

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:)
) Chapter 11
NOVAN, INC., *et al.*,¹)
) Case No. 23-10937 (LSS)
Debtors.)
) (Joint Administration Requested)
)
_____)

**DEBTORS’ MOTION FOR ENTRY OF INTERIM AND FINAL ORDERS
(I) AUTHORIZING DEBTORS TO (A) PAY CERTAIN PREPETITION
EMPLOYMENT OBLIGATIONS AND (B) MAINTAIN EMPLOYEE
BENEFITS PROGRAMS AND (II) GRANTING RELATED RELIEF**

The above-captioned debtors and debtors in possession (the “Debtors”) hereby file this motion (the “Motion”) for the entry of interim and final orders, substantially in the forms attached hereto as **Exhibit A** (the “Proposed Interim Order”) and **Exhibit B** (the “Proposed Final Order,” and together with the Proposed Interim Order, the “Proposed Orders”), (i) authorizing the Debtors to pay all amounts required under or related to the Prepetition Employee Obligations (as defined below) and maintain their employee compensation practices, programs, benefits, and policies (as they may be modified, amended, or supplemented from time to time in the ordinary course of the Debtors’ business, as were in effect on the Petition Date (as defined below); and (ii) granting related relief. In support of this Motion, the Debtors submit the *Declaration of Paula Brown Stafford in Support of Debtors’ Chapter 11 Petitions and First Day Motions* (the “First Day Declaration”).² In further support of this Motion, the Debtors respectfully represent as follows:

¹ The Debtors in these chapter 11 cases, along with the last four digits of the Debtors’ federal tax identification number (if applicable), are: Novan, Inc. 7682 and EPI Health, LLC 9118. The corporate headquarters and the mailing address for the Debtors is 4020 Stirrup Creek Drive, Suite 110, Durham, NC 27703.

² Capitalized terms used but not defined herein are defined in the First Day Declaration.



JURISDICTION AND VENUE

1. The United States Bankruptcy Court for the District of Delaware (this “Court”) has jurisdiction over these chapter 11 cases and this Motion pursuant to 28 U.S.C. §§ 157 and 1334 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware, dated February 29, 2012. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2).

2. Pursuant to rule 9013-1(f) of the Local Rules of Bankruptcy Practice and Procedure of the United States Bankruptcy Court for the District of Delaware (the “Local Rules”), the Debtors consent to the entry of a final order with respect to this Motion if it is later determined that the Court, absent consent of the parties, cannot enter final orders or judgments consistent with Article III of the United States Constitution.

3. Venue of these chapter 11 cases (the “Chapter 11 Cases”) and this Motion in this District is proper under 28 U.S.C. §§ 1408 and 1409.

4. The statutory and legal predicates for the relief requested herein are sections 105(a), 363(b), 507(a) and 541 of title 11 of the United States Code, 11 U.S.C. §§ 101–1532 (the “Bankruptcy Code”), Rules 6003 and 6004 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”), and Local Rule 9013-1.

BACKGROUND

5. On the date hereof (the “Petition Date”), the Debtors each filed with the Court a voluntary petition for relief under chapter 11 of the Bankruptcy Code.

6. The Debtors are authorized to operate their businesses and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. As of the date hereof, no trustee, examiner, or official committee of unsecured creditors has been appointed in these Chapter 11 Cases.

7. Additional factual background regarding the Debtors, including their business operations, capital structure, and the events leading to the filing of these Chapter 11 Cases, is set forth in detail in the First Day Declaration, which is fully incorporated into this Motion by reference.

RELIEF REQUESTED

8. The Debtors request entry of the Proposed Orders authorizing, but not directing, the Debtors to: (i) pay all prepetition wages, salaries and compensation to Employees (as defined below) and all related administrative and incidental costs, as well as all prepetition employee benefits (all as described below and, collectively, the “Compensation Obligations”); (ii) pay all employment, unemployment, Social Security, and federal, state, and local taxes relating to the Compensation Obligations, whether withheld from wages or paid directly by the Debtors to governmental authorities (collectively, “Payroll Taxes”), and make other payroll deductions, including, but not limited to, retirement and other employee benefit plan contributions, and voluntary deductions (all as described below and, collectively with the Payroll Taxes, the “Payroll Deduction Obligations” and, collectively with the Compensation Obligations, the “Prepetition Employee Obligations”); and (iii) honor and continue the Debtors’ prepetition programs, policies and practices as described in this Motion in the ordinary course of business (the “Compensation and Benefits Programs”).

9. To fulfill these commitments, the Debtors request entry of the Proposed Interim Order, authorizing the Debtors to pay Prepetition Employee Obligations in an amount not to exceed \$225,000.00 (the “Interim Amount”), subject to the \$15,150 statutory cap per current or former employee established by sections 507(a)(4) and (a)(5) of the Bankruptcy Code. Further, the Debtors request that this Court authorize applicable banks and other financial institutions to receive, process, honor, and pay all checks, drafts, electronic fund transfers or other forms of

payment drawn or issued on the Debtors' bank accounts before the Petition Date for Prepetition Employee Obligations (or to reissue checks, drafts, electronic fund transfers or other forms of payment drawn or issued on the Debtors' bank accounts, as may be necessary), and authorize, but not direct, the banks and financial institutions to rely on the Debtors' representations as to which checks, drafts, electronic fund transfers or other forms of payment drawn or issued on the Debtors' bank accounts are subject to this Motion; provided that sufficient funds are on deposit in the applicable bank accounts to cover such payments.³

10. The prepetition amounts sought to be paid by this Motion are discussed in greater detail below and are summarized in the following chart:

Prepetition Obligations	Interim Amount	Final Amount
Prepetition Compensation Obligations	\$141,302.68	\$141,302.68
Prepetition Withholding Obligations	\$64,000.00	\$64,000.00
Total Prepetition Employee Obligations	\$205,302.68	\$205,302.68

THE DEBTORS' EMPLOYEES

11. As of the Petition Date, the Debtors employ approximately thirty-eight (38) full-time employees and one (1) part-time employee (collectively, the "Employees") in the United States. The workforce is divided among the Debtors' headquarters located in Durham, North Carolina, and additional offices in Charleston, South Carolina. In addition, a majority of the of

³ Contemporaneously with the filing of this Motion, the Debtors have filed the *Debtors' Motion for Interim and Final Orders (I) Authorizing the Debtors to (A) Continue Their Existing Cash Management System, (B) Honor Certain Prepetition Obligations Related Thereto, (C) Maintain Their Bank Accounts and Existing Business Forms, (D) Implement Changes to the Existing Cash Management System as Necessary, and (E) Continue Ordinary Course Intercompany Transactions, (II) Waiving the Requirements of 11 U.S.C. § 345(b) and the U.S. Trustee's Operating Guidelines, and (III) Granting Related Relief* (the "Cash Management Motion"), which seeks, among other things, authority to continue using the Debtors' cash management system, including their Bank Accounts (as defined in the Cash Management Motion).

the Debtors' current Employees are salaried Employees, while four (4) are hourly employees. None of the Debtors' Employees are represented by labor unions.

