

JURISDICTION

This Court has jurisdiction over this Motion under 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2). Venue of this proceeding and this Motion in this district is proper under 28 U.S.C. §§ 1408 and 1409. The statutory bases for the relief requested herein are sections 105(a), 363, 507(a)(4)-(5), 1107(a) and 1108 of title 11 of the United States Code, 11 U.S.C. §§ 101-1532 (the "Bankruptcy Code"), and Rule 6003 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

GENERAL BACKGROUND

1. On November 16, 2009 (the "Petition Date"), the Debtor filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code.

2. The Debtor continues to operate its business and manage its properties as a debtor in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. No trustee, examiner or official committee of unsecured creditors has been appointed in this chapter 11 case.

A. Overview of Debtor's Businesses and Performance

3. The Debtor was incorporated in 1996. Through its subsidiary Islensk erfðagreining ehf ("ehf"), an Icelandic private limited company, it is engaged in gene discovery with the goal of bringing to market DNA-based reference laboratory tests and consumer genome analysis services to assess individual risk of common diseases. ehf also provides genomics services to third parties. In 2002, the Debtor acquired MediChem Life Sciences, Inc. ("MediChem"). Through MediChem's subsidiaries, deCODE Chemistry, Inc. ("Chemistry"), deCODE Biostructures, Inc. ("Biostructures") and Emerald BioSystems, Inc. ("Emerald"), the Debtor expanded its business to include the discovery and commercialization of novel therapeutics designed against certain targets identified in its population based gene discovery work. In addition, these subsidiaries offer drug discovery services and products to third-party

customers. In September 2009, the Debtor terminated operations of Chemistry and, in November 2009, it sold Biostructures and Emerald to an unrelated third party.

4. The Debtor has developed and is marketing six DNA-based diagnostic tests for assessing individual risk of disease. It also operates deCODEme, a consumer genetics analysis service. The Debtor's lead drug development programs include DG041 for the prevention of arterial thrombosis, G051 and DG031 for the prevention of heart attack and DG071 for Alzheimer's and other cognitive disorders, the intellectual property underlying which is held substantially by ehf. These compounds are in clinical development and the Debtor has been seeking licensing or other collaborative arrangements for ehf to advance the development of these programs or, alternatively, an outright sale of one or more of the compounds.

5. Since its inception, the Debtor has devoted its resources primarily to research and development. It incurred a net loss of \$80.9 million, \$95.5 million and \$85.5 million in 2008, 2007 and 2006, respectively, and had an accumulated deficit of \$712.2 million as of December 31, 2008. Indeed, the Debtor has never generated a profit and has not generated significant revenues except for payments received in connection with its research and development collaborations with pharmaceutical companies, from contract services, the sale of Emerald products and instruments and under grants. The Debtor's research and development expenditures and general and administrative costs have exceeded its revenue to date. Moreover, the Debtor believes that significant additional amounts will be required to develop its diagnostics and deCODEme™ products and services, fund research and development and undertake product development (including drug development and related clinical trials). The Debtor does not expect to receive material revenues from commercial sales of products developed using its technology in the near term and expects to incur net losses for several years.

6. The Debtor's corporate headquarters and ehf's management staff and gene discovery business are located in Reykjavik, Iceland in an approximately 150,000 square-foot building which is leased by ehf under a 15-year operating lease expiring in 2020. The lease is in payment default because rent was not paid for October 2009. The landlord has not retaken possession of the premises but has obtained from the Reykjavik District Court a temporary restraining order to prevent ehf from transferring its Icelandic and US patent rights in an apparent attempt to recover amounts allegedly due and owing under the lease. The Debtor and ehf continue to occupy the premises and conduct their business activities therefrom. The facilities of Chemistry are located in Woodridge, Illinois in a 103,000 square-foot facility leased under a 17-year lease expiring in 2024. The lease is in default as Chemistry was unable to and did not pay rent for the month of September 2009 or thereafter. As a consequence, the landlord has terminated the lease and, the Debtor believes, drawn on a letter of credit, which had been arranged and secured by \$5 million of cash collateral. The Debtor was a lease guarantor and, as such, posted the cash collateral.

B. The Debtor's Capital and Debt Structure

(i) Prepetition Debt

7. In April 2004 and November 2006, the Debtor issued an aggregate of \$230 million of unsecured 3.5% Senior Convertible Notes due April 15, 2011 (the "Notes") pursuant to Indentures dated April 14, 2004 and November 17, 2006. The Bank of New York is the indenture trustee for the Notes. A semi-annual payment of interest on the Notes was due and payable on or about October 15, 2009, but was not paid prior to the expiration of a 30-day grace period that ran on November 16, 2009. The Debtor did not have the financial wherewithal to make and did not make such interest payment, including by borrowing under either the Bridge Loan or the DIP Loan (each as described below).

(ii) Bridge Loan

8. Additionally, on September 11, 2009, the Debtor entered into a bridge loan facility (the "Bridge Loan") with Saga Investments LLC ("Saga"). The Debtor and its subsidiaries, MediChem and Biostructures (collectively, the "Prepetition Borrowers"), entered into that certain Secured Promissory Note dated as of September 11, 2009 (the "Original Note"), whereby Saga agreed to provide the Prepetition Borrowers with a secured loan in the original principal amount of \$700,000 (the "Existing Credit Facilities"). The other direct and indirect subsidiaries of the Debtor (the "Guarantors") guaranteed the Prepetition Borrowers' obligations under the Original Note, as it may be amended from time to time. Biostructures and Emerald were released from their obligations in connection with the Note at the time of their sale. The Original Note was subsequently amended and restated on nine occasions to increase the principal amount of the Original Note to \$5.424 million.² Interest under the Amended and Restated Note is payable in arrears on the first day of each month at a rate of 8% by increasing the then aggregate principal amount of the loan outstanding on such date. Moreover, the outstanding obligations under the Amended and Restated Note are secured by liens on substantially all of the Prepetition Borrowers' and Guarantors' assets. As of the Petition Date, the aggregate amount outstanding under the Amended and Restated Note is approximately \$3,055,262.20.

