UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re:	)	Chapter 11
Phoenix Payment Systems, Inc.	)	Case No. 14-_____ (_____)
Debtor.	)	

DECLARATION OF MICHAEL E. JACOBY IN SUPPORT OF CHAPTER 11 PETITION AND FIRST DAY MOTIONS

Under 28 U.S.C. § 1764, Michael E. Jacoby declares as follows under the penalty of perjury:

1. I am the Chief Restructuring Officer of Phoenix Payment Systems, Inc., a corporation organized under the laws of the state of Delaware and the debtor (the "**Debtor**") in the above-captioned chapter 11 case (the "**Chapter 11 Case**"). I have served as the Chief Restructuring Officer of the Debtor since February 3, 2014 and am authorized to submit this declaration (the "**First Day Declaration**") on behalf of the Debtor.

2. I am generally familiar with the Debtor's business, day-to-day operations, financial matters, results of operations, cash flows, and underlying books and records. All facts set forth in this declaration are based upon my personal knowledge of the Debtor's business, operations, and related financial information gathered from my review of its books and records, relevant documents, and information supplied to me by members of the Debtor's management team and advisors. If called to testify, I could and would testify competently to the facts set forth in this First day Declaration.

3. On August 4, 2014 (the "**Petition Date**"), the Debtor filed a voluntary petition for relief in the United States Bankruptcy Court for the District of Delaware (the "**Court**"). The

purpose of this Chapter 11 filing is to facilitate the entry into an asset purchase agreement to sell substantially all of the Debtor's assets to a wholly-owned subsidiary (the "**Purchaser**") of North American Bancard ("**NAB**") or another higher or otherwise better bidder pursuant to Section 363 of the Bankruptcy Code (the "**Sale**"). The Sale is somewhat unusual in today's Chapter 11 environment in that, upon consummation, it will provide sufficient proceeds to pay all undisputed creditors in full as well as a significant distributions to the Debtor's equity holders.

4. I submit this First Day Declaration on behalf of the Debtor in support of the Debtor's (a) voluntary petition for relief that was filed under chapter 11 of the Bankruptcy Code and (b) "first day" motions, which are being filed concurrently herewith (collectively, the "**First Day Motions**").[1] The Debtor seeks the relief set forth in the First Day Motions to minimize the adverse effects of the commencement of the Chapter 11 Case on its business so as to preserve the business pending the Sale. I have reviewed the Debtor's petition and the First Day Motions, or have otherwise had their contents explained to me, and it is my belief that the relief sought therein is essential to ensure the uninterrupted operation of the Debtor's business and to successfully maximize the value of the Debtor's estate.

5. Part I of this First Day Declaration provides an overview of the Debtor's business, capital structure, and significant prepetition indebtedness, as well as a discussion of the Debtor's financial performance and the events leading to the Debtor's chapter 11 filing. Part II sets forth the relevant facts in support of the First Day Motions.

[1] Unless otherwise defined herein, all capitalized terms shall have the meanings ascribed to them in the applicable First Day Motion.

PART I

A. General Background

6. Founded on March 4, 2004, the Debtor is an international payment processor with corporate headquarters in Wilmington, Delaware and technology headquarters in Phoenix, Arizona. The Debtor provides secure, reliable, easy-to-use and cost-effective acceptance, processing, support, authorization and settlement services for credit card, debit card and e-check payments.

7. The Debtor, a top 35 merchant processor, has direct connections to all four major card associations, which establish all payment types in all payment environments. Providing processing services at more than 8,700 locations worldwide, the Debtor processed, in multiple currencies, approximately 280 million transactions in 2013 and expects to process 400 million in 2014. The Debtor serves hundreds of merchants (the "**Merchants**") and financial institutions, including Fortune 500 firms, large public entities and governments and small-to-medium businesses.

8. The Debtor provides its services through its proprietary software and systems platform which was designed and built from the ground up in 2004 to address current and future front- and back-end processing needs. This feature-rich platform includes: secure payment processing; a "webSuite" which allows for real-time, web-based reporting, data analysis and exports, exception transactions, chargebacks and merchant statements; a "PayPage" that enables eCommerce merchants to outsource online payment acceptance; a virtual terminal offering mode for processing point-of-sale, mail order/telephone order and eCommerce transactions; and a "vPost" which emulates all of the functionality of a high-volume point-of-sale terminal through a web browser.

