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UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF NEVADA

In re:	Case No.: BK-S-18-10453-LED
U.S.A. DAWGS, INC.,	Chapter 11
Debtor.	Date: OST Pending Time: OST Pending

EMERGENCY MOTION FOR ENTRY OF AN INTERIM ORDER PURSUANT TO BANKRUPTCY RULE 4001(b) AND LR 4001(b): (1) PRELIMINARILY DETERMINING EXTENT OF CASH COLLATERAL AND AUTHORIZING INTERIM USE OF CASH COLLATERAL BY DEBTOR; AND (2) SCHEDULING A FINAL HEARING TO DETERMINE EXTENT OF CASH COLLATERAL AND AUTHORIZING USE OF CASH COLLATERAL BY DEBTOR

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U.S.A. Dawgs, Inc., debtor and debtor-in-possession ("Debtor"), by and through its undersigned proposed counsel, hereby submits its motion ("Motion") requesting that the Court: (i) enter an interim order (the "Interim Order"), a proposed copy of which is attached hereto as **Exhibit "1,"** preliminarily determining the extent of Cash Collateral[1] as defined by Section 363(a) and authorizing the interim use of Cash Collateral to pay costs of administration and to operate Debtor's business in the ordinary course pending a final hearing (the "Final Hearing"); and (2) setting the Final Hearing to determine the extent of Cash Collateral and authorizing Debtor to use Cash Collateral during the pendency of Debtor's Chapter 11 Case.

This Motion is made and based on the memorandum of points and authorities provided herein, the *Omnibus Declaration of Steven Mann in Support of Debtor's Chapter 11 Petition, First Day Motions, and Employment Application* (the "Omnibus Decl."), the pleadings, papers and other records contained in the Court's file, judicial notice of which is hereby requested, and any evidence or oral argument presented at the time of the hearing on this Motion.

MEMORANDUM OF POINTS AND AUTHORITIES

I.
INTRODUCTION, JURISDICTION, AND VENUE

On January 31, 2018 (the "Petition Date"), Debtor filed its voluntary Chapter 11 petition for relief, thereby commencing this Chapter 11 Case. See ECF No. 1. Debtor continues operating its business and managing its property as debtor and debtor-in-possession pursuant to Sections 1107(a) and 1108. No request has been made for the appointment of a trustee or examiner, and no official committees have been established.

This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157(b)(1)(A) and (M) and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2). Venue in this district is proper pursuant to 28 U.S.C. §§ 1408 and 1409. Sections 361 and 363,

[1] "Cash Collateral" is defined in Section 363(a) as "cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest and includes the proceeds, products, offspring, rents, or profits of property and the fees, charges, accounts or other property for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties subject to a security interest provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title."

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Bankruptcy Rule 4001(b), and LR 4001(b) provide the statutory basis for the relief sought herein.

Pursuant to LR 9014.2, Debtor consents to entry of a final order or judgment by the bankruptcy judge if it is determined that the bankruptcy judge, absent consent of the parties, cannot enter final orders for judgment consistent with Article III of the U.S. Constitution.

II.
SUMMARY OF RELIEF SOUGHT

1. Debtor entered into a revolving loan agreement with Lender effective October 24, 2012, whereby Lender provided a Revolving Loan Commitment to Debtor of up to $2 Million, later amended up to $7.5 Million, and thereafter decreased to the amount of $5.5 Million as of the Petition Date (the "Loan"), which Loan is secured by Debtor's inventory, accounts receivables, certain intellectual property, and certain commercial tort claims (collectively, the "Collateral").

2. As of the Petition Date, Lender contends the outstanding balance of the Loan is approximately $3,895,000.00.

3. As Lender did not have possession or control over Debtor's cash, cash equivalents, or deposit accounts on the Petition Date, Lender does not have a perfected security interest in such cash, cash equivalents, or deposit accounts. However, pursuant to Section 552(b)(2), Lender retains its security interest in Debtor's cash proceeds that are identifiable and traceable directly from the Collateral generated after the Petition Date.

4. To the extent Lender has a valid and perfected interest in Debtor's post-petition cash constituting Cash Collateral, Debtor seeks authorization to use such Cash Collateral to pay the ordinary course administrative expenses of Debtor's estate, including, but not limited to, the costs of operations, including, without limitation, utility charges, trade payables, insurance, taxes, replacement inventory, and all other expenses incurred in operating and administering Debtor's estate during its Chapter 11 Case.

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5. Attached hereto as **Exhibit "2"** is a budget of projected income and expenses for the first 90 days following the Petition Date (the "Budget").[2] Debtor proposes that it be permitted a fifteen percent (15%) variance for the Budget line items titled "Total Cash Paid Out" to account for the inherent fluctuations in monthly expense. Similarly, in the event that Debtor's "Total Cash Paid Out" for any month are less than projected, Debtor requests that it be authorized to carryover and include such positive variance into the following month.

6. Through the Motion, Debtor requests that it be entitled to use Cash Collateral on an emergency interim basis pending the Final Hearing in accordance with the Budget, which is necessary to avoid immediate and irreparable harm to Debtor and its bankruptcy estate. Without the authority to use Cash Collateral, Debtor will be forced to cease its operations, thereby eliminating its ability to reorganize. See Omnibus Decl. ¶ 52.

III.
PERTINENT FACTS

A. Debtor's Operations

7. In the early 2000s, Steven Mann, Debtor's president and chief executive officer, suffered from excruciating back pain and required chiropractic visits at least multiple times per month to find relief. That all changed when he commenced wearing special footwear made of light-weight, ultra-soft, and easy to clean conforming material that proved to provide relief that he was unable to find anywhere else. See Omnibus Decl. ¶ 4.

