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10
11 **UNITED STATES BANKRUPTCY COURT**
12 **CENTRAL DISTRICT OF CALIFORNIA**
13 **LOS ANGELES DIVISION**

14 In re:
15 WORLD BAZAARS, INC., a California
16 corporation,
17 Debtor.

Case No. LA 00-24386 ES

Chapter 11

18
19 **MEMORANDUM OF POINTS AND
20 AUTHORITIES SUPPORTING
21 CONFIRMATION OF SECOND
22 AMENDED CHAPTER-11 PLAN
23 PROPOSED BY WORLD BAZAARS,
24 INC. (DATED NOVEMBER 10, 2000), AS
MODIFIED**

25
26 **Confirmation Hearing**

27 Date: January 25, 2001
28 Time: 10:00 a.m.
Place: 255 E. Temple St.
Courtroom 1645
Los Angeles, CA 90012

1

OVERVIEW

World Bazaars, Inc.¹ respectfully submits this Memorandum of Points and Authorities supporting confirmation of the *Second Amended Chapter-11 Plan Proposed by World Bazaars, Inc. (Dated November 10, 2000)*, as modified (the "Plan"). This Memorandum is supported by:

- The *Declaration of Frank Budetti* (the "Budetti Declaration") that is being filed concurrently with this Memorandum;
- The *Declaration of Martin Barrett* that is being filed concurrently with this Memorandum;
- The *Declaration of James Goldman* that is being filed concurrently with this Memorandum;
- The *Declaration of Shanda Pearson Regarding Analysis and Tabulation of Ballots and in Support of Confirmation of Second Amended Chapter-11 Plan Proposed by World Bazaars, Inc. (Dated November 10, 2000), as Modified* (the "Ballot Tabulation");
- The various declarations of service filed in connection with the Plan;
- The solicitation materials previously filed with the Court and distributed to all parties entitled to vote to accept or reject the Plan;
- The Disclosure Statement² accompanying the Plan;
- The *Declaration of Frank Budetti* previously filed in support of the Disclosure Statement;
- The record in this case;³ and

¹ World Bazaars, Inc. is referred to hereafter as World Bazaars or the company.

² Capitalized terms used in this Memorandum and not otherwise defined have the meaning ascribed to them in the Plan.

³ Pursuant to Federal Rule of Evidence 201, World Bazaars hereby requests that the

1 • Any other argument and evidence that may be presented at or be-
2 fore the hearing regarding confirmation of World Bazaars' Plan.

3 As demonstrated by this evidence and in this Memorandum, the Plan
4 should be confirmed. First, the Plan is widely supported by World Bazaars' creditors.
5 The Plan itself is the culmination of many months of negotiations among the major con-
6 stituencies in this case—including World Bazaars, the Bank Group, the SKM Funds and
7 SKM Lenders, and the Creditors' Committee—all of which either support or do not op-
8 pose Plan confirmation. Moreover, following a solicitation conducted in accordance with
9 the Bankruptcy Code, the Bankruptcy Rules, and this Court's order establishing solicita-
10 tion procedures (the "Solicitation Order"), creditors entitled to vote on the Plan over-
11 whelmingly accepted the Plan with respect to all impaired classes. As for Classes that
12 have been deemed to reject the Plan, the treatment of all such Classes complies with
13 the requirements of Bankruptcy Code section 1129(b), and the Plan may therefore be
14 crammed down upon these Classes.

15 Second, the Plan proposes to distribute World Bazaars' remaining assets
16 on terms that are fair, reasonable, and economically feasible. World Bazaars com-
17 menced this case to wind down its affairs and to arrange for the orderly liquidation and
18 distribution of its assets. World Bazaars has now successfully liquidated substantially
19 all of its assets, and its Plan provides for the orderly distribution of the resulting cash
20 proceeds. As set forth in detail in Section III.A.11, below, World Bazaars has available
21 approximately \$250,000 in free and clear cash, and World Bazaars is also authorized to
22 use up to \$500,000 of the Bank Group's cash collateral to satisfy certain Effective Date
23 and postconfirmation obligations. These funds are more than adequate to satisfy the
24 \$570,000 in estimated allowed Administrative and Priority Claims and postconfirmation
25 expenses. The Plan will distribute all remaining assets among all other creditors hold-
26 ing allowed claims against World Bazaars' Estate. The Plan also provides for the
27

28 Court take judicial notice of all documents previously filed or entered in this case.

1 prosecution of certain potential causes of action and the distribution of the net proceeds
2 derived therefrom. For example, the Plan establishes a \$500,000 Litigation Fund to be
3 used by the Creditors' Committee to pursue avoidance actions and claim objections for
4 the benefit of certain unsecured creditors. The Plan also authorizes a Plan Administra-
5 tion Committee to pursue Insider Litigation against Insiders such as the Abulafias. The
6 Insider Litigation will be pursued on a contingency basis by Pircher, Nichols & Meeks
7 (whose employment application is currently pending before this Court) with a \$150,000
8 retainer to be provided by the Bank Group.

9 Third, as discussed in detail below, the Plan complies with all of the Bank-
10 ruptcy Code's requirements for confirmation of a Chapter-11 plan. Accordingly, World
11 Bazaars respectfully requests that the Court enter an order confirming the Plan.

12 **II.**

13 **OUTCOME OF VOTING**

14 On or about December 8, 2000, in accordance with the Solicitation Order
15 in this case, World Bazaars caused the Plan and related solicitation materials to be
16 served upon all parties in interest. The Solicitation Order established January 11, 2001
17 as the deadline for receipt of ballots accepting or rejecting the Plan. As summarized
18 below, all impaired Classes that were entitled to vote on the Plan and that timely submit-
19 ted ballots have unanimously voted to accept the Plan.⁴

20 **SUMMARY OF PLAN CLASSES AND VOTING**

21 **Class 1 Accepted.**

22 Bank Group Accepted by:
23 100% in amount (\$17,013,000) and
24 100% in number (1)

25 **Class 2 Ballot Deadline: January 22, 2001.**

26 The SKM Lenders

27

28 ⁴ See the Ballot Tabulation.

SUMMARY OF PLAN CLASSES AND VOTING

3	Class 3	Rejected.
4	The Abulafias	Deemed to reject under the Plan.
5	Class 4	Accepted.
6	Other Secured Lenders	Unimpaired—not entitled to vote.
7	Class 5	Accepted.
8	Priority Claims	Unimpaired—not entitled to vote.
9	Class 6	Accepted.
10	General Unsecured Claims	Accepted by: 96% in amount (\$998,753.81) 84% in number (80)
11	Class 7	Ballot Deadline: January 22, 2001
12	The SKM Lenders	
13	Class 8	Rejected.
14	The Abulafias	Deemed to reject under the Plan.
15	Class 9	Rejected.
16	The WARN Act Claims	Deemed to reject under the Plan.
17	Class 10	Rejected.
18	Interests	Deemed to reject under the Plan.

21 In summary, the following classes are impaired under the Plan and were
22 entitled to vote: Class 1 (Bank Group's Secured Claims under the Credit Facility); Class
23 2 (the SKM Lenders' Secured Claims under the Term Loan); Class 6 (General Unse-
24 cured Claims); and Class 7 (the SKM Lenders' Unsecured Claims). Except for Classes
25 3 and 7, whose ballot deadline is January 22, 2001, these Classes all voted to accept
26 the Plan. In addition, Classes 4 (Other Secured Claims) and 5 (Priority Claims) are un-
27 impaired and are therefore deemed to accept the Plan.

28 The remaining Classes are deemed to reject the Plan. Class 3 (the Abula-

1 fia Trust's Secured Claims under the Term Loan) and Class 8 (the Abulafia Trust's Un-
2 secured Claims) have been deemed to reject because the Plan proposes to place any
3 distributions to holders of Class-3 and Class-8 into an interest-bearing escrow account
4 pending the resolution of significant litigation against these claim holders. The claims
5 asserted against the Class-3 and Class-8 claim holders include, among other things,
6 potential fraudulent-transfer or illegal-dividend claims surrounding the Abulafia Trust's
7 receipt of \$23.6 million in dividends in 1988; potential fraudulent-transfer claims sur-
8 rounding the transfer of certain lease benefits to Hayim and Julie Abulafia in 1999;
9 claims arising from the Abulafias' alleged interference with the administration of this es-
10 tate and public auction of World Bazaars' inventory in July 2000; and various equitable-
11 subordination claims. Class 9 (the WARN Act Claims) is deemed to reject the Plan be-
12 cause the Plan proposes to equitably subordinate or separately classify Class 9 claims.
13 Class 10 (Interests) is deemed to reject the Plan because holders of Class 10 interests
14 will receive or retain no value on account of those interests. As discussed in Section
15 III.B, below, the treatment of Classes 3, 8, 9, and 10 under the Plan complies with the
16 requirements of Bankruptcy Code section 1129(b), and the Plan may therefore be
17 crammed down on these Classes.

18 **III.**

19 **ARGUMENT**

20 **A. The Plan Should Be Confirmed Because It Complies With the**
21 **Requirements of Bankruptcy Code Section 1129(a).**

22 Bankruptcy Code section 1129(a) provides in substance that the Court
23 shall confirm a Chapter-11 plan if all elements of the statute's thirteen subsections are
24 satisfied.⁵ Each of these thirteen subsections and their application to World Bazaars'
25 Plan are discussed in detail below. As demonstrated in this discussion, the Plan satis-
26 fies all of the applicable statutory requirements of Section 1129(a) and therefore should

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28 ⁵ See 11 U.S.C. § 1129(a) ("The court shall confirm a plan only if all of the following
requirements are met . . .").

1 be confirmed.

2 1. **Section 1129(a)(1): The Plan Complies With**
3 **Applicable Provisions of the Bankruptcy Code.**

4 Bankruptcy Code section 1129(a)(1) requires that a plan "compl[y] with the
5 applicable provisions of [the Bankruptcy Code]."⁶ The legislative history of this section
6 indicates that it incorporates the requirements of Bankruptcy Code sections 1122 and
7 1123, which govern the classification of claims and interests and set forth the manda-
8 tory contents of a plan.⁷ Because, as demonstrated below, the Plan complies with both
9 sections 1122 and 1123 and with all other applicable provisions of the Bankruptcy
10 Code, the requirements of section 1129(a)(1) are satisfied here.

11 a. **The Plan Satisfies the Requirements of**
12 **Bankruptcy Code Section 1122.**

13 Bankruptcy Code section 1122 provides that "a plan may place a claim or
14 interest in a particular class only if such claim or interest is substantially similar to other
15 claims or interests of such class."⁸ By its plain language, Section 1122 prohibits only
16 the classification of dissimilar claims in the same class; it does not prohibit the separate
17 classification of similar claims.⁹ Moreover, case law has established that Bankruptcy
18 Courts have broad discretion to determine the propriety of classification schemes in light
19 of the facts of each case.¹⁰

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22 6 11 U.S.C. §1129(a)(1).