B. The Debtor's Relationship with Bancorp

i. The Bancorp Agreements

9. The Debtor derives substantially all of its revenues from merchants whose customers pay with VISA U.S.A. Inc. ("**VISA**"), MasterCard International Incorporated ("**MasterCard**"), Discover Financial Services ("**Discover**") and American Express ("**Amex**," and) collectively, the "**Associations**"). The Debtor's ability to provide the Merchants with access to and process merchant payment transactions with the Associations is vital to the Debtor's ongoing business as an independent sales organization. In order to be in a position to accept and receive credit for purchases made with VISA or MasterCard credit cards, the Merchants must be a party to a merchant services agreement or similar agreement with a party that has access to the VISA/MasterCard payment and collection systems. Bancorp currently is such a party that has access to the VISA/MasterCard payment and collections systems. Pursuant to the processing agreements discussed below, Bancorp (i) sponsors sales and credit transactions submitted by the Debtor's Merchants whose customers use their VISA or MasterCard credit cards; (ii) sponsors the Debtor into the Associations as an independent sales organization and establishes and maintains a dedicated segregated Association Bank Identification Number (BIN) and Interbank Card Association (ICA) for Debtor; (iii) and makes payment to VISA or MasterCard for fees, and then makes certain settlement payments to the Debtor. In addition, as a result of overdrafts and negative cash flow, Bancorp advanced monies to the Debtor in connection with the processing of transactions above, over a period of years, which sums, were secured (together with Guaranty of Moyer Obligations (defined below), as discussed below) against all of the assets of the Debtor. The advances and guaranty obligations enabled the Debtor to continue to operate while in a cash deficit position.

10. As a result, the Debtor has multiple agreements with The Bancorp Bank ("**Bancorp**"). They fall into two categories: (a) agreements that enable the Debtor to operate its business with Bancorp as its sponsor bank, including (i) the ISO Agreement, dated May 31, 2005, and all related schedules and ancillary agreements attached thereto, including that certain Surety Agreement (the "**Surety Agreement**"), executed by Raymond D. Moyer, the largest stockholder of the Debtor and the Debtor's former Chief Executive Officer ("**Moyer**") (as amended pursuant to the First Amendment to the ISO Agreement, dated June 1, 2010, and the Second Amendment to the ISO Agreement, dated November 31, 2011, the "**ISO Agreement**"); (ii) the Processor Agreement, effective May 31, 2005 (as amended pursuant to the First Amendment to the Processor Agreement, dated June 1, 2010, the "**Processor Agreement**"); (iii) the Sponsorship Agreement, dated May 31, 2005 (as amended pursuant to the First Amendment to the Sponsorship Agreement, dated June 1, 2010, the "**Sponsorship Agreement**"); and (iv) the Originating Depository Financing Institution Agreement, dated June 15, 2007; and (b) financial accommodation arrangements, including the financial accommodation letter from Bancorp to the Debtor, accepted on April 11, 2012 (the "**Accommodation Agreement**") and all exhibits thereto, including that certain Security Agreement, dated April 11, 2012 (as amended on or about June 27, 2012 and further amended on May 9, 2014, the "**Security Agreement**"). All of these agreements are collectively referred to herein as the "**Bancorp Agreements**."

11. In addition to the Bancorp Agreements, Moyer personally was a party to several agreements with Bancorp, including, (a) in 2002, a promissory note, credit agreement (which was modified in 2010) and mortgage whereby Bancorp extended a loan in the original principal amount of $2,000,000.00 to Moyer (the "**Moyer Loan Documents**") and (b) the Stock Pledge and Security Agreement, dated April 11, 2011 (as amended twice on June 27, 2012, the "**Stock**

Pledge," and together with the Moyer Loan Documents, the "**Moyer Agreements**"), between the Bancorp and Moyer and the Agreement and Acknowledgment of Stock Pledge, executed by the Debtor on even date. The obligations under the Moyer Loan Documents were secured by Moyer's personal residence located in Pennsylvania. As explained below, the Debtor later guaranteed Moyer's obligations under the Moyer Loan Documents, and the obligations under the Guaranty of Moyer Obligations (defined below) are governed by the Security Agreement.

12. The purpose and relevant provisions of each Bancorp Agreement and Moyer Agreement are as follows:

- The ISO Agreement
  - ♦ establishes the Debtor as an "Independent Sales Organization" (an "**ISO**");
  - ♦ sets forth the Debtor's duties, among other things, as (a) marketing Bancorp's transaction processing and other services relating to transactions that use payment cards of VISA and Mastercard, (b) providing software or technical documentation and technical support in order to allow the Merchants to process sales transactions through the VISA/MasterCard processing systems, and (c) providing authorization, settlement, chargeback processing and reporting, 24 hours per day, 365 days per year; and
  - ♦ provides that accepted Merchants, Bancorp, and the Debtor enter into a merchant agreement (each such agreement a "**Merchant Agreement**").
- The Surety Agreement serves as a guaranty from Moyer to Bancorp of the obligations of the Merchants under the Merchant Agreements.
- The Processor Agreement engages the Debtor to provide merchant processing and settlement services for the benefit of the Merchants on behalf of Bancorp, in its capacity as a licensee of VISA and MasterCard.
- The Sponsorship Agreement provides the Debtor with sponsorship services from Bancorp that VISA and MasterCard require in exchange for providing endpoint processing equipment.
- The Accommodation Agreement provides the Debtor with extensions of credit and extensions of payment terms from Bancorp under the Bancorp Agreements.
- The Security Agreement establishes a security interest in all of the assets of the Debtor to secure the Debtor's obligations to Bancorp.

