

TAX CONSEQUENCES OF THE BANKRUPTCY OF SEARS HOLDINGS CORPORATION

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When Kmart Holding Corporation acquired Sears, Roebuck and Co. in 2005, the resulting new company, Sears Holdings Corporation (Old Sears), became the third largest retailer in the U.S. operating about 3,800 retail stores in the U.S. and Canada with annual revenue of approximately \$55 billion. It was *“the leading home appliance retailer and a leader in tools, lawn and garden, home electronics and automotive repair and maintenance.”*¹ Old Sears’ brands and products included Kenmore, Craftsman, DieHard, Lands’ End, Jaclyn Smith, Joe Boxer, and Martha Stewart Everyday (see Exhibit 1). By October 2018, Old Sears operated 687 retail stores and employed about 68,000 individuals. Its total revenue had declined to \$16.7 billion.² Old Sears had about \$7 billion in assets, \$11.3 billion in liabilities, and more than 300,000 creditors.³ On October 15, 2018, Old Sears filed a voluntary petition for relief under Chapter 11 of the U.S. Bankruptcy Code.⁴

Exhibit 1. Sears Storefront

Source: YouTube https://www.youtube.com/watch?v=rcBS-yau0_o



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On February 11, 2019, one of Sears’ largest creditors and shareholders, the hedge fund ESL Investments, Inc. (ESL), through its affiliate, Transform Holdco, LLC (New Sears), acquired substantially all of Old Sears’ go-forward retail footprint and component businesses of Old Sears on a going concern basis. New Sears assumed certain of Old Sears’ liabilities for approximately \$5.2 billion.⁵ What would have been the U.S. tax and non-tax consequences of Old Sears’ bankruptcy reorganization for Old Sears, Old Sears’ creditors and shareholders, and New Sears?

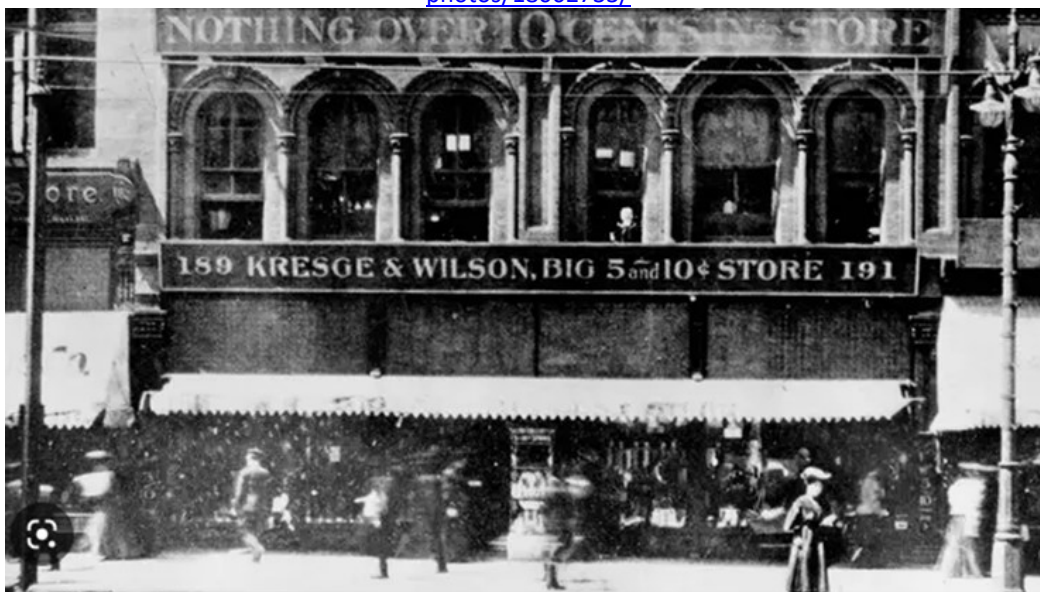
History of Kmart Holding Corporation

In 1899, Sebastian Spering Kresge founded the S.S. Kresge Company (Kresge) and opened his first five-and-dime store in Detroit, Michigan selling everything for 5 or 10 cents (see Exhibit 2). By 1912, Kresge had expanded to 85 stores with annual sales of over \$10 million. Kresge became a publicly traded company on the New York Stock Exchange (NYSE) in 1918. By the mid-1920s, Kresge was opening stores that sold items for \$1 or less.

Exhibit 2. S.S. Kresge Variety Store in Madison, Wisconsin

Source: Detroit Free Press

<https://www.freep.com/picture-gallery/money/business/2014/10/28/kresge-and-kmart-historical-photos/18062733/>



In 1962, Kresge opened its first Kmart discount department store in Garden City, Michigan. A few years later, sales from 162 Kmart stores and 753 Kresge stores were approximately \$1 billion.⁶ In 1977, Kresge changed its name to Kmart Corporation (Kmart) and began trading on the NYSE under the symbol KM.⁷ See Exhibit 3.

After struggling for several years to compete with retailers such as Wal-Mart Stores, Inc. and Target Corp., on January 22, 2002, Kmart filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code.⁸ After Kmart filed for bankruptcy protection, ESL, founded in 1988 by Chairman and CEO Edward S. Lampert, acquired more than \$1 billion worth of Kmart's bonds and \$400 million of its bank debt.⁹

Kmart emerged from bankruptcy the next year and became a wholly owned subsidiary of Kmart Holding Corporation (Kmart Holding). ESL and Third Avenue Value Fund (Third Avenue), a mutual fund that held approximately \$100 million of Kmart bonds, received approximately 32 million shares of Kmart Holdings' common stock in exchange for their creditor claims against Kmart. As a result of the reorganization, ESL owned over 50 percent of Kmart Holdings' common stock.¹⁰ Mr. Lampert became the chairman of Kmart Holding's board of directors. In June 2003, Kmart Holding began trading on Nasdaq under the symbol KMART.¹¹

Exhibit 3. Kmart Storefront

Source: Business Insider

<https://www.businessinsider.com/australian-kmart-department-store-chain-wesfarmers-2019-10>



History of Sears Holdings Corporation

History of Sears Roebuck and Co.

In 1886, Richard W. Sears, a Minnesota railroad station agent, purchased for \$12 each a shipment of watches from a Minnesota jeweler who had refused to sign for them. Mr. Sears resold the watches to his co-workers for \$14 each. Later that year, Mr. Sears founded R.W. Sears Watch Co. and began selling watches and jewelry by mail order. Shortly after, he moved his business to Chicago and hired a watchmaker, Alvah C. Roebuck. Mr. Sears sold his watch business in 1889. See Exhibit 4.

Exhibit 4. Early Sears Auto Toolkit circa 1910-1914

Source: Bay State Tool Company <http://alloy-artifacts.org/bay-state-tool.html>



In 1893, Messrs. Sears and Roebuck founded another mail-order business, Sears, Roebuck and Co. (Sears Roebuck). To reach customers in rural areas, Sears Roebuck started selling watches and jewelry through mail order catalogues. They later expanded to selling a variety of products

such as clothes, wagons, stoves, furniture, firearms, and home building kits.¹² In 1906, Sears Roebuck became the first major U.S. retailer to have an initial public offering, raising \$40 million in preferred and common stock. Sears Roebuck began trading on the NYSE under the symbol S.¹³

In 1925, Sears Roebuck opened its first retail store in Chicago, Illinois and then built hundreds of stores across the U.S. Product offerings were expanded to include Kenmore brand appliances, DieHard batteries and Craftsman tools. By 1950, Sears Roebuck had 650 stores nationwide.¹⁴ In 1942, Sears Roebuck opened its first international store in Havana, Cuba and later opened stores in Central and South America, Canada, and Europe.

In 1931, for the first time, the sales from Sears Roebuck’s retail stores exceeded its mail-order sales. Recognizing a need for low-cost automobile insurance, in 1931, Sears Roebuck founded Allstate Insurance Co. In 1953, Sears Roebuck launched its own credit card. See Exhibit 5.

Exhibit 5. Ad for Sears’ DieHard Battery

Source: YouTube <https://www.youtube.com/watch?v=7KQTZ0HoSSM>



In 1981, Sears Roebuck acquired the securities brokerage firm, Dean Witter Reynolds Organization, Inc. (Dean Witter) and the real estate company, Coldwell Banker & Company (Coldwell Banker). Through Dean Witter, Sears Roebuck introduced the Discover Card, which was the first credit card to offer cash rewards to customers based on the volume of their purchases.

