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15 Debtors' Mailing Address:
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17 1000 Pleasant Valley Road
18 Harrisonburg, VA 22801-9790

19 **UNITED STATES BANKRUPTCY COURT**
20 **CENTRAL DISTRICT OF CALIFORNIA**
21 **LOS ANGELES DIVISION**

22 In re:) Case No. 13-bk-27689-WB
23)
24 COLOREP, INC.,) Chapter 11
25 a California corporation,)
26) (Motion for Joint Administration With
27 Debtor.) Case No. 13-bk-27698-WB Pending)
28)
29 Tax I.D. No. 94-3055023)
30)

31 In re:) **DECLARATION OF MARK A. FOX IN**
32) **SUPPORT OF EMERGENCY FIRST DAY**
33) **MOTIONS**
34) Hearing:
35) Date: July 15, 2013
36) Time: 2:00 p.m.
37) Place: United States Bankruptcy Court
38) Edward R. Roybal Federal Building
39) 255 E. Temple Street
40) Courtroom 1375
41) Los Angeles, CA 90012
42)
43)
44)
45)
46)
47)
48)

1 I, Mark A. Fox, hereby declare as follows:
2

3 **Introduction**

4 1. I am over 18 years of age and, if called as a witness, I could and would testify
5 to the matters set forth herein based upon my personal knowledge.

6 2. Colorep, Inc. ("**Colorep**") and Transprint USA, Inc. ("**Transprint**," and
7 together with Colorep, the "**Debtors**") commenced these cases by filing voluntary petitions for relief
8 under chapter 11 of the United States Bankruptcy Code (the "**Bankruptcy Code**") on July 10, 2013
9 (the "**Petition Date**").

10 3. On or about March 8, 2013, the Debtors formally engaged my firm, The Fox
11 Group to assist with the restructuring of the Debtors' operations. I assumed primary responsibility as
12 the Chief Restructuring Officer ("**CRO**") and interim Chief Executive Officer ("**Interim CEO**")
13 from or about March 8, 2013.

14 4. Based upon my personal knowledge of the Debtors, their business operations,
15 history, industry, and books and records, and based upon information contained in the Debtors'
16 books and records, I am qualified to give this declaration on behalf of the Debtors.

17 5. I submit this declaration in support of the following motions (collectively, the
18 "**Emergency Motions**"), each of which was filed shortly after the Petition Date by the Debtors:

19 (i) "*Ex Parte* Motion for Order Authorizing Joint Administration of Related
20 Chapter 11 Cases" (the "**Joint Administration Motions**");

21 (ii) " Emergency Motion For Order Limiting Notice And Permitting Service On
22 Insured Depository Institutions By First-Class Mail" (the "**Limit Notice Motion**");

23 (iii) "Emergency Motion For Order Extending The Deadline To File Schedules
24 and Statements of Financial Affairs" (the "**Schedules/Statements Extension Motion**");

25 (iv) "Emergency Motion for Order: (I) Deeming Utilities Adequately Assured of
26 Future Performance; and (II) Establishing Procedures for Determining Requests for Additional
27 Assurance Pursuant to Bankruptcy Code section 366 " (the "**Utilities Motion**")
28

1 (v) "Emergency Motion For Order Pursuant To 11 U.S.C. §§ 105 And 363
2 Authorizing (1) The Continued Maintenance Of Certain Existing Bank Accounts; (2) The Continued
3 Use Of Existing Cash Management System; And (3) The Continued Use Of Existing Business
4 Forms (the "**Cash Management Motion**");

5 (vi) "Emergency Motion For Authorization To Pay Prepetition Payroll And Other
6 Obligations And To Honor Prepetition Employment And Compensation Programs," (the "**Employee**
7 **Wage and Benefits Motion**"); and

8 (iiii) "Emergency Motion Of Debtors And Debtors In Possession For Interim And
9 Final Orders (1) Authorizing Post-Petition Financing; (2) Authorizing Use Of Cash Collateral; (3)
10 Granting Priming Liens And Superpriority Claims; (4) Providing Adequate Protection; And (5)
11 Granting Related Relief" (the "**Cash Collateral and DIP Financing Motion**," and together with the
12 foregoing, the "**First Day Emergency Motions**").

13 6. Except as otherwise indicated, all facts set forth in this Declaration are based
14 upon my personal knowledge, my review of relevant documents and court filings, and discussions
15 with employees, officers, directors, and other professionals retained by the Debtors in the prepetition
16 period. If I was called upon to testify, I could and would testify competently as to my knowledge
17 regarding the veracity of the facts set forth herein.

