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Co-Counsel to the Debtors and Debtors in Possession

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
RICHMOND DIVISION**

)	
In re:)	Chapter 11
)	
TOYS “R” US, INC., <i>et al.</i> , ¹)	Case No. 17-34665 (KLP)
)	
Debtors.)	(Jointly Administered)
)	

**DEBTORS’ MOTION FOR ENTRY OF
AN ORDER (A) APPROVING THE DEBTORS’ SENIOR
EXECUTIVE INCENTIVE PLAN AND (B) GRANTING RELATED RELIEF**

The above-captioned debtors and debtors in possession (collectively, the “Debtors”)² respectfully state as follows in support of this motion (this “Motion”):

¹ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor’s federal tax identification number, are set forth in the *Order (I) Directing Joint Administration of Chapter 11 Cases and (II) Granting Related Relief* [Docket No. 78]. The location of the Debtors’ service address is One Geoffrey Way, Wayne, NJ 07470.

² A detailed description of the Debtors and their business, and the facts and circumstances supporting the Debtors’ chapter 11 cases, are set forth in greater detail in (i) the *Declaration of David A. Brandon, Chief Executive Officer of Toys “R” Us, Inc., in Support of Chapter 11 Petitions and First Day Motions* (the “Brandon Declaration”) and (ii) the *Declaration of Michael J. Short, Chief Financial Officer of Toys “R” Us, Inc., in Support of First Day Motions* (the “Short Declaration”) and together with the Brandon Declaration, the “First Day Declarations”), filed contemporaneously with the Debtors’ voluntary petitions for relief filed under chapter 11 of title 11 of the United

Relief Requested

1. The Debtors seek entry of an order, substantially in the form attached hereto as **Exhibit A** (respectfully, the “Order”), (a) approving the Debtors’ senior executive incentive plan (the “SEIP”), (b) authorizing the Debtors to implement the SEIP for the specified participants, and (c) allowing the Debtors’ payment obligations thereunder as administrative expenses of these estates. In support of this Motion, the Debtors submit the declaration of Brian L. Cumberland (the “Cumberland Declaration”), attached hereto as **Exhibit B**. The allocation of SEIP payments among the Debtors has not yet been determined. The Debtors will submit a supplemental declaration discussing the allocation methodology before the hearing.

Jurisdiction and Venue

2. The United States Bankruptcy Court for the Eastern District of Virginia (the “Court”) has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334 and the *Standing Order of Reference from the United States District Court for the Eastern District of Virginia*, dated July 10, 1984. The Debtors confirm their consent, pursuant to Rule 7008 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”), to the entry of a final order by the Court in connection with this Motion to the extent that it is later determined that the Court, absent consent of the parties, cannot enter final orders or judgments in connection herewith consistent with Article III of the United States Constitution.

3. Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

States Code (the “Bankruptcy Code”), on September 18, 2017 (the “Petition Date”). Capitalized terms used, but not otherwise defined in this Motion shall have the meanings ascribed to them in the First Day Declarations.

4. The bases for the relief requested herein are sections 363(b) and 503(c) of the Bankruptcy Code, Bankruptcy Rules 6004, and rule 6004-2 of the Local Rules of the United States Bankruptcy Court for the Eastern District of Virginia (the “Local Bankruptcy Rules”).

Preliminary Statement

5. The impact to the Debtors’ businesses following widespread media speculation in early September regarding the possibility of the filing of these chapter 11 cases, and the subsequent filing of these chapter 11 cases, has been profound. The general challenges in the ever-changing retail landscape have further compounded this impact, as competitors accelerate (and strengthen) their efforts to take market share. The stress on the Debtors’ operations (and its senior management team) has been lasting and continues, as efforts continue to stabilize the worldwide enterprise and position the company to win during the all-important holiday season, where approximately 40 percent of the Debtors’ annual net sales are realized.

6. The most important asset in this equation is the Debtors’ employees. Armed with capital from the recently approved debtor-in-possession financing facilities (the lenders thereunder, the “DIP Lenders”), it is the Debtors’ employees—and more particularly the senior management team—that must execute at this critical juncture and provide the foundation for a successful turnaround. Recognizing the vitality of incentivizing their workforce in the most challenging environment, the Debtors (at the direction of the Compensation Committee),³ designed, approved, and seek to implement a series of compensation plans that are focused on maximizing the enterprise value of these estates for the benefit of all stakeholders. As it relates to the Debtors’ senior executive team (the “SEIP Participants”), the Debtors seek approval of the

³ The members of the Compensation Committee of the Debtors’ board of directors (the “Compensation Committee”) include Matt Levin, Nate Taylor, Alan Miller, Richard Goodman, and Mohsin Meghji. None of these individuals would be entitled to any compensation under the SEIP.

SEIP, which provides incentive payments to the SEIP Participants to the extent they are able to achieve certain final targets. Timing, of course, is everything. Two weeks into the fourth quarter holiday season, now more than ever the senior management team must be properly motivated and incentivized to handle the panoply of responsibilities attendant to their two full-time jobs of leading the Debtors through this restructuring and, at the same time, implementing a worldwide strategy to increase sales following a near shut-down of operations just eight short weeks ago. The task at hand cannot be underestimated.

7. In consultation with their advisors, including the Alvarez & Marsal Compensation and Benefits team (the “Compensation Consultants”), the Debtors developed the SEIP for 17 senior members of the management team as part of an overall compensation package that is both consistent with the Debtors’ historical compensation programs and offers payments similar to its peers. The SEIP is designed specifically to incentivize Toys “R” Us’ employees to maximize the Debtors’ earnings before interest, depreciation and amortization (“EBITDA”). Using the EBITDA metric, SEIP payments are interpolated between “threshold,” “target,” and “stretch” goals. However, as the Debtors have explained to their key stakeholders (including the official committee of unsecured creditors (the “Creditor’s Committee”) and the ad hoc group of B4 lenders), the Debtors focus is on the “target” goal. The impact of these chapter 11 filings on the Debtors’ businesses and operations, coupled with the general retail environment, make the “stretch” goal very challenging to achieve. If the Debtors are at or below the “threshold” goal, no payment is contemplated. To the extent the “target” goal is realized, a total payment of \$16 million is contemplated.

