chains and structured the US path to entry for some of the most iconic fashion brands in the world such as Max Mara, Issey Miyake, and several others.

In 2010, he co-founded SHM Corporate Navigators™, a corporate advisory and merchant banking firm to enable middle market companies, family businesses, and portfolio companies of private equity firms to further differentiate themselves in the market and grow by integrating and enhancing their financial, marketing, operational, and channel performance, and providing the necessary capital to achieve these results.

Harry's executive experience includes roles as Chief Operating Officer, Chief Restructuring Officer and Chief Financial Officer at both public and private middle market companies.

Harry holds a BS in Finance and Accounting from Brooklyn College and graduated with honors. He is a Certified Public Accountant, licensed in New York and is an alumnus of Ernst and Young where he was a member of the Assurance Group as a Senior Audit Manager for over seven (7) years.

Industry affiliations include: New York State Society of CPAs Financial Reorganization Committee, Chairman Emeritus; The Economic Club of New York, Member; Association for Corporate Growth (ACG), Member, Programming Committee; and American Institute of CPAs, Member. He has published editorials and white papers in *Middle Market Growth* published by ACG.

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Samuel A. Newman

Partner, Gibson, Dunn & Crutcher LLP
333 South Grand Avenue, Los Angeles, CA 90071-3197
Tel: +1 213.229.7644
SNewman@gibsondunn.com

Sam Newman is a partner in the Los Angeles office of Gibson, Dunn & Crutcher and a member of both the Business Restructuring and Reorganization Group and the Corporate Department. His practice involves representing creditors, debtors and other parties-in-interest in Chapter 11 cases. He also advises buyers, sellers, lenders and borrowers in transactions involving distressed assets. Currently, Mr. Newman represents or has recently represented a variety of retail and consumer goods companies and their creditors in insolvencies, workouts, restructurings and bankruptcy:

- Natrol, Inc., manufacturer an distributor of vitamins and nutraceutical products, in its chapter 11 case;
- SK Telecom Americas, Inc. in its bid for the assets of Blockbuster Video, Inc. ;
- Contec Corp. in its acquisition of the PowerBalance Corporation through a sale conducted pursuant to Section 363 of the Bankruptcy Code; and
- Credit Managers Association in its capacity as Assignee for the benefit of creditors of Westinghouse Digital Electronics LLC ("WDE").

Mr. Newman has been named as one of California's leading lawyers in business and restructuring by *Chambers USA – America's Leading Business Lawyers* and recognized by his peers as one of *The Best Lawyers in America®* in the area of Bankruptcy and Creditor-Debtor Rights Law. Mr. Newman has also been named as a Southern California Super Lawyer in the area of Bankruptcy & Creditor/Debtor Rights. His speaking engagements include *Debtor In Possession Financings: Current Developments*, Los Angeles County Bar Association, *When Lenders Fail: The Ultimate Indignity*, The Financial Lawyers Conference; *The Subprime Meltdown From an Insolvency Litigation Perspective*, 11th Annual Southwest Bankruptcy Conference of the American Bankruptcy Institute; *The Subprime Lending Industry: A Look at the Restructuring of a Market in Turmoil*, the American Bar Association Annual Meeting, Section of Business Law; *When Good Loans Go Bad: An In-Depth Discussion of the Subprime Lending Industry*, Turnaround Management Association.

Mr. Newman earned his law degree *magna cum laude* from Georgetown University Law Center where he was elected to the Order of the Coif. He received his B.S. in Foreign Service from Georgetown University's School of Foreign Service in 1992. Prior to joining Gibson, Dunn, he held political and fundraising positions with the Democratic National Committee in Washington, DC and served in legislative and policy positions for Senator John Glenn (OH) and Representatives Gary Ackerman (NY) and Rob Andrews (NJ).

Martin L. Okner

Managing Director, SHM Corporate Navigators
260 Madison Avenue, 8th Floor, New York, New York 10016
Martin.Okner@shmcnglobal.com

With a total of over 20 years of experience in branded consumer goods, Martin has created and developed strategic plans in marketing, channel development, and business lifecycle management to grow middle market companies through proven methodologies. He has accomplished this with middle market companies and with companies such as Revlon, Cadbury and Philip Morris. His strategies have generated over $2.5 billion of incremental retail value with many iconic brands.

In 2010, he co-founded SHM Corporate Navigators™, a corporate advisory and merchant banking firm to enable middle market companies, family businesses, and portfolio companies of private equity firms to further differentiate themselves in the market and grow by integrating and enhancing their financial, marketing, operational, and channel performance, and providing the necessary capital to achieve these results. He has advised private equity firms on investment targets in fashion and beauty retail such as Fossil, Timberland, Hanesbrands, and Wet Seal.

Martin holds an MBA from Fordham University Graduate School of Business Administration in Corporate Finance, and a Bachelor of Arts degree in Political Science (Minor, Business Administration) from Seton Hall University where he graduated Summa Cum Laude. Additionally, he is an Adjunct Professor of Marketing at Fordham Graduate School of Business Administration and Parsons, The New School for Design.

Industry affiliations include: Association for Corporate Growth (ACG), Chairman; the Economic Club of New York, Member; and ACG Cares New York Chapter, Inc., Board Member. He has published editorials and white papers in *Forbes*, *Chain Drug Review*, *Mergers & Acquisitions* and *Middle Market Growth* published by ACG. Mr. Okner was recognized by M&A Advisor as the 2011 winner of the 40 Under 40 Award and by Walmart and Cadbury Adams USA as 2005 Supplier of the Year.

Janet M. Weiss

Partner, Gibson, Dunn & Crutcher LLP
200 Park Avenue, New York, NY 10166-0193
Tel: +1 212.351.3988
JWeiss@gibsondunn.com

Ms. Weiss is a partner in the New York office of Gibson, Dunn & Crutcher and a member of the Business Restructuring and Reorganization Practice Group. She has more than 25 years of experience representing debtors, creditors, committees, secured lenders, DIP financing lenders and acquirers in bankruptcy cases, including pre-negotiated and pre-packaged cases, and out of court restructurings. She also has significant experience in bankruptcy litigation and bankruptcy aspects of asset-backed and mortgage-backed securities. Ms. Weiss has been named as one of the elite bankruptcy lawyers in New York and one of New York City's top women lawyers by *Avenue Magazine*. *The Deal's Bankruptcy Insider named her* as one of the top ten lawyers for acquirers in bankruptcy acquisitions. She has lectured on bankruptcy topics at numerous programs sponsored by the American Bankruptcy Institute, the American Bar Association and the New York State Bar. Her article, *The Time Bomb in Your Indenture—No Action Clauses and Creditor Standing*, and a chapter entitled *Rights of Trademark Licensees: Protection for Non-Debtors After Rejection of Trademark License Agreements* were recently published.

Representations related to fashion include:

- representation of Saks Fifth Avenue in proposed acquisition of Barney's in Barney's first chapter 11 case;
- representation of BCBG MaxAzria in acquisition of substantially all leases from G+G Retail's chapter 11 case;
- representation of Hoop Holdings LLC, which sold Disney clothing and other Disney products, in chapter 11 case;
- representation of The Finish Line in proposed acquisition of Footstar; and
- representation of landlord for Syms retail space.