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## **Sports Authority May Shape Future of Retailer Ch. 11**

By **Matt Chiappardi**

Law360, Wilmington (March 18, 2016, 5:29 PM ET) -- [Sports Authority's](#) bitter dispute with consignment sellers over proceeds has the potential to shape the role of vendors in retail Chapter 11s for years to come, and the results of the fight could send shocks to an already weak sector, bankruptcy experts say.

The conflict, which has thus far dominated the [two-week-old](#), \$1 billion case, centers on the proceeds reaped from the about \$85 million worth of consignment goods supplied by roughly 170 vendors.

The consignment vendors argue that the merchandise they've supplied, which accounts for 20 percent of the retail chain's business, is not property of Sports Authority's bankruptcy estate and that the portion of the proceeds they're due, based on their prepetition agreements with the debtor, should go back to them and not be used to satisfy lenders.

But Sports Authority is [challenging the vendors' rights](#) to those proceeds, launching a campaign of more than 160 adversary actions to that effect.

U.S. Bankruptcy Judge Mary F. Walrath has urged the sides to come to some sort of settlement, but if she has to rule, bankruptcy experts say her decision is poised to have a resounding impact not only on how vendors deal with their protections in Chapter 11 cases but also on the future of retailers' financing options and relationships with suppliers.

"If somebody has to walk the plank, it's going to have an effect on the industry one way or another," said Francis A. Monaco Jr., managing director at corporate restructuring firm Gavin/Solmonese.

One of Sports Authority's key drivers, Monaco said, is access to post-petition financing that is based on the value of its inventory. If lenders find out that bankruptcy law places their liens secondary to vendors in this situation, it could make them think twice about extending money and take a closer look at the inventory structure of retailers.

"If the decisions goes in favor of the banks, it means consignors will be cautious about this arrangement in the future and be much less willing to do it on this basis if they get even a whiff that the store is in trouble," Monaco said.

How closely aligned the positions of Sports Authority and its secured lenders — a group that includes [Bank of America](#), [Wells Fargo Bank](#) and [JPMorgan Chase Bank NA](#) — are in the campaign against the vendors raised the eyebrows of Melissa Jacoby, a bankruptcy law professor at the University of North Carolina School of Law.

Jacoby said that the adversary actions, lodged by the debtor, appear to be fighting on behalf of the secured lenders' interest and might be "emblematic of a process designed primarily to benefit" them.

"If this is part of a broader movement, as we see so many quick sales already and so many structured dismissals, then it shapes the strategy for next time around," Jacoby said.

If Sports Authority is successful in what amounts to a major litigation push, then that tactical stance is bound to be repeated in other cases and set up a new, perhaps more adversarial, model for dealing with vendors in Chapter 11. Moreover, the impact could spill out into the market, dulling vendors' appetite to deal with retailers without bringing on a host of other interest protections and adding more uncertainty to an industry already hurting from consumers' migration to online shopping.

"There is a cautionary tale for vendors here," Jacoby said. "They are extending credit, in essence, even if that's not how they see the deal. If vendors want to be more careful it will be harder for retailers to stay out of bankruptcy."

While Sports Authority is taking an aggressive posture, consignment vendors are also being equally steadfast in their opposition, and Matthew Bruckner, a professor at Howard University School of Law, says that if the clash goes the distance it will go a long way toward creating a framework for how these issues are dealt with going forward.

"There's just not a lot of case law out there in this area," Bruckner said. "This will be one of two major decisions on this issue."

The other major dispute came in the Whitehall Jewelers Inc. bankruptcy, also in Delaware in 2008, and that fight ended with a global settlement approved by U.S. Bankruptcy Judge Kevin Gross that had the proceeds on consignment goods go back to the vendors.

Bruckner added that vendors need to be cautious, especially if there does turn out to be faults in how their interests are perfected under Uniform Commercial Code standards. Under bankruptcy law, a debtor is entitled to sell whatever it has an interest in, and the real question becomes: How much of interest does Sports Authority actually have in the merchandise?

"Presumably, [the vendors] were happy to have Sports Authority sell their stuff," Bruckner said. "Why were they before and not after [the bankruptcy filing]? Is it because Sports Authority is in bankruptcy? Judges are not super-receptive to that argument."

To make matters even more complex, Judge Walrath is going to have to consider the adversary action under the patchwork of state law applications of the Uniform Commercial Code, which could lead to a bunch of diverging decisions, said Aaron M. Kaufman of Dykema [Cox Smith](#).

"Retail cases always bring out issues in the code," Kaufman said. "It's a new and novel issue and debtors have proceeded to press it."

In court, Sports Authority attorney Robert Klyman of [Gibson Dunn](#) has stressed that the adversary actions were not just boilerplate complaints but were tailored specifically to each vendor and to the issues surrounding the particular agreement.

If it does come to a ruling, or a group of rulings, it's very likely going to clarify issues in the Bankruptcy Code important for retail cases and shape those types of cases going forward, Kaufman said.

"Like any decision that comes out of Delaware, it's one we all will watch," he said.

--Editing by Jeremy Barker and Catherine Sum.