IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	Chapter 11
	)	
Axion International, Inc., *et al*.,[1]	)	Case No. 15-12415 (CSS)
	)	(Jointly Administered)
Debtors.	)	
	)	**Objections Due: February 17, 2016 @ 4:00 p.m. (ET)**
	)	**Hearing Date: February 24, 2016 @ 10:00 a.m. (ET)**
	)	

MOTION OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS FOR AN ORDER DIRECTING THE APPOINTMENT OF A CHAPTER 11 TRUSTEE UNDER 11 U.S.C. § 1104

The Official Committee of Unsecured Creditors (the "Committee") appointed in the chapter 11 cases (the "Chapter 11 Cases") of the above-captioned debtors-in-possession (the "Debtors"), by and through its undersigned proposed counsel, moves for an order directing the appointment of a Chapter 11 trustee in the Chapter 11 Cases pursuant to 11 U.S.C. § 1104(a)(1) and 1104(a)(2) and Rule 2007.1 of the Federal Rules of Bankruptcy Procedure (the "Trustee Motion"). In support of the Trustee Motion, the Committee respectfully states as follows:

PRELIMINARY STATEMENT

1. From day one, the only concern of the Debtors in these cases has been how to give all the Debtors' assets to Allen Kronstadt and/or his affiliated entities (collectively, "Kronstadt") for nothing, and they have never wavered from this goal. The Committee has lost faith in Debtors' management as the Debtors' management continues to eschew opportunities to realize value for the creditors through a meaningful sale process, a liquidation or a reorganization. No thought has been given to any alternative other than getting the assets into Kronstadt's hands.

[1] The Debtors are Axion International, Inc., Axion International Holdings, Inc., and Axion Recycled Plastics Incorporated.

2. A month has passed since the hearing denying the final DIP order and bidding procedures, and instead of seriously considering the full gamut of options, the Debtors continue to try to force a failed insider 363 sale on the Committee on a tight schedule that this Court has already denied. This time, the Debtors hope to have the Court's blessing simply by adding Gordian Group and its $250,000 upfront administrative expense fee, which actually puts unsecured creditors in a worse position.

3. Make no mistake, Gordian has not been provided with full discretion to consider all alternatives as directed by the Court at the January 4th hearing. Rather, Gordian's engagement is limited to a proposed sale with gerrymandered lots of assets, so that each lot is secured either by Kronstadt or the DIP Lender with whom he is colluding. Gordian's engagement letter expressly states it is limited to a 363 sale and does not cover a liquidation. Dkt. No. 139-2, Ex. A at Sch. 1 (Jan. 20, 2016 ltr. at ¶ 1). Gordian cannot advise whether a liquidation or a plan of reorganization would provide more value to creditors. Still no attempt has been made to value various assets, including the causes of action *in which Kronstadt has no liens*.

4. This approach is contrary to management fulfilling its fiduciary duties to creditors. *See In re Marvel Entm't Grp., Inc.*, 140 F. 3d 463, 471 (3d Cir. 1998)("The debtor-in-possession is a fiduciary of the creditors, and, as a result, has an obligation to refrain from acting in a manner which could damage the estate, or hinder a successful reorganization")(internal citations omitted).

5. The Gordian engagement is a clear attempt to "muzzle" Gordian whom the Debtors and Kronstadt viewed as critical of the sale process. In fact, the new proposed engagement letter (Dkt. No. 139-2, Ex. A at Sch. 1) contains a sweeping confidentiality

provision that was not in the previous engagement letter, *id.* at¶ 7, and, on information and belief, is not typical of Gordian engagement letters. Rather it is designed to prevent a free flow of information to the Committee. Accordingly, Gordian has declined to speak to Committee professionals about the sale process without the Debtors' professionals present, and the Debtors have "instructed" Committee professionals in writing not to contact Gordian directly.

6. Although this new sale process is dressed up with the imprimatur of a highly qualified investment banker, it nonetheless will fail to maximize value for numerous reasons:

- Kronstadt is being allowed to credit bid despite the Committee having demonstrated that there are significant colorable challenges to his liens. Not only is this highly inappropriate and certain to chill bidding, s*ee e.g., In re Fisker Auto. Holdings, Inc.* 510 B.R. 55, 61 (Bankr. D.Del. 2014), but it also inappropriately moots the proposed Lien Challenge which is a significant opportunity for creditors to realize value and has been developed at great cost to the estates. It is difficult to see how a competing bidder would spend the time and money to engage in meaningful due diligence if a combination of bidders, including one with a highly dubious lien, can credit bid $13.5 million. No sale should take place with Kronstadt's ability to credit bid unless and until the Lien Challenge is resolved. Debtors' willingness to chill bidding and to moot a potentially valuable Lien Challenge demonstrates the extent to which Debtors are acting as Kronstadt's puppets and why an independent trustee is necessary.

- Debtors' going concern value is tied to its superior technology which is licensed to a great extent from Rutgers University. Rutgers has stated on the record that it believes its license cannot be assumed due to non-monetary pre-petition defaults. *See*

Rutgers, The State University of New Jersey's Objection to Bid Procedures Motion, Dkt. No. 59, ¶ 3 ("In this case, the breach alleged by Rutgers cannot be cured by the payment of money;"). The Committee has objected strenuously to a sale going forward until this issue is resolved. Gordian has responded that a bidder can "risk adjust" his bid for the contingency that the license will not be assumable, but it is difficult to see how a sale process can maximize value when a potential bidder must "risk adjust" his bid for the possibility that the company they are buying may not be able to manufacture and distribute any of its products. On information and belief, Debtors, with Kronstadt's knowledge, have set up a three way meeting among Debtors, Rutgers, and Sicut (the co-licensee of the Rutgers technology) for *after* bids are due. Though Kronstadt knows this, other bidders will not have that knowledge, thus the bidding will be chilled.

- No alternative to a 363 sale has been evaluated. The Committee believes significantly more value will be realized by the estates through a liquidation and pursuit of causes of action, or by a reorganization. Debtors' failure to even consider alternatives to Kronstadt has caused the Committee to lose confidence in management.

- As long as Kronstadt can control the sale process through the DIP financing, as he has done, it is unlikely to produce a salutary result; yet, Debtors have never shopped the DIP financing. As discussed in more detail below, *see infra* pp. 23-26, alternatives are available, but the Debtors refuse to look at any alternative that does not favor Kronstadt. *See e.g.*, Exhibit A (Term Sheet from Industrial Assets).

7. The Court should see through Debtors' attempt to flagrantly abuse the bankruptcy process to favor Kronstadt's suspect security interests[2] over the interests of the creditor body as a whole, including unsecured creditors. Because it is apparent that management's ties to Kronstadt are wound too tightly to allow it to fulfill its fiduciary duties to the creditors, the Committee respectfully requests the appointment of a chapter 11 trustee so that an independent assessment of Debtors' assets and options can take place.

8. The Committee has requested a chapter 11 trustee rather than conversion, because it firmly believes that there is value in the Debtors as operating companies. Such value cannot be realized, however, until someone is in charge that has an agenda other than helping Allen Kronstadt steal the estates' assets away from creditors.