8. Certain SEIP Participants received retention payments prior to the commencement of these chapter 11 cases in the amount of \$8.2 million. However, these payments are not part of

the SEIP. Rather, the retention payments were contemplated as part of the overall compensation package approved by the Debtors’ board of directors—each aspect constituting an essential part of the overall compensation package. Notably, individuals who received retention payments must return such payments if they voluntarily terminate their employment, or their employment is terminated for cause, with the Debtors within a year of the Petition Date.

9. The Debtors are hopeful that they can reach consensus for the SEIP amongst all major stakeholders. Consensus, however, does not exist at the time of the filing of this Motion. Nonetheless, the Debtors must proceed with the filing of this Motion to ensure that the SEIP can be presented on December 5, 2017—just three weeks before the Christmas holiday and well into the fourth quarter. The Debtors intend to continue discussions, diligence, and negotiations with the U.S. Trustee (as defined herein) and their major creditor constituencies in an effort to develop consensus for the SEIP and avoid unnecessary litigation.

SEIP Description

10. With the assistance of the Compensation Consultants, the Debtors identified 17 key members of the Debtors’ management team who are critical to the Debtors’ business operations and the maximization of value during and beyond these chapter 11 cases. The 17 key members of the team include:

SEIP Participants	
David Brandon	Chief Executive Officer and Chairman of the Board
Richard Barry	EVP Chief Merchandising Officer
Timothy Grace	EVP Global Talent Officer
Lance Wills	EVP Global Chief Technology Officer
Kevin Macnab	EVP President of TRU International
Carla Hassan	EVP Global Chief Marketing Officer
Michael Short	EVP Chief Financial Officer
Amy Von Walter	EVP Communications and Customer Care
Diane Preston	EVP U.S. Supply Chain
James Young	EVP General Counsel

Mark Johnson	EVP U.S. Marketplace Operations
Chetan Bhandari	Sr. Finance Director
Charles Knight	SVP Controller / Director of Certain Debtor Entities
Robert Zarra	VP International Controller / Director of Certain Debtor Entities
Matthew Finigan	VP Treasurer / Director of Certain Debtor Entities
Joel Tennenberg	VP Litigation & Regulatory Counsel / Director of Certain Debtor Entities
Antoinette Duah	VP Global Tax

11. The total amount available for payment under the SEIP on an annual basis is \$16 million at the Target Threshold (as described below). That amount could double if management attained its “stretch” goal—a result the Debtors will find very difficult to achieve.

12. The SEIP Participants are at the forefront of the Debtors’ most important endeavors: executing on daily performance and leading Toys “R” Us through its restructuring. The importance of having these individuals fully incentivized cannot be overstated.

13. The Debtors, through their Compensation Committee and Board of Directors, want to ensure these key members of the Debtors’ management team are properly incentivized to meet the significant challenges upon us and ahead, particularly in light of the uncertainties and additional workload resulting from the Debtors’ simultaneous efforts to revitalize their businesses and effectuate a global restructuring. With that goal in mind, the Debtors, and the Compensation Consultants, evaluated the existing compensation structure for the SEIP Participants and determined that the total compensation for the SEIP Participants, if the SEIP is approved, is within the range of relevant benchmarks in the retail industry.

Terms of the SEIP

14. The Debtors developed the terms of the SEIP to be commensurate with the Team Achievement Dividend Plan (the “TAD Plan”)—an incentive program the Debtors have had in place since 2015. The SEIP is similar to the TAD Plan, except that it has been modified to adjust

to the additional demands and lack of viable long-term incentives caused by the bankruptcy filing. Specifically, the SEIP provides for payouts on a quarterly basis, adjusts the EBITDA targets to take into account the current circumstances and operating environment following the filing of these chapter 11 cases, and changes the payout percentages solely to account for loss of other forms of long-term compensation.

15. Under the SEIP, SEIP Participants can earn a quarterly cash incentive payment, based on a percentage of each SEIP Participant's salary, but only if the Debtors achieve above certain targeted cumulative levels of EBITDA. The SEIP Participants receive no payment under the SEIP if the Debtors' EBITDA does not meet or only reaches the Minimum Threshold set forth below. The potential EBITDA thresholds are detailed below.

16. As the Debtors' EBITDA increases to the Target Threshold set forth below, the SEIP Participants' incentive payment increases incrementally to the target award amount. Similarly, in the unlikely scenario the Debtors' EBITDA exceeds the Target Threshold up to a particularly aggressive stretch goal (the "Maximum Threshold"), the SEIP Participants' incentive payment increases incrementally to twice the target award amount. The payouts under the SEIP are slightly higher than the Debtors' historical program to compensate employees for the discontinuation of the historical long-term compensation plans. Altogether, the payments under the SEIP, together with the retention payments described above, remain at or below market rates. The three annual threshold levels are summarized in the table below.

SEIP FY 2017 Global EBITDA Targets	
<i>Minimum Threshold</i>	\$484,000,000
<i>Target Threshold</i>	\$550,000,000
<i>Maximum Threshold</i>	\$616,000,000

17. These thresholds will only be used to measure performance in the fourth quarter of 2017. Although the SEIP Participants are working tirelessly to reach the Target Threshold, this

number will be difficult to achieve—and reaching the Maximum Threshold would be an exceptional result. The Debtors will consult with the DIP Lenders and Creditors’ Committee to set the applicable targets for the first three quarters of 2018 as soon as reasonably practicable. Ultimately, if the parties are unable to reach an agreement on subsequent thresholds, the Debtors will seek Court approval for them.

