

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE**

	X	
In re:	:	Chapter 11
	:	
RESPONSE GENETICS, INC.	:	Case No. 15-11663 (LSS)
	:	
Debtor.	:	
	X	

**DEBTOR’S STATUS REPORT REGARDING
POST-SALE CLOSING AND WIND DOWN OF ESTATE**

The above-captioned debtor and debtor in possession (the “**Debtor**”) hereby files this status report (the “**Status Report**”) and respectfully represents as follows:

1. The above-captioned debtor and debtor in possession (the “**Debtor**”) hereby files this status report (the “**Status Report**”) to apprise the Court of the status of the Debtor’s efforts to negotiate an acceptable wind down budget with SWK. The Debtor requires sufficient liquidity with which to administer the Debtor’s estate after the closing of the sale of substantially all of the Debtor’s assets (the “**Sale**”) to Cancer Genetics, Inc. (“**CGI**”). As the Debtor informed the Court at the October 1, 2015 hearing to approve the Sale, unless SWK Funding, LLC (“**SWK**”) agrees to provide the Debtor with an acceptable wind down budget, the Debtor will be left with no option other than to convert the case to a chapter 7 case.

2. The Court scheduled a hearing for October 9, 2015 to have the parties report on the progress, if any, the parties were able to make to resolve their differences. Unfortunately, SWK has not engaged the Debtor in any discussions or negotiations regarding an acceptable wind down budget and appears content to have the case converted to chapter 7 – an unfortunate result which will delay distributions to creditors, leave the estate with a variety of post closing tasks to be completed by people unfamiliar with the Debtor’s operations and minimal liquidity to do so while otherwise allowing SWK to reap the benefits of the sale.

3. As the Court is aware, this case was filed for the principal purpose of enabling the Debtor to market and sell substantially all of its assets to CGI, or an overbidder. The Asset Purchase Agreement (“APA”) negotiated with CGI provided for a purchase price of \$14 million, consisting of \$7 million in cash and \$7 million in stock – significantly less than the amount of the secured debt owed to (a) SWK (on account of its prepetition secured debt and its anticipated debtor in possession financing loan) and (b) Silicon Valley Bank (“SVB”). Importantly, the APA carved out certain receivables that CGI would not be purchasing (the “Retained Receivables”) that would be left with the estate after closing. Accordingly, pursuit of the Sale was principally for the benefit of SWK. The Sale is anticipated to close on October 9, 2015.

4. The Debtor contemplated that unless the Retained Receivables were sold to an overbidder in connection with the auction process, the Debtor would be left to monetize the Retained Receivables after the closing of the Sale. To that end, the Debtor intended to engage SWK in a discussion regarding how best to monetize the Retained Receivables post-closing in the context of a broader discussion regarding SWK’s funding of a modest wind down budget to administer the estate post-closing¹. Requiring a secured creditor to fund a modest wind down budget post-closing is typical and appropriate given that most cases, like this case, are run principally for the benefit of the secured creditor.

¹ A dispute has arisen between SWK and SVB regarding whether SVB will be paid in full from a closing of the Sale. SWK apparently contends that SVB is not entitled to be paid in full because only a portion of its primary collateral (the accounts receivable) are being sold such that SVB should await payment from post sale collection of the Retained Receivables. SWK’s current position is in stark contrast to representations made by SWK’s counsel to Debtor’s counsel at the commencement of this case that SVB would be paid in full even though the Retained Receivables were not being acquired by CGI provided that the transaction that closed was the transaction reflected in the Asset Purchase Agreement with CGI.

5. During the case, the Debtor, the Committee, and SWK reached agreement resolving the Committee's issues with the sale process and provided for money to be available to distribute to general unsecured creditors. On October 1, 2015, the Court entered its *Order Granting Joint Motion Of The Official Committee Of Unsecured Creditors And The Debtor For Order Approving Compromise Of Controversies In Accordance With Settlement Term Sheet* [Docket No. 187]. The settlement provides for a fund equal to the lesser of \$325,000 or 10% of the allowed amount of unsecured claims to be available to pay general unsecured claims. Importantly, the settlement contemplated that the Debtor and the Committee would be in charge of the claims reconciliation process post-closing and earmarked \$75,000 of the Committee carve out to be available to it post-closing to reconcile claims. The parties contemplated that the claims would be resolved post-closing and the parties would consider seeking a structured dismissal of the case. None of that could occur, however, without funding a wind down process.