23 7 See H.R. Rep. No. 595, 95th Cong., 1st Sess. 412 (1977) ("Paragraph (1) requires
24 that the plan comply with the applicable provisions of chapter 11, such as sections
1122 and 1123, governing classification and contents of [the] plan.").

25 8 11 U.S.C. § 1122(a).

26 9 See 7 Collier on Bankruptcy at ¶ 1122.03[1][a] (15th ed. rev. 1999).

27 10 See *Steelcase Inc. v. Johnston (In re Johnston)*, 21 F.3d 323, 327 (9th Cir. 1994)
28 ("bankruptcy judges must have discretionary power in classifying claims under §
1122(a)").

(1) The Claims in Classified in Each Class Are Substantially Similar to One Another.

Section IV of the Plan classifies claims and interests into 10 different classes. Because each claim or interest that is classified in a particular class is substantially similar to the other claims or interests classified in that class, the Plan satisfies Section 1122. For example, secured claims are divided into the following four classes of substantially similar claims: Class 1 (the Bank Group's Secured Claims under the Credit Facility); Class 2 (the SKM Lenders' Secured Claims under the Term Loan); Class 3 (the Abulafia Trust's Secured Claims under the Term Loan); and Class 4 (Other Secured Claims). Priority claims are classified in Class 5 (Priority Claims). And general unsecured claims are classified in the following classes of substantially similar claims: Class 6 (General Unsecured Claims); Class 7 (the SKM Lenders' Unsecured Claims); Class 8 (the Abulafia Trust's Unsecured Claims); and Class 9 (the WARN Act Claims). All interests are separately classified in Class 10 (Interests).

(2) Substantially Dissimilar Claims Are Separately Classified.

Although not required by the Bankruptcy Code, each claim that is classified in a particular class is substantially *dissimilar* from those claims that are classified in other classes or its separate classification is otherwise permissible under the Bankruptcy Code. For example, priority claims are separately classified in Class 5, and interests are separately classified in Class 10.¹¹ Moreover, the secured claims classified in Class 1 (Bank Group's Secured Claims under the Credit Facility), Class 2 (the Abulafia Trust's Secured Claims under the Term Loan), Class 3 (the SKM Lenders' Secured Claims under the Term Loan), and Class 4 (Other Secured Claims) hold different priorities with respect to the relevant collateral, arise under different contracts or statutes.

¹¹ See 7 Collier on Bankruptcy, ¶ 1122.03[3] at 1122-7 (15th Ed. 1999) (noting that "a plan of reorganization must separately classify nonpriority prepetition unsecured claims, priority claims, secured claims, . . . and equity interests").

1 and have different rights to payment.¹² Similarly, the unsecured claims classified in
2 Class 6 (General Unsecured Claims), Classes 7 (the SKM Lenders' Unsecured Claims),
3 Class 8 (the Abulafias' Unsecured Claims), and Class 9 (the WARN Act Claims) also
4 have different statutory or contractual rights to payment or are of a different legal char-
5 acter.¹³ The separate classification of these claims is therefore appropriate.

6 The separate classification of the Class 2 and 3 and Class 7 and 8 claims
7 is also appropriate and well-supported by relevant law because World Bazaars has as-
8 sserted significant litigation against the different holders of these claims. Case law holds
9 that bankruptcy courts have broad latitude in approving the classification of claims¹⁴
10 and that the classification itself is not nearly as significant as the consequences of the
11 classification.¹⁵ For example, in *Steelcase v. Johnston*,¹⁶ the Ninth Circuit Court of Ap-
12 peals held that, where a creditor was embroiled in litigation with the debtor and, depend-
13 ing upon the result of that litigation, its claim against the debtor could be offset or could
14 be exceeded by the debtor's own claims, it was appropriate separately to classify the
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17 ¹² *Id.* at ¶ 1122.03[4][b] at 1122-13 ("Ordinarily each holder of an allowed claim se-
18 cured by a security interests in specific property of the debtor must be placed in a
separate class.") (citations omitted).

19 ¹³ *Id.* at ¶ 1122.03[4][a] at 1122-10 (noting that general unsecured claims "may be di-
20 vided into separate classes is separate classification is reasonable").

21 ¹⁴ See *Steelcase, Inc. v. Johnston (In re Johnston)*, 21 F.3d 323, 327 (9th Cir. 1994)
22 (recognizing that judges have discretionary power in classifying claims and that
Congress intended to give courts broad latitude in doing so) (citation omitted).

23 ¹⁵ *Bruce Energy Centre Ltd. v. ORFA Corp. of America (In re Orfa Corp.)*, 129 B.R.
24 404, 416 (Bankr. E.D. Penn. 1991) ("[T]he classification itself was not nearly so sig-
25 nificant as the consequence of disparate treatment of like or similar claims.") (citation
omitted); *accord In re Coventry Commons Assocs.*, 155 B.R. 446, 453 n.4 (E.D. Mi.
1993) ("Technically, the debtor's plan violates the requirement in § 1122 that only
similar claims can be classified together. This plan classifies Travelers' secured and
unsecured claims in the same class, and treats them identically. However, because
Travelers' unsecured claim will be paid in full with interest, the Court concludes that
this technical violation creates no actual prejudice to Travelers' substantive rights.")
(citation omitted).

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28 ¹⁶ *Steelcase*, 21 F.3d at 323.

1 creditors' claims.¹⁷

2 In this case, the secured claims of the SKM Lenders and the Abulafia
3 Trust under the Term Loan have been separately classified in Classes 2 and 3, respec-
4 tively, while the unsecured claims of the SKM Lenders and the Abulafias have been
5 separately classified in Classes 7 and 8. This separate classification is appropriate be-
6 cause—as discussed at length in Sections IV.C.1.b.(2) and (6) of the Disclosure State-
7 ment—World Bazaars has asserted different claims against the SKM Lenders and the
8 Abulafias and these claims may materially affect the treatment of the claims that the
9 SKM Lenders and the Abulafias have asserted against World Bazaars. As discussed in
10 Section IV.C.1.b.(2) of the Disclosure Statement, World Bazaars holds substantial
11 claims against the Abulafia Trust and other Abulafias, including among other things, po-
12 tential fraudulent-transfer or illegal-dividend claims surrounding the Abulafia Trust's re-
13 ceipt of \$23.6 million in dividends in 1998; potential fraudulent-transfer claims surround-
14 ing the transfer of certain lease benefits to Hayim and Julie Abulafia in 1999; and claims
15 arising from the Abulafias' alleged interference with the administration of this estate and
16 the public auction of World Bazaars' inventory in July 2000. These claims give rise to
17 offset rights, rights of equitable subordination, or counterclaims against the Abulafias.
18 The Creditors' Committee has conducted a significant investigation concerning these
19 claims, and it is currently engaged in prelitigation discovery in an effort to settle these
20 claims, if possible, or to prepare for litigation. Until these claims are resolved, World
21 Bazaars has reserved any rights that it may have with respect to the Abulafias' claims,
22 and it has proposed to escrow their distributions under the Plan.

23 As set forth in Section IV.C.1.b.(6) of the Disclosure Statement, it was also
24 suggested that World Bazaars may have had claims or causes of action against the
25 SKM Lenders. Until these claims could be resolved, the Plan similarly proposed to re-

27 ¹⁷ *Id.* at 328 ("Steelcase's separate classification under the Johnston plan does not vio-
28 late § 1122(a) because the legal character of its claim is *not* 'substantially similar to
the other claims or interests of such classes.'") (citations omitted).

1 serve World Bazaars rights against the SKM Lenders and to escrow any distributions on
2 account of their Class-2 or Class-7 claims. World Bazaars subsequently entered into a
3 settlement agreement, which has been approved by this Court, in which it resolved all
4 claims against the SKM Lenders. In essence, due to the different nature of the claims
5 against the SKM Lenders and the Abulafias, the Plan separately classified their claims
6 and enabled them to receive different treatment on account of those claims. Approval
7 of the settlement agreement with the SKM Lenders has caused their claims to be differ-
8 ently treated based upon the resolution of World Bazaars' claims. The separate classi-
9 fication of the various claims asserted by the SKM Lenders and the Abulafia Trust is
10 therefore reasonable and appropriate in this case.

b. The Plan Complies With the Required Provisions of Bankruptcy Code Section 1123(a).

(1) Section 1123(a)(1): The Plan Designates Classes of Claims and Interests.

²⁷ || ¹⁸ 11 U.S.C. § 1123(a).

28 || 19 11 U.S.C. § 1123(a)(1)

(2) Section 1123(a)(2): The Plan Identifies Unimpaired Classes.

Section 1123(a)(2) requires that a plan "specify any class of claims or interests that is not impaired under the plan."²⁰ Section IV of the Plan complies with section 1123(a)(2) by indicating that Classes 4 and 5 are not impaired.

(3) Section 1123(a)(3): The Plan Specifies the Treatment of Impaired Classes.

Bankruptcy Code section 1123(a)(3) requires that a plan "specify the treatment of any class of claims or interests that is impaired under the plan."²¹ Section IV of the Plan complies with section 1123(a)(2) by indicating that Classes 1, 2, 3, 6, 7, 8, 9, and 10 are impaired and by setting forth their treatment.

(4) **Section 1123(a)(4): The Plan**
Provides for the Same Treatment of Claims Within Each Class Except to the Extent That the Holder of the Claim Has Agreed to a Less Favorable Treatment.

Bankruptcy Code section 1123(a)(4) requires that a plan provide the same treatment for each claim or interest in a particular class unless the holder of the particular claim or interest agrees to a less favorable treatment.²² Section IV of the Plan satisfies Section 1123(a)(4) by providing the same treatment to each claim or interest that is classified in each a particular class established under the Plan except to the extent that the Bank Group has agreed to a less favorable treatment, as discussed below.

The Plan represents a compromise regarding the claims and liens of the Bank Group and, in connection with the compromise, the Bank Group has agreed to permit certain creditors with Allowed Claims in Classes 7 and 8 to receive enhanced recoveries in relation to the recoveries to be provided to the Bank Group on account of its

²⁰ 11 U.S.C. § 1123(a)(2).

²¹ 11 U.S.C. § 1123(a)(3).

22 11 U.S.C. § 1123(a)(4).

