IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: ADVANCED MARKETING SERVICES, INC., a Delaware corporation, *et al.* Debtors.	Chapter 11 Case No. 06-11480 (CSS) (Jointly Administered)
SIMON & SCHUSTER, INC., Plaintiff, v. ADVANCED MARKETING SERVICES, INC., Defendant.	Adv. Proc. No. 07-50004 (CSS) RE: Docket Nos. 8-10 Hearing Date: January 17, 2007 at 2:00 p.m.

WELLS FARGO FOOTHILL'S ANSWERING BRIEF IN OPPOSITION TO THE EMERGENCY APPLICATION OF SIMON & SCHUSTER FOR TEMPORARY RESTRAINING ORDER PURSUANT TO BANKRUPTCY RULE 7065

Dated: January 17, 2007
Wilmington, Delaware

Kurt F. Gwynne (No. 3951)
Kimberly E. C. Lawson (No. 3966)
REED SMITH LLP
1201 Market Street, Suite 1500
Wilmington, DE 19899
Telephone: (302) 778-7500
Facsimile: (302) 778-7575
E-mail: kgwynne@reedsmith.com
klawson@reedsmith.com

-and-

Paul S. Arrow
BUCHALTER NEMER
1000 Wilshire Blvd., 15th Floor
Los Angeles, CA 90017
Telephone: (213) 891-0700
Facsimile (213) 896-0400
Email: parrow@buchalter.com

Counsel for Wells Fargo Foothill

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I. NATURE AND STAGE OF PROCEEDINGS

On December 29, 2006 (the "Petition Date"), Advanced Marketing Services, Inc. (the "Debtor" or "Defendant") filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code, 11 U.S.C. §§ 101 *et seq.* (the "Bankruptcy Code"). On the Petition Date, Simon & Schuster ("Simon") apparently sent a reclamation demand to the Debtor. On January 5, 2007, Simon filed the Complaint for Reclamation of Goods Pursuant to 11 U.S.C. § 546(c) and Related Relief (D.I. 1) (the "Complaint") and commenced the above captioned adversary proceeding against the Debtor. On January 11, 2007, Simon filed its Emergency Application of Simon & Schuster for Temporary Restraining Order Pursuant to Bankruptcy Rule 7065 (D.I. 8) (the "Application"). The Court set a hearing on the Application for January 17, 2007 at 2:00 p.m. and an objection deadline of 10:00 a.m. on January 17, 2007.

Having waited nearly two weeks after making its reclamation demand to file the Application, and having failed to serve or join the lenders in its action (even though it seeks control over, and ultimately possession of, the lenders' collateral), Simon now runs into Court screaming that it needs emergency relief.

II. SUMMARY OF ARGUMENT[1]

As demonstrated in detail below, the Application is rife with legal flaws, factual inaccuracies, and logical leaps. In sum, the Application must be denied for at least the following reasons, each of which is sufficient by itself to defeat Simon's claims.

1. Simon's right of reclamation is nothing more than a rescissional remedy. It is not a lien or security interest. As Simon admits, its rescissional right of reclamation is subject and subordinate to the lenders' prepetition liens. At the same time, Simon urges the Court to ignore that determinative fact, suggesting that the prepetition advances may be soon be repaid. Whether the prepetition advances may at some future time be repaid does not help Simon obtain an injunction today. Simon simply cannot justify the need for emergency injunctive relief based on something that may (or may not) happen in the future. Simon tries to gloss over this fatal flaw in its argument by suggesting that the lenders' oversecured status somehow justifies relief. That is wrong as a matter of law. The reclamation cases are clear that a secured creditor cannot be forced to marshal regardless of whether there is equity in its collateral. Marshaling is also precluded under the postpetition loan agreement. Simon would not be entitled to reclaim its goods under applicable nonbankruptcy law, and its rights are no greater in the Debtors' chapter 11 bankruptcy.