6. Accordingly, it should have come as no surprise to SWK that it would be asked to fund a wind down budget to enable the Debtor to complete the traditional tasks required in a chapter 11 case after the sale of substantially all of its assets².

7. The Debtor did not receive any qualified overbids on or before the September 25, 2013 bid deadline. On September 28, 2015, the Debtor transmitted a proposed

² SWK apparently claims that it already agreed to fund a wind down on account of the \$100,000 post-termination carve out as set forth in the *Order (1) Authorizing the Debtor to Obtain Post-Petition Financing on a Final Basis, Granting Senior Postpetition Security interests and According Superpriority Administrative Expenses Status Pursuant to Sections 364(c) and 364(d) of the Bankruptcy Code, (2) Authorizing the Use of Cash Collateral, (3) Granting Adequate Protection, (4) Modifying the Automatic Stay, and (5) Granting Related Relief* [Docket No. 111] (the "**Final DIP Order**"). The \$100,000 post-termination carve out was not a fund to wind down the estate. Rather it was funds that would be available for fees incurred by estate professionals after SWK issued a notice of "Termination Date" under the Final DIP Order. It was not earmarked generally to a wind down of the estate and not to any costs and expenses that would be incurred in a wind down other than professional fees.

wind down budget (the “**Initial Proposed Wind Down Budget**”) to SWK. See **Exhibit A** attached hereto.

8. The Initial Proposed Wind Down Budget sought additional funding of \$380,000 from SWK³ to, among other things, to (a) reconcile unpaid administrative claims and pay them from funding authorized under the Budget attached to the Final DIP Order; (b) address post-closing matters with CGI; (c) provide for winding down of the Debtor’s 401(k) plan; (d) address employee issues arising post closing; (e) commissioning the preparation of final tax returns; (f) reconcile claims; (g) retain an independent board member to supervise the wind down; and (h) pay United States Trustees Fees. Of the \$380,000, \$225,000 was contemplated for Debtor’s counsel and Chief Restructuring Officer and the remaining \$155,000 for wind-down related tasks.

9. SWK rejected the Initial Proposed Wind Down Budget prior to the hearing on October 1, 2015 without providing any counterproposal.

10. At the October 1, 2015 hearing, the Debtor apprised the Court of the impasse that had been reached surrounding the funding of the wind down. At the hearing, SWK informed the Court that its consideration of funding a wind down was tied to its acceptance of a proposal to monetize the Retained Receivables.

11. The Debtor’s position is that the funding of the wind down is independent from any determination of how the Retained Receivables are to be collected. Nevertheless, on Friday, October 2, 2015 the Debtor transmitted to SWK a proposal for the monetization of the Retained Receivables (the “**AR Proposal**”), which involves utilizing a Debtor consultant, with

³ The Initial Proposed Windown Budget also contemplated using any unused pre-petition closing funds allocated for professionals under the professional fee carve-out and funded into Debtor’s counsel’s trust account.

the assistance of former RGI employees, to collect the Retained Receivables⁴⁴. The AR Proposal reflected that the Debtor expects to generate no less than approximately \$1,300,000 in recoveries net of the costs incurred in connection therewith (prior to funding of any wind down costs).

12. Since October 2, 2015 SWK has not engaged the Debtor in a discussion regarding the Initial Wind Down Budget. While SWK has had a couple of discussions with the Debtor regarding the AR Proposal, no agreement has been reached on how to monetize the Retained Receivables.