9. Section 1104(a) of the Bankruptcy Code provides in pertinent part that the Court

"…shall order the appointment of a trustee –

> (1) for cause, including fraud, dishonesty, incompetence or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause…; or
>
> (2) if such appointment is in the interests of creditors…"

10. The Committee submits that a chapter 11 trustee is in the interests of the creditors in this case due to management's mismanagement of the sale process pre-petition as outlined by Judge Sontchi, 1/4/16 Tr. at p. 145, line 11 through p. 146, line 10; its ongoing mismanagement and incompetence outlined herein, and its dishonesty as outlined herein.

[2] The Committee has respectfully requested standing to challenge Kronstadt's liens and the Committee's Standing Motion is scheduled for hearing on February 10, 2016. *See* Dkt. Nos. 145 and 148. If the Debtors' proposed bidding procedures are allowed (*See* Dkt. No. 153), it will effectively moot the proposed Lien Challenge and ensure unsecured creditors get nothing.

JURISDICTION AND VENUE

11. This Court has jurisdiction to consider this Trustee Motion pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding under 28 U.S.C. § 157(b).

12. Venue is proper in this District pursuant to 28 U.S.C. §§ 1408 and 1409. The statutory predicates for the relief requested herein are sections 1104(a)(1), 1104(a)(2) and 1109(b) of chapter 11 of title 11 of the United States Code (the "Bankruptcy Code") and Rule 2007.1 of the Federal Rules of Bankruptcy Procedure.

BACKGROUND

13. The Debtors are Axion International Holdings, Inc. ("Holdings"), a Colorado corporation and a publicly-held holding company; Axion International, Inc. ("Axion International"), a Delaware corporation and an operating company that is wholly-owned by Holdings; and Axion Recycled Plastics Incorporated ("Recycled"), an operating company incorporated in Ohio that is wholly-owned by Axion International.

14. Holdings, Axion International and Recycled filed voluntary chapter 11 bankruptcy petitions in this Court on December 2, 2015, and continue to manage their businesses as debtors-in-possession. Pursuant to an order of the Court, the cases are being jointly administered.

15. On December 14, 2015, the Office of the United States Trustee ("U.S. Trustee") appointed the Committee to represent the interests of unsecured creditors in these bankruptcy cases.[3]

[3] The Committee members are the following: (i) Addax Trading LLC; (ii) Coyote Logistics; and (iii) Sicut Enterprises, Ltd. ("Sicut").

16. Kronstadt is a businessman and investor, based in Rockville, Maryland. He is the principal of A.R. Kronstadt Realty Investors, Inc., a firm focused on developing and managing retail, industrial and indoor sports facilities.

17. Recycled and Axion International are in the business of manufacturing and selling railroad ties, construction mats, and other building materials made from recycled plastics and operate from leased manufacturing facilities in Zanesville, Ohio, and Waco, Texas.

18. Kronstadt first became involved with the companies in or about 2012. Over the years he has served many functions with the Debtors. He has variously been a noteholder, a lender, a major equity holder, as well as the initial stalking horse bidder for this case. He served as a director of the Debtors until June 2015. In addition, Kronstadt has posted bonds for the Debtors, serves as a personal guarantor of bank debt, and he currently controls the DIP Lender. Kronstadt, the DIP Lender and the initial stalking horse purchaser, Washington Amigos, LLC ("Washington Amigos") share the same counsel.

19. Kronstadt is also the landlord of the Debtors' Waco facility. Kronstadt's conduct in connection with the Waco, Texas, facility should not be disregarded. Kronstadt was on Axion's board when, in 2013, Axion inexplicably abandoned its former business plan of outsourcing all its manufacturing and entered into a lease of a manufacturing facility in Waco, Texas. Then, in May 2014, it quietly transpired – without disclosure in any of Axion's SEC filings – that the ownership of the Waco property being leased by Axion was acquired by another alter ego of Kronstadt and his investor colleagues, Waco Amigos Real Estate LLC.[4]

[4] The Court denied the Debtors' effort to bind the estates to a railroad agreement regarding a land transaction with Kronstadt in which Kronstadt's relationship to the deal was only disclosed during Fallon's cross-examination at the December 29th hearing (*see* Dkt. No. 106).

20. Kronstadt cannot deny that he is an insider of the Debtors. *See, In re Washington Mut., Inc.*, 461 B.R. 200, 263 (Bankr. D. Del. 2011) ("Insiders of a corporation are not limited to officers and directors, but may include 'temporary insiders' who have 'entered into a special confidential relationship in the conduct of the business of the enterprise and are given access to information solely for corporate purposes.'" (citing *Dirks v. SEC*, 463 U.S. 646, 655 n. 14 (1983)); cf. *N.J. Carpenters Pension Fund v. info GRP, Inc.*, No. Civ A 5334-VCN, 2011 WL 4825888, at *11 (Del. Ch. Sept. 30, 2011) (*de facto* control can be found to exist through contact with board of directors sufficient to give rise to fiduciary duties); *In re Winstar Commc'ns, Inc.*, 554 F.3d 382, 399 (3d Cir. 2009) (determining that major creditor was non-statutory insider based on findings that creditor had "the ability to coerce [debtor] into a series of transactions that were not in [debtor's] best interests.) Throughout this case, Kronstadt has guided the Debtors' actions and exerted control over the Debtors, often to the detriment of creditors. He is an insider.

21. In the first day motions, the Debtors, among other things, sought approval for interim and final debtor-in-possession financing (the "DIP Loan") from Plastic Ties Financing LLC ("Plastic Ties" or the "DIP Lender"), and approval of sale and bidding procedures for a section 363 sale of all assets of all Debtors to Washington Amigos, a nominee for Kronstadt. *See* Dkt. Nos. 10 and 11. The DIP Loan was entered into on an interim basis by Order dated December 4, 2015 (Dkt. No. 24) (the "Interim DIP Order"). The DIP Loan was negotiated by Kronstadt and his counsel, and Kronstadt appears to control the DIP Lender. As part of the sale and bidding procedures, it was proposed that Kronstadt would credit bid some or all of his putative $5.2 million lien to buy all of the assets of the three Debtors, leaving the Debtors with

no cash and no assets. The Committee objected on the ground, *inter alia*, that Kronstadt could not credit bid for all the assets, as he did not have a lien on all the assets.[5]

22. Following almost two full days of hearings, on January 4, 2016, this Court did not approve the Debtors' requested final DIP order (Dkt. No. 10) and Bidding Procedures Motion (Dkt. No. 11), leading one to question the competence of Debtors' management for bringing these obviously flawed motions in the first place. As illustrated below, at the January 4th hearing, the Court provided the parties with some useful guidance regarding what was expected if and when the parties returned for approval of a DIP financing package and bidding procedures. The Debtors' second chance bidding procedures do not follow the Court's guidance.

23. As noted by the Debtors in the recently filed *Debtors' Amended Motion for Orders (I)(A) Authorizing and Approving the Bidding Procedures, (B) Approving Certain Notice Procedures, (C) Approving Credit Bid Rights, and (D) Setting a Date for the Sale Hearing; and (II) Authorizing and Approving (A) The Sale of the Debtors' Assets, and (B) The Assumption and Assignment of Certain Contracts and Leases* (Dkt. No. 153), (the "Revised Bidding Procedures") the Court in connection with its ruling held:

> And there are numerous problems with the Revised Bidding procedures. The primary one is that the debtors are asking for a highly expedited sales process without hiring or having an experienced professional in place to run that process, based on the fact that a prepetition process was run.

