Docket #0147 Date Filed: 2/11/2013

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	**Chapter 11**
SCHOOL SPECIALTY, INC., *et al.*,	**Case No. 13-10125 (KJC)**
Debtors.	**Jointly Administered**
	Re: Docket Nos. 5, 71
	Obj. Deadline: 2/15/13, 4:00 p.m.
	Hearing Date: 2/25/13, 11:00 a.m.

OBJECTION OF CERTAIN UTILITY COMPANIES TO THE MOTION FOR AN ORDER PURSUANT TO SECTION 366 OF THE BANKRUPTCY CODE (I) PROHIBITING UTILITY COMPANIES FROM ALTERING, REFUSING, OR DISCONTINUING UTILITY SERVICES, (II) DEEMING UTILITY COMPANIES ADEQUATELY ASSURED OF FUTURE PERFORMANCE, (III) ESTABLISHING PROCEDURES FOR DETERMINING ADEQUATE ASSURANCE OF PAYMENT, AND (IV) SETTING A FINAL HEARING RELATED THERETO

Georgia Power Company, Westar Energy, Inc. and Public Service Company of New Hampshire (collectively, the "Utilities"), by counsel, hereby object to the *Motion For An Order Pursuant To Section 366 of the Bankruptcy Code (I) Prohibiting Utility Companies From Altering, Refusing, or Discontinuing Utility Services, (II) Deeming Utility Companies Adequately Assured of Future Performance, (III) Establishing Procedures For Determining Adequate Assurance of Payment, and (IV) Setting a Final Hearing Related Thereto* (the "Utility Motion"), and set forth the following:

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Introduction

In 2005, Congress amended Section 366 of the Bankruptcy Code to add, among other things, Section 366(c) to address adequate assurance of payment requests in Chapter 11 cases. Prior to 2005, Section 366(b) governed adequate assurance of payment determinations in all bankruptcy cases. Section 366(b), which has not been modified, provides, in pertinent part:

> On request of a party in interest and after notice and a hearing, the court may order reasonable modification of the amount of the deposit or other security necessary to provide adequate assurance of payment.

As set forth above, courts had the authority under Section 366(b) to modify the amount of the deposit or other security that was necessary to provide adequate assurance of payment, which is significantly broader than the legal standard established in Sections 366(c)(2) and (3).

Sections 366(c)(2) and (3) of the Bankruptcy Code provide:

> (2) Subject to paragraphs (3) and (4), with respect to a case filed under chapter 11, a utility referred to in subsection (a) may alter, refuse, or discontinue utility service, if during the 30-day period beginning on the date of the filing of the petition, the utility does not receive from the debtor or the trustee adequate assurance of payment for utility service that is satisfactory to the utility;
>
> (3)(A) On request of a party in interest and after notice and a hearing, the court may order modification of the amount of an assurance of payment under paragraph (2).

The significant difference between the two provisions is the pre-2005 standard required a court to focus on whether or not to "order reasonable modification of the amount of the deposit or

other security necessary to provide adequate assurance of payment" and Section 366(c) now requires a court to focus on whether or not to "order modification of the amount of an assurance of payment under paragraph (2)." The amount of assurance of payment under paragraph (2) (Section 366(c)(2)) in these cases is the two-month deposits requested by the Utilities. Accordingly, under the foregoing legal standard, it is the Debtors' burden to present evidence to demonstrate, why, if at all, the amounts of the Utilities' deposit requests should be modified. *See In re Stagecoach Enterprises, Inc.*, 1 B.R. 732, 734 (Bankr. M.D. Fla. 1979) (holding that the debtor, as the petitioning party at a Section 366 hearing, bears the burden of proof); *see also Great Atlantic & Pacific Tea Company, Inc.*, 2011 WL 5546954 at page 5 (Bankr. S.D.N.Y. 2011). Courts that have found that the courts retain the same discretion as under Section 366(b), or allow the debtor to pick the form and/or amount of security, simply refuse to follow the plain language of the statute.

