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6
7 Reorganization Counsel
for Debtors and Debtors in Possession

8 Debtors' Mailing Address:
Colorep, Inc. and Transprint USA, Inc.
9 100 Pleasant Valley Road
Harrisonburg, VA 22801-9790
10 Attn: Robert Katz, [Proposed] CRO

11 **UNITED STATES BANKRUPTCY COURT**
12 **CENTRAL DISTRICT OF CALIFORNIA**
13 **LOS ANGELES DIVISION**

13 In re)
14)
15 COLOREP, INC.,)
a California corporation, *et al.*,)
16)
Debtors.)
17)
18 Tax I.D. Nos. 94-3055026 (Colorep, Inc.) and)
54-1200596 (Transprint USA, Inc.))

) Case No. 13-bk-27689-WB
)
) Chapter 11
) (Jointly Administered)

) **DECLARATION OF ROBERT D. KATZ**
) **IN SUPPORT OF DEBTORS' MOTION**
) **FOR ORDER PURSUANT TO**
) **BANKRUPTCY CODE SECTIONS 105,**
) **363, AND 365 APPROVING SALE OF**
) **THE DEBTORS' ASSETS FREE AND**
) **CLEAR OF INTERESTS**

) **Hearing Date**

) DATE: October 3, 2013
) TIME: 10:00 A.M.
) PLACE: Courtroom 1475
) 255 East Temple Street
) Los Angeles, CA 90012
)

1 I, ROBERT D. KATZ, declare as follows:

2 1. I am over 18 years of age and if called upon I would and could competently
3 testify to the matters set forth herein from my own personal knowledge. I am a Managing Director
4 of Executive Sounding Board Associates Inc. ("ESBA"), a financial and management consulting
5 firm having expertise in turnaround, bankruptcy and financial advisory issues. ESBA has provided
6 clients with financial and management consulting services for over thirty-five (35) years, and
7 ESBA's consultants individually have on average over thirty (30) years of business experience.

8 2. I am a Certified Public Accountant and a Certified Turnaround Professional. I
9 hold a Masters in Business Administration from Temple University, and a BSE in accounting and
10 management from the Wharton School of Business at the University of Pennsylvania. I have led
11 companies through crises and turnarounds for over twenty-two (22) years. In many instances, I have
12 acted as Interim President, Chief Financial Officer, Chief Operating Officer, Chief Restructuring
13 Officer, or Treasurer.

14 3. ESBA has been retained by Colorep, Inc. and Transprint USA, Inc.
15 (collectively, the "Debtors") to serve as their Chief Restructuring Officer ("CRO"), application
16 pending in this Court. I am the supervising professional at ESBA with primary responsibility over
17 ESBA's role as CRO for the Debtors. In addition, certain of my staff at ESBA has been retained to
18 similarly provide crisis management services for the Debtors as a part of the Debtors' pending
19 bankruptcy proceedings. ESBA has been serving as the Debtors' CRO since early July 2013. I am
20 involved in and supervise the ongoing business affairs, day-to-day operations, financial condition,
21 and books and records of each of the Debtors. I have also played a primary role in coordinating with
22 the Debtors' bankruptcy counsel in matters relating to the Debtors' pending chapter 11 bankruptcy
23 proceedings. Moreover, I have personal familiarity with the Debtors' general operations and
24 obligations in their pending bankruptcy proceedings.

25 4. I submit this Declaration in support of the Debtors' *Supplemental*
26 *Memorandum of Points and Authorities in Support of Debtors' Motion for Order Pursuant to*

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1 *Bankruptcy Code Sections 105, 363, and 365 Approving Sale of the Debtors' Assets Free and Clear*
2 *of Interests* (the "Sale Motion").¹

3 **A. General Background.**

4 5. The Debtors are companies engaged in the business of industrial printing in
5 the textile industry. The Debtors hold, and have applied for, the patents for a process for dyeing and
6 decorating fabric, which is novel because the process does not result in water pollution and
7 significantly reduces energy use, costs and time from design to market.

8 6. Beginning in 2007, Colorep licensed this technology to manufacturers and
9 resellers. At the end of 2007, Colorep acquired Transprint, a privately held, employee-owned
10 company, with headquarters and manufacturing facilities in Harrisonburg, Virginia. In addition to
11 their production and manufacturing facility in Harrisonburg, Virginia (the "Harrisonburg Factory"),
12 the Debtors maintain sales operations in Charlotte, North Carolina and New York, New York. The
13 Debtors also own proprietary designs and trademarks. Although the Debtors' operations are
14 geographically dispersed, and each of the Debtors have different asset bases and different creditor
15 constituencies, the business of the Debtors is conducted in a centralized manner as parts of a unified
16 whole. It is partially for this reason that, as explained below, the Debtors' assets were marketed as a
17 package, rather than in separate pools of assets specific to each Debtor.