(iii) Capital Structure

9. As of the Petition Date, the Debtor has approximately 61.4 million shares of common stock outstanding.

² The Tenth Amended and Restated Secure Promissory Note, dated November 12, 2009, shall hereinafter be referred to as the "Amended and Restated Note."

C. Events Leading to the Filing of the Chapter 11 Case

(i) The Debtor's Liquidity Needs

10. As described above, the Debtor has not generated material revenue and needs to obtain financing in order to continue operations. During 2008, the Debtor sought to obtain financing through collaborations and licensing arrangements, public or private equity offerings, and other forms of financing without sufficient success to sustain its operations. The Debtor's situation was worsened by the global economic crisis and its effect on capital markets and by the illiquidity and decline in value of approximately \$30 million of auction-rate securities ("ARS") in which Lehman Brothers, Inc. had invested a portion of the Debtor's cash resources in violation of the Debtor's cash management instructions. It also sought, without success, to restructure the Notes.

(ii) Marketing Efforts

11. In the summer of 2008, the Debtor began a review of its long-term business strategy and in mid-August 2008 engaged the Stanford Group Company ("SGC") as financial advisor to, among other things, advise and assist it in evaluating strategic alternatives and identifying buyers and partners for business units, programs and intellectual property and pursue possible advantageous transactions and relationships. SGC and management of the Debtor contacted, and discussed or negotiated with, numerous potential partners and buyers for the Debtor's various business units and assets, as well as with large holders of the Notes. After SCG collapsed in February 2009 for reasons unrelated to this case, management, under the oversight and direction of a special committee of the board of directors (the "Special Committee") that was established in October 2008, continued such efforts but was unable to consummate a material transaction or restructure the Notes. The Debtor was able to meet some of its short-term liquidity needs through the sale of rights to a diagnostics test to an industry player and the sale

of ARS to an Icelandic bank, but the net proceeds only provided interim funding, which was soon exhausted. In the Winter and Spring of 2009, the Debtor's long-term economic prospects worsened considerably as operating costs continued significantly to surpass cash flow.

12. Starting in late March 2009, the Debtor, through management and a representative of the Special Committee, commenced discussions with investors in Saga about the possibility of a transaction to restructure the Notes, obtain funding from such investors and continue the Debtor's gene discovery business. The Debtor continued its discussions with such investors, as well as other contacted parties, into the summer of 2009. In August 2009, investors in Saga indicated a willingness to pursue a sale transaction under section 363 of the Bankruptcy Code whereby Saga would acquire the capital stock of ehf, any assets related to ehf's business held by the Debtor or its non-Debtor U.S. subsidiaries and some or all of the drug compounds.

13. As discussed above, on September 11, 2009, Saga and the Debtor entered into the Original Note implementing the Bridge Loan. At about such time, the Special Committee engaged restructuring professionals from a major accounting firm to advise and assist the Debtor in evaluating the proposed transaction with Saga, as well as any alternative transactions that may be available, and to assist the Debtor in navigating through the pre-bankruptcy and bankruptcy processes. On September 23, 2009, the parties entered into a nonbinding term sheet (the "Term Sheet") that contemplated a proposed sale transaction, an amendment and extension of the secured bridge loan and the provision of debtor in possession secured financing, with Saga serving as the DIP lender, in connection with a chapter 11 filing. The Term Sheet also contained a binding exclusive dealings provision that terminated on October 8, 2009. The Debtor and Saga proceeded to negotiate a definitive sale transaction agreement, but did not enter into such an agreement until November 16, 2009.

14. Following the expiration of the exclusive dealings period, the Debtor, through the Special Committee and certain members of management, with the assistance of its restructuring professionals, identified a list of strategic and financial parties (in addition to Saga) that it viewed as potential purchasers of the Debtors' assets (either as an alternative to Saga or as a competing bidder through an auction process). Over a period of several weeks until the present, contacts have been made and discussions have been held in some cases with approximately 15 of such potential transactional parties but without an alternative transaction being entered into.

(iii) The Stalking Horse APA

15. The Debtor's efforts culminated in the negotiation and execution of an asset purchase agreement with Saga (the "Stalking Horse APA") for the sale of (a) all of the equity interests of ehf and (b) all intellectual property rights and other tangible and intangible assets of the Debtor and its direct and indirect U.S. subsidiaries related to (i) the business conducted by ehf and its subsidiary or (ii) the drug compounds that the Debtor has historically designated as DG041, DG051 and DG071. The Debtor has also entered into a debtor in possession financing credit agreement (the "DIP Credit Agreement") with Saga whereby Saga, as lender, will provide a loan in an aggregate amount not to exceed \$11,117,928 in accordance with an agreed-upon budget. The Debtor believes that the DIP Credit Agreement provides the Debtor with sufficient liquidity to commence and consummate a sale process under section 363 of the Bankruptcy Code that will enable the Debtor to maximize value for creditors and other interested parties. The Stalking Horse APA will serve as the basis for this Court supervised sale process that will involve an auction designed to maximize the value of the Debtor's estate for the benefit of its economic stakeholders. Following consummation of the proposed sale, the liquidation of the Debtor and its subsidiaries will be completed pursuant to a plan of liquidation for the benefit of the Debtor's economic stakeholders.