In addition to changing the legal standard, Section 366(c) also changes the adequate assurance of payment determination as follows: (1) The statute provides the Debtors with 30 days to provide adequate assurance of payment instead of 20 days; (2) Section 366(c)(1) defines the forms of adequate assurance of payment, which was not included in Section 366(b); and (3)

Section 366(c)(1)(B) and (c)(3)(B) limit what the Court can consider.

The post-petition deposits sought by the Utilities in this case are as follows: (A) Georgia Power Company ("Georgia Power") – Georgia Power held a prepetition deposit in the amount of $6,202.59 that it will recoup against prepetition debt pursuant to Section 366(c)(4) of the Bankruptcy Code, resulting in a deposit credit of $4,483.61 that can serve as adequate assurance of payment for Georgia Power;(B) Westar Energy, Inc. ("Westar") – a two-month deposit in the amount of $26,535; and (C) Public Service Company of New Hampshire ("PSNH") – a two-month deposit in the amount of $25,100.

As set forth herein, this Court should deny the Utility Motion because the amounts of the post-petition deposit requests of the Utilities are reasonable and should not be modified.

Facts

Procedural Facts

1. On January 28, 2013 (the "Petition Date"), the Debtors commenced their cases under Chapter 11 of title 11 of the United States Code (the "Bankruptcy Code") that are now pending with this Court. The Debtors continue to operate their businesses and manage their properties as debtors in possession pursuant to Bankruptcy Code sections 1107(a) and 1108.

2. The Debtors' cases are being jointly administered.

The Utility Motion

3. On the Petition Date, the Debtors filed the Utility Motion.

4. Proper notice of the Utility Motion was not provided to the Utilities prior to the Court entering the *Interim Order Pursuant To Section 366 of the Bankruptcy Code (I) Prohibiting Utility Companies From Altering, Refusing, or Discontinuing Utility Services, (II) Deeming Utility Companies Adequately Assured of Future Performance, and (III) Setting a Final Hearing Related Thereto* (the "Interim Utility Order") on January 30, 2013.

5. Because the Utilities were not served with the Utility Motion and the Debtors never attempted to contact the Utilities regarding their adequate assurance requests prior to the filing of the Utility Motion, the Utilities had no opportunity to respond to the Utility Motion or otherwise be heard at the *ex parte* hearing on the Utility Motion that took place on January 30, 2013, despite the fact that Section 366(c)(3) (presuming this was the statutory basis for the relief sought by the Debtors) requires that there be "notice and a hearing" to the Utilities.

6. In the Utility Motion, the Debtors seek to avoid the applicable legal standards under Sections 366(c)(2) and (3) by seeking Court approval for their own form of adequate assurance of payment, which is a newly-created segregated account (the

"Bank Account") in the amount of $330,000 that purportedly represents 50% of the Debtors' estimated monthly utility charges. Utility Motion at ¶ 12. The foregoing proposal is unacceptable to the Utilities and should not be considered relevant by this Court because Sections 366(c)(2) and (3) do not allow the Debtors to establish the form or amount of adequate assurance of payment. Under Sections 366(c)(2) and (3), this Court and the Debtors are limited to modifying, if at all, the amount of the security sought by the Utilities under Section 366(c)(2).

7. Although the Debtors propose in the proposed Final Utility Order that the Bank Account would be maintained with a minimum balance of $330,000, which may be adjusted to account for (i) termination of post-petition accounts, (ii) agreements between the Debtors and certain utilities, the Debtors' proposed Final Utility Order also provides that the Debtors' obligation to maintain the Bank Account would terminate upon the Effective Date of a plan. (Proposed Final Utility Order at ¶ 4). However, the Utilities will likely continue to provide post-petition utility goods/services to the Debtors through the Effective Date of the Plan, and would bill the Debtors for services to the Effective Date in arrears, i.e. after the Effective Date. As such, it does not make sense that any funds remaining in the Bank Account on a plan Effective Date should be returned to the Debtors when

utility service through the Effective Date would be billed subsequent to the Effective Date.

