

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF MARYLAND  
(Baltimore Division)**

<p><b>In re</b></p> <p><b>The Boyds Collection, Ltd., et al.</b><sup>1</sup></p> <p style="text-align: center;"><b>Debtors.</b></p>	<p>*</p> <p>*</p> <p>*</p> <p>*</p> <p>*</p> <p>*</p> <p>*</p>	<p>Case No. 05-____ (____) through 05-____ (____)</p> <p>Chapter 11 (Jointly Administered under Case No. 05-____ (____))</p>
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**DEBTORS' EMERGENCY MOTION FOR ENTRY OF AN ORDER (A)  
AUTHORIZING, BUT NOT REQUIRING, THE DEBTORS TO REMIT AND PAY  
SALES, USE AND FRANCHISE TAXES AND CERTAIN OTHER GOVERNMENT  
CHARGES AND (B) AUTHORIZING BANKS AND OTHER FINANCIAL  
INSTITUTIONS TO RECEIVE, PROCESS, HONOR AND PAY CHECKS ISSUED AND  
ELECTRONIC PAYMENT REQUESTS MADE RELATING TO THE FOREGOING**

The Boyds Collection, Ltd., et al., the debtors and debtors in possession in the above-captioned cases (collectively, the "Debtors"), by counsel, file this Emergency Motion for Entry of an Order (A) Authorizing, but not Requiring, the Debtors to Remit and Pay Sales, Use and Franchise Taxes and Certain Other Government Charges and (B) Authorizing Banks and Other Financial Institutions to Receive, Process, Honor and Pay Checks Issued and Electronic Payment Requests Made Relating to the Foregoing (the "Motion"), and in support thereof state:<sup>2</sup>

**Jurisdiction**

1. 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.

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<sup>1</sup> The Debtors in the proposed jointly administered cases include: The Boyds Collection, Ltd.; The Boyds Collection, Ltd., LP; Boyds Operations Inc.; The Boyds Collection - Pigeon Forge, LLC; The Boyds Collection - Myrtle Beach, LLC; The Boyds Collection - Branson, LLC; J&T Designs and Imaginations, Inc.; HC Accents & Associates, Inc.; and Boyds Bear and Company, LP.

<sup>2</sup> The facts and circumstances supporting this Motion are set forth in the Affidavit of Jan L. Murley in Support of First Day Motions filed contemporaneously herewith.

2. The statutory bases for the relief requested herein are sections 105(a), 363(b), 541 and 507(a)(8) of title 11 of the United States Code (the “Bankruptcy Code”).

### **Background**

3. On the date hereof (the “Commencement Date”), the Debtors each filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code (collectively, the “Reorganization Cases”). The Debtors continue to operate their businesses and manage their properties as debtors-in-possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. Contemporaneously herewith, the Debtors requested an order for the joint administration of the Reorganization Cases pursuant to Rule 1015(b) of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”).

4. The Boyds Collection, Ltd. (“Boyds”) is a leading designer, marketer and distributor of high-quality, hand-crafted collectibles, gift and other specialty products. Boyds was founded in 1979 and is the parent company, holding direct or indirect ownership interests in eight (8) domestic subsidiaries and four (4) foreign subsidiaries.

5. Boyds operates in two segments: a wholesale gift business and a retail gift/entertainment business. Boyds’ wholesale business designs, imports and distributes plush animals, resin figurines and other specialty giftware via a global network of independent retailers and distributors. Boyds imports substantially all of its products from manufacturers in China through buying agencies. Boyds’ retail business sells plush animals, resin figurines and specialty giftware products and provides a unique interactive entertainment experience at its Gettysburg, Pennsylvania and Pigeon Forge, Tennessee retail stores.

6. As set forth in the Form 10-Q filed by Boyds on August 12, 2005, as of June 30, 2005, the Debtors’ consolidated books and records reflected assets totaling approximately \$66.9 million and liabilities totaling approximately \$101.7 million. For the three months ended June 30, 2005, Boyds reported revenues of approximately \$17.1 million and net losses of approximately \$101.3 million.

7. The significant indebtedness of Boyds consists of: (i) approximately \$56.5 million in aggregate principal amount under a senior secured credit agreement, dated as of February 23, 2005 (the “Pre-Petition Credit Agreement”) and (ii) approximately \$34.4 million in aggregate principal amount pursuant to certain 9% senior subordinated notes due in 2008.

8. During 2001, Boyds’ financial results began to deteriorate significantly as a consequence of industry-wide and company-specific factors. Over a period of several years, retail sales of plush toys shifted from small independent retailers, in which Boyds had a leading presence, to large regional and national retailers and mass merchandisers, in which Boyds did not have a meaningful presence. Moreover, the large retailers competed with Boyds’ product line at lower price points. This shift in distribution channels coincided with a general cooling of consumer demand for “collectible” products. As a result, the retail sales of Boyds and its direct industry competitors were negatively affected.