1 Allowed Class-7 Claims. By its vote to accept the Plan, the Bank Group has agreed to
2 receive this less favorable treatment. For example, although the Bank Group's Allowed
3 Class-7 Claim is estimated to comprise roughly 56% of Class-7 Claims, the Bank Group
4 will receive only 50% of the first \$500,000 of Net Insider Recoveries and other cash,
5 and any Net Avoidance Recoveries to which the Bank Group would otherwise have
6 been entitled will be distributed to Class-7 claimants other than the Bank Group.

(5) Section 1123(a)(5): The Plan Has Adequate Means for Implementation.

- Rejection of executory contracts and unexpired leases;
- Creation of the Continuing Estate and the vesting in the Continuing Estate of the Postconfirmation Litigation and any undistributed assets;
- Appointment of a Plan Administration Committee to supervise World Bazaars' postconfirmation affairs;
- Provisions for Post-Effective-Date Operating and Litigation Expenses to be incurred by the Continuing Estate and the Plan Administration Committee;
- Creation of an adequate source of funding for distributions under the Plan;
- Cancellation of existing stock, warrants, and options and issuing new securities; and
- Designation of procedures for making the distributions under the

²³ 11 U.S.C. § 1123(a)(5).

1 Plan and for appointing a Disbursing Agent, if needed.

2 (6) **Section 1123(a)(6): The Plan**
3 **Provides Appropriate Charters for**
4 **Reorganized IC.**

5 Section 1123(a)(6) requires that, with respect to a corporate debtor, a
6 Chapter-11 plan must provide for the inclusion in the reorganized debtor's charter of a
7 prohibition against the issuance of nonvoting equity securities and related protections
8 for holders of preferred shares.²⁴ Section IX.G. of the Plan satisfies and complies with
9 section 1123(a)(6) by providing that, on the Effective Date, all Interests will be can-
10 celed, annulled, and extinguished. Simultaneously, the Continuing Estate will be
11 deemed to issue one share of new common stock, which will be held by the Plan Ad-
12 ministration Committee until this case has been closed, at which time the new share of
13 stock will automatically be cancelled without any further action. In addition, World Ba-
14 zaars' corporate charter will be deemed amended to prohibit the issuance of nonvoting
securities.

15 (7) **Section 1123(a)(7): The Plan Pro-**
16 **vides for the Selection of Postcon-**
17 **firmation Management.**

18 Finally, section 1123(a)(7) provides that a plan must "contain only provi-
19 sions that are consistent with the interests of creditors and equity security holders and
20 with public policy with respect to the manner of selection of any officer, director, or trus-
21 tee under the plan and any successor to such officer, director, or trustee."²⁵ Section
22 VI.B. of the Plan complies with section 1123(a)(7) by identifying the persons who will
23 serve as the initial members of the Plan Administration Committee and by indicating the
24 conditions under which new members may be selected.

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28 ²⁴ 11 U.S.C. § 1123(a)(6).
²⁵ 11 U.S.C. § 1123(a)(7).

c. The Plan Includes Permissive Provisions Authorized by Bankruptcy Code Section 1123(b).

Bankruptcy Code section 1123(b) sets forth several provisions that may, but need not, be included within a Chapter-11 plan.²⁶ For example, a Chapter-11 plan may provide for the rejection of any executory contract or unexpired lease;²⁷ the settlement of any claim belonging to the debtor;²⁸ or the retention by an appointed representative of the estate of any claim belonging to the debtor.²⁹ A Chapter-11 plan may also include "any other appropriate provision not inconsistent with the applicable provisions of [the Bankruptcy Code]."³⁰

2. Section 1129(a)(2): The Debtors Have Complied With All Applicable Provisions of the Bankruptcy Code.

Bankruptcy Code section 1129(a)(2) requires that the proponent of a Chapter-11 plan comply with the applicable provisions of the Bankruptcy Code.³¹ The principal purpose of Section 1129(a)(2) is to ensure that a proponent complies with the Bankruptcy Code's requirements regarding the solicitation of plan acceptances.³² In its Solicitation Order, the Court found that the Disclosure Statement contains adequate information within the meaning of Bankruptcy Code section 1125(b), and the Court authorized World Bazaars to disseminate the Plan and related solicitation materials to parties in interest and to solicit votes under certain specified procedures. World Bazaars

26 11 U.S.C. § 1123(b).

²⁷ 11 U.S.C. § 1123(b)(2).

²⁸ 11 U.S.C. § 1123(b)(3)(A).

²⁹ 11 U.S.C. § 1123(b)(3)(B)

30 11 U.S.C. § 1123(h)(6)

31 11 U.S.C. § 1129(a)(2)

³² See *In re Texaco Inc.* 84 B.R. 893, 906-07 (Bankr. S.D.N.Y. 1988).

1 has previously filed Declarations of Service³³ demonstrating that World Bazaars, its pro-
2 fessionals, and its agents have complied with all of the procedures set forth in the Solici-
3 tation Order and with all other applicable provisions of the Bankruptcy Code and Bank-
4 ruptcy Rules. The requirements of Section 1129(a)(2) have therefore been satisfied.

3. Section 1129(a)(3): World Bazaars Has Proposed the Plan in Good Faith.

Bankruptcy Code section 1129(a)(3) requires that a Chapter-11 plan be "proposed in good faith and not by any means forbidden by law."³⁴ Bankruptcy Rule 3020(b)(2) provides that: "If no objection is timely filed, the court may determine that the plan has been proposed in good faith and not by means forbidden by law without receiving evidence on such issues."³⁵ Barring any objection to the Plan on the grounds of a lack of good faith, the Court therefore should find that the requirements of section 1129(a)(3) are satisfied.

Even absent Rule 3020(b)(2)'s presumption of good faith, World Bazaars' good faith in this case is evident. World Bazaars filed its Chapter-11 petition to liquidate its assets and wind down its affairs as rapidly and efficiently as possible. At all times, the objective of World Bazaars' efforts has been to provide for the orderly distribution of its assets so that value is fairly distributed among its respective creditors in accordance with applicable law. This objective is consistent with the objectives and purposes of the Bankruptcy Code.³⁶ As the record reflects, World Bazaars has successfully liquidated

22 ³³ See World Bazaars' *Submission of Proof of Service of Solicitation Materials and its*
23 *Affidavit of Publication re "Notice of Hearing on Second Amended Chapter-11 Plan*
Proposed by World Bazaars, Inc. (Dated November 10, 2000), both of which were
filed with this Court on or about January 17, 2001.

24 ||³⁴ 11 U.S.C. § 1129(a)(3).

²⁵ ³⁵ Fed. R. Bankr. P. 3020(b)(2).

26 36 See *In re Coastal Equities, Inc.*, 33 B.R. 898 (Bankr. S.D. Cal. 1983) (finding that
27 debtor's liquidation plan was proposed in good faith because a Chapter-11 liquidation
28 is consistent with the objectives and purposes of the Bankruptcy Code in general and Section 1123(b)(4) in particular, which authorizes the sale of substantially all of a debtor's assets and the distribution of the sale proceeds).

1 substantially all of its assets. The Plan—which provides for the orderly distribution of
2 the liquidation proceeds—is the culmination of many months of constructive, good-faith
3 negotiations that have been conducted at arms' length among the major constituencies
4 in this case. Creditor support for the Plan is a strong indication that the Plan has
5 achieved its intended objectives and that the Plan is fair and equitable to creditors.
6 Thus, there can be no serious question that the Plan satisfies the good faith require-
7 ment of Section 1129(a)(3).

8 **4. Section 1129(a)(4): The Plan Provides for Court**
9 **Approval of All Payments for Services Rendered**
 in Connection with the Case.

10 Bankruptcy Code section 1129(a)(4) requires that payments "for services
11 or for costs and expenses in or in connection with the case, or in connection with the
12 plan and incident to the case," be approved by the Court as reasonable.³⁷ In other
13 words, Section 1129(a)(4) requires that any and all payments made for non-ordinary
14 course expenses of administration be subject to court review and approval.³⁸ Section
15 IV.A. of the Plan provides that the Continuing Estate will not pay Non-Ordinary Course
16 Administrative Claims or Professional-Fee Claims unless and until the Court allows
17 such claims. The Plan therefore complies with Section 1129(a)(4).

18 **5. Section 1129(a)(5): The Plan Discloses the**
19 **Identity of Postconfirmation Management.**

20 Bankruptcy Code section 1129(a)(5) requires that: (a) the proponent of a
21 plan disclose the identity of any individual proposed to serve after confirmation as a di-
22 rector, officer, or voting trustee of the reorganized debtor; (b) the appointment of such

23
24 ³⁷ 11 U.S.C. § 1129(a)(4).

25 ³⁸ *In re Resorts, Int'l, Inc.*, 145 B.R. 412, 475-76 (Bankr. D.N.J. 1990); see also *In re*
26 *Elsinore Shore Assocs.*, 91 B.R. 238, 268 (Bankr. D.N.J. 1988) (the requirements of
27 section 1129(a)(4) are satisfied where a plan provides for payment of "allowed" ad-
28 ministrative expenses). *But see In re Future Energy Corp.*, 83 B.R. 470, 488 (Bankr.
S.D. Ohio 1988) ("Court approval of payments for services and expenses are gov-
erned by various Code provisions—e.g., §§ 328, 329, 330, 331 and 503(b)—and
need not be explicitly provided for in a chapter 11 plan.").

1 individuals be consistent with the interests of creditors and shareholders and with public
2 policy; and (c) the proponent disclose the nature of any insider that will be employed by
3 the reorganized debtor and the nature of the compensation to be provided to that in-
4 sider.

5 Section VI.B. of the Plan sets forth the identity and qualifications of the
6 proposed members of the Plan Administration Committee on the Effective Date, and as
7 is disclosed in Section VI.B.1., the committee members will receive no compensation for
8 their services. Specifically, the Plan Administration Committee will consist of the Bank
9 Group Agent and Richard Havel, as counsel for the Creditors' Committee. The Bank
10 Group Agent and the Creditors' Committee have been extensively involved in the ad-
11 ministration of this case and the formulation of World Bazaars' Plan. Moreover, the
12 Bank Group and the Creditors' Committee hold the vast majority of the claims to be sat-
13 isfied through the prosecution of Postconfirmation Litigation. The appointment of the
14 Bank Group Agent and Richard Havel as the members of the Plan Administration
15 Committee will therefore provide continuity to World Bazaars' liquidation and will appro-
16 priately align postconfirmation management with the economic interests of World Ba-
17 zaars' creditors. Their appointment is therefore in the best interests of creditors and is
18 consistent with public policy.

19 6. **Section 1129(a)(6): World Bazaars Is Not Subject**
20 **to Public Regulation.**

21 Bankruptcy Code section 1129(a)(6) requires that any regulatory commis-
22 sion with jurisdiction over the rates of a debtor approve any rate changes provided in a
23 Chapter-11 plan.³⁹ World Bazaars is not subject to public regulation and Section
24 1129(a)(6) is therefore inapplicable.

