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6  
7 Bankruptcy Counsel for eStyle, Inc.,  
Debtor and Debtor in Possession

8  
9 **UNITED STATES BANKRUPTCY COURT**  
10 **CENTRAL DISTRICT OF CALIFORNIA, LOS ANGELES DIVISION**

11 In re  
12  
13 ESTYLE, INC., a Delaware corporation,  
dba babystyle, Cadeau, and Cadeau  
Designs,

14 Debtor.

15  
16  
17  
18  
19 Tax Id # 95-4712564  
20

Case No. 2:08-bk-13518-SB

Chapter 11

**DECLARATION OF ROBERT S.  
KELLEHER IN SUPPORT OF DEBTOR'S  
REPLY TO WACHOVIA CAPITAL  
FINANCE CORPORATION'S OBJECTIONS  
TO DEBTOR'S MOTION FOR ORDERS  
AUTHORIZING USE OF CASH  
COLLATERAL**

DATE: April 17, 2008  
TIME: 2:00 p.m.  
PLACE: U.S. Bankruptcy Court  
Courtroom 1575  
255 East Temple Street  
Los Angeles, CA 90012

21 I, Robert S. Kelleher, declare:

22 1. I have person knowledge of the facts stated herein. I can testify that  
23 said facts are true and correct.

24 2. I am Chief Executive Officer of eStyle, Inc. (the "Debtor").

25 3. This Declaration is submitted in support of the Debtor's Reply To  
26 Wachovia Capital Finance Corporation's Objections to Debtor's Motion for Orders  
27 Authorizing Use of Cash Collateral (the "Reply").  
28

1           4.       This Declaration supplements my prior declaration filed on March 19,  
2 2008, in support of the Debtor's "first-day" motions, including the Debtor's motion for use  
3 of cash collateral. Additionally, my declarations were previously submitted in support of  
4 the Debtor's motion to enforce the automatic stay against Wachovia Capital Finance  
5 Corporation (Western) ("Wachovia") filed on March 20, 2008, and the Debtor's reply to  
6 Wachovia's objection to the motion regarding violation of the automatic stay filed on  
7 March 21, 2008. Attached as Exhibit 1 to the Reply is an updated Budget prepared by  
8 the Debtor (covering through June 21, 2008) providing for payments to Wachovia.

9           5.       I have reviewed the objections (the "Objection") of Wachovia  
10 received on the afternoon of April 14, 2008, with respect to the Debtor's motion for  
11 continued use of cash collateral. The Objection contains numerous inaccurate and/or  
12 misleading statements, including (page and line references below are to pages and lines  
13 in the Objection):

14               a.       At page 2, line 16, Wachovia incorrectly describes the Budget  
15 period as continuing through June 30, 2008 (the Budget period actually runs through  
16 June 21, 2008).

17               b.       At page 2, lines 17-21, Wachovia mischaracterizes "all . . .  
18 discussions" between the Debtor and Wachovia and all "cash collateral models" as  
19 assuming that Wachovia's loan would be paid down by \$.50 for every \$1.00 reduction  
20 and cost value of the Debtor's inventory. In fact, Wachovia's own suggestion was to  
21 impose a borrowing base (the borrowing base formula used pursuant to Wachovia's  
22 prepetition credit facility with the Debtor) plus 20% formula. That is, Wachovia had made  
23 a proposal to the Debtor that the Debtor maintain a ratio that showed the borrowing base  
24 of eligible inventory pursuant to Wachovia's prepetition credit facility requirements (less  
25 reserves) did not fall lower than a number that is 20% higher than the outstanding loan  
26 balance, or the Debtor would pay an amount on the loan balance that would get back to  
27 the 20% cushion. The Debtor structured the cash collateral model that was presented to  
28 Wachovia on April 11, 2008, to comply with this proposal previously made by Wachovia,

1 but it was rejected by Wachovia at the April 11, 2008 meeting with Wachovia that I  
2 participated in (along with Richard Alston) on behalf of the Debtor.

3 c. At page 2, lines 24-25, Wachovia asserts that it is losses that  
4 prevent the prepayment of Wachovia in the manner in which it demands. Rather, it is  
5 cash flow that includes the payment of amounts for inventory that limits the ability of the  
6 Debtor to comply with Wachovia's current demands. Inventory purchases are essential  
7 to the normal functioning of the Debtor's business and Wachovia apparently seeks to  
8 strip the Debtor with its ability to do so and to force a complete liquidation of the Debtor.