18. Because the Debtors’ fourth quarter accounts for a disproportionate amount of revenue compared to the other quarters, the metrics are weighted according to quarter. The current fourth quarter is weighted 40 percent and subsequent first, second, and third quarters are each weighted 20 percent.

19. The SEIP incentive payment is based on a percentage of a SEIP Participant’s salary based on their role. The table below summarizes title and associated salary percentage if the Target Threshold is met.

SEIP Target Percentage of Base Salary⁴	
<i>Executive Vice President and Above</i>	160%
<i>Senior Vice President</i>	90%
<i>Vice President</i>	75%

20. Thus, the SEIP is tied directly to the Debtors’ operational performance. In this regard, the SEIP incentivizes a targeted group of key employees to maximize the value of the Debtors’ estates to the benefit of all stakeholders. Indeed, the thresholds were deliberately set at challenging levels and reaching these targets will require a substantial effort from the Debtors’ management team—especially given the enormous market and bankruptcy-related challenges the Debtors are facing at the most critical time of the year for their businesses. If the SEIP Participants

⁴ The previous targets at each of these levels was 120 percent for the CEO, 100 percent for the EVPs, 80 percent for the SVPs, and 60 percent for the VPs. These targets were increased from the TAD Plan to account for the loss of long-term incentive compensation programs.

are indeed able to meet these challenge, the Debtors' submit it is wholly appropriate to reward them for their substantial efforts.

Basis for Relief

I. Applicable Legal Standard.

21. The Debtors' implementation of the SEIP is authorized under section 503 of the Bankruptcy Code. *See* 11 U.S.C. § 503(c)(3). Section 503(c)(3) prohibits certain transfers made to officers, managers, consultants, and others that are both outside the ordinary course of business and not justified by the facts and circumstances of the case. *See id.* Payments characterized as "incentive plans" have received approval under section 503(c)(3) from courts even where the key employees are officers. *In re Alpha Nat. Res., Inc.*, 546 B.R. 348, 359 (Bankr. E.D. Va. 2016) (approving an incentive based plan and noting that "every dollar earned under the KEIP is earned based on the financial and operational performance of the Debtors"); *In re Fieldstone Mortg. Co.*, 427 B.R. 357, 363 (Bankr. D. Md. 2010) (distinguishing incentive and retention plans). Because the SEIP is designed to incentivize the SEIP Participants to maximize the Debtors' EBITDA while operating in chapter 11 and not for the primary purpose of inducing insiders to remain with the Debtors' business, this Motion does not implicate section 503(c)(1) of the Bankruptcy Code. *See id.* (holding that incentive pay to senior managers is not governed by the provisions in section 503(c)(1) prohibiting retentive pay to insiders).

22. Section 503(c)(3) of the Bankruptcy Code provides, in relevant part, that "there shall be neither allowed nor paid . . . other transfers or obligations that are outside the ordinary course of business and not justified by the facts and circumstances of the case..." 11 U.S.C. § 503(c)(3).

23. A majority of courts agree that the requirement of section 503(c)(3) of the Bankruptcy Code that a transaction be "justified by the facts and circumstances of the case" is the

same as the business judgment standard under section 363(b) of the Bankruptcy Code. *See, e.g., Alpha Nat.*, 546 B.R. at 356 (collecting cases applying the business judgment standard to approve an insider compensation program); *In re Dana Corp.*, 358 B.R. 567, 576 (Bankr. S.D.N.Y. 2006) (“[S]ection 503(c)(3) gives the court discretion as to bonus and incentive plans, which are not primarily motivated by retention or in the nature of severance.”); *In re Global Home Prods., LLC*, 369 B.R. 778, 783 (Bankr. D. Del. 2007) (“If [the proposed plans are] intended to incentivize management, the analysis utilizes the more liberal business judgment review under § 363.”).

24. Section 363 of the Bankruptcy Code provides, in relevant part, that “[t]he [debtor], 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 use property of the estate when such use has a “sound business purpose” and when the use of the property is proposed in good faith. *See In re W.A. Mallory Co.*, 214 B.R. 834, 836 (Bankr. E. D. Va. 1997); *In re WBQ P’ship*, 189 B.R. 97, 102 (Bankr. E.D. Va. 1995).

25. Courts generally require a debtor to demonstrate that a valid business purpose exists for the use of estate property in a manner that is not in the ordinary course of business. *See In re Lionel Corp.*, 722 F.2d 1063, 1070-71 (2d Cir. 1983). Once the debtor has articulated a valid business justification, a presumption arises that the debtor’s decision was made on an informed basis, in good faith and in the honest belief the action was in the best interest of the company. *See In re Integrated Res., Inc.*, 147 B.R. 650, 656 (Bankr. S.D.N.Y. 1992). Furthermore, once “the debtor articulates a reasonable basis for its business decisions (as distinct from a decision made arbitrarily or capriciously), courts will generally not entertain objections to the debtor’s conduct.” *In re Johns-Manville Corp.*, 60 B.R. 612, 616 (Bankr. S.D.N.Y. 1986). The business judgment rule has vitality in chapter 11 cases and shields a debtor’s management from judicial

second-guessing. *See Integrated Res.*, 147 B.R. at 656; *Johns-Manville*, 60 B.R. at 615-616 (“[T]he Code favors the continued operation of a business by a debtor and a presumption of reasonableness attaches to a debtor’s management decisions.”). Thus, if a debtor’s actions satisfy the business judgment rule, then the transaction in question should be approved under section 363(b)(1).