SPECIFIC BACKGROUND

A. The Debtor's Workforce

16. As set forth in the First Day Affidavit, the Debtor currently staffs approximately nineteen (19) staff members (the "Staff Members") through a third-party staffing and services agreement (the "Agreement") with TriNet Employer Group, Inc. ("TriNet") (as described in detail below) at its U.S. and Icelandic locations. The Debtor's workforce consists of eighteen (18) salaried Staff Members and one (1) hourly Staff Member. None of the Debtor's Staff Members are covered by a collective bargaining agreement. The Debtor's full-time Staff Members are financial professionals, investor relations professionals, scientific researchers, management and sales staff.

B. TriNet Agreement

17. As noted above, to administer its workforce, the Debtor is party to the Agreement with TriNet. A copy of the Agreement is attached hereto as Exhibit B. Pursuant to the terms of the Agreement, each Staff Member (as defined below) is actually an employee of TriNet, but is staffed with the Debtor. TriNet then administers the employment relationship with each Staff Member by, among other things, paying wages and withholding and remitting payroll-related taxes and employee benefits.³

18. All disbursements made by TriNet on account of its responsibilities under the Agreement are pre-funded by the Debtor. In other words, the Debtor remits all Staff Member-related disbursements to TriNet prior to TriNet making any payments to the Staff Members. Once TriNet has received funds from the Debtor, it makes payments to the Staff Members under

³ While TriNet administers the employment relationship, the Debtor retains responsibility for the workplace and all activities therein, including, but not limited to, evaluating job performance, establishing work schedules, ensuring compliance with regulatory requirements relating to leave from work, making hiring and termination decisions and instructing each Staff Member in the safe performance of their job.

the terms of the Agreement. Should the Debtor fail to pre-fund TriNet's obligations, TriNet is holding a cash deposit of approximately \$103,000.00 to cure any arrearage. As of the Petition Date, there is a *de minimis* prepetition obligation owing to TriNet in the amount of \$14,452.53 (which represents the Staff Member wages incurred on November 16, 2009). Specifically, the Debtor is one (1) day behind on its Staff Member wage pre-payments to TriNet. Accordingly the Debtor is requesting authority to pay up to \$14,452.53 to TriNet in respect of such Staff Member wage obligations.

19. There may also be outstanding prepetition amounts owed to employees for Vacation Time and Sick/Personal Leave (as discussed below) that are not pre-funded through TriNet. As described below, in the ordinary course of business, the Debtor cashes out accrued Vacation Time to Staff Members at the time of their termination. Given that the Debtor does not know if or when Staff Members will be terminated, accrued prepetition amounts exist with respect to Staff Member Vacation Time obligations.

20. Moreover, the Agreement characterizes the Vacation Time and Sick/Personal Leave obligations as obligations belonging solely to the Debtor. Section 5(q)(ii) provides that

[a]ny wages and benefits in excess of minimum wage, including without limitation bonuses, commissions or other non-regular wages, are considered discretionary, voluntarily elected by [the Debtor] without obligation by TriNet, and the sole responsibility of [the Debtor], because each represents compensation for the economic value of the labor, service or intellectual property provided by Employees exclusively to [the Debtor]. TriNet will only process such discretionary wages if [the Debtor] has duly authorized and funded the discretionary wages prior to payment....

Section 5(q)(v) goes on to further provide that "the requirements of this [Section 5(q)] shall apply regardless of [the Debtor's] financial condition." Thus, the Debtor believes that its Vacation Time obligations and Sick/Personal Leave obligations are governed by these two

sections of the Agreement and are direct obligations of the Debtor which result in prepetition accruals that require Bankruptcy Court authority to pay and/or honor.

C. Vacation and Sick/Personal Leave Obligations

21. In the ordinary course of its business, the Debtor provides certain Vacation Time and Sick/Personal Leave benefits to both its full-time and part-time⁴ Staff Members. Temporary Staff Members and Independent Contractors are not eligible to receive Vacation Time or Sick/Personal Leave benefits and consequently are not eligible to accrue, earn or use Vacation Time or Sick/Personal Leave benefits.

(i) *Vacation Time*

22. All Staff Members are eligible to accrue Vacation Time. Typically, each Staff Member can accrue up to three weeks of Vacation Time per year; however, certain Staff Members may be eligible to accrue more than three (3) weeks based on the terms of their respective agreements with the Debtor. A Staff Member's Vacation Time begins accruing and can be used immediately upon being staffed with the Debtor.⁵ Vacation Time stops accruing once a Staff Member has accrued Vacation Time in an amount equal to their single year cap which, as noted above, is typically three (3) weeks.

⁴ Part-time Staff Members are eligible to accrue Vacation Time and Sick/Personal Leave on a pro-rated basis as compared to full-time Staff Members. Part-time Staff Members' Vacation Time and Sick/Personal Leave is pro-rated by calculating the ratio of part-time hours worked divided by full-time hours, and multiplying that ratio by the accrual rate. The Debtor currently has no part-time Staff Members.