9 d. At page 3, lines 1-2, Wachovia contends that purported losses  
10 reflected in the April 11 Budget deny Wachovia adequate protection. This is incorrect.  
11 First, the Budget is not an income statement showing profits and losses. Second, as set  
12 forth in the Debtor's motion and the Reply, the Debtor believes that Wachovia is  
13 adequately protected by a substantial equity cushion.

14 e. At page 3, lines 9-12, Wachovia implies that there is a highly  
15 speculative effect of reserves regarding the Debtor's credit card receivables. However,  
16 the Debtor has already accounted for \$400,000 in Chase reserves and \$200,000 in  
17 American Express reserves (and the Debtor believes that the American Express reserves  
18 will either be voluntarily reduced or that the matter will be brought before the Court to  
19 address a reduction and elimination of these reserves that were asserted in their entirety  
20 post-petition as a result of the Debtor's chapter 11 filing).

21 f. At page 3, line 14, Wachovia refers to "inventory" when the  
22 figure it is referring to is actually an orderly liquidation value figure.

23 g. At page 3, Line 21, Wachovia asserts that the Debtor "still has  
24 no exit plan". However, as discussed above, the Debtor is in the process of evaluating  
25 various alternatives that could serve as the basis for a chapter 11 plan. Moreover, this  
26 case was commenced only 4 weeks ago and the Debtor has been consumed with  
27 numerous urgent issues, including continued use of cash collateral, that have had to be  
28

1 addressed on an immediate and continuous basis since the commencement of the  
2 Debtor's chapter 11 case.

3 h. At page 3, lines 23-24, Wachovia refers to the Debtor's  
4 projections for June. The month of June is historically a lower sales month for the Debtor  
5 than May. While there may be a negative cash flow resulting from the lower sales,  
6 Wachovia's inventory collateral increases during that period.

7 i. Wachovia's references to "losses" at page 3, lines 25 and 26,  
8 are, once again, a mischaracterization, since the Budget is not an income statement and  
9 the cash forecasts do not equate to losses as Wachovia implies.

10 j. At page 4, line 18, Wachovia again misstates "inventory"  
11 value to be \$4.9 million, while this is an orderly liquidation value, the inventory amount  
12 cited by Wachovia should be \$5,545,121.

13 k. At page 4, line 26, Wachovia asserts that cash costs of the  
14 Debtor other than inventory purchases would remain the same in a full liquidation mode  
15 as they are today. This is not correct. The Debtor would prepare a plan for such a  
16 liquidation that would include significant expense reductions at, among other things, the  
17 Debtor's corporate office. This fact makes Wachovia's statements on page 5, lines 5  
18 and 6, incorrect. For example, in a 6 week liquidation, if inventory purchases were  
19 eliminated you would also eliminate, among other things, UPS logistics costs of  
20 \$170,926, and salaries and wages related to a portion of the Debtor's corporate office  
21 would be reduced.

22 l. Wachovia's arguments appearing at page 6, section E, are  
23 incorrect and misleading. The revenue decline of \$116,790 that Wachovia points to is  
24 less than 7% below the cumulative 2-week sales forecast amount. Moreover, Wachovia  
25 fails to point out that the real factor on which to focus is not revenues but net cash flow  
26 which takes into consideration the disbursements which were well below forecast in the  
27 first two weeks of the Budget. In week one, the cash disbursement in the original Budget  
28 was to have been \$910,729, with an estimated negative cash flow of \$275,228. The

1 actual disbursements were \$546,999, creating a positive cash flow in week one of  
2 \$224,948. Accordingly, net cash flow was more favorable than in the original Budget (or  
3 for that matter in the March 25, 2008 Budget attached to the Court's order approving  
4 interim use of cash collateral). Further, the liquidation of the Cadeau inventory was  
5 always footnoted in the Budget as occurring in either the DTC (Direct to Consumer –  
6 Internet) or the Cadeau New York Store. This accounts for approximately half of the  
7 sales being less than projected. The reason for this change in liquidation location is that  
8 the Cadeau LA Store had low traffic and was closed by the Debtor.