- The Stock Pledge establishes a security interest in all of Moyer's stock certificates in the Debtor to secure Moyer's obligations under the Surety Agreement and grants an irrevocable voting proxy, exercisable at Bancorp's election upon a continuing event of default, to vote, as Moyer's proxy, Moyer's shares.

ii. The Debtor's Obligations to Bancorp Under the Bancorp Agreements and the Guaranty of Moyer Obligations and the Forbearances

13. In May 2012, the Debtor defaulted under the Bancorp Agreements and Moyer defaulted under the Bancorp Agreements and the Moyer Loan Documents. Pursuant to that certain Forbearance Agreement, dated as of June 27, 2012 (the "**Forbearance Agreement**"), Bancorp agreed to forbear from exercising its remedies under the Bancorp Agreements during the period of time commencing on June 27, 2012 and ending on the earlier of October 1, 2013 or the occurrence of certain events specified in the Forbearance Agreement, including failure to comply with the Forbearance Agreement or any of the Bancorp Agreements, failure to make agreed payments to Bancorp, failure to maintain a positive cash balance, or the occurrence of certain insolvency events involving the Debtor or Moyer.

14. In exchange for Bancorp's agreement to forbear, the Debtor agreed, among other things, to (a) pay a forbearance fee and (b) provide an unconditional and absolute guaranty of payment to Bancorp of the obligations under the Moyer Loan Documents (the "**Guaranty of Moyer Obligations**"). The Guaranty of Moyer Obligations was secured by all assets of the Debtor other than computer equipment that is leased to the Debtor and Moyer's stock certificates in the Debtor pursuant to the Security Agreement and the Stock Pledge.

15. In February 2013, the Debtor, Bancorp and Moyer entered into the first amendment to the Forbearance Agreement (the "**First Amendment**"). Pursuant to the First Amendment, Bancorp agreed to delay invoicing the Debtor for certain fines assessed by VISA in November and December of 2012. Throughout 2013 and in January 2014, the Debtor received multiple notices of default of the Bancorp Agreements and the Forbearance Agreement. All of

the obligations due under the Bancorp Agreements, the Forbearance Agreement and the Guaranty of Moyer Obligations were accelerated and due in full. However, the Debtor had no means to and did not make the payments.

16. On February 3, 2014, Bancorp exercised its right under the Stock Pledge and Voting Proxy to serve as Moyer's proxy for the purpose of voting Moyer's stock (which represents a majority of voting shares of the Debtor's stock) to remove Moyer as the sole director of the board of directors and replace him with an independent director. In turn, the independent director (constituting 100% of the board of directors) exercised a written consent removing Moyer from his position as the Debtor's Chief Executive Officer and terminating his employment with the Debtor. As set forth in further detail below, the independent director also authorized my retention as the Debtor's Chief Restructuring Officer. Later, the board was expanded to three directors, and Nancy Reilly, who had been (and continues to be) the Debtor's Chief Financial Officer, was named as the Debtor's new Chief Executive Officer.[2]

17. On May 9, 2014, the Debtor and Bancorp entered into the Second Forbearance Agreement (the "**Second Forbearance Agreement**"). The Second Forbearance Agreement confirms that, as of May 8, 2014, the Debtor was indebted to Bancorp in the aggregate amount of at least $3,123,620.74 (the "**Bancorp Obligations**"), $1,759,175.25 of which was the Guaranty of Moyer Obligations. The Debtor's obligations to Bancorp are secured by a lien on all of the Debtor's property other than equipment that is leased to the Debtor.

18. In exchange for Bancorp's agreement to continue to forebear from exercising its remedies under the Bancorp Agreements, the Forbearance Agreement and the Guaranty of

[2] In order to induce each of these directors, as well as myself, to take on their new positions with a cash flow insolvent company, Bancorp agreed to indemnify each board member as well as my firm, PMCM, LLC, and me. The agreements are general indemnifications which cover claims arising from the board members' and my service as directors and/or officers, as applicable.

Moyer Obligations, the Debtor agreed to consummate a transaction meeting the specifications set forth in the Second Forbearance Agreement within certain milestones, including entering into a definitive agreement for a transaction with a purchaser/investor that is reasonably acceptable to Bancorp on or before June 30, 2014 and closing a transaction with an approved purchaser on or before August 31, 2014. These milestone dates were subsequently extended to July 21, 2014 and September 8, 2014, respectively.

C. Capital Structure

19. As of the Petition Date, the Debtor had total outstanding liabilities and other obligations of approximately $16.6 million and approximately 9.8 million shares of outstanding preferred and common stock. A detailed discussion of the Debtor's capital structure, including its various debt obligations, is set forth below.

i. Debt Structure

20. As set forth above, the Debtor has certain monetary obligations to Bancorp pursuant to the Bancorp Agreements and the Guaranty of Moyer Obligations. As further set forth above, the aggregate amount of these obligations as of May 8, 2014 was approximately $3,123,620.74. The Debtor estimates that as of the Petition Date the Debtor's obligations to Bancorp are approximately $6.2 million. Pursuant to the Security Agreement, Bancorp holds a first priority lien on all of the Debtor's assets other than equipment leased to the Debtor to secure these obligations.