⁵ In addition to Vacation Time, all Staff Members are eligible to receive certain paid holidays each year. All Staff Members receive the following days as paid holidays each year: New Year's Day, Memorial Day, Independence Day, Labor Day, Thanksgiving Day, the day after Thanksgiving, Christmas Day and New Year's Eve. All Staff Members are also eligible to receive two (2) floating holidays. Floating holidays must be scheduled in advance with the Staff Member's manager and are subject to manager approval. The floating holidays may be used for time off related to a Staff Member's birthday, anniversary or a holiday not currently observed by the Debtor. Floating holidays are not carried over from one year to the next, and must be used within the calendar year.

23. All Staff Members eligible to accrue Vacation Time may carry twenty-four (24) hours of unused Vacation Time forward to be used in the following year. Any unused Vacation Time above the twenty-four (24) hour carry-over is forfeited at the end of the year absent management approval based on special circumstances.⁶

24. When a Staff Member elects to take Vacation Time, the Debtor pays such Staff Member his or her regular salaried rate. If a Staff Member subsequently leaves the Debtor's employ, whether voluntarily or involuntarily, his or her Vacation Time accrual will be calculated and cashed out in a final paycheck. The Debtor estimates that, as of the Petition Date, its obligation to Staff Members for earned, unused Vacation Time is approximately \$279,305.01. However, the Debtor is only seeking authority to honor and/or pay Vacation Time obligations to its Staff Members in the ordinary course of its business up to the statutory cap of \$10,950.00 per Staff Member. Thus, in the aggregate, the Debtor is seeking authority to pay up to \$123,885.03.

(ii) Sick and Personal Leave

25. In addition to the Vacation Time, all Staff Members are eligible to accrue a total of six (6) days per year that may be used for Sick/Personal Leave. The Sick/Personal Leave accrues in the same way as Vacation Time and stops accruing once the Staff Member has six (6) days of Sick/Personal Leave. Each day of Sick/Personal Leave may be taken by the Staff Member at any time over the course of a year. Unlike Vacation Time, however, Sick/Personal Leave cannot be carried forward to the next year. Moreover, in the event that the Staff Member leaves the Debtor's staff, whether voluntarily or involuntarily, his or her remaining Sick/Personal

⁶ Staff Members seeking to carry over more than twenty-four (24) hours of Vacation Time per year must seek approval of their immediate supervisor to do so based on special or unique facts and circumstances. If the requesting Staff Member's immediate supervisor approves of the request, the Staff Member may carry over additional hours of Vacation Time.

Leave is not cashed out in a final paycheck. As such, the Debtor is only seeking authority to honor accrued prepetition Sick/Personal Leave and will not make any cash distributions on account of the Sick/Personal Leave.

26. All of the Staff Members are crucial to the Debtor's ability to successfully navigate the chapter 11 process. Should the Debtor fail to honor accrued prepetition Sick/Personal Leave or renege on its obligations and fail to honor and/or pay amounts owed in connection with accrued prepetition Vacation Time, many Staff Members could become disillusioned or even leave the Debtor for other opportunities. Therefore, to maintain morale and stability in the Debtor's workforce during this critical time, the Debtor, by this Motion, seeks authority, to be exercised in its sole discretion, to honor and/or pay certain Vacation Time obligations, and to honor certain Sick/Personal Leave obligations. In addition, the Debtor requests the right to modify, change and/or discontinue any of the Vacation Time and Sick/Personal Leave benefits in the ordinary course of business during this chapter 11 case in its sole discretion without the need for further Court approval.

RELIEF REQUESTED

27. By this Motion, the Debtor seeks entry of an order, granting it authority to (i) pay certain prepetition Staff Member wage obligations, (ii) honor and/or pay certain obligations related to Vacation Time and (iii) honor certain Sick/Personal Leave obligations in the ordinary course of business during this chapter 11 case in its sole discretion without the need for further Court approval.

28. Moreover, the Debtor requests that the Court authorize and direct financial institutions to receive, process, honor and pay to all checks issued by the Debtor that are presented for payment by TriNet and all electronic payment requests issued by the Debtor that

are submitted by TriNet relating to the foregoing, whether such checks were presented or electronic requests were submitted prior to or after the Petition Date. The Debtor also requests that the Court authorize applicable financial institutions to rely on the Debtor's designation of any particular check or electronic payment request as appropriate pursuant to this Motion.

BASIS FOR RELIEF

A. Ample Authority Exists to Support Allowing the Debtor to Pay Staff Member Wage Obligations, Pay Vacation Time Obligations and Honor Sick/Personal Leave

29. Courts generally acknowledge that it is appropriate to authorize the payment (or other special treatment) of prepetition obligations in appropriate circumstances.⁷ In authorizing payments of certain prepetition obligations, courts rely on several legal theories rooted in sections 1107(a), 1108, 363(b) and 105(a) of the Bankruptcy Code.

30. Pursuant to sections 1107(a) and 1108 of the Bankruptcy Code, a debtor in possession is a fiduciary "holding the bankruptcy estate and operating the business for the benefit of its creditors and (if the value justifies) equity owners." In re CoServ, L.L.C., 273 B.R. 487, 497 (Bankr. N.D. Tex. 2002). Implicit in the fiduciary duties of any debtor in possession is the obligation to "protect and preserve the estate, including an operating business's going-concern value." Id. Some courts have noted that there are instances in which a debtor can fulfill this fiduciary duty "only . . . by the preplan satisfaction of a prepetition claim." Id. The CoServ court specifically noted that the satisfaction of prepetition claims would be a valid exercise of a debtor's fiduciary duty when the payment "is the only means to effect a substantial enhancement of the estate." Id.