8. That concept formed the foundation of a company Mr. Mann initially founded in Canada called Double Diamond Distribution Ltd. ("Diamond"). Diamond began by developing and selling DAWGS Brand footwear. Finding initial success in Canada and realizing a greater ability to conduct business in the United States, Mr. Mann formed Debtor, a Nevada corporation, in June 2006. Debtor began substantive operations in 2007 and began shipping footwear in

[2] The Budget will be revised and updated for each subsequent 90-day period throughout the Chapter 11 Case. No later than fifteen (15) calendar days prior to the end of each 90-day period, Debtor will deliver to Lender a proposed budget for the next 90-day period (each such updated budget, a "Supplemental Budget"). Lender shall have five (5) days to review and approve such Budget and, if approved or if no response is received within five (5) days, such Budget shall constitute the approved Budget without further notice, motion, or application to, order of, or hearing before, the Court. To the extent that Lender objects to the Supplemental Budget and Debtor and Lender cannot agree upon a Supplemental Budget, Debtor shall be entitled to seek Court approval of such Supplemental Budget on order shortening time.

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2008. See id. ¶ 5.

9. Soon after its launch, the DAWGS brand footwear label quickly became a significant competitor in the shoe industry's evolution towards new comfort, leading to substantial sales of merchandise. See id. ¶ 6.

10. Today, Debtor operates out of a 44,0000 square-foot warehouse (the "Property") in southwest Las Vegas and concentrates on distributing specialized quality and value priced footwear. Debtor currently employs a workforce of twenty-one people and in recent years has had sales ranging between $9 and $17 million per year in gross-revenue. See id. ¶ 7.

11. Debtor sells DAWGS branded products and other private labels including "Doggers" and "Hounds," which are owned by Diamond, not only on its website, www.usadawgs.com (the "Website"), but also through third-party online sites, retailers, wholesalers, and catalog companies throughout the United States. In addition to its DAWGS brand and other private label brands of footwear, Debtor also sells Agiato and Steven Craig brands of apparel. See id. ¶ 8.

B. The Events Leading to Chapter 11.

12. Despite its early success, Debtor has encountered more than its fair share of challenges. While Debtor has consistently been able to overcome these obstacles, the confluence of them has led Debtor to seek the protections of the Bankruptcy Code to protect its assets and creditors. See id. ¶ 9.

1. Debtor's 12-Year Litigation with Crocs, Inc.

13. Within months of formation, by April 2006, Diamond found itself the target of Crocs, Inc. ("Crocs"), which claimed that certain of Diamond's DAWGS branded footwear infringed two patents. On March 31, 2006, Crocs filed a Complaint with the International Trade Commission ("ITC") against Diamond and other respondents. Three days later, on April 3, 2006, Crocs filed a lawsuit (the "2006 Lawsuit") against Diamond and other defendants, asserting the same two patents. The 2006 Lawsuit was stayed while the ITC investigation proceeded. See id. ¶ 10.

14. As the case made its way through the ITC, Diamond initially was successful. On

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April 11, 2008, the presiding Administrative Law Judge ("ALJ") found no violation by Diamond. On July 25, 2008, the ITC affirmed the ALJ's determination. However, on February 24, 2010, the U.S. Court of Appeals for the Federal Circuit issued a limited-scope decision reversing the ITC's determination. As a result, in 2011 the ITC issued remedial orders that prevented the importation of certain DAWGS branded footwear into the U.S. See id. ¶ 11.

15. In 2012, the 2006 Lawsuit was reopened and Crocs amended its complaint to add Debtor as a defendant. After Diamond filed a request for reexamination of one of Crocs' patents with the U.S. Patent Office, Crocs retaliated by suing Debtor's then-largest customer, CVS Pharmacy ("CVS"), five days later. Debtor subsequently sought reexamination of the other patent that Crocs had asserted, which is Crocs' cornerstone patent ("the '789 Design Patent"). The 2006 Lawsuit was then again stayed to allow the U.S. Patent Office to conduct the reexamination proceedings. See id. ¶ 12.

16. In 2013, 2016, and finally in 2017, the U.S. Patent Office rejected the '789 Design Patent as unpatentable. In the 2017 action, which was mailed on August 9, 2017, the U.S. Patent Office issued a Right of Appeal Notice rejecting the '789 Design Patent as unpatentable for the third time. Unless Crocs is successful in its efforts to overturn the decision of the U.S. Patent Office on appeal, the '789 Design Patent will be cancelled by the U.S. Patent Office. See id. ¶ 13.

17. The results of the reexamination of the '789 Design Patent have confirmed the belief long held by Diamond and Debtor that the patents asserted by Crocs are invalid and never should have been granted in the first place. However, the multiple rejections of the '789 Design Patent have not stopped Crocs from continuing to pursue litigation against Debtor. Crocs has also purposely used the existence of the lawsuit to harass Debtor's customers. As discussed above, in 2012, Crocs sued Debtor's largest customer, CVS. However, after CVS moved to dismiss the lawsuit against it, Crocs dismissed the suit instead of responding to the motion to dismiss, and filed a new lawsuit against CVS that same day in a different district. Debtor intervened in that lawsuit, which Crocs filed in the Southern District of Florida, and with a trial date five months away and discovery commencing in earnest, Crocs successfully moved to

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dismiss its own lawsuit over the opposition of Debtor. In addition to that obviously harassing lawsuit, Crocs issued subpoenas to dozens of Debtor's customers. More recently, over the past few months, Crocs has used the customer list supplied by Debtor in the litigation to contact Debtor's customers and threaten them with lawsuits. The foregoing actions have strained Debtor's relationship with its customers and, in many cases, caused Debtor's customers to diminish or cease their business with Debtor. See id. ¶ 14.

18. While Crocs' claims against Debtor in the 2006 Lawsuit are without merit, Debtor has been forced to expend large sums defending against them. In contrast to Crocs' claims, Debtor has also raised counterclaims against Crocs, which Debtor believes to be of substantial value. In essence, Crocs has been falsely promoting the material from which its footwear is made as "patented," "proprietary," and "exclusive," for the past fifteen years, when the material is none of those things. While Debtor's claims against Crocs (and against eighteen current and former Crocs officers and directors) has already survived motions to dismiss, Debtor has had to expend significant resources ensuring that it is able to bring the litigation to a successful resolution. See id. ¶ 15.

19. Today, two cases remain pending between Debtor and Diamond, and Crocs and its current and former officers: (1) *Crocs, Inc. v. Effervescent et al*, Civil Action No. 06-cv-605 pending in the United States District Court for the District of Colorado; and (2) *U.S.A. Dawgs, Inc. v. Snyder, et al.*, Civil Action No. 16-cv-2004 pending in the United States District Court for the District of Colorado (collectively, the "Crocs Litigation"). Debtor and Diamond have also sought to have the ITC modify or rescind the exclusion order that prevents the importation of certain DAWGS brand footwear into the U.S. The ITC's denial of the petition of Debtor and Diamond is now in front of the U.S. Court of Appeals for the Federal Circuit, in Case No. 18-1219. See id. ¶ 16.

2. Debtor's Largest Customer Files for Bankruptcy and Its Customers Continued to be Threatened by Crocs.

20. Debtor operates with a myriad of online retailers for which it acquires and stocks products and fulfills online orders. See id. ¶ 17.

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21. One such retailer was Choxi.com, Inc. f/k/a Nomorerack ("Choxi"). Choxi unexpectedly (to Debtor, at least) found itself the subject of an involuntary Chapter 7 bankruptcy filing in the United States Bankruptcy Court for the Southern District of New York on November 10, 2016. On December 5, 2016, Choxi filed a voluntary petition under Chapter 11, which case remains pending as Case No. 1613131. See id. ¶ 18.

22. Choxi and Debtor's business relationship was irreparably harmed as a result of the bankruptcy filing, which caused Debtor's sales to Choxi to be significantly reduced from between $7 million and $9 million per year in 2014 and 2015 to zero as a result of Choxi's bankruptcy. In addition, Debtor holds an unpaid claim against Choxi of approximately $78,000. See id. ¶ 19.

23. This, compounded with the aggressive and improper attack by Crocs on Debtor's other customers, resulted in a temporary income decline that Debtor has steadily been rebuilding. See id. ¶ 20.

3. Lender Breaches the Loan Agreement and Refuses to Provide Adequate Funding to Debtor.

24. From its inception until approximately 2012, Debtor operated without any traditional corporate financing in place, instead funding its operations primarily through revenue. However, given the strains caused by the Crocs Litigation and Crocs' improper tactics to interfere with Debtor's relationship with its customers, Debtor found itself in a position of having to locate outside financing. See id. ¶ 21.

25. As Mr. Mann is a Canadian citizen and given the pending Crocs Litigation, traditional funding from Debtor's operations were not readily available. Therefore, Debtor was forced to seek unconventional financing, which came with burdensome terms and extraordinary interest rates. Debtor located such funding through GemCap Lending I, LLC ("Lender"). See id. ¶ 22.

26. On or about October 24, 2012, Debtor entered into the *Loan and Security Agreement by and between GemCap Lending I, LLC as Lender and U.S.A. Dawgs Inc.as*

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Borrower (the "Loan Agreement")[3] which provided for lending (the "Revolving Loan Commitment") up to the lesser of: (1) $2,000,000 (the "Maximum Credit") or, the Borrowing Base, calculated as set forth in 1.15 of the Loan Agreement (the "Borrowing Base Calculation"). See id. ¶ 23; Exhibit "1."

27. Concurrently with the Loan Agreement, Lender and Debtor executed the *Loan Agreement Schedule* dated as of October 24, 2014 (the "Loan Agreement Schedule"), (ii) *Secured Promissory Note (Revolving Loans)* dated as of October 24, 2012 (the "Promissory Note"); and (iii) other Loan Documents (collectively, the "Loan Documents"). The original maturity date (the "Maturity Date") under the Promissory Note was October 2014. See id. ¶ 24; Exhibits "2" – "4."

28. The Loan Agreement is guaranteed by both Steven Mann and Barrie Mann, one of Debtor's other owners. See id. ¶ 25.

29. The Loan Agreement provides for substantial fees to Lender in addition to an annual interest rate of 17%, and a default rate of 24%. In addition, the Loan Agreement specifically provided for amounts to be advanced over the Revolving Loan Commitment, defined as "Overadvances." See id. ¶ 26.

30. The revolving loan works as follows, Lender initially provides funding secured by Debtor's inventory and accounts receivables and is repaid in part as the accounts receivables are paid. Then, based on a formula involving the value of the inventory and receivables, Lender advances additional funds that Debtor uses for business expenses and operations, which loan is repaid in part through the accounts receivable. The revolving loan payments are called Advances. See id. ¶ 27.

31. Lender quickly realized the strength of Debtor's business and, through a series of seven amendments over approximately five years, Lender continually increased the amount available under the Revolving Loan Commitment and amended certain terms in the Loan Agreement and Loan Documents. The amendments (collectively, the "Loan Agreement

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Amendments")[4] provide as follows:

> *Amendment No. 1 to Loan and Security Agreement* (the "First Loan Amendment") dated December 9, 2013 - Increased the Revolving Loan Commitment from $2,000,000 to $2,500,000.
>
> *Amendment No. 2 to Loan and Security Agreement* (the "Second Loan Amendment") dated January 30, 2014 – Increased the Revolving Loan Commitment from $2,500,000 to $3,000,000.
>
> *Amendment No. 3 to Loan and Security Agreement* (the "Third Loan Amendment") dated March 15, 2014 – (1) Increased the Revolving Loan Commitment from $3,000,000 to $4,500,000; (2) Extended the Maturity Date to March 31, 2015; and (3) decreased the interest rate commencing March 15, 2014 from 17% to 13%.
>
> *Amendment No. 4 to Loan and Security Agreement* (the "Fourth Loan Amendment") dated November 25, 2014 – (1) Increased the Revolving Loan Commitment from $4,500,000 to $5,500,000 and (2) Extended the Maturity Date to March 31, 2015.
>
> *Amendment No. 5 to Loan and Security Agreement and to the Loan Agreement Schedule* (the "Fifth Loan Amendment") dated April 9, 2015 – (1) Increased the Revolving Loan Commitment from $5,500,000 to $7,500,000; (2) extended the Maturity Date to March 31, 2016; and (3) Increased the interest rate to 15%.
>
> *Amendment No. 6 to Loan and Security Agreement* (the "Sixth Loan Amendment") dated March 31, 2016 – Extended the Maturity Date to March 31, 2017.
>
> *Amendment No. 7 to Loan and Security Agreement and to the Loan Agreement Schedule* (the "Seventh Loan Amendment") dated April 1, 2017 – (1) decreased the Maximum Credit to $5,500,000; (2) Extended the Maturity Date to March 31, 2018; and (3) Increased the interest rate to the greater of (I) fifteen percent and (II) sum of (i) the "Prime Rate" as reported in the "Money Rates" column of The Wall Street Journal, adjusted as and when such prime rates changes plus (ii) eleven percent (11%).

See id. ¶ 28, Exhibits "6" – "12."

32. Debtor's strong operations proved to be an incredible investment for Lender which, on average, received interest (at the rate of between 13% and 17%) and significant fees. Since October 2012, Debtor has paid Lender over $3,200,000 in interest and fees. Recently, for

[4] The Loan Agreement Amendments generally had corresponding amendments to the Loan Documents.

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example, in Debtor's fiscal year 2016, Debtor paid Lender over $910,000 in interest and fees, and in fiscal year 2017, Debtor paid Lender over $759,000 in interest and fees. These amounts are *in addition to principal repayment*. See id. ¶ 29.

33. Consistent therewith, in its approximately five-year history with Lender, Debtor's assets always supported a sufficient Borrowing Base to obtain adequate capital and Overadvances were never necessary nor utilized. See id. ¶ 30.

34. Debtor has also repaid significant principal. For example, on December 31, 2015, the loan balance was approximately $5,900,000, and in January 2018, Lender acknowledges that the outstanding loan balance had been reduced to less than $3,900,000. Thus, the loan balance was reduced by $2,100,000 in a short period of twenty-five months (while Dawgs was paying huge amounts of interest, as specified above). See id. ¶ 31.

35. However, despite receiving all of the aforementioned payments, inexplicably, by mid-2017, Lender decreased the Revolving Loan Commitment and begin reducing the Borrower Base to prevent Debtor from obtaining sufficient funds to adequately continue operations. Based on Lender's own comments and publicly available information, it appears that Lender's decrease may have been a result of Lender's own cash-flow concerns, including a number of underperforming loans in its portfolio. See id. ¶ 32.

36. Compounding Lender's limit to proper access to funds, contrary to the express Borrowing Procedures, as well as the parties' course of conduct since October 2012, in order to delay timely providing the required Advances, for months, Lender began demanding information not required in the Borrowing Certificate as a condition to providing the requested Advances. Further exacerbating the harm, Lender often intentionally made these demands minutes before the Advance deadline to ensure that the Advance could not be made until the next day. Lender made these demands in spite of the fact that it conducted extensive audits of Debtor that lasted weeks on at least an annual basis, and had constant access to Debtor's financial information and status. See id. ¶ 33.

37. The cumulative result was that Debtor was prohibited from borrowing up to its Revolving Loan Commitment of $5,500,000. Instead, with more than $1,600,000 available

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under the Revolving Loan Commitment, Lender contended the Borrowing Base had become insufficient and, refused to provide the funds customarily provided in order for Debtor to meet its normal business operations, including its payroll liabilities. See id. ¶ 34.

38. Also in mid-2017, Lender presented the *Amendment Number 8 to the Loan and Security Agreement and the Loan Agreement Schedule* (the "Eighth Loan Amendment") providing for an Overadvance of $240,000 at an immediate fee to Lender of $50,000 payable at approximately $17,000 per month for three months. See id. ¶ 35, Exhibit "13."

39. In addition to the significant fees obtained by Lender as a result of the Overadvance, Lender demanded that, in exchange for providing the $240,000 Advance, in addition to the interest in the inventory and accounts receivable, Debtor grant Lender a security interest in the Crocs Litigation. This occurred after Debtor informed Lender of the significant value of the Crocs Litigation. See id. ¶ 36.

40. Pursuant to the Loan Agreement Schedule, Lender is obligated to apply the collection of proceeds and collateral: first, to Overadvances; second, to all fees costs and expenses; third, to accrued and unpaid interest; and fourth, to matured and unpaid obligations. See id. ¶ 37.

41. On August 22, 2017, following the $240,000 Overadvance, the balance under the Loan Agreement was $4,453,175.28. Since August 2017, in excess of $2,000,000 has been collected by from Debtor by Lender. As set forth in the Loan Agreement Schedule, the first $240,000 of the over $2 million received should have been applied to the Overadvance. However, Lender has failed to properly apply the funds it has received to the Overadvance. See id. ¶ 38.

42. Additionally, as repayment for its loan, Lender would be paid nearly all of Debtor's receivables, yet, beginning in 2017, Lender refused to provide sufficient and proper Advances thereon. For example, between December 22, 2017 through January 24, 2018, Lender directly received more than $400,000 in cash receivables from Debtor's sales. Lender, in turn, has only provided Advances of $23,100 during that same time period. At the same time, Lender sharply reduced Advances requested by Debtor in certain instances and in others outright refused

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to provide any Advances at all. Since January 11, 2018, Lender funded only one Advance for $3,600, despite receiving over $400,000 in payments. Lender has failed to provide information as to how it has applied the $400,000 it received. See id. ¶ 39.

43. Furthermore, in recent months, Lender has made demand on Debtor to quickly reduce inventory in order to provide additional payments to Lender. While Debtor believes that doing so does not maximize the value of its inventory, Lender has left Debtor with no other choice, yet uses such reduced sales as further purported evidence of a decreased Borrowing Base. See id. ¶ 40.

44. It became increasingly clear to Debtor that Lender was attempting to manufacture defaults and to quickly obtain Debtor's assets in order to address its own liquidity concerns. Moreover, Lender's intention to force Debtor to go out of business and/or to take control of Debtor and of the Crocs Litigation is further evidenced by the fact that Lender has been consistently aware of the precise financial condition and needs of Debtor. See id. ¶ 41.

45. Sure enough, despite *its own breaches* of the Loan Agreement commencing, at the latest, in mid-2017, on January 23, 2018, Lender delivered a *Notice of Default* (the "Notice of Default") to Debtor contending that *Debtor was in breach* of the Loan Agreement for the following:

> •Borrower has failed to comply with certain representations and warranties and covenants and conditions set forth in the Loan Agreement, including, but not limited to, the following:
>
> • Section 9.1 (Notify Lender) – Borrower failed to notify Lender of all material adverse information relating to the financial condition of Borrower.
>
> • Section 9.4 (Observe Covenants, etc.) – Borrower failed to observe its covenant to timely pay interest on the Loan and to cause all Collections with respect to all Accounts to be directed to Lender and deposited into the Collection Account.
>
> In addition, Events of Default as described in the Loan Agreement have occurred (such Events of Default are referred to as the "Specified Events of Default"), including, but not limited to, the following:

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> • Section 11.1 (Failure to Pay) – Borrower failed to pay interest when due.
>
> • Section 11.2 (Failure of Insurance)
>
> • Section 11.3 (Failure to Perform) - Borrower failed to notify Lender of all material adverse information relating to the financial condition of Borrower and failed to observe its covenant to cause all Collections with respect to all Accounts to be directed to Lender and deposited into the Collection Account.
>
> • Section 11.9 (Change of Condition)

See id. ¶ 42, Exhibit "14."

46. As a result, Lender (i) accelerated the payment of all obligations under the Loan Agreement and demanded immediate payment of the same on or before 5:00 p.m. EST on January 26, 2018, (ii) purported to increase the interest rate under the Loan Agreement to the default rate of 24%; and (iii) demanded that Debtor assemble and make available to Lender all the Collateral at any place and time designated by Lender. Lender asserts that the amount due as of the Petition Date is $3,895,104.83. See id. ¶ 43.

47. The following day, on January 24, 2018, Debtor sent a letter to Lender refuting Lender's assertions that Debtor had breached the Loan Agreement. The letter also explained that Lender had in fact breached its own obligations under the Loan Agreement, including:

- Improper and artificial deflation of borrowing base under Section 1.15;
- Improper denial and delay of funding advances under Section 1(v);
- Improper application of payments under Section 1(x); and
- Failure to act fairly and in good faith.

See id. ¶ 44, Exhibit "15."

48. Debtor requires breathing room to refocus its efforts from dealing with Lender's interruptions to maximizing the value of its estate and investigating its options against Lender regarding its improper breach of the Loan Agreement. See id. ¶ 45.

49. Debtor also has significant assets to protect. Debtor estimates, through extensive

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evaluation, its potential recovery in the Crocs Litigation could reach hundreds of millions of dollars, and is extremely likely to exceed tens of millions of dollars. See id. ¶ 46. Lender has also expressed that it believes its lien in the Crocs Litigation to have a value over $2,000,000.

50. Debtor also holds approximately $6,000,000 of inventory at cost which, based on sales prices over the last twelve months (which themselves were reduced prices due to the pressure applied by Lender to sell inventory on an expedited basis) would be sold for approximately $18,000,000. In a normalized environment, without the pressure from Lender, this same inventory should be sold for in excess of $25,000,000. Contrary to typical fashion products, which may decrease in value as trends change, Debtor's inventory consists of functional evergreen products which Debtor has sold for the past ten-years, and Debtor anticipates being able to sell for several more years to come. Debtor also holds more than $450,000 in accounts receivable, approximately $390,000 of which the Debtor anticipates are collectible. Debtor holds other assets too, including a customer list of over 500,000 customers. See id. ¶ 47.

51. Notably, without Lender's continued interference and with proper access to its income, Debtor has sufficient funds, and sufficient history of running a profitable operation, to continue operations and proceed towards proposing a plan of reorganization for the benefit Debtor, the estate, and its creditors. See id. ¶ 48.

C. Debtor's Use of Cash Collateral Is Necessary to Preserve the Value of the Property.

52. On the Petition Date, Debtor had cash and cash equivalents on hand as of the Petition Date (the "Cash on Hand") and cash in its bank account as of the Petition Date (the "Deposit Accounts") in the approximate aggregate sum of $34,500. Such cash was not in the possession of or under the control of Lender. See id. ¶ 51.

53. Debtor cannot meet its ongoing post-petition obligations unless it has the immediate ability to use Cash on Hand, the Deposit Accounts, and the cash generated or received by Debtor from and after the Petition Date (the "Post-Petition Cash"). In the absence of such use, immediate and irreparable harm will result to Debtor, its estate, and its creditors, and

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will render an effective and orderly reorganization of Debtor's business impossible. See id. ¶ 52.

54. An integral aspect of maintaining Debtor's business operations is Debtor's ability to use Cash on Hand, the Deposit Accounts, and Post-Petition Cash to maintain a sufficient level of working capital in order to pay ordinary course obligations such as those to its vendors, utilities, taxing authorities, insurance, and to pay for necessary ordinary business expenses. Debtor also requires the use of the Cash Collateral to obtain new inventory to generate additional accounts receivable. See id. ¶ 53.

55. Debtor is solely seeking to utilize the Cash Collateral to maintain the value of the business, to satisfy its obligations to its customers, and to pay its necessary operating expenses. Each expense included within the Budget is a necessary expense to maintain, preserve, and/or continue Debtor's operations, which is the sole means of generating revenue, thereby increasing the value of Debtor's business and providing the resources for Debtor to effectuate its Chapter 11 plan and an expeditious resolution of this Chapter 11 Case. See id. ¶ 54.

56. In addition to its intellectual property, its inventory is valued at $6,000,000 at cost and in excess of $25,000,000 when properly sold, and its accounts receivable total $450,000, which amounts Debtor anticipates are collectible. Beyond these assets, Debtor is seeking hundreds of millions of dollars of damages in the Crocs Litigation, could to go to trial as soon as within a year. See id. ¶¶ 46-47. Lender contends that all of these asserts serve as its collateral (the "Collateral").[5]

57. Thus, the value of Lender's Collateral far exceeds Lender's claim as of the Petition Date. Even without taking into consideration the intellectual property, Lender has an over $3 million equity cushion (valuing inventory at cost) and over $20 million equity cushion (valuing inventory at going concern). Further, as to the intellectual property and Crocs Litigation, the Collateral will not diminish in value. As to the accounts receivable and inventory,

[5] For the avoidance of doubt, Debtor reserves all rights to determine the extent of Lender's collateral.

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Lender will continue to obtain replacement liens on any new inventory or accounts receivables acquired after the Petition Date pursuant to the Loan Agreement. Therefore, Lender is more than adequately protected.

IV.
LEGAL ARGUMENT

A. Statutory Framework.

Section 363 provides that a debtor in possession may not use, sell, or lease cash collateral unless: (1) each entity with an interest in such cash collateral consents; *or* (2) the court, after notice and hearing, authorizes the use, sale, or lease of such cash collateral in accordance with the provisions of Section 363. See 11 U.S.C. § 363(c)(2). "[A]t any time, on request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased, by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest." 11 U.S.C. § 363(e). While the Debtor has the burden of proof on the issue of adequate protection, the entity claiming an interest in the alleged cash collateral has the burden of proof on the issue of validity, priority, and/or extent of its interest in the property. See 11 U.S.C. § 363(p).

Pursuant to Section 363(a), cash collateral includes cash, cash equivalents, deposit accounts, rents, and proceeds "in which the estate and an entity other than the estate have an interest." 11 U.S.C. § 363(a). Whether an entity has a security interest in a particular item of property is generally determined by state law. See Butner v. United States, 440 U.S. 48, 57 (1979); Raleigh v. Illinois Dept. of Revenue, 530 U.S. 15, 20 (2000).

The "interest" set forth in Section 363(a) refers to a valid and perfected security interest between the parties that secures the cash collateral.[6] A creditor holding a perfected security interest in property "will be entitled to the protection of the cash collateral provisions of [Section] 363(a)" because such interests are not avoidable under the "strong arm" provisions of

[6] See In re Corner Pockets of the Southwest, Inc., 85 B.R. 559, 563 (Bankr. D. Mont. 1988) (stating that only perfected security interests give rise to "cash collateral" as defined by Section 363) (citing Waldron v. Northwest Acceptance Corp. (In re Johnson), 62 B.R. 24, 28-29 (B.A.P. 9th Cir. 1986)); In re Fairview-Takoma Ltd. P'ship, 206 B.R. 792, 796-800 (Bankr. D. Md. 1997).

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Section 544(a)(1) and (3). See In re Fairview-Takoma Ltd. P'ship, 206 B.R. 792, 799 (Bankr. D. Md. 1997); see also Indian Motorcycle Assocs. III L.P. v. Massachusetts Housing Fin. Agency, 66 F.3d 1246, 1252 (1st Cir. 1995).

B. Lender's Interest in Cash Collateral Is Limited and any Property Deemed Cash Collateral Should be Authorized for Debtor's Use.

As previously set forth herein, the Loan Agreement and Loan Documents granted Lender a security interest in the Collateral. However, pursuant to Nevada law, a security interest in cash, cash equivalents, or a deposit account may solely be perfected by possession or control.[7] On the Petition Date, Debtor's Cash on Hand and Deposit Accounts were neither in the possession of nor under the control of Lender. Thus, Debtor's Cash on Hand and Deposit Accounts existing on the Petition Date are not subject to a valid and perfected security interest and do not constitute Cash Collateral.

To the extent that Debtor is authorized to use the Post-Petition Cash, commencing on the Petition Date and each day thereafter, as set forth in the Budget, Debtor will generate revenue from post-petition revenue (the "Post-Petition Revenues"). Debtor concedes that such Post-Petition Revenues will constitute Lender's Cash Collateral but that, as further set forth below, Debtor should be authorized to use such Cash Collateral in order to protect the Collateral and, in turn, Debtor's estate and creditors.

C. The Equities of the Case Allow for Debtor's Use of Cash Collateral.

Sections 552(b)(1) and (2) provide that pre-petition security interests, in certain circumstances, may extend to revenues generated post-petition by the collateral, but allows the Court "based on the equities of the case" to order otherwise. As aptly explained by the United States Bankruptcy Court for the Southern District of New York:

> Even if there is a valid security interest in post-petition acquired property constituting the proceeds, products, offspring, or profits of pre-petition

[7] See NRS 104.9312(2) (providing in pertinent part that: "(a) a security interest in a deposit account may be perfected only by control under NRS 104.9314;…. (c) a security interest in money may be perfected only by the secured party's taking possession under NRS 104.9313"); see also Rus, Miliband & Smith, APC v. Yoo (In re Dick Cepek, Inc.), 339 B.R. 730, 740 (B.A.P. 9th Cir. 2006); see also NRS 104.9313(1) (providing in relevant part that "a secured party may perfect a security interest in negotiable documents, goods, instruments, money, or tangible chattel paper by taking possession of the collateral.").

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> collateral, § 552(b)(1) still allows a court to trump a pre-petition lien to this post-petition acquired property after notice and a hearing and based on the equities of the case. Depending on equities of the case, profit or loss of the property may be given to the estate or to the secured party, or apportioned between them. The equities of the case doctrine is intended to ensure that secured creditors do not receive a windfall benefit when a trustee uses assets of the estate, for example, to finish uncompleted inventory, and it is also used to adjust recovery by a secured creditor in situations where there is an improvement or decline in the post-petition collateral, especially in situations where the change in value is brought about by a party in the bankruptcy.

In re Barbara K. Enterprises, Inc., 2008 WL 2439649 *11 (Bankr. S.D.N.Y. 2008):

Furthermore, the case law and the legislative history accompanying Section 552(b) similarly demonstrate that this equitable exception applies where an expenditure of estate funds increases the value of the collateral subject to the security interest in question, rather than depletes it. See H. Rep. No. 595, 95th Cong., 1st Sess. 376-77 (1977); see also J. Catton Farms, Inc. v. First Nat. Bank of Chicago, 779 F.2d 1242, 1246 (7th Cir. 1985); Wolters Village, Ltd. v. Village Props., Ltd. (In re Village Props., Ltd.), 723 F.2d 441, 444 (5th Cir. 1984). Indeed,

> [w]hen the secured creditor has undertaken affirmative action to protect its right to post-bankruptcy rents, . . . the courts have tended to limit the use to which the rents might be put. For the most part, Debtor in possession or trustee is permitted to use the rents for purposes of maintaining the property, for making real estate tax payments and, if there is a surplus, to make mortgage amortization payments. *These holdings comport with the requirement of adequate protection.*

Saline State Bank v. Mahloch, 834 F.2d 690, 693 n.7 (8th Cir. 1987) (emphasis added); see also Hartsgan v. Pine Lake Village Apt. Co. (In re Pine Lake Village Apt. Co.), 16 B.R. 750 (Bankr. S.D.N.Y. 1982) (holding that despite the absence of a creditor's consent to Debtor's use of post-petition cash collateral, Debtor was authorized to use cash collateral to maintain its apartment property, and that this would ensure that the creditor was adequately protected); In re Carbone Companies, Inc., 395 B.R. 631, 636-637 (Bankr. N.D. Ohio 2008) (authorizing the use of cash collateral and finding that lender was adequately protected where debtor expected to operate at a profit and to generate positive cash flows); In re Franklin Pembroke Venture II, 105 B.R. 276, 278 (Bankr. E.D. Pa. 1989); McCombs Properties VI, Ltd. v. First Texas Sav. Ass'n (In re McCombs Props. VI, Ltd.), 88 B.R. 261 (Bankr. C.D. Cal. 1988); In re Gunnison Center Apartments, LP, 320 B.R. 391, 397-399 (Bankr. D. Colo. 2005) (finding that a secured creditor

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was adequately protected where the cash collateral was utilized to "operate the property in good fashion, pay the expenses of operation and the costs of maintenance to preserve and protect the property, and account for the monies received and the expenses paid").

As exemplified by the Budget, Debtor is solely seeking to utilize the Cash Collateral to maintain its business operations by satisfying its obligations to its vendors and customers, paying necessary operating expenses, and acquiring new inventory to continue sales and generate additional revenue on which Lender will retain its liens. See Exhibit "2." Each expense included within the Budget is a necessary expense to maintain and preserve Debtor's assets and/or operate Debtor, which is the sole means of generating revenue, thereby increasing the value of the estate and providing the resources for Debtor to reorganize. See Omnibus Decl. ¶ 54. Further, in addition to the replacement liens that Lender will acquire on any new inventory or accounts receivable, as such, Debtor should be granted authority by this Court to use its Cash Collateral as such use will enhance, not diminish, the value of the estate and the Collateral.

D. The Significant Equity in the Collateral Adequately Protects Lender's Interest.

"Adequate protection" is not expressly defined in the Code. Section 361, however, details three non-exclusive examples of what may constitute adequate protection, including (1) periodic case payments equivalent to decrease in value, (2) an additional or replacement lien on other property, or (3) other relief that provides the indubitable equivalent. 11 U.S.C. § 361; In re Mellor, 734 F.2d 1396, 1400 (9th Cir. 1984).

Courts have determined that the existence of a sufficient equity cushion may provide adequate protection. See In re BLX Group, Inc., 419 B.R. 457, 470 (citing In re Mellor, 734 F.2d at 1400). The Ninth Circuit has explained regarding an equity cushion:

> 58. [I]t is the classic form of protection for a secured debt justifying the restraint of lien enforcement by a bankruptcy court. In re Curtis, 9 B.R. [110,] 112 [(Bankr. E.D. Pa. 1982)]. In fact, it has been held that the existence of an equity cushion, standing alone, can provide adequate protection. In re San Clemente Estates, 5 B.R. 605, 610 (Bankr.S.D.Cal.1980); In re Tucker, 5 B.R. 180, 182 (Bankr.S.D.N.Y.1980); 2 Collier on Bankruptcy, § 361.02[3] at 361–9; (15th ed.1979). A sufficient equity cushion has been found to exist although not a single mortgage payment had been

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made. In re Curtis, 9 B.R. at 111.

In re Mellor, 734 F.2d at 1400.

. . .

An equity cushion is "the value in the property, above the amount owed to the creditor with a secured claim, that will shield that interest from loss due to any decrease in the value of the property during time the automatic stay remains in effect." In re Mellor, 734 F.2d at 1400 n. 2; In re BLX Group, 419 B.R. at 470. Where an equity cushion is small, and the collateral's value is not rising, courts may determine that a secured creditor is not adequately protected even at early stages of a case. See La Jolla Mortg. Fund v. Ranco El Cajon Assoc., 18 B.R. 283, 288 (Bankr. S.D. Cal. 1982).

Although no absolute benchmarks have been established, and the court retains discretion to fashion relief based on the unique circumstances of the case, courts have commonly found that an equity cushion of approximately 20% may constitute adequate protection. See, e.g., In re Holt, 2010 WL 3294693, at *6 (Bankr. D. Mont. 2010) (citing In re Timbers of Inwood Forest, 793 F.2d 1380, 1387 (5th Cir. 1986), aff'd, 484 U.S. 365, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988); In re Mellor, 734 F.2d at 1401; In re Avila, 311 B.R. 81, 82 (Bankr. N.D. Cal. 2004)). While a sufficient equity cushion could establish adequate protection when the debtor has not made payments on its secured debt prior to the filing of the bankruptcy if the value of the secured collateral is sufficiently stable, see, e.g., In re Rogers Development Corp., 2 B.R. 679, 685 (Bankr. E.D. Va. 1980), courts alternatively have considered the impact of mounting taxes, interest, fees and costs. See, e.g., In re Faires, 34 B.R. 549, 553 (Bankr. W.D. Wash. 1983).

For the avoidance of doubt, courts within the Ninth Circuit have held that the analysis regarding adequate protection in the context of cash collateral pursuant to Section 363 is the same as in the context of stay relief pursuant to Section 362. See, e.g., In re McCombs Properties VI, Ltd., 88 B.R. 261, 266 (Bankr. C.D. Cal. 1988). This expressly includes that an equity cushion may constitute adequate protection in the cash collateral context. See id.; see also In re WRB West Associates Joint Venture, 106 B.R. 215, 219-220 (Bankr. D. Mont. 1989).

The value of the Collateral significantly exceeds the Lender's claim as of the Petition

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Date. In addition to its intellectual property, Debtor's inventory is valued at $6,000,000 at cost and in excess of $25,000,000 when properly sold, and its accounts receivable total $450,000, approximately $390,000 of which Debtor anticipates are collectible. Beyond these assets, Debtor has sought hundreds of millions of dollars of damages in the Crocs Litigation, which is currently expected to go to trial within a year. See Omnibus Decl. ¶¶ 46-47. Debtor also believes, as to the intellectual property and Crocs Litigation, the Collateral will not diminish in value. As to the accounts receivable and inventory, Lender will continue to obtain replacement liens on any new inventory or accounts receivables acquired after the Petition Date pursuant to the Loan Agreement. See id. ¶ 55. As a result, Lender is more than adequately protected and Debtor should be permitted to utilize the cash collateral.

E. The Bankruptcy Code's Policy of Favoring Reorganization Calls for Granting the Motion.

A bankruptcy court, where possible, should resolve issues presented in favor of reorganization. See NLRB v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984) ("[t]he fundamental purpose of reorganization is to prevent a debtor from going into liquidation, with an attendant loss of jobs and possible misuse of economic resources."); United States v. Whiting Pools, Inc., 462 U.S. 198, 203 (1983) ("By permitting reorganization, Congress anticipated that the business would continue to provide jobs, to satisfy creditors' claims, and to produce a return for its owner.

The U.S. Court of Appeals for the Tenth Circuit summarized this principle as follows:

> Because the ultimate benefit to be achieved by a successful reorganization inures to all the creditors of the estate, a fair opportunity must be given to Debtors to achieve that end. Thus, while interests of the secured creditor . . . are of concern to the court, the interests of all the creditors also have bearing upon the question of whether use of cash collateral shall be permitted during the early stages of administration.
>
> The first effort of the court must be to insure that the value of the collateral will be preserved. Yet, prior to confirmation of a plan of reorganization, the test of that protection is not to be the same measurements applied to the treatment of a secured creditor in a proposed plan. In order to encourage Debtors' efforts in a formative period prior to the proposal of a reorganization, the court must be flexible in approving the adequate protection standard.

In re O'Connor, 808 F.2d 1393, 1397 (10th Cir. 1987).

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As such, granting Debtor's request to use Cash Collateral to pay its ordinary course expenses is in keeping with the Bankruptcy Code's general policy favoring reorganizations, particularly as such relief will not result in the diminution of Lender's Collateral.

V.
NOTICE AND REQUEST FOR WAIVER OF THE STAY

Bankruptcy Rule 6004(h) provides that an "order authorizing the use, sale, or lease of property . . . is stayed until the expiration of 14 days after entry of the order, unless the court orders otherwise." In view of the urgency of the relief requested herein and the risk to Debtor's operations if Debtor cannot use Cash Collateral, a fourteen-day stay of the relief sought herein is impractical. Accordingly, Debtor requests that this Court waive the stay under Bankruptcy Rule 6004(h) and provide in the order granting the relief sought herein that such order shall be effective immediately.

27. Debtor shall serve notice of this Motion on the following: (i) the Office of the United States Trustee for the District of Nevada; (ii) the holders of the twenty (20) largest unsecured claims against Debtor, or any official committee of unsecured creditors, if one is appointed pursuant to Section 1102 of the Bankruptcy Code; (iii) any other committee that is appointed pursuant to Section 1102 of the Bankruptcy Code; (iv) Lender; and (v) other interested parties as listed on the service list, and any entity which files and serves on Debtor a request for special notice prior to the filing of this Motion.

28. Given the emergency nature of the relief requested herein, and the potential disruption to Debtor's business that will ensue if such relief requested is not granted, Debtor submits that no further notice need be given prior to granting the relief sought herein.

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VI.
CONCLUSION

WHEREFORE, Debtor requests that the Court grant the Motion and enter the Interim Order, a proposed copy of which is attached hereto as Exhibit "1," and for such other and further relief as this Court deems just and proper.

DATED this 1st day of February, 2018.

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