13. The Court should not let SWK turn its back on the Debtor's estate after it has reaped the benefits of a chapter 11 case that has been run principally for its benefit. Leaving the estate without cash to complete customary wind down tasks will only result in the case being converted to a chapter 7 trustee with the chapter 7 trustee being left to pick up the pieces. This is not how cases like this should be allowed to end. This is especially true in this case where the Debtor has operated better than projected during the course of this case. Attached as **Exhibit B** is an analysis of actual performance as compared to budgeted performance (the "**Actual to Budget Analysis**"). As the Actual to Budget Analysis reflects, cash flow (before budgeted restructuring costs) has been approximately \$1,125,000 better than what was contemplated in the Budget attached to the Final DIP Order. As a result the Debtor has had to draw down on the debtor in possession financing approximately \$733,000 less than originally contemplated.

14. Against this backdrop, SWK's unwillingness to fund a \$380,000 wind down budget (\$280,000 in excess of what SWK apparently believed it originally committed to under the post-default carve-out under the Final DIP Order) is petty.

⁴⁴ The AR Proposal contemplates that certain former RGI employees, including the Debtor's CFO Kevin Harris, might be retained and compensated by the consultant to assist in the collection efforts.

15. The Debtor wants to finish what it started. As a good corporate citizen, the Debtor believes that it is only fair to administrative creditors, employees, creditors, and others that remaining wind down tasks to be completed in a professional and timely manner. Converting the case to chapter 7 will impede this process, put the administration of the estate in the hands of people unfamiliar with the Debtor's operations and delay distributions to general unsecured creditors. The Debtor does not want to see that happen. Accordingly, the Debtor will agree to reduce its request to fund a wind down budget to \$325,000 (plus the unused portions of any pre closing budgeted professional fees).

Dated: October 9, 2015

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EXHIBIT A

(Wind Down Budget)

Response Genetics, Inc. Wind Down Budget**Scenario 1 - Estate Wind Down****Estimates for approximate 3-Month Wind Down Disbursements****Explanatory Notes**

Scenario 1 - "Estate Wind Down" - assumes bare-bones approach to winding down RGI estate with the goal of completing the wind down by December 31, 2015. Conway Mackenzie has estimated direct case administration professional fees based upon prior experiences in analogous situations involving chapter 11 estate wind downs. Other services estimates are based upon known anticipated issues for the estate, in addition to certain contingencies ("Other") held in reserve.

	<u>Scenario 1</u>	<u>Commentary</u>
<i>Direct Case Administration</i>		
Legal (PSZ)	\$ (100,000) (a)	- PSZ will use its remaining pre-closing carve out funds plus the \$100k to fund the wind down.
Financial Advisor (CM)	(125,000) (b)	- See footnote (b) below.
RGI Consultant	(15,000)	- K. Harris estimated monthly retainer of \$5,000.
<i>Subtotal, Direct Case Admin</i>	<u>(240,000)</u>	
<i>Other Services</i>		
2015 Tax Return Preparation & Filing	\$ (30,000)	- Estimate for preparation and filing of 2015 tax return.
BOD Fees	(30,000)	- Ultimate BOD composition and fees to be determined.
US Trustee Fees	(20,000)	- Estimated UST fees payable through case dismissal.
Other	(50,000)	- Reserve for additional legal advisors; subsidiary issues, employment lawsuits, and other non-budgeted admin items.
401k Wind Down	(10,000)	- Estimated fees for plan audit and plan administrator fees.
<i>Subtotal, Other Services</i>	<u>(140,000)</u>	
<i>Total Disbursements</i>	<u>\$ (380,000)</u>	

Notes

(a) PSZ intends to seek permission to use up to \$15,000 of its approved DIP budget allocation to offset other unpaid professional fees.

(b) Among other things, CM duties to include, claims validation, resolution of RGI liabilities (excluded from APA), issues with customers and vendors, coordination on tax matters, bankruptcy reporting to court and U.S. Trustee, transition issues with CGIX, payment processing and reporting to BOD.