25 7. **Section 1129(a)(7): The Plan Is in the Best Inter-**
26 **ests of Creditors.**

27 Bankruptcy Code section 1129(a)(7) establishes what is commonly re-

28 ³⁹ 11 U.S.C. § 1129(a)(6).

1 referred to as the "best-interests test." Specifically, section 1129(a)(7) requires that, with
2 respect to each class of impaired claims or interests under a plan, every holder of a
3 claim or interest in such impaired class either: (a) accept the plan; or (b) receive or re-
4 tain property of a value, as of the Plan's effective date, that is not less than the amount
5 that the claim holder would receive or retain if the debtor were liquidated under Chapter
6 7 of the Bankruptcy Code.⁴⁰

7 The requirements of Section 1129(a)(7) are satisfied with respect to
8 Classes 4 and 5 because they are not impaired under the Plan. The requirements of
9 Section 1129(a)(7) are also satisfied with respect to Class 1 because all of the creditors
10 in that class have voted to accept the Plan. (Classes 2 and 8 have not yet voted, but
11 they have previously agreed to support or not oppose the Plan)

12 With respect to Class 6, the Ballot Tabulation demonstrates that a suffi-
13 cient number of creditors, both in number and amount, that hold claims in Class 6 have
14 voted to accept the Plan such that Class 6 has, as a class, voted to accept the Plan.
15 With respect to those creditors who hold claims in Class 6 and who have voted to reject
16 the Plan as well as creditors in Classes 3, 8, 9, and 10, all of whom are deemed to re-
17 ject the Plan, the requirements of Section 1129(a)(7) also are satisfied. As explained in
18 Section VII.C. of the Disclosure Statement and in the Budetti Declaration, World Ba-
19 zaars has prepared a liquidation analysis demonstrating that, in a hypothetical Chapter-
20 7 liquidation, any distribution available to these creditors would be equal to or less than
21 their distributions under the Plan and that, under either the Plan or a Chapter-7 liquida-
22 tion, there would likely be no distribution available for equity interests. Thus, under the
23 Plan, the distributions provided to dissenting impaired creditors are expected to be
24 equal to or greater than the distributions that these entities would receive if World Ba-
25 zaars was liquidated in a Chapter 7, and the requirements of Section 1129(a)(7) are
26 therefore satisfied.

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⁴⁰ 11 U.S.C. § 1129(a)(7).

1 **8. Section 1129(a)(8): The Plan Has Been Accepted**
2 by All Impaired Classes Entitled to Vote.

3 Except as otherwise set forth in Bankruptcy Code section 1129(b)'s cram
4 down provisions, Bankruptcy Code section 1129(a)(8) requires that each class of claims
5 and interests established under a Chapter-11 plan either accepts the plan or is not im-
6 paired under the plan.⁴¹ A class of claims accepts a plan if holders of at least two-third
7 in dollar amount and a majority in number of claims in that class vote to accept the plan,
8 counting only those claims whose holders actually vote.⁴² A class of claims or interests
9 that is not impaired is deemed to accept the plan.⁴³ A class of claims or interests that
10 does not receive or retain any property under the plan is deemed to reject the plan.⁴⁴

11 Classes 4 and 5 are not impaired under the Plan and are therefore
12 deemed to accept the Plan. As set forth in the Ballot Tabulation and summarized in
13 Section II, above, Classes 1 and 6 are impaired under the Plan and have voted in requi-
14 site amounts and numbers to accept the Plan. (Classes 2 and 7 have not yet voted, but
15 they have indicted that they support or do not oppose the Plan. Moreover, as set forth
16 below, the Plan has been modified to delete Classes 2 and 7 from the Plan.)

17 The remaining classes, Classes 3, 8, 9, and 10, are deemed to reject the
18 Plan under Bankruptcy Code section 1126(g). However, as set forth in Section B, be-
19 low, the Plan nevertheless may be crammed down on these classes under Bankruptcy
20 Code section 1129(b) and should be confirmed.

21 **9. Section 1129(a)(9): The Plan Complies With the**
22 Required Treatment of Administrative Claims and
23 Priority Claims.

24 Bankruptcy Code section 1129(a)(9) requires that, unless the holder of a

25 ⁴¹ 11 U.S.C. § 1129(a)(8).

26 ⁴² 11 U.S.C. § 1126(c); *see also* 11 U.S.C. § 1126(d) (governing classes of interests).

27 ⁴³ 11 U.S.C. § 1126(f); 11 U.S.C. § 1129(a)(8).

28 ⁴⁴ 11 U.S.C. § 1126(g).

1 claim agrees to a different treatment: (a) the holder of a claim entitled to priority under
2 Section 507(a)(1) or (2) must receive on the plan's effective date cash in the allowed
3 amount of its claim; (b) the holder of a claim entitled to priority under Section 507(a)(3),
4 (4), (5), (6), or (7) must receive either cash in the allowed amount of its claim on the
5 plan's effective date or deferred cash payments of a value, as of the effective date,
6 equal to the allowed amount of its claim; and (c) the holder of a tax claim entitled to pri-
7 ority under Section 507(a)(8) must receive on account of its claim deferred cash pay-
8 ments, over a period not exceeding six years after the date of assessment of its claim,
9 equal to the allowed amount of such claim on the plan's effective date.⁴⁵

10 The Plan satisfies the requirements of Section 1129(a)(9). First, as re-
11 quired by section 1129(a)(9)(A), Section IV.A.1. of the Plan provides that, unless agreed
12 otherwise, Allowed Administrative Claims will be paid in cash, in the full amount, without
13 interest, on or before the later of: (a) as soon as practicable after the Effective Date, (b)
14 30 days after the date on which the Administrative Claim becomes an Allowed Adminis-
15 trative Claim; or (c) the date on which the Allowed Administrative Claim becomes due
16 and payable.

17 Second, as required by section 1129(a)(9)(B), Section IV.C. of the Plan
18 provides that, unless agreed otherwise, Allowed Priority Claims—other than Allowed
19 Priority Tax Claims—will be paid in cash equal to the allowed amount of the claims,
20 without interest, as soon as practicable after the Effective Date.

21 Third, Section IV.A. 2. of the Plan provides that, unless agreed otherwise,
22 holders of Allowed Priority Tax Claims will be paid in full, in cash—without premium or
23 penalty of any kind—as soon as practicable after the Effective Date. This treatment is
24 more favorable than the treatment required under Section 1129(a)(9)(c), which permits
25 deferred payment over a period of up to six years.

26
27
28 ⁴⁵ See 11 U.S.C. § 1129(a)(9).

10. Section 1129(a)(10): More Than One Impaired Class of Claims Has Voted to Accept the Plan.

Bankruptcy Code section 1129(a)(10) requires that at least one class of claims that is impaired under a Chapter-11 plan has voted to accept the plan, determined without including any acceptance by an insider.⁴⁶ As noted in the Ballot Tabulation and in Section II, above, each of the four impaired classes that is entitled to vote on the Plan has accepted the Plan. Excluding the acceptances of insiders, there are two impaired, accepting classes: Classes 1 and 6. Thus, the Plan satisfies the requirements of Section 1129(a)(10).

11. **Section 1129(a)(11): The Plan Is Feasible.**

Bankruptcy Code section 1129(a)(11), which establishes the so-called "feasibility" standard, requires that the Court determine that "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation . . . is proposed in the plan."⁴⁷ Section 1129(a)(11) does not require an absolute assurance of financial success by the debtor. Rather, the feasibility standard requires only "a 'reasonable' prospect for financial stability and success."⁴⁸

As indicated in the Budetti Declaration, World Bazaars has the financial means to satisfy all of its Effective Date and postconfirmation obligations under the Plan. Under the Plan, World Bazaars is required, on the Effective Date, to make certain one-time payments to holders of Allowed Administrative and Priority Claims. World Ba-

⁴⁶ 11 U.S.C. § 1129(a)(10).

47 11 U.S.C. § 1129(a)(11).

⁴⁸ *In re Sound Radio, Inc.*, 103 B.R. 521, 524 (D.N.J. 1989), *aff'd*, 908 F.2d 964 (3d Cir. 1990); *accord Kane v. Johns-Manville Corp.* (*In re Johns-Manville Corp.*), 843 F.2d 636 at 649 (2^d Cir. 1988) ("[T]he feasibility standard is whether the plan offers a reasonable assurance of success. Success need not be guaranteed."); *In re Orlando Investors, L.P.*, 103 B.R. 593, 600 (Bankr. E.D. Pa. 1989) ("The purpose behind the statutory requirement of feasibility is to prevent confirmation of visionary schemes which promise creditors and equity security holders more under a proposed plan than the debtor can possibly attain after confirmation.") (quotations omitted).

1 zaars estimates that all of these obligations should not exceed, in the aggregate, \$630
2 million. The Effective Date cash obligations are summarized as follows:

3 **ESTIMATED EFFECTIVE DATE CASH OBLIGATIONS**

5	<i>General Priority Claims</i>	\$20,000
6	<i>WARN Act Claims</i>	<u>\$130,000</u>
7	Total Priority Claims	\$150,000
8	<i>Ordinary Course Administrative Claims</i>	\$0
10	<i>Non-Ordinary Course Administrative Claims (Disputed)</i>	\$60,000
11	<i>Professional-Fee Claims</i>	\$350,000
12	<i>Administrative Tax Claims</i>	<u>\$0</u>
13	Total Administrative Claims	\$420,000
14	Total Administrative & Priority Claims	\$570,000

16 In addition, as set forth in the Operating Budget attached to the Disclosure Statement,
17 World Bazaars anticipates that roughly \$70,000 will be needed to fund the Continuing
18 Estate's postconfirmation operations.

19 World Bazaars is currently holding approximately \$250,000 in free and
20 clear cash assets. In addition, this Court previously approved a settlement agreement
21 under which the Bank Group has agreed to permit World Bazaars to use up to \$500,000
22 of the Bank Group's cash collateral to satisfy any shortfall in meeting Effective Date or
23 postconfirmation expenses. Thus, in total, World Bazaars has roughly \$750,000 avail-
24 able to satisfy up to \$640,000 in Effective Date and postconfirmation expenses. These
25 available funds are more than sufficient to permit World Bazaars to meet its Effective
26 Date obligations under the Plan, and World Bazaars' projections indicate that these
27 funds should also be more than sufficient to ensure that the Continuing Estate has
28

1 enough cash over the life of the Plan to meet anticipated postconfirmation obligations.
2 Thus, as required under Section 1129(a)(11), confirmation of the Plan is not likely to be
3 followed by any further liquidation of this Estate except as contemplated under the Plan
4 itself.