2. Simon also ignores the fact that the lenders' prepetition liens also secure the postpetition advances. The postpetition loan agreement provides that all prepetition liens granted to the lenders are preserved in favor of the postpetition lenders in order to

[1] The Lenders reserve their right to challenge Simon's case in chief at the hearing on the Application, including without limitation, whether the Debtors are insolvent and whether Simon's claim is otherwise valid under applicable law. Simon bears the burden of proving its entitlement to a reclamation claim. See, e.g., *Allegiance Healthcare Corp. v. Primary Health Sys., Inc. (In re Primary Health Sys., Inc.)*, 258 B.R. 111, 114 (Bankr. D. Del. 2001).

secure the postpetition advances. Thus, Simon's reclamation rights are subject and subordinate to the aggregate outstanding advances under the prepetition and postpetition agreements. Today, that aggregate amount is at least $26,649,000 (including interest and fees), far in excess of the value of Simon's reclamation demand.

3. Simon further ignores the fact that its reclamation claims are subject and subordinate to the lenders' postpetition liens. The interim order approving Debtors' postpetition financing provides that the postpetition liens granted to the lenders are first and senior in priority to all other interests and liens of every kind and nature. The limited exception to that broad grant of priority for liens existing at the petition date cannot help Simon. First, Simon admits that its rescissional reclamation right is not a security interest or a lien. That is correct because its right does not secure repayment of a debt, but rather permits Simon, under appropriate circumstances, to rescind the sale of its goods and recover them. Moreover, even if Simon could be granted a lien under Section 546(c) of the Bankruptcy Code, Simon still does not fall within the limited exception because it had no such lien as of the time Debtors commenced these cases.

4. Simon ignores the fact that its reclamation claims are subject and subordinate to the lenders adequate protection liens. In exchange for the use of its cash collateral, the interim financing order provides the lenders with adequate protection liens to protect against any diminution in the value of their collateral. The adequate protection liens enjoy the same priority as the prepetition liens to which they apply. Indeed, adequate protection liens would hardly adequately protect the lenders' interests if their priority was altered because that would permit later claims, just like Simon's reclamation claims, to leap ahead.

5. Simon's reclamation claims are valueless. A reclamation claim is valueless where its value does not exceed the secured claim of a lender with a prior right to the reclaimed goods. Simon's reclamation claim is dwarfed by the lenders' secured claims. As a result, not only is Simon not entitled to recover the underlying goods (and hence not entitled to an injunction), it is also not entitled to any other relief, whether an administrative claim, lien, or any other compensation on account of its claims (whether under the Debtors' proposed reclamation procedures or otherwise).

6. In the event that despite above arguments the Court nonetheless grants the Application, Simon must post a bond to protect the Lenders' interests. The Third Circuit mandates a bond when an injunction is granted. Since any injunction would adversely affect the lenders' collateral, any bond posted by Simon must be protective of the lenders' interests and well as the Debtors' interests.

III. STATEMENT OF FACTS

Prior to the Petition Date, Debtors and Foothill (as agent and lender), along with other lender parties (collectively, the "Prepetition Lenders"), were parties to that certain Loan and Security Agreement dated as of April 27, 2004 (the "Prepetition Loan Agreement"). In order to ensure repayment of the obligations under the Prepetition Loan Agreement, Debtors granted Lenders a security interests in substantially all of their assets (the "Prepetition Liens"), including without limitation the Debtors' inventory. The Prepetition Liens are valid, perfected and fully enforceable. The assets encumbered by the Prepetition Liens include the goods with respect to which the Application seeks a temporary restraining order (the "TRO").

On January 3, 2007 the Court entered its Interim Order (the "Interim Order") approving that certain Amended and Restated Loan and Security Agreement dated as of January 3, 2007 (the "DIP Loan Agreement") between Debtors and the same parties that comprise the Prepetition Lenders (the "Postpetition Lenders").[2] In order to ensure repayment of the obligations under the DIP Loan Agreement, Debtors granted Lenders a security interests in substantially all of their assets, including their pre and post petition assets (the "Postpetition Liens"). The assets encumbered by the Postpetition Liens also include the goods with respect to which the Application seeks a TRO.

Pursuant to Section 3.1.3 of the Interim Order, with a very limited exception for certain permitted liens, the Postpetition Liens enjoy broad priority over all other clams, liens and interests:

> The Postpetition Liens shall be and shall continue to be at all times first and senior in priority to all other interests and liens of every kind and nature, whether created consensually, by an order of any court including this Court, or otherwise, including without limitation liens or interests granted in favor of any other person or entity in conjunction with section 363, 364, or any other section of the Bankruptcy Code; provided, however, that the Postpetition Liens shall not prime and shall be subject and junior to those Prepetition Liens that were valid and existing as of the Petition Date.