18 Background

19 A. General Background

20 7. Originally founded as a technology development company in 1989, the
21 company that later became known as Colorep shifted its focus in 2003 to industrial printing
22 applications. By 2005 Colorep had advanced its textile technology and had invented a patented
23 process for dyeing and decorating fabric known as AirDye®, which is widely regarded as
24 revolutionary because it does not result in water pollution and significantly reduces energy use, costs
25 and time from design to market.

26 8. In 2007 Colorep began licensing AirDye® technology to manufacturers and
27 resellers in the home interior, hospitality and apparel industries, which licensing continues to be very
28 profitable for Colorep.

1 9. Due to the success of the AirDye® technology, in September 2009, Colorep
2 began doing business as "AirDye Solutions."

3 10. At the end of 2007, Colorep acquired Transprint, a privately held, employee-
4 owned company, with headquarters and manufacturing facilities in Harrisonburg, Virginia..
5 Transprint, a leading supplier of transfer-printing paper was a strategic and potentially lucrative
6 acquisition for Colorep as it gave Colorep access to manufacturing capabilities, a global customer
7 base, and a design library exceeding 15,000 unique designs.

8 11. Transprint is the wholly-owned subsidiary of Colorep. Colorep is owned by
9 over 300 shareholders, with interests in 1 or more of the 5 series of preferred stock (Series A-E)
10 and/or in Colorep's common stock.

11 12. In addition to their production and manufacturing facility in Harrisonburg,
12 Virginia, the Debtors maintain operations in Charlotte, North Carolina and New York, New York.
13 The Debtors share common management, jointly own most assets and are co-obligors or
14 obligor/guarantor on most of the Debtors' collective obligations. Due to the commonalities, the
15 Debtors have not historically maintained separate books and records, but have the ability to
16 generally identify which entity owns a particular asset or is the sole or primary obligor on a
17 particular debt. Postpetition, the Debtors will maintain separate books and records.

18 **B. Events Leading to Chapter 11 Filing**

19 13. In 2011, the Debtors began experiencing significant cash flow constraints,
20 which rendered the Debtors unable to acquire necessary raw materials to meet customer demands
21 and purchase parts and supplies required for the maintenance of their equipment and manufacturing
22 and production facility in Virginia. As a result, the quality and availability of the Debtors' product
23 began to shrink and its key vendor and customer relationships were harmed.

24 14. In or around June 2011, the Debtors entered into that certain Loan and
25 Security Agreement (as amended, supplemented and modified, the "**Meserole Prepetition Loan**
26 **Agreement**") with Meserole, LLC ("**Meserole**"). Pursuant to the Meserole Prepetition Loan
27 Agreement, the Debtors had the ability to access up to \$25 million on the terms and conditions set
28

1 forth in the Meserole Loan and Security Agreement. In exchange, the Debtors granted Meserole a
2 first priority secured lien on virtually all of their tangible and intangible assets.

3 15. Unfortunately, Meserole loan did not result in the stabilization of the Debtors'
4 operations as had been hoped. Accordingly, throughout 2012, the Debtors continued to experience
5 cash shortages and, therefore, were unable to purchase necessary raw materials and timely produce
6 ordered product. Further, the Debtors were unable to sustain the quality of the product they did
7 produce as they lacked the capital necessary to improve or even perform necessary service and
8 repairs to the equipment utilized in their production process. The Debtors' inability to timely meet
9 demand and resolve the increasing quality control issues resulted in material cancellations and a
10 shrinking customer base.

11 16. The Debtors' working capital constraints also resulted in their inability to meet
12 their obligations to their employees in a timely and consistent manner. This resulted in significant
13 morale issues and ultimately in the loss of many key employees in 2012, which further diminished
14 their capacity to fulfill customer orders and meet obligations to vendors.

15 17. By the end of 2012, the situation had worsened and the Debtors went through
16 a number of "dark" periods during which time production halted completely and employees went
17 unpaid.

18 18. In March 2013, the Debtors, with the consent of their primary secured lender,
19 hired me as the Chief Restructuring Officer and interim Chief Operating Officer. Since that time, I
20 have worked to improve customer relationships and employee morale, and, most importantly, to try
21 and resolve the operational issues faced by the Debtors.

22 19. From March through June 2013, the Debtors adjusted staffing to appropriate
23 levels, minimized overall expenditures and eliminated expenditures that did not directly support the
24 Debtors' production and research and development operations. Further, the Debtors have focused on
25 rebuilding the most valuable customer and vendor relationships and on minimizing the Debtors'
26 exposure with respect to those relationships that had historically not been profitable. Moreover, the
27 Debtors focused on improving inventory analysis and control with an aim to improving the Debtors'
28 ability to timely meet customer orders. Although significant cash shortages did not permit extensive

1 business development efforts, to the extent feasible, the Debtors have worked to expand their
2 licensing activities to new, active markets around the globe.