5 **12. Section 1129(a)(12): The Plan Provides for Full**
6 **Payment of All Fees Payable Under 28 U.S.C. §**
7 **1930.**

8 Section 1129(a)(12) requires that a Chapter-11 plan provide that all fees
9 payable under 28 U.S.C. § 1930 (which consist primarily of the quarterly fee owing to
10 the U.S. Trustee) be paid on or before the plan's effective date. Section IV.A.1 of the
11 Plan provides for payment in full of all Allowed Administrative Claims, including all Al-
12 lowed Ordinary-Course Administrative Claims, on or before the later of: (a) as soon as
13 practicable after the Effective Date; (b) 30 days after the date on which the Administra-
14 tive Claim becomes an Allowed Administrative Claim; or (c) the date on which the Al-
15 lowed Administrative Claim becomes due and payable. Section I of the Plan, in turn,
16 defines Allowed Ordinary Course Administrative Claims to include fees or charges as-
17 sessed against the Estate under 28 U.S.C. § 1930. Thus, the Plan satisfies the re-
18 quirements of Section 1129(a)(12).

19 **13. Section 1129(a)(13) Is Inapplicable.**

20 Bankruptcy Code section 1129(a)(13) requires that a Chapter-11 plan pro-
21 vide for the continuation of all retiree benefits, as defined in Bankruptcy Code section
22 1114.⁴⁹ As set forth in the Budetti Declaration, World Bazaars does not believe that any
23 such retiree benefits exist. Section 1129(a)(13) is therefore inapplicable in this case.

24 **B. The Plan Should Be Confirmed Because Those Classes That**
25 **Are Deemed to Have Rejected the Plan May Be Crammed**
26 **Down Under Bankruptcy Code Section 1129(b).**

27 Bankruptcy Code section 1129(b) provides that if a Chapter-11 plan has
28 satisfied all confirmation requirements except Section 1129(a)(8)'s requirement that all

28 ⁴⁹ 11 U.S.C. § 1129(a)(13).

1 impaired classes accept the plan, the court nevertheless "shall confirm the plan notwithstanding
2 the requirements of [Section 1129(a)(8)] if the plan does not discriminate unfairly,
3 and is fair and equitable, with respect to each class of claims or interests that is
4 impaired under, and has not accepted, the plan."⁵⁰ The only classes that have rejected
5 or are deemed to have rejected the Plan are Classes 3, 8, 9, and 10, and as discussed
6 below, the requirements of Section 1129(b) are satisfied with respect to these classes.
7 The Court should therefore confirm the Plan notwithstanding its failure to comply with
8 Bankruptcy Code section 1129(a)(8).

9 **1. The Class-3 and Class-8 Escrow Provisions.**

10 As alluded to in Section A.1.a(2), above, the Plan proposes to place all
11 distributions to the Abulafias on account of their Class-3 or Class-8 claims into an interest-bearing
12 escrow account pending resolution of numerous claims against these former insiders.
13 Specifically, Sections I and IV.B.3 of the Plan provide, in substance, that
14 all distributions on account of Class 3 claims (the Abulafia Trust's Claims Under the
15 Term Loan) will be placed into a segregated, interest-bearing escrow account to be
16 maintained by the Estate pending the resolution of certain, significant claims that World
17 Bazaars may have against the Abulafias. If, in connection with prosecution of those
18 claims, this Court enters a Final Order authorizing distributions to the Abulafia Trust to
19 be transferred to the Estate, then all funds in the interest-bearing escrow account will be
20 transferred to World Bazaars' Operating Account. However, if the Estate's claims are
21 ultimately determined by this Court to be invalid, then the funds in the interest-bearing
22 escrow account will be distributed to the Abulafia Trust under the Plan:

23 Class 3 will receive, as soon as practicable after the Effective Date, 30.8% of the Net Equipment Proceeds (subject to
24 the Estate's right to assert equitable subordination claims or any other claims). However, all distributions under the Plan
25 on account of the Abulafia Trust's allowed Class-3 Claims will be placed into the Abulafia Escrow Account pending
26 resolution of all Insider Litigation against the Abulafias and any other claims that World Bazaars or the Estate may have

27
28 ⁵⁰ 11 U.S.C. § 1129(b)(1).

against the Abulafias. On or before the Final Distribution Date, the funds in the Abulafia Escrow Account will either be transferred to the Operating Account for the benefit of the Estate in accordance with a Final Order or they will be distributed to the Abulafias.⁵¹

Similarly, Sections I and IV.F of the Plan provide that the Abulafias will receive on account of their Class 8 claims (the Abulafias' Unsecured Claims) the same treatment to be provided to Class 7 claimants on account of their general unsecured claims but that any distributions on account of Class 8 claims will be placed into an interest-bearing escrow account on substantially the same terms and conditions as are established for the Class-3 claims.⁵²

- a. **Under Bankruptcy Code Section 502(d), the Debtor May Withhold Distributions on Account of Any Claim Asserted by an Entity That Has Received a Fraudulent Transfer or Whose Claims Are Subject to Offset.**

As the Abulafias themselves have conceded, a Bankruptcy court may delay distributions on disputed claims pending resolution of claims litigation:

Courts sometimes permit Chapter 11 debtors on equitable grounds to delay making plan distributions on disputed claims pending resolution of the claims litigation where the debtor reserves for the disputed claims . . .⁵³

Notwithstanding this acknowledgement, and without citing to any case or Bankruptcy Code authority, the Abulafias contend that the withholding of distributions as to the Abulafias' Class-3 claim is somehow improper here, because the estate has acknowledged the validity of the Abulafias' lien. In substance, the Abulafias contend that the Court must ignore the mountain of claims and counterclaims asserted by the Estate against the Abulafias and require the Estate to satisfy the Abulafias' secured claim before these

⁵¹ See Plan at Section IV.B.3.

⁵² See Plan at Section IV.H.

⁵³ See *Objection of Abulafia to Confirmation of the Debtor's Second Amended Chapter 11 Plan Proposed by World Bazaars, Inc. (Dated November 10, 2000)* (the "Abulafia Objection") at 3:5-11.

1 claims and counterclaims are resolved. This contention is wrong.

2 As established below, both the Bankruptcy Code and case law plainly es-
3 tablish that withholding distributions with respect to an otherwise valid lien or claim is
4 not only appropriate but mandatory where, as here, the holder of that lien or claim is
5 subject to claims and counterclaims asserted by the estate. The theory underpinning
6 this doctrine is that a debtor should not be forced to make payments on claims that may
7 not be valid. Under Bankruptcy Code section 502(d), a debtor may withhold distribu-
8 tions on account of any claim asserted by an entity that, among other things, has re-
9 ceived a fraudulent transfer or whose claims are subject to offset:

10 [T]he court shall disallow any claim or any entity from which
11 property is recoverable under section 542, 543, 550, or 553
12 of this title or that is a transferee of a transfer avoidable un-
13 der section 522(f), 522(h), 545, 547, 548, 549, or 724(a) of
14 this title, unless such entity or transferee has paid the
15 amount, or turned over any such property, for which such
16 entity or transferee is liable under section 522(i), 542, 543,
17 550, or 553 of this title.⁵⁴

18 The principal purpose of Section 502(d) is to ensure that estate assets are distributed
19 *pro rata* among all legitimate creditors and that those creditors who have received void-
20 able transfers to the detriment of others cannot further deplete estate assets. Section
21 502(d) also serves as a coercive mechanism to assist a debtor in enforcing judgments
22 that it may obtain against the beneficiaries of these voidable transfers.⁵⁵ It is well estab-
23 lished that, to invoke Section 502(d), a debtor need only allege that the holder of a claim
24 has received a voidable transfer.⁵⁶ The debtor need not actually receive an avoidance

25 ⁵⁴ 11 U.S.C. § 502(d) (emphasis added).

26 ⁵⁵ See *Committee of Unsecured Creditors v. Commodity Credit Corp. (In re KF Dairies, Inc.)*, 143 B.R. 734, 735-36 (B.A.P. 9th Cir. 1992) ("The Act evidences a natural de-
27 sire to restore the equality of a distribution disturbed by the illicit preference.") (cita-
28 tion omitted); see also 7 Collier on Bankruptcy, ¶ 502.05[2][a] at 502-56 (15th Ed.
1999).

⁵⁶ See 7 Collier on Bankruptcy, ¶ 502.05[2][a] at 502-56 (15th Ed. 1999) ("[A] claim may
be disallowed at least temporarily and for certain purposes, subject to reconsidera-
tion, simply upon the allegation of an avoidable transfer.").

1 judgment; in fact, Section 502(d) may be asserted as an affirmative defense to a claim
2 even if the underlying avoidance action is time-barred or otherwise nonrecoverable. For
3 example, in *KF Dairies* a creditor received postpetition transfers that were avoidable
4 under Section 549, but no actions under that section were ever commenced. After the
5 bar-date for asserting the Section 549 avoidance actions had passed, the estate in-
6 voked Section 502(d) to object to other claims asserted by the recipient of the postpeti-
7 tion transfers.⁵⁷ The Bankruptcy Appellate Panel for the Ninth Circuit Court of Appeals
8 held that Section 502(d) was properly invoked to disallow the claims even though the
9 Section 549 avoidance action had never been, and in fact could not be, commenced
10 against the creditor.⁵⁸ This reasoning was recently adopted by the Ninth Circuit Court of
11 Appeals in *El Paso v. American Airlines*.⁵⁹

12 Similarly, relevant case law establishes that a Bankruptcy Court may ap-
13 prove plan provisions that permit a debtor to exercise setoff rights against payments
14 that would otherwise be made under the Plan and that the Court may authorize the
15 debtor to withhold payment to an entity holding an otherwise allowable claim pending a
16 determination of those setoff rights. For example, in *Walnut Equipment Leasing*,⁶⁰ the
17 Bankruptcy Court approved a Chapter-11 plan that permitted the debtor to setoff against
18 any payments to be made under the Plan any claims that the debtor might have against
19 the claimant.⁶¹ After plan confirmation, the debtor commenced an action against its offi-
20 cers and directors in which it asserted, among other things, that it was entitled to setoff
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22 ⁵⁷ See *Id.* at 734.
23

24 ⁵⁸ *Id.* at 736-37.
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26 ⁵⁹ *El Paso v. America West Airlines, Inc. (In re American West Airlines, Inc.)*, 217 F.3d
27 1161, 1167 (9th Cir. 2000) (adopting reasoning of *KF Dairies* and holding that 502(d)
28 may be invoked to disallow a claim where the creditor received an avoidable transfer
under Section 546 even where that avoidance action was now time barred).