8. The Utility Motion also does not address why the Bank Account would be undercapitalized at a two-week deposit amount when the Debtors know that the Utilities are required by applicable state laws, regulations and/or tariffs to bill the Debtors monthly.

9. Furthermore, the Utility Motion does not address why this Court should consider modifying, if at all, the amount of the Utilities' adequate assurance requests pursuant to Section 366(c)(2).

10. The Interim Utility Order provides that: (a) the final hearing on the Utility Motion shall be on February 25, 2013 at 11:00 a.m.; and (b) objections to the Utility Motion are due on or before February 15, 2013.

Facts Regarding the Debtors

11. Debtor School Specialty, Inc. ("School Specialty"), the primary operating company of the Debtors, is one of the largest suppliers of supplemental educational products, equipment, and standards-based curriculums to the pre-kindergarten through twelfth grade market in the United States. *Declaration of Gerald T. Hughes In Support of Chapter 11 Petitions and First Day Motion* at ¶ 5 (hereinafter "Hughes Dec. at ¶__").

12. As of the Petition Date, School Specialty had

approximately $139.6 million in secured indebtedness, consisting of a revolving credit facility and a term loan which the company entered into on May 22, 2012 to repay existing secured indebtedness. Hughes Dec. at ¶ 19.

13. School Specialty's revolving senior secured asset-based credit facility (the "ABL") is provided under the Credit Agreement (the "ABL Agreement") between School Specialty and certain of its domestic subsidiaries, as borrowers, the lenders thereto (the "ABL Lenders"), and Wells Fargo Capital Finance, LLC, as administrative agent (the "ABL Agent"). The ABL Agreement provides up to $200 million in revolving credit and matures on September 30, 2014. As of the Petition Date, the aggregate amount outstanding under the ABL Agreement was approximately $47.62 million, inclusive of related letters of credit. Hughes Dec. at ¶ 20.

14. Obligations under the ABL Agreement are secured by a first-priority security interest in substantially all of the assets of School Specialty and its subsidiary borrowers and guarantors. Pursuant to an intercreditor agreement between the ABL Agent and the Term Loan Agent (defined below) dated May 22, 2012 (the "Intercreditor Agreement"), the ABL Lenders have (i) a first-priority security interest in substantially all of the working capital assets of School Specialty and its subsidiary borrowers and guarantors and (ii) a second-priority security

interest in all other assets, subordinate only to the first-priority security interest of the Term Loan Lender. Hughes Dec. at ¶ 21.

15. School Specialty's term loan (the "Term Loan") is provided under the Credit agreement (the "Term Loan Agreement" and together with the ABL Agreement, the "Prepetition Loan Agreements") among School Specialty and certain of its domestic subsidiaries, as borrowers, and Bayside Finance, LLC, as administrative agent, collateral agent and lender ("Bayside" or the "Term Loan Agent" or "Term Loan Lender" and together with the ABL Lenders, the "Prepetition Secured Lenders"). Bayside is the sole Term Loan Lender. The Term Loan Agreement provides up to $70 million in term loan credit and matures on October 31, 2014. As of the Petition Date, the aggregate principal amount outstanding under the Term Loan Agreement was approximately $92 million, inclusive of the Make-Whole (discussed below). Hughes Dec. at ¶ 22.

16. Obligations under the Term Loan Agreement are secured by a first-priority security interest in substantially all of the assets of School Specialty and the subsidiary borrowers and guarantors. Pursuant to the Intercreditor Agreement, Bayside has (i) a second-priority security interest in substantially all of the working capital assets of School Specialty and the subsidiary borrowers and guarantors, subordinate only to the first-priority

security interest of the ABL Lenders, and (ii) a first-priority security interest in all other assets. Hughes Dec. at ¶ 23.