In addition, pursuant to the Interim Order, the Lenders were granted adequate protection liens in all collateral (both prepetition and postpetition) in order to protect them against any diminution in the value of their collateral (the "Adequate Protection Liens"). Specifically, Section 3.1.2 provides that "Lender and Senior Lender shall have and is [sic] hereby granted a Postpetition Adequate Protection Lien on all Collateral."

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[2] The Prepetition Lenders and the Postpetition Lenders will be referred to collectively as the "Lenders".

Moreover, the Adequate Protection Liens enjoy the same priority as the Prepetition Liens to which they relate. Interim Order, Section 3.1.3.2.

The DIP Loan Agreement also provides that the Prepetition Liens granted to the Prepetition Lenders continue in full force and effect, and secure repayment of all obligations owed to the Postpetition Lenders under the DIP Loan Agreement. Specifically, Section 17.10 provides that:

> Each Borrower hereby ratifies, adopts, confirms and agrees that (i) the Senior Agreement and each document comprising the Senior Facility is, and shall continue to be, in full force and effect and is hereby ratified and confirmed in all respects in relation to this Agreement except that on and after the Closing Date all references in any such document comprising the Senior Facility to "the Agreement", "thereto", "thereof", "thereunder" or words of like import referring to the Senior Agreement shall mean this Agreement; and (ii) *to the extent that any such document comprising the Senior Facility purports to assign or pledge to the Senior Agent for the benefit of the Senior Lenders a security interest in or lien on, any collateral as security for the Senior Obligations, such pledge, assignment or grant of the security interest or lien is hereby ratified and confirmed in all respects in favor of Agent for the benefit of Lenders in connection with this Agreement and the Loan Documents to secure the Obligations.*

DIP Loan Agreement at § 17.10 (emphasis added).

According to the Application, Simon sent its reclamation demand to Debtors on the Petition Date. Foothill is informed and believes that the demand was made after Debtors filed their petitions commencing these cases. On January 5, 2007 Simon filed its Complaint seeking, among other things, return of goods allegedly delivered to Debtors within the 45 days before the Petition Date. Despite the fact that Simon seeks control over, and ultimately possession of, Foothill's collateral, Simon failed to join Foothill in the action, or even serve it with its papers. On January 11, nearly two weeks after its

initial demand, Simon filed the Application (which likewise was not served on Foothill) seeking an "emergency" hearing.

IV. ARGUMENT

A. The Application Must Be Denied Because Claimant Cannot Not Prevail On The Merits.[3]

1. Reclamation Rights Are Subject To The Prior Rights Of A Secured Creditor.

A seller's right to reclamation in bankruptcy arises under section 546(c) of the Bankruptcy Code. Prior to the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), section 546(c) of the Bankruptcy Code expressly grounded a seller's right of reclamation in nonbankruptcy law. Typically, the nonbankruptcy statutory basis of a seller's right to reclaim is a state's version of section 2-702 of the UCC. Of note, section 2-702(3) of the UCC subjects "the seller's right to reclaim ... to the rights of a buyer in ordinary course of business or other good faith purchaser for value ...." It is well settled that a secured creditor with a lien on the goods to be reclaimed qualifies as a "good faith purchaser for value" of those goods within the meaning of section 2-702(3) of the UCC. See, e.g., *Galey & Lord, Inc. v. Arley Corp.* (In re *Arlco Inc.*), 239 B.R. 216, 267-68 (Bankr. S.D.N.Y. 1999) (stating that "[m]ost courts have treated a holder of a prior perfected, floating lien on inventory ... as a good faith purchaser with rights superior to those of a reclaiming seller" and collecting

[3] Foothill believes that the Application should be denied for many reasons in addition to those set forth here. Foothill leaves those additional arguments to the Debtors.

cases demonstrating the majority rule) (quotation omitted); *In re Victory Markets,* 212 BR. 738, 742 (Bankr. N.D.N.Y. 1997) (same). Accordingly, under applicable state law reclamation principles (which were incorporated into the pre-BAPCPA version of section 546(c) of the Bankruptcy Code), the prior lien defense is a viable defense to the right of a seller seeking to reclaim goods.