⁶⁰ *Walnut Equipment Leasing Co.*, 2000 Bank. LEXIS 1401 (Bankr. E.D. Pa. 2000).

⁶¹ *Id.* at *8.

1 any judgment against what it conceded to be otherwise valid claims of these officers
2 and directors. Pending the resolution of that litigation and the related setoff issues, the
3 Bankruptcy Court authorized the debtor to withhold distributions to the officer and direc-
4 tor claimants.⁶²

5 Finally, in closely analogous circumstances, courts applying Bankruptcy
6 Code section 363(f)(4) governing the treatment of liens subject to *bona fide* disputes
7 have held that it is not necessary that a lien be the subject of a pending adversary pro-
8 ceeding or other formal action; the court need only determine that there is an objective
9 basis for either a factual or legal dispute.⁶³ Under the standard, a court "need not de-
10 termine the probable outcome of the dispute, but merely whether one exists." The
11 same is true here.

12 Although World Bazaars has previously acknowledged that the Abulafia
13 Trust's Class 3 claims are subject to valid, duly perfected and non-voidable first liens on
14 and security interests against certain collateral, there are a multitude of significant
15 claims against the Abulafias—which have been estimated at up to \$23 million—all of
16 which trigger the withholding of distributions on the Abulafias' claims under Section
17 502(d). And, notwithstanding its acknowledgment of the validity of the liens securing
18 the Class 3 claims, World Bazaars has—in every relevant settlement agreement pre-
19 sented to this Court, including the very agreement relied upon by the Abulafias—
20 consistently preserved all of its potential claims against the Abulafias.⁶⁴ These claims

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22 ⁶² *Id.* at *10; see also *In re Cumberland Farms, Inc.*, 249 B.R. 341 (Bankr. D. Mass
23 2000) (holding that the existence of valid setoff rights against a claimant constitute a
24 sufficient basis to disallow that claimant's otherwise allowable claims against the
debtor).

25 ⁶³ See, e.g., *In re Collins*, 180 B.R. 447, 452 (Bankr. E.D. Va. 1995); *In re Octagon
Roofing*, 123 B.R. at 590.

26 ⁶⁴ See, e.g., Paragraph 4(a) of the *Settlement Agreement* dated December 15, 2000, a
27 true and correct copy of which is attached to the Abulafia Objection as Exhibit 1
28 ("This release does not apply to . . . any claims of World Bazaars against Hayim
Abulafia or the Abulafia Trust, or any person or party related thereto . . . , including,
without limitation, any claims of setoff against distributions payable to the Abulafia
Trust on account of its claims as Equipment Lender.").

1 are set forth at length in Section IV.C.1.b.(2) of Disclosure Statement and in numerous
2 declarations that have been filed in this case. For convenience, some of these claims
3 are summarized below:

- 4 • In 1998, the Abulafia Trust received approximately \$23.6 million in
5 so-called "dividends" for which the Estate did not receive reasona-
6 bly equivalent value. These transfers may have rendered the com-
7 pany insolvent or inadequately capitalized, and the company could
8 not pay these "dividends" from either current earnings or surplus
9 assets. As such, the transfers may constitute avoidable fraudulent
10 transfers or illegal dividends;
- 11 • In 1994, World Bazaars entered into a commercial real-estate lease
12 with Hayim and Julie Abulafia. In August 1998, the Abulafias
13 caused World Bazaars to amend that lease so that, in essence, the
14 Abulafias received additional rent payments of \$35,000 per month,
15 or an additional \$337,500 during the nine months before the Peti-
16 tion Date. World Bazaars does not appear to have received any
17 value in exchange for this agreement.
- 18 • During the one year before the Petition Date, Hayim Abulafia re-
19 ceived from World Bazaars approximately \$71,000 in cash pay-
20 ments in excess of his salary.
- 21 • The Abulafias are also parties an outstanding account receivable
22 for \$95,000 and an outstanding \$112,000 note payable.

23 These claims include several actions against the Abulafias for fraudulent transfers that
24 may be avoidable and recoverable under Section 550. Thus, these claims fall directly
25 within the ambit of Section 502(d) and provide a clear basis for withholding distributions
26 on any of the Abulafias' claims. These claims also give rise to substantial offset rights,
27 rights of equitable subordination, or counterclaims against the Abulafias. Through op-
28 eration of Section 553, these claims, too, provide a basis for withholding distributions

1 under Section 502(d). Moreover, some of the relief to which World Bazaars might be
2 entitled, such as its rights to equitably subordinate the Abulafias' claims, could be ren-
3 dered meaningless if this Court does not briefly escrow distributions to the Abulafias un-
4 til such time as it can fully consider the merits of World Bazaars' claims.

5 As discussed above, World Bazaars need only allege that the Abulafias
6 have received avoidable transfers to come within Section 502(d). These allegations
7 have been disclosed in numerous declarations and pleadings filed during the course of
8 this case, and they have been discussed at length in the Disclosure Statement. In addi-
9 tion, the accompanying Declarations of Martin Barrett and James Goldman establish a
10 clear evidentiary basis for these allegations. Although, due in part to the complexity and
11 sheer volume of the claims against the Abulafias, World Bazaars has not previously
12 been able to prepare its complaint, its claims are not merely speculative. The Bank
13 Group has already agreed to provide a substantial, \$150,000 retainer to special litiga-
14 tion counsel to fund the prosecution of these claims. Moreover, concurrently with this
15 Memorandum, World Bazaars has submitted to the U.S. Trustee an application seeking
16 to employ special litigation counsel to pursue the Estate's claims against the Abulafias,
17 and World Bazaars anticipates that its special litigation counsel will file a complaint
18 against the Abulafias promptly after approval of the employment application. Under the
19 circumstances, the Plan's escrow provisions are clearly authorized under Section
20 502(d). In fact, under Section 502(d), the Plan could provide that the Abulafias will re-
21 ceive no distribution whatsoever. The Plan has actually provided the Abulafias with
22 more favorable treatment by providing only that the Abulafias' distributions will be
23 placed into an interest-bearing escrow account pending resolution of the Estate's claims
24 against the Abulafias.

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28

b. The Escrow Provisions May Be Crammed Down on the Class 3 and Class 8 Claimants Under Bankruptcy Code Section 1129(b).

(1) The Plan Does Not Unfairly Discriminate Against Class-3 or Class-8.

As noted above, Bankruptcy Code section 1129(b) provides that a Chapter-11 plan may be crammed down on a dissenting, impaired class if the plan does not discriminate unfairly and is fair and equitable with respect to that class. The Bankruptcy Code does not set forth any specific criteria for determining whether a plan does not discriminate unfairly with respect to a dissenting class. Some guidance is provided by the legislative history and commentary surrounding Section 1129(b). Specifically, these sources indicate that "if a plan protects the legal rights of a dissenting class in a manner consistent with the treatment of other classes whose legal rights are intertwined with those of the dissenting class, then the plan does not discriminate unfairly with respect to the dissenting class."⁶⁵ The Plan provides essentially the same treatment for the Abulafia Trust with respect to its secured claims under the Term Loan as is provided to other lenders with secured claims under the Term Loan, and it provides essentially the same treatment for the Abulafias with respect to their Class-8 claims as is provided to general unsecured creditors on account of their Class-7 claims. The only significant difference in their treatment is that the Abulafias' distributions continue to be subject to escrow pending the resolution of significant claims against the Abulafias whereas the other creditors have either entered into a settlement agreement resolving the claims against them or are not subject to any such claims. If World Bazaars' claims are ultimately determined to be without merit, then the Abulafias will receive the distributions that have been escrowed together with all interested earned on those distributions, thus putting them in an economically comparable position to other creditors. Given the significant differences between these creditors—some of whom have entered into a settlement

⁶⁵ Kenneth N. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AMERICAN BANKR. L.J. 133, 142 (1979) (citations omitted).

1 agreement resolving the claims against them or whom are not subject to claims and the
2 others of whom are subject to roughly \$23 million in claims asserted by this Estate—the
3 Plan does not unfairly discriminate against the Abulafias by placing their potential distri-
4 butions into an interest-bearing escrow account pending the resolution of the substantial
5 claims against them.

(2) The Plan Is Fair and Equitable with Respect to Class 3.

Section 1129(b)(2)(A) sets forth several criteria under which the treatment of a class of secured claims is fair and equitable. Among other things, a plan is fair and equitable if it provides a secured creditor with the indubitable equivalent of its claims.⁶⁶ The Plan, in fact, provides the Abulafia Trust with the indubitable equivalent of its Class-3 claim. Promptly after a determination, if any, by this Court that the Abulafias hold allowed Class 3 claims that are not subject to disallowance under Section 502(d), the Abulafia Trust will receive on account of these claims the proceeds in the Abulafia Escrow Account. These proceeds represent the cash proceeds generated from the liquidation of the Abulafia Trust's collateral together with all interest earned thereon. Such treatment has long been held out as the quintessential example of the indubitable equivalent of a creditor's collateral.⁶⁷

The Abulafias have asserted several additional objections to the cramdown of their Class-3 claims under Section 1129(b)(2), all of which are based on erroneous readings of the relevant statute and the Plan. First, the Abulafias have asserted that the Plan's treatment of Class 3 is not fair and equitable because the Plan does not provide for the retention of liens and deferred cash payments permitted under Section 1129(b)(2)(A)(i). This treatment, however, is only one of three, alternative treatments

⁶⁶ 11 U.S.C. § 1129(b)(2)(A)(iii) (a plan is fair and equitable with respect to a class of secured claims if it provides "for the realization by such holders of the indubitable equivalent of such claims").

⁶⁷ See *In re Hollanger*, 15 B.R. 35, 47 (Bankr. W.D. La. 1981) (payment in full over reasonable period of time, with appropriate interest, constitute indubitable equivalent for cram down purposes).

1 authorized under Section 1129(b)(2)(A). As discussed above, the collateral securing
2 the Abulafias' claim already has been sold and the proceeds have been set aside, sub-
3 ject to the Abulafias' lien. The Plan provides for the payment of the Abulafia's secured
4 claim, plus interest, upon resolution of the estate's claims and counterclaims. Thus,
5 contrary to the Abulafias' contention, the Plan provides for payment in full of this se-
6 cured claim, plus interest. At a minimum, the Plan provides Class-3 claimants with the
7 indubitable equivalent of their secured claims, by providing that the cash proceeds de-
8 rived from their collateral will be paid to them, plus interest. As discussed extensively
9 above, the withholding of payment pending resolution of these disputes is fully consis-
10 tent with the Bankruptcy Code and case law. Under the plain language of Section
11 1129(b)(2)(A)(iii), this treatment constitutes one permissible method of providing fair and
12 equitable treatment to a secured claim.