17. The Prepetition Loan Agreements impose a variety of financial ratio covenants and other standard terms, including a $20 million liquidity covenant that is tested on a monthly basis. Additionally, the Term Loan Agreement includes a make-whole payment in the approximate amount of $25 million due in the event of a prepayment of the debt during certain periods or upon acceleration of the debt due to an event of default (the "Make-Whole"). Hughes Dec. at ¶ 24.

18. The Debtors have approximately $60 million in ordinary course trade debt that was unpaid as of the Petition Date. Hughes Dec. at ¶ 27.

Events Leading to the Debtors' Chapter 11 Cases

19. The recent economic downturn, coupled with the company's leverage and liquidity positions, have resulted in a material decrease in the Debtors' financial performance in recent years. The Debtors' discretionary and supplemental business lines in particular, which historically have enjoyed some of the highest profit margins at the company, have experienced extensive downturns. In fiscal year 2012, the company reported total revenues of $731.9 million and gross profits of $283 million compared to revenues of $1.087 billion and gross profit of $461.2 million in fiscal year 2008. Hughes Dec. at ¶ 33.

20. In December 2012, the Debtors negotiated one-month forbearance agreements with their Prepetition Secured Lenders with respect to the company's month-end breach of the $20 million Minimum Liquidity Covenant under the Prepetition Agreements. On January 4, 2013, the Debtors reported that they were not in compliance with the Minimum Liquidity Covenant, thereby triggering events of default under the Prepetition Loan Agreements. As a result, pursuant to the terms of those agreements, the ABL Agent and Bayside each were entitled to accelerate the debt and declare the amounts outstanding under the Prepetition Loan Agreements immediately due and payable On January 4, 2013, Bayside exercised that right, and provided the company with a notice of acceleration of the Term Loan. However, pursuant to negotiated forbearance agreements dated January 4, 2013, the Prepetition Secured Lenders agreed to forebear with respect to the events of default until the earlier of February 1, 2013 and certain specified events. Hughes Dec. at ¶ 41.

21. The Debtors' management determined that the post-petition financing proposals made by the Prepetition Secured Lenders, including the requirement in Bayside's proposal that the Debtors conduct a Section 363 sale of substantially all of their assets, were the best and only viable options available under the circumstances. Hughes Dec. at ¶ 45.

The Debtors' Post-Petition Financing

22. On the Petition Date, the Debtors filed the *Motion of Debtors For Entry of Interim and Final Orders (I) Authorizing Debtors To (A) Obtain Postpetition Financing Pursuant To 11 U.S.C. §§ 105, 361, 362, 364(c)(1), 364(c)(3), 364(d)(1), 364(e) and 507, (B) Utilize Cash Collateral Pursuant To 11 U.S.C. § 363, (C) Grant Priming Liens and Superpriority Claims To the DIP Lenders, (D) Provide Adequate Protection To Prepetition Secured Parties Pursuant To 11 U.S.C. §§ 361, 362, 363 and 364, and (E) Repay In Full Amounts Owed In Connection With the Prepetition Secured Loans or Otherwise Converting the Prepetition Secured Obligations Into Postpetition Secured Obligations, (II) Scheduling a Final Hearing Pursuant To Bankruptcy Rules 4001(b) and (c) and (III) Granting Related Relief* (the "Financing Motion"). Through the Financing Motion, the Debtors are seeking authority to obtain (i) super-priority postpetition financing in the aggregate principal amount of up to $144,665,931.42 from Bayside (the "Bayside DIP Facility") consisting of (a) a credit facility in the amount of $50 million of new money funding, and (b) upon entry of the Final Financing Order, a repayment by way of a "roll up" of $94,665,931.42 of the Prepetition Debt; (ii) (a) a super-priority revolving credit facility made available to the DIP Borrowers in an aggregate principal amount of up to $175 million to be provided under the ABL DIP Facility, and (b)

repayment of the full amounts outstanding as of the Petition Date with respect to the Prepetition ABL Debt; and (iii) use of cash collateral. Financing Motion at ¶ 5.