18 **B. Prepetition Loan and Security Agreement with Meserole.**

19 7. In or around June 2011, in response to significant cash flow restraints, the
20 Debtors entered into that certain Loan and Security Agreement and related documents (as amended,
21 supplemented and modified, the "Prepetition Loan Agreement") with Meserole. Pursuant to the
22 Prepetition Loan Agreement, Colorep had the ability to access up to \$25 million on the terms and
23 conditions set forth in the Prepetition Loan Agreement (the "Prepetition Loan"). Meserole asserts a
24 first priority secured lien on substantially all of the Debtors' tangible and intangible assets as security
25 for the Prepetition Loan.

26
27 ⁱ Capitalized terms not otherwise defined herein shall have the meaning afforded to them in the
28 Sale Motion.

1 8. Meserole has filed a Proof of Claim against the Debtors [Claim No. 14-1],
2 alleging that, as of the Petition Date, the Debtors owe Meserole \$20,083,057.80 under the
3 Prepetition Loan, secured by the Debtors' real and personal property.

4 9. With the assistance of their reorganization counsel, the Debtors have
5 conducted an investigation as to the validity and priority of the liens Meserole contends secure the
6 Prepetition Loan (the "Prepetition Loan Collateral"). Based on the Debtors' investigation, the
7 Debtors believe Meserole has a first priority lien on all of the Debtors' real and personal property
8 against which it asserts an interest, except with respect to, among other potential issues, perfection of
9 certain of the intellectual property assets and commercial tort claims, and documentation with
10 respect to modifications of the Prepetition Loan, for which the Debtors have raised a challenge with
11 Meserole pursuant to the terms and conditions of the Final DIP Order, thereby preserving such
12 challenges. Meserole disputes the challenges and asserts they lack merit.

13 10. With respect to the Debtors' Harrisonburg Factory, the Debtors have identified
14 only one deed of trust recorded with the Rockingham County Recorder of Deeds, other than deeds of
15 trust which secure obligations that have been paid or otherwise satisfied. This deed of trust was
16 recorded on August 15, 2011 in favor of Meserole. The Debtors have also identified six (6)
17 individuals or entities asserting interests in the Harrisonburg Factory junior to the deed of trust of
18 Meserole, having recorded money judgments against the Debtors in the Commonwealth of Virginia
19 subsequent to August 15, 2011 (the "Harrisonburg Junior Lienholders").

20 11. The Debtors also own personal property, consisting of, among other things,
21 intellectual property, equipment, inventory, cash and account receivables (the "Personal Property").
22 The Debtors' investigation has uncovered only two UCC-1 financing statements filed by parties prior
23 to the filing of the UCC-1 financing statement by Meserole (the "2010 Liens"). The Debtors' records
24 show that the obligations secured by the 2010 Liens were satisfied in full as part of the Prepetition
25 Loan from Meserole, and no amounts were owing to the holders of the 2010 Liens as of the Petition
26 Date. The Debtors have also identified a number of individuals or entities (together with the
27 Harrisonburg Junior Lienholders, the "Junior Lienholders") that have filed UCC-1 financing
28

1 statements or obtained judgment liens against the Debtors' assets subsequent to Meserole's perfection
2 of its security interest in the Personal Property.

3 12. Based on the foregoing, except as stated above, the Debtors believe
4 Meserole's Prepetition Loan is secured by a valid first priority lien on the Debtors' Personal Property
5 and real property.

6 **C. DIP Financing.**

7 13. As set forth more fully in the Final DIP Order, the Debtors entered into an
8 agreement with Meserole, pursuant to which Meserole, or any successor, agreed to provide
9 postpetition financing to the Debtors in the amount of \$2.5 million (the "DIP Financing"), and
10 consented to the Debtors' use of cash collateral, pursuant to a set budget. The DIP Financing is
11 secured by a security interest in all of the Debtors' tangible and intangible property, except for
12 avoidance actions (the "DIP Financing Lien"). Through the DIP Financing, the Debtors have been
13 able to operate in the ordinary course of business, thereby working to preserve going concern value
14 of the Debtors' assets.

15 **D. Compliance with the Sale Procedures.**

16 14. On August 12, 2013, the Court entered the Sale Procedures Order, setting
17 forth procedures for the Debtors to, among other things, market and provide notice of a sale of the
18 Debtors' assets and the potential assumption and assignment of executory contracts to interested
19 parties. The Debtors have satisfied all of the obligations set forth in the Sale Procedures Order, as
20 specifically described below.