13 Second, the Abulafias have complained that the Plan improperly "trans-
14 fers" the liens securing their Class-3 claims to the Estate. However, the proposed lien
15 transfer served solely to effect the equitable subordination of Class-3 claims originally
16 provided for under the Plan. World Bazaars subsequently elected not to pursue equita-
17 ble subordination under the Plan, and the lien-transfer provision is therefore no longer
18 operable.⁶⁸ The estate has merely reserved in full its right to seek equitable subordi-
19 nation after plan confirmation.

20 Third, the Abulafias have suggested that the Plan does not provide them
21 with interest on their Class-3 claims and that, if it does, that interest rate is not ade-
22 quately disclosed. In fact, the Plan does provide that the distributions on the Class-3
23 claims will be placed into an interest-bearing account. Furthermore, Section IV.C.1.a of
24 the Disclosure Statement indicates that World Bazaars' cash is invested in a Wells
25

26
27 ⁶⁸ See *Notice of Election, Without Prejudice, to Withdraw Request to Equitably Subor-*
28 *dinate Class-3 and Class-8 Claims in Conjunction with Confirmation of Second*
Amended Chapter-11 Plan Proposed by World Bazaars, Inc. (Dated November 10,
2000).

1 Fargo deposit account that is currently accruing interest at an annual rate of approxi-
2 mately 6%. World Bazaars anticipates that any escrowed funds will be similarly in-
3 vested. In any event, the Abulafias complaint, at best, constitutes a question regarding
4 the adequacy of the Disclosure Statement. The Disclosure Statement has long since
5 been approved by this Court after considering argument from numerous parties, includ-
6 ing the Abulafias, at not one but two separate hearings. The Abulafias failed to raise
7 any questions regarding the disclosure of the interest rate either in their pleadings or at
8 these hearings, and the adequacy of that disclosure does not now constitute grounds
9 for failing to confirm World Bazaars' Plan.

(3) The Plan Is Fair and Equitable With Respect to Class 8.

2. Class 9 (the WARN Act Claims).

Class 9 (the WARN Act Claims) is, as a technical matter, deemed to reject

25 69 See 11 U.S.C. § 1129(b)(2)(B)(a plan is fair and equitable with respect to a class of
26 unsecured claims if " the holder of any claim or interest that is junior to the claims of
27 such class will not receive or retain under the plan on account of such junior claim or
28 interest any property"); see also 7 Collier on Bankruptcy, ¶ 1129.04[4][a] at 1129-94
(15th Ed. 1999) ("Thus, if all of the debtor's reorganization value is allocated to senior
classes, and they are still not paid in full, absolute priority is not violated so long as
no junior class participates on account of its junior interest.") (emphasis added).

1 the Plan. Section IV.G. of the Plan currently provides for the equitable subordination of
2 the WARN Act Claims asserted as Priority Claims against the Estate or, in the alterna-
3 tive, for the WARN Act Claims to be separately classified in Class 9 and to receive no
4 consideration except to the extent that these claims are proven to be claims for actual
5 damages, to which extent the Claims would be deemed to be Class-7 Claims. How-
6 ever, on December 28, 2000, this Court entered its order approving a settlement
7 agreement among World Bazaars and the WARN Act claimants. Under the terms of
8 this settlement agreement, the WARN Act Claims have been deemed to be allowed as
9 Class-5 Priority Claims in specified amounts.⁷⁰ As a result of this settlement agreement,
10 there are no claims in Class 9. Accordingly, World Bazaars hereby modifies the Plan to
11 eliminate Class 9.

12 **3. Class 10 (Interests).**

13 Section 1129(b)(2)(C)(ii) specifically provides that, with respect to a class
14 of interests, a Chapter-11 plan is fair and equitable if no interest holder receives or re-
15 tains any property on account of an interest in a junior class of interests.⁷¹ Section
16 IV.H. of the Plan provides that all interests will be cancelled on the Effective Date and
17 that no interest will receive or retain any value under the Plan. The treatment of Class
18 10 is therefore fair and equitable under Section 1129(b)(2)(C)(ii) because there is no
19 class of junior interests that will receive or retain property under the Plan.

20 Furthermore, this treatment does not unfairly discriminate against Class
21 10. The interests classified in Class 10 are: (a) unlike any other claims classified under
22 the Plan; and (b) junior in legal rights of distribution to every other claim classified under
23 the Plan.⁷²

24

25 ⁷⁰ See the Order: (1) Authorizing Debtor to Enter Into Settlement Agreement re: Cer-
26 tain Warn Act Claims; and (2) Allowing Certain Warn Act Claims in Accordance With
the Settlement Agreement.

27 ⁷¹ 11 U.S.C. § 1129(b)(2)(C)(ii).

28 ⁷² See, e.g., *In re Acequia, Inc.*, 787 F.2d 1352, 1364 (9th Cir. 1986).

1 **C. The Plan Modifications Comply with Bankruptcy Code Section
2 1127(a).**

3 World Bazaars has entered into several written settlement agreements
4 modifying its Plan with respect to certain creditors. These modifications all comply with
5 Bankruptcy Code section 1127(a) in as much as they do not modify the plan such that
6 the Plan fails to meet the requirements of Bankruptcy Code sections 1122 and 1123.

7 Specifically, World Bazaars has entered into three settlement agreements
8 with the SKM Funds and the SKM Lenders. In substance, these agreements affect a
9 global settlement of all claims among World Bazaars, the SKM Funds, and the SKM
10 Lenders and authorize World Bazaars to distribute to the SKM Lenders the cash pro-
11 ceeds from the liquidation of their collateral. These agreements implicitly modify the
12 Plan—and the Plan is hereby so modified—to provide that that claims of the SKM
13 Funds and the SKM Lenders have been satisfied in full by the treatment provided in the
14 settlement agreements; that the SKM Funds and the SKM Lenders will receive no addi-
15 tional distributions under the Plan; and that Class 3 (the SKM Lenders' Secured Claims
16 under the Term Loan) and Class 7 (the SKM Parties' Unsecured Claims) are hereby de-
17 leted from the Plan. In furtherance of these settlement agreements, the parties also en-
18 tered into a stipulation extending until January 22, 2001 the deadline for the SKM Par-
19 ties to submit a ballot accepting or rejecting the Plan or to file and serve any objections
20 and evidence in opposition to confirmation of the Plan.

21 Similarly, World Bazaars has entered into two settlement agreements with
22 the Bank Group. These settlement agreements made available to World Bazaars cer-
23 tain of the Bank Group's cash collateral, and in exchange, World Bazaars has already
24 made two interim distributions to the Bank Group and the Bank Group has already
25 funded certain of its commitments under the Bank such as its commitment to provide a
26 \$500,000 Litigation Fund for the benefit of certain unsecured creditors. These agree-
27 ments implicitly modify the Plan—and the Plan is hereby so modified—to provide that,
28 to the extent that commitments otherwise existing under the Plan have already been

1 performed in connection with the settlements, no further action is needed under the
2 Plan.

3 World Bazaars has also entered into a settlement agreement with certain
4 parties who asserted WARN Act claims classified in Class 9 under the Plan. As dis-
5 cussed in Section III.B.2, above, this settlement agreement provided the WARN Act
6 claimants with specified, allowed priority claims in Class 5 and otherwise disallowed
7 their claims. Accordingly, there are no claimants in Class 9 and the Plan has been
8 modified to delete Class 9.

9 Finally, World Bazaars and Majestic Realty have entered into a stipulation
10 that modifies the Plan to provide that any non-ordinary course administrative claim to be
11 asserted by Majestic Realty must be asserted no later than January 15, 2001. Majestic
12 Realty has already timely asserted such a claim. This Court, however, has *sua sponte*
13 questioned whether the Plan's existing provisions—which call for any non-ordinary-
14 course claims arising on or before October 31, 2000, to be asserted on or before No-
15 vember 30, 2000, *i.e.*, before the Plan confirmation hearing—are appropriate. In re-
16 sponse, World Bazaars hereby modifies Section IV.A.1. of its Plan to provide that—
17 except inasmuch as Majestic Realty has consented to the January 15, 2001 deadline
18 with respect to its claims—the deadline for asserting any non-ordinary-course adminis-
19 trative claim against World Bazaars will be 60 days after the Plan's Effective Date.

20 **IV.**

21 **MISCELLANEOUS OBJECTIONS TO CONFIRMATION**

22 Only two objections to plan confirmation have been filed: (1) the *Objection*
23 *of Abulafia to Confirmation of the Debtor's Second Amended Chapter 11 Plan Proposed*
24 *by World Bazaars, Inc. (Dated November 10, 2000)* (the "Abulafia Objection"); and (2)
25 *the Objection to Confirmation of Debtor's Second Amended Chapter-11 Plan* (the "IRS
26 Objection"). The issues raised in these objections are discussed below.

27

28

1 **A. The Abulafia Objection.**

2 The Abulafia Objection raises several issues regarding the treatment of
3 Class-3 and Class-8 claims, all of which have already been discussed in detail in this
4 Memorandum.⁷³ In addition, the Abulafia Objection asserts that this Court should not
5 confirm World Bazaars' Plan because the accompanying Disclosure Statement alleg-
6 edly contains an inadequate description of the Plan's proposed settlement of various
7 claims between World Bazaars and the Bank Group. First, even if the description of the
8 Bank Group settlement agreement were inadequate, this is at best an issue regarding
9 the adequacy of the Disclosure Statement. The Disclosure Statement was approved by
10 this Court long ago after considering arguments from numerous parties, including the
11 Abulafias, at not one but two separate hearings. The Abulafias failed to raise any ques-
12 tions regarding the adequacy of the Disclosure Statement's discussion of the Bank
13 Group Settlement either in their pleadings or at these hearings, and the adequacy of
14 that disclosure does not now constitute grounds for failing to confirm World Bazaars'
15 Plan.

16 Second, the Abulafias themselves concede in their objection that the Dis-
17 closure Statement contains a description of the various claims against the Bank Group
18 as well as the consideration that the Bank Group is providing in connection with the
19 proposed settlement agreement:

20 [A] reader can glean . . . the following regarding the Debtor's
21 claims against the Bank Group: a) there may be a question
22 as to whether the Debtor received fair value for the Credit
23 Facility in the 1998 Restructuring, b) the Bank Group's agent
24 may have improperly contacted significant customers
25 regarding a potential liquidation of the Debtor's inventory
which may have given rise to claims for tortious interference
with business relations, and c) there may have been claims
for fraudulent conveyances and preferences arising out of
the 1998 Restructuring because the Debtor is waiving such

26
27 ⁷³ See Section III.B.1.a (authority for withholding distributions); Section III.B.1.a. (dis-
28 cussion of claims against the Abulafias); Section II.B.1.b.(1) (treatment of Classes 3
and 8 is not unfairly discriminatory); and Sections III.B.1.b.(2) and
II.B.1.b.(3)(treatment of Classes 3 and 8 is fair and equitable).