3 20. Despite the significant improvements made since March 2013, it became clear
4 in June 2013, that the Debtors could not continue to operate absent either a material de-leveraging of
5 their balance sheet or significant, additional capital infusions. When it became clear that new capital
6 would not be available on reasonable terms, the Debtors determined that a chapter 11 process
7 whereby value of the Debtors' assets could be maximized through an efficient sale process was the
8 only feasible alternative.

9 21. Given the current, significant constraints and problems facing the Debtors, I
10 believe that if their assets are not sold on an expedited basis the value of such assets will continue to
11 deteriorate and the going concern value of the Debtors will be lost. In order to preserve the Debtors'
12 going concern value and to maximize the recovery on a sale of their assets from the Petition Date to
13 the closing of such sale, the Debtors will need access to cash collateral and the additional funds to be
14 lent to the Debtors on a postpetition basis by their prepetition lenders (and such other parties as may
15 ultimately participate) those lenders, including Meserole, that are proposing to provide the debtor-in-
16 possession financing described herein below and more fully in the motion with respect thereto.

17 **C. Description Of The Debtors' Secured Debt and Assets**

18 22. The Debtors' primary assets are its intellectual property rights and interests,
19 including numerous patents, pending patent applications and copyrights, its manufacturing and
20 operational facility in Harrisonburg, Virginia, its furniture, fixtures and equipment, and its design
21 studio and customer files in Charlotte, North Carolina and New York, New York.

22 23. As previously indicated, the Debtors' primary secured lender is Meserole,
23 which, as of the Petition Date, was owed approximately \$17 million, exclusive of interest, fees, costs
24 and expenses. Meserole asserts a validly perfected, first priority secured lien on virtually all of the
25 Debtors' assets.

26 24. Several other parties assert secured liens on the Debtors' assets, including,
27 significantly, taxing authorities, judgment lien creditors, and subordinated debt holders. It is
28 presently unclear whether such parties have legitimate secured claims, have validly perfected any

1 alleged security interests or liens, and/or whether any funds would remain after the satisfaction of
2 Meserole's claims to pay these allegedly secured claims even if they are determined to represent
3 legitimate debts of the Debtors.

4 **D. The First Day Emergency Motions**

5 • *Joint Administration Motion*

6 25. I believe that it would be wasteful to administer the estates of the Debtors
7 separately. The burdens on the Debtors and likely on the Court and creditors would be increased
8 materially if these cases were not jointly administered. Specifically, I believe the following reasons
9 support joint administration:

10 a. The Debtors are closely related entities, sharing common management
11 and ownership and common facilities in Harrisonburg, Virginia; Charlotte, North Carolina;
12 and New York, New York;

13 b. There is a substantial overlap in the Debtors' creditors. Jointly
14 administering the estates will eliminate unnecessary and expensive duplication of effort and
15 expenditure of valuable resources that would be caused by requiring the Debtors to prepare
16 and serve the same creditors with duplicative sets of differently captioned, but substantively
17 identical papers; and

18 c. Due to the integrated manner in which the Debtors operate their
19 business, some creditors may be uncertain as to which Debtor is their obligor. Joint
20 administration of the estates would provide each creditor with notice of all matters relating to
21 all of the Debtors, thereby insuring that creditors are fully informed of all matters potentially
22 affecting their claims.

23 26. I believe that joint administration will greatly reduce the cost of administering
24 the Debtors' cases and would eliminate the substantial waste, unnecessary paperwork, duplication,
25 and confusion that would otherwise be created by maintaining separate pleadings dockets for these
26 related cases. Most motions and other pleadings filed in these cases will concern both of the
27 Debtors. If such motions (and the related responses and other pleadings) were required to be filed
28 separately in each Debtor's case, it is likely that the only material difference among each set of

1 pleadings would be the caption. Thus, requiring each Debtor to file separate pleadings in each
2 matter would entail considerable duplication and additional paperwork at substantial cost, without
3 generating any additional benefit to creditors.

4 27. I believe that joint administration of the Debtors' cases will also benefit
5 creditors, because creditors who respond to motions affecting most or all of the Debtors, or who file
6 their own motions affecting most or all of the Debtors, will not be forced to prepare and file multiple
7 sets of papers that may be identical except for the captions.

8 28. The Debtors intend for each Debtor to have a separate claims register unless
9 the Court orders otherwise.