26. Courts have found that a debtor’s use of reasonable performance-based payments and other incentives for employees is a valid exercise of a debtor’s business judgment. *See, e.g., Alpha Nat.*, 546 B.R. at 363 (approving the KEIP as a valid exercise of business judgment); *In re Am. W. Airlines, Inc.*, 171 B.R. 674, 678 (Bankr. D. Ariz. 1994) (noting that it is the proper use of a debtor’s business judgment to propose payments for employees who helped propel the debtor successfully through the bankruptcy process); *In re Interco Inc.*, 128 B.R. 229, 234 (Bankr. E.D. Mo. 1991) (stating that a debtor’s business judgment was controlling in the approval of a “performance/retention program”). Many courts have approved employee payment programs as valid exercises of business judgment. *See, e.g., In re Velo Holdings, Inc.*, 472 B.R. 201, 209 (Bankr. S.D.N.Y. 2012) (noting that Bankruptcy Code section 503(c) does not “foreclose a chapter 11 debtor from *reasonably* compensating employees, including ‘insiders,’ for their contribution to the debtors’ reorganization”); *Global Home Prods. LLC*, 369 B.R. at 778 (approving management incentive program for benefit of nine employees of the debtors provided that such employees fulfilled their obligations to the debtors through the closing of a sale of substantially all of the Debtors’ assets). While predominantly or purely retentive payments to insiders are expressly prohibited by the terms of section 503(c)(1), incentive payments that may have some retentive effect are permissible so long as they motivate senior management “to produce and increase the value of the estate.” *Dana Corp.*, 358 B.R. at 571.

27. Courts in this district have approved plans similar to the SEIP. *See, e.g., In re Alpha Nat. Res., Inc.*, No. 15-33896 (KRH) (Bankr E.D. Va. Jan. 27, 2016) [Docket No. 1387]; *In re Patriot Coal Corp.*, No. 15-32450 (KLP) (Bankr. E.D. Va. July 29, 2015) [Docket No. 672]; *In re James River Coal Company*, No. 14-31848 (KRH) (Bankr. E.D. Va. June 12, 2014) [Docket No. 376]; *In re AMF Bowling Worldwide, Inc.*, No. 12-36495 (Bankr. E.D. Va. Jan. 18, 2013) [Docket No. 394]; *In re Movie Gallery, Inc.*, No. 10-30696 (DOT) (Bankr. E.D. Va. Sept. 21, 2010) [Docket No. 1811]; *In re Roper Bros. Lumber Co.*, No. 09-38215 (KRH) (Bankr. E.D. Va. Feb. 25, 2010) [Docket No. 190]; *In re LandAmerica Fin. Grp., Inc.*, No. 08-35994 (KRH) (Bankr. E.D. Va. June 22, 2009) [Docket No. 1639]; *In re Circuit City Stores, Inc.*, No. 08-35653 (KRH) (Bankr. E.D. Va. Mar. 3, 2009) [Docket No. 2394]; *In re Rowe Cos.*, No. 06-11142 (SSM)(Bankr. E.D. Va. Nov. 9, 2006) [Docket No. 339]; *In re US Airways, Inc.*, No. 04-13819 (SSM) (Bankr. E.D. Va. June 15, 2005) [Docket No. 2268]; *In re NTELOS, Inc.*, No. 03-32094 (DOT)(Bankr. E.D. Va. June 9, 2003) [Docket No. 328].

II. The SEIP's Sound Business Purpose.

28. In determining if the structure of a compensation proposal meets the “sound business judgment” test, courts consider: (a) the relationship between the plan proposed and the results to be obtained; (b) the relative cost of the plan; (c) the scope of the plan; (d) whether the plan is consistent with industry standards; (e) the due diligence in investigating the need for a plan; and (f) whether the debtor received independent counsel. *Dana Corp.*, 358 B.R. at 576-77.

A. The SEIP Will Drive Results that Benefit All Stakeholders.

29. The Debtors and the Compensation Consultants developed the SEIP with the goal of motivating the SEIP Participants for the benefit of the Debtors' creditors and other stakeholders. As such, the SEIP is focused exclusively on incentivizing the SEIP Participants to increase profitability, which will provide tangible, meaningful benefits to the Debtors and their estates.

Specifically, the SEIP is tied to the Debtors' EBITDA, which in turn aligns with every stakeholder's interest in maximizing value available for the Debtors' estates. No payments will be made under the SEIP if the performance metrics are not met. Accordingly, the SEIP incentivizes the SEIP Participants to maximize value, which benefits all stakeholders.

30. In leading the Debtors' restructuring efforts, the SEIP Participants have shouldered responsibilities well beyond their ordinary duties without a corresponding increase in compensation. The SEIP thus rewards the SEIP Participants for achieving strong business performance while guiding the Debtors through these chapter 11 cases.

B. The Cost of the SEIP Is Reasonable Relative to Revenue and Other Plans in the Retail Industry.

31. Courts take a holistic view of compensation packages and their relative costs. *Dana Corp.*, 358 B.R. at 571. Factors for consideration include the cost of the plan relative to revenue, and relative to other plans in the relevant industry. *See In re Borders Group, Inc.*, 453 B.R. 459, 476 (Bankr. S.D.N.Y. 2011).

32. Here, the total payout for meeting the SEIP's target is \$16 million on an annual basis. These amounts are commensurate with the size of the Debtors' operations (revenues of approximately \$11.5 billion in 2016) and the monumental tasks being asked of the SEIP Participants. As set forth in the Cumberland Declaration, the costs associated with such compensation are more than justified by the benefits that the Debtors will realize by creating appropriate incentives for the SEIP Participants. And the SEIP Participants only receive these payments to the extent they drive performance that will redound to the estate.

C. The Scope of the SEIP Is Appropriate.

33. The scope of an incentive plan under section 503(c)(3) of the Bankruptcy Code may be limited to a small group of key management, particularly where they are the group "that will

effectively guide the [Debtor] through bankruptcy.” *Borders Group, Inc.*, 453 B.R. at 475-6. Here, the Debtors identified a group of 17 individuals who are critical to the Debtors’ operations. *See, e.g., Alpha Nat.*, 546 B.R. at 360 (finding that an incentive plan covering the 15 individuals “necessary for the development and implementation of the Debtors’ business plan” was appropriate).

34. For the foregoing reasons, in consideration of the facts and circumstances of these cases, implementation of the SEIP is an exercise of the Debtors’ sound business judgment and would be in the best interests of the Debtors, their estates, employees, and stakeholders.