23. Through the Financing Motion, the Debtors also seek a carve-out of $500,000 for the payment of fees and expenses of the Debtors' professionals. Financing Motion at p. 16.

24. On January 31, 2013, the Court entered the Interim Financing Order. Attached as Exhibit "A" to the Interim Financing Order is a twelve-week budget (the "Budget"). It is unclear from the Budget whether the Debtors have budgeted sufficient funds for the timely payment of their post-petition utility charges.

The Debtors' Sale Motion

25. On the Petition Date, the Debtors filed the *Debtors' Motion For Entry of (A) An Order (I) Scheduling Hearing on Approval of Asset Sale, Assumption and Assignment of Executory Contracts To Bayside School Specialty, LLC (Or Its Assignee) and Assumption of Certain Liabilities, and (II) Approving Bidding Procedures, Assumption & Assignment Procedures, Breakup Fee and Expense Reimbursement, and Form and Manner of Notice Thereof; and (B) An Order (I) Approving the Asset Purchase Agreement; (II) Authorizing the Sale of All or Substantially All of the Debtors' Assets Free and Clear of All Liens, Claims, Interests or Encumbrances; (III) Authorizing the Assumption and Assignment of*

Certain Executory Contracts and Unexpired Leases; and (IV) Granting Related Relief (the "Sale Motion").

26. Through the Sale Motion, the Debtors request the entry of an order approving an asset sale and assumption and assignment of executory contracts to Bayside (or its assignee (the "Proposed Purchaser" or "Stalking Horse Bidder"). Bayside indicated an interest in acquiring substantially all of the Debtors' assets through a credit bid of its secured debt under the Term Loan Agreement and the DIP Credit Agreement. Sale Motion at ¶ 11.

27. Pursuant to Section 11.1(c) of the Asset Purchase Agreement (the "APA"), the APA may be terminated at any time prior to the consummation and effectuation of the transactions contemplated in the APA pursuant to the terms and conditions therein, including: (i) the Bidding Procedures Order is not entered by February 9, 2013, unless agreed to in writing by the Purchaser; (ii) the Auction has not commenced by March 25, 2013, unless agreed to in writing by the Purchaser; (iii) the Court has not entered the Sale Order by March 27, 2013 (or such later date as the Purchaser may designate in writing); and (iv) the Sale Closing has not occurred by April 11, 2013 and such failure to close is not caused by the Purchaser's breach of the Asset Purchase Agreement. Sale Motion at p. 8.

28. The hearing on the Sale Motion is scheduled for February 11, 2013.

The Debtors' Critical Vendor Motion

29. On the Petition Date, the Debtors filed the *Debtors' Motion For Entry of Interim and Final Orders Authorizing the Debtors To Pay Prepetition Claims of Certain Critical Vendors, Foreign Suppliers, Freight Carriers and Section 503(b)(9) Claimants* (the "Critical Vendor Motion"). Through the Critical Vendor Motion, the Debtors are seeking authority to pay certain prepetition claims and 503(b)(9) claims of certain creditors who are (i) sole source suppliers, manufacturers and other critical vendors, (ii) suppliers who are located outside of the United States, (iii) freight carriers who ship goods to the Debtors' customers, and (iv) suppliers who provided goods to the Debtors in the 20-day period prior to the Petition Date (collectively, the "Critical Vendors"). Critical Vendor Motion at ¶ 9. Interestingly, despite stating in paragraph 10 of the Utility Motion that the Utilities' supply of goods/services "are essential to the operation of the Debtors' businesses" and it is "critical that Utility Services continue uninterrupted," the Debtors do not consider their utility providers to be Critical Vendors for the purposes of the Critical Vendor Motion.

Facts Concerning the Utilities

30. Each of the Utilities provided the Debtors with prepetition utility goods and/or services and have continued to provide the Debtors with utility goods and/or services since the

Petition Date.