10 • **Limit Notice Motion**

11 29. Given that the Debtors potentially have hundreds of creditors and interest
12 holders, mailing of notices of all matters to all such parties in these cases would be impracticable and
13 would impose a heavy administrative and economic burden upon the Debtors' estates. This would
14 only further serve to reduce potential recoveries in these cases.

15 30. I therefore believe that it is appropriate under the facts and circumstances of
16 these cases to permit the Debtors to limit the parties upon whom notice should be served and to
17 further direct the manner in which such service should be effected as delineated in the Limit Notice
18 Motion.

19 31. The use of the proposed notice procedures is imperative in these cases where
20 resources are limited and would quickly be depleted if the Debtors were required to serve every
21 pleading filed in these cases on the hundreds of potential creditors and interest holders. Indeed, I
22 believe that providing notice of all matters to the large number of parties with potential claims and
23 interests, would: (a) delay substantially the provision of notice in each particular instance; (b) place a
24 heavy administrative burden on the Debtors' estates; and (c) impede the timely consummation of
25 transactions, the negotiation of settlements, or the granting of other relief that may be advantageous
26 to the Debtors' estates and their creditors.

27 • **Schedules/Statements Extension Motion**

1 32. Although the Debtors have been working diligently to prepare for these
2 chapter 11 filings, I believe that it will take additional time for the Debtors to analyze and compile
3 the information needed to complete their Schedules and Statements.¹ Consequently, I believe that it
4 is almost a certainty that the Debtors will *not* be able to prepare and file the Schedules and
5 Statements within fourteen days of the Petition Date. Specifically, I believe that the analysis and
6 compilation of the information for the Schedules and Statements will take additional time for the
7 following reasons:

8 a. There are urgent other demands upon the Debtors as a result of the
9 filing of these cases that will consume the time of the Debtors' small staff;

10 b. The Debtors, with the consent of their primary prepetition secured
11 lenders, brought Executive Sounding Board Associates Inc. ("**ESBA**") on board as of the Petition
12 Date, subject to Court approval, to aid the Debtors in analyzing their assets and liabilities and to
13 prepare for the expedited sale of the Debtors' assets. ESBA and its members require sufficient time
14 to get up to speed with respect to the Debtors' operations and to evaluate the Debtors' assets and
15 liabilities before they can properly evaluate the information comprising the Schedules and
16 Statements once compiled;

17 c. Certain of the Debtor's liabilities may constitute contingent,
18 unliquidated claims relating to obligations that are difficult to quantify; and

19 d. The Debtors do not have a large corporate staff available to perform
20 and/or oversee all work necessary to prepare the Schedules and Statements.

21 33. While the Debtors have commenced the process of assembling the
22 requisite information to prepare their Schedules and Statements, I believe that the fourteen-day
23 automatic extension of time to file such Schedules and Statements provided by Bankruptcy Rule
24 1007(c) will not be sufficient to permit completion of the Schedules and Statements.

25 34. At this juncture, I believe that an extension of twelve (12) additional days
26 will provide sufficient time for the Debtors to prepare and file their respective Schedules and
27

28 ¹ Capitalized terms not otherwise defined here are defined in the relevant motion.

1 Statements. Should the Debtors require additional time, they will return to the Court and seek
2 permission for an additional, brief extension.

3 • **Utilities Motion**

4 35. In connection with their ongoing business, the Debtors currently obtain
5 electricity, natural gas, water, telephone, telecommunications services, sewage, and other similar
6 services from thirteen (13) companies.

7 36. By their nature, the Utility Services are critical to the Debtors' operations and
8 cannot be replaced. This is particularly true as most of the Utilities provide necessary services at the
9 Debtors' Harrisonburg, Virginia production and manufacturing facility. Accordingly, if the Utility
10 Services were disrupted, even for a brief period, the Debtors simply could not operate, and the effect
11 on the value of the Debtors' estates would be devastating.

12 37. From July 1, 2012 through June 30, 2013, the Debtors owed these Utilities an
13 average of approximately \$45,190 per month for the Utility Services.

14 38. The Debtors intend to comply with Bankruptcy Code section 366 by
15 providing the Utilities with adequate assurance of payment as required. The Debtors will establish a
16 segregated escrow account into which the Debtors will deposit funds equaling two (2) weeks average
17 payments to all of the Utilities, for a total of \$22,595, which will serve as security for the Utilities
18 during the pendency of these cases.

19 39. The assurance proposed by the Debtors is substantial and represents a
20 significant portion of the cash available during the most difficult point in any bankruptcy case.

21 40. If Utilities are permitted to unilaterally terminate Utility Services on the 31st
22 day after the Petition Date because they insist on a greater deposit or some more onerous security,
23 they could severely disrupt the Debtors' operations, significantly diminish the Debtor's going
24 concern value, and jeopardize the Debtors' proposed sale and prospects for successful emergence
25 from chapter 11.