D. The SEIP Is Consistent with Industry Standards.

35. As discussed in the Cumberland Declaration, the SEIP comports with retail industry standards.

36. To evaluate an appropriate compensation structure for the SEIP Participants, the Compensation Consultants gathered external market compensation data from several sources, encompassing a representative database of compensation information for the Debtors’ retail industry and labor market of executives. The Compensation Consultants determined that current overall compensation for the SEIP Participants generally fell well below applicable benchmarks. The Compensation Consultants determined, however, that base salaries plus a retention payments plus the potential SEIP payout for the SEIP Participants would fall within the appropriate range of total compensation for the Debtors’ industry, particularly considering the additional duties and uncertainties faced by the SEIP Participants and the challenging goals necessary to achieve the SEIP award.

E. The Debtors Exercised Due Diligence in Investigating the Need for the SEIP and Designing the SEIP.

37. The Debtors proposed the SEIP after discussions with the Compensation Consultants and after careful consideration. In addition, the SEIP relies upon significant input from the Debtors' legal and financial advisors. Prior to filing this Motion, the Debtors consulted with their advisors and previewed the SEIP with the Creditors' Committee, the DIP Lenders, and the U.S. Trustee.

F. The Debtors Relied on Advisors to Design the SEIP.

38. The involvement of independent professional advice in the formulation of a key employee incentive program weighs in favor of the program being approved. *See, e.g., In re Velo Holdings, Inc.*, 472 B.R. 201, 213 (Bankr. S.D.N.Y. 2012) (approving an incentive program developed by independent financial advisors); *In re Dewey & Leboeuf LLP*, 2012 Bankr. LEXIS 3484, *16-17 (Bankr. S.D.N.Y. July 30, 2012) (approving an incentive program developed by debtor's counsel and CRO). In this case, the Debtors employed the Compensation Consultants to evaluate the current incentive program and recommend modifications to that program to ensure that it is aligned with the market and provides appropriate incentives to management. The Debtors' financial advisors played a significant role in developing the SEIP, including EBITDA target thresholds, as well. In addition, the SEIP was approved by the Compensation Committee before being submitted, and subsequently approved, by the Debtors' board of directors. Notably, the Compensation Committee includes two independent directors, Alan Miller and Mohsin Meghji, with a combined restructuring experience of more than 50 years.

III. The SEIP is Consistent with Previously Approved Employee Incentive Plans.

39. The SEIP is consistent with other programs of its type that have been approved by courts in cases following the passage of the Bankruptcy Abuse Prevention and Consumer

Protection Act of 2005. Many courts have approved of incentive programs that reward payments based on achieving performance thresholds. *See, e.g., In re Energy Future Holdings Corp.*, No. 14-10979 (CSS) (Bankr. D. Del. Oct. 15, 2014) (noting that the debtors' incentive plan based on EBITDA targets "define the gold standard"); *Dana Corp.*, 358 B.R. at 583 (approving an incentive program based on cutting costs and maximizing EBITDAR, despite not reaching past years' EBITDAR levels); *Borders Group, Inc.*, 453 B.R. at 472 (approving an incentive program based on cost reductions, increases in the distribution to unsecured creditors, and speed in exiting bankruptcy); *In re Mesa Air Group, Inc.*, 2010 Bankr. LEXIS 3334, 2-3 (Bankr. S.D.N.Y. Sept. 24, 2010) (approving an incentive program based on maintaining flight schedules and improving financial performance).

40. Courts regularly approve of incentive programs with graduated cash rewards. *See, e.g., Velo Holdings, Inc.*, 472 B.R. at 210-211 (approving an incentive program for insiders based on meeting the terms of a DIP loan and selling businesses to third parties); *In re Nobex Corp.*, 2006 Bankr. LEXIS 417 (Bankr. D. Del. Jan. 19, 2006) (approving sale-related incentive pay for insiders); *In re Dewey & Leboeuf LLP*, 2012 Bankr. LEXIS 3484 at *16-17 (approving an incentive plan linking payments to collection on receivables). The distinguishing characteristic of an appropriate SEIP is motivation: "when a plan is designed to motivate employees to achieve specified performance goals, it is primarily incentivizing, and thus not subject to section 503(c)(1)." *In re Residential Capital, LLC*, 478 B.R. 154, 172 (Bankr. S.D.N.Y. 2012).

41. In this case, the Debtors' proposed SEIP has no guaranteed payments to the SEIP Participants. The SEIP Participants are eligible only if the Debtors meet the EBIDTA goals. Accordingly, the Debtors have a "sound business purpose" for, and have properly exercised their business judgment in developing, the SEIP. In so doing, they have satisfied the standards of

section 363(b) and the “facts and circumstances” test set forth in section 503(c)(3) of the Bankruptcy Code.

Waiver of Bankruptcy Rule 6004(h)

42. To implement the foregoing successfully, the Debtors seek a waiver of the 14-day stay of an order authorizing the use, sale, or lease of property under Bankruptcy Rule 6004(h).