⁷ See, e.g., In re Wickes Holdings, LLC, Case No. 08-10212 (KJC) (Bankr. D. Del. Feb. 5, 2008); In re Tweeter Home Entm't Group, Inc., Case No. 07-10787 (PJW) (Bankr. D. Del. June 13, 2007); In re Pope & Talbot, Inc., Case No. 07-11738 (CSS) (Bankr. D. Del. Nov. 21, 2007); In re Hancock Fabrics, Inc., Case No. 07-10353 (BLS) (Bankr. D. Del. Mar. 22, 2007).

31. Consistent with a debtor's fiduciary duties, courts have also authorized payment of prepetition obligations under section 363(b) of the Bankruptcy Code where a sound business purpose exists for doing so. See, e.g., In re Ionosphere Clubs, Inc., 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989) (finding that a sound business justification existed to justify payment of prepetition wages); see also Armstrong World Indus., Inc. v. James A. Phillips, Inc., (In re James A. Phillips, Inc.), 29 B.R. 391, 397 (S.D.N.Y. 1983) (relying on section 363 to allow contractor to pay prepetition claims of suppliers who were potential lien claimants because the payments were necessary for general contractors to release funds owed to debtors).

32. In addition, the Court may authorize payment of prepetition claims in appropriate circumstances based on section 105(a) of the Bankruptcy Code. Section 105(a), which codifies the inherent equitable powers of the bankruptcy court, empowers the bankruptcy court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a). Under section 105(a), courts may permit preplan payments of prepetition obligations when essential to the continued operation of the debtor's business. Specifically, the Court may use its power under section 105(a) to authorize payment of prepetition obligations pursuant to the "necessity of payment" rule (also referred to as the "doctrine of necessity").

33. The "doctrine of necessity" or the "necessity of payment" rule originated in railway cases and was first articulated by the United States Supreme Court in Miltenberger v. Logansport, C.&S.W.R. Co., 106 U.S. 286 (1882). The doctrine was expanded to non-railroad debtors in the mid-century. See Dudley v. Mealey, 147 F.2d 268, 271 (2d Cir. 1945) (holding, in a hotel reorganization case, that the court was not "helpless" to apply the rule to supply creditors of non-railroad debtors where the alternative was the cessation of operations).

34. The United States Court of Appeals for the Third Circuit recognized the “necessity of payment” doctrine in In re Lehigh & New England Ry. Co., 657 F.2d 570, 581 (3d Cir. 1981). The Third Circuit held that a court could authorize the payment of prepetition claims if such payment was essential to the continued operation of the debtor. Id. (stating that court may authorize payment of prepetition claims when there “is the possibility that the creditor will employ an immediate economic sanction, failing such payment”); see also In re Penn Cent. Transp. Co., 467 F.2d 100, 102 n.1 (3d Cir. 1972) (holding that the necessity of payment doctrine permits “immediate payment of claims of creditors where those creditors will not supply services or material essential to the conduct of the business until their pre-reorganization claims have been paid”); In re Just for Feet, Inc., 242 B.R. 821, 824-845 (Bankr. D. Del. 1999) (noting that, in the Third Circuit, debtors may pay prepetition claims that are essential to continued operation of business); In re Columbia Gas Sys., Inc., 171 B.R. 189, 191-92 (Bankr. D. Del. 1994) (same).

35. Today, the rationale for the necessity of payment rule—the rehabilitation of a debtor in reorganization cases—is “the paramount policy and goal of Chapter 11.” In re Ionosphere Clubs, Inc., 98 B.R. at 176; see also Just For Feet, 242 B.R. at 826 (finding that payment of prepetition claims to certain trade vendors was “essential to the survival of the debtor during the chapter 11 reorganization”); In re Quality Interiors, Inc., 127 B.R. 391, 396 (Bankr. N.D. Ohio 1991) (“[P]ayment by a debtor-in-possession of pre-petition claims outside of a confirmed plan of reorganization is generally prohibited by the Bankruptcy Code,” but “[a] general practice has developed . . . where bankruptcy courts permit the payment of certain pre-petition claims, pursuant to 11 U.S.C. § 105, where the debtor will be unable to reorganize without such payment.”); In re Eagle-Picher Indus., Inc., 124 B.R. 1021, 1023 (Bankr. S.D. Ohio

1991) (approving payment of prepetition unsecured claims of tool makers as “necessary to avert a serious threat to the Chapter 11 process”); Burchinal v. Cent. Wash. Bank (In re Adams Apple, Inc.), 829 F.2d 1484, 1490 (9th Cir. 1987) (recognizing that allowance of “unequal treatment of pre-petition debts when necessary for rehabilitation” is appropriate); Mich. Bureau of Workers’ Disability Comp. v. Chateaugay Corp. (In re Chateaugay Corp.), 80 B.R. 279, 287 (S.D.N.Y. 1987) (authorizing payment of prepetition workers’ compensation claims on grounds that the fundamental purpose of reorganization and equity powers of bankruptcy courts “is to create a flexible mechanism that will permit the greatest likelihood of survival of the debtor and payment of creditors in full or at least proportionately”); 3 COLLIER ON BANKRUPTCY, 105.04[5][a] (15th ed. rev. 2004) (discussing cases in which courts have relied on the “doctrine of necessity” or the “necessity of payment” rule to pay prepetition claims immediately).

36. Courts also have permitted postpetition payment of prepetition claims pursuant to section 105(a) in other situations, such as if nonpayment of a prepetition obligation would trigger a withholding of goods or services essential to the debtors’ business reorganization plan. See In re UNR Indus., 143 B.R. 516, 520 (Bankr. N.D. Ill. 1992) (permitting the debtor to pay prepetition claims of suppliers or employees whose continued cooperation is essential to the debtors’ successful reorganization); Ionosphere Clubs, 98 B.R. at 167-77 (finding that section 105 empowers bankruptcy courts to authorize payment of prepetition debt when such payment is needed to facilitate the rehabilitation of the debtor).

37. This flexible approach is particularly critical where a prepetition creditor provides vital goods or services to a debtor that would be unavailable if the debtors did not satisfy their prepetition obligations. In In re Structurlite Plastics Corp., 86 B.R. 922, 931 (Bankr. S.D. Ohio 1988), the bankruptcy court stated that “a bankruptcy court may exercise its equity powers under

§ 105(a) [of the Bankruptcy Code] to authorize payment of prepetition claims where such payment is necessary ‘to permit the greatest likelihood of survival of the debtors and payment of creditors in full or at least proportionately.’” *Id.* The court explained that “a *per se* rule proscribing the payment of prepetition indebtedness may well be too inflexible to permit the effectuation of the rehabilitative purposes of the Code.” *Id.* at 932.

B. Sufficient Cause Exists to Authorize the Debtor to Pay Staff Member Wage Obligations, Pay Vacation Time Obligations and Honor Sick/Personal Leave

38. By this Motion, the Debtor seeks authority pay TriNet \$14,452.53 on account of certain prepetition Staff Member wage obligations that accrued prepetition.⁸ The Debtor also seeks authority to pay certain Vacation Time up to the \$10,950 cap under sections 507(a)(4) and 507(a)(5) of the Bankruptcy Code. The Debtor is not seeking authority to honor and/or pay any amounts to Staff Members in excess of the \$10,950 cap under sections 507(a)(4) and 507(a)(5) of the Bankruptcy Code pursuant to this Motion. Finally, the Debtor seeks authority to honor Sick/Personal Leave obligations. Even though the Debtor is not seeking to pay any amounts with regard to the Sick/Personal Leave obligations, the same rational -- preserving Staff Member loyalty necessary to navigate the chapter 11 process -- applies with equal force to both making payments in respect of Vacation Time obligations as well as honoring Sick/Personal leave.

39. As discussed above, there are several provisions of the Bankruptcy Code that authorize a debtor to pay and/or honor prepetition obligations if the circumstances warrant and that therefore support the relief requested in this Motion. Such payments are justified by the critical nature of the services provided by such Staff Members. If the Debtor is unable to satisfy

⁸ To the extent that the Court believes such payment to TriNet on account of the Debtor’s prepetition Staff Member wage obligations is subject to the \$10,950 cap provided for in sections 507(a)(4) and 507(a)(5) of the Bankruptcy Code, the Debtor submits that no Staff Member will receive any payment in excess of such cap.

such obligations, Staff Member morale and loyalty will be jeopardized at a time when their support is critical.

40. If the Debtor does not pay TriNet on account of its Staff Member wage obligations, honor and/or make payments on account of the Vacation Time obligations and honor its Sick/Personal Leave obligations, the Debtor's Staff Members may seek alternative employment opportunities. Such a development would deplete the Debtor's workforce, hindering the Debtor's ability to meet its business obligations and likely diminishing creditor confidence in the Debtor. Moreover, the loss of valuable Staff Members and the recruiting efforts that would be required to replace such Staff Members would be a massive and costly distraction at a time when the Debtor should be focusing on stabilizing its operations. Accordingly, the Debtor must pursue all reasonable measures to retain its Staff Members by, among other things, paying TriNet amounts owed in connection with its Staff Member Wage obligations, paying and/or honoring its Vacation Time obligations and honoring Sick/Personal Leave obligations.

41. Moreover, any claims based on the Vacation Time that the Debtor seeks to pay and/or honor would arguably be entitled to priority treatment up to \$10,950 for each individual under sections 507(a)(4) and 507(a)(5) of the Bankruptcy Code. As priority claims, the Debtor is required to pay these claims in full to confirm a chapter 11 plan. See U.S.C. § 1129(a)(9)(B) (requiring payment of certain allowed unsecured claims for (a) wages, salaries or commissions, including vacation, and sick leave pay earned by an individual, and (b) contributions to an employee benefit plan). Thus, granting the relief sought herein would only cause such Staff Member claims to be paid at the outset of this chapter 11 cases rather than waiting until the confirmation of any potential plan in this chapter 11 case, to the extent that they constitute

priority claims. For all of the foregoing reasons, honoring and/or paying the Vacation Time obligations and Sick/Personal Leave obligations will benefit the estate and its creditors by allowing the Debtor's business operations to continue without interruption.⁹

42. The importance of a debtor's employees to its operations has been repeatedly recognized by courts in this district and other jurisdictions in granting relief similar to the relief requested herein.¹⁰

C. Cause Exists to Authorize the Debtor's Financial Institutions to Honor Checks and Electronic Fund Transfers Made in Respect of Vacation Time Payments

43. The Debtor represents it has sufficient availability of funds to pay the amounts described herein in the ordinary course of business by virtue of cash reserves, expected cash flows from ongoing business operations and anticipated access to debtor-in-possession financing. Also, under the Debtor's existing cash management system, the Debtor represents that checks or wire transfer requests can be readily identified as relating to an authorized payment to TriNet in respect of the Vacation Time obligations. Accordingly, the Debtor believes that checks or wire transfer requests, other than those relating to authorized payments to TriNet, will not be honored

⁹ Critically, the Debtor does not at this time seek to assume any executory contracts or obligations, and the Motion should not be deemed to be an assumption or adoption of any Staff Member agreements or policies. Rather, the Debtor merely seeks to take steps that it believes is necessary to retain its existing workforce and to maximize the value of the bankruptcy estate. Also, the Debtor will retain the discretion not to make the payments contemplated by the Motion for particular Staff Members, and nothing in the Motion shall, in and of itself, confer upon any Staff Members or other parties an entitlement to administrative priority or other preferences in distribution from the Debtor's estate.

¹⁰ See, e.g., In re Filene's Basement, Inc., Case No. 09-11525 (MFW) (Bankr. D. Del. May 5, 2009); In re Abitibowater Inc., Case No. 09-11296 (KJC) (Bankr. D. Del. Apr. 17, 2009); In re The Fairchild Corporation, Case No. 09-10899 (CSS) (Bankr. D. Del. Apr. 15, 2009) (final order); In re Sportsman's Warehouse, Inc., Case No. 09-10990 (CSS) (Bankr. D. Del. Mar. 23, 2009); In re Masonite Corporation, Case No. 09-10844 (PJW) (Bankr. D. Del. Apr. 14, 2009) (final order); In re Robbins Bros. Corporation, Case No. 09-10708 (PJW) (Bankr. D. Del. Mar. 5, 2009); In re Nortel Networks Inc., Case No. 09-10138 (KG) (Bankr. D. Del. Jan. 15, 2009); In re Motor Coach Industries International, Inc., Case No. 08-12136 (BLS) (Bankr. D. Del. Oct. 7, 2008) (final order); In re Linens Holding Co., Case No. 08-10832 (CSS) (Bankr. D. Del. May 2, 2008); In re Wickes Holdings, LLC, Case No. 08-10212 (KJC) (Bankr. D. Del. Feb. 5, 2008); In re Pope & Talbot, Inc., Case No. 07-11738 (CSS) (Bankr. D. Del. Nov. 21, 2007); In re Delta Financial Corp., Case No. 07-11880 (CSS) (Bankr. D. Del. Dec. 19, 2007); In re Tweeter Home Entm't Group, Inc., Case No. 07-10787 (PJW) (Bankr. D. Del. June 13, 2007).

inadvertently and that the Court should authorize all applicable financial institutions (collectively, the “Cash Management Banks”), when requested by the Debtor, to receive, process, honor and pay any and all checks issued by the Debtor that are presented for payment by TriNet or wire transfer requests issued by the Debtor that are submitted by TriNet in respect of the Vacation Time obligations.

44. For all of the foregoing reasons, the Debtor believes that granting the relief requested herein is appropriate and in the best interests of all parties in interest.

D. Failure to Honor Prepetition Staff Member Wages Obligations, Vacation Time Obligations and Sick/Personal Leave Obligations Within 20 Days of the Petition Date Would Cause Immediate and Irreparable Harm

45. Pursuant to the recently revised Rule 6003 of the Bankruptcy Rules, the Court may grant relief regarding a motion to pay all or part of a prepetition claim within 20 days after the Petition Date if the relief is necessary to avoid immediate and irreparable harm.

46. As described above, the Debtor’s Staff Members are integral to the Debtor’s operations. Failure to satisfy obligations with respect to its Staff Member wage payments to TriNet, Vacation Time obligations and Sick/Personal Leave obligations in the ordinary course of business during the first 20 days of this chapter 11 case will jeopardize their loyalty and trust, causing Staff Members to leave the Debtor’s employ and severely disrupting the Debtor’s operations at this critical juncture. Accordingly, the Debtor submits that it has satisfied the requirements of Bankruptcy Rule 6003 to support immediate payment of its Staff Member wage obligations to TriNet, immediate payment and/or honoring of its Vacation Time obligations and immediate honoring of its Sick/Personal Leave obligations.

BANKRUPTCY RULE 6003 COMPLIANCE

47. The Debtor further submits that because the relief requested in this Motion is necessary to avoid immediate and irreparable harm to the Debtor for the reasons set forth herein, Bankruptcy Rule 6003 has been satisfied.

REQUEST FOR WAIVER OF STAY

48. The Debtor further seeks a waiver of any stay of the effectiveness of the order approving this Motion pursuant to Rule 6004(h) of the Bankruptcy Rules or otherwise. As set forth above, the immediate honoring and/or payment of Vacation Time obligations is essential to prevent potentially irreparable damage to the Debtor's operations, value and ability to navigate the chapter 11 process. The Debtor further requests that any stay imposed by Rule 6004(h) or otherwise be waived with respect to honoring Sick/Personal Leave obligations for the same reasons. Accordingly, the Debtor submits that ample cause exists to justify a waiver of any stay imposed by Rule 6004(h), to the extent it applies, or otherwise.

DEBTOR'S RESERVATION OF RIGHTS

49. Nothing contained herein is intended to or should be construed as an admission of the validity of any claim against the Debtor, a waiver of the Debtor's rights to dispute any claim, or an approval or assumption of any agreement, contract or lease under section 365 of the Bankruptcy Code. The Debtor expressly reserves its right to contest any claim of a Staff Member under applicable non-bankruptcy law. Likewise, if this Court grants the relief sought herein, any payment made pursuant to the Court's order is not intended to and should not be construed as an admission of the validity of any claim or a waiver of the Debtor's rights to dispute such claim subsequently.

