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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
RICHMOND DIVISION

In re:	)	Chapter 11
TOYS "R" US, Inc., *et al.*,	)	Case No. 17-34665 (KLP)
Debtors.[1]	)	(Jointly Administered)

LIMITED OBJECTION AND RESERVATION OF RIGHTS OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS WITH RESPECT TO THE DEBTORS' WIND DOWN MOTION

[1] The Debtors in these cases, along with the last four digits of each Debtor's tax identification number, are set forth in the *Order (I) Directing Joint Administration of Chapter 11 Cases and (II) Granting Related Relief* [Dkt. No. 78].

The Official Committee of Unsecured Creditors (the "**Committee**") of the debtors and debtors-in-possession (collectively, the "**Debtors**" or the "**Company**") in the above-captioned chapter 11 cases (the "**Chapter 11 Cases**") hereby files this limited objection and reservation of rights (the "**Limited Objection**") with respect to the *Debtors' Omnibus Motion for Entry of Orders: (I) Authorizing the Debtors to Wind-Down U.S. Operations, (II) Authorizing the Debtors to Conduct U.S. Store Closings, (III) Establishing Bidding Procedures for the Sale of the Debtors' Canadian Equity, (IV) Enforcing an Administrative Stay, and (V) Granting Related Relief* (the "**Wind Down Motion**") [Dkt. No. 2050].[2] In support of this Response, the Committee respectfully represents as follows:

PRELIMINARY STATEMENT

1. As the Committee stated on the record at the March 15th hearing, the Committee is extremely disappointed that the Debtors are liquidating all of their operations in the United States, causing tremendous hardship to hundreds of vendors and landlords, thousands of employees, millions of customers and other creditors. The Wind Down Motion appears to be the culmination of a series of events that were unfathomable when the Debtors filed for bankruptcy a mere six months ago. At that time, the Debtors were actively promoting a reorganization, not a liquidation, and made two points clear to the Court and their constituents: first, that the "unprecedented" $3.125 billion DIP Facilities would provide the Debtors sufficient liquidity to ensure a successful holiday season and provide additional capital to re-invest in their businesses; and second, that the Debtors would have 16 months of runway – more than enough time to complete a successful reorganization – with no case milestones or case controls. On the basis of these assurances, which formed the backbone of the Debtors' expansive requests for first day

[2] Capitalized terms used but not defined herein have the meanings ascribed to them in the Wind Down Motion.

relief, the Committee agreed to allow the DIP Lenders to obtain liens on hundreds of millions of dollars in unencumbered assets, in addition to over $80 million in financing fees for those lenders. Suppliers, including vendors, likewise agreed (and in some cases, were *obligated* under trade agreements) to extend hundreds of millions of dollars of unsecured credit to the Company post-petition to deliver merchandise – including inventory for which the Debtors have not paid, but now seek to liquidate for the benefit of their secured lenders.

2. Despite the assurances of a successful reorganization path just six months ago, the Debtors now seek to shutter all of their U.S. operations (as well as certain foreign businesses) and implement a swift, massive liquidation. The limited and flexible DIP case controls the Debtors previously promoted are now being used to force an immediate liquidation of all U.S. operations, to the severe prejudice of the unsecured creditors that the Debtors relied on post-petition to fund their now-failed reorganization effort. To date, the Committee understands that the Debtors have over $450 million in post-petition merchandise payables that remain unpaid, and have defaulted on approximately $150 million in post-petition trade agreement obligations they had contractually agreed to pay for the extension of post-petition credit. More disturbing, the goods shipped to the Debtors under trade agreements that obligated vendors to provide unsecured trade credit are now being liquidated in GOB sales for the benefit of secured lenders. And while the Committee was able to obtain limited relief under the DIP Orders relating to marshalling, 506(c), and 552(b) – each of which may ultimately be essential to preserving value for unsecured creditors – they will likely not be sufficient to compensate vendors and landlords for the post-petition losses and the contractual promises of compensation for critical suppliers.

3. A key question of the Committee is how did one of the largest, publicly reporting retail debtors have such a dramatic decline in operations in just six months. This is a question

that needs to be answered, even as this liquidation progresses. The Committee does not fully adopt or accept the Debtors' narrative – both in their Wind Down Motion or their statements to the Court – of the events that led to this massive meltdown and virtually unprecedented destruction of value. That investigation will come.[3]

4. In the interim, the Committee continues to explore all avenues of maximizing recoveries for creditors – and continues to believe that all such avenues must be preserved – including ensuring that the Debtors have adequate time to facilitate having a sub-set of the U.S. stores sold as a going concern in connection with the Canadian sale transaction. The Committee's overarching goal at this point is to maximize value, while also making sure that post-petition creditors are treated fairly and equitably.[4] To that end, any liquidation of assets authorized by this Court must be conducted in a considered, organized way that takes account of the interests of all parties involved.