Notice

43. The Debtors will provide notice of this Motion via first class mail and email (where available) to: (a) the Office of the United States Trustee for the Eastern District of Virginia (the “U.S. Trustee”), Attn: Robert B. Van Arsdale and Lynn A. Kohen; (b) the Creditors’ Committee and the advisors and counsel thereto; (c) DIP ABL Agent and the advisors and counsel thereto; (d) DIP Taj Term Loan Agent and the advisors and counsel thereto; (e) DIP Delaware Term Loan Agent and the advisors and counsel thereto; (f) the indenture trustee for the TRU Taj 12.00% Senior Notes and the advisors and counsel thereto; (g) the administrative agent for the prepetition Secured Revolving Credit Facility and the advisors and counsel thereto; (h) the administrative agent for the prepetition Secured Term Loan B Facility and the advisors and counsel thereto; (i) the prepetition administrative agent for the Propco I Unsecured Term Loan Facility and the advisors and counsel thereto; (j) the agent for the Propco II Mortgage Loan and the advisors and counsel thereto; (k) the agent for the Giraffe Junior Mezzanine Loan and the advisors and counsel thereto; (l) the administrative agent for the prepetition European and Australian Asset-Based Revolving Credit Facility and the advisors and counsel thereto; (m) the administrative agent for the Senior Unsecured Term Loan Facility and the advisors and counsel thereto; (n) the indenture trustee for the Debtors’ 7.375% Senior Notes and the advisors and counsel thereto; (o) the indenture trustee for the Debtors’ 8.75% Unsecured Notes and the advisors and counsel thereto; (p) counsel to the ad hoc group of the Term B-4 Holders; (q) counsel to the Ad Hoc Committee of Taj Noteholders;

(r) the monitor in the CCAA proceeding and counsel thereto; (s) the Debtors' Canadian Counsel, (t) the Internal Revenue Service; (u) the office of the attorneys general for the states in which the Debtors operate; (v) the Securities and Exchange Commission; and (w) any party that has requested notice pursuant to Bankruptcy Rule 2002. The Debtors submit that, in light of the nature of the relief requested, no other or further notice need be given.

No Prior Request

44. No prior request for the relief sought in this Motion has been made to this or any other court.

[Remainder of page intentionally left blank.]

WHEREFORE, the Debtors respectfully request that the Court enter the Order granting the relief requested herein and such other relief as the Court deems appropriate under the circumstances.

Richmond, Virginia

Dated: November 14, 2017

/s/ Michael A. Condyles

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Exhibit A

Proposed Order

the Debtors to make payments to certain management employees under the SEIP, (c) granting administrative expense priority status to all payment obligations of the Debtors under the SEIP, and (d) granting related relief, all as more fully set forth in the Motion; and the Court having considered the Cumberland Declaration; and the upon having found that it has jurisdiction to consider this Motion and the relief requested therein in accordance with 28 U.S.C. §§ 157 and 1334; and the Court having found that consideration of the Motion and the relief requested therein is a core proceeding pursuant to 28 U.S.C. § 157(b)(2) and that it may enter a final order consistent with Article III of the United States Constitution; and the Court having found that venue is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409; and the Court having found that the Debtors provided due and proper notice of the Motion that is adequate and appropriate under the particular circumstances; and the Court having held a hearing to consider the relief requested in the Motion (the "Hearing"); and upon consideration of the record of the Hearing, and all proceedings had before the Court; and the Court having found and determined that the relief sought in the Motion is in the best interests of the Debtors' estates, their creditors, and other parties in interest, and that the legal and factual bases set forth in the Motion and the Cumberland Declaration and at the Hearing establish just cause for the relief granted herein; and upon all of the proceedings had before the Court; and any objections to the relief requested herein having been withdrawn or overruled on the merits; and after due deliberation and sufficient cause appearing therefor, it is

HEREBY ORDERED THAT:

1. The Motion is granted as set forth in this Order.
2. The SEIP is approved in its entirety.
3. Any and all payment obligations of the Debtors under the SEIP shall constitute administrative expenses of the estates.

4. With respect to EBITDA metrics for quarter one, quarter two, and quarter three of 2018, which have not yet been determined, the Debtors may implement such metrics once determined, in consultation with the DIP Lenders and Creditors' Committee.

5. This Order shall not apply to Debtor Toys "R" Us (Canada) Ltd. Toys "R" Us (Canada) Ltee ("Toys Canada"). Toys Canada shall be permitted to maintain, implement and perform such compensation programs and arrangements as may be authorized or permitted in proceedings in respect of Toys Canada pursuant to the *Companies' Creditors Arrangement Act* (Canada) pending before the Ontario Superior Court of Justice (Commercial List).

6. Notice of the Motion as provided therein shall be deemed good and sufficient notice of such Motion and the requirements of Bankruptcy Rule 6004(a) are satisfied by such notice.

7. Notwithstanding Bankruptcy Rule 6004(h), the terms and conditions of this Order are immediately effective and enforceable upon its entry.

8. The Debtors are authorized to take all actions necessary to effectuate the relief granted in this Order.

9. This Court retains exclusive jurisdiction with respect to all matters arising from or related to the implementation, interpretation, and enforcement of this Order.

Dated: _____, 2017
Richmond, Virginia

United States Bankruptcy Judge

WE ASK FOR THIS:

/s/ Michael A. Condyles

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Co-Counsel to the Debtors and Debtors in Possession

CERTIFICATION OF ENDORSEMENT
UNDER LOCAL BANKRUPTCY RULE 9022-1(C)

Pursuant to Local Bankruptcy Rule 9022-1(C), I hereby certify that the foregoing proposed order has been endorsed by or served upon all necessary parties.

/s/ Michael A. Condyles

Exhibit B

Cumberland Declaration

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
RICHMOND DIVISION**

In re:)	
)	Chapter 11
TOYS “R” US, INC., <i>et al.</i> , ⁷)	Case No. 17-34665 (KLP)
Debtors.)	(Jointly Administered)
)	

**DECLARATION OF BRIAN L. CUMBERLAND
IN SUPPORT OF DEBTORS’ MOTION FOR ENTRY
OF AN ORDER (A) APPROVING THE DEBTORS’ SENIOR
EXECUTIVE INCENTIVE PLAN AND (B) GRANTING RELATED RELIEF**

I, Brian L. Cumberland, hereby declare under penalty of perjury as follows:

1. I am a National Managing Director of the Compensation & Benefits practice at Alvarez & Marsal North America, LLC (“A&M”), a financial advisory firm. A&M has been engaged as a financial advisor to Toys “R” Us, Inc. and certain of its direct and indirect subsidiaries as debtors and debtors in possession (collectively, the “Debtors”) since July 26, 2017.