26 • **Cash Management Motion**

27 41. Prior to the Petition Date, the Debtors maintained two (2) funding accounts at
28 Union Bank, N.A. (the "**Funding Accounts**"). The Funding Accounts held money funded under the

1 Debtors' prepetition loan agreement. Funds in the Funding Accounts were swept to the Debtors'
2 operating accounts to pay operating expenses on an as needed basis.

3 42. As of the Petition Date, the Debtors intend to close this account and open a
4 new debtor in possession funding account (the "**DIP Funding Account**") with an approved
5 depository that will hold money funded under the Debtors' postpetition financing facility, if
6 approved.

7 43. Prior to the Petition Date, the Debtors also maintained one general account at
8 Wells Fargo Bank, N.A., bearing Account No. 2050000472204 (the "**General Account**"). This
9 account was used for the occasional check that would get mailed to the Debtors' office instead of its
10 lock box. The funds in the General Account were used for operations and could be wired out
11 directly to vendors or wired into the Transprint Operating Account (defined below) ending in 4181.
12 On the Petition Date, the Debtors intend to close the General Account.

13 44. In addition to the Funding Account and the General Account, the Debtors also
14 maintained three (3) operating accounts at Union Bank, N.A. prior to the Petition Date: one (1) in the
15 name of Colorep, bearing Account No. 1100970506 (the "**Colorep Operating Account**"), and two
16 (2) in the name of Transprint, bearing Account Nos. 3340060708 and 4100004181 (the "**Transprint**
17 **Operating Accounts**" and together with the Colorep Operating Account, the "**Operating**
18 **Accounts**"). Each of the Operating Accounts were funded by disbursements from their company's
19 respective deposit accounts. Through their Operating Accounts, the Debtors paid their vendors,
20 payroll and other operational expenses.

21 45. As of the Petition Date, the Debtors intend to close their Operating Accounts
22 and open new debtor in possession operating accounts (the "**DIP Operating Accounts**") with an
23 approved depository. Funds from the Debtors' existing Deposit Accounts (defined below) will be
24 swept daily into the DIP Operating Accounts, and will be used to pay the Debtors' obligations to
25 vendors, employees and other ordinary course operational expenses.

26 46. Additionally, the Debtors maintain three deposit accounts: two (2) in the name
27 of Colorep, bearing Account Nos. 1441098918 and 3523000028 (the "**Colorep Deposit Accounts**"),
28 and one (1) in the name of Transprint, bearing Account No. 3523000044 (the "**Transprint Deposit**

1 **Account**" and together with the Colorep Deposit Accounts, the "**Deposit Accounts**"). The Deposit
2 Accounts are all maintained at Union Bank, N.A., and are used to collect customer remittances,
3 which in turn are used to fund essential business expenses such as payroll through the Operating
4 Accounts. Prior to the Petition Date, the Deposit Accounts were manual transfer accounts, and the
5 funds in the Deposit Accounts were transferred to the Operating Accounts on an as-needed basis.
6 Generally, funds from the Deposit Accounts were transferred to the Operating Accounts
7 approximately three to four times per week.

8 47. In the Cash Management Motion, the Debtors are seeking the authority to
9 keep their existing Deposit Accounts open and operational for a limited, 21-day period after the
10 Petition Date, through July 31, 2013 (the "**Waiver Period**"). During the Waiver Period, the Debtors
11 will not have the ability to write checks or make wires from the Deposit Accounts, and the Deposit
12 Accounts will be swept daily into the DIP Operating Accounts. On or before the end of the Waiver
13 Period, the Debtors will close their Deposit Accounts and will open new debtor in possession deposit
14 accounts (the "**DIP Deposit Accounts**") with an approved depository.

15 48. I believe that the requested limited, 21- day waiver of the UST's requirement
16 that their Deposit Accounts be closed and new debtor in possession deposit accounts be opened post-
17 petition is necessary and justified under the unique circumstances of these cases. Specifically, I
18 believe that the Waiver Period is necessary to ensure that payments made by the Debtors' customers
19 to the Debtors are timely received and processed during the period immediately following the
20 Petition Date. The Waiver Period will allow the Debtors the opportunity to ensure that each of their
21 customers is made aware that they will be opening new DIP Deposit Accounts and should forward
22 any and all future payments to the DIP Deposit Accounts after the Waiver Period expires.