9. In response, during 2004 Boyds began to implement various operational restructuring and cost reduction programs. Such programs focused on (i) redirecting sales efforts towards larger regional and national channels, (ii) developing products specifically targeted to these channels, (iii) selectively expanding distribution to include direct in-home marketing initiatives and (iv) developing co-branding campaigns with well-recognized brands such as NASCAR, Coca-Cola, Crayola and M&Ms. Unfortunately, despite the efforts of Boyds’ management to reposition the business in response to the changing industry sales dynamics, Boyds was not able to increase sales in the new channels quickly enough to offset the decline in sales from the company’s traditional core-market of independent retailers.

10. By the fall of 2005, it had become apparent that Boyds could not avoid a financial restructuring. From September to the Commencement Date, Boyds engaged in discussions with the lenders (the “Pre-Petition Lenders”) under the Pre-Petition Credit Agreement regarding the terms of a comprehensive plan to restructure Boyds’ operations and existing debt obligations. Though Boyds and the Pre-Petition Lenders made substantial progress in these negotiations, as of the Commencement Date, negotiations were still ongoing. The Pre-Petition Lenders were

unwilling to extend the waiver or commit to providing any further liquidity outside of a reorganization. On the Commencement Date, the Debtors, in the exercise of their prudent business judgment, determined that it was in the best interest of all their stakeholders to commence the Reorganization Cases, continue negotiations with the Debtors' creditor constituencies and consummate a restructuring under the auspices of this Court.

### **Relief Requested**

11. In the ordinary course of business, the Debtors (a) collect sales taxes from their customers and incur taxes, including, but not limited to, use and franchise taxes and other taxes necessary to operate their businesses (collectively, the "Taxes") and (b) charge fees, licenses, permits and other similar charges and assessments (collectively, the "Fees")<sup>3</sup> on behalf of various taxing and licensing authorities (collectively, the "Authorities") and pay Fees to such Authorities for licenses and permits required to conduct the Debtors' businesses.<sup>4</sup> The Taxes and Fees are paid either monthly, quarterly or annually to the respective Authorities.

12. Although the Debtors' records reflect that they are current on all of their Taxes and Fees owed as of the Commencement Date, the Debtors seek the relief requested in the event and to the extent that any Taxes and Fees that accrued pre-petition were not in fact paid pre-petition, or were paid in an amount that was less than is actually owed, or in the event that any payments made pre-petition were rejected, lost or otherwise not received in full by any Authorities. Further, there may be taxes incurred or collected from sales and services provided pre-petition that will become due shortly after the filing.

13. The Debtors estimate that the total amount of pre-petition Taxes and Fees owing to the various Authorities will not exceed approximately \$650,000.<sup>5</sup> Any amounts that are

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<sup>3</sup> The Debtors hereby request authority to pay Taxes and Fees regardless of whether they constitute trust fund obligations.

<sup>4</sup> The Debtors currently face potential taxation in three states: Georgia, Pennsylvania and Tennessee.

<sup>5</sup> This estimate does not include any potential pre-petition tax liability that may later come due as the result of an audit. In particular, there is an ongoing audit by the State of Pennsylvania with respect to sales and use taxes.

(Continued...)

actually due, but have not yet been paid to the Authorities because of the bankruptcy filings, represent a small fraction of the Debtors' total assets. Additionally, some, if not all, of the Authorities may cause the Debtors to be audited if the Taxes and Fees are not paid immediately. Such audits will unnecessarily divert the Debtors' attention away from the reorganization process. Furthermore, if the Debtors do not pay such amounts in a timely manner, the Authorities may attempt to suspend the Debtors' operations, file liens, seek to lift the automatic stay and pursue other remedies that will harm the estates. Moreover, some of these outstanding tax liabilities are for trust fund taxes that the Debtors have collected and hold in trust for the benefit of the Authorities. Therefore, such funds do not constitute property of the estate and could not otherwise be used by the estates.

14. In all cases, the Debtors' failure to pay the Taxes and Fees could have a material adverse impact on their ability to operate in the ordinary course of business. The Debtors operate a transactional business and any disputes that could impact their ability to conduct business in a particular jurisdiction could have a wide-ranging and adverse effect on the Debtors' operations as a whole.

15. Accordingly, the Debtors seek authority to pay, in their sole discretion, the Taxes and Fees to the relevant Authorities in the ordinary course of business.

#### **Basis for Relief**

16. Section 541(d) of the Bankruptcy Code provides, in relevant part, that “[p]roperty in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest . . . becomes property of the estate under subsection (a)(1) or (a)(2) of this section only to the extent of the Debtors' legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.” 11 U.S.C. § 541(d).