12. The Employees perform a variety of critical functions throughout the Debtors' business. Of the Debtors' thirty-eight (38) full-time Employees, thirteen (13) are in general and administrative functions including executives, human resources, finance and information technology, eight (8) are in pharmaceutical and formulation development, seven (7) are in clinical, medical, quality and regulatory operations, five (5) are dedicated to the Debtors' manufacturing capability and product operations, three (3) are in commercial operations, marketing and market access, and two (2) are in facilities management. The Debtors' one (1) part-time Employee serves in a technology and formulation science research and development function.

13. The Debtors' ability to run their business safely and productively, and consequently the value of the Debtors' business as a going concern, depends entirely on the expertise and continued support and service of their Employees. Due to the disruption and uncertainty that typically accompanies a chapter 11 filing, the Debtors believe that the continuity and competence of their workforce would be jeopardized if the relief requested herein is not granted. Moreover, if the Debtors fail to pay the Prepetition Employee Obligations in the ordinary course of business, their workforce will suffer extreme personal hardship and, in some cases, may be unable to pay their basic living expenses. This would have a highly negative impact on workforce morale and productivity and would risk immediate and irreparable harm to the Debtors' continuing operations and their estates. Accordingly, the Debtors have determined that paying those obligations and continuing all of the Compensation and Benefits Programs described in this Motion are each vital to preventing the loss of key members of the workforce during the pendency of these Chapter 11 Cases and to maintaining the continuity and stability of the Debtors' operations.

I. Compensation Obligations

A. Wages Compensation

14. Employees are paid their wages or salaries on account of their services to the Debtors every two weeks with a one-week lag period (collectively, the “Wages”). Over the past twelve (12) months, the average monthly payroll for Employees aggregated approximately \$612,311.63 for the current employees. The Debtors estimate that as of the Petition Date, the total amount of outstanding prepetition Wages is approximately \$141,302.68. As of the Petition Date, no Employees are owed Wages in an amount exceeding the \$15,150 statutory cap imposed by section 507(a)(4) of the Bankruptcy Code.

B. Payroll Processing Services

15. The Debtors use Paycom Software, Inc. (“Paycom”) to administer their payroll, which includes calculating and processing gross-to-net payroll, issuing payroll payments to the appropriate funds transfer networks, generating pay statements and coordinating the payment of any Deductions or other applicable withholdings. Paycom debits the Payroll Account (as defined in the Cash Management Motion) to satisfy all payroll and associated withholding obligations. The ongoing services of Paycom are imperative to the smooth functioning of the Debtors’ operations and payroll processing. The Debtors pay Paycom approximately \$1,850.00 every two-week period for its services. The Debtors estimate that, as of the Petition Date, they currently do not have any accrued but unpaid fees related to such services.

II. Payroll Deduction Obligations

16. Pursuant to federal, state, and local law, through the service provided by Paycom, the Debtors take deductions from Employees’ paychecks for payments to third parties on behalf of Employees for various federal, state and local income, employment, payroll, and other taxes (collectively, the “Payroll Taxes”). The Debtors are obligated to remit such Payroll Taxes to the

appropriate taxing authorities. The Debtors are also required to make payments from their own funds on account of Social Security and Medicare taxes and to pay, based on a percentage of gross payroll (and subject to state-imposed limits), additional amounts to taxing authorities for, among other things, state and federal unemployment insurance (collectively, and together with the Payroll Taxes, the “Payroll Tax Obligations”). In the aggregate, the Debtors’ monthly Payroll Tax Obligations total approximately \$199,000.00. As of the Petition Date, the Debtors estimate that they owe approximately \$46,000.00 on account of Payroll Tax Obligations relating to the prepetition period, all of which will become due and payable during the first 21 days of the Chapter 11 Cases.

17. In the ordinary course of processing payroll, the Debtors also may (a) be required by law, in certain circumstances, to withhold from certain Employees’ Wages amounts for various garnishments, such as tax levies, child support and other court-ordered garnishments, as well as (b) make other routine deductions for 401(k) contributions, employee 401(k) loan repayments, health plan contributions, as well as other pre- and after-tax deductions payable pursuant to certain of the employee benefit plans discussed herein (collectively, the “Deductions” and together with the Payroll Tax Obligations, the “Withholding Obligations”). Each pay cycle, the Debtors withhold Deductions from applicable Employees’ paychecks and remit them to the appropriate authorities or entities. On average, the Debtors withhold approximately \$30,000.00 in Deductions every two weeks from Employees’ Wages. As such, as of the Petition Date, the Debtors estimate that approximately \$15,000.00 has accrued on account of Deductions every pay cycle.

As of the Petition Date, the Debtors estimate that the aggregate amount of accrued but unremitted Withholding Obligations is approximately \$64,000.00, excluding pre- and after-tax deductions payable pursuant to some of the employee benefit plans discussed herein. Pursuant

to this Motion, the Debtors seek authority to continue remitting and paying the Withholding Obligations (whether pre- or postpetition) to the appropriate authorities and entities in the ordinary course of business and to pay any administrative fees with respect to the Withholding Obligations.

III. Employee Benefits Programs

A. Paid and Unpaid Leaves of Absence

18. The Debtors maintain several paid leave benefit programs for their Employees, providing paid leave for personal time off (“PTO”), holidays, and other paid leave (collectively, the “Paid Leave”). Historically, eligible Employees were granted a specified number of PTO days based on the Employee’s length of service with the Debtors since his or her hire date. PTO would carry forward into the next year up to a maximum accrued amount based upon years of service with the Debtors. As of the Petition Date, the Debtors believe that they owe approximately \$194,999.83 on account of accrued and payable PTO for Employees. The other forms of Paid Leave do not involve incremental cash outlays beyond the standard payroll obligations.

19. Other Leaves of Absence. The Debtors also permit Employees to take certain other paid and unpaid leaves of absence for personal reasons. For example, the Debtors offer paid military leave, paid time off for voting, paid leave for jury duty and witness duty, paid bereavement leave, unpaid and paid time off for parents, and paid break times for nursing mothers. The Debtors also permit Employees to take other paid and unpaid leaves of absence for personal reasons and any other leave, paid or unpaid, as required by jurisdiction of an employee’s work location.

20. These forms of compensation are, in certain cases, required by statute, and in all cases, usual, customary and necessary if the Debtors are to retain qualified Employees to operate their business. Failure to provide these benefits could contravene applicable law, harm Employee morale and encourage the premature departure of Employees. The Debtors therefore request

authority to continue these benefits programs in the ordinary course of business during the Chapter 11 Cases.