Changes in technology and marketing ultimately resulted in a loss of effectiveness for the catalog. In 1993, the Sears Roebuck catalog was discontinued; brick and mortar and internet shopping had become the primary sales outlets.

Acquisition of Sears Roebuck and Co. by Kmart Holding Corporation

On March 24, 2005, Kmart Holding purchased Sears Roebuck for approximately \$11.9 billion with the companies becoming subsidiaries of Sears Holdings Corporation (Old Sears), with each operating separately under their own brand names. As part of the acquisition, Kmart Holding shareholders received one share of Old Sears' common stock for each of their Kmart Holding shares. Approximately 94.9 million shares of Old Sears common stock were issued in exchange for all outstanding Kmart Holdings common stock. Sears Roebuck shareholders received either \$50 in cash or 0.5 shares of Old Sears for each Sears Roebuck share. Approximately 62.2 million shares of Old Sears common stock, valued at about \$6.5 billion, was issued to Sears Roebuck shareholders. Also, \$5.4 billion in cash was paid in consideration for all outstanding Sears Roebuck common stock and stock options.¹⁵

Sears Roebuck was delisted from the NYSE and began trading on the Nasdaq under the symbol SHLD.¹⁶

After the acquisition ESL owned approximately 40 percent of Old Sears' stock.¹⁷ Mr. Lampert, who became chairman of Old Sears' board of directors and later its CEO, stated:

*"This new enterprise will seek to leverage the combined strengths of Sears and Kmart to create a long-term value than either could have generated on a stand-alone basis."*¹⁸

Prior to Old Sears filing for bankruptcy in 2015, ESL was its largest shareholder owning approximately 49.7 percent of Old Sears' outstanding common stock.¹⁹ Over several years, ESL had loaned \$2.4 billion to Old Sears enabling it "... to continue operations and seek to implement its transformation plan..."²⁰

Old Sears' Business Environment

As a retail department store business, Old Sears participated in "a highly competitive market segment" competing with both a variety of brick-and-mortar stores such as Walmart and Target, and online retailers such as Amazon. Like other traditional retailers, due to the growth of e-commerce, Old Sears was forced to reduce its prices to remain competitive. Starting in 2013, it closed 71.7 percent of its store locations.

During the five years prior to the bankruptcy, Old Sears' revenues declined to \$19.5 billion representing a 53.8 percent drop. In fiscal year 2017, its revenues decreased to \$16.7 billion from \$22.1 billion in fiscal year 2016.

By 2018, Old Sears had approximately \$5.6 billion of debt, which it mostly incurred to offset declining revenues, honor pension obligations, and purchase inventory. Over \$1.7 billion of its debt was due in fiscal years 2018 and 2019. Its annual cash interest expense was approximately \$400 million, and it lost approximately \$125 million in cash each month.

Most of Old Sears' assets were encumbered, including over 200 real property locations, intellectual property, credit card and pharmacy receivables, and cash. Old Sears had net operating losses (NOLs) in excess of \$5 billion and tax credits of approximately \$900 million.²¹ In fiscal year 2019, Old Sears contributed \$459.3 million to its two pension plans, which were underfunded by about \$1.5 billion and covered approximately 94,000 current and former employees.²²

Bankruptcy Timeline

Pre-Chapter 11 Bankruptcy Proceedings

For several years prior to filing for bankruptcy, Old Sears made efforts to reduce its expenses and operating losses. For example, Old Sears simplified its organizational structure and improved its supply chain and logistics. It evaluated store-level performance to rationalize the size of its retail footprint. It also monetized its assets, refinanced its debts, and reduced and managed its legacy liabilities.²³

In September 2018, ESL submitted to Old Sears a restructuring proposal to reduce its \$5.5 billion of debt to \$1.24 billion. Under the proposal, Old Sears would sell approximately \$1.5 billion worth of assets and \$1.5 billion of real estate and some creditors would convert their loans into Old Sears' stock and others would accept a cash payout.²⁴ ESL president, Kunal S. Kamlani, stated that the proposal was *"... designed to help create sufficient runway for [Old Sears] to continue its transformation and return to profitability for the benefit of its many stakeholders."*²⁵ Old Sears' board of directors did not approve the proposal. Also, Old Sears did not reach an agreement about the proposal with its creditors.²⁶

On October 10, 2018, Old Sears formed a restructuring committee (Restructuring Committee) composed of independent directors to consider, evaluate, and oversee the implementation of strategic alternatives for Old Sears.²⁷

Chapter 11 Bankruptcy Proceedings

Events from October 15, 2018 to December 4, 2018.

On October 15, 2018, Old Sears and certain of its direct and indirect subsidiaries filed for Chapter 11 bankruptcy protection. Old Sears stated that it filed for bankruptcy protection in order “...to establish a sustainable capital structure, continue streamlining its operating model and grow profitably for the long term.”²⁸ Mr. Lampert stated that the bankruptcy process would give Old Sears the flexibility to strengthen its balance sheet thus enabling Old Sears “... to accelerate its strategic transformation, continue to right sizing its operating model, and return to profitability.”²⁹ Upon filing for bankruptcy, Mr. Lampert resigned as CEO of Old Sears, but remained chairman of Old Sears’ board of directors.³⁰

On October 18, 2018, Old Sears filed a motion asking the Bankruptcy Court to approve global bidding and sale procedures “for the efficient marketing, auction and sale of [its] assets in an orderly and value maximizing manner.”³¹ Old Sears believed that there was “... a viable path forward for a reorganization around a smaller footprint of profitable stores.”³² It intended to sell its stores as a going concern because the sale would “...not only save [Old] Sears and Kmart, but also the jobs of thousands of employees that depend on the continued operation...” of its stores.³³ See Exhibit 6.

Exhibit 6. Announcement of Store Closing

Source: YouTube <https://www.youtube.com/watch?v=tQ80Etozka>



On October 24, 2018, the U.S. Bankruptcy Trustee overseeing the bankruptcy appointed a committee to represent Old Sears unsecured creditors' interests (Unsecured Creditors Committee).³⁴

On November 15, 2018, Bankruptcy Court Judge Robert D. Drain approved Old Sears' global bidding and sales procedures and authorized Old Sears to solicit proposals, negotiate transactions, hold auctions, and consummate transactions for the highest or best value. As part of the process, Old Sears would solicit bids and designate a "stalking horse" bidder whose bid would set the floor price for other bids. If Old Sears received more than one bid, it would conduct an auction.³⁵

On November 20, 2018, Judge Drain approved debtor-in-possession financing (DIP) for Old Sears of \$1.83 billion senior secured super priority priming DIP asset-based credit facility (DIP ABL Facility).³⁶

On November 21, 2018, Old Sears began soliciting bids for its assets, including its retail stores on a going concern or liquidation basis and for several of its individual businesses, such as Sears Home Services, Sears Auto Centers, and Innovel (Global Assets).³⁷

Events from December 5, 2018 to December 27, 2018.

On December 5, 2018, ESL notified Old Sears that it was interested in acquiring substantially all of Old Sears' assets for approximately \$4.6 billion (ESL's proposal).

As part of its proposal, ESL would make job offers to approximately 50,000 Old Sears employees. In addition, Old Sears would release ESL, Mr. Lampert, and others from future claims against them over past transactions between ESL and Old Sears (ESL Liability Release).³⁸ Some of Old Sears' unsecured creditors objected to ESL's proposal because of the credit bid and the ESL Liability Release. See Exhibit 7.

Exhibit 7. Photo of Edward S. Lampert

Source: The Wall Street Journal

<https://www.wsj.com/articles/edward-lamperts-non-strategy-to-save-sears-1539403293>



Besides ESL's proposal, Old Sears received multiple bids, including bids from liquidation firms to close some or all of Old Sears' stores and bids from others to acquire specific assets and divisions. Instead of selecting a "stalking horse" bidder for an auction of Old Sears' assets, in the middle of December 2018, Old Sears decided to "push" other bidders to make offers before the December 28, 2018 final bid deadline.³⁹

Events from December 28, 2018 to January 8, 2018.