23 49. Because the Debtors' will be using cash receipts to help fund its ordinary
24 course operating expenses, the timely receipt of receivables is essential to the success of the Debtors'
25 ongoing business operations pending the sale of their assets. The Debtors therefore need time to
26 provide their customers with new banking and remittance information so as to avoid any further
27 disruption in their cash flow.

28

1 50. The Debtors are also seeking the authority to continue to utilize their existing
2 cash management system. Prepetition, the Debtors accessed and controlled the Prepetition Accounts
3 from their offices through the use of an on-line banking system. In the ordinary course of business,
4 the centralized on-line banking system was utilized to transfer monies collected by the Debtors to
5 fund business operations. The banking system facilitated cash forecasting and reporting, allowed the
6 Debtors to monitor collections and disbursement of funds, and maintain control over the
7 administration of the various bank accounts. The Debtors' online banking functionality and all other
8 procedures that the Debtors use to transfer and monitor funds among accounts allowed the Debtors
9 to conduct business in the ordinary course, and collectively comprise the Debtors' "Cash
10 Management System."

11 51. The benefits that the Cash Management System provide are critical to the
12 Debtors' collection, disbursement and movement of cash, and the Debtors desire the ability to
13 continue utilizing its Cash Management System after the Petition Date so as not to further disrupt
14 operations and delay their efforts to commence the sale process. The Cash Management System
15 assures prompt receipt and allocation of funds and the generation of timely and accurate financial
16 information necessary to manage the Debtors' operations.

17 52. I believe that the failure to preserve the Cash Management System in
18 essentially the same manner as it existed prepetition, particularly at a time when the Debtors are
19 subject to the operational dislocation attendant to these chapter 11 filings, would severely disrupt the
20 Debtors' ordinary financial affairs and business operations, and would likely interfere significantly
21 with efforts to preserve and maximize value.

22 53. Finally, the Debtors are seeking the authority to continue to use their existing
23 business forms after the Petition Date. I believe that changing correspondence and business forms
24 would be expensive, unnecessary, and burdensome to the Debtors' estates and disruptive to the
25 Debtors' business operations and would not confer any benefit upon those dealing with the Debtors.
26 Parties doing business with the Debtors will undoubtedly be aware of the Debtors' status as debtors
27 in possession, and will receive direct notice of the commencement of the Debtors' cases. Moreover,
28

1 any payments made by the Debtors postpetition will be made from newly opened "debtor in
2 possession" accounts, and their checks will designate their status as "debtors in possession."

3 • **(Non-Insider) Employee Wages And Benefits Motion**

4 54. As of the Petition Date, the Debtors directly employed approximately 101 full
5 and part time employees. These non-insider employees work in the Debtors' manufacturing and
6 production plant in Harrisonburg, Virginia (the "**Virginia Plant**"), the Debtors' design office in
7 Charlotte, North Carolina (the "**Carolina Office**") or the Debtors' sales office in New York, New
8 York (the "**New York Office**").

9 55. Approximately two-thirds of the Debtors' employees are paid wages on an
10 hourly basis, and the remaining one-third are salaried. The Debtors' hourly employees are to be paid
11 on a weekly basis and salaried employees are to be paid on a bi-weekly basis on Fridays. The
12 Debtors retain a third-party payroll service, Custom Payroll, to prepare paychecks for the Debtors'
13 employees, which checks are paid directly from the Operating Accounts.

14 56. The Debtors' last regularly-scheduled payday was Friday, July 5, 2013, on
15 which date employees were paid amounts that had accrued but gone unpaid through and including
16 June 14, 2013.² No wages or salaries have been paid to employees for services provided during the
17 period beginning June 22, 2013 through the Petition Date.

18 57. As of the Petition Date, the Debtors estimate that they will owe no more than
19 \$500,213.47³ in prepetition wages, salaries, commissions, and reimbursable expenses to non-insider
20 employees of the Debtors. The Debtors are not seeking to pay any insider employees any prepetition
21 amounts pursuant to the Employee Wages and Benefits Motion.

22 58. As of the Petition Date, the Debtors' would require approximately
23 \$388,213.47 to satisfy their existing payroll obligations to non-insider employees for accrued but
24 unpaid payroll during the 180-days prior to the Petition Date.

25 _____
26 ² On June 28, 2013, the Debtors made payroll, paying employees for services provided for the
week ending June 21, 2013.

27 ³ This number is comprised of the amounts owed by the Debtors for accrued, unpaid wages
28 (\$388,213.47), accrued, unpaid commissions (\$42,000), and accrued, unpaid reimbursable
expenses (\$70,000).