B. Expense Reimbursement

21. The Debtors, in the ordinary course of business, may reimburse Employees for a variety of ordinary, necessary, and reasonable business-related expenses that the Employees incur on behalf of the Debtors in the scope of their employment (the “Reimbursable Expenses”). Most Employees initially incur and pay such Reimbursable Expenses by using personal funds or credit cards, but are subsequently reimbursed by the Debtors after submission and approval of expense reimbursement reports. Employees are expected to use sound judgment and good business sense when incurring such expenses, and the Debtors reserve executive approval to accept or deny repayment of all requested Reimbursable Expenses. The Debtors estimate that, as of the Petition Date, a *de minimis* amount is owed on account of prepetition Reimbursable Expenses.

22. In addition, the Debtors provide certain Employees with credit cards (the “Corporate Credit Cards”) issued by Silicon Valley Bank (the “Corporate Credit Card Company”) to be used in connection with the Employees’ day-to-day functions as well as for payment of Reimbursable Expenses. Depending on the type of Corporate Credit Card issued, Employees may use the Corporate Credit Cards to pay for job-related expenses (including, for example, inventory purchases) and/or work-related travel and similar expenses.

23. As of the Petition Date, the Debtors have issued approximately seven (7) Corporate Credit Cards to Employees. In addition, the Debtors have three (3) corporate administration credit cards. All Corporate Credit Cards issued by the Debtors to Employees have detailed restrictions on permissible expenditures, and Employees are responsible for any non-reimbursable amounts charged to the Corporate Credit Cards. Most of the obligations arising under the Corporate Credit

Cards are paid directly by the Debtors (with the applicable Employee reimbursing the Debtors for any non-reimbursable amounts charged to the cards). The Debtors estimate that they incur obligations under the Corporate Credit Cards of approximately \$72,000.00 per month (the “Corporate Credit Card Obligations”). As of the Petition Date, the Debtors estimate that they do not owe any outstanding Corporate Credit Card Obligations.

C. Health and Welfare Benefits

24. The Debtors offer eligible Employees a large portfolio of benefits, including medical, dental coverage, vision coverage, health savings accounts, coverage under the Consolidated Omnibus Budget Reconciliation Act of 1985 (“COBRA”), flexible spending accounts, life insurance, disability insurance and other benefit programs provided to Employees in the ordinary course of business (collectively, and as listed in detail in paragraphs 25 - 31 below, the “Health and Welfare Benefits”). As of the Petition Date, the Debtors estimate that total accrued but unpaid obligations owed by the Debtors relating to the Health and Welfare Benefits are of a *de minimis* amount.

1. Medical, Dental, and Vision Benefits

25. The Debtors offer all eligible Employees and their dependents medical coverage (the “Medical Plans”). The Medical Plans are administered through Aetna Life Insurance Company. The Debtors currently offer three plans which consist of two high deductible healthcare plan and one Medical PPO plan. The Debtors pay, on average, approximately \$37,595.37 per month to cover outstanding claims and fees associated with the Medical Plans. The Debtors estimate that, as of the Petition Date, there are no amounts owed on account of the Medical Plans.

26. Additionally, the Debtors offer all eligible Employees the option of participating in a dental plan (the “Dental Plan”) administered by The Guardian Life Insurance Company of America (“Guardian Life”). On average, the Debtors contribute approximately \$4,805.96 per

month for the Dental Plan. The Debtors estimate that, as of the Petition Date, there are *de minimis* amounts owed on account of the Dental Plan.

27. The Debtors also offer all eligible Employees the option of participating in a vision plan administered through Guardian Life (the "Vision Plan"). On average, the Employees contribute approximately \$532.94 per month for the Vision Plan. The Vision Plan is 100% funded by the Employees and as such, the Debtors have no amounts owed on account of the Vision Plan.

2. Flexible Spending Accounts

28. All eligible Employees may elect to participate in the Debtors' tax-advantaged flexible spending account plans (the "FSA Plan") administered by Flores & Associates (the "FSA Plan Administrator"), under which the Debtors offer Employees the ability to contribute a portion of their pre-tax compensation to flexible spending accounts to pay for eligible out-of-pocket health care and dependent care expenses (the "FSA Plan Contributions"). Eligible Employees may set aside pre-tax dollars up to the maximum amount allowed under IRS regulations to pay for eligible health care expenses and dependent care expenses. Employees who elect to participate in the FSA Plan designate a certain amount per month to be withheld from their payroll as a Deduction.

29. The Debtors withhold approximately \$3,518.88 per month from Employees' compensation on account of the FSA Plan. As of the Petition Date, the Debtors estimate that they are currently withholding approximately \$812.05 on account of the FSA Plan Contributions. Pursuant to this Motion, the Debtors seek authority to transfer withheld amounts and to continue to withhold amounts on account of the FSA Plan and to transfer such amounts to the FSA Plan Administrator in the ordinary course of business. The Debtors pay administrative fees of approximately \$175.00 per month to the FSA Plan Administrator. The Debtors estimate that, as

of the Petition Date, they owe approximately \$175.00 in administrative fees to the FSA Administrator, all of which will become due and payable during the Interim Period.

3. Health Savings Account

30. Employees enrolled in certain Medical Plans may elect to participate in the Debtors' tax-advantaged health savings account (the "HSA Plan") administered by PayFlex (the "HSA Plan Administrator"), under which the Debtors offer eligible Employees the ability to contribute a portion of their pre-tax compensation to a health savings account to pay for qualified out-of-pocket health care expenses for the Employee and qualified dependents. Employees who elect to participate in the HSA Plan designate a certain amount per paycheck to be withheld from their payroll as a Deduction. The Debtors do not pay a monthly administration fee for the HSA Plan Administrator and withhold approximately \$5,191.23 per month from Employee paychecks on account of the HSA. As of the Petition Date, the Debtors estimate that they owe approximately \$1,197.98 to the HSA Plan Administrator in withholdings, all of which will come due and payable during the Interim Period.

4. Life and Disability Insurance

31. The Debtors provide all eligible Employees with basic life and basic accidental death and dismemberment insurance coverage through Guardian Life in the event of serious illness, injury or death ("Basic Life/AD&D Insurance"). The Basic Life/AD&D Insurance and Disability Coverage costs the Debtors approximately \$999.09 per month. The Debtors also offer short-term and long-term disability coverage ("Disability Coverage") through Guardian Life, in the event an Employee becomes unable to work due an illness or injury. The Disability Coverage costs the Debtors approximately \$4,125.11 per month.

5. Other Welfare Programs

32. In addition to the foregoing, the Debtors have in place miscellaneous practices, programs, and policies that provide medical and welfare benefits to eligible Employees, including COBRA and other programs (collectively, the “Other Welfare Programs”). The Debtors believe that the Other Welfare Programs are important to maintaining Employee morale and assisting in the retention of the Debtors’ Employees. The monthly cost of such programs for the Debtors is negligible in the context of the Debtors’ aggregate compensation and benefit obligations. By way of example, there is no cost to the Debtors for the COBRA offering as the Debtors are reimbursed 100% for the premiums paid out. The Debtors believe that failing to honor expected benefits under such Other Welfare Programs, as well as the other Health and Welfare Benefits, would have an adverse effect on the Employees. The Debtors believe that there are no accrued amounts under the Other Welfare Programs as of the Petition Date.