On December 28, 2018, Judge Drain approved a \$350 million multiple-draw junior debtor-in-possession term loan (Junior DIP Financing) together with DIP ABL Facility, DIP Financing.⁴⁰

Also on December 28, 2018, ESL submitted a formal bid (ESL's 1st Bid) to acquire for \$4.4 billion substantially all of Old Sears' assets including:

- 1) the go-forward retail footprint of approximately 425 stores.
- 2) Sears Auto Centers, Shop Your Way, Kenmore, DieHard, Innoval, and Sears Home Services;
- 3) Old Sears' tax assets, such as NOLs and tax credits; and
- 4) approximately \$1.7 billion of Old Sears' retail inventory and credit card and pharmacy receivables (ESL's 1st Bid).

ESL stated that it believed in Old Sears' *"immense potential to evolve and operate profitably as a going concern with a new capitalization and organizational structure."*⁴¹ ESL described Old Sears *"as an iconic fixture in American retail"* and that it believed that

*"a future for [Old] Sears as a going concern is the only way to preserve tens of thousands of jobs and bring continued economic benefits to the many communities across the United States that are touched by Sears and Kmart Stores."*⁴²

The terms of ESL's 1st Bid were similar to its earlier proposal, but the purchase price was reduced from \$4.6 billion to \$4.4 billion, the credit bid was reduced from \$1.8 billion to \$1.3 billion, and ESL would pay \$35 million as consideration for the ESL Liability Release. If ESL's 1st Bid were not accepted by Old Sears, ESL offered to purchase specific assets including Innovent, Sears Home Service, and Shop Your Way.

About its first bid, the Restructuring Committee rejected ESL's 1st Bid over concerns about the amount of cash, the credit bid, and the ESL Liability Release, but allowed ESL additional time to submit a revised bid. In early January 2019, ESL submitted a second bid (ESL's 2nd Bid), which the Restructuring Committee also rejected. After several weeks of negotiations, on January 8, 2019, Old Sears agreed to consider another revised bid from ESL.⁴³

Events from January 9, 2019 to February 10, 2019.

On January 9, 2019, ESL submitted a third bid increasing its offer from \$4.4 billion to \$5.3 billion (ESL's 3rd Bid). In addition to the terms of ESL's Bids 1 and 2, its 3rd Bid assumed up to an additional \$663 million of Old Sears' liabilities, including amounts owed to vendors, severance costs, and property taxes. ESL would acquire additional Old Sears' assets, including 57 real estate properties, more than \$300 million in accounts receivables, and more than \$300 million worth of inventory. ESL stated that its 3rd Bid would

*"...provide substantially more value to stakeholders than any other option, in particular a liquidation, and it is the best path forward for Sears, its associates and the many communities across the United States touched by Sears and Kmart stores."*⁴⁴

About the 3rd Bid, Lampert stated,

“For as long as I have been involved with Sears, I have cared deeply about the company, its associates and the people they serve. While the opportunity I saw from the start for Sears to benefit from the disruptive changes in retail and technology has not worked out so far, it is still there to be taken...”

However, Lampert was hopeful that Old Sears could *“execute better and faster on [a] smaller platform”* and there was *“every reason to fight for its future.”*⁴⁵

As part of an auction held on January 14, 2019, Old Sears considered ESL’s 3rd Bid, which was the only going concern bid, five bids from parties interested in buying Old Sears’ individual businesses, and bids from liquidators.⁴⁶ On January 16, 2019, Old Sears’ Board of Directors accepted ESL’s 3rd Bid as the highest and best offer for Old Sears’ assets.⁴⁷

On January 17, 2019, Old Sears announced that the auction was closed and ESL was the successful bidder.⁴⁸ On the same day, Old Sears and ESL’s affiliate, Transform Holdco LLC (New Sears), entered into a sale and purchase agreement (Purchase Agreement) pursuant to which under Section 363 of the U.S. Bankruptcy Code (363 Sale),⁴⁹ for approximately \$5.3 billion, New Sears would purchase substantially all of Old Sears’ global assets and assume certain of Old Sears’ liabilities, then Old Sears would liquidate.⁵⁰

Concerning the 363 Sale, the Restructuring Committee stated that it was *“... pleased to have reached a deal that would provide a path for [Old] Sears to emerge from the chapter 11 process....”* And *“Importantly, the consummation of the transaction would preserve employment for tens of thousands of associates [and] relationships with many vendors and suppliers who provide Sears with goods and services.”*⁵¹ ESL stated that it had

*“... been steadfast in its commitment to [Old] Sears because ... its emergence from Chapter 11 as a going concern is the best path for the company, its associates and the many communities touched by Sears and Kmart stores.”*⁵²

On January 17, 2019, the Unsecured Creditors Committee filed a motion with the Bankruptcy Court opposing the sale of Old Sears to New Sears. It claimed that Lampert and ESL operated

Old Sears like a “private portfolio company that existed solely to provide the greatest returns on their investment” disregarding the damage to Old Sears and its employees and creditors.⁵³ Also ESL’s bid was “... nothing but the final fulfillment of a years-long scheme to deprive [Old] Sears and its creditors of assets and its employees of jobs while lining Lampert’s and ESL’s own pockets.”⁵⁴ Further, the Unsecured Creditors Committee argued that although Mr. Lampert and ESL “painted themselves as saviors” by attempting to keep about 400 Sears stores open, Sears could not survive as a going concern.⁵⁵

On February 6, 2019, Old Sears and the Pension Benefit Guaranty Corp. (PBGC), a federal agency that protected pension benefits in private-sector defined benefit plans, entered into a settlement agreement with PBGC agreeing to withdraw its opposition to the 363 Sale and taking over Old Sears’ pensions.⁵⁶ Also, PBGC’s \$1.4 billion unsecured claim against Old Sears for pension funding and unfunded benefit liabilities was reduced to \$800 million and PBGC received a senior, secured non-interest bearing \$80 million note.⁵⁷

On February 8, 2019, Judge Drain rejected the Unsecured Creditors Committee’s and other parties’ objections to the 363 Sale and approved it stating that Old Sears had “... demonstrated good, sufficient, and sound business purposes and justifications...” for the 363 Sale.⁵⁸ Judge Drain stated that one of the business justifications for the 363 Sale was that the purchase price was the highest and best offer and was fair and reasonable considering for Old Sears’ assets. Judge Drain stated that another business justification for the 363 Sale was that it was

“...the best opportunity to maximize the value of the Acquired Assets, whether on a going concern basis or otherwise, and avoid decline and devaluation of the Acquired Assets that would occur in an immediate liquidation” of them.⁵⁹

Events from February 11, 2019 to February 12, 2019.

On February 11, 2019, in accordance with Bid #3, New Sears purchased for approximately \$5.2 billion substantially all of Old Sears’ assets.⁶⁰ The purchase price consisted of cash, a credit bid, and the assumption of certain of Old Sears’ liabilities.⁶¹ In exchange for its creditor claims

against Old Sears, ESL received stock in New Sears. Old Sears' shareholders did not receive any stock, cash, and/or property from New Sears.

Following the 363 Sale, New Sears consisted of 223 Sears and 202 Kmart stores and several brands and operating businesses, including Kenmore DieHard, Craftsman, Sears Home Services, Sears Auto Centers, and Innovel.⁶² Upon announcing the completion of the 363 sale, New Sears stated that it was moving forward from bankruptcy and was *“positioned for success”* with a *“footprint of profitable retail stores, a robust digital platform and an integrated ecosystem of businesses that drive franchise value,”* a healthier capital structure, and strong brand recognition and market positions in key segments.⁶³

Upon completion of the 363 Sale, Mr. Lampert stated that ESL looked *“...forward to a new era at Sears and Kmart that builds on their proud histories, while finding new ways to innovate and grow to adapt to the forces transforming the retail industry.”*⁶⁴ Further, ESL was *“...ready for this exciting opportunity to help return [Old] Sears to profitability”* and would apply itself *“every day in pursuit of that goal.”*⁶⁵

Some of the assets New Sears acquired included:

1. A go-forward retail footprint of 425 Sears and Kmart stores;
2. Several brands, including Sears Auto Centers, Sears Home Services, and Sears Home Improvement;
3. Several business, including Kenmore, Diehard, and Monark Premium Appliance Co.;
4. Shop Your Way membership program;
5. Inventory;
6. Account receivables;
7. Equipment;
8. Intellectual property;
9. Old Sears' goodwill;
- and
10. Tax assets including Old Sears' NOLs and tax credits, refunds, and rebates.⁶⁶

Some of Old Sears' liabilities that New Sears assumed included:

1. Liabilities for warranties and protection agreements or other service contracts for goods and services Old Sears sold or performed.
2. Customer credits related to customer loyalty programs, Shop Your Way, and gifts cards and certificates.
3. Employment related liabilities for employees transferred from Old Sears to New Sears after the 363 Sale;
4. Employee severance reimbursement obligations;
5. Inventory account payables;
6. Property tax liabilities;
- and
7. Certain environmental liabilities.⁶⁷

The \$350 million outstanding amount under the Junior DIP Financing was rolled over to New Sears and the DIP ABL Facility was refinanced.⁶⁸ On February 12, 2019, Mr. Lampert resigned from Old Sears Board of Directors. While New Sears conducted a search for a CEO, its management team included Chief Financial Officer Robert A. Riecker, Chief Digital Officer Leena Munjal, and President of Softlines Greg Ladley.⁶⁹

Post-363 Sale Events.