21. In addition to the secured obligations due to Bancorp, the Debtor has approximately $471,345 in second lien debt in favor of the law firm of Wollmuth, Maher & Deutsch, LLP. The Debtor also has capital lease obligations in an approximate amount of $161,881 as of May 31, 2014. The remainder of its liabilities are unsecured and were incurred in the ordinary course of business in the amount of approximately $9.7 million.

ii. Equity Structure

22. The Debtor has issued both preferred stock (7,514,859 shares in 6 series) and common stock (2,322,788 shares) to individuals and corporate entities. Those individuals and entities, and their percentage ownership in each type of stock is set forth in the Debtor's Chapter 11 petition.

23. The Debtor received cash between February 2010 and September 2013 from the following entities: Frascella Capital, LLC, JEMS Venture Capital, LLC and DFW Investments, LLC. The amounts received were always intended to be Class B-2 preferred stock investments. Seven days after Moyer was terminated, for the first time, the Debtor received purported "notes" with respect to the cash received from these entities. The "notes" purport to have a feature whereby on any sale of the Debtor, the "noteholders" will receive double the amount of their investment. While dated in 2010, 2011 and 2013, the "notes" are virtually identical, and state that they were entered into in connection with each other, which does not logically follow. Moreover, one of the "notes" purports to apply to amounts for which a Class B-2 stock certificate in fact had been issued years earlier, and a portion of a second "note" was similarly previously documented as a Class B-2 preferred stock investment. The Debtor's position is that these "notes" are invalid under several different legal theories and that the amounts advanced that were not previously documented as a Class B-2 preferred stock investment -- approximately $6.5 million -- are in fact preferred equity. The $6.5 million in questions is not reflected elsewhere in any of the amounts set forth in this Section I.C.

D. Events Leading Up to the Chapter 11 Case

i. The Debtor's Defaults Under the Bancorp Agreements and the Guaranty of Moyer Obligations; My Appointment as Chief Restructuring Officer

24. As set forth above, in 2012, the Debtor defaulted under the Bancorp Agreement and has been operating under forbearance agreements since that time. The Second Forbearance Agreement, dated May 9, 2014, required the Debtor to consummate a transaction within the milestones set forth in paragraph 18 above and paragraph 21 of the Second Forbearance Agreement. The transaction was required "to include termination of the [Bancorp Agreements] unless otherwise consented to by Bancorp."

25. In addition, the Debtor has been cash flow insolvent since at least December 2013 (if not significantly earlier) and could not meet its debts as they came due without funding from Bancorp, which Bancorp was not required to provide. Moreover, the Debtor was a defendant in several lawsuits (with others threatened) and began suffering default and stipulated judgments due to its inability to pay undisputed claims as well as defense counsel to defend those suits.

26. On February 3, 2014, following the termination of Moyer's employment, I was appointed as Chief Restructuring Officer of the Debtor. Upon my appointment and after evaluating the financial condition of the Debtor, the Debtor retained Raymond James (based on my recommendation as approved by the Debtor's board of directors) to assist in advising on the Debtor's strategic options, including a recapitalization, investment, sale of assets, sale of stock or other transaction in or out of court. Immediately upon its retention, Raymond James commenced the marketing process set forth below.

ii. Pre-Petition Marketing Efforts

27. With the Debtor's assistance, Raymond James identified financial and strategic investors (collectively, the "**Interested Parties**") to garner interest in pursuing a transaction with

the Debtor of any type, including a sale, recapitalization or investment in the Debtor (a "**Potential Transaction**"). Commencing on March 25, 2014, Raymond James contacted and sent teasers to 140 Interested Parties. Fifty-four (54) of them executed non-disclosure agreements and were asked to submit initial non-binding letters of intent ("**Initial LOIs**") by April 23, 2014. Interested Parties that had executed non-disclosure agreements were then given the opportunity to gain access to an electronic data room. On or around that date, nine (9) Interested Parties submitted Initial LOIs, all of which focused on acquiring the Debtor's assets or stock. Accordingly, at that point, the Debtor devoted its attention and focus to pursuing a sale of its assets or stock. Thereafter, six (6) Interested Parties attended management presentations at the Debtor's offices in Delaware or Arizona.

28. Due, in large part, to the Debtor receiving a significant amount of interest from Interested Parties, and with the expectation that Interested Parties would increase and/or otherwise refine their offers for the Debtor's assets or stock once they performed further diligence, Raymond James requested that Interested Parties submit revised non-binding letters of intent ("**2nd Round LOIs**") by May 27, 2014. On or around the deadline, four (4) Interested Parties submitted 2nd Round LOIs. After reviewing and carefully considering the letters of intent, the Debtor, in consultation with its advisors, (i) determined that it should provide Interested Parties with the option to submit yet another non-binding letter of intent ("**Best and Final LOIs**") to further increase the proposed purchase price for the Debtor's assets or stock and (ii) set June 17, 2014 as the deadline to submit Best and Final LOIs. On or around such date, four (4) Interested Parties submitted Best and Final LOIs. After reviewing and carefully considering the letters of intent, the Debtor determined, in consultation with its advisors, that the Best and Final LOI submitted by NAB was the highest or otherwise best offer.