31. Under the Utilities' billing cycles, the Debtors receive approximately one month of utility goods and/or services before the Utility issues a bill for such charges. Once a bill is issued, the Debtors have approximately 15 to 30 days to pay the applicable bill. If the Debtors fail to timely pay the bill, a past due notice is issued and, in most instances, a late fee may be subsequently imposed on the account. If the Debtors fail to pay the bill after the issuance of the past due notice, the Utilities issue a notice that informs the Debtors that they must cure the arrearage within a certain period of time or their service will be disconnected. Accordingly, under the Utilities' billing cycles, the Debtors could receive at least two months of unpaid charges before the utility could cease the supply of goods and/or services for a post-petition payment default.

32. In order to avoid the need to bring witnesses and have lengthy testimony regarding the Utilities regulated billing cycles, the Utilities request that this Court, pursuant to Rule 201 of the Federal Rules of Evidence, take judicial notice of the Utilities' billing cycles. Pursuant to the foregoing request and based on the voluminous size of the applicable documents, the Utilities are providing the following web site links to the tariffs and/or state laws, regulations and/or ordinances:

Georgia Power:
http://www.georgiapower.com/pricing/gpc_rates.asp

Westar:
http://www.westarenergy.com/wcm.nsf/9696428027fd605386257735006b6631/a6dfefd38d917990862578f4006babc7?OpenDocument&Highlight=0,tariffs

PSNH:
http://www.psnh.com/Templates/Content.aspx?id=4294967779&terms=tariffs

33. Subject to a reservation of the Utilities' right to supplement their post-petition deposit requests if additional accounts belonging to the Debtors are subsequently identified, the Utilities' post-petition deposit requests are as follows:

Utility	No. of Accts.	Est. Prepet. Debt	Dep. Request
Georgia Power	1	$1,718.98	$5,715 (2-month)
Westar	2	n/a	$26,535 (2-month)
PSNH	2	n/a	$25,100 (2-month)

34. Georgia Power held a prepetition deposit in the amount of $6,202.59 that it will recoup against prepetition debt pursuant to Section 366(c)(4) of the Bankruptcy Code, resulting in a deposit credit of $4,483.61 that can serve as adequate assurance of payment for Georgia Power.

Discussion

A. THE UTILITY MOTION SHOULD BE DENIED AS TO THE UTILITIES.

Sections 366(c)(2) and (3) of the Bankruptcy Code provide:

> (2) Subject to paragraphs (3) and (4), with respect to a case filed under chapter 11, a utility referred to in subsection (a) may alter, refuse, or discontinue utility service, if during the 30-day period beginning on the date of the filing of the petition, the utility does not receive from the debtor or the trustee adequate assurance of payment for utility service that is satisfactory to the utility;
>
> (3)(A) On request of a party in interest and after notice and a hearing, the court may order modification of the amount of an assurance of payment under paragraph (2).

As set forth by the United States Supreme Court, "[i]t is well-established that 'when the statute's language is plain, the sole function of the courts--at least where the disposition required by the text is not absurd--is to enforce it according to its terms.'" *Lamie v. United States Trustee*, 540 U.S. 526, 534, 124 S. Ct. 1023, 157 L. Ed. 2d 1024 (2004) (*quoting Hartford Underwriters Ins. Co.* v. *Union Planters Bank, N. A.,* 530 U.S. 1, 6, 120 S. Ct., 1942, 147 L. Ed. 2d 1 (2000)). *Rogers v. Laurain (In re Laurain)*, 113 F.3d 595, 597 (6th Cir. 1997) ("Statutes . . . must be read in a 'straightforward' and 'commonsense' manner."). A plain reading of Section 366(c)(2) makes clear that a debtor is required to provide adequate assurance of payment satisfactory to its utilities on or within thirty (30) days of the filing of the petition. If a debtor believes the **amount** of

the utility's request needs to be modified, then the debtor can file a motion under Section 366(c)(3) requesting the court to modify the **amount** of the utility's request under Section 366(c)(2).