In April 2019, Old Sears sued Mr. Lampert, ESL, and others alleging that Mr. Lampert and others *"... caused more than \$2 billion of assets to be transferred to himself and Sears' other shareholders and beyond the reach of Sears' creditors."*⁷⁰ Further, Old Sears claimed:

*"As [Mr.] Lampert and the other Defendants stripped [Old] Sears of billions of dollars of assets and encumbered its remaining property with new liens, [Old] Sears was suffering billions of dollars of losses annually, and had not generated positive cash flow from operations for years..."*⁷¹

In response to the lawsuit, ESL stated:

*"ESL Investments, Inc. vigorously disputes the claims in the debtors' complaint against ESL, Mr. Lampert, and Mr. Kamlani, which repeats baseless allegations and fanciful claims... [Old Sears'] allegations are misleading or just flat wrong."*⁷²

After the 363 Sale, New Sears began to close stores and announced in November 2019 that it would be operating only 189 of the 425 stores it had acquired.⁷³ Also, in November 2019, New

Sears borrowed \$250 million from ESL and other investors.⁷⁴ At the same time, New Sears began sold the DieHard batteries business and Innovel. New Sears took on an additional \$100 million in debt by borrowing from Brigade Capital Management, a hedge fund.

Old Sears' Liquidation Plan.

On October 1, 2019, Old Sears filed a Chapter 11 Plan (Liquidation Plan) with the Bankruptcy Court. It was projected that Old Sears was short by \$36.5 million to \$104.5 million in covering the payment of its obligations to its creditors and other before exiting bankruptcy. At the hearing on October 7, 2019, Judge Drain stated that despite Old Sears not having the cash to pay its essential bills, he would approve the Liquidation Plan, which he did on October 15, 2019.

Under the Liquidation Plan, the Old Sears Secured Creditors were to be paid in full and unsecured creditors would be paid 2.5 cents for every dollar they were owed.⁷⁵ Old Sears shareholders' common stock and warrants to purchase Old Sears common stock were to be cancelled. Old Sears would liquidate by transferring its remaining assets and liabilities to a trust.⁷⁶

Conclusion

In the 363 Sale, Old Sears sold substantially all of its assets to New Sears with its largest creditor, ESL exchanging its claims against Old Sears for New Sears stock. The 363-sale resulted in U.S. federal income tax consequences for Old Sears, Old Sears' creditors and shareholders, and New Sears. Under U.S. tax laws, what would have been their tax consequences?



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Appendix A. U.S. Tax Concepts

Sources: U.S. Code: Title 26: Subtitle A-Income Taxes and Title 26 of the Code of Federal Regulations (26 CFR)

Overview

For U.S. federal tax purposes, Internal Revenue Code (IRC) § 368 provides several different types of corporate tax-free (tax-deferred) reorganizations, including a Type G bankruptcy reorganization, which the U.S. Congress intended to “*facilitate the rehabilitation of financially troubled businesses [and] corporate debtors in bankruptcy.*” In a Type G reorganization, the assets of a corporation in bankruptcy (Debtor Corp) are exchanged for the stock and/or securities of another corporation (Acquirer) with Debtor Corp’s creditors receiving Acquirer’s stock and/or securities in satisfaction of their claims against Debtor Corp and Debtor Corp’s shareholders exchanging their Debtor Corp stock or securities for Acquirer stock and securities. If a bankruptcy reorganization does not qualify as a Type G reorganization, it may be considered a taxable bankruptcy reorganization and treated as a taxable sale of Debtor Corp’s assets.

Tax-Free Type G Bankruptcy Reorganization

Statutory Requirements

For a reorganization to qualify as a Type G reorganization, both statutory and non-statutory requirements must be met. IRC § 368(a)(1)(G) provides that in a Type G reorganization:

1. Debtor Corp transfers all or part of its assets to Acquirer in exchange for Acquirer’s stock or securities, such as bonds and notes, in a Title 11 or similar case, such as receiverships and foreclosures; and
2. Pursuant to a plan of reorganization, the stock or securities received from Acquirer are distributed in a transaction that qualifies under IRC §§ 354, 355, or 356.

For purposes of IRC § 368(a), securities are defined as stock, warrants, and other rights to acquire stock. Generally, long-term debt instruments, such as bonds and notes, with terms of ten years or more are securities and short-term debt instruments with terms less than five years are not securities. Also, debt instruments are securities if they represent an investment and/or participation in a business, rather than a temporary advance to meet current corporate needs.⁷⁷

If a bankruptcy reorganization meets the requirements of IRC § 354, it is an acquisitive Type G reorganization. To meet the requirements of IRC § 354:

1. Debtor Corp must transfer substantially all of its assets to Acquirer in exchange for Acquirer's stock and securities;
2. Debtor Corp's shareholders and security holders must exchange their Debtor Corp stock and securities for Acquirer's stock or securities; and
3. Debtor Corp must liquidate by distributing all stock, securities, and other properties received from Acquirer and all of the assets that Debtor Corp did not transfer to Acquirer.

The substantially all requirement is met if the assets transferred by Debtor Corp to Acquirer constitute over 70 percent of the fair market value (FMV) Debtor Corp's operating assets and more than 50 percent of the FMV of its gross assets.⁷⁸

If a bankruptcy reorganization meets the requirements of IRC § 355, it is a divisive Type G reorganization. To meet the requirements of IRC § 355:

1. Debtor Corp must control Acquirer;
2. Debtor Corp must distribute Acquirer's stock or securities to its shareholders in exchange for their Debtor Corp stock and securities;
3. Debtor Corp must distribute enough of Acquirer's stock and securities to constitute control;
4. Both Debtor Corp and Acquirer must be engaged in an active trade or business; and
5. The distribution cannot be a device to distribute earnings and profits.

Non-Statutory Requirements

Besides meeting the statutory requirements, Type G reorganizations must also meet the following non-statutory requirements: 1) plan of reorganization; 2) business purpose; 3) continuity of business enterprise (COBE); and 4) continuity of interest (COI). A Type G reorganization must be carried out pursuant to a plan of reorganization that is adopted by each corporation that is a party to the reorganization, but it does not have to be in a particular form or in writing. Other than avoiding federal income taxes, a Type G reorganization must have a valid purpose, such as facilitating the rehabilitation of Debtor Corp, allowing Debtor Corp to continue as a business, or transferring Debtor Corp's "wanted" assets and liabilities to Acquirer while retaining its "unwanted" assets and liabilities. To meet the COBE

requirement, Acquirer must either continue at least one significant line of a Debtor Corp's historical business or use a significant portion of Debtor Corp's historic business assets in a business.⁷⁹

The COI doctrine requires that the former shareholders of an acquired corporation must have a substantial equity interest in Acquirer after the reorganization.⁸⁰ However, if Debtor Corp shareholders are eliminated in its bankruptcy proceedings (e.g., their Debtor Corp stock is cancelled), there will not be Debtor Corp shareholders to receive an equity interest. For purposes of the COI requirement, in Type G reorganizations, Debtor Corp's creditors are treated as its former shareholders. Under Treas. Reg. § 1.368-1(e)(2)(v) Ex 1, the COI requirement is met in Type G reorganizations if at least 40 percent of the FMV of the total consideration received by Debtor Corp's creditors and any remaining shareholders consists of Acquirer's stock.