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This audit and any other potential audits may result in tax liability. The Debtors, therefore, request that the relief sought herein apply likewise to any liability resulting from audits of pre-petition taxes, in the event such liability arises.

17. Many of the Taxes and Fees constitute “trust fund” taxes, which are required to be collected from their customers and held in trust for payment to the Authorities. See, e.g., Plett v. United States, 185 F.3d 216, 218 (4th Cir. 1999) (federal withholding taxes and social security taxes are “trust fund taxes”); Shank v. Washington State Dep’t of Revenue (In re Shank), 792 F.2d 829, 833 (9th Cir. 1986) (sales tax required by state law to be collected by sellers from their customers is a “trust fund” tax and not released by bankruptcy discharge); DeChiaro v. New York State Tax Comm’n, 760 F.2d 432, 435-36 (2d Cir. 1985) (same). To the extent these “trust fund” taxes are collected, they are not property of the Debtors’ estates under section 541(d) of the Bankruptcy Code. See Begier v. Internal Revenue Serv., 496 U.S. 53, 57-60 (1990) (holding that any pre-petition payment of trust fund taxes is not an avoidable preference since funds are not the debtor’s property); In re Al Copeland Enter., Inc., 133 B.R. 837 (Bankr. W.D. Tex. 1991), aff’d, 991 F.2d 233 (5th Cir. 1993) (debtor obligated to pay Texas sales tax plus interest because such taxes were “trust fund” taxes); In re Sunrise Paving, Inc., 204 B.R. 691, 696 (Bankr. D. Md. 1996) (property held in trust by the Debtor is not property of the estate). The Debtors, therefore, generally do not have an equitable interest in the Taxes or Fees, and should be permitted to pay them to the Authorities as they become due.

18. Furthermore, state authorities could assert that the Debtors’ officers and directors may be held personally liable if the Debtors fail to meet the obligations imposed upon them to remit Taxes and Fees. To the extent such accrued Taxes or Fees of the Debtors were unpaid as of the Commencement Date, the Debtors’ officers and directors may be subject to lawsuits in certain jurisdictions during the pendency of these Reorganization Cases, even if the failure to pay such Taxes and Fees was not a result of any malfeasance on their part. Such potential lawsuits would prove extremely distracting for the Debtors, for the named officers and directors whose attention to the Debtors’ reorganization process is required and for this Court, which may be asked to entertain various motions seeking injunctions with respect to the potential state court actions. Therefore, it is in the best interests of the Debtors’ estates and the Debtors’ prospects for reorganization to eliminate the possibility of the foregoing distractions.

19. In addition, the Taxes are, and some of the Fees may be, entitled to priority status pursuant to section 507(a)(8) of the Bankruptcy Code and, therefore, must be paid in full under section 1129(a)(9)(C) of the Bankruptcy Code to confirm any plan of reorganization. Thus, the payment of the Taxes and Fees at this time only affects the timing of the payment and does not prejudice the rights of other creditors.

20. The Court may also authorize the Debtors to pay the Taxes and Fees under section 363(b) of the Bankruptcy Code, which provides that “[t]he trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate.” 11 U.S.C. § 363(b)(1). Under this section, a court may authorize a debtor to pay certain pre-petition claims. See FV Steel and Wire Co., Case No. 04-22421 (Bankr. E.D. Wis. Feb. 26, 2004) (authorizing the continuation of customer programs and the payment of pre-petition claims under section 363 of the Bankruptcy Code); In re UAL Corp., Case No. 02-48191 (Bankr. N.D. Ill. Dec. 9, 2002) (authorizing payment of pre-petition claims under section 363 of the Bankruptcy Code as an out-of-the-ordinary-course transaction); In re Ionosphere Clubs, Inc., 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989) (affirming lower court order authorizing payment of pre-petition wages pursuant to section 363(b) of the Bankruptcy Code). To do so, “the debtor must articulate some business justification, other than the mere appeasement of major creditors.” Ionosphere Clubs, 98 B.R. at 175. As discussed above, the Debtors’ failure to pay the Taxes and Fees could have a material adverse impact on their ability to operate in the ordinary course of business.

21. Finally, section 105(a) of the Bankruptcy Code provides that “[t]he court may 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). The purpose of section 105(a) of the Bankruptcy Code is “to assure the bankruptcy courts power to take whatever action is appropriate or necessary in aid of the exercise of their jurisdiction.” See 2 Collier on Bankruptcy ¶ 105.01 (15th ed. rev. 2003). Thus, section 105 of the Bankruptcy Code essentially codifies the Bankruptcy Court’s inherent equitable powers. The relief requested in this Motion is critical to

the Debtors' operations and reorganization and is therefore justified under section 105(a) of the Bankruptcy Code.