21 15. On August 13, 2013, the Debtors served the *Notice of Auction and Sale*
22 *Hearing* on all of the Debtors' known creditors (the "Creditors Notice"), notifying such creditors
23 that, among other things, September 18, 2013 (the "Bid Deadline") was the deadline for parties to
24 submit bids for the purchase of the Debtors' assets, and that the Court would hold a hearing on the
25 Debtors' proposed Sale on September 26, 2013 (the "Sale Hearing").

26 16. On August 15, 2013, the Debtors served the *Notice of Sale Procedures,*
27 *Auction Date and Sale Hearing* (the "Sale and Bid Procedures Notice") on all parties required to be
28 notified under the Sale Procedures Order, including but not limited to all known parties asserting a

1 security interest in any of the Debtors' assets, all parties to prepetition litigation with the Debtors,
2 and environmental authorities in the states in which the Debtors conduct business .

3 17. On August 27, 2013 and September 9, 2013, the Debtors filed and served the
4 *Notice to Counterparties to Executory Contracts and Unexpired Leases That May Potentially be*
5 *Assumed and Assigned* (the "Original Cure Notice") and the *First Supplemental Notice to*
6 *Counterparties to Executory Contracts and Unexpired Leases That May Potentially be Assumed and*
7 *Assigned* (the "First Supplemental Cure Notice"), respectively. On September 13, 2013, the Debtors
8 filed and served a *Second Supplemental Notice to Counterparties to Executory Contracts and*
9 *Unexpired Leases That May Potentially be Assumed and Assigned* (the "Second Supplemental Cure
10 Notice", and together with the Original Cure Notice and the First Supplemental Cure Notice, the
11 "Cure Notice"). The Second Supplemental Cure Notice served the Cure Notice on parties that were
12 served with the Original Cure Notice, but for which the Debtors received returned mail. The Cure
13 Notice provided notice to all known counterparties to executory contracts and unexpired leases (the
14 "Contract Counterparties") the amounts necessary to cure outstanding defaults under Bankruptcy
15 Code section 365(b)(1) (the "Cure Amounts"), and the procedures for objecting to the Debtors'
16 proposed Cure Amounts and to the assumption and assignment of any executory contracts or
17 unexpired leases.

18 18. On September 20, 2013, the Debtors served on Contract Counterparties to a
19 contract or lease that the Buyer desires the Debtors to assume and assign in connection with the Sale
20 (the Assigned Contracts), a notice that the Debtors intend to assume and assign such contracts or
21 leases to the Buyer under Bankruptcy Code section 365(f) (the "Assumption Notice").

22 **E. The Sale Process.**

23 19. Having decided that a sale of substantially all of the Debtors' assets would be
24 in the best interests of the Debtors' estates, the Debtors have engaged in a marketing process
25 designed to generate maximum value for the Debtors' assets. In order to implement such a
26 marketing process, the Debtors engaged Hilco IP Services LLC d/b/a Hilco Streambank ("Hilco") to
27 act as the exclusive agent for the marketing and sale of the Debtors' assets. I was actively involved
28 in assisting Hilco in the marketing of the Debtors' assets, and regularly engaged in conference calls

1 with representatives of Hilco and the Debtor's reorganization counsel as to the status and strategy
2 surrounding the marketing and bid process for the Debtors' assets.

3 20. Despite Hilco's efforts, no interested parties submitted a "Qualified Bid" for
4 the Debtors' assets prior to the Bid Deadline, as required under the Court-approved Sale Procedures.

5 **F. The Agreement with the Buyer.**

6 21. During the course of these cases, Meserole advised the Debtors that it, acting
7 alone or in concert with others, intended to make a bid for the assets of the Debtors, and would use
8 its prepetition and post petition claims for a "credit bid." On September 15, 2013, the Debtors
9 received a proposed Asset Purchase Agreement from Meserole and Fuller Smith, as purchasers
10 (collectively, the "Buyer"). Subsequently, on the Bid Deadline, the Debtors received another
11 proposed agreement from the same parties. Pursuant to the APA, Meserole and Fuller Smith intend
12 to assign their rights and interests under the APA to AirDye Solutions, LLC. The Debtors and the
13 prospective Buyer engaged in extensive negotiations covering a wide variety of terms and
14 conditions regarding the proposed purchase agreement. As a result, the Debtors and the Buyer
15 reached an agreement, as reflected in the APA, a true and correct copy of which is attached hereto as
16 Exhibit "A", which the Debtors believe will provide the best possible outcome for their respective
17 estates.