Tax Consequences: Debtor Corporation's Tax Consequences

Recognition of Gains and Losses

In Type G reorganizations, under IRC § 361, Debtor Corp will not recognize gain or loss on exchanging its assets for Acquirer's stock, securities, money, and other property (boot).⁸¹ It will also not recognize gain or loss on exchanging Acquirer stock, securities, money, and other property received from Acquirer for its creditors' claims and its shareholders' Debtor Corp stock. However, if Debtor Corp retains any Acquirer stock, securities, money, and property received from Acquirer, or assets it did not transfer to Acquirer, it will recognize gain, but not loss. Under IRC § 357(c)(1), Debtor Corp may recognize gain if the liabilities assumed by Acquirer exceed the basis of its transferred assets. However, under IRC § 357(c)(2)(B), this rule will not apply if Debtor Corp's former shareholders do not receive any consideration for their Debtor Corp stock.

Cancellation of Debt (COD) Income

In Type G reorganizations, Debtor Corp may realize COD income, if it distributes Acquirer's stock to its creditors in exchange for their claims against Debtor Corp. Under IRC § 108(e)(8), the amount of Debtor Corp's COD income equals the FMV of Acquirer's stock. However, under IRC § 108(a)(1), Debtor Corp's gross income will not include the COD income, because the creditors' claims were discharged in a Title 11 case or while insolvent.

Under IRC §§ 108(b)(1) and (2)(A)-(G), Debtor Corp will reduce the tax attributes and the basis of property not transferred to Acquirer by the amount of its COD income in the following order: 1) net operating losses (NOLs) arising in the taxable year of the discharge and NOL carryovers; 2) general

business credits carryovers; 3) minimum tax credit carryovers; 4) net capital losses or capital loss carryovers; 5) basis of depreciable and nondepreciable property; 6) passive activity loss and credit carryovers; and 7) foreign tax credit carryovers. Or, under IRC § 108(b)(5), Debtor Corp can elect to first reduce the basis of its depreciable property, then reduce any remaining tax attributes in the order listed in IRC § 108(b)(2).

Acquirer Corporation’s Tax Consequences

Under IRC §§ 361 and 1032(a), Acquirer will not recognize gain or loss on exchanging its stock, securities, money, and other property (boot) for Debtor Corp’s assets. Under IRC § 362(b), Acquirer’s basis in the transferred assets will be the same as Debtor Corp’s basis in those assets immediately prior to the exchange. Under IRC § 1223(2), Acquirer’s holding period in the transferred assets will include Debtor Corp’s holding period in those assets immediately prior to the exchange.

Under IRC § 381, Acquirer will succeed to Debtor Corp’s tax attributes, such as Debtor Corp’s NOLs, earnings and profits, and capital loss carryovers. If Debtor Corp realizes COD income, Acquirer must reduce the tax attributes it succeeded to and the basis of property it acquired from Debtor Corp by the amount of the COD income in the order listed in IRC § 108(b)(2). Or, Acquirer can elect to first reduce the basis of Debtor Corp’s depreciable property, then reduce any remaining tax attributes and other property in the order described above.

If a corporation with a net operating loss (NOL) (Loss Corp) undergoes an ownership change, IRC § 382(a) imposes an annual limit on the amount of Loss Corp’s NOL carryovers that can be used to offset gains arising after the ownership change (Section 382 Limit). Under IRC § 382(b)(1), the annual limit equals Loss Corp’s equity value multiplied by the long-term tax-exempt rate. IRC § 382(g) provides that an ownership change occurs if there is an increase in the stock ownership of five percent shareholders aggregating more than 50 percent during a three-year period.

However, under IRC §§ 382(l)(5)(A) and (l)(6), the Section 382 Limit does not apply if:

1. Loss Corp’s ownership change occurs in a title 11 or similar proceeding, such as a Type G reorganization; and
2. Loss Corp’s shareholders or creditors before the ownership change own, after the ownership change, at least 50 percent of Loss Corp’s stock.

IRC § 382(l)(5)(E) states that the stock received by the creditors will count towards the 50 percent change if: 1) their claims were held for 18 months before the date when the bankruptcy case was filed; or 2) the claims arose in the ordinary course of Loss Corp's trade or business.

Under IRC §§ 382(l)(5)(B) and (D), Loss Corp's NOL carryovers must be reduced by any interest deductions taken by Loss Corp during the taxable year in which the ownership change occurs and the three preceding taxable years with respect to indebtedness that was converted into, or exchanged for, stock pursuant to the bankruptcy reorganization. If there is a second ownership change within two years of a bankruptcy reorganization, the NOL carryovers that arose prior to the bankruptcy reorganization cannot be used to offset future gains arising after the second ownership change.

Under IRC § 382(l)(6), if Loss Corp elects out of the bankruptcy exception or the exception does not apply, Loss Corp's NOL carryforwards will be subject to the Section 382 Limit. However, the Section 382 Limit may be increased to reflect an increase in Loss Corp's value resulting from the surrender or cancellation of Loss Corp creditors' claims as part of a Type G reorganization.

Debtor Corporation Creditors' Tax Consequences

Debtor Corporation Creditors Who are Security Holders

Under IRC § 354, if a creditor's claim against Debtor Corp is a security, the creditor will not recognize gain or loss on exchanging the claim for Acquirer stock and securities. The creditor's claim is a security if the debt instrument being exchanged is a long-term debt instrument with a term of ten years or more, but not less than five years, and/or represents an investment in or participation in Debtor Corp.

If along with Acquirer's stock and securities, a creditor receives money and other property, under IRC §§ 356(a)(1) and (c), the creditor will recognize gain, not loss, in an amount not in excess of the amount of money and the FMV of the other property. Also, the creditor will recognize ordinary income to the extent that the stock the creditor received was in exchange for interest that accrued, but was not paid, during the period the creditor held the claim.

Under IRC § 358(a)(1), the creditor's adjusted basis in Acquirer stock and securities will equal the adjusted basis of the claim immediately before the exchange less the amount money and the FMV of other property received from Acquirer plus any gain recognized by the creditor (Adjusted basis of creditor's claim – amount of money - FMV of other property + creditor's recognized gain = Acquirer

stock and securities basis). Under IRC § 1223(1), if the creditor held the claim as a capital asset, the holding period in Acquirer stock and securities will include the period the creditor held the claim.⁸² Under IRC § 358(a)(2), the basis of money and other property received by a creditor in the exchange will equal the amount of money and the FMV of the other property. The creditor's holding period in the other property will not include Acquirer's holding period in the property.

Debtor Corporation Creditors Who are Not Security Holders

If a creditor's claim against Debtor Corp is not a security, under IRC § 1001, the creditor will recognize gain or loss on exchanging the claim for Acquirer's stock and securities. The creditor's recognized gain or loss will equal the difference between the FMV of Acquirer stock and securities plus the amount of money and the FMV of other property received from Acquirer and the adjusted basis of the claim (FMV of Acquirer stock and securities + amount of money + FMV of other property – adjusted basis of creditor's claim = creditor's recognized gain or loss).

The creditor's basis in Acquirer stock will equal the FMV of the stock and securities and the holding period in Acquirer stock and securities will not include the period the creditor held the claim. Under IRC § 358(a)(2), the basis of money and other property received by the creditor will equal the amount of money and the FMV of the other property. The creditor's holding period in the other property will not include Acquirer's holding period in the property.

Creditors Who Do Not Participate in Debtor Corp's Type G Reorganization

For Debtor Corp creditors, who do not participate in Debtor Corp's Type G reorganization, if their claim becomes worthless and it was a capital asset, under IRC § 165(g), they may be able to claim a worthless securities deduction, or under IRC § 166, claim a bad debt deduction, but not both.

Debtor Corporation Shareholders' Tax Consequences

Shareholders Who Participate in Debtor Corp's Type G Reorganization

If Debtor Corp shareholders participate in Debtor Corp's Type G reorganization, under IRC § 354, they will not recognize gain or loss on exchanging their stock for Acquirer's stock and securities. Under IRC §§ 356(a)(1) and (c), if the shareholders receive money and other property along with Acquirer's stock and securities, they will recognize gain, not loss, in an amount not in excess of the amount of money and the FMV of the other property.⁸³

Debtor Corp shareholders' basis in their Acquirer stock and securities equals their Debtor Corp stock basis plus any recognized gain less the amount of money less the FMV of other property received from Acquirer less the amount of liabilities assumed by Acquirer as part of the reorganization (Debtor Corp stock basis + recognized gain – amount of money - FMV of other property – amount of assumed liabilities = Acquirer stock and securities basis). If Debtor Corp shareholders held their Debtor Corp stock as a capital asset, their holding period in their Acquirer stock and securities will include their holding period in their Debtor Corp stock.⁸⁴

Under IRC § 358(a)(2), the basis of money and other property received by Debtor Corp shareholders will equal the amount of money and the FMV of the other property. Their holding period in the other property will not include Acquirer's holding period in them.