22. In numerous chapter 11 cases, bankruptcy courts in this and other districts have exercised their equitable powers under section 105 of the Bankruptcy Code to authorize debtors to pay pre-petition tax obligations. See, e.g., In re Nat'l Energy & Gas Transmission, Inc., Case No. 03-30459 (PM) (Bankr. D. Md. Sept. 5, 2003); In re Baltimore Marine Indus., Inc., Case No. 03-80215 (JFS) (Bankr. D. Md. June 24, 2003); In re MCSi, Inc., Case No. 03-80169 (JFS) (Bankr. D. Md. June 6, 2003); In re Startec Global Commc'ns Corp., Case No. 01-25013 (DK) (Bankr. D. Md. Feb. 7, 2002); see also, e.g., In re Choice One Commc'ns Inc., Case No. 04-16433 (RDD) (Bankr. S.D.N.Y. Oct. 7, 2004); In re Adelpia Bus. Solutions, Inc., Case No. 02-41729 (REG) (Bankr. S.D.N.Y. June 27, 2002). The Debtors submit that the present circumstances warrant similar relief in these Reorganization Cases.

23. Granting the relief requested is appropriate and in the best interest of the Debtors, their estates and their creditors. However, nothing in this Motion or the order granting this Motion should be construed as impairing the Debtors' ability to contest the amounts of any Taxes and Fees allegedly owing to the various Authorities.

24. The Debtors also request that all applicable banks and other financial institutions be authorized to receive, process, honor and pay all checks presented for payment, and to honor all electronic payment requests made by the Debtors related to the pre-petition obligations described herein, whether such checks were presented or electronic requests were submitted prior to or after the Commencement Date. The Debtors further request that all such banks and financial institutions be authorized to rely on the Debtors' designation of any particular check or electronic payment request as approved pursuant to this Motion. The Debtors have sufficient cash reserves to promptly pay all pre-petition obligations set forth herein on an ongoing basis and in the ordinary course of their businesses.

### **Memorandum of Law**

25. This Motion includes citations to the applicable authorities and a discussion of their application to this Motion. Accordingly, the Debtors respectfully submit that such citations and discussion satisfy the requirement that the Debtors submit a separate memorandum of law in support of this Motion pursuant to Rule 9013-2 of the Local Bankruptcy Rules for the District of Maryland.

### **Notice**

26. Notice of this Motion has been given to (a) the office of the United States trustee; (b) counsel to the Agent to the Debtors' Pre-Petition Lenders; (c) counsel for the indenture trustee for the Debtors' 9% Senior Subordinated Notes due 2008; and (d) each of the Debtors' top twenty (20) unsecured creditors.

### **No Prior Request**

27. No prior motion for the relief requested herein has been made to this or any other Court.

## Conclusion

WHEREFORE, the Debtors respectfully request the entry of an order, substantially in the form attached hereto as Exhibit A, (i) authorizing, but not requiring, the Debtors to remit and pay sales, use and franchise taxes and such other taxes as the Debtors, in their discretion, deem necessary, as well as fees, licenses and other similar charges and assessments, (ii) authorizing financial institutions to receive, process, honor and pay all checks issued and electronic payment requests made relating to the foregoing and (iii) granting such other and further relief as the Court deems appropriate.

Washington, D.C.  
Dated: October 16, 2005

Respectfully submitted,

### **SWIDLER BERLIN LLP**

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Proposed Counsel for the Debtors and Debtors in  
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**EXHIBIT A**  
**Proposed Order**

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF MARYLAND  
(Baltimore Division)**

**In re** \* Case No. 05-\_\_\_\_ (\_\_\_\_) through  
\* 05-\_\_\_\_ (\_\_\_\_)  
**The Boyds Collection, Ltd., et al.**<sup>1</sup> \*  
\*  
**Debtors.** \* Chapter 11  
\* (Jointly Administered under  
\* Case No. 05-\_\_\_\_ (\_\_\_\_))  
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**ORDER (A) AUTHORIZING THE DEBTORS TO REMIT AND PAY SALES, USE AND  
FRANCHISE TAXES AND CERTAIN OTHER GOVERNMENT CHARGES AND (B)  
AUTHORIZING BANKS AND OTHER FINANCIAL INSTITUTIONS TO RECEIVE,  
PROCESS, HONOR AND PAY ALL CHECKS ISSUED AND ELECTRONIC PAYMENT  
REQUESTS MADE RELATING TO THE FOREGOING**

Upon the Debtors' Emergency Motion for Entry of an Order (A) Authorizing, But Not Requiring, the Debtors to Remit and Pay Sales, Use and Franchise Taxes and Certain Other Government Charges and (B) Authorizing Banks and Other Financial Institutions to Receive, Process, Honor and Pay Checks Issued and Electronic Payment Requests Made Relating to the

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