[5] In the Interim DIP Order, Kronstadt was granted extensive replacement liens based on Debtors' false representation that Kronstadt has a valid, perfected first priority lien on all assets of all three Debtors, and a second lien on the assets which are collateral for Community Bank. This falsehood has been repeated by Debtors numerous times throughout this case under penalty of perjury. It is only after the Committee, at great expense to the estates, filed a motion for standing to challenge Kronstadt's liens (Dkt. No.145) which thoroughly demonstrated that Kronstadt has no liens on any assets of Recycled and no liens on any causes of action, that the Debtors conceded this in the revised bidding procedures (*See* Dkt. No. 153). Now the Debtors propose to allow Kronstadt to bid the very replacement lien he obtained based on their misrepresentation. This repeated dishonesty concerning the extent and validity of Kronstadt's liens has immeasurably damaged the creditors and will continue to do so under the Revised Bidding Procedures, demonstrating the importance of an independent chapter 11 trustee.

See Transcript of Continuation of Evidentiary Hearing Before the Honorable Christopher S. Sontchi, United States Bankruptcy Judge of January 4, 2016 (the "January 4th Hearing"). What the Debtors fail to recognize is that the Court noted other numerous problems with the bidding procedures. They have solved the problem of a financial professional by seeking to hire Gordian, but have tied their hands by forcing them only to consider a 363 sale in a timeframe that will not maximize value due to uncertainties about the Kronstadt liens and Rutgers. In essence, they have repackaged the exact same sale the Court previously denied by putting installing an expensive investment banker, while making sure it cannot get the best result.

24. While the Debtors may have made some cosmetic changes to its previous bidding procedures, most of this Court's concerns are not adequately addressed, which calls into question whether the Revised Bidding Procedures may be approved by the Court, and the judgment of the management proposing them.[6] For example, an initial review of the Revised Bidding Procedures indicates that the Court's problems continue to be an issue:

	Concerns re Bidding Procedures Raised by the Court (1/4/16 Hearing Transcript)	**Status**	**Notes**
1.	Financial professional with time, access and cooperation, p. 146, lines 11-17	Possibly resolved.	Committee has been advised this is happening, but has no independent confirmation since Debtors have limited Committee access to Gordian.
2.	DIP must be much larger and cover longer period of time. Current proposed DIP inadequate, p. 146, lines 18-21; p. 149, lines 7-21	Unresolved.	No new DIP proposal or budget despite repeated requests from Committee. Debtors have advised that new DIP will have money for Gordian, but not other professionals, rendering estates administratively insolvent.
3.	The financial professional must have all alternatives	Unresolved.	Debtors have only contemplated going concern sale. Gordian retention application is

[6] The Committee is continuing to review the recently filed revised bidding procedures and reserves all rights and objections relating thereto.

	on table: breaking up company, liquidating company, selling company as going concern, pp. 146-147, lines 25-9		only for a 363 sale. Expressly states Gordian cannot liquidate. Apparently no contemplation of a plan. No break up of company is provided; though, bidding procedures attempt to pay lip service to this requirement by saying there may be an offer to purchase particular assets in lot without buying whole lot, but that puts onus on bidder with no analysis or help from Gordian. In addition, Gordian has not seriously looked at breaking up the company, or at selling the company without selling causes of action. The Debtors have created separate lots for mats and railroad ties, but provide no indication as to what is in those lots or what are the financial results of each line of business to permit a bidder to knowledgably bid on a separate lot. There has been no attempt to value various components.
4.	Any asset purchase agreement which purports to buy causes of action, under chapter 5 or otherwise, needs to separate out and allocate consideration to those causes of action, p. 147, lines 10-14; p. 148, lines 10-11.	Unresolved.	Offer No. 1 doesn't do this, nor is it required of competing bids. Offer No. 2 says it will allocate at auction, but gives no values now, so, a bidder knows what his target to beat is.
5.	If don't have blanket lien on everything, or have a junior lien on some assets and a senior lien on others, documents must be specific as to what is being credit bid on what collateral and what non-collateral is subject to cash bid, p. 147, lines 15-25; p. 148, lines 11-13.	Unresolved.	Kronstadt and Plastic Ties liens are combined, with no indication of identity or amount and which assets. Appears Kronstadt may credit bid Kronstadt's liens against assets on which he has no lien. Furthermore, no determination is made of amount of his replacement lien on chapter 5 actions (which is limited to diminution in value of his pre-petition liens), yet he can bid any amount of his total secured debt against the "chapter 5 Lot." Indeed, the proposed Revised Bidding Procedures allow Plastic Ties and Kronstadt combined to credit bid MORE than their outstanding debt![7]

[7] The Debtors acknowledge (the Committee believes incorrectly) that Kronstadt has a lien for $5.2 million, and Plastic Ties "will have" a lien for $2 million (although not necessarily by the Auction Date), for a total of $7.2 million. Yet Offer 1 allows Kronstadt and Plastic Ties combined to credit bid $7.5 million. Offer 2 allows Plastic

6.	It is a better process if competing bids mark up an APA. Committee and Debtors should work on APA, p. 150, lines 11-17.	Unresolved.	No APA has been provided nor terms of sale, making it very difficult and expensive for a competing bidder to come in and difficult to compare bids to determine highest and best.
7.	Rutgers should have an opportunity between designation of winning bid and sale hearing to negotiate adequate assurance of future performance, and not just a weekend, p. 150, line 23 – p. 151, line 5.	Unresolved to the satisfaction of the Committee.	Rutgers is given more time; however, the Debtors seek to require an objection to adequate protection *before* the auction in case Kronstadt is successful bidder, and another objection after the auction should Kronstadt not be the successful bidder. Such a requirement is onerous to parties to executory contracts.

25. The proposed bidding procedures also require potential bidders to certify that they are not colluding with other bidders, yet Kronstadt, Plastic Ties, and Washington Amigos do not need to make this representation. Kronstadt and Plastic Ties may cover each other's alleged deficiencies in their secured position to the detriment of other potential bidders. The lots are gerrymandered, such that, Plastic Ties initially bids and exhausts its first lien bidding on assets on which Kronstadt has no liens. Kronstadt's liens on the remaining assets then move up to a first position, so, he can bid on the remaining assets, as well as on the assets on which Plastic Ties has no liens. And if these bids succeed, Kronstadt and Plastic Ties hand the assets over to a third bidder, Washing Amigos, who has no liens at all. If this is not the very definition of collusion, what is? Such credit bidding collusion should not be permitted in order to preserve the integrity of the process. Nonetheless, management continues to jeopardize their credibility by aligning with Kronstadt at every turn. By accepting Kronstadt's proposal, management keeps

Ties to bid $2 million and Kronstadt to bid $7.5 million, for a total of $9.5 million. In both cases, the credit bidders are allowed to "credit bid" more than their debt!

their jobs. At the heart of all of the continued animosity with the Committee is management's continued acquiescence to the financial interests of Kronstadt.

26. The "sale" now being proposed is nothing more than a scheme designed to hand over the assets to Kronstadt. There simply cannot be a robust sale process until the extent, priority and validity of Kronstadt's liens – and hence the ability to credit bid – is determined and the Rutgers issue is resolved. Until then, there is too much uncertainty to attract competing bidders who can "beat" the inflated credit bid. Yet the Debtors continue to bring forth the same flawed process that this Court has already turned down *without considering any other alternative*. One has to question the competency and management skills of a management team that does that.