Shareholders Who Do Not Participate in Debtor Corp's Type G Reorganization

For Debtor Corp shareholders who do not participate in Debtor Corp's Type G reorganization, if they sell their Debtor Corp stock and it was a capital asset, under IRC §§ 165(f) and 1222, they may realize capital gains or losses. Or, if their Debtor Corp stock becomes worthless and it was a capital asset, under IRC § 165(g), they may be able to claim a worthless stock deduction.

Also, under IRC §§ 302 and 317, if Debtor Corp acquires its stock from its shareholders in exchange for cash or other property, but not Debtor Corp's own stock, the exchange may be characterized as a stock redemption, which depending on the circumstances, may be treated as if the shareholders had sold their stock, thus realizing gain or loss, or it may be treated as if they had received a dividend from Debtor Corp.

Taxable Bankruptcy Reorganization

If a bankruptcy reorganization does not qualify as a tax-free Type G reorganization, it may qualify as a taxable bankruptcy reorganization and treated as a taxable sale of Debtor Corp's assets.

Tax Consequences

Debtor Corporation's Tax Consequences

In a taxable bankruptcy reorganization, Debtor Corp will realize gain, which may be offset by its NOLs, or loss, equal to the difference between FMV of its assets and their adjusted basis (FMV of Debtor Corp's assets – adjusted basis of Debtor Corp's assets = Debtor Corp's realized gain or loss).

If as part of a taxable bankruptcy reorganization, Debtor Corp's debts are discharged, it will realize, but not recognize, COD income because its debts were discharged in a Title 11 case or while insolvent. For tax attributes and property not transferred to Acquirer, Debtor Corp will reduce the tax attributes and the basis of the property by the amount of its COD income in the order described in IRC § 108(b)(2). Or, under IRC § 108(b)(5), Debtor Corp can elect to first reduce the basis of Debtor Corp's depreciable property, then reduce any remaining tax attributes in the above order.

Acquirer Corporation's Tax Consequences

Acquirer's basis in Debtor Corp's assets will equal their FMV. Its holding period in the assets will not include Debtor Corp's holding period in those assets. Acquirer will not succeed to Debtor Corp's tax attributes, such as its NOLs. If Debtor Corp realizes COD income, Acquirer must reduce the basis of the property it acquired from Debtor Corp by the amount of the COD income in the order listed in IRC § 108(b)(2). Or Acquirer can elect to first reduce the basis of Debtor Corp's depreciable property and then reduce the basis of other property in the order described above.

Debtor Corporation Creditors' Tax Consequences

If as part of a taxable bankruptcy reorganization, Debtor Corp's creditors exchange their claims for Acquirer stock, securities, money, and/or other property, under IRC § 1001, it will be a taxable exchange. The creditors will recognize gain or loss equal to the difference between the FMV of Acquirer stock and securities plus the amount of money and the FMV of other property received from Acquirer and the adjusted basis of their claims against Debtor Corp (FMV of Acquirer stock and securities + amount of money + FMV of other property – adjusted basis of creditors' claim = creditors' recognized gain or loss).

Their basis in Acquirer stock and securities will equal the FMV of the stock and securities and their holding period in their Acquirer stock and securities will not include the period they held their claims.

Under IRC § 358(a)(2), the basis of money and other property received by Debtor Corp creditors will equal the amount of money and the FMV of the other property. Their holding period in the other property will not include Acquirer's holding period in the property.

For Debtor Corp creditors, who do not participate in a taxable bankruptcy reorganization, their tax consequences will be the same as discussed above for Debtor Corp creditors, who do not participate in Debtor Corp's Type G reorganization.

Debtor Corporation Shareholders' Tax Consequences

If, as part of a taxable bankruptcy reorganization, Debtor Corp shareholders exchange their stock for Acquirer stock, securities, money, and/or other property, it will be a taxable exchange. The shareholders will recognize gain or loss equal to the difference between the FMV of Acquirer stock and securities plus the amount of money and the FMV of the other property they received from Acquirer and the adjusted basis of their Debtor Corp stock (FMV of Acquirer stock and securities + amount of money + FMV of other property – adjusted basis of Debtor Corp stock = Debtor Corp shareholders' recognized gain or loss). Their holding period in their Acquirer stock and securities will not include the period they held their Debtor Corp stock.

Under IRC § 358(a)(2), the basis of money and other property received by Debtor Corp shareholders will equal the amount of money and the FMV of the other property. Their holding period in the other property will not include Acquirer's holding period in them.

For Debtor Corp shareholders, who do not participate in Debtor Corp's taxable bankruptcy reorganization, their tax consequences will be the same as discussed above for Debtor Corp shareholders, who do not participate in Debtor Corp's Type G reorganization.

Appendix B. Bankruptcy Timeline

Source: Authors' notes

DATE	EVENT
Sept. 2018	Sears Holdings Corporation's (Old Sears) largest shareholder and creditor, hedge fund ESL Investments, Inc. (ESL) submitted a restructuring proposal to reduce Old Sears' \$5.5 billion debt to \$1.24 billion.
10/10/2018	Old Sears formed a restructuring committee (Restructuring Committee) composed of independent directors to consider, evaluate, and oversee the implementation of strategic alternatives for Old Sears.
10/15/2018	Old Sears and certain of its direct and indirect subsidiaries filed for Chapter 11 bankruptcy protection. Edward Lampert resigned as CEO of Old Sears and remained chairman of Old Sears' board of directors
10/15/2018	Founder and chairman of ESL, Edward Lampert resigned as CEO of Old Sears and remained chairman of Old Sears' board of directors.
Oct. 2018	Old Sears' stock stopped being traded on the Nasdaq and began trading on the over-the-counter market under the trading symbol SHLDQ.
10/18/2018	Old Sears filed a motion asking the Bankruptcy Court to approve global bidding and sale procedures with the intention of selling the company as a going concern.
10/24/2018	The U.S. Trustee overseeing Old Sears' bankruptcy appointed a committee to represent Old Sears unsecured creditors' interests (Unsecured Creditors Committee).
11/15/2018	Bankruptcy Court Judge Robert D. Drain approved Old Sears' global bidding and sales procedures authorizing Old Sears solicit proposals, negotiate transactions, hold auctions, and consummate transactions for the highest or best value.
11/20/2018	Judge Drain approved debtor-in-possession financing (DIP) for Old Sears of \$1.83 billion senior secured super priority priming DIP asset-based credit facility (DIP ABL Facility).
11/21/2018	Old Sears began soliciting bids on its assets including its retail stores on a going concern or liquidation basis and individual businesses including Sears Home Services, PartsDirect, Sears Auto Centers, and Innovel (Global Assets).
12/5/2018	ESL submitted a proposal to acquire for approximately \$4.6 billion substantially all of Old Sears' assets.
12/2018	Instead of selecting a stalking horse bidder for an auction of Old Sears' assets, Old Sears decided to encourage other bidders to make offers before the December 28, 2018 final bid deadline.
12/28/2018	ESL submitted a formal bid to acquire Old Sears for \$4.4 billion with a \$1.3 billion financing commitment from several financial institutions (ESL's 1 st Bid).
12/28/2018	Judge Drain approved a \$350 million multiple-draw junior debtor-in-possession term loan (Junior DIP Financing) (together with DIP ABL Facility, DIP Financing).
12/28/2018 to early January 2019	<ul style="list-style-type: none"> • Old Sears' Restructuring Committee rejected ESL's 1st bid • ESL submitted a revised bid (ESL's 2nd Bid), which was rejected by Old Sears' Restructuring Committee.
1/8/2019	After several weeks of negotiations, Old Sears agreed to consider another revised bid from ESL.
1/9/2019	ESL submitted a revised bid increasing its offer from \$4.4 billion to \$5.3 billion (ESL's 3 rd Bid).
1/14/2019	As part of an auction, Old Sears considered ESL's 3 rd Bid, which was the only going concern bid, five bids from parties interested in buying individual businesses, and bids from buyers who would liquidate it.
1/16/2019	Old Sears board of directors accepted ESL's 3 rd Bid as the highest and best offer for Old Sears' assets.
1/17/2019	Old Sears announced that the auction was closed, and ESL was the successful bidder.