5. The Committee therefore does not object, in principle, to certain of the relief requested in the Wind Down Motion, but certain aspects of the relief must be modified to serve the interests of fairness and equity. Given the current condition of these cases, we cannot simply defer to the business decisions of the Debtors and their management. Accordingly, any approval of the Motion must be conditioned on the various critical changes, protections and reservation of rights outlined below.

LIMITED OBJECTION

6. In the Wind Down Motion, the Debtors seek significant relief from this Court – on an extremely expedited basis – to immediately implement a liquidation of the domestic

[3] The Committee assumes that the Debtors and any lenders or other parties-in-interest will continue to maintain and not destroy any documents relating to both pre- and post-petition transactions.

[4] The Committee will also continue to focus on reorganization or other going concern transactions that preserve various of the international operations.

businesses, while maintaining the flexibility to sell certain of the U.S. stores as part of a going concern sale with the Canadian business. As set forth in more detail below, the Committee has serious concerns that the Debtors are seeking certain overbroad, permanent relief, at this stage of the domestic liquidation process, when the only immediate relief that the Debtors require on a final basis is the approval of the GOB Sales. The rest of the requested relief – to the extent the Court is inclined to grant it – should be limited to approval on an interim basis or subject to reservations of rights, allowing the Committee and creditors alike sufficient time to analyze and understand the implications of all aspects of the liquidation.

7. Both before and after the filing of the Wind Down Motion, the Committee professionals have been flooded with calls and questions from the Debtors' pre- and post-petition creditors, who have transacted with the Debtors in good faith, but are now faced with a lack of payment both under negotiated Critical Vendor agreements and/or on account of post-petition goods provided to the Debtors on trade terms with the promise and expectation of full payment. With a liquidation now being run primarily, if not entirely, for the benefit of secured creditors, it is imperative that any relief granted in connection with the Wind Down Motion be appropriately tailored to protect creditors (including post-petition vendors, landlords, employees, and others), while maximizing value for all stakeholders.

8. Because the Committee does not wish to burden the Court with a lengthy pleading,[5] it is succinctly identifying some of its major concerns and aspects of the Wind Down Motion that must be modified. The Committee will continue to work with the Debtors to modify the proposed form of Order to address many, if not all, of these concerns amicably, including:

[5] The Committee is aware that various creditors, including post-petition vendors, have filed pleadings raising concerns over the payment of goods shipped to the Debtors, accepted by the Debtors, but not paid for – including goods that will now be liquidated for the sole benefit of the secured lenders. As noted in this Limited Objection, the Committee shares various of the concerns of these post-petition vendors and landlords.

a. Administrative Stay. The Wind Down Motion seeks to implement an administrative stay preventing the enforcement or collection of any claim that is not authorized by the Wind Down Budget (which was only just filed this evening). While the Committee understands that the Debtors need to induce certain parties-in-interest to provide services to the Debtors notwithstanding the impending domestic liquidation,[6] a blanket stay for the remainder of the case may unduly prejudice vendors and other creditors that, based on their contractual or other relationships with the Debtors, continued doing business in the months and weeks leading up to the liquidation and now may be prevented from seeking to collect. A blanket permanent stay preventing creditors from seeking to collect post-petition amounts owed is overly broad at this time. The Committee agrees that given the unfortunate circumstances, the Debtors' estates and constituents (including the Committee) must focus on both maximizing value and identifying any going-concern opportunity for domestic operations. A barrage of litigation to pursue administrative expense claims will be both distracting (if not chaotic) and unnecessarily drain the estates of costs to respond to each one. But, an open-ended stay seems imprudent at this time. **Accordingly (and assuming the Debtors agree to escrow proceeds on the terms described herein), the Committee requests that any administrative stay instead be a temporary one for 90-days, subject to further extension by order of the Court, including in connection with orderly procedures for the assertion and payment of stayed claims, and be narrowly tailored to post-petition claims.[7]**

