

BANKRUPTCY UPDATE

Expert Analysis

Retailers Gymboree and Payless Again Seek Bankruptcy Relief

This issue of the Bankruptcy Update focuses on second bankruptcy filings, and particularly on recent bankruptcies of Gymboree and Payless. Both companies emerged from Chapter 11 protection in the last two years and now find themselves back in bankruptcy court. Unsurprisingly, both Gymboree and Payless have switched their reorganization strategies to focus on sales of significant portions of their assets.

Gymboree Group

On Jan. 17, 2019, children's clothing retailer Gymboree Group Inc. and affiliated debtors filed petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Eastern District of Virginia. *Gymboree Group Inc.* (Bankr. E.D. Va. Case No. 19-30258).

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The company is returning to bankruptcy court with a plan to liquidate a substantial portion of its footprint less than a year and a half after emerging from Chapter 11. This is in stark contrast to the 2017 proceeding wherein Gymboree restructured its debt obligations and kept its business intact. Gymboree's 2017 plan included the following key components: (1) \$171 million of unsecured notes were canceled; (2) approximately \$770 million of Gymboree's funded debt was converted to equity in the reorganized company; (3) \$80 million of new capital was raised via a rights offering; and (4) the company obtained \$285 million in exit financing.

Gymboree attributes its return to bankruptcy court to an unanticipated decline in the brick-and-mortar retail industry which left the company unable to handle operating costs and support its capital structure. Following its 2017 reorganization the company closed a number of underperforming locations,

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including all of its South Korean and Australian stores, and implemented new marketing programs. Nevertheless, retail sales declined 27 percent in 2018 leading the company to report a \$106 million loss by November 2018.

Gymboree entered bankruptcy with a \$30 million debtor-in-possession financing package from Special Situations Investing Group and Goldman Sachs Specialty Lending Holdings to finance its operations and sale process. SSIG would also

act as the stalking horse bidder with a credit bid in the amount of \$85 million for the company's 147-store Janie and Jack business as well as its intellectual property and e-commerce program. Contemporaneously, Gymboree sought authority to commence going-out-of-business sales at its 534 Gymboree and 264 Crazy 8 locations.

On March 5, 2019, Gymboree secured court approval to sell certain of its assets to the Gap and the Children's Place who collectively exceeded SSIG's \$85 million stalking horse credit bid and were deemed the highest and best bids at a March 1, 2019 auction. The Gap acquired the debtors' Janie and Jack chain for \$35 million while The Children's Place purchased the intellectual property, Internet domains and business data associated with the Gymboree and Crazy 8 brands for \$76 million.

Payless Holdings

On Feb. 18, 2019, shoe retailer Payless Holdings LLC and affiliated debtors filed petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Eastern District of Missouri. *Payless Holdings LLC* (Bankr. E.D. Mo. Case No. 19-40883).

Like Gymboree, Payless finds itself seeking bankruptcy protection for the second time in less than two years. Payless last sought bankruptcy relief in April 2017,

commencing Chapter 11 proceedings with almost \$850 million in debt and a restructuring support agreement that required immediate closure of 400 stores and an overall reduction of its brick-and-mortar presence. The company emerged from Chapter 11 four months later cutting approximately \$635 million in debt obligations and 675 stores.

Nevertheless, reductions achieved in Payless' last Chapter 11 case proved insufficient as the debtors were unable to shoulder their debt burden and support their large remaining footprint. Payless attributes its return to bankruptcy court to several issues, including inventory shortfalls in 2017 followed by oversupply in 2018 and an inability to effectively integrate their physical and online stores. Payless' North American stores had negative adjusted EBITDA of \$66 million in 2018, a drastic plunge from \$11 million EBITDA in 2017.

Concurrently with the bankruptcy filing, Payless sought approval of a consulting agreement with a joint venture of national liquidation firms comprised of Great American Group and Tiger Capital Group who will conduct liquidation sales at all U.S. brick-and-mortar locations while the company attempts to reorganize around its profitable Latin American and franchise business segments.

The debtors initially only sought permission to operate utilizing their pre-petition lenders' cash collateral. Subsequently, on Feb. 25, 2019, Payless obtained interim approval to enter into a \$25 million DIP financing facility with Wilmington Saving Funds Society FSB acting as DIP agent. The additional liquidity will be used to purchase additional discounted inventory to augment ongoing liquidation sales. Key milestones proposed under the DIP facility include a June 15, 2019 deadline to complete liquidation sales and a June 28, 2019 deadline to confirm a Chapter 11 plan. A hearing on final DIP financing approval, initially scheduled for March 14, 2019, was adjourned to March 28, 2019 following the recent appointment of an official committee of unsecured creditors.