As amended by BAPCPA, section 546(c) of the Bankruptcy Code no longer expressly references and incorporates nonbankruptcy law. Under the amended version of section 546(c) of the Bankruptcy Code, however, a reclaiming seller's subordination to the prior rights of a holder of a security interest in the reclaimed goods has now been made explicit in the federal statute itself. See 11 U.S.C. § 546(c) (expressly stating that a reclaiming creditor's rights in bankruptcy are "subject to the prior rights of a holder of a security interest in such goods or the proceeds thereof...."). Accordingly, while section 546(c) has been amended to delete the explicit reference to nonbankruptcy law, the corresponding addition of express language subjecting reclamation rights to prior liens makes clear that prior lien defense continues to apply to reclamation claims asserted under the Bankruptcy Code, regardless of whether the current version of Section 546(c) incorporates state law or creates a federal reclamation right.

In fact, Foothill submits that both sources of law apply post-BAPCPA, This is because the language of section 546(c) of the Bankruptcy Code now is phrased in the form of a reservation of rights: the reclaiming seller possesses certain rights "subject to the prior rights of a holder of a security interest in such goods." (emphasis added) As the Bankruptcy Code otherwise gives no indication of what those "prior rights" might be, the only available referent for such "prior rights" is nonbankruptcy law. Foothill

accordingly submit that section 546(c) of the Bankruptcy Code, as revised by BAPCPA, preserves nonbankruptcy law with respect to the Prior Lien Defense. See, e.g., 5 *Collier on Bankruptcy* ¶ 546.04[21][a][vii] (15th ed. rev. 2006) (stating that "[u]sing prior versions of section 546(c)(l) as a guide, this provision appears intended to state that the seller's reclamation rights remain 'subject to' the secured creditor's rights."). Indeed, nothing in the legislative history suggests otherwise. Ultimately, however it matters little to the issues addressed here whether the source of law for determining the validity of reclamation claims is state or federal law. Either way, such claims remain subject and subordinate to prior liens.

2. The Reclamation Claims Are Subject To The Prepetition Liens.

As discussed above, prior to the Petition Date, Debtors and the Prepetition Lenders were parties to the Prepetition Loan Agreement. In order to ensure repayment of the obligations under the Prepetition Loan Agreement, Debtors granted the Prepetition Lenders a security interests in substantially all of their assets, including without limitation, their inventory. The Prepetition Liens are valid, perfected and fully enforceable. The assets encumbered by the Prepetition Liens include the goods with respect to which the Application seeks the TRO. As of the Petition Date, the prepetition obligations totaled approximately $41 million. As of this date, the Prepetition Lenders are still owed approximately $13,017,000 on account of prepetition obligations.

Simon urges the Court to ignore that determinative fact, suggesting that the prepetition advances may soon be repaid. Whether the prepetition advances may at some future time be repaid does not help Simon obtain an injunction today. As

mentioned above, Simon simply cannot justify the need for emergency injunctive relief based on something that may (or may not) happen in the future.

Simon tries to gloss over this fatal flaw in its argument by suggesting that the lenders' oversecured status somehow justifies relief. Yet, that does not help Simon. See *Yenkin-Majestic Paint Corp. v. Wheeling-Pittsburgh Steel Corp. (In re Pittsburgh-Canfield Corp.)*, 309 B.R. 277, 291-92 (B.A.P. 6th Cir. 2004) (stating that the reclaiming seller was entitled to recovery "only to the extent that the value of the *specific inventory* in which the reclaiming seller asserts an interest exceeds the amount of the floating lien in the debtor's inventory" and finding that the bankruptcy court did not abuse its discretion in holding that seller's reclamation claims aggregating $450,000 were valueless where the substantially oversecured prepetition lender was owed $130 million) (emphasis added).

This result makes sense because a reclamation claimant has no lien and, therefore, no right to demand that a holder of a prior lien marshal the debtor's assets in a manner favorable to the reclamation claimant. *In re Pittsburgh-Canfield Corp.* 305 B.R. 688, 693 (Bankr. N.D.Ohio 2003), (reclaiming creditors have "no right to invoke the equitable doctrine of marshaling, because each of the Vendors is unsecured as to its reclamation claim"), *aff'd*, 309 B.R. 277 (B.A.P. 6th Cir. 2004); *Arlco*, 239 B.R. at 273 and 276-77 (marshaling was inappropriate because the reclaiming seller was not a secured creditor and, therefore, was not entitled to marshaling); *In re Quality Stores, Inc.*, 289 B.R. 324, 340 (Bankr. W.D.Mich. 2003) (reclamation creditors' marshaling argument would be "futile"). While junior secured creditors sometimes have the right to require the marshaling of collateral under applicable law, courts have "denie[d]

unsecured creditors standing to invoke the doctrine of marshaling." *In re Gibson Group, Inc.*, 151 B.R. 133, 134-35 (Bankr. S.D. Ohio 1993); see also *U.S. v. Herman*, 310 F.2d 846, 848 (2d Cir. 1962) (denying even junior lienholder any right to require marshaling of assets where doing so would inconvenience senior lienholder).

If that were not enough, the Interim Order prohibits marshaling. Section 4.5 of the order provides that "[n]either Lender nor the Collateral shall be subject to the doctrine of marshaling." Collateral in that context means all of the Debtors prepetition and postpetition assets.

Thus, any reclamation right that Simon may have is subject and subordinate to the Lenders' Prepetition Liens. In addition, absent the right to direct the Lenders to satisfy their claims out of goods other than the goods in which Simon alleges its reclamation claim, Simon cannot enforce its rights to reclaim their specific goods.

3. The Prepetition Liens Also Secure Postpetition Advances.

Simon ignores the fact that the Prepetition Liens also secure the postpetition advances. Section 17.10 of the DIP Loan Agreement (set forth above) provides that all Prepetition Liens granted to the Prepetition Lenders are preserved in favor of the Postpetition Lenders in order to secure the postpetition advances under the DIP Loan Agreement.

In *Pittsburgh-Canfield*, the panel found "of significant importance" the fact that ". . . the liens and security interests of the Prepetition Lenders were assigned and transferred . . . to the Lenders under the DIP Facility . . . ." 305 B.R. at 282. See also *In re Phar-Mor*, 301 B.R. 482 (N.D. Ohio 2003) (citing its own opinion in

Pittsburgh-Canfield to underscore the determinative nature of an assignment of the prepetition liens to the postpetition lender, a critical factor lacking in, and leading to, the decision in *Phar-Mor* that the reclamation claims had some value and should be accorded priority claims.); Cf. *In re Kravitz*, 278 F.2d 820, 822 & n.3 (3d Cir. 1960) ("the seller's right of rescission is not an absolute right at all but is subject to the right of a lien creditor who extended credit" and noting that "[w]e do not think that the principle that a reclamation seller's interest is subordinate to that of a lien creditor who extended credit subsequent to the sale is 'displaced by the particular provisions' of Section 2-702").

Thus, Simon's reclamation rights are subject and subordinate to the aggregate outstanding advances under the prepetition and postpetition agreements. Today, that aggregate amount is $26,649,000, far in excess of the value of Simon's reclamation demand.

4. The Reclamation Claims Are Subject To The Lenders' Postpetition Liens

As discussed above, in order to ensure repayment of the obligations under the DIP Loan Agreement, Debtors granted the Postpetition Lenders a security interests in substantially all of their assets, including their prepetition and post petition assets. The assets encumbered by the Postpetition Liens also include the goods with respect to which the Application seeks a TRO. As set forth above, under Section 3.1.3 of the Interim Order, with a very limited exception, the Postpetition Liens enjoy broad priority over virtually all other clams, liens and interests. The limited exception to the broad mandate of seniority for prepetition liens existing as of the Petition Date is not applicable to Simon's claims.

To begin with, reclamation rights are not security interests or liens. Simon admitted as much in the Application by arguing that the new version of Bankruptcy Code section 546(c) "specifically divested the court of the authority contained in the previous version of the statute to deny a reclamation claim where the seller is granted a replacement lien or administrative claim. *The only remedy available under the current statute is reclamation of the specific goods by the seller.*" Application Para. 16 (emphasis added).