29. On July 31, 2014, the Debtor and the Purchaser entered into a stalking horse asset purchase agreement (the "**Stalking Horse Agreement**"). As a result of the robust and multi-staged pre-petition marketing process conducted by Raymond James, the proposed purchase price for the Debtor's assets under the Stalking Horse Agreement is 3.5 times greater than an indication of interest received late in 2013 from NAB. Moreover, the Stalking Horse Agreement provides the Debtor with a firm commitment that is not subject to any financing or due diligence contingencies and thereby provides the Debtor with a floor against which other bidders can submit competing bids for the Debtor's assets through an auction process.

30. The Stalking Horse Agreement's $50 million purchase price also is highly attractive in that it is sufficient to pay all undisputed creditors in full provides a substantial recovery for the Debtor's equity security holders.

iii. Anticipated Chapter 11 Process

31. As set forth above, the Debtor has determined that value will be maximized by commencing a Chapter 11 case and continuing an orderly sale process. While the pre-petition process already was extensive and lengthy, the commencement of this Chapter 11 Case and the implementation of a Bankruptcy Court supervised sale process allows other bidders to make competing bids and therefor to maximize the value of its estate for the benefit of the Debtor's stakeholders.

32. A sale pursuant to Section 363 of the Bankruptcy Code is the most appropriate course of action for the Debtor. As set forth above, if the proposed Sale is consummated, not only will the Debtor's creditors recover 100% on account of any allowed claims against the estate, the Debtor's equity holders will also receive significant distributions from the proceeds of such Sale. The Debtor does not believe that the Sale could be consummated outside of this bankruptcy proceeding. Among other reasons, while the purchaser originally was willing to

entertain non-bankruptcy options, it required certain representations and warranties that the Debtor could not have provided in an out of court deal. It also required certain third party consents that the Debtor was unable to obtain. Accordingly, the Debtor commenced the Chapter 11 Case.

PART II

33. In furtherance of the reorganization of the Debtor through a sale of all or substantially all of the Debtor's assets, the Debtor is seeking approval of the First Day Motions and related orders (the "**Proposed Orders**").

34. I have reviewed each of the First Day Motions, Proposed Orders, and exhibits thereto (or have otherwise had their contents explained to me), and the facts set forth therein are true and correct to the best of my knowledge, information, and belief. Moreover, I believe that the relief sought in each of the First Day Motions (a) is vital to enabling the Debtor to make the transition to, and operate in, chapter 11 with minimum disruption to its business or loss of productivity or value and (b) constitutes a critical element in the Debtor's being able to successfully maximize value for the benefit of its estate.

A. Application to Appoint Rust Consulting/Omni Bankruptcy as Claims Agent

35. The Debtor filed a motion (the "**Section 156(c) Application**") contemporaneously herewith to retain Rust Consulting/Omni Bankruptcy ("**Rust/Omni**"), as claims, noticing, soliciting, and balloting agent pursuant to Sections 105(a), 156(c), and rule 2002-1(f) of the Local Rules of Bankruptcy Practice and Procedure for the United States Bankruptcy Court for the District of Delaware (the "**Local Rules**"). Rust/Omni is one of the country's leading chapter 11 administrators, with significant experience in noticing, claims administration, solicitation, balloting, and other administrative aspects of chapter 11 cases. Appointing Rust/Omni as the claims and noticing agent in the Chapter 11 Case will relieve the

administrative burden on the Clerk of the Bankruptcy Court for the District of Delaware (the "**Clerk**").

36. The Debtor's selection of Rust/Omni to act as the claims and noticing agent has complied with the Court's *Protocol for the Employment of Claims and Noticing Agents under 28 U.S.C. § 156(c)*, in that the Debtor has obtained and reviewed engagement proposals from at least two (2) other court-approved claims and noticing agents to ensure selection through a competitive process. Moreover, the Debtor submits, based on all engagement proposals obtained and reviewed, that Rust/Omni's rates are competitive and reasonable given Rust/Omni's quality of services and expertise. The Section 156(c) Application pertains only to the work to be performed by Rust/Omni under the Clerk's delegation of duties permitted by Judicial Code Section 156(c) and Local Rule 2002-1(f), and any work to be performed by Rust/Omni outside of this scope is not covered by the Section 156(c) Application or by any order granting approval thereof. A separate retention application addressing Rust/Omni's services beyond Section 156(c) of the Bankruptcy Code will be filed shortly.