18 22. The consideration the Debtors shall receive in exchange for the Acquired
19 Assets (the "Purchase Price"), is summarized as follows:

20 (a) a credit bid in the amount of \$20 million consisting of:

21 (i) a credit bid by Fuller Smith of \$250,000 of the amount outstanding under
22 the DIP Financing (the "DIP Financing Credit Bid"); and

23 (ii) a credit bid by Meserole of the outstanding amount owing under the
24 Prepetition Loan in the amount equal to \$20 million less the DIP Financing Credit Bid, which
25 amount is \$19,750,000;

26 (b) the Buyer's payment of Cure Amounts for all Assigned Contracts and the
27 assumption of the "Assumed Liabilities," as that term is defined in the APA; and

28 (c) the payment of \$25,000.

1 23. Under the terms of the APA, the Assumed Liabilities the Buyer has agreed to
2 assume and pay include, without limitation, (i) certain accrued but unpaid operating expenses and
3 payables incurred by the Debtors after the Petition Date and prior to the Closing Date in the ordinary
4 course of business, (ii) certain unpaid but yet to be incurred operating expenses of the Debtors, (iii)
5 certain pre-petition wage claims and PTO obligations owed to the Debtors' employees and (iv)
6 certain other administrative expenses, including certain professional fees, and also include those
7 expenses and obligations listed on Schedule 2.3(f) to APA. The liabilities assumed by the Buyer
8 will result in the payment of substantially all of the administrative expense claims incurred by the
9 Debtors in the ordinary course of business, certain administrative professional fees and certain pre-
10 petition priority wage and PTO obligations of the Debtors to their employees.

11 24. As a result of the Credit Bid, a significant portion of the Prepetition Loan will
12 be satisfied and I have been advised that the Debtors will have no remaining obligations with respect
13 thereto other than as part of the Remaining Lender Claim (as defined below) . In addition, as part of
14 the APA, any remaining amount of the DIP Financing and Prepetition Loan not satisfied pursuant to
15 the Credit Bid, approximately \$2,500,000 (the "Remaining Lender Claim"), I have been advised that
16 it will be treated solely as unsecured claim against the Debtors and their respective estates. Any
17 remaining liens or security interests shall be deemed released. I have been advised that the
18 Remaining Lender Claim will have no rights or remedies against the Debtors or their respective
19 estates inside or outside of bankruptcy except to use the Remaining Lender Claim for the purpose of
20 asserting such claim as an unsecured claim and as a defense, offset, recoupment or similar right or
21 defense against any Person asserting a claim or cause of action that is derivative of the Debtors'
22 rights or those of the Debtors' estates which have been transferred and assigned to the Purchaser
23 pursuant to this Agreement.

24 25. In sum, as a result of the proposed Sale, the Debtors will, through the
25 assumption and payment of the Assumed Liabilities by the Buyer, satisfy certain administrative
26 claims and expenses against their estates and certain priority claims that would not take place in the
27 absence of the proposed Sale. Moreover, by selling the Acquired Assets while operating as a going
28 concern, the deal provides for the preservation of jobs of at least 77 employees.

1 26. I believe the proposed sale of the Debtors' Acquired Assets to the Buyer, or its
2 assignee, under the terms of the APA is in the best interests of the Debtors' estates. Moreover, in
3 light of Hilco's substantial marketing efforts, and the monetary and time limits imposed by the terms
4 of the DIP Financing, I do not believe the Debtors could have received any consideration for the
5 purchase of their assets that is materially greater than what is being provided under the proposed
6 Sale. Accordingly, I believe the Debtors' request for approval of the sale of substantially all of the
7 Debtors' assets under the terms of the Final APA represents a sound exercise of the Debtors' business
8 judgment.

9 27. I understand that pursuant to section 363(f) of the Bankruptcy Code, the
10 Debtors' assets may be sold and transferred free and clear of all liens, claims, interests and
11 encumbrances except as otherwise provided in the Final APA and that is a requirement of the Sale.

12 28. It is not the purpose of the Sale or the intent of the Debtors that the
13 Purchasers, the Purchaser Assignee, or their respective affiliates, managers, successors or assigns, as
14 a result of the consummation of the transactions set forth in the Final APA: (i) be a successor to the
15 Debtors or the Debtors' estates; (ii) have, de facto or otherwise, merged or consolidated with or into
16 the Debtors or the Debtors' estates; (iii) be a continuation or substantial continuation of the Debtors
17 or any enterprise of the Debtors; or (iv) be a joint employer or co-employer with, or successor
18 employer of the Debtors.

19 29. I have been advised that other than the Assumed Liabilities and other
20 obligations contemplated by the Final APA and by the Assignment and Assumption Agreement
21 executed in connection therewith, the Purchaser Assignee and its affiliates (including Purchasers) is
22 not assuming and will not in any way be responsible for any claim, lien, liability or obligation of the
23 Debtors and/or their estates.

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