2. I have been employed by A&M with over 25 years of experience in the field. My responsibilities at A&M primarily involve consulting with corporate clients, specifically with regard to executive compensation. In this capacity, I have worked with numerous Fortune 1000 companies to advise on their management-compensation strategies, programs, and pay levels. I have participated in the development and design of over 100 management-incentive plans for companies inside and outside of chapter 11. Prior to joining A&M, I led KPMG’s Compensation

⁷ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor’s federal tax identification number, are set forth in the *Order (I) Directing Joint Administration of Chapter 11 Cases and (II) Granting Related Relief* [Docket 78]. The location of the Debtors’ service address is One Geoffrey Way, Wayne, New Jersey 07470.

and Benefits Group for the Southwest United States, and I was also a member of KPMG's National Tax Practice in Washington, D.C.

3. I submit this declaration (this "Declaration") to support the relief requested in the *Debtors' Motion for Entry of an Order (A) Approving the Debtors' Senior Executive Incentive Plan and (B) Granting Related Relief* (the "Motion").⁸ Unless otherwise indicated, all facts set forth in this declaration are based upon: (a) my personal knowledge of the Debtors' operations and financial performance; (b) information learned from my review of relevant financial and operational data regarding the Debtors; (c) information received from members of the Debtors' management or their advisors; and (d) my 25 years of compensation experience. I am not a participant in any of the compensation programs described herein and in the Motion, and I will receive no payments under such programs.

4. Based on my analysis, I have concluded that the payouts proposed under the SEIP, and the allocations thereof, are reasonable and consistent with market practice. This conclusion is based upon a comparison (discussed below) of the design structures and proposed payouts under the SEIP with market data regarding incentive payments for other companies going through chapter 11. I have also concluded that the structure of the SEIP, including the metrics used within, are consistent with other plans within the retail industry.

5. I am authorized to submit this declaration on behalf of the Debtors, and, if I were called upon to testify, I could and would testify competently to the facts set forth herein.

⁸ I have reviewed the Motion. Capitalized terms used but not defined herein have the meaning ascribed to them in the Motion.

Importance of the SEIP Participants

6. The Debtors' senior management team—and specifically, the 17 SEIP Participants—play an indispensable role in the performance of the business. The Debtors are two weeks into the fourth quarter holiday season, and during this critical time the senior management team must be properly incentivized to lead the Debtors through this restructuring and, at the same time, implement a world-wide strategy to increase sales. Accordingly, the Debtors have an immediate need to implement the SEIP and provide incentive opportunities that will enable the Debtors to achieve their business and restructuring goals.

Overview and Necessity of the SEIP

7. The SEIP Participants have worked extensive hours, shouldering responsibilities that are well above and beyond their day-to-day duties outside of chapter 11. On an extremely short timeline, the SEIP Participants have, among other things, been called upon to respond to myriad complex issues to ensure the continued viability of their businesses, including negotiating the debtor in possession financing facilities and the cash flow projections and required budgets related thereto, responding to and communicating with their numerous creditors including the Debtors' valuable trade partners, expending significant time and energy complying with bankruptcy-related reporting obligations, responding to discovery requests, and formulating and negotiating trade agreements with their critical vendors.

8. At the same time, the SEIP Participants, consisting of those employees that have the greatest ability to influence the Debtors' financial performance, have little clarity regarding their post-restructuring employment status or even who the future owners of the business will be. These employees have already experienced dramatically increased workloads as a result of operating in chapter 11 and the Debtors' related restructuring efforts. As a result, it is critical that these employees be appropriately incentivized to drive performance for all stakeholders.

9. Recognizing that achieving a successful restructuring would require appropriately incentivizing the Debtors' senior management, the Debtors retained A&M, in part, to assist the Debtors' management and the board of directors of Toys "R" Us, Inc. in designing a management incentive plan to provide employees instrumental to the success of the Debtors' restructuring efforts and operational performance with appropriate compensation.

10. I am not a participant in the SEIP, and I played a pivotal role in formulating and negotiating its terms on behalf of the Debtors. The development of an effective management incentive plan is essential under the circumstances to improve the Debtors' financial and operational performance and achieve a value-maximizing restructuring on an accelerated timeline, and the SEIP is an effective plan in this regard.

11. In summary, the payments contemplated under the SEIP are reasonable and will adequately and fairly incentivize the SEIP Participants. The Debtors, in consultation with A&M and their other advisors, conducted extensive due diligence and invested a great deal of thought into the best way to structure the SEIP to ensure that it is competitive, market-based, and, above all, effective.

Development of the SEIP

12. The Debtors historically sought to attract and motivate talented executives to achieve strong financial and operational results. To this end, the Debtors compensated members of their senior management team not only through base salary, but also through cash bonuses and long-term equity programs that tied financial rewards to the Debtors' financial and operational performance.

13. Prior to the commencement of these chapter 11 cases, the Debtors recognized that their senior management team would play a crucial role in driving the Debtors' business performance and successfully implementing the Debtors' restructuring strategy. Thus, the

Debtors, with the assistance of their advisors, developed the SEIP to properly incentivize the senior management team during this crucial and challenging time and to ensure its competitiveness with the Debtors' market competitors.

14. The Debtors' SEIP covers 17 members of the Debtors' senior management (the "SEIP Participants").⁹ The SEIP Participants have devoted, and will continue to devote, significant attention and effort to addressing the Debtors' restructuring initiatives while simultaneously running the Debtors' global businesses. A successful restructuring of the Debtors depends on the SEIP Participants' success on these parallel paths. The SEIP Participants comprise the individuals with the greatest ability to influence the performance of the Debtors' business. Accordingly, the Debtors have an immediate need to implement the SEIP. Doing so will help the Debtors achieve their near- and long-term operating performance and restructuring goals. Before the SEIP was submitted and approved by the Debtors' Board of Directors, it was approved by the Compensation Committee of the Debtors' Board of Directors—all of whom took are not potential SEIP Participants.