D. Workers’ Compensation

33. The Debtors maintain workers’ compensation insurance that provides coverage for employee-related injuries, disability or death, as prescribed by state and federal workers’ compensation laws and other statutes, at no cost to Employees (the “Workers’ Compensation Program”). In connection with these requirements, the Debtors maintain a workers’ compensation insurance policy (the “Workers’ Compensation Policy”) through Travelers Insurance (“Travelers”). Under the Workers’ Compensation Policy, Travelers provides full insurance coverage for workers’ compensation claims. The annual premium for the Workers’ Compensation Policy is \$25,037.00, paid annually for the complete policy period.⁴ As of the Petition Date, the

⁴ The Workers’ Compensation Policies have payroll audits that may result in an increase of the annual premium.

Debtors believe that they are current with premiums and administrative expenses in connection with the Workers' Compensation Program.

34. There are currently no covered claims (the "Workers' Compensation Claims") open against the Debtors. As a result, as of the Petition Date, the Debtors do not owe any obligations in connection with the Workers' Compensation Claims.

35. To ensure that the Debtors comply with state law requirements, it is necessary to obtain authority to continue to maintain the Workers' Compensation Program in the ordinary course of business and authority, but not direction, to pay any prepetition amounts related thereto, including, without limitation, any payments for future Workers' Compensation Claims, premiums, deductibles, and fees owed for administrative costs, and other amounts required in connection with the Workers' Compensation Program as such amounts become due in the ordinary course of business.

E. Employee Severance Obligations

36. In the ordinary course of business, the Debtors have historically provided severance benefits to non-insider Employees when they determine, in an exercise of their reasonable business judgement, that such severance benefits are justified (the "Non-Insider Severance Program"). Prior to the Petition Date, the Debtors' practice was to provide severance to certain non-Insider Employees terminated due to a work-force adjustment or any not-for-cause employer-initiated termination. In 2023, the amounts granted to individual Employees under the Non-Insider Severance Program ranged from 2 to 6 weeks of base pay.

37. The Debtors believe that the Non-Insider Severance Program has been, and will continue to be, critical to maintaining Employee morale and loyalty. Any increase in the instability in the Debtors' workforce could undermine the Debtors' ability to continue as a going concern

thereby reducing the value Debtors' estates to interested parties. The Non-Insider Severance Program will supersede any other severance agreement that a non-insider Employee may have entered into prepetition with the Debtors. Further, to be eligible for the Non-Insider Severance Program, Employees will have to be terminated after committing to remain with the Debtors for as long as they were needed.

38. In the months leading up to the Petition Date, the Debtors paid approximately \$281,978.00⁵ on account of the Non-Insider Severance Program. Through this Motion, the Debtors do not seek authority to pay any amounts for the Non-Insider Severance Program that accrued or owed prior to the Petition Date. The Debtors only seek authority to honor their any obligations under the Non-Insider Severance Program in the ordinary course for Employees terminated after the Petition Date.

39. The Debtors further seek the authority, but not the direction, to provide severance payments to the Chief Executive Officer and Chief Financial Officer (collectively, the "Insiders") of Debtor Novan, Inc., pursuant to section 503(c)(2) of the Bankruptcy Code (the "Insider Severance Program"). These Insiders were instrumental in ensuring that the Debtors' operations continued during a difficult and trying time. Through the committed and determined efforts of these Insiders, the Debtors were able to maximize their value, to the benefit of all stakeholders.

40. To entice the Insiders to remain, the Debtors offered the Insiders severance packages (the "Insider Severance Packages"). To be sure, the Insider Severance Packages provided for severance payments of 12 and 18 months respectively. The Debtors seek authorization to honor the Insider Severance Packages up to the limit imposed under section

⁵ This equates to an average of \$7,230.00 per Employee. However, a majority of these Employees were sales reps who had an incentive-based compensation program. Since severance payments were based on the base salary of the Employee, this necessarily skewed the average payment downward. Excluding the severance payments to the sales reps increases the average severance payment for Employees to \$14,585.00.

503(c)(2) of the Bankruptcy Code. The Debtors calculate that the mean of the Non-Insider Severance Program was \$7,230.00. As such, the Debtors seek authorization to pay the Insiders \$72,000.00 each on account of their Insider Severance Packages.

F. Employee Retirement Benefits

41. The Debtors maintain a 401(k) savings plan, a qualified defined contribution plan pursuant to section 401(k) of the Internal Revenue Code for all Employees (the “401(k) Plan”). The 401(k) Plan is managed by Fidelity Investments, which does not charge administrative fees to the Debtors. The Debtors match 100% of the first 5% gross Wages that an Employee contributes to his or her account, subject to mandated limitations (the “401(k) Matching Contribution”). Approximately 34 Employees currently participate in the 401(k) Plan with monthly contributions to the 401(k) Plan totaling approximately \$74,126.04. This includes approximately \$49,325.66 of Employee contributions, made up of withholdings from participating Employees’ paychecks, and approximately \$24,800.38 of 401(k) Matching Contributions. As of the Petition Date, the Debtors believe they owe \$5,723.17 on account of the prepetition 401(k) Matching Contribution.

BASIS FOR RELIEF

I. Payment of the Prepetition Employee Obligations Is a Sound Exercise of the Debtors’ Business Judgment and Is Appropriate Under Sections 363 and 105(a) of the Bankruptcy Code.

42. 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 section 363(b) of the Bankruptcy Code, courts require only that the debtor “show that a sound business purpose justifies such actions.” *Dai-Ichi Kangyo Bank, Ltd. v. Montgomery Ward Holding Corp. (In re Montgomery Ward Holding Corp.)*, 242 B.R. 147, 153 (D. Del. 1999); *see also In re Phoenix Steel Corp.*, 82 B.R. 334, 335–36 (Bankr. D. Del. 1987); *see also, e.g., In re Adelpia Commc’ns Corp.*, No. 02-41729

(REG), 2003 WL 22316543, at *31 (Bankr. S.D.N.Y. Mar. 4, 2003); *Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.2d 1063, 1071 (2d Cir. 1983). Moreover, “[w]here 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.” *Comm. of Asbestos-Related Litigants v. Johns-Manville Corp. (In re Johns-Manville Corp.)*, 60 B.R. 612, 616 (Bankr. S.D.N.Y. 1986); *In re Global Home Prods., LLC*, 369 B.R. 778, 783-84 (Bankr. D. Del. 2007); *In re Dana Corp.*, 358 B.R. 567, 584 (Bankr. S.D.N.Y. 2006).