9 m. Wachovia's assertions appearing at page 6 regarding the  
10 Debtor's reported inconsistent and inaccurate inventory reporting are incorrect. First,  
11 Wachovia is comparing certain figures to the original Budget, while the Debtor has been  
12 using the March 25, 2008 Budget approved by the Court attached as Exhibit 1 to the  
13 Court's order entered on March 26, 2008, as a Budget against which comparisons should  
14 be made. The March 25, 2008 Budget accounts for actual changes in inventory due to  
15 less purchases coming in after the commencement of the Debtor's chapter 11 case and  
16 timing differences relating to the chapter 11 filing and actual cash/expenses adjusted in  
17 connection with its timing.

18 n. At pages 6 and 7, Wachovia makes certain allegations  
19 regarding the Debtor's "flash reporting" that is misleading and inaccurate. The Debtor  
20 has always done its reporting to Wachovia on the borrowing base certificate with all of the  
21 inventory reserves, etc. and the flash reporting was to roll off the monthly reporting to be  
22 adjusted as the Debtor completed it each month. This is what occurred in March as the  
23 Debtor reported the month end for February (reported on March 15, 2008) and then the  
24 flash reporting was adjusted on March 21, 2008. The flash report was corrected on the  
25 March 21 flash report to Wachovia (for the period ending March 15, 2008) and has been  
26 correctly rolled forward thereafter. The Debtor is reporting to Wachovia weekly on the  
27 borrowing base certificate and is tying that to the flash report. The Debtor has updated  
28

1 some assumptions on its current reporting for newer information on the wholesale  
2 inventory balances which it has noted in its reports.

3           6.       The updated Budget attached as Exhibit 1 to the Reply provides for a  
4 paydown of Wachovia in the sum of \$583,856. This is in addition to the \$303,000 sum  
5 the Debtor believes that Wachovia took from the Debtor's concentration bank account  
6 after the commencement of the Debtor's chapter 11 case. Attached to the Reply as  
7 Exhibit 2 and incorporated herein by this reference is a comparison of the Debtor's  
8 operating results for the first 3 weeks of this case to the Budget attached as Exhibit 1 (the  
9 March 25 Budget) to the Court's interim order authorizing the Debtor's use of cash  
10 collateral signed on March 25 and entered on March 26, 2008. As set forth in the  
11 comparison analysis attached hereto as Exhibit 2, the Debtor's net cash flow has been a  
12 positive \$393,382 for the first 3 weeks of this case. Moreover, the variance of the  
13 Debtor's actual net receipts compared to budgeted net receipts was less than 9% for the  
14 first 3 weeks of this case. As a result, actual net cash flow exceeds projected net cash  
15 flow set forth in the Budget attached as Exhibit 1 to the Court's interim order by \$447,476  
16 for the first 3 weeks of the case.

17           7.       Further, it should be noted that while Wachovia is more than  
18 adequately protected by the Debtor's inventory, the Debtor has other tangible assets,  
19 including other personal property and intellectual property rights, and the Debtor believes  
20 that it has significant additional value as a going concern.

21           8.       As set forth in the Debtor's motion filed on March 20, 2008, for an  
22 order enforcing the automatic stay against Wachovia and the declaration and exhibits  
23 attached thereto and the Debtor's reply, filed on March 21, 2008, to Wachovia's objection  
24 with respect to the motion for violation of the automatic stay and the declaration and  
25 exhibits attached to the Reply, the Debtor believes that Wachovia improperly took  
26 \$303,000 from the Debtor's concentration bank account after the commencement of this  
27 chapter 11 case. Thereafter, Wachovia improperly removed approximately an additional  
28 \$260,000 from the Debtor's concentration bank account and subsequently returned to the

1 Debtor the approximate \$260,000 sum that Wachovia admitted was improperly taken.  
2 However, Wachovia has not returned the \$303,000 that was the subject of the Debtor's  
3 motion to enforce the automatic stay filed prior to the initial "first-day" hearings conducted  
4 in this case on March 21, 2008. It is undisputed that \$303,000 in funds were taken by  
5 Wachovia from the Debtor's concentration bank account. The question of whether the  
6 funds were taken post-petition should be very simple to answer and that information is  
7 clearly within the possession and control of Wachovia. Accordingly, Wachovia should be  
8 required to come forward with evidence of the exact time that the \$303,000 was removed  
9 from the Debtor's concentration account. If Wachovia requires additional time to provide  
10 this information, the Debtor does not understand why it is needed, but does not object to  
11 the Court allowing Wachovia additional time to provide this information.

12 9. To the detriment of other creditors, Wachovia in the Objection  
13 appears to seek to force the immediate liquidation of the Debtor. While the Debtor is in  
14 the process of closing certain stores (the Court has previously authorized store closing  
15 sales at 6 of the Debtor's stores) and while the Debtor anticipates that it will close some  
16 additional stores, this chapter 11 case was only commenced 4 weeks ago. The Debtor is  
17 currently in the process of evaluating alternatives that might serve as the basis for a  
18 chapter 11 plan. These alternatives include the sale of all or different parts of the  
19 Debtor's business, a refinancing of the Debtor's secured debt, new equity investments in  
20 the Debtor, a combination of financing and equity investments, and/or a wind down and  
21 liquidation of portions or all of the Debtor's business operations. The Debtor has  
22 commenced discussions with various different parties regarding these potential  
23 alternatives, has disseminated nondisclosure agreements to various parties who have  
24 expressed interest, and has provided information to those interested parties who have  
25 returned executed nondisclosure agreements.

26 10. Wachovia is the only party who has opposed the Debtor's use of  
27 cash collateral. An unsecured creditors committee was just appointed on April 10, 2008.  
28

1 I believe that the Debtor has a reasonable prospect of a feasible and successful  
2 reorganization in this case.

3 11. Further, the Debtor is in process of implementing a new business  
4 model that represents a dramatic departure from its prior business model. Under the new  
5 business model, the Debtor will operate fewer stores, have a smaller overhead structure,  
6 and will be better positioned to take advantage of new trends (based on a revised  
7 purchasing plan). Further reductions in overhead (more than \$1,000,000 annually have  
8 been identified) and the further reduction in stores (to eliminate unprofitable operations)  
9 will position the Debtor so that it will be able to generate positive cash flow and profit in  
10 the 12-month period following full implementation of these changes. The Debtor's sales  
11 margins reflected in the first 3 weeks of operation following the commencement of this  
12 chapter 11 case are not indicative of the profit generating capacity of the Debtor's  
13 business without the above-referenced changes. The recent results are severely  
14 impacted on both the revenue line (as a result of cannibalization of ongoing store sales  
15 located new stores conducting store closing sales) as well as on the margin line (store  
16 closing efforts naturally impact the margins due to the progressive markdown strategy  
17 employed in the store closing sale process).

18 12. Wachovia is adequately protected by a substantial equity cushion.  
19 Nonetheless, the Debtor is prepared to paydown the Wachovia debt by the sum of  
20 \$583,856 during the period covered by the Budget (through June 21, 2008). This is in  
21 addition to the \$303,000 previously taken by Wachovia from the Debtor's concentration  
22 bank account.

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

24 EXECUTED THIS 15<sup>th</sup> DAY OF APRIL, 2008, AT LOS ANGELES,  
25 CALIFORNIA.

26  
27 

28 \_\_\_\_\_  
Robert S. Kelleher

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1 PROOF OF SERVICE

2  
3 **STATE OF CALIFORNIA, COUNTY OF LOS ANGELES**

4 At the time of service, I was over 18 years of age and **not a party to this action**. I  
5 am employed in the County of Los Angeles, State of California. My business address is  
333 South Hope Street, Thirty-Fifth Floor, Los Angeles, California 90071-1406.

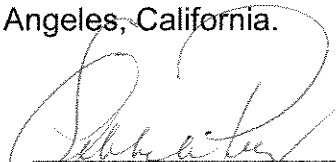
6 On April 16, 2008, I served the following document(s) described as **DECLARATION OF**  
7 **ROBERT S. KELLEHER IN SUPPORT OF DEBTOR'S REPLY TO WACHOVIA**  
8 **CAPITAL FINANCE CORPORATION'S OBJECTIONS TO DEBTOR'S MOTION FOR**  
9 **ORDERS AUTHORIZING USE OF CASH COLLATERAL** on the interested parties in this  
action as follows:

10 **SEE ATTACHED SERVICE LIST**

11 **BY E-MAIL OR ELECTRONIC TRANSMISSION:** I caused the document(s) to be sent  
12 from the e-mail address dperezp@sulmeyerlaw.com to the persons at the e-mail  
addresses listed above. I did not receive, within a reasonable time after the transmission,  
any electronic message or other indication that the transmission was unsuccessful.

13 I declare under penalty of perjury under the laws of the United States of America  
14 that the foregoing is true and correct and that I am employed in the office of a member of  
the bar of this Court at whose direction the service was made.

15 Executed on April 16, 2008, at Los Angeles, California.

16   
17 \_\_\_\_\_  
Debbie A. Perez

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