In this case, the Debtors filed the Utility Motion to improperly shift the focus of their obligations under Section 366(c)(3) from modifying the amount of the adequate assurance of payment requested under Section 366(c)(2) to setting the form and amount of the adequate assurance of payment acceptable to the Debtors. Accordingly, this Court should not reward the Debtors for their failure to comply with the requirements of Section 366(c) and deny the Utility Motion as to the Utilities. *See In re Viking Offshore (USA), Inc.*, 2008 WL 782449 at *3 (Bankr. S.D. Tex. Mar. 20, 2008) ("The relief requested by Debtors would reverse the burden, by making an advance determination that the proposed assurance was adequate. . . . the court lacks the power to reverse the statutory framework for provision of adequate assurance of payment."); *see also In re Pilgrim's Pride Corporation*, Case No. 08-45664 (DML)(Docket No. 447), United States Bankruptcy Court For the Northern District of Texas, *Memorandum Order* entered on January 5, 2009 (Denying debtors' motion seeking to establish adequate assurance of payment); *see also In re Ramsey Holdings, Inc.*, Case No. 09-13998-M (TLM).

1. The Debtors' Proposed Bank Account Is Not Relevant And Even If It Is Considered, It Is Unsatisfactory Because It Does Not Provide the Utilities With Adequate Assurance of Payment.

This Court should not even consider the Bank Account as a form of adequate assurance of payment because: (1) It is not relevant because Section 366(c)(3) provides that a debtor can only modify "the amount of an assurance of payment under paragraph (2)"; and (2) The Bank Account is not a form of adequate assurance of payment recognized by Section 366(c)(1)(A). Although the cases cited by the Debtors in the Utility Motion approved a bank account as adequate assurance, they only did so by improperly ignoring the plain language of Section 366(c)(3) and Section 366(1)(A). Moreover, even if the Court were to consider the Bank Account, the Bank Account is an improper and otherwise unreliable form of adequate assurance of future payment for the following reasons:

i. It is underfunded from the outset because the Utilities are required by applicable law to issue monthly bills;

ii. Unlike the Debtors' professionals' Carve-Out, the Bank Account may not remain if the Debtors default on their post-petition financing; and

iii. The Bank Account is illusory because the proposed Final Utility Order provides that it will be eliminated before all of the Utilities' post-petition charges are paid in full.

Accordingly, the Court should not approve the Bank Account as adequate assurance to the Utilities because the Bank Account

is: (a) not the **form** of adequate assurance requested by the Utilities; (b) not a form recognized by Section 366(c)(1)(A); and (c) an otherwise unreliable form of adequate assurance.

2. The Utility Motion Should Be Denied As To the Utilities Because the Debtors Have Not Set Forth Any Basis For Modifying the Utilities' Requested Deposits.

In the Utility Motion, the Debtors fail to address why this Court should modify the amount of the Utilities' requests for adequate assurance of payment. Under Section 366(c)(3), the Debtors have the burden of proof as to whether the amounts of the Utilities' adequate assurance of payment requests should be modified. *See In re Stagecoach Enterprises, Inc.*, 1 B.R. 732, 734 (Bankr. M.D. Fla. 1979) (holding that the debtor, as the petitioning party at a Section 366 hearing, bears the burden of proof). However, the Debtors do not provide the Court with any evidence or factually supported documentation to explain why the amount of the Utilities' adequate assurance requests should be modified. Accordingly, the Court should deny the relief requested by Debtors in the Utility Motion and require the Debtors to comply with the requirements of Section 366(c) with respect to the Utilities.

B. THE COURT SHOULD ORDER THE DEBTORS TO PROVIDE THE ADEQUATE ASSURANCE OF PAYMENT REQUESTED BY THE UTILITIES PURSUANT TO SECTION 366 OF THE BANKRUPTCY CODE.