DATE	EVENT
1/17/2019	Old Sears and ESL's affiliate, Transform Holdco LLC (New Sears), entered into a sale and purchase agreement (Purchase Agreement).
1/17/2019	The Unsecured Creditors Committee filed a motion with the Bankruptcy Court opposing the sale of Old Sears to New Sears
2/6/2019	<ul style="list-style-type: none"> • Old Sears and Pension Benefit Guaranty Corp. (PBGC), the federal government's pension insurer, entered into a settlement agreement with PBGC agreeing to withdraw its opposition to the 363 Sale and taking over the Old Sears' pensions. • PBGC's \$1.4 billion unsecured claim against Old Sears was reduced to \$800 million with the PBGC receiving a senior, secured non-interest bearing \$80 million note.
2/8/2019	Judge Drain rejected creditors' and others' objections to the 363 Sale and approved it.
2/11/2019	<ul style="list-style-type: none"> • New Sears purchased for approximately \$5.2 billion substantially all of Old Sears' assets. • The purchase price consisted of cash, a credit bid, and the assumption of certain of Old Sears' liabilities. • ESL forgave approximately \$1.4 billion of the debt Old Sears owed it and received New Sears stock in exchange for its creditor claims against Old Sears.
2/12/2019	Edward Lampert resigned from Old Sears Board of Directors
10/1/2019	Old Sears filed a Chapter 11 Plan (Liquidation Plan) with the Bankruptcy Court.
10/15/2019	<ul style="list-style-type: none"> • Judge Drain approved the Liquidation Plan. • Under the Liquidation Plan: <ul style="list-style-type: none"> ○ Old Sears Secured Creditors were to be paid in full; ○ Old Sears unsecured creditors would be paid 2.5 cents for every dollar they were owed; ○ PBGC's \$1.4 billion unsecured claim against Old Sears would be reduced to \$800 million with the PBGC receiving a senior, secured non-interest bearing \$80 million note; ○ Old Sears shareholders' common stock and warrants to purchase Old Sears common stock would be cancelled; and ○ Old Sears would liquidate by transferring its remaining assets and liabilities to a trust.
Nov. 2019	New Sears began to close stores and announced that it would be operating 189 of the 425 stores it had acquired.
Nov. 2019	New Sears borrowed \$250 million from ESL and other investors.
April 2019	Old Sears sued Edward Lampert, ESL, and others for allegedly wrong actions prior to Old Sears filing for bankruptcy.
Dec. 2019	New Sears sold its DieHard business to Advance Auto Parts for \$200 million.
Feb. 2020	New Sears borrowed \$100 million from hedge fund, Brigade Capital Management LP.
March 2020	New Sears sold Innovent to Costco Wholesale Corporation for \$1 billion.

Appendix C. Old Sears' Pre-bankruptcy Debt Facilities

Sources: Sears Holdings Corporation, Declaration of Robert A. Riecker Pursuant to Rule 1007-2 of Local Bankruptcy Rules for Southern District of New York: Case 18-23538 (October 15, 2018)

<u>Debt Facilities</u>	<u>Principal Outstanding</u> (\$ millions)
Revolving Credit Facility	836.0
First Lien Letters of Credit	123.8
First Lien Term Loan A	-
First Lien Term Loan B	570.8
FILO (First In, Last Out) Term Loan	125.0
Total First Lien Debt	1,655.6
Stand-Alone L/C (Letters of Credit) Facility	271.1
Second Lien Term Loan	317.1
Second Lien Line of Credit	525.0
Alternative Tranche Line of Credit Loans	45.0
Second Lien PIK (Paid in Kind) Notes	175.4
Second Lien Notes	89.0
Total Second Lien Debt	1,151.5
IP/Ground Lease Term Loan	231.2
Consolidated Secured Note A	108.1
Consolidated Secured Note B	723.3
Total Secured Loan Debt	1,062.6
Holdings Unsecured PIK (paid in kind) Notes	222.6
Holdings Unsecured Notes	411.0
SRAC Unsecured PIK (paid in kind) Notes	107.9
SRAC Unsecured Notes	185.6
Total Unsecured Debt	927.0
Total Funded Debt	5,067.8
<u>Intercompany Notes</u>	
KCD Asset-Backed Notes	900.0
SRAC Medium Term Notes	2,311.8
Total Intercompany Debt	3,211.8
<u>Sparrow Structure</u>	
Sparrow Term Loan	111.0
Sparrow Mezzanine Term Loan	513.2
Total Sparrow Structure Debt	624.2

Appendix D. Old Sears' Pre-bankruptcy Debt Facilities Held by ESL Investments

Sources: Declaration of Robert A. Riecker Pursuant to Rule 1007-2 of Local Bankruptcy Rules for Southern District of New York: Case 18-23538 (October 15, 2018)

Debt Facility	Total Principal Outstanding (\$ millions)	Amount of Total Principal Outstanding Held by ESL (and/or Its Affiliates) (\$ millions)	Debt Facility's Term
FILO (First In, First Out) Term Loan	125.0	70.0	7/21/2015 (approximately) – 7/20/2020
Stand-Alone L/C (Letters of Credit) Facility	271.1	105.7	12/28/2016-12/28/2019
Second Lien Credit Facility (consisting of Second Lien Term Loan (\$317.1), Second Lien Line of Credit (\$525.0) & Alternative Tranche Line of Credit Loans(\$45))	887.1	819.6	<ul style="list-style-type: none"> Second Lien Term Loan (9/1/2016-7/20/2020) Second Lien Line of Credit (started 9/1/2016, due 270 days from each time amount was borrowed) Alternative Tranche Line of Credit (9/1/2016-10/15/2018)
Second Lien PIK (paid in kind) Notes	175.4	20.7	3/20/2018-10/15/2019
IP/Ground Lease Term Loan	231.2	152.4	4/4/2018-7/20/2020
Consolidated Secured Note B	723.3	723.3	6/4/18-7/20/2020
Holdings Unsecured PIK (paid in kind) Notes	222.6	195.1	3/20/2018-12/15/2019

Appendix E. Old Sears' 5 Largest Pre-bankruptcy Secured Creditors

Sources: Sears Holdings Corporation, Declaration of Robert A. Riecker Pursuant to Rule 1007-2 of Local Bankruptcy Rules for Southern District of New York: Case 18-23538 (October 15, 2018)

No.	Holder	Amount of Claim (\$)	Type of Collateral
1	First Lien Revolving Credit Agreement (Bank of America, N.A., and Wells Fargo Bank, National Association)	836,000,000	Credit card receivables, pharmacy receivables, Inventory, prescription lists, deposit accounts and cash
2	Consolidated Secured Note B (held by JPP, LLC and JPP, II, LLC (ESL Investment affiliates))	723,300,000	Real estate
3	2016 First Lien Term Loan (B) (Bank of America, N.A., and Wells Fargo Bank, National Association)	570,800,000	Credit card receivables, pharmacy receivables, Inventory, prescription lists, deposit accounts and cash
4	Second Lien Line of Credit (JPP, LLC administrative agent (ESL Investments affiliate))	570,000,000	Credit card receivables and inventory
5	Second Lien PIK (paid in kind) Term Loan (6 5/8% Senior Secured Convertible PIK Toggle Notes Due 2019)	317,100,000	Credit card receivables and inventory

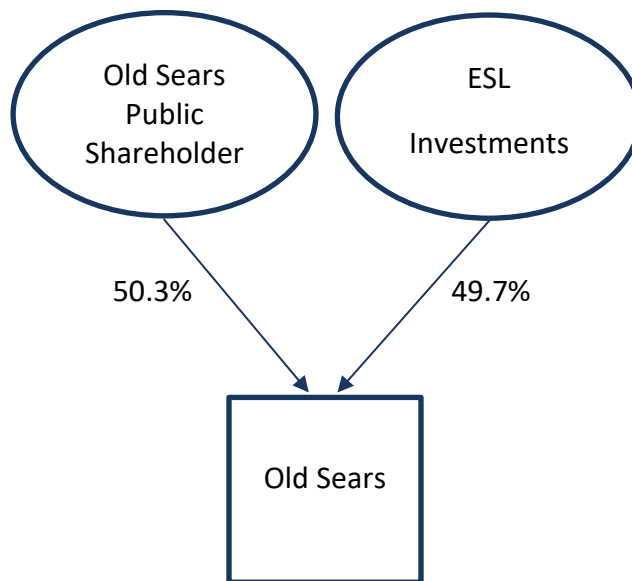
Appendix F. Old Sears’ 20 Largest Pre-bankruptcy Unsecured Creditors