Moreover, case law supports the notion that a reclamation claim is not a security interest or lien, but rather is only a rescissional remedy. *Pittsburgh-Canfield Corp.*, 309 B.R. at 284 ("The right of reclamation is a rescissional remedy, based on the theory that the seller has been defrauded."); *Pittsburgh-Canfield Corp.*, 305 B.R. at 693 ("a reclamation right is not a lien or security interest"); *In re PFA Farmers Market Ass'n*, 583 F.2d 992, 1003 n.17 (8th Cir. 1978) (right of reclamation is not a lien); *Arlco*, 239 B.R. at 274 (right of reclamation is not a lien); *Guy Martin Buick, Inc. v. Colorado Springs National Bank*, 519 P.2d 354 (1974) ("§ 2-507(2) is "a right to undo the transaction, not a right to 'secure' payment of the price as required by the definition of a 'security interest.'"). This makes sense because, again as Simon admits, a reclamation rights does not secure payment of a debt, but rather permits the claimant, under appropriate circumstances, to recover the actual goods. In light of the BAPCPA's elimination of any reclamation claimant's right to a lien (or an administrative expense claim), it cannot reasonably be disputed that Simon had no prepetition lien *and* bas no right to obtain a post-petition lien under Section 546(c).

Finally, even if a reclamation right could be construed as a lien right, Simon's right did not exist as of the Petition Date, thus excluding it from the limited exception to the primacy of the Postpetition Liens. As mentioned above, the Lenders are informed and believe that Simon's reclamation demand was made after Debtors commenced these cases. Therefore, any rights they may have did not exist as of the petition date. See e.g. *Phar-Mor*, 301 B.R. at 497 (date reclamation rights are asserted is the operative date for determination of relative rights).

For all of theses reason, Simon's reclamation rights are subject and subordinate to the Postpetition Liens.

5. The Reclamation Claims Are Subject To The Lenders' Adequate Protection Liens.

Simon ignores the fact that its reclamation claims are subject and subordinate to the Lenders' adequate protection liens. In exchange for the use of their cash collateral, the Interim Order provides the Lenders with adequate protection liens to protect against any diminution in the value of their collateral. The adequate protection liens granted to the Lenders enjoy the same priority as the Prepetition Liens to which they apply. Interim Order, Section 3.1.3.2; *In re Sun Healthcare Group, Inc.*, 245 B.R. 779, 781 (Bankr. D.Del. 2000) (noting that the "First Day Order also permitted the Debtors to use their cash collateral and granted to any party having a pre-petition lien in cash collateral replacement liens in post-petition collateral of the same type and priority, to the extent the use of cash collateral resulted in a diminution in the value of the pre-petition collateral."). Adequate protection liens would hardly adequately protect the Lenders' interests if their priority was altered because that would permit later claims, just like Simon's reclamation claims, to leap ahead.

6. The Reclamation Claims Are "Valueless."

As described above, section 546(c) of the Bankruptcy Code preserves nonbankruptcy law with respect to the primacy of prior liens. Thus, Simon, whose reclamation rights are subordinated to the rights of the Lenders, is not entitled to a recovery on account of reclamation claims greater than the recovery that would be available to it under nonbankruptcy law. See, e.g., *Toshiba Am., Inc. v. Video King of Illinois, Inc. (In re Video King of Illinois, Inc.)*, 100 B.R. 1008, 1017 (Bankr. N.D. Ill. 1989) (A seller's reclamation rights "would be valueless outside of bankruptcy because the goods in question for whatever reason would go first to satisfy [the secured lender's] claim, those rights are equally valueless in the bankruptcy context."); *Victory Markets*, 212 B.R. at 743 ("If the goods of the seller would be filly used to satisfy the lien of the superior lien creditor, the seller's right of reclamation would be valueless" and that a reclaiming seller is "required to show that its claim has value beyond the claims of the priority secured lienholders."). Because a reclamation claim is valueless outside of bankruptcy where its value does not exceed the secured claim of a lender with a prior right to the reclaimed goods, Simon's reclamation claim (which is dwarfed by the obligations owed to the Lenders) are similarly valueless inside the Debtors' chapter 11 cases.