27. In fact, Debtors' attempt to allow Kronstadt to credit bid the full amount of his alleged liens with no cash escrow or back up plan for getting value back if his liens are disallowed, abundantly demonstrates the Debtors' incompetence and mismanagement. As noted, the Revised Bidding Procedures ostensibly permits Kronstadt and the DIP Lender to bid in excess of any alleged secured interest. It is unknown whether this is due to simple mathematical incompetence or a deliberate attempt to mislead and chill bidding as Debtors have done in the past. Previously, Debtors asserted that Kronstadt has $5.2 million in outstanding secured 8% convertible notes which are secured by (a) a second priority perfected security interest in the State of Ohio collateral and The Community Bank collateral, and (b) a first priority perfected security interest in all of the other assets of all three Debtors. Such second and first liens are referred to as the "Kronstadt Collateral". *See,* Interim DIP Order, paragraph 10, *supra*. The Debtors have repeated false assertions that Kronstadt has a valid, perfected and enforceable

second lien in the Ohio State and The Community Bank collateral, and a valid, perfected and enforceable first lien in everything else. *See, e.g., Declaration of Donald W. Fallon in Support of Chapter 11 Petitions and Related Motions*, Dkt. No. 3, ¶ 13; Schedules for Debtor Axion International, Inc., Dkt. No. 96, Schedule D; Schedules for Debtor Axion International Holdings, Inc., Dkt. No. 97, Schedule D; and Schedules for Debtor Axion Recycled Plastics, Incorporated, Dkt. No. 98, Schedule D. Now that the Committee has spent considerable time and money to mount the Lien Challenge and demonstrate that he does not, Debtors now appear to admit he does not in the Revised Bidding Procedures. They no longer need to promote this falsehood since they are permitting Kronstadt to collude with Plastic Ties to cover the frailties in his security. Is this not a management that creditors can trust?

28. As part of their duties, the Committee and its professionals undertook an extensive analysis of the liens of Kronstadt. The Committee did an extensive review of both law and facts, including a review of all of the security agreements with Kronstadt, the notes, the note purchase agreement, all of the pleadings heretofore filed by the Debtors, UCC filings with the states of Delaware, Ohio, Colorado and Texas, a review of the items in the Debtors' virtual data room, and a review of the Debtors' SEC filings over the past several years. The Committee also had extensive discussions with Kronstadt's and the Debtors' professionals and members of Debtors' management team, and had an opportunity to cross-examine Debtors' management concerning the liens both in Court and at the 341 Meeting. A true and correct copy of the 341 meeting transcript, conducted on January 15, 2016, is attached as Exhibit B.

29. As set forth in the Standing Motion, this review has permitted the Committee to conclude that (a) Kronstadt does not have a valid, perfected second lien on any of the collateral

of The Community Bank; (b) Kronstadt does not have a valid, perfected lien on the assets of Recycled, and the purported lien can be avoided for the benefit of the estate; (c) Kronstadt does not have a lien on certain identifiable assets of Axion and Holdings; (d) cause exists to recharacterize Kronstadt's "loans" as equity; and (e) cause exists to equitably subordinate Kronstadt's liens. These conclusions were reached at great expense to the estate – expense which could have been avoided had the Debtors been honest from the start.

30. Furthermore, the Committee and its professionals investigated the DIP Lender's pre-petition advance to the Debtors which was repaid from the first draw on the interim DIP loan, and determined this was an improper attempt to convert a pre-petition unsecured or undersecured debt into a post-petition first priority secured debt to the detriment of other creditors. Nonetheless, Debtors want to let the DIP Lender credit bid this ill-gotten lien, again demonstrating their poor judgment and mismanagement.

31. The Committee maintains that Krontadt's liens are invalid and cannot be the subject of credit bidding. The law leaves no doubt that the holder of a lien the validity of which has not been determined, as here, may not bid its lien. *See In re Fisker Auto. Holdings, Inc.* 510 B.R. at 61 (Bankr. D.Del. 2014) (citing *In re Daufuskie Isl. Props., LLC,* 441 B.R. 60 (Bankr.D.S.C. 2010)). Yet, the Debtors continue to advocate Kronstadt's interest to the detriment of creditors, by, for example, permitting Kronstadt to credit bid a flawed security interest so that management may be retained. This is the height of incompetence, self-dealing and mismanagement.

32. These concerns, which have been apparent from the beginning of this case, have only been exacerbated following the Committee's recent Standing Motion to challenge

Kronstadt's liens. The Committee continues to believe that if the Debtors insist on the current timetable, Kronstadt should be required to cash bid at auction and may later recover his cash if he proves his liens. *See e.g., Morgan Stanley Dean Witter Mortg. Capital, Inc. v. Alon USA L.P., (In re Akard St. Fuels, L.P.)*, 2001 WL 1568332 at *3 (N.D.Tex. Dec. 4, 2001). That way creditors might realize some value. Instead, the Debtors are working with Kronstadt to end-run the Committee's Lien Challenge by allowing Kronstadt to collude with Plastic Ties to shore up his liens where they may face challenge and effectively moot the Committee's objection through a sham sale process. Once the assets are "sold" to Kronstadt for no consideration, even a successful lien challenge will not get them back. The Committee has set forth colorable challenges to Kronstadt's liens. Debtors' willful decision to silence the creditors' objection through an untimely sale process demonstrates it is in the best interests of creditors to put someone independent in charge.[8]

Continued inequitable conduct.

33. The Debtors have allowed Kronstadt to misuse his insider position both before and during this case to influence the Debtors to take actions which have gravely harmed creditors

[8] Management's collusion with Kronstadt will not end at the sale. The Revised Bidding Procedures specifically provide that if Kronstadt and Plastic Ties are the successful bidder "…Plastic Ties and Kronstadt shall be entitled to allocate as much or as little of their credit bids to the purchase price as they deem appropriate in their sole and absolute discretion (and Washington Amigos may assume as much or as little of Plastic Ties' and Kronstadt's debts as agreed upon among the three parties in their sole and absolute discretion), so long as the Debtors and their bankruptcy estates are no longer liable for any such indebtedness." *See* Revised Bidding Procedures (Dkt. No. 153), Offer Number 1, ¶ 1(a)(2); Offer Number 2, ¶ 2.d. In other words, Kronstadt will win the bidding on Debtors' assets by being able to credit bid the full amount of his dubious lien, and the Debtors' assets will rematerialize at Washington Amigos still unencumbered by the exact same liens. He really will have bought the Debtors for absolutely nothing, with the full consent and participation of Debtors' management. This is particularly troubling given the testimony of the Debtors' CFO that the Debtors felt the one benefit to the unsecured creditors of the sale to Kronstadt would be the benefit of still being able to do business with the now viable company going forward. *See* 12/29/15 Tr. p. 51, lines 2-8. So now, having lost their money once to allegedly higher priority liens of Kronstadt, they are supposed to be happy with the "benefit" of getting to extend credit once again behind the very same liens that their credit already paid off once. Any management that thinks this is a good result for creditors simply needs to be replaced, or, as Judge Sontchi put it: "Well, I think management and the board of directors of this company need a reality check." 1/4/16 Tr. p. 145, liens 11-12.

and provided him with undue advantages. The Debtors' acquiescence in Kronstadt's abuse of the bankruptcy process demonstrates their incompetence. Included among the examples set forth in the Standing Motion, some of the inequitable actions taken by Kronstadt and consented to by management include:

- Kronstadt, as the proposed stalking horse bidder, induced the Debtors to bring on a sale that was justified by mischaracterizing the previous sale process. As this Court ruled on January 4, 2016: "There was no process run that was a fulsome process to sell this company." *See* 1/4/16 Tr., p. 145, lines 12-13. This management not only proposed a sale that benefited no one but Kronstadt and themselves, but also acquiesced in providing incredible advantages to their future employer, including a 28% breakup fee and the ability to credit bid on assets in which he either had no lien or purportedly had a second lien. By the Debtors proposing this ill-fated sale, the creditors were severely damaged by not only the loss of time and opportunity, but also an enormous expense that was required to successfully defeat the sale. Prior to the hearing in which the sale was successfully defeated, Kronstadt refused to negotiate with the Committee about a meaningful solution, further increasing the costs and administrative burden to the estates. The Debtors, who could not negotiate a meaningful solution without the DIP Lender, made no attempt to find another DIP Lender or consider solutions other than a sale. And now, the Debtors want to revive the exact same sale with a few cosmetic changes. It is time for a change.

- Kronstadt had the Debtors misrepresent his liens in their First Day Motions, the Fallon Declaration, the Motions for an Interim and Final DIP Loan, and the Debtors' Schedules and Statements of Financial Affairs. Indeed, under the Interim DIP Order and the failed proposed Final DIP Order, the Debtors are prohibited from contesting that Kronstadt (i) had a valid, perfected second lien on the assets subject to the State of Ohio and The Community Bank's liens, and (ii) has a first secured valid, perfected lien on all other assets of all three Debtors. In the Interim DIP Order and the failed proposed Final DIP Order, Kronstadt attempted to wrongfully obtain replacement liens on all such assets and succeeded in doing so in the Interim DIP Order, to the detriment of other creditors. At the time he did this, however, Kronstadt knew that he did not have a second lien on the assets

subject to The Community Bank's lien, and that he had no lien at all on the assets of Recycled, and the Debtors should have, too. Even as the Debtors' representatives were called to the stand to testify under penalty of perjury that Kronstadt had valid, perfected liens on all of the assets of all three debtors, Kronstadt filed proofs of claim only against Debtors Holdings and Axion International, and not against Recycled, indicating he knew he did not have liens on the assets of Recycled. Kronstadt's counsel has since conceded to the Committee that Kronstadt has no perfected liens at Recycling, but absurdly, under the terms of the Interim DIP Order, the Debtors are prohibited from conceding this. A chapter 11 trustee would not be. In any event, by the time Kronstadt conceded what he and the Debtors knew to be the truth all along, harm was already done to the creditors, both by the replacement liens on unencumbered assets that were improperly obtained and by the great expenditure of resources resulting from the Committee's investigation and challenge of the liens that the Debtors knew or should have known did not exist.

- While Kronstadt was still on the board, the Debtors moved assets of Recycled to Texas, where they were comingled with the assets of Axion International. The Debtors' Chief Financial Officer, Mr. Fallon, has testified that Axion International and Recycled were treated as one entity (1/15/16 341 Meeting Tr. at p. 49, lines 4-5). The creditors were irrefutably harmed because unencumbered assets of Recycled were transformed into assets of Axion International, which in turn, are encumbered by Kronstadt's lien, without compensation to Recycled.

- Kronstadt took a lien in the Debtors' assets when he knew he was essentially contributing equity. "Courts have recognized that obtaining a lien for the purpose of gaining an advantage over other creditors may be inequitable, depending on the circumstances surrounding that act." *In re Optim Energy, LLC*, 527 B.R. 169, 177 (D. Del. 2015). *Id.* (quoting *U.S. v. State St. Bank and Trust Co.*, 520 B.R. 29, 84 (Bankr. D. Del. 2014)). The reasons why the Three Amigos knew they were really contributing equity and not debt are set forth above in detail (Standing Motion, at ¶¶ 41-49), but especially when one considers that the note itself only granted Kronstadt a lien in the assets of Holdings, but he took a lien in the assets of both Holdings and Axion International, this would appear to be the type of lien meant to gain an advantage over creditors referred to in the *State Street Bank* case. The Debtors consented to the mischaracterization and continue to do so.

- Kronstadt proposed to buy the Debtors through an entity named Washington Amigos. The Committee was informed by the Debtors that Washington Amigos had just been recently formed as a shell corporation in order to buy the assets. In point of fact, Washington Amigos had been dealing with the Debtors at least since August 2015, which dealings were covered up. The Committee discovered that Washington Amigos had been dealing with the Debtors since August by locating a UCC-1 prepared and filed by the Debtors' own counsel in favor of Washington Amigos in August 2015 purporting to give Washington Amigos a lien on all of the Debtors' assets. When asked, the Debtors said Washington Amigos had posted a bond in favor of Debtors, which amount had been repaid a few weeks later. No termination statement, however, was ever filed. Thus, any potential buyer checking the liens against the Debtors would see that the stalking horse bidder had a lien against all of the assets of the Debtors. This fact hurt, and continues to hurt, the creditors by chilling other buyers from coming into the sale process, thus giving Washington Amigos a leg up. In addition, the relationship with Washington Amigos was hidden, in that, when discussing the bond and the subsequent lien, it was indicated in the Debtors' SEC filings that the lien went to Kronstadt, not to Washington Amigos, whose name was never mentioned. At the hearings on the Final DIP and bidding procedures, the Debtors' witnesses purported to have no idea who Washington Amigos (12/29/15 Tr. at p. 51, lines 22-24) and another Kronstadt affiliate, Waco Amigos Real Estate, even are, despite having done business with both for a long time. *See* 12/29/15 Tr. at p. 35, lines 14-20; p. 37 line 11 – p. 38, line 3. This leaves one to wonder whether management is dishonest or merely incompetent.

- This Court has already remarked: "It is clear to me from the testimony that management eschewed several opportunities to put this thing up for a real marketing process, a real market test, as to what the value is; refused to even consider breaking up the business units; refused to allow the financial professional to contact potential purchasers; refused to cooperate with the financial professional; ultimately, frankly got its feelings hurt, as far as I can tell or maybe its ego bruised, when the financial professional actually sought to do its job." *See* Jan. 4, 2016 Transcript, *supra* at p. 145, lines 13–22. It is now evident that when the Debtors should have been aggressively marketing the company, it was already in bed with Washington Amigos to whom

> it gave a lien on all the assets in August 2015. It is certainly colorable to conclude that investigation will show that one of the reasons the Debtors dragged their feet on the fulsome sale process was to accommodate Kronstadt, who plans to retain management should he acquire the company. The Debtors' failure to run a fulsome process inestimably hurt the creditors. And yet, after being given a second chance after its botched sale process and a road map from the Court, Debtors want to compound their previous mismanagement by bringing the same sale process forward again on a timetable that dooms it to failure due to the unresolved issues over the Kronstadt liens and the Rutgers license.

34. The Committee provides these examples as illustrative of the Debtors and Kronstadt's inequitable conduct, which remain subject to the Committee's challenges and the subject of formal discovery, and of the incompetence of Debtors' management that blindly continues to let this person who abuses the bankruptcy process dictate the Debtors' conduct. As this Court knows, the Committee has taken the first step to challenge Kronstadt's liens through the filing of its Standing Motion (Dkt. No. 145) which is scheduled to be heard on February 10, 2016.

35. The procedural posture is important to the Court's consideration of this Trustee Motion because, in an effort to circumvent the Committee's investigation, Debtors, through the Revised Bidding Procedures, intend to essentially re-submit a DIP financing with bidding procedures to allow for Kronstadt to continue to serve as the stalking horse bidder and credit bid his interest and the interest of Plastic Ties as DIP Lender, *without* satisfying the Court's requirements outlined at the January 4th hearing, and thereby moot the Lien challenge which offers the promise to unsecured creditors of a real return in this case.

36. While the Committee recognizes that the Debtors' Revised Bidding Procedures and DIP financing are ongoing and remain subject to Committee comment, the Revised Bidding

Procedures filed with this Court on February 3, 2016, show the Debtors continue to firmly support Kronstadt's interests, without an analysis of whether a liquidation or possible reorganization is appropriate under the circumstances.

37. The Debtors look to somehow cleanse the flawed insider transaction with the blessing of Gordian Group, whose retention by the Debtors remains subject to this Court's approval; yet, even the most brilliant investment banker cannot overcome the fact that they are not being allowed to consider all options, nor the timing being foisted upon them that forces them to market a company which may not have the ability to produce its only products if the Rutgers issue is not resolved. Nor can they magically produce interested buyers when the Debtors purport to allow liens of over $13 million to go ahead of other bidders, whether or not such liens are valid. Until recently, when Gordian was offered $250,000 upfront to serve as investment banker for this truncated sale, it was one of the biggest advocates for exposing the flaws of management, as well as the proposed transaction. Having them now working for Debtors does not change Debtors' pre-petition mismanagement on which this Court has already remarked. Nor does it automatically transform an intrinsically flawed sale process into an opportunity to maximize value. An independent trustee must be appointed to fully utilize all the advice of a financial advisor.

38. Noticeably absent from the Revised Bidding Procedures is the Debtors' representation that they have fully considered the Debtors' options, whether through sale, liquidation, reorganization, or breakup of the business as suggested by this Court at the January 4th hearing. It is shocking that a month after this Court's ruling, the Debtors have still made no attempt whatsoever to value Kronstadt's putative collateral on the Petition Date, value

unencumbered assets and consider how to do a plan around them, look at liquidation or breaking up the business and selling off parts. There has been no attempt to determine what type of transaction is in the best interest of the Debtors' estates – and not simply for the betterment of Kronstadt's financial position.

39. Further evidence that the Debtors are not able to fulfill their fiduciary duties to creditors – including undertaking the honest evaluation of potential fraudulent conveyance actions – is their continued deceitfulness as to the state of their finances prepetition. In their Revised Bidding Procedures Motion, the Debtors have once again asserted, or at least strongly implied, that their state of insolvency only arose relatively shortly before the Petition Date. They wrote: "Due to [various generic factors] …, the Debtors' recently questioned in notes to their financial statements their ability to continue as a going concern." Debtors' Amended Bid Procedures Motion (Dkt. No. 153) at ¶9 (emphasis added).

40. In fact, the Debtors have acknowledged that their certified public accountants expressed "substantial doubt" about the Debtors' ability to continue as a going concern in every single annual 10K filing that Holdings has filed with the SEC since 2009. That includes their 10K filings for FY 9-30-09; FY 9-30-10; the 3-month transition period ending 12-31-10; FY 12-31-11; FY 12-31-12; FY 12-31-13; and FY 12-31-14. In light of this, pre-petition transactions, including payments to Kronstadt and his cronies, should be reviewed for possible attack as fraudulent conveyances. The Debtors have not done so, and if the proposed sale to Kronstadt for nothing goes through, they won't be able to.

41. This case will likely succumb under its own administrative weight if faced with another contested DIP financing and bidding procedures hearing. The issues, once again raised in the Revised Bidding Procedures have been raised and litigated. For this reason alone, the

Court may find cause exists to warrant the appointment of a chapter 11 trustee. This case can no longer afford a management focused solely on handing all assets to Kronstadt on a silver platter.

42. Although the Committee does not feel the time is ripe for a sale with the Lien Challenge and Rutgers unresolved, it cannot help but also note that the Debtors' unswerving devotion to Kronstadt has blinded them to other sale possibilities.

Debtors have failed to consider other potential replacement DIP lenders and pre-auction bidders.

43. The Committee, without solicitation, has received inquiry regarding the acquisition of the Debtors' assets. On at least three occasions, the interested party has indicated to Committee counsel that they would be interested in acquiring the assets if management is replaced, but they cannot get traction with the Debtors to discuss.

44. Most recently, the Committee was approached by a potential buyer who felt it was being ignored by Debtors. Industrial Assets first contacted the Debtors in December, but it asserts it was ignored. When they contacted the Debtors again in January, they were told to wait until an investment banker was retained. They then got access to the data room, but no serious dialogue. When they contacted Gordian again and offered to put up a minimum guarantee for a liquidation which would leave the Debtors with all of its general and bankruptcy causes of action to pursue, they were told the Debtors preferred "a transaction". They then had a call with Gordian and indicated they would be pleased to come in as a DIP lender or stalking horse buyer for an acquisition of the Debtors. They never heard from Gordian or the Debtors again.

45. Industrial Assets is a legitimate lead that the Debtors' failed to pursue. By ignoring them, the Debtors failed to realize a golden opportunity to determine, at no cost to the estates, what a liquidation would be worth. The Committee continues to believe a liquidation of

the hard assets followed by pursuit of the many causes of action unencumbered by Kronstadt's liens would allow the Debtors to repay the DIP and return value to unsecured creditors, but the Debtors refuse to test this theory.

46. Debtors also ignore a golden opportunity to replace the Kronstadt DIP Loan, which has been a noose around the Debtors' necks, with a takeout DIP Loan. With less than an hour of discussion, Industrial Assets has provided the Committee with a term sheet for a takeout DIP Loan that has significant benefits to the estates and their creditors. *See* proposed Axion Term Sheet from Industrial Assets, attached hereto as Exhibit A (the "Term Sheet"). Not only does this proposed Term Sheet provide more funding to the Debtors than the current DIP, it is available for a much longer period of time, allowing the Debtors to properly consider all options and have time to complete the Lien Challenge, try to resolve Rutgers, and then have a robust sale process. Furthermore, Industrial Assets has indicated it is not likely to buy either the general or bankruptcy causes of action, which can then be litigated or monetized for the benefit of the estates' creditors. While Industrial Assets may, like Kronstadt, try to use a DIP Loan to parlay itself into the stalking horse bidder role, and this Term Sheet needs to be negotiated, because it is a viable alternative opportunity for the Debtors. Makes one wonder what an independent trustee who actually wants to shop the DIP and listen to potential buyers and liquidators other than Kronstadt might accomplish.

47. The Committee has secured a replacement proposed DIP lender and stalking horse bidder in short order. This seriously calls into question whether Debtors' current management may be trusted to truly find the best DIP Lender or run a robust marketing process, even if provided with a second chance, this time with Gordian in their hip pocket.

48. Both the Committee and Industrial assets realize that the Term Sheet requires further revision and discussion. But one can only guess whether the treatment of Industrial Assets is illustrative of how non-Kronstadt bidders are treated. The proposed stalking horse Term Sheet shows that there is value either in a liquidation or sale that must be explored. The Debtors fail to even consider that there may be other "pre-auction" bids available aside from the problematic baseline provided by Kronstadt and Plastic Ties (*see* Revised Bidding Procedures at ¶ 33).

49. With Debtors' myopic focus on Kronstadt, they have failed not just the unsecured creditors, but other secured creditors, as well. Community Bank was forced to file a lift stay motion because miraculously, while Kronstadt was being adequately protected and Plastic Ties gets its pre-petition debt converted to post-petition first priority secured debt, Community Bank, which purports to have a valid, perfected first priority lien on the majority of the Debtors' equipment, has received nothing: no adequate protect payments, no interest payments, no consultation in the sale process, nothing. Accordingly, it has moved to lift the stay and pursue its remedies against the Debtors, including foreclosing on a majority of the Debtors' equipment and machinery. *See* Dkt. No. 151. Such a move would be disastrous for other creditors, as the Debtors would be left with so few assets it will become even harder to attract competing bidders to a robust sale process or to interest a liquidator to step in.

50. Looking beyond the ill-fated sale process, Debtors have proven themselves inept in the day-to-day management of the business, as well. Among their many business missteps:

- Management is largely absent, which is particularly harmful to Debtors during the stressful time of chapter 11. They have no handle on the day-to-day operations, because they are not there and do not see the operations. The CEO lives in Michigan and

"commutes" to Debtors, at Debtors' expense, when he visits. The CFO lives in Maryland, and also "commutes" at Debtors' expense when his presence is required in Ohio. The CFO testified that he has never even been to Debtors' main plant in Texas. (Ex. B at p. 47, lines 18-19). How is he supposed to develop cost-cutting measures during these difficult times if he has never even seen the operations? On information and belief, the Manager of Quality Control has also never been to the plant. Is it any wonder that the Debtors are mismanaged when there is no hands-on management?

- The Debtors bought Y Recycling in 2013 for millions of dollars. By 2014, they had already shuttered the Recycling operations as a huge mistake. Management blames the seller, Brian Coll, for misrepresentations, but have done nothing to pursue him for fraudulent conveyance, misrepresentation, or breach of contract. Rather, on information and belief, they released Mr. Coll from his non-compete, and he is now setting up a competing railroad ties company that offers a similar product for a significantly lower cost, which has attracted one of Debtors' major customers, Union Pacific.

- Until recently, Debtors outsourced manufacturing. The current CEO decided to bring manufacturing in-house, which has never been profitable for the Debtors. Where they once sold railroad ties for a decent profit margin, it now costs them more to produce each tie than it can be sold for. This is unlikely to change without significant revision of the Debtors' business plan.

- The Committee has repeatedly asked the Debtors to consider curtailing production while we figure out an appropriate plan for the Debtors, since, Debtors have to borrow from the DIP Lender to keep up production, and the products cannot be sold at a profit. Management has refused to even consider curtailing production, or to work on a set of business projections, which they do not have. When Committee's counsel recently renewed this request as a way of saving money in order to put off the sale process until a better time, Debtors' counsel told the Committee, "It's our business judgment, not yours. We don't have to justify it to you."

- The dispute with Rutgers has been simmering since about October 2015. Despite the vital importance of the Rutgers license to the Debtors' going concern value, they have proven incapable of resolving it, or even of making it a high priority.

51. Debtors' current management is inept. They have mismanaged the Debtors both before and after the Petition Date and repeatedly demonstrated their incompetence and dishonestly. They have eschewed their fiduciary duty to the estates and their creditors in favor of appeasing Allen Kronstadt and keeping their jobs. Under these circumstances, it is in the interests of creditors to appoint an independent chapter 11 trustee.

BASIS FOR RELIEF

52. Because Debtors' current management cannot or does not fulfill their duties to the creditors and the estates, the Committee moves for an order directing the appointment of a chapter 11 trustee under 11 U.S.C. § 1104(a)(1) and (a)(2). The Bankruptcy Code mandates appointment of an independent trustee where, as here, the debtors-in-possession cannot fulfill their duties to the creditors and the estates and have exhibited mismanagement, incompetency and dishonesty. Although chapter 11 generally permits debtors to retain control of their assets and business operations, "the willingness of courts to leave debtors in possession is premised upon an assurance that the officers and managing employees can be depended upon to carry out the fiduciary responsibilities of a trustee." *CFTC v. Weintraub*, 471 U.S. 343, 355 (1985) (citation and internal quotation marks omitted).

53. Because it is apparent that management has no intent to fulfill its fiduciary duties to the creditors, the Committee respectfully requests that the Court order the appointment of a chapter 11 trustee and that the Debtors be ordered to cooperate with the chapter 11 trustee and immediately turn over to the chapter 11 trustee all records and property of the estates in their possession, custody or control or as otherwise directed by the chapter 11 trustee.

ARGUMENT

54. Bankruptcy Code section 1104 establishes grounds to appoint a trustee in these Chapter 11 Cases. Specifically, section 1104(a) of the Bankruptcy Code requires the appointment of a chapter 11 trustee if *either* (1) cause exists *or* (2) such appointment "is in the interests of creditors, any equity security holders, and other interests of the estate[.]" 11 U.S.C. § 1104(a)(1) & (2). The movant bears the burden of establishing the need for a trustee, but once cause is shown, appointment is mandatory. "Cause" and "interests of creditors" are non-specific and thus require fact-intensive analysis on a case-by-case basis.

55. Section 1104(a)(1) authorizes the appointment of a trustee "for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs by current management, either before or after the commencement of the case…" The list of examples of cause is not meant to be exhaustive and courts have rejected attempts to limit the "for cause" analysis to enumerated items. *See In re Marvel Entm't Corp.,* 140 F.3d 463 at 472; *In re Casco Bay Lines, Inc.*, 17 B.R. 946, 950 n. 4 (B.A.P. 1st Cir. 1982) (noting that "[t]he Code 'includes' some examples of 'cause,' but does not restrict the term to those examples"). The Bankruptcy Code thus implicitly authorizes the court to determine whether the unique facts of each case satisfy the "for cause" requirement. *In re Sharon Steel Corp.*, 871 F.2d 1217, 1226 (3d Cir. 1989)(finding decision to appoint a trustee "must be made on a case-by-case basis" and that the Court has discretion "to appoint a trustee when to do so would serve the parties' and the estate's interests.").

56. Once the court finds that "cause" exists, a trustee *shall* be appointed. See 11 U.S.C. § 1104(a). A bankruptcy court has no discretion and must then grant the requested relief. *See In re V. Savino Oil & Heating Co.*, 99 B.R. 518, 525 (Bankr. E.D.N.Y. 1989).

57. The acrimony in these cases resulting from the Debtors blindly following Kronstadt (and Plastic Ties) constitutes "cause" and justifies the appointment of a chapter 11 trustee. As set forth above, this acrimony is evident from even a cursory review of the docket and the transcripts from the hearing on the failed proposal for Final DIP Financing Order and Bidding Procedures Motion, and from the 341 Meeting transcript. While the Committee had hoped for the Debtors to act truly independently following the failed DIP hearing, unfortunately, the Debtors, without adequate justification, continue to be beholden to Kronstadt. As a result, the Committee fears a continued rise of acrimony to the detriment of the Debtors' estates should a chapter 11 trustee not be appointed.

58. Under the circumstances, the creditors have lost faith in current management. Where there is sufficient "acrimony" between the creditors and debtors, courts have not hesitated to appoint a trustee. *See e.g., Marvel Entm't Grp., Inc.*, 140 F.3d at 472-473; *In re Plaza de Retiro, Inc.*, 417 B.R. 632, 640-41 (Bankr. D. N.M. 2009)([t]he Court has observed that acrimony between a debtor-in-possession's management and the creditors that impedes the reorganization effort has routinely been found to constitute a ground for appointing a trustee."); *Petit v. New England Mortg. Servs., Inc. (In re Petit)*, 182 B.R. 64, 70 (D. Me. 1995) ("deep-seeded conflict and animosity between a debtor and its creditors provides a basis for the appointment of a trustee."). *In re Biolitec, Inc.*, 2013 WL 1352302, at * 13 (Bankr. D.N.J. April

3, 2013) (appointing trustee due to deep-seeded conflicts between the parties and their inability to resolve such conflicts).

59. In *Marvel Entertainment*, the Third Circuit Court of Appeals affirmed the appointment of a trustee due to the "deep-seeded conflict and animosity," between the debtors and its creditors. 140 F.3d 473. The Court of Appeals stated, "[t]he intense and high-stakes bickering between the [debtor] interests and the Lenders does not instill confidence that the [debtor] interests could fairly negotiate with creditors to whom they owe [fiduciary] duties, nor that reorganization will occur effectively." *Id.* at 474.

60. The acrimony that supported the appointment of a trustee in the above cases is unfortunately present here, and it has only increased since this Court's January 4th ruling. Notwithstanding the pre-petition conduct resulting in the Debtors hitching their future to Kronstadt that extended to entry of the Interim DIP Order and the now defeated final DIP order, the Debtors have not resolved the continued acrimony with its creditors in order to be able to satisfy their fiduciary duties. With the proposed retention of Gordian, the Debtors are now seeking to have Gordian rubberstamp Kronstadt's sale proposal with no significant revisions from the version previously rejected by the Court. Simply having Gordian on board to bless a flawed insider transaction is not good enough. The Committee has continued to maintain that the Debtors need to evaluate the gamut of options available – sale, liquidation or reorganization – as directed by this Court on January 4th. To date, there is no indication that the Debtors have taken the Court's words to heart. They continue to jam Kronstadt's questionable liens and rights as a secured creditor as the best offer available to the Debtors, while not attempting to consider other alternatives.

61. The Debtors' failure to advance these Chapter 11 Cases has resulted in accrued professional fees and such fees will only increase as the Debtors force the parties to continue to litigate over issues that, frankly, should be a matter of Bankruptcy 101.[9] Nonetheless, the disputes continue, the Chapter 11 Cases get no closer to resolution, and the recoveries for unsecured creditors, if any, continue to fade.

62. Nor is acrimony the only reason the Committee seeks a trustee. The Debtors' plans for a sale process are flawed. They cannot hope to maximize value and attract competing bids until the outcome of the Lien Challenge and the dispute with Rutgers are known. Yet the Debtors chug on, noticing a sale that is designed to produce no tangible value and will just increase litigation and costs. Management has displayed a lack of good judgment throughout this case and even before the petitions were filed. Their mismanagement, incompetence, and even downright dishonesty in representations made to this Court, are cause for a trustee appointment under 11 U.S.C. § 1104(a)(1).

63. The Court may also appoint a chapter 11 trustee under 11 U.S.C. § 1104(a)(2) because such appointment is in the interests of the estates and all other parties. Even when "cause" to appoint a trustee is not otherwise established under Bankruptcy Code section 1104(a)(1), section 1104(a)(2) creates a flexible standard, authorizing the Court to appoint a

[9] For example, the Committee has tried repeatedly to demonstrate to the Debtors and Kronstadt that he does not have a valid lien on any of the assets of Recycled or against the general causes of action of the three Debtors, but we were ignored. No one was interested in settling this matter, and the Committee was told the Interim DIP Loan gave us the right to challenge the liens if we wanted to. The Debtors and Kronstadt refused to even discuss it. Only after the Committee professionals spent countless hours and tens of thousands of dollars investigating and laying out these challenges, among others, did the Debtors – without any discussion with or advance notification to the Committee – file a stipulation with this Court between the Debtors and Kronstadt agreeing that (a) Kronstadt has no lien on general causes of action; (b) Kronstadt has no lien on any assets of Recycled; and (c) Kronstadt does not have a lien on The Community Bank collateral that consists of Recycled's equipment. See, Stipulation By and Between the Debtors and Allen Kronstadt Regarding Certain Security Interests and Liens (Dkt. No. 159). The Debtors forced the Committee to engage in costly litigation to establish what a review of the documents should have made clear.

trustee when it is in the best interest of the creditors and the estate to do so. S*ee Sharon Steel Corp.*, 871 F.3d at 1126.

64. Where the best interests of creditors would be served by appointment of a chapter 11 trustee, cause for such appointment almost always exists, and *vice-versa*. Indeed, the balancing test some courts employ reveals the extensive overlap between the two. Under the "best interests" balancing test, courts consider: (i) the benefits to be derived by appointing a trustee compared to the costs of appointment; (ii) a debtor's performance and its rehabilitation prospects; (iii) the debtor's trustworthiness; and (iv) confidence of creditors and the business community in current management. *In re Ionosphere Clubs, Inc.*, 113 B.R. 164, 168 (Bankr. S.D.N.Y. 1990). By placing these Chapter 11 Cases in the hands of an able and trusted fiduciary, the appointment of a trustee in such case will likely decrease litigation, control costs and increase confidence of creditors and other parties in interest. *See In re Colorado Ute Elec. Ass'n, Inc.*, 120 B.R. 164, 177 (Bankr. D. Colo. 1990).

65. The benefits of appointing a chapter 11 trustee would greatly outweigh the burden, if any, to current management resulting from such appointment. Among other things, the appointment of a trustee to truly act independent when assessing the various options for the sale, liquidation or reorganization of the Debtors presents an opportunity to maximize value for creditors which has previously been missing. Such an unbiased evaluation of the prospects for recovery for unsecured creditors, if any, would reassure creditors that assets would be evaluated and handled appropriately. A trustee could take any necessary steps to preserve value for creditors, including, as necessary, to operate the Debtors' businesses as a going concern. In that

regard, it is worth noting that the Committee believes there is value in the Debtors which would be lost in a conversion to chapter 7.

66. The appointment of a trustee has another beneficial aspect for the estates: it ends the Debtors' exclusivity period to file a plan. The Committee believes that a plan of reorganization or liquidation is possible with the right changes at the Debtors, and this could well maximize value, but the current Interim DIP does not allow the Debtors to consider anything other than a 363 sale, and leaves the Debtors with no money to structure a resolution of this case once the assets are given away to Kronstadt. Once a trustee is in place, he can negotiate a more favorable DIP loan, such as the one attached as Exhibit A, and then proceed to consider suggestions for a plan or liquidation.

RESERVATION OF RIGHTS

67. The Committee reserves its right to amend or supplement, through and including the date of any hearing on this Trustee Motion, any of the factual recitations or legal arguments contained herein.

NO PRIOR REQUESTS

68. No prior requests for the relief sought herein have been made by the Committee to this or any other court.

WHEREFORE, the Committee respectfully requests that the Court enter an order substantially in the form attached hereto appointing a chapter 11 trustee in these cases and grant such other and further relief as the Court deems just and proper.

Date: February 4, 2016

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