EXHIBIT B

(Actual to Budget Analysis)

Response Genetics, Inc. Budget

CF Variance Reporting

9-Wks ended Oct 2, 2015

	9-Wk TOTAL DIP Forecast	9-Wk TOTAL Actual	9-Wk TOTAL Variance (\$)	9-Wk TOTAL Variance (%)
Week ended:	10/2/2015	10/2/2015	10/2/2015	10/2/2015
Beg. Cash Balance	\$ 752,232	\$ 752,232	\$ -	
Operating Receipts:				
Pharma	674,466	613,569	(60,897)	(9.0%)
DX	1,253,619	1,233,424	(20,195)	(1.6%)
Estimated Transaction Proceeds	-	-	-	- %
Total Collections	\$ 1,928,084	\$ 1,846,993	\$ (81,091)	(4.2%)
Operating Disbursements:				
Lab Supplies	(823,894)	(392,992)	430,902	52.3%
Payroll	(1,581,877)	(1,381,964)	199,914	12.6%
Vendors	(121,645)	(70,765)	50,880	41.8%
Contractors	(150,595)	(91,651)	58,944	39.1%
Rent	(211,941)	(115,925)	96,016	45.3%
Communications	(27,602)	(6,072)	21,530	78.0%
Outside Legal	(133,632)	(21,294)	112,338	84.1%
Leases	(47,042)	(58,013)	(10,971)	(23.3%)
Insurance - Business & Benefits	(471,563)	(343,404)	128,159	27.2%
SWK Interest Expense	-	-	-	- %
SVB Interest Expense	(20,645)	(20,601)	44	0.2%
Expense Reimbursement	(104,150)	(85,527)	18,623	17.9%
Miscellaneous	(136,054)	(35,059)	100,995	74.2%
Total Operating Disbursements	\$ (3,830,641)	\$ (2,623,268)	\$ 1,207,374	31.5%
Net Cash from Ops	\$ (1,902,557)	\$ (776,274)	\$ 1,126,282	59.2%
Restructuring Disbursements:				
<u>Advisors</u>				
Pachulski - legal	(650,000)	(550,000)	100,000	15.4%
Conway Mackenzie - Financial Advisor	(310,387)	(272,887)	37,500	12.1%
Canaccord - Investment Banker	(100,000)	(100,000)	-	- %
SWK Professional Fees	(179,444)	-	179,444	100.0%
SVB Professional Fees	(45,556)	-	45,556	100.0%
UCC Professional Fees	(43,750)	(37,500)	6,250	14.3%
<u>Other</u>				
Claims & Noticing Agent	(25,750)	(23,500)	2,250	8.7%
D&O Tail	(263,000)	(260,202)	2,798	1.1%
Crisis Manager	(32,778)	(30,556)	2,222	6.8%
KEIP - Insiders	-	-	-	- %
KEIP - Non-Insiders	-	-	-	- %
PTO Payments	-	-	-	- %
BDO Payments	(53,280)	(53,280)	-	- %
BOD Fees	-	-	-	- %
UST Fees	(10,400)	-	10,400	100.0%
Total Restructuring Disbursements	\$ (1,714,345)	\$ (1,327,925)	\$ 386,420	22.5%
Net Cash Flow including Restructuring	\$ (3,616,902)	\$ (2,104,199)	\$ 1,512,703	41.8%
Financing Activity:				
SVB Facility	-	-	-	- %
SWK Debt:				
DIP Facility	2,614,670	1,881,089	(733,580)	(28.1%)
Pre-Petition TL	500,000	500,000	-	- %
Ending Cash Balance After Financing	\$ 250,000	\$ 1,029,122	\$ 779,118	311.6%
Financial Debt - Post-Petition Status				
SVB Facility	\$ 1,465,662	\$ 1,465,662	\$ -	- %
SWK Debt:				
DIP Facility	2,614,670	1,881,089	(733,580)	28.1%
Pre-Petition TL	13,250,000	13,250,000	-	- %
Total SWK - Assumes Roll-Up	\$ 15,864,670	\$ 15,131,089	\$ (733,580)	4.6%