1 59. In addition to base pay, certain of the Debtors' non-insider employees are
2 entitled to payment in the form of commissions. Five (5) of the Debtors' employees, specifically,
3 sales workers and the Debtors' studio manager, are entitled to receive commissions in certain
4 circumstances. As of the Petition Date, the Debtors' estimate that they will owe a total of
5 approximately \$42,000 to these five (5) employees as a result of commissions earned, but not yet
6 paid, for the 180-day period prior to the Petition Date.

7 60. Certain of the Debtors' sales force and executive management are also entitled
8 to reimbursement for business expenses, including travel, meals, and entertainment. As of the
9 Petition Date, the Debtors estimate that they owe such people approximately \$70,000 for
10 reimbursable expenses, including expenses which have accrued but have not yet been submitted.

11 61. The Debtors' significant cash-flow shortages in the prepetition period, coupled
12 with the commencement of these cases, have disrupted the Debtors' normal operations and payment
13 policies. I believe that unless the Debtors can promptly assure their employees that they will timely
14 meet their employee-related obligations, the going-concern value of their businesses and their ability
15 to maximize proceeds from the contemplated sale of their assets will be irreparably harmed and
16 significantly diminished.

17 62. The Debtors lost a significant number of employees in the prepetition period
18 and I believe that the Debtors' remaining employees are the key to their continued ability to operate
19 successfully and preserve the going-concern value of the businesses. It is my belief that the failure
20 to timely pay employees and a failure to honor their existing benefits would likely lead to further
21 employee losses, decreased productivity and product quality, and would harm the already faltering
22 employee morale.

23 63. Unquestionably, if the Debtors' remaining employees were to leave *en masse*
24 as a result of the Debtors' chapter 11 filings, it would devastate the Debtors' operations and would
25 result in a significant devaluation of the Debtors' assets, which are to be sold on an expedited basis in
26 these cases.

27 64. Therefore, I believe that if the Debtors do not receive authority, in their sole
28 and absolute discretion and subject to availability, to honor their existing obligations to employees,

1 they are highly unlikely to be able to retain the personnel necessary to operate and maintain
2 operations until a sale can occur.

3 65. Accordingly, I believe it is imperative that the Debtors be given the authority,
4 in their sole discretion, to pay prepetition compensation that remained unpaid as of the Petition Date
5 and accrued during the 180-days prior thereto as, if and when funding becomes available and in
6 accordance with the budget approved by the Debtors' proposed postpetition lenders. The Debtors
7 will not pay any amounts to insiders and will not exceed the statutory cap for priority wage claims.

8 66. The Debtors also provide their employees with certain benefit programs in
9 addition to wages and salaries. These benefit programs include medical benefits (including
10 prescription drug benefits), dental insurance, life insurance (including accidental death and
11 dismemberment insurance), workers' compensation insurance, disability insurance, and 401(k)
12 benefits (collectively, "**Benefits**").

13 67. On average, the total monthly cost to the Debtors with respect to such benefits
14 is approximately \$69,555. As of the Petition Date, the Debtors estimate that they owe approximately
15 \$466,752.62 in past-due Benefits-related payments, which amount is comprised primarily in past-
16 due insurance premiums. As with employee wages, I believe that the Debtors must be given the
17 authority, in their sole discretion, to pay those amounts necessary to continue to provide Benefits to
18 their employees, as, if and when funding becomes available and in accordance with the budget
19 approved by the Debtors' postpetition lenders.

20 68. If the Debtors cannot promptly assure their employees of uninterrupted
21 payments of wages, as well as continuing Benefits, I believe their operations will suffer immediate
22 and irreparable harm due to resulting employee resentment and resignations and a loss of employee
23 goodwill, or, at the very least, the disintegration of employee morale. Given that the Debtors are
24 attempting to sell their businesses on a going-concern basis, the retention of good employees is
25 critical to the success of the sale process.

26 • **Cash Collateral And DIP Financing Motion**

27 69. The Debtors have obtained a commitment, subject to the Court's approval,
28 from Meserole (together with other lenders from time to time party to the DIP Financing Facility, the

1 "**DIP Lenders**"), pursuant to which Meserole, as prepetition lender, will permit the use of its cash
2 collateral ("**Cash Collateral**") and the DIP Lenders will provide up to \$2 million in postpetition
3 financing pursuant to the 13-week budget annexed to the Interim Order, which the Debtors require to
4 operate their business, conduct a transparent and efficient sale of their assets or, possibly, emerge
5 from chapter 11 pursuant to a confirmed chapter 11 plan.

6 70. The Debtors need funding from the DIP Financing Facility and use of Cash
7 Collateral in order to cover the Debtors' budgeted operating and administrative expenses pending a
8 sale of their assets or a conclusion of these cases. Absent authorization to utilize the proceeds of the
9 DIP Financing Facility and Cash Collateral, the Debtors will have insufficient cash available to
10 conduct ordinary business operations and to maintain and preserve the value of the Debtors'
11 businesses and operations pending a sale of their assets.