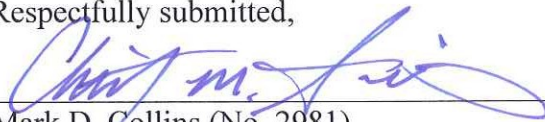
NOTICE

50. The Debtor has provided notice of this Motion by facsimile and/or overnight mail to: (a) the Office of the United States Trustee for the District of Delaware; (b) each of the Debtor's creditors holding the twenty (20) largest unsecured claims; (c) counsel to the Debtor's prepetition and proposed postpetition secured lender; (d) the Internal Revenue Service; (e) the Securities and Exchange Commission; (f) the United States Department of Justice; and (g) the Cash Management Banks. As this Motion is seeking first-day relief, notice of this Motion and any order entered hereon will be served on all parties required by Local Rule 9013-1(m). Due to the urgency of the circumstances surrounding this Motion and the nature of the relief requested herein, the Debtor respectfully submits that no further notice of this Motion is required.

WHEREFORE, for the reasons set forth herein and in the First Day Affidavit, the Debtor respectfully requests that the Court enter an order, substantially in the form attached hereto as Exhibit A: granting it authority to (i) pay certain prepetition Staff Member wage obligations, (ii) honor and/or pay certain Vacation Time obligations, (iii) honor certain Sick/Personal Leave obligations and (iv) granting such other and further relief as the Court may deem just and proper.

Dated: November 16, 2009
Wilmington, Delaware

Respectfully submitted,



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*Proposed Attorneys for the Debtor and
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EXHIBIT A

(Order)

U.S.C. §§ 157 and 1334; and it appearing that this Motion is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2); and it appearing that venue of this proceeding and this Motion in this district is proper pursuant to 28 U.S.C. §§ 1408 and 1409; and due and proper notice of this Motion having been provided; and it appearing that no other or further notice need be provided; and after due deliberation and sufficient cause appearing therefor,

It is hereby ORDERED

1. The Motion is GRANTED to the extent provided herein.
2. The Debtor is authorized, but not directed, to pay Staff Members,² in the ordinary course of business, amounts related to Vacation Time as set forth in the Motion and subject to the any caps in this Order.
3. The Debtor is authorized, but not directed, to pay TriNet, in the ordinary course of business, amounts related to prepetition Staff Member wages, in an amount not to exceed \$14,452.53.
4. The Debtor is authorized, but not directed, to pay Staff Members, in the ordinary course of business, amounts related to Vacation Time, in an amount not to exceed \$123,885.03. The Debtor is not authorized to honor and/or pay any amounts to Staff Members in excess of the \$10,950 statutory cap under sections 507(a)(4) and 507(a)(5) of the Bankruptcy Code; however, the foregoing is without prejudice to the Debtor's rights to seek such relief after notice and a hearing.
5. The Debtor is authorized, but not directed, to honor its obligations related to accrued prepetition Sick/Personal Leave in the ordinary course of business.

² Capitalized terms not otherwise defined herein shall have the meaning ascribed to them in the Motion.

6. The Debtor is authorized, but not directed, to issue postpetition checks, or to effect postpetition fund transfer requests, in replacement of any checks or fund transfer requests in respect of prepetition amounts owed to the Staff Members that are dishonored as a consequence of this chapter 11 case and to the extent such prepetition amounts are authorized to be paid pursuant to this Order.

7. All applicable banks and other financial institutions are hereby authorized and directed to receive, process, honor and pay any and all checks evidencing amounts paid by the Debtor pursuant to the Motion, whether presented prior to or after the Petition Date; and it is further

8. Any Cash Management Bank may rely on the representations of the Debtor with respect to whether any check or other payment order drawn or issued by the Debtor prior to the Petition Date should be honored pursuant to this Order, and such Cash Management Bank shall not have any liability to any party for relying on such representations by the Debtor as provided for herein.

9. Except as provided under the Bankruptcy Code, nothing contained herein is intended or should be construed to create an administrative priority claim on account of obligations owing to the Staff Members or, conversely, to prejudice the Staff Member's right to assert claims against the Debtor or its estate that are not satisfied by payments made pursuant to this Order.

10. The relief granted herein shall not constitute or be deemed an assumption of or an authorization to assume, pursuant to section 365 of the Bankruptcy Code, any of the employment or insurance agreements to which the Debtor is a party.

11. The requirements set forth in Rule 6003(b) of the Bankruptcy Rules are satisfied by the contents of the Motion.

12. Notwithstanding the possible applicability of Rule 6004(h) of the Federal Rules of Bankruptcy Procedure, the terms and conditions of this Order shall be immediately effective and enforceable upon its entry.

13. Notwithstanding anything to the contrary contained herein, any payment to be made, or authorization contained, hereunder shall be subject to the requirements imposed on the Debtor under any approved debtor-in-possession financing facility, any budget in connection therewith and any order regarding the use of cash collateral.

14. Nothing in the Motion or this Order, nor as a result of the Debtor's payment of claims pursuant to this Order, shall be deemed or construed as: (a) an admission as to the validity or priority of any claim against the Debtor, (b) a waiver of the Debtor's rights to dispute any claim, or (c) an approval or assumption of any agreement, contract or lease pursuant to section 365 of the Bankruptcy Code.

15. The Debtor is authorized and directed to take all actions necessary to effectuate the relief granted pursuant to this Order in accordance with the Motion.

16. This Court retains jurisdiction with respect to all matters arising from or related to the implementation of this Order.

Dated: November __, 2009
Wilmington, Delaware

UNITED STATES BANKRUPTCY JUDGE