A review of applicable nonbankruptcy law makes clear that Simon would have no reclamation rights outside of chapter 11. First, under applicable nonbankruptcy law, the right of reclamation is an *in rem* right of rescission. Thus, a reclaiming seller is obliged to satisfy its reclamation claims only out of the specific goods to be reclaimed. See *Pittsburgh-Canfield Corp.* 309 B.R. at 287-88 (stating that "a

seller's right to reclaim goods ... only extends to the particular goods it sold to the buyer") (quoting *In re Bridge Information Sys., Inc.*, 288 BR. 133, 138 (Bankr. E.D. Mo. 2001)); *Action Indus., Inc. (Dollarama) v. Dixie Enters., Inc. (In re Dixie Enters., Inc.,)*, 22 B.R. 855, 859 (Bankr. S.D. Ohio 1982) ("A right to reclamation is literally an *in rem* right.").

Because a reclamation claim must be satisfied out of the specific goods being reclaimed, where the value of a secured lender's claim exceeds the value of *a seller's individual reclamation claim*, the reclamation claim is valueless. See, e.g., *Allegiance Healthcare Corp. v. Primary Health Sys., Inc. (In re Primary Health Sys., Inc.)*, 258 B.R. 111, 117-18 (Bankr. D. Del. 2001) ("A reclaiming seller would not have been able to reclaim its goods if *the goods* were not worth more than the value of the floating lien") (emphasis added); *Arlco*, 239 B.R. at 272 ("It is only when *the reclaiming seller's goods* or traceable proceeds from those goods are in excess of the value of the superior claimant's claim that the reclaiming seller will be allowed either to reclaim the goods or receive an administrative claim or lien in an amount equal to the goods that remain after the superior claim has been paid.") (emphasis added); see also *Pittsburgh-Canfield Corp.*, 309 B.R. at 287. As demonstrated above, the fact that the holder of a prior security interest in reclaimed goods may be oversecured after taking into account other collateral does not alter the foregoing analysis.

As stated above, the aggregate indebtedness owed to the Lenders (all of which is senior to Simon's reclamation claim), totals approximately $26,649,000 today. By contrast, the total reclamation claim alleged by Simon is only approximately

$6 million. Because the senior secured indebtedness exceeds (by a large margin) the alleged value of Simon's claim, Simon's reclamation claim is valueless.[4]

B. If The Court Grants The Application, Foothill's Interest Must Be Protected By A Bond.

Simon cavalierly suggests that the Court dispense with the requirement that it post a bond pursuant to Bankruptcy Rule 7065(c). Yet, the posting of such a bond is *mandatory* in the Third Circuit. On its face, the language of Rule 65(c) "admits no exception" and, in fact, the Third Circuit Court of Appeals has "interpreted the bond requirement very strictly." *Hoxworth v. Blinder, Robinson & Co.*, 903 F.2d 186, 210 (3d. Cir 1990) (citing *Atomic Oil Co. v. Bardahl Oil Co.*, 419 F.2d 1097, 1100 (10th Cir. 1969) ("Rule 65(c) states in mandatory language that the giving of security is an absolute condition precedent to the issuance of a preliminary injunction."), *cert. denied*, 397 U.S. 1063 (1970)). The Third Circuit has acknowledged that "important policies undergird[] a strict application of the bond requirement." *Instant Air Freight Co. v. C.F. Air Freight, Inc.*, 882 F.2d 797, 805-06 n.9 (3d Cir. 1989); see also *Hoxworth,* 903 F.2d at 210. A "bond provides a fund to use to compensate incorrectly enjoined defendants." *Instant Air*, 882 F.2d at 804; *Hoxworth*, 903 F.2d at 210. A bond also "deters rash applications for interlocutory orders; the bond premium and the chance of liability on it cause plaintiff

[4] "Any seeming unfairness to [the sellers] ... is illusory, for the sellers could have protected their interests, even as against [a secured party's] prior perfected interest, if they had merely complied with the U.C.C.'s purchase money provisions. The [UCC] favors purchase-money financing, and encourages it by granting to a seller of goods the power to defeat prior liens. The seller at most need only (1) file a financing statement and (2) notify the prior secured party of its interest before delivery of the new inventory. The procedure [to perfect such liens] is not unduly complex or cumbersome. But whether cumbersome or not, a [seller] who chooses to ignore its provisions takes a calculated risk that a loss will result." *In re Samuels & Co., Inc.*, 526 F.2d 1238, 1247-48 (5th Cir.), *cert. denied sub nom. Stowers v. Mahon*, 429 U.S. 834 (1976).