1 claims under the settlement. In return for waiving these
2 claims, the Bank Group will a) waive all Claims (except un-
3 der the Plan) against the Debtor, b) make available
\$500,000 for a litigation fund, and c) agree to a slightly less
4 favorable treatment on account of its Class 6 claims.⁷⁴

5 The Bank Group settlement also provides for the Bank Group to furnish a
6 \$150,000 retainer to be used by World Bazaars' special litigation counsel to pursue sig-
7 nificant claims against the Abulafias, and the Bank Group has furnished from its cash
8 collateral roughly \$70,000 to fund the Continuing Estate's anticipated postconfirmation
9 expenses, most of which are directly related to litigation support in connection with the
10 Abulafia litigation.⁷⁵ Thus, despite the Abulafias' assertion that the Disclosure Statement
11 does not adequately disclose the terms of the settlement agreement and that the pro-
12 posed settlement agreement will not benefit World Bazaars' creditors, it is plain to all
13 parties, including the Abulafias, that the proposed settlement agreement will provide
14 significant recoveries to unsecured creditors. In particular, the settlement agreement
15 will provide unsecured creditors with a \$500,000 litigation fund to pursue avoidance ac-
16 tions and claim objections for their benefit; it carves out some recoveries that would
17 otherwise be distributed to the Bank Group on account of its deficiency claims and
18 makes these recoveries available to general unsecured creditors; and most importantly,
19 it provides the funding needed for the estate to pursue roughly \$23 million in claims
20 against the Abulafias. The prosecution of these claims will likely provide general unse-
21 cured creditors with their most significant source of recovery in this case.

22 Third, the Abulafias state—with no authority whatsoever—that this Court
23 cannot approve the proposed settlement agreement because World Bazaars has not
24 furnished an exhaustive analytical and evidentiary analysis of its claims against the
25 Bank Group, including a description of the evidence that World Bazaars has to pursue
26 these claims, an analysis of the potential recoveries, a substantive analysis of the value

27
28⁷⁴ See Abulafia Objection at 6:8-19.

⁷⁵ See Plan at Section VII.A.2.

1 and merits of its potential claims, a discussion of the availability of contingency counsel,
2 and an analysis of any possible collection issues. This is simply not required. The
3 Ninth Circuit has long recognized that "[t]he bankruptcy court has great latitude in ap-
4 proving compromise agreements."⁷⁶ Accordingly, when approving a settlement agree-
5 ment, the Court need conduct neither an exhaustive investigation into the validity, nor a
6 mini-trial on the merits, of the claims sought to be compromised.⁷⁷ Rather, it is sufficient
7 that the Court determine that the settlement was negotiated in good faith and is reason-
8 able, fair, and equitable.⁷⁸ World Bazaars respectfully submits that its Plan and Disclo-
9 sure Statement and the accompanying confirmation materials contain adequate infor-
10 mation for this Court and World Bazaars' creditors to make this determination.

11 **B. The IRS Objection.**

12 The IRS Objection asserts three separate objections to Plan confirmation.
13 First, the IRS Objection asserts that World Bazaars' filed its Plan in bad faith under
14 Bankruptcy Code section 1129(a)(3) because World Bazaars has not yet filed its tax re-
15 turns for the 2000 tax year.

16 In determining whether a plan has been filed in good faith, Courts look to
17 the totality of the circumstances surrounding the plan.⁷⁹ Where the plan is proposed
18 with a legitimate and honest purpose and has a reasonable hope of success, the good
19 faith requirement of 11 U.S.C. § 1129(a)(3) is met.⁸⁰ It is not disputed that World Ba-
20 zaars' Plan meets these requirements. As set forth earlier in this Memorandum, World
21

22 ⁷⁶ *Woodson v. Fireman's Fund Ins. Co. (In re Woodson)*, 839 F.2d 610, 620 (9th Cir.
23 1988).

24 ⁷⁷ *United States v. Alaska National Bank (In re Walsh Constr., Inc.)*, 669 F.2d 1325,
25 1328 (9th Cir. 1982).

26 ⁷⁸ *Robinson v. Kane (In re A & C Properties)*, 784 F.2d 1377, 1381 (9th Cir. 1986).

27 ⁷⁹ *McCormick v. Banc One Leasing Corp. (In re McCormick)*, 49 F.3d 1524, 1526 (11th
28 Cir. 1995); *In re Block Shim Dev. Co. – Irving*, 939 F.2d 289, 292 (5th Cir. 1991).

⁸⁰ *McCormick*, 49 F.3d at 1526.

1 Bazaars' Plan was filed to effect the orderly liquidation of the company's assets for the
2 benefit of all creditors. Nonetheless, the IRS seems to believe that the failure properly
3 to file any one tax return is *per se* bad faith. In the IRS Objection, the IRS asserts that
4 World Bazaars' "failure to file [a single tax return form] demonstrates that the plan was
5 proposed in bad faith."⁸¹ The cases cited by the IRS in support of this conclusion,
6 however, bear no relation whatsoever to the World Bazaars' case.

7 Greatwood v. *United States*⁸² involved a chapter 13 debtor that had failed
8 to file income tax returns prepetition, denied that he owed any income tax, and did not,
9 during the 9 months that his Chapter-13 case was pending, file any plan that proposed
10 payment to the IRS or any other creditor. The Court found that the debtor was using the
11 bankruptcy process solely to resolve a tax dispute with the IRS and not for any other
12 legitimate purpose.⁸³ This debtor had previously discharged much of its debt in a recent
13 Chapter-7 case, and the court found that the Chapter-13 case had been filed to deal
14 with a tax liability to the IRS that had been found to be nondischargeable in the debtor's
15 prior Chapter-7 case.⁸⁴

16 The debtors in *In re Hahn*,⁸⁵ *In re Tobias*,⁸⁶ and *In re MacLean*⁸⁷ all failed
17 to file their tax returns even though the Bankruptcy Court had ordered them to do so. In
18 each of those cases, the court found that the debtor's disregard of the court order dem-
19 onstrated a lack of good faith and justified dismissal of case.

20
21 _____
22⁸¹ See IRS Objection at 2.

23⁸² *Greatwood v. United States (In re Greatwood)*, 194 B.R. 637 (B.A.P. 9th Cir. 1996)

24⁸³ *Id.* at 641.

25⁸⁴ *Id.* at 641.

26⁸⁵ *In re Hahn*, 200 B.R. 249, 252 (Bankr. M.D. Fla. 1996)

27⁸⁶ *In re Tobias*, 200 B.R. 415 (Bankr. M.D. Fla. 1996)

28⁸⁷ *In re MacLean*, 200 B.R. 417, 419 (Bankr. M.D. Fla. 1996)

1 Unlike the cases cited above, World Bazaars' has not willfully refused to file its returns
2 for the 2000 tax year in order to avoid tax liabilities nor has World Bazaars used the
3 bankruptcy process solely as a means of dealing with the IRS claim. Significantly,
4 World Bazaars has violated no Court order directing it to file tax returns. Thus, none of
5 the elements present in the IRS's cases that led to a finding bad faith are present here.
6 In fact, World Bazaars' Disclosure Statement and the records in this case establish that
7 World Bazaars anticipates that, once it files its returns for the 2000 tax year, it will be en-
8 titled to a tax refund of approximately \$210,000. World Bazaars has transferred its
9 rights and interest in this refund to the Bank Group in exchange for the Bank Group's
10 consent to World Bazaars' use of roughly \$400,000 in cash collateral in this case, and
11 World Bazaars anticipates that the Bank Group will soon file the needed tax returns to
12 recover this refund. The filing of a request for an extension of time to file this returns—
13 which the IRS Objection itself states is an automatic extension—was a mere oversight
14 and, under the circumstances in this case, does not support a finding that World Ba-
15 zaars' has filed its Plan in bad faith.

16 Second, the IRS Objection asserts that World Bazaars has failed to pro-
17 vide for the payment of administrative expenses. Yet on page 4 of the IRS Objection,
18 the IRS acknowledges that World Bazaars has in its Plan provided for the treatment of
19 Administrative Tax Claims. In fact, the IRS complains that this treatment requires the
20 IRS to file a proof of claim or motion asserting its Administrative Tax Claims on or be-
21 fore the later of 60 days after the Effective Date or 120 days after World Bazaars files its
22 tax returns, a treatment that it claims is contrary to the provisions of Bankruptcy Code
23 section 505(b)(1)(B), which establishes a 180-day period for the IRS to review a tax re-
24 turn. Accordingly, World Bazaars hereby modifies its Plan to extend this 120-day period
25 to 180 days.

26 Third, the IRS Objection asserts that the Plan does not satisfy Bankruptcy
27 Code section 1129(a)(7) because the IRS, an administrative tax claimant, does not ac-
28 cept the Plan and because World Bazaars has not established that the IRS will receive

1 at least as much under the Plan as it would receive under a Chapter-7 liquidation. Section
2 1129(a)(7), however, applies only to creditors who are classified under the Plan.
3 The claims of administrative claimants are not classified, and therefore do not fall within
4 the ambit of Section 1129(a)(7), because these claims will receive certain treatment
5 specifically established under the Bankruptcy Code. As an administrative claimant, the
6 IRS is entitled to be paid in full under Bankruptcy Code section § 503(b)(1)(B), and the
7 IRS is therefore not impaired and is deemed to accept the Plan under Bankruptcy Code
8 section 1126(f). In any event, as discussed above, World Bazaars has clearly estab-
9 lished that creditors will receive at least as much under this the Plan as they would re-
10 ceive in a Chapter-7 liquidation.

11 **V.**

12 **CONCLUSION**

13 Based upon the foregoing, the pleadings, and evidence referenced in this
14 Memorandum, and the record in this case, World Bazaars believes that its Plan satisfies
15 all of the applicable requirements for confirmation and that confirmation of the Plan is
16 reasonable, appropriate, and in the best interests of all creditors and shareholders.

17 ///

18 ///

19 World Bazaars therefore respectfully requests that the Court confirm the Plan and grant
20 to World Bazaars any other related relief that the Court may deem appropriate under
21 the circumstances.

22
23
24 Dated: August 25, 2003

25 METTE H. KURTH, ESQ., an Attorney with
26 KLEE, TUCHIN, BOGDANOFF & STERN LLP
Bankruptcy Counsel for World Bazaars, Inc.

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