Terms of the SEIP

15. The Debtors developed the terms of the SEIP to be commensurate with the Team Achievement Dividend Plan (the "TAD Plan")—an incentive program the Debtors have had in place since 2015. The SEIP is similar to the TAD Plan, except that it has been modified to adjust to the additional demands and lack of viable long-term incentives caused by the bankruptcy filing. Specifically, the SEIP provides for payouts on a quarterly basis, adjusts the EBITDA targets to take into account the current circumstances and operating environment following the filing of these

⁹ I understand all of the SEIP Participants likely are considered to be "insiders" as defined in section 101(31) of the Bankruptcy Code.

chapter 11 cases, and changes the payout percentages to account for loss of other forms of long-term compensation.

16. To appropriately incentivize the SEIP Participants and maximize the value of the Debtors’ businesses, the SEIP Participants’ compensation is tied to achieving certain performance levels—“Minimum,” “Target,” and “Maximum”—related to the global EBITDA metric (collectively, the “Threshold Levels”). The Threshold Level goals for the performance metric were determined based on the DIP Budget and adjusted for business impacts around the filing and post-filing. The Debtors adjusted for the following factors : (a) supply chain disruption due to news of the Debtors’ bankruptcy filing; (b) difficulty of securing allowances from vendors at levels consistent with prior allowances; (c) continued disruption to the retail industry; and (d) increased gift card redemptions and decreased gift card purchases. The Threshold Levels are summarized in the table below.¹⁰

SEIP Global FY 2017 EBITDA Threshold Levels	
<i>Minimum Threshold</i>	\$484,000,000
<i>Target Threshold</i>	\$550,000,000
<i>Maximum Threshold</i>	\$616,000,000

17. The Threshold Levels are calculated on an annual basis. As described in further detail below, achievement of the Threshold Levels under the SEIP—which are not easy-to-achieve milestones—will require the SEIP Participants’ best efforts to achieve and, if met, will significantly benefit the Debtors’ stakeholders. Indeed, to meet the targets, the Debtors will need

¹⁰ The Debtors will consult with the DIP Lenders and Creditors’ Committee to set the applicable targets for the first three quarters of 2018 as soon as reasonably practicable. Ultimately, if the parties are unable to reach an agreement on subsequent thresholds, the Debtors will seek Court approval for them.

to perform better than current trends both in terms of same stores sales and margin rate. In addition, the Company will need to successfully negotiate significant vendor allowances in the fourth quarter. Given these hurdles, the Maximum Threshold is most likely unattainable. As such, the scope of the SEIP is fair and reasonable, and importantly, does not discriminate unfairly among SEIP Participants.

18. If the Debtors do not reach the Minimum Threshold, no payments will be made pursuant to the SEIP. The Target Threshold is the level at which the SEIP Participants will receive the target award due under the SEIP. In the unlikely scenario the Debtors hit the Maximum Threshold, the SEIP Participants would receive twice the target award due under the SEIP. The award is computed as a percentage of the SEIP Participant’s salary based on their role. The table below summarizes title and associated salary percentage if the Target Threshold is met.

SEIP Target Percentage of Base Salary	
<i>Executive Vice President and Above</i>	160%
<i>Senior Vice President</i>	90%
<i>Vice President</i>	75%

19. The Debtors’ business is cyclical and depends heavily on the results of the holiday shopping season in the fourth quarter. As such, the SEIP is designed to reflect that trend—the Threshold Level is weighted by quarter. The current fourth quarter is weighted 40 percent and subsequent first, second, and third quarters are each weighted 20 percent. This aligns the terms of the SEIP with the Debtors’ natural business cycle and helps ensure that the SEIP Participants are focused on driving bottom-line performance for the benefit of all stakeholders.

A&M's Independent Review of the Reasonableness of the SEIP

20. I and my team at A&M have assessed and discussed the Debtors' operational history and challenges with the Debtors and their advisors. I have a thorough understanding of the Debtors' key executive compensation arrangements and their recent performance. In the past few years, regular annual incentives have not been earned and the value of historical long-term incentive awards is highly uncertain.

21. The estimated total direct compensation of each of the SEIP Participants fell within a range of competitive practice for comparable positions when including the SEIP amounts at the target level. However, without the SEIP, the total direct compensation of each SEIP Participant, inclusive of the retention payments made prepetition, will be well below the competitive medians. The SEIP as structured creates the incentive for the key executives to perform and achieve the desired goals and also works to close the gap between the executives' total compensation and the competitive practice for comparable positions.

22. To evaluate the competitiveness and reasonableness of the SEIP, data were drawn from the SEIPs of companies similar to the Debtor. A&M compared the SEIP to other incentive plans implemented since the enactment of the Bankruptcy Abuse and Consumer Protection Act of 2005 by companies that are either in the retail industry or had prepetition assets of greater than \$1 billion and prepetition revenue of greater than \$3.5 billion. A&M also compared the SEIP to incentive plans by peer companies outside of bankruptcy and historical total compensation targets for the executives. The data set forth in **Exhibit 1** attached hereto illustrates that the proposed SEIP falls within the range of reasonable market practice for the top five SEIP Participants. The proposed compensation for the other SEIP Participants also falls within the range of reasonable market practice.

23. I have reviewed the overall structure of the SEIP, its performance goals, the participants and the target payout levels. Based on my review and analysis, the overall design and structure of the SEIP, along with the proposed target incentive opportunities, are consistent with market practice and will incentivize the SEIP Participants to achieve the Debtors' operating and financial goals.

24. Accordingly, and for the reasons set forth in this Declaration, I believe that the Debtors' SEIP is reasonable in design and structure, and provides reasonable award opportunities as compared to the Debtors' peers.

[Remainder of the page intentionally left blank.]

Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge, information and belief.

Dated: November 14, 2017
Dallas, Texas

s/ Brian L. Cumberland

Brian L. Cumberland
Managing Director
Alvarez & Marsal North America, LLC

Exhibit 1

Executive Compensation Comparables