Sources: Sears Holdings Corporation, Declaration of Robert A. Riecker Pursuant to Rule 1007-2 of Local Bankruptcy Rules for Southern District of New York: Case 18-23538 (October 15, 2018)

No	Creditor	Nature of Claim	Amount of Claim (\$)
1	The Pension Benefit Guaranty Corp (PUBGC)	Pension Benefits	Unknown
2	SRAC Medium Term Notes (8%)	Unsecured Notes	3,211,800,000
3	Holdings Unsecured Notes (8%)	Unsecured Notes	411,000,000
4	Holdings Unsecured PIK (paid in kind) Notes (8%)	Unsecured Notes	222,600,000
5	SRAC Unsecured Notes	Unsecured Notes	185,600,000
6	SRAC Unsecured PIK (paid in kind) Notes	Unsecured Notes	107,900,000
7	Whirlpool Corporation	Trade Debt	23,409,729
8	Frigidaire Company	Trade Debt	18,617,186
9	Winia Daewoo Electronics America	Trade Debt	15,180,156
10	Cardinal Health	Trade Debt	13,877,913
11	Icon Health & Fitness, Inc.	Trade Debt	12,102,200
12	HK Greatstar Int’l Co. Ltd.	Trade Debt	10,354,683
13	Samsung Electronics America HA	Trade Debt	8,054,247
14	Apex Tool International, LLC	Trade Debt	6,605,582
15	Black & Decker US, Inc.	Trade Debt	5,893,734
16	Eastern Prime Textile Limited	Trade Debt	5,761,992
17	Winners Industry Company Limited	Trade Debt	5,359,201
18	Tata Consultancy Services Ltd.	Trade Debt	5,333,545
19	Active Media Services, Inc.	Trade Debt	5,192,874
20	Automotive Rentals, Inc.	Trade Debt	4,830,313

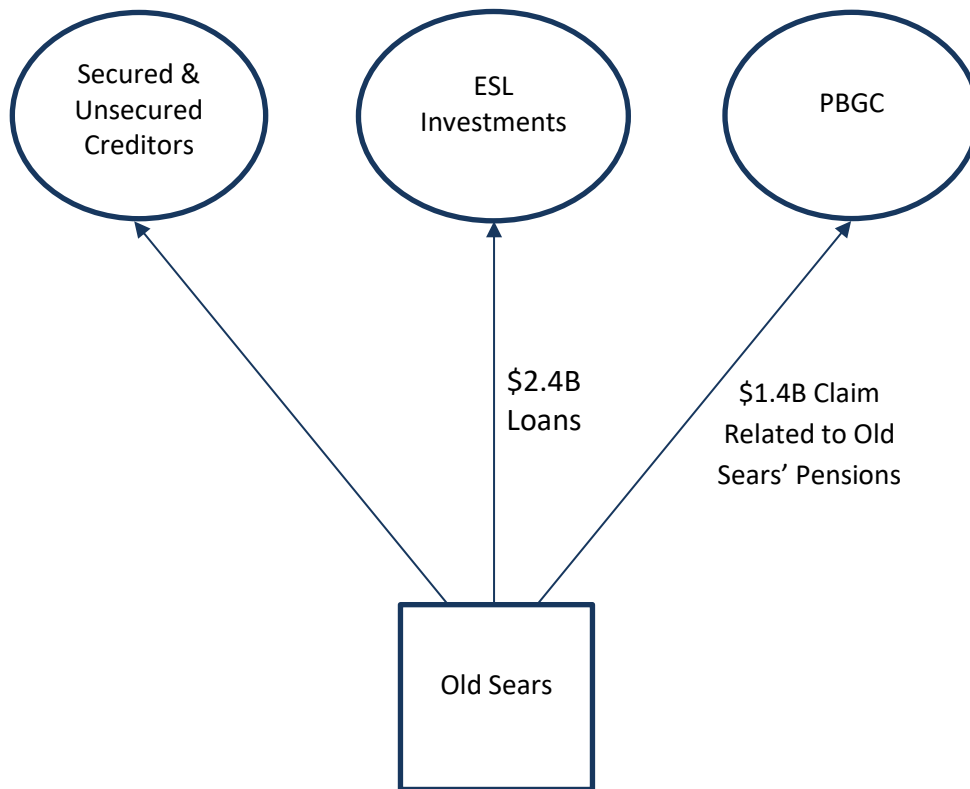
Appendix G. Pre-section 363 Sale: Old Sears’ Shareholders

Source: Authors’ notes



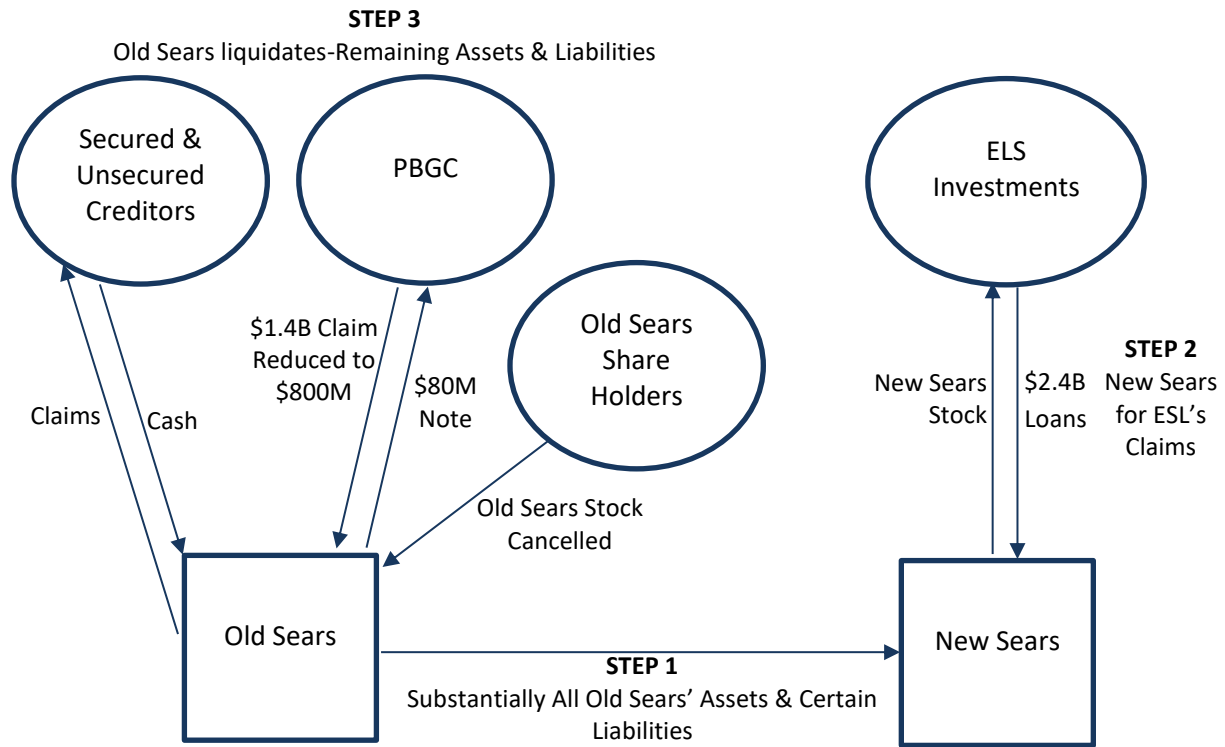
Appendix H. Pre-section 363 Sale: Old Sears' Creditors

Source: Authors' notes



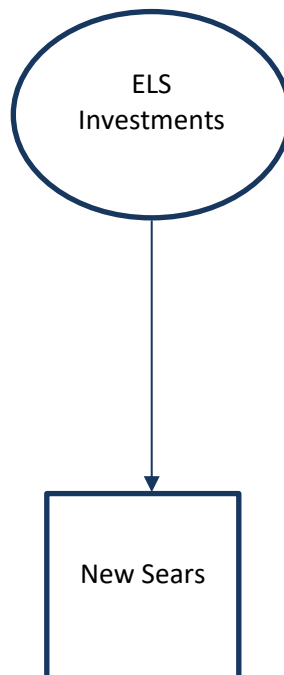
Appendix I. Section 353 Sale

Source: Authors' notes



Appendix J. Post-section 363 Sale Ownership of New Sears

Source: Authors' notes



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