b. March 5, 2018 Date for Vendors. While the Debtors tout that their lenders "have agreed" to let them pay for new merchandise delivered on or after March 5, 2018 in full, they have yet to establish why March 5th is the correct payment date. The Wind Down Motion and statements made on the record by Debtors' counsel indicate that the Debtors had concerns about a potential liquidation before March 5th, and additional information is necessary to determine at what point the Debtors (and their secured lenders) believed they might not be able to pay for new merchandise ordered by the Debtors and shipped by vendors. To the extent merchandise was ordered by the Debtors prior to March 5th with uncertain, if not little, expectation of their ability to pay on terms provided by the vendors (e.g., 30, 60, or 90 days later), it may be inequitable to allow such goods to be liquidated for the primary, if not sole, benefit of secured lenders, without payment to the vendors. In particular, many vendors were subject to Critical Vendor agreements with the Debtors

[6] The providing of what is tantamount to a super-priority administrative expense claim to ongoing vendors, suppliers and other creditors to induce an extension of credit terms is consistent with section 364(c)(1) of the Bankruptcy Code.

[7] The Committee understands that the Debtors may couple their request for an administrative stay with a new post-petition claims procedures to be the subject of a separate motion. The Committee suggests that any stay put in place now be condition upon such procedures being approved after notice and opportunity to object and be heard. The Committee would further recommend that the Court hold a status conference within 45-days of the imposition of the temporary stay to assess the status of the liquidation process.

that obligated vendors to continue shipping merchandise to the Debtors on trade terms that provide for payment long after the merchandise is received, or face the threat of damages. The *quid pro quo* was the contractual obligation by the Debtors to make payments under these Critical vendor agreements – which obligations have gone unfulfilled to the tune of $150 million. **The Committee is continuing to analyze these issues to determine if a date earlier than March 5th is more appropriate and reserves all rights in this regard.**[8] At the very least, there should be flexibility in the March 5th cut-off depending on the circumstances of the business relationship between the Debtors and their creditors and any approval of a March 5th date should be subject to a reservation of rights to revisit that an earlier date if more appropriate.

c. Escrow of Certain Proceeds from GOB Sales & Canadian Equity. As noted above, as part of the GOB sales, the Committee understands that the Debtors currently hold over $450 million in inventory provided post-petition by vendors but that *has not been paid for*. The Debtors now seek to include this inventory – which they've essentially taken for free – in liquidation sales, and use the proceeds of those liquidation sales for the benefit of the secured lenders, including the prepetition secured lenders. The secured lenders should not benefit from the sale of unpaid for inventory, nor should they benefit from an immediate paydown upon the sale of any Canadian equity – and certainly not until there has been a full opportunity to evaluate the events leading up to this drastic change in direction. **A process and appropriate safeguards, including an escrow of certain GOB sale proceeds and the proceeds from the sale of the Canadian assets, must be implemented to ensure that the secured lenders – especially the prepetition lenders asserting liens on "free inventory" – are not repaid immediately with proceeds of such inventory. Various rights may exist, including equitable remedies, that should be preserved and, at a minimum, not barred by expedited relief.**

d. Goods in Transit. The Debtors have continued placing orders for goods and merchandise from vendors, including as recently as March 12, 2018. Accordingly, many vendors' goods are currently in transit to the Debtors. The Wind Down Motion, however, does not provide any clarity as to the

[8] One of the drivers of the liquidation is a determination by the Debtors that they would purportedly be in breach of a covenant in Section 6.16 of the North American DIP Agreement that requires the Debtors to deliver a revised budget on January 31, 2018, which the Debtors did not deliver. The B-4 Lenders waived this covenant through March 3, 2018, and then further extended. During the period from February 1, 2018 forward, the Committee was actively engaged in facilitating the Debtors' reorganization efforts, working on various business plan concepts and going concern models, as well as negotiating with the Taj Lenders, the Debtors and the Debtors' disinterested directors concerning a stand-alone plan for Europe and Asia. On March 2, 2018, the Debtors' advisors informed the Committee and its advisors that the Debtors believed they were unable to meet or obtain a general waiver of the 6.16 covenant, and their purported breach could cause a liquidation of the entire domestic business. From March 2nd to the filing of the Wind Down Motion, the Committee sought, unsuccessfully, to persuade the Debtors and their secured lenders to defer the liquidation of all U.S. operations to allow the Debtors to pursue a sale of at least a subset of the U.S. operations as a going concern.

disposition of these goods in transit, including goods shipped based on orders both before and after March 5, 2018. **The Debtors should be required to immediately communicate with all post-petition vendors with goods on order with specific instructions on (i) whether such goods will be accepted, and if so, how and when paid for[9] and (ii) if not, exactly how and when such goods will be returned to the vendors, including in instances where multiple vendors' goods have been consolidated for shipment.** In addition, the Debtors need to clarify with clear and unequivocal language that any actions taken by vendors (either with the Debtors or with common carriers) to coordinate the return of vendor goods for cancelled orders will not result in any actual or potential violations of the automatic stay.

e. Store-Brand (Private Label) Goods. Various vendors sell store-brand (private label) goods that were made specifically for the Debtors. These vendors historically have been unable to sell these branded goods to third parties due to intellectual property and/or trademarks with Toys "R" Us. In light of the full-scale liquidation of the Debtors' domestic businesses, **to the extent vendors have such store-brand goods that have already been manufactured and for which the Debtors are cancelling orders, the Court should permit these vendors to sell these goods to third parties – notwithstanding prior restrictions – allowing them to mitigate their damages resulting from the Debtors' wind down.**

f. Conduct of the GOB Sales.[10] The Committee has asked the Debtors to clarify in the order approving the GOB Sales that the Debtors and the Consultants shall only be permitted to conduct GOB Sales at the stores themselves and shall not use the Debtors' or any other websites to conduct such "going out of business" or any other similarly-themed liquidation or deeply-discounted sales. In addition, to the extent any unsold Merchandise remains at the conclusion of the GOB Sales, the subsequent disposition of that Merchandise shall be subject to further order of the Court and the Debtors shall not seek, absent further Court order, to dispose of such Merchandise through any other means, including "grey markets" or off-price retailers. Finally, the Order should make clear that neither the Debtors nor the Consultants are authorized to sell any Non-Merchandise Goods owned by third parties, including specialty fixtures provided by various vendors, without express prior written consent of the third party. Presently, the Full Chain Consultant Agreement (section 4(C)) says that such Non-Merchandise Goods may be sold *either* subject to the Court's approval *or* the required consent.

[9] Vendors with goods being shipped and accepted for payment should not be required to provide terms to the Debtors for these accepted goods, irrespective of any existing Critical Vendor agreements which have been breached by the Debtors.

[10] The Committee has sent specific changes to the proposed Wind Down Order to the Debtors, which are still being reviewed by the Debtors. Some, if not all, of the Committee's specific concerns on the conduct of the GOB Sales may be addressed consensually through changes to the order.

g. Canadian Sale Process. The Debtors' Canadian business has continued to perform successfully post-petition, and remains a valuable and viable part of the Debtors' operations. In the Wind Down Motion, the Debtors seek to implement an *extremely expedited process* for the sale of the equity in the Canadian businesses, with bids due by March 26th and an auction to occur by March 29th. As the Wind Down Motion states, there may be a path for up to 200 of the Debtors' better performing domestic stores to continue in operation (even after the GOB sales commence at such stores) as part of a "reverse-merger" transaction with the Canadian operations. This is a critical opportunity to preserve some "Toys R Us" operations in the United States and this process must be given a reasonable amount of time to be tested. This would have the potential to bring significant value into the estates that would otherwise be largely unavailable in GOB Sales at those stores, as well as preserve employment opportunities and mitigate vendor and other post-petition claims. All parties have an interest in maximizing the value generated from such a sale. However, the extremely expedited sale process will have the opposite effect and could depress value as bidders will have insufficient time to conduct due diligence with respect to these assets. **The sale timeline must be extended to provide at least an additional 30 days for bids on these assets (i.e., bids due at the end of April 2018).**[11] The Committee is prepared to work with the Debtors on a more rational timeline for the Canadian auction sale process. In addition, it must be clear that the commencement of "going out of business" sales at stores will not preclude later removing various stores from the GOB process to allow them to be sold and continued as ongoing sale operations as part of any Canadian sale transaction or otherwise. Indeed, the GOB Sales are contemplated to take place over a 14-16 week period; much longer than any process for the sale of the Canadian assets. Thus, the GOB Sales for the U.S. stores should in no way hinder a robust marketing process for the Canadian assets.

h. Wind Down Bonuses. The Debtors are also seeking to approve certain "non-insider incentive programs for the Debtors' remaining store and headquarters employees as necessary to manage an orderly and efficient Wind-Down." Wind Down Motion ¶ 10. The Committee is continuing to diligence the proposed Wind-Down Incentive Program to determine whether the amounts are reasonable, in line with the market, and will have the intended effect of incenting the remaining employees to maximize value during the wind down process. The Committee is also clarifying in the Order that under no circumstances will any insiders or management be receiving additional bonuses as part of the Wind-Down Incentive Program.

[11] The Committee understands that the Debtors may be proposing an extension of the deadlines and will work with the Debtors to agree upon mutually acceptable dates for the Canadian sale process.

i. Wind Down Budget. The Committee reserves all rights with respect to the Debtors' just-filed Wind Down Budget.[12] Upon a preliminary review, the Committee has identified at least two important issues. *First*, it is the Committee's understanding that the Wind-Down Budget will contain amounts sufficient to pay all administrative claims incurred on and after March 5, 2018. Providers of goods and/or services to the Debtors following this date are only doing so in reliance on assurances from the Debtors that those claims will be paid. **Accordingly, any order approving the Wind-Down Budget should make clear that in the event the actual amount of post-March 5th claims exceeds a line item in the Wind-Down Budget, the Budget will be adjusted accordingly to account for the liability of those claims and all such claims will be paid.** Moreover, all such amounts should be paid promptly upon reconciliation, and without offsets for allowances and/or discounts (which offsets should only be dealt with in the context of determining the amount of any unpaid administrative claims). *Second*, the Debtors have indicated that they are implementing the Wind Down Budget with the goal of limiting expenses during the liquidation process. Nevertheless, this goal must be balanced against the important need for protecting the massive universe of unsecured and administrative creditors – a responsibility that falls squarely (if not solely) on the Committee. As the liquidation progresses, the Committee will need to continue dealing with numerous issues that directly impact creditors, including identifying and preserving unencumbered assets, determining the relative rights of administrative, secured and unsecured creditors, addressing intercreditor issues, and overseeing the sale of various of the Debtors' assets (including inventory, real estate and leases, and Canadian assets) to ensure that the Debtors are garnering maximum value for these assets. So long as these cases remain in Chapter 11 and the Debtors and their secured lenders seek to take advantage of Chapter 11, the Bankruptcy Code compels a functioning creditors' committee. Thus, the Wind Down Budget must reflect a reasonable budget for the Committee and its professionals to allow it to exercise its fiduciary duties from April through the completion of the wind down process.

9. In addition to the above-referenced specific issues with the Wind Down Motion, the Committee must be actively involved in all aspects of the Wind Down, including all marketing processes, GOB Sales, and the liquidation of other assets of the Debtors, and the Debtors must be cooperative and transparent. To this end, the Debtors must provide the

[12] In addition, to date, the Debtors have not authorized the Committee professionals to share much of the information underlying the Wind-Down Budget with Committee members. For the Committee to appropriately analyze the terms of the Wind-Down Budget and determine an appropriate exercise of its fiduciary duties, the Committee members must be able to review and analyze this information on a confidential basis.

Committee with all reporting information provided to the secured lenders, and make the appropriate subject matter experts available as reasonably requested by the Committee on the following topics: (i) the Wind-Down Budget, including weekly budget to actual results and variance explanations, explanations regarding subsequent amended budgets and a detail buildup of receipts and escrowed amounts, (ii) the sizing of unpaid administrative expenses as of the March 5th date or an alternative date determined by the Court, including detail sufficient for the Committee to do its own independent analysis, (iii) ongoing reporting of administrative claim balances and payments to ensure that all obligations after March 5th are paid timely, (iv) US and Canadian sales process updates, including at least a weekly call where updates of interested parties, status of due diligence, and reporting of indications of interest are disclosed, and (v) other information as reasonably requested by the Committee.

10. As stated on the record at the hearing held on March 15, 2018, the Committee has received numerous questions from vendors and other creditors regarding the liquidation process. To facilitate increased communication in this regard, the Committee is in the process of updating its website to include information about the proposed wind down process, as well as answers to many of the questions about this process that the Committee has received thus far. The Committee has also asked the Debtors to provide the name of an authorized representative or representatives from the Company who can directly assist with creditor communications.[13]

11. The Committee has provided the Debtors with comments to the proposed Order addressing many of these issues. To the extent the Committee's concerns are not resolved or addressed in an amended proposed order, the Committee reserves all rights relating to the Wind

[13] The Committee's website is available at: http://www.jndla.com/cases/toyscommittee. The Committee's website also includes a hotline and an email inbox for creditors with questions not otherwise answered by the website, and contact information for the professionals for both the Debtors and the Committee.

Down Motion, including to supplement this Limited Objection and to make such other and further statements or objections as may be necessary or appropriate.

Dated: March 19, 2018

Respectfully submitted,

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