12 71. As set forth in the Budget, the Debtors will need the infusion of working
13 capital from the DIP Financing Facility and Cash Collateral during the initial weeks of this
14 chapter 11 case primarily to: (a) fund the payment of obligations in the ordinary course of business
15 (including payroll obligations) in order to maintain the going concern value of, and maximize the
16 ultimate return to, the Debtors' estates; (b) address the extraordinary demands on cash created by
17 vendors refusing to grant ordinary credit terms and assist in maintaining ongoing relationships with
18 these vendors; (c) permit the Debtors to honor pre-petition employee payroll and benefit claims to
19 prevent significant losses of necessary personnel for ongoing operations; and (d) fund the expenses
20 of professionals who are necessary for the ultimate success of the sale process.

21 72. I believe that the expenses identified in the Budget are reasonable and
22 necessary business expenses that must be paid in order to continue their business, and maintain the
23 value of the Debtors' businesses and operations pending the sale of their assets. The Debtors will
24 suffer immediate, irreparable injury if they are not allowed to gain access to the DIP Financing
25 Facility and Cash Collateral in accordance with the Budget.

26 73. Given the Debtors' current financial condition, their capital structure and,
27 most significantly, the fact that Meserole, as the Debtors' primary prepetition lender, has senior liens
28 on substantially all of the Debtors' assets, the Debtors could not obtain postpetition financing: (a) on

1 a solely unsecured basis allowable as an administrative expense; (b) solely on a junior secured basis ;
2 or (c) on any other basis that I am told would be permissible under the Bankruptcy Code.

3 74. Based upon the Debtors' evaluation of alternative funding sources prior to the
4 Petition Date, I believe that the terms of the proposed DIP Financing Facility as described in the DIP
5 Term Sheet are more favorable to the Debtors than any other financing arrangement they could
6 realistically expect to obtain from any other financing source.

7 75. The terms and conditions of the DIP Term Sheet were the subject of
8 significant and extensive prepetition negotiations between the Debtors and the DIP Agent, and are
9 fair and reasonable under the circumstances of these cases.

10 76. The Debtors were forced to file these cases on an expedited basis and as a
11 result of mounting liabilities and insufficient cash. While they evaluated the alternative of obtaining
12 debtor in possession financing from other lenders, they concluded that, to the extent that they could
13 even obtain any sort of debtor in possession financing from lenders other than the DIP Lenders, they
14 would be unable to obtain terms any more favorable than those offered under the DIP Term Sheet.

15 77. I believe the Debtors' decision to enter into the DIP Financing Facility
16 represents an exercise of sound business judgment in the continued operation of the Debtors'
17 business and preservation of asset value. Like most business decisions, the Debtors' decision to
18 enter into the DIP Financing Facility will both confer a number of benefits on the Debtors and
19 impose several tradeoffs. The DIP Financing Facility should provide the Debtors with sufficient
20 capital to operate their business in the ordinary course, pending the marketing and sale of the assets
21 as a going concern. The DIP Agent and the DIP Lenders have also agreed to fund certain carve-outs
22 for payment of statutory fees, approved professional fees, and other necessary expenses.

23 78. In exchange for the foregoing, the Debtors have agreed, among other things,
24 that: (i) the Debtors' obligations under the DIP Financing Facility shall be secured by a lien on
25 substantially all of the Debtors' assets; (ii) post-petition borrowings will bear interest at a rate of no
26 less than 16% per annum; (iii) the Debtors shall pay certain fees to the DIP Lenders, the DIP Agent
27 and the Pre-Petition Lender; (iv) the Debtors will provide financial information to the DIP Agent and
28 the DIP Lenders; (v) the Debtors will waive certain claims, rights and powers against Pre-Petition

1 Lender and its collateral; and (vi) the Debtors will request that this Court, as part of the Final Order
2 approving the DIP Financing Facility, set a bar date for challenges to any claims or liens of Pre-
3 Petition Lender.

4 79. In sum, the substantial benefits the Debtors will derive from the proposed
5 financing amply justify the Debtors' decision to enter into the DIP Financing Facility, a decision that
6 I believe the Court should ratify as being in the best interests of the Debtors and their estates.

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1 I declare under penalty of perjury under the laws of the United States of America that
2 the foregoing is true and correct.

3 Executed at Harrisonburg, Virginia on July 11, 2013.

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5 _____
6 Mark A. Fox
7 Chief Restructuring Officer and
8 Interim Chief Executive Officer
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