to think carefully beforehand." *Instant Air*, 882 F.2d at 804. A bond is important because a defendant wrongfully enjoined has recourse only against the bond. *W.R. Grace & Co. v. Local Union 759, Etc.*, 461 U.S. 757, 770 n.14 (1983); *Frank's GMC Truck Ctr., Inc. v. GMC*, 847 F.2d 100, 103 n.5 (1988). Moreover, any bond must protect the Lenders' interests. Since any injunction would adversely affect the Lenders' collateral, any bond posted by Simon must be protective of the Lenders' interests and well as the Debtors' interests.

V. CONCLUSION

Simon has forced the Debtors and the Lenders to turn away from the many pressing issues in these cases to address its ill-conceived Application on an emergency basis. For each of the reasons set forth above, the Lenders urge the Court to deny the Application. In fact, the Court should go one step further and rule that Simon's reclamation claims are valueless.

Dated: January 17, 2007
Wilmington, Delaware

Respectfully submitted,

REED SMITH LLP

By: /s/ Kimberly E. C. Lawson
Kurt F. Gwynne (No. 3951)
Kimberly E. C. Lawson (No. 3966)
1201 Market Street, Suite 1500
Wilmington, Delaware 19801
Telephone: (302) 778-7500
Facsimile: (302) 778-7575
Email: kgwynne@reedsmith.com
klawson@reedsmith.com

-and-

Paul S. Arrow
BUCHALTER NEMER
1000 Wilshire Blvd., 15th Floor
Los Angeles, CA 90017
Telephone: (213) 891-0700
Facsimile (213) 896-0400
Email: parrow@buchalter.com

Counsel for Wells Fargo Foothill

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: ADVANCED MARKETING SERVICES, INC., a Delaware corporation, *et al.* Debtors.	Chapter 11 Case No. 06-11480 (CSS) (Jointly Administered)
SIMON & SCHUSTER, INC., Plaintiff, v. ADVANCED MARKETING SERVICES, INC., Defendant.	Adv. Proc. No. 07-50004 (CSS) RE: Docket Nos. 8-10 Hearing Date: January 17, 2007 at 2:00 p.m.

CERTIFICATE OF SERVICE

I, Kimberly E. C. Lawson, Esquire, certify that I am over 18 years of age and that on this 17th day of January, 2007, I caused a true and correct copy of the **WELLS FARGO FOOTHILL'S ANSWERING BRIEF IN OPPOSITION TO THE EMERGENCY APPLICATION OF SIMON & SCHUSTER FOR TEMPORARY RESTRAINING ORDER PURSUANT TO BANKRUPTCY RULE 7065** to be served upon the parties on the attached service list in the manner indicated.

By: /s/ Kimberly E. C. Lawson
Kimberly E. C. Lawson (No. 3966)

SERVICE LIST

VIA HAND DELIVERY & ELECTRONIC MAIL
Mark Minuti, Esq.
Jeremy W. Ryan, Esq.
Saul Ewing LLP
222 Delaware Avenue
Suite 1200
Wilmington, DE 19801
mminuti@saul.com
jryan@saul.com
(Counsel to Plaintiff)

VIA HAND DELIVERY & ELECTRONIC MAIL
Mark D. Collins, Esq.
Paul N. Heath, Esq.
Chun I. Jang, Esq.
Richards Layton & Finger, P.A.
920 N. King Street
Wilmington, DE 19801
collins@rlf.com
heath@rfl.com
jang@rlf.com
(Counsel to Debtors)

VIA FIRST CLASS & ELECTRONIC MAIL
Craig A. Wolfe, Esq.
Robert L. LeHane, Esq.
Kelley Drye & Warrant
101 Park Avenue
New York, NY 10178
cwolfe@kelleydrye.com
rlehane@kelleydrye.com
(Counsel to Plaintiff)

VIA FIRST CLASS & ELECTRONIC MAIL
Sussanne S. Uhland, Esq.
Austin K. Barron, Esq.
Alexandra B. Feldman, Esq.
O'Melveny & Myers, LLP
275 Battery Street
San Francisco, CA 94111-3305
suhland@omm.com
abarron@omm.com
afeldman@omm.com
(Counsel to Debtors)