Section 366(c) was amended to overturn decisions such as *Virginia Electric and Power Company v. Caldor, Inc.*, 117 F.3d 646 (2d Cir. 1997), that held that an administrative expense, without more, could constitute adequate assurance of payment in certain cases. Section 366(c)(1)(A) specifically defines the forms that assurance of payment may take as follows:

> (i) a cash deposit;
> (ii) a letter of credit;
> (iii) a certificate of deposit;
> (iv) a surety bond;
> (v) a prepayment of utility consumption; or
> (vi) another form of security that is mutually agreed upon between the utility and the debtor or the trustee.

Section 366 of the Bankruptcy Code was enacted to balance a debtor's need for utility services from a provider that holds a monopoly on such services, with the need of the utility to ensure for itself and its rate payers that it receives payment for providing these essential services. *See In re Hanratty*, 907 F.2d 1418, 1424 (3d Cir. 1990). The deposit or other security "should bear a reasonable relationship to expected or anticipated utility consumption by a debtor." *In re Coastal Dry Dock & Repair Corp.*, 62 B.R. 879, 883 (Bankr. E.D.N.Y. 1986). In making such a determination, it is appropriate for the Court to consider "the length of time necessary for the utility to effect termination

once one billing cycle is missed." *In re Begley*, 760 F.2d 46, 49 (3d Cir. 1985). Based on the Debtors' anticipated utility consumption, the minimum period of time the Debtors could receive service from the Utilities before termination of service for non-payment of bills is approximately two (2) months or more. Moreover, even if the Debtors timely pay their post-petition utility bills, the Utilities still have potential exposure of 45 to 60 days based on their Tariff-mandated billing cycles. Furthermore, the amounts of the Utilities' deposit requests are the amounts that the applicable public service commission, which is a neutral third-party entity, permits the Utilities to request from their customers. Although the Utilities recognize that this Court is not bound by the applicable Tariffs, the Tariffs are extremely relevant information of a determination made by an independent entity on the appropriate amount of adequate assurance that should be paid to the Utilities. Accordingly, the amounts of the deposits requested by the Utilities are reasonable and should not be modified. *See In re Stagecoach*, 1 B.R. 732, 735-36 (Bankr. M.D. Fla. 1979) (holding that a two month deposit is appropriate where the debtor could receive sixty (60) days of service before termination of services because of the utilities' billing cycle.); *see also In the Matter of Robmac, Inc.*, 8 B.R. 1, 3-4 (Bankr. N.D. Ga. 1979).

In contrast, the Debtors fail to address in the Utility Motion why this Court should modify, if at all, the amounts of the Utilities' adequate assurance of payment requests, which is the Debtors' statutory burden. Instead, the Debtors merely ask this Court to approve their proposed form of adequate assurance of payment in the form of the two-week Bank Account. As set forth in Section A.1. above, the proposed Bank Account does not provide adequate assurance of payment to the Debtors' utility providers.

It is clear from the Critical Vendor Motion the type of creditors that the Debtors intend to favor with special treatment and the Utilities are not on that list. Moreover, unlike the "critical vendors" that are receiving preferential treatment in the Critical Vendors Motion, the Utilities are willing to continue to provide the Debtors with their generous trade terms established by the Tariffs or contracts (i.e. bills issued monthly in arrears with due dates 15 to 30 days thereafter) without requiring the Debtors to pay their prepetition claims in full at the outset of the case.

Furthermore, Debtors' counsel, who have access to inside information regarding the Debtors' operations, are not taking any chances regarding the payment of their post-petition charges because they are seeking to secure the payment of their fees through a $500,000 carve out. Accordingly, based on the

foregoing, the Debtors should be required to tender the deposits sought by the Utilities.

WHEREFORE, the Utilities respectfully request that this Court enter an order:

1. Denying the Utility Motion as to the Utilities;
2. Awarding the Utilities the post-petition adequate assurance of payment pursuant to Section 366 in the amount and form satisfactory to the Utilities; and
3. Providing such other and further relief as the Court deems just and appropriate.

Dated: February 11, 2013

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