B. Cash Management Motion

37. The Debtor has also filed a motion (the "**Cash Management Motion**"), pursuant to sections 105(a), 345(b) and 363(c) of the Bankruptcy Code, requesting the entry of an order: (i) authorizing, but not directing, the Debtor to continue to maintain and use its existing cash management system, including maintenance of the Debtor's existing bank accounts, checks and business forms; (ii) granting the Debtor a waiver of certain bank accounts requirements and related requirements of the Office of the United States Trustee to the extent that such requirements are inconsistent with (a) the Debtor's existing practices under the cash management system or (b) any action taken by the Debtor in accordance with any order granting this Motion

or any other order entered in the Chapter 11 Case; and (iii) granting the Debtor additional time to comply with section 345 of the Bankruptcy Code.

38. In the ordinary course of its business, the Debtor maintains a cash management system (the "**Cash Management System**"). The Cash Management System is integral to the operation and administration of the Debtor's business. The Cash Management System is an ordinary course, customary and essential business practice and allows the Debtor to efficiently identify the Debtor's cash requirements and efficiently monitor and control all of the Debtor's cash receipts and disbursements. The Cash Management System is similar to those utilized by many other companies of comparable size and complexity to collect, transfer and disburse funds in a cost-effective and efficient manner.

39. The continued use of the Debtor's Cash Management System during the pendency of the Chapter 11 Case is essential to the Debtor's business operations and its goal of maximizing value for the benefit of all parties in interest. Requiring the Debtor to adopt new cash management systems at this early and critical stage would be expensive, impose needless administrative burdens and cause undue disruption. Any such disruption would adversely affect the Debtor's ability to maximize estate value for the benefit of creditors and other parties in interest. Moreover, such a disruption would be wholly unnecessary insofar as the Debtor's cash management system provides a valuable and efficient means for the Debtor to address its cash management requirements. Maintaining the Debtor's existing cash management system without disruption is both essential to the Debtor's ongoing operations and in the best interests of the Debtor, its estate and all interested parties. Accordingly, the Debtor requests that it be allowed to maintain and continue to use its Cash Management System and bank accounts.

40. To minimize expenses to its estate, the Debtor seeks authorization to continue using all checks substantially in the forms existing immediately prior to the Petition Date, without reference to the Debtor's status as debtor in possession; provided, however, that in the event the Debtor generates new checks during the pendency of this case other than from its existing stock of checks, such checks will include a legend referring to the Debtor as "Debtor in Possession." Most parties doing business with the Debtor undoubtedly will be aware of the Debtor's status as a debtor in possession as a result of the publicity of this case, planned outreach, the correspondence the Debtor intends to provide to customers and vendors, and additional press coverage. Moreover, the Debtor will provide notice of the commencement of the Chapter 11 Case to creditors and other parties-in-interest. Changing the Debtor's existing checks, correspondence and other business forms would be expensive, unnecessary and burdensome to the Debtor's estate. Further, such changes would be disruptive to the Debtor's business operations and would not confer any benefit upon those dealing with the Debtor.

41. The Debtor believes that the funds held in its bank accounts are secure and that obtaining bonds to secure those funds, as required by section 345(b) of the Bankruptcy Code, would be unnecessary and detrimental to the Debtor's estate and creditors. However, the Debtor needs time to consult with the United States Trustee in order to determine whether its Cash Management System is currently in compliance with the requirements of section 345(b) of the Bankruptcy Code and/or whether the Debtor needs to take any further action to bring its Cash Management System into compliance with the requirements of section 345(b). The Debtor is therefore requesting a sixty (60) day extension of its time to comply with the requirements of section 345(b) of the Bankruptcy Code.

42. I believe that the continued operation of the Debtor's Cash Management System is in the best interests of the Debtor's estate and creditors, will avoid immediate and irreparable harm to the Debtor, and is both necessary and appropriate to further the reorganization policy of chapter 11.

C. Employee Obligations Motion

43. The Debtor has also filed a motion (the "**Employee Obligations Motion**") seeking the entry of an order authorizing them, in their discretion, to pay, continue or otherwise honor various prepetition Workforce-related (as defined below) obligations (collectively, the "**Prepetition Workforce Obligations**") to or for the benefit of its (a) full-time regular employees who are not in a temporary status and who are typically scheduled to work more than thirty (30) hours per week (the "**Full-Time Employees**"), (b) part-time employees who are not in a temporary status and who are typically scheduled to work less than thirty (30) hours per week (the "**Part-Time Employees**" and, together with the Full-Time Employees, the "**Employees**"), (c) individuals that are employed through staffing agencies (the "**Temporary Employees**"), and (d) certain independent contractors retained by the Debtor (the "**Independent Contractors**" and, together with the Employees and the Temporary Employees, the "**Workforce**"), for, among other things, (i) compensation to the Workforce, (ii) expenses and expense reimbursements to the Employees, (iii) continuation of benefits provided to the Employees under all plans, programs and policies maintained or contributed to, and agreements entered into, by the Debtor prior to the Petition Date (the foregoing collectively, and as described in greater detail below, the "**Workforce Programs**"). In addition, the Debtor requests that the Court confirm its right to continue each of the Workforce Programs in the ordinary course of business during the pendency of this Chapter 11 Case in the manner and to the extent that such Workforce Programs were in effect immediately prior to the filing of such case and to make

payments in connection with expenses incurred in the postpetition administration of any Workforce Program.

44. The Workforce Programs under which the Prepetition Workforce Obligations arise are described more fully the Employee Obligations Motion and include, without limitation, plans, programs, policies and agreements providing for (a) wages, salaries, vacation pay, sick pay and other accrued compensation; (b) reimbursement of business and other reimbursable expenses; and (c) benefits, with coverage as applicable for eligible spouses, domestic partners and dependents, in the form of medical, dental and vision coverage, coverage continuation under COBRA,[3] basic term life, supplemental life, accidental death and dismemberment, short-term disability, long-term disability, workers' compensation, and miscellaneous other benefits provided to the full-time Employees in the ordinary course of business.[4]

45. The Employee Obligations Motion also seeks authorization to pay any and all local, state and federal withholding and payroll-related or similar taxes relating to the Prepetition Workforce Obligations including, but not limited to, all withholding taxes, social security taxes and Medicare taxes. In addition, the Debtor seeks authorization to pay to third parties any and all amounts deducted from Employee paychecks by the Debtor for payments on behalf of Employees for benefit plans, insurance programs and other similar programs, or for garnishments, support payments, and similar items.

46. The Debtor also requests in the Employee Obligations Motion that, with respect to any Workforce Programs and Prepetition Workforce Obligations that are administered,

[3] See 29 U.S.C. §§ 1161 et seq.

[4] The Debtor may separately seek authorization to implement new postpetition retention, severance or similar employment protection programs designed to preserve Employee morale, encourage continuing employment and otherwise ameliorate the effects on Employees of this Chapter 11 Case. Pending approval of any such postpetition programs, the prepetition programs will continue in the ordinary course, subject to the provisions of Bankruptcy Code Section 503(c)(2).

insured or paid through a third-party administrator or provider, the Debtor requests authorization, in its discretion, to pay any prepetition claims of such administrator or provider in the ordinary course of business to insure the uninterrupted delivery of payments or other benefits to the Employees.

47. As of the Petition Date, the Debtor employed 36 Full-Time Employees, 4 Part-Time Employees, 1 Temporary Employee and 9 Independent Contractors. Approximately 18 of the Debtor's Full-Time Employees are employed at the Debtor's Arizona office which houses the bulk of the Debtor's developmental and customer service teams. The remaining 18 Full-Time Employees, which satisfy all of the Debtor's other employment needs, work at the Debtor's Delaware office.

48. I believe that the Debtor's ability to preserve its business and successfully maximize the value of the estate is dependent on the expertise and continued enthusiasm and service of its Workforce. Due to the disruption and uncertainty that typically accompanies a chapter 11 filing, I believe that the morale and, thus, the performance of the Workforce may be adversely affected. If the Debtor fails to pay the Prepetition Workforce Obligations in the ordinary course, its Employees and Temporary Employees will suffer extreme personal hardship and, in some cases, may be unable to pay their basic living expenses. Such a result would have a highly negative impact on Workforce morale and likely would result in unmanageable performance issues or turnover, thereby resulting in immediate and irreparable harm to the Debtor and its estate. In addition, the Debtor has determined that continuation of the Workforce Programs is vital to preserving and rebuilding Workforce morale during the pendency of the Chapter 11 Case and to minimizing the level of attrition that might otherwise occur.

D. Utilities Motion

49. In the Debtor's utilities motion (the "**Utilities Motion**"), the Debtor requests entry of interim and final orders approving procedures that would provide adequate assurance of payment to their utility service providers (the "**Utility Companies**") under Bankruptcy Code Section 366, while allowing the Debtor to avoid the threat of imminent termination of electricity, water, and phone and internet services (collectively, the "**Utility Services**") from those Utility Companies. Specifically, the Debtor requests entry of interim and final orders (a) approving the Debtor's deposit of $15,000 (which is approximately 50% of the estimated monthly cost of the Utility Services based on historical averages over the preceding 12 months) into a newly created, segregated, interest-bearing account, as adequate assurance of postpetition payment to the Utility Companies pursuant to Bankruptcy Code Section 366(b), (b) approving the additional adequate assurance procedures described below as the method for resolving disputes regarding adequate assurance of payment to Utility Companies, and (c) prohibiting the Utility Companies from altering, refusing, or discontinuing services to or discriminating against the Debtor except as may be permitted by the proposed procedures.

50. The Utility Services are crucial to the continued operations of the Debtor's business. Given the technological components of the Debtor's business, I believe that the Debtor could not operate its business without the Utility Services. If the Utility Companies refuse or discontinue service, even for a brief period, the Debtor's business operations would be severely disrupted, and the Debtor could be forced to cease operations. Accordingly, the Debtor has proposed certain protections and procedures in the Utilities' Motion to provide additional assurance of payment for future services to the Utility Companies.

E. Critical Vendors Motion

51. Pursuant to the Debtor's critical vendors motion (the "**Critical Vendors Motion**"), the Debtor seeks entry of interim and final orders authorizing, but not directing, the Debtor to pay prepetition claims (the "**Critical Vendor and Service Provider Claims**") held by critical vendors and service providers (the "**Critical Vendors and Service Providers**") in an aggregate amount not to exceed $350,000 (the "**Critical Vendor Cap**"). In the Debtor's ordinary course of business, it relies on a range of goods and services that are necessary to operate its payment processing business. The Debtor purchases such goods and obtains such services from a limited number of vendors and independent contractors. Replacing such vendors—even when possible, which is often not the case—could also result in substantially higher costs for the Debtor and its estate.

52. With the assistance of its advisors, the Debtor spent significant time reviewing and analyzing its books and records, reviewing contracts and supply agreements, and analyzing applicable laws, regulations, and historical practice to identify certain critical business relationships and/or suppliers of goods and services—the loss of which could materially harm its business.

53. The Debtor seeks to pay all or part of the Critical Vendor and Service Provider Claims up to the applicable Critical Vendor Cap to ensure that the Critical Vendors and Service Providers provide necessary goods and services to the Debtor on a postpetition basis. The Debtor does not, however, seek to pay any prepetition obligations of Critical Vendors or Service Providers arising under enforceable, long-term contractual relationships.

54. Because the Debtor anticipates that if the Sale is consummated, it will be able to satisfy all of the allowable claims against its estate, no Critical Vendor or Service Provider will receive more than it otherwise would have received following the close of the Sale or more than

any other unsecured creditor holding an allowable claim against the Debtor's estate. The payment of any Critical Vendor and Service Provider Claim, therefore, only changes the timing of satisfaction of any claims held by Critical Vendors and Service Providers.

55. Accordingly, the relief requested in the Critical Vendors Motion is narrowly tailored to facilitate the Debtor's efforts during the pendency of the Chapter 11 Case. By contrast, the harm suffered by the estate if essential goods and services provided by the Critical Vendors and Service Providers are withheld would be irreparable to the Debtor's ability to continue to operate in Chapter 11 and sell its assets pursuant to the proposed Sale, and so I submit that payment of the Critical Vendor and Service Provider Claims is a sound exercise of business judgment and necessary to preserve the value of the Debtor's business.

F. Debtor in Possession Financing Motion

56. This Chapter 11 Case is predicated on the Debtor's sale of substantially all its assets. To assist in funding this process, the Debtor engaged in what I believe were vigorous, arm's-length negotiations with Bancorp on the terms of a debtor in possession facility (the "**DIP Facility**"), which is appropriately sized to meet the Debtor's financing needs until the Sale is consummated. As a result of this process, the Debtor negotiated the DIP Facility to be provided by Bancorp on terms that I believe are fair and reasonable under the circumstances and reflect the Debtor's exercise of prudent business judgment consistent with its fiduciary duties.

57. The Debtor has an immediate and critical need to obtain post-petition financing under the DIP Facility and to use the Prepetition Collateral of the DIP Lender, including Cash Collateral, in order to permit the orderly continuation of the Debtor's business and its ongoing compliance with the Bancorp Agreements. Further, obtaining post-petition financing will enable the Debtor to make capital expenditures, pay professionals, satisfy other working capital and operational needs, pay interest, fees and expenses in accordance with the DIP Facility, pay

amounts approved by other order of this Court, and fund an orderly sale process of the Debtor's ongoing business and assets.

58. After efforts made by me and, at my direction, by Raymond James, the Debtor's financial advisor, I do not believe that alternative sources of financing are readily available on terms that are more favorable than those set forth in DIP Facility.

59. Because there is simply no viable alternative for the Debtor to maintain operations uninterrupted while facilitating both the sale of substantially all of its assets without the DIP Facility, the advances thereunder are vital to the preservation and maintenance of the going concern value of the Debtor's estate and to maximize the value of the Debtor's estate for the benefit of all parties in interest. Without access to the DIP Facility, the Debtor and its estate would suffer immediate and irreparable harm. Consummation of the DIP Facility and the use of Cash Collateral in accordance with the Budget are therefore in the best interest of the Debtor's estate.

CONCLUSION

60. The Debtor's ultimate goal in this Chapter 11 Case is to maximize the value of its estate for the benefit of its stakeholders. A sale of the Debtor's assets via Section 363 is the best way to accomplish this. In the near term, however, to minimize any loss of value to its business, the Debtor's immediate objective is to promote stability and maintain ordinary course operations during the early stages of this Chapter 11 Case, with as little disruption to operations as possible. I believe that if the Court grants the relief requested in each of the First Day Motions, the prospect for achieving these objectives and completing a successful sale of the Debtor's business will be substantially enhanced.

61. I hereby certify that the foregoing statements are true and correct to the best of my knowledge, information and belief and respectfully request that all of the relief requested in the First Day Motions be granted, together with such other and further relief as is just and proper.

I declare under penalty of perjury that the foregoing is true and correct.

Executed this 4th day of August, 2014.

Phoenix Payment Systems, Inc.
Debtor and Debtor in Possession

Michael E. Jacoby
Chief Restructuring Officer