43. In addition to being justified under section 363(b)(1) of the Bankruptcy Code, payment of the Prepetition Employee Obligations is warranted under the doctrine of necessity. Section 105(a) of the Bankruptcy Code, which codifies the inherent equitable powers of the bankruptcy court, empowers the bankruptcy court to “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.” 11 U.S.C. § 105(a). Under section 105(a) and the “doctrine of necessity,” the Court may exercise its broad grant of equitable powers to permit the payment of Prepetition Employee Obligations when such payment is essential to the continued operation of the debtor’s business. *See, e.g., In re Just for Feet, Inc.*, 242 B.R. 821, 824–25 (D. Del. 1999) (holding that section 105(a) of the Bankruptcy Code provides a statutory basis for the payment of prepetition claims under the doctrine of necessity and noting that “[t]he Supreme Court, the Third Circuit and the District of Delaware all recognize the court’s power to authorize payment of pre-petition claims when such payment is necessary for the debtors’ survival during chapter 11”); *In re Columbia Gas Sys., Inc.*, 171 B.R. 189, 191–92 (Bankr. D. Del. 1994) (confirming that the doctrine of necessity is the standard in the Third Circuit for enabling a court to authorize the payment of prepetition claims prior to the confirmation of a reorganization plan).

44. The United States Court of Appeals for the Third Circuit recognized the “necessity of payment” doctrine in *In re Lehigh & New England Ry. Co.*, 657 F.2d 570, 581 (3d Cir. 1981). The Third Circuit held that a court could authorize the payment of prepetition claims if such payment was essential to the continued operation of the debtor. *Id.* (stating that a court may authorize payment of prepetition claims when there “is the possibility that the creditor will employ an immediate economic sanction, failing such payment”); *see also Official Comm. of Unsecured Creditors of Motor Coach Indus. Int’l, Inc. v. Motor Coach Indus. Int’l, Inc. (In re Motor Coach Indus. Int’l, Inc.)*, No. 08-12136-BLS, 2009 WL 330993, at *3 (D. Del. Feb. 10, 2009) (denying stay pending appeal on grounds that doctrine of necessity had not been brought into serious question by courts in Third Circuit).

45. The necessity of payment doctrine is designed to foster a debtor’s rehabilitation, which courts have recognized is “the paramount policy of Chapter 11.” *In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 176 (Bankr. S.D.N.Y. 1989); *see also In re Chateaugay Corp.*, 80 B.R. 279, 287 (S.D.N.Y. 1987) (authorizing payment of prepetition workers’ compensation claims on grounds that the fundamental purpose of reorganization and equity powers of bankruptcy courts “is to create a flexible mechanism that will permit the greatest likelihood of survival of the debtor and payment of creditors in full or at least proportionately”); *In re Just for Feet*, 242 B.R. at 826 (finding that payment of prepetition claims to certain trade vendors was “essential to the survival of the debtor during the chapter 11 reorganization”); *In re Quality Interiors, Inc.*, 127 B.R. 391, 396 (Bankr. N.D. Ohio 1991) (“A general practice has developed . . . where bankruptcy courts permit the payment of certain pre-petition claims, pursuant to 11 U.S.C. § 105, where the debtor will be unable to reorganize without such payment.”); *In re Eagle-Picher Indus., Inc.*, 124 B.R. 1021, 1023 (Bankr. S.D. Ohio 1991) (approving payment of prepetition unsecured claims of tool makers

as “necessary to avert a serious threat to the Chapter 11 process”). Moreover, Bankruptcy Rule 6003 itself implies that the payment of Prepetition Employee Obligations may be permissible within the first twenty-one (21) days of a case where doing so is “necessary to avoid immediate and irreparable harm.” Fed. R. Bankr. P. 6003.

46. It is a sound exercise of the Debtors’ business judgment to pay the Prepetition Employee Obligations because doing so will help the Debtors avoid the potential for value-destructive interruption to their business operations during the Chapter 11 Cases. For the reasons discussed herein, payment of the Prepetition Employee Obligations enhances value for the benefit of all interested parties. The Debtors’ ability to maximize value and continue operations depends, in large part, on the retention, motivation and productivity of their Employees, whose efforts will be critical to the Debtors’ successful reorganization. Most of the Debtors’ Employees rely exclusively on the Prepetition Employee Obligations to satisfy their daily living expenses. If amounts owed are not received or other benefits are delayed, the Employees may be exposed to significant financial hardship and, in some cases, will be unable to meet their basic needs, which may make continuing to work for the Debtors impossible. If the Debtors are unable to satisfy their various compensation and benefits obligations, the Employees will suffer at a time when their support is critical to the Debtors. Therefore, in order to provide certainty to the Debtors’ Employees, maintain morale and productivity, limit turnover and minimize the adverse effect of the commencement of the Chapter 11 Cases, it is necessary to continue providing ordinary course compensation and benefits. Moreover, for the avoidance of doubt, no Employee will receive payment under this Motion in excess of the statutory cap of \$15,150 on account of any existing and outstanding Prepetition Employee Obligations as of the Petition Date.

47. Indeed, courts in this district have recognized the importance of satisfying employee obligations in cases requesting relief similar to that requested here. *See, e.g., In re Town Sports Int'l, LLC*, No. 20-12168 (CSS) (Bankr. D. Del. Sept. 16, 2020) (authorizing debtors to continue employee compensation and benefit programs and pay certain prepetition obligations related thereto on a postpetition basis); *In re Extraction Oil and Gas, Inc.*, No. 20-10548 (Bankr. D. Del. July 13, 2020) (same); *In re APC Automotive Technologies Intermediate Holdings, LLC*, No. 20-11466 (CSS) (Bankr. D. Del. June 4, 2020) (same); *In re Akorn, Inc.*, No. 20-11177 (KBO) (Bankr. D. Del. May 22, 2020) (same); *In re Bluestem Brands, Inc.*, No. 20-10566 (MFW) (Bankr. D. Del. Mar. 30, 2020) (same). Accordingly, the Debtors respectfully request that the Court authorize the Debtors to pay and continue the Prepetition Employee Obligations in the ordinary course of business and consistent with past practice.

II. Payment of Certain of the Prepetition Employee Obligations Should Be Authorized Under Section 507(a) of the Bankruptcy Code.

48. The majority of the Prepetition Employee Obligations constitute priority claims under sections 507(a)(4), (a)(5) and (a)(8) of the Bankruptcy Code, which must be satisfied before any general unsecured claims against the Debtors' estates. *See* 11 U.S.C. §§ 507(a)(4), 507(a)(5), 507(a)(8), 726. Specifically, under section 507(a)(4)(A) of the Bankruptcy Code, claims of employees for "wages, salaries, or commissions, including vacation, severance, and sick leave pay" earned within 180 days before the Petition Date are afforded priority unsecured status up to \$15,150 per individual. *See* 11 U.S.C. § 507(a)(4)(A).

49. Similarly, under section 507(a)(5) of the Bankruptcy Code, employees' claims for contributions to certain employee benefit plans are also afforded priority unsecured status up to \$15,150 per employee covered by such plan, less any amount paid under section 507(a)(4). *See* 11 U.S.C. § 507(a)(5)(A). The same holds true for the payment of the Payroll Taxes, as the

relevant taxing authorities generally would hold priority claims under section 507(a)(8) of the Bankruptcy Code for such obligations and their payment will not prejudice other creditors of the Debtors. *See* 11 U.S.C. § 507(a)(8).⁶

50. The Debtors believe that no Employee is owed accrued and unpaid wages in excess of the cap and no amounts are accrued and owing under any benefits plan in excess of the cap. Thus, all the Prepetition Employee Obligations are priority claims that, in any event, will have to be paid in full, and payment of the Prepetition Employee Obligations merely expedites the treatment afforded to such claims and is consistent with the priority scheme of the Bankruptcy Code. Regardless, by this Motion, the Debtors do not seek authority to pay any Prepetition Employee Obligations in excess of the statutory cap for any individual Employee. Accordingly, the Debtors request entry of the Proposed Interim Order authorizing the Debtors to pay the Prepetition Employee Obligations in an aggregate amount not to exceed the Interim Amount subject to the \$15,150 per Employee cap, followed by the final hearing on this Motion authorizing the Debtors to continue paying the Prepetition Employee Obligations in the ordinary course.

III. Funds Related to the Payroll Taxes and Payroll Deduction Obligations May Be Held in Trust and Are Not Property of the Estate.

51. Payroll taxes withheld from an Employee's wages and any other Withholding Obligations are collected or withheld by the Debtors and may be held in trust for the benefit of the applicable taxing authority. As a result, Payroll Tax Obligations and other Deductions are not property of the Debtors' estates under section 541 of the Bankruptcy Code, and those funds, therefore, are not available for the satisfaction of creditors' claims. *See, e.g., Begier v. IRS*, 496

⁶ Section 507(a)(8) of the Bankruptcy Code affords priority to, among other things, unsecured claims of governmental units for (i) taxes required to be collected or withheld and for which the debtor is liable in whatever capacity (§ 507(a)(8)(C)) and (ii) under certain circumstances, employment taxes on wages, salaries, or commissions (§ 507(a)(8)(D)).

U.S. 53 (1990) (withheld taxes are property held by the debtor in trust for another and, as such, not property of the debtor's estate); *City of Farrell v. Sharon Steel Corp.*, 41 F.3d 92, 95 (3d Cir. 1994) (withheld taxes were subject to a trust); *see generally In re Columbia Gas Sys. Inc.*, 997 F.2d 1039, 1060 (3d Cir. 1993) (indicating that even if a statute does not establish an express trust, a constructive trust may be found). Instead, the Debtors may be obligated to remit these funds to the applicable taxing authority.

52. Many federal, state and local statutes also impose personal liability on officers and directors of companies for certain Payroll Tax Obligations and other Payroll Deduction Obligations. To the extent that the relevant Payroll Taxes and other Deductions remain unpaid by the Debtors, the Debtors' directors, officers and executives may be subject to lawsuits or criminal prosecution during the pendency of these Chapter 11 Cases. Any such lawsuit or criminal prosecution (and the ensuing potential liability) would distract the Debtors and their directors, officers and executives from devoting their full attention to the Debtors' business and the orderly administration of the Chapter 11 Cases. The Debtors believe that these distractions would materially undermine their ability to operate in the ordinary course of business and to administer these Chapter 11 Cases, with resulting detriment to any parties-in-interest.

53. For these reasons, the Debtors submit that the relief requested is essential, appropriate and in the best interests of their estates, creditors, and any parties in interest, and therefore should be granted.

IV. A Limited Waiver of the Automatic Stay for Workers' Compensation Claims Is Appropriate Here.

54. Section 362(a)(1) of the Bankruptcy Code operates to stay:

[T]he commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim

against the debtor that arose before the commencement of the case under this title

Section 362 of the Bankruptcy Code, however, permits a debtor or other parties-in-interest to request a modification or termination of the automatic stay for “cause.” 11 U.S.C. § 362(d)(1).

55. Although no workers’ compensation claims exists as of the Petition Date, the Debtors seek authorization under section 362(d) of the Bankruptcy Code to permit their Employees to proceed with Workers’ Compensation Claims should one have arisen prior to the Petition Date (if any) under the Workers’ Compensation Policies in the appropriate judicial or administrative forum. The Debtors believe that cause exists to modify the automatic stay because staying an employee’s workers’ compensation claim could have a detrimental effect on the financial well-being and morale of the Employees and lead to the departure of certain Employees. As discussed above, such departures could cause a severe disruption in the Debtors’ business to the detriment of all stakeholders. Accordingly, the Debtors request a limited waiver of the automatic stay for purposes of allowing the Workers’ Compensation Claims to proceed.

V. Processing of Checks and Electronic Fund Transfers Should Be Authorized.

56. The Debtors further request that the Court authorize and direct their banking institutions and all other applicable banks and other financial institutions to receive, process, honor and pay any and all checks drawn or electronic funds relating to the Prepetition Employee Obligations, whether such checks were presented before or after the Petition Date; provided that sufficient funds are on deposit in the applicable bank accounts to cover such payments. The Debtors have sufficient funds to pay any amounts described in this Motion in the ordinary course of business. In addition, under the Debtors’ existing cash management system, the Debtors can readily identify checks or wire transfer requests as relating to an authorized payment to be made hereunder. For that reason, the Debtors believe that checks or wire transfer requests, other than

those relating to authorized payments, will not be honored inadvertently. The Debtors also seek authority to issue new postpetition checks or effect new electronic fund transfers, on account of the Prepetition Employee Obligations to replace any prepetition checks or electronic fund transfer requests that may be dishonored or rejected as a result of the commencement of the Debtors' Chapter 11 Cases.

SATISFACTION OF BANKRUPTCY RULE 6003

57. Pursuant to Bankruptcy Rule 6003, the Court may grant relief within twenty-one (21) days after the filing of the petition regarding a motion to “use, sell, lease, or otherwise incur an obligation regarding property of the estate” only if such relief is necessary to avoid immediate and irreparable harm. Fed. R. Bankr. P. 6003(b). Immediate and irreparable harm exists where the absence of relief would impair a debtor’s ability to reorganize or threaten the debtor’s future as a going concern. *See In re Ames Dep’t Stores, Inc.*, 115 B.R. 34, 36 n.2 (Bankr. S.D.N.Y. 1990) (discussing the elements of “immediate and irreparable harm” in relation to Bankruptcy Rule 4001).

58. As described herein and in the First Day Declaration, the Debtors will suffer immediate and irreparable harm without authorization for the relief requested herein. Accordingly, Bankruptcy Rule 6003 has been satisfied and the relief requested herein should be granted.

WAIVER OF BANKRUPTCY RULE 6004(a) AND 6004(h)

59. The Debtors also request that the Court waive the stay imposed by Bankruptcy Rule 6004(h), which provides that “[a]n order authorizing the use, sale, or lease of property other than cash collateral is stayed until the expiration of 14 days after entry of the order, unless the court orders otherwise.” Fed. R. Bankr. P. 6004(h). As described above, the relief that the Debtor seeks in this Motion is necessary for the Debtors to operate their business without interruption and to preserve value for their estates. Accordingly, the Debtors respectfully request that the Court waive

the fourteen (14) day stay imposed by Bankruptcy Rule 6004(h), as the exigent nature of the relief sought herein justifies immediate relief.

60. To implement the foregoing immediately, the Debtors respectfully request a waiver of the notice requirements of Bankruptcy Rule 6004(a) to the extent they are deemed to apply.

RESERVATION OF RIGHTS

61. Nothing in the Proposed Orders or this Motion (i) is intended or shall be deemed to constitute an assumption of any agreement pursuant to section 365 of the Bankruptcy Code or an admission as to the validity of any claim against the Debtors and their estates; (ii) shall impair, prejudice, waive, or otherwise affect the rights of the Debtors and their estates with respect to the validity, priority, or amount of any claim against the Debtors and their estates; (iii) shall impair, prejudice, waive, or otherwise affect the rights of the Debtors and their estates with respect to any and all claims or causes of action; or (iv) shall be construed as a promise to pay a claim.

NOTICE

62. Notice (a) the Office of the United States Trustee (Attn: Linda J. Casey, Esq. (linda.casey@usdoj.gov)); (b) counsel to the Debtors' proposed debtor in possession financing lender; (c) the Internal Revenue Service; (d) the parties included on the Debtors' consolidated list of their 30 largest unsecured creditors; (e) the United States Attorney for the District of Delaware; (f) the state attorneys general in states where the Debtors are authorized to do business; (g) the Securities and Exchange Commission; (h) the Banks; and (i) all parties entitled to notice pursuant to Bankruptcy Rule 2002-1. Notice of this Motion and any order entered in connection with this Motion will be served on all parties in accordance with Local Rule 9013-1(m). The Debtors respectfully submit that, in light of the nature of the relief requested, no further notice of this Motion is required.

CONCLUSION

WHEREFORE, the Debtors respectfully request that the Court: (i) enter the Interim Order, substantially in the form attached hereto as **Exhibit A** granting the relief requested in this Motion, including scheduling a final hearing on this Motion; (ii) thereafter enter the Final Order substantially in the form attached hereto as **Exhibit B**; and (iii) grant such other and further relief as the Court may deem proper.

Dated: July 17, 2023
Wilmington, Delaware

Respectfully submitted,

/s/ Derek C. Abbott

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*Proposed Counsel to the Debtors and
Debtors in Possession*

Exhibit A

Proposed Interim Order

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re:)
) Chapter 11
NOVAN, INC., <i>et al.</i> , ¹)
) Case No. 23-10937 (LSS)
Debtors.)
) (Joint Administration Requested)
)
) Re: D.I __
)

**INTERIM ORDER (I) AUTHORIZING DEBTORS TO (A) PAY CERTAIN
PREPETITION EMPLOYMENT OBLIGATIONS AND (B) MAINTAIN EMPLOYEE
BENEFITS PROGRAMS AND (II) GRANTING RELATED RELIEF**

Upon consideration of the motion (the "Motion")² of the above-captioned debtors and debtors in possession (the "Debtors") for the entry of interim and final orders, pursuant to sections 105(a), 363(b), 507(a) and 541 of the Bankruptcy Code, Bankruptcy Rules 6003 and 6004, and Local Rule 9013-1, (i) authorizing the Debtors, but not directing, to (a) pay all Prepetition Employee Obligations and (b) honor and continue the Debtors' prepetition programs, policies and practices as described in the Motion in the ordinary course of business; and (ii) granting certain related relief, all as more fully set forth in the Motion; and upon consideration of the Motion and all pleadings related thereto, including the First Day Declaration; and due and proper notice of the Motion having been given; and having determined that no other or further notice of the Motion is required; and having determined that this Court has jurisdiction to consider the Motion in accordance with 28 U.S.C. §§ 157 and 1334 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware, dated as of February 29, 2012; and

¹ The Debtors in these chapter 11 cases, along with last four digits of the Debtors' federal tax identification number (if applicable), are: Novan, Inc. (7682) and EPI Health, LLC (9118). The corporate headquarters and the mailing address for the Debtors is 4020 Stirrup Creek Drive, Suite 110, Durham, NC 27703.

² Capitalized terms used but not defined in this Interim Order are defined in the Motion.

having determined that this is a core proceeding pursuant to 28 U.S.C. § 157(b)(2); and having determined that venue of this proceeding and the Motion is proper pursuant to 28 U.S.C. §§ 1408 and 1409; and after due deliberation and sufficient cause appearing therefor,

IT IS HEREBY ORDERED THAT:

1. The Motion is GRANTED on an interim basis as set forth herein.

2. A final hearing on the relief sought in the Motion shall be conducted on _____, 2023 at _____ (ET) (the “Final Hearing”). Any objections or responses to entry of a final order on the Motion (each, an “Objection”) shall be filed on or before **4:00 p.m. (EST) on _____, 2023**, and served on the following parties: (i) proposed counsel to the Debtors, Morris, Nichols, Arsht & Tunnell LLP, 1201 Market Street, 16th Floor, Wilmington, Delaware 19801 (Attn: Derek C. Abbott, Esq. (dabbott@morrisonichols.com)); (ii) the Office of the United States Trustee, J. Caleb Boggs Federal Building, 844 King St., Lockbox 35, Wilmington, DE 19801 (Attn: Linda J. Casey, Esq. (linda.casey@usdoj.gov)); (iii) counsel to Ligand Pharmaceuticals, Incorporated (the “DIP Lender”), Morgan Lewis and Bockius LLP, 101 Park Ave. New York, NY 10174 (Attn: Craig A. Wolfe, Esq. (craig.wolfe@morganlewis.com), Jason R. Alderson (jason.alderson@morganlewis.com), and David K. Shim (david.shim@morganlewis.com)); and (iv) counsel to any statutory committee appointed in these Chapter 11 Cases. In the event no Objections to entry of a final order on the Motion are timely received, this Court may enter such final order without need for the Final Hearing.

3. The Debtors are authorized, but not directed, to (i) pay or otherwise honor all Prepetition Employee Obligations in an amount not to exceed \$225,000.00 on an interim basis; (ii) pay postpetition Compensation Obligations and honor and continue their programs, policies and practices described in the Motion that were in effect as of the Petition Date, in the ordinary course

of business; and (iii) withhold and remit all federal, state and local taxes relating to the Prepetition Employee Obligations as required by applicable law; provided that in no event shall the Debtors pay any Prepetition Employee Obligations before such amounts are due and payable, and this Interim Order shall not be deemed to allow the Debtors to accelerate any payment of any amounts of Prepetition Employee Obligations that may be due and owing by the Debtors.

4. Notwithstanding any other provision of this Interim Order and absent further order of the Court, the Debtors shall not make any payments on account of the Prepetition Employee Obligations in excess of the limits provided for under section 507(a)(4) and (a)(5) of the Bankruptcy Code and capped at the amount afforded priority by those statutory subsections. Further, the Debtors are not authorized to “cash out” unpaid vacation days upon termination/resignation of an employee in excess of the caps provided by section 507(a)(4) or (a)(5) of the Bankruptcy Code unless applicable state law requires such payment.

5. The Debtors may only make material changes or modifications to their Compensation and Benefits Programs or introduce any new employee compensation or benefit plans or programs in prior consultation with the DIP Lender.

6. The Debtors shall maintain a matrix or schedule of amounts paid pursuant to the Non-Insider Severance Program, the Insider Severance Program, and the Insider Severance Packages, subject to the terms and conditions of this Interim Order, including the following information: (a) the title of the claimant paid; (b) the amount and date of the payment to such claimant; and (c) the total amount paid to the claimant to date. The Debtors shall provide a copy of such matrix or schedule to the U.S. Trustee, counsel to the DIP Lender, and any statutory committee appointed in these Chapter 11 Cases every 30 days beginning upon entry of this Interim Order.

7. Pursuant to section 362(d) of the Bankruptcy Code, Employees are authorized to proceed with their Workers' Compensation Claims (if any) in the appropriate judicial or administrative forum, and the Debtors are authorized to continue the Workers' Compensation Policies and pay the Workers' Compensation Claims. This modification of the automatic stay pertains solely to pursuing Workers' Compensation Claims.

8. The Debtors are authorized to reissue payment for the Prepetition Employee Obligations and to replace any inadvertently dishonored or rejected payments. Further, the Debtors are authorized to reimburse any expenses that Employees may incur as a result of any bank's failure to honor a prepetition check.

9. The Banks are authorized, when requested by the Debtors, in the Debtors' discretion, to honor and process checks or electronic fund transfers drawn on the Debtors' bank accounts to pay Prepetition Employee Obligations authorized to be paid hereunder, whether such checks or other requests were submitted prior to, or after, the Petition Date, provided that sufficient funds are available in the applicable bank accounts to make such payments. The Banks may rely on the representations of the Debtors with respect to whether any check or other transfer drawn or issued by the Debtors prior to the Petition Date should be honored pursuant to this Interim Order, and any such Bank shall not have any liability to any party for relying on such representations by the Debtors, as provided for in this Interim Order.

10. The Banks are hereby authorized to continue to service and administer the Bank Accounts as accounts of the Debtors as debtors in possession without interruption and in the usual and ordinary course, and to receive, process, honor and pay any and all checks and drafts drawn on, or electronic transfer requests made on, the Bank Accounts after the Petition Date by the holders or makers thereof, as the case may be; provided, however, that any check drawn or issued

by the Debtors before the Petition Date may be honored by a Bank if specifically authorized by order of this Court.

11. Nothing in this Interim Order (i) is intended or shall be deemed to constitute an assumption of any agreement pursuant to section 365 of the Bankruptcy Code or an admission as to the validity of any claim against the Debtors; (ii) shall impair, prejudice, waive or otherwise affect the rights of the Debtors or their estates with respect to the validity, priority or amount of any claim against the Debtors and their estates; (iii) shall impair, prejudice, waive, or otherwise affect the rights of the Debtors and their estates with respect to any and all claims or causes of action; or (iv) shall be construed as a promise to pay a claim.

12. The Debtors are authorized to take any and all actions necessary to effectuate the relief granted herein.

13. The requirements of Bankruptcy Rule 6003(b) have been satisfied because the relief set forth in this Interim Order is necessary to avoid immediate and irreparable harm.

14. Notwithstanding any applicability of Bankruptcy Rule 6004(h), the terms and conditions of this Interim Order shall be effective and enforceable immediately upon its entry.

15. This Court shall retain jurisdiction with respect to all matters arising from or related to the implementation of this Interim Order.

Exhibit B

Proposed Final Order

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re:)
) Chapter 11
NOVAN, INC., *et al.*,¹)
) Case No. 23-10937 (LSS)
Debtors.)
) (Jointly Administered)
)
) **Re: D.I. __**
)

**FINAL ORDER (I) AUTHORIZING DEBTOR TO (A) PAY CERTAIN PREPETITION
EMPLOYMENT OBLIGATIONS AND (B) MAINTAIN EMPLOYEE
BENEFITS PROGRAMS AND (II) GRANTING RELATED RELIEF**

Upon consideration of the motion (the “Motion”)² of the above-captioned debtors and debtors in possession (the “Debtors”) for the entry of interim and final orders, pursuant to sections 105(a), 363(b), 507(a) and 541 of the Bankruptcy Code, Bankruptcy Rules 6003 and 6004, and Local Rule 9013-1, (i) authorizing the Debtors, but not directing, to (a) pay all Prepetition Employee Obligations and (b) honor and continue the Debtors’ prepetition programs, policies and practices as described in the Motion in the ordinary course of business; and (ii) granting certain related relief, all as more fully set forth in the Motion; and upon consideration of the Motion and all pleadings related thereto, including the First Day Declaration; and due and proper notice of the Motion having been given; and having determined that no other or further notice of the Motion is required; and having determined that this Court has jurisdiction to consider the Motion in accordance with 28 U.S.C. §§ 157 and 1334 and the *Amended Standing Order of Reference* from the United States District Court for the District of Delaware, dated as of February 29, 2012; and

¹ The Debtors in these chapter 11 cases, along with the last four digits of the Debtors’ federal tax identification number (if applicable), are: Novan, Inc. (7682) and EPI Health, LLC (9118). The corporate headquarters and the mailing address for the Debtors is 4020 Stirrup Creek Drive, Suite 110, Durham, NC 27703.

² Capitalized terms used but not defined in this Final Order are defined in the Motion.

having determined that this is a core proceeding pursuant to 28 U.S.C. § 157(b)(2); and having determined that venue of this proceeding and the Motion is proper pursuant to 28 U.S.C. §§ 1408 and 1409; and after due deliberation and sufficient cause appearing therefor,

IT IS HEREBY ORDERED THAT

1. The Motion is GRANTED on a final basis as set forth herein.
2. The Debtors are authorized, but not directed, to (i) pay or otherwise honor all Prepetition Employee Obligations in an amount not to exceed \$225,000.00, in the aggregate, on a final basis; (ii) pay postpetition Compensation Obligations and honor and continue their programs, policies and practices described in the Motion that were in effect as of the Petition Date, in the ordinary course of business; and (iii) withhold and remit all federal, state and local taxes relating to the Compensation Obligations as required by applicable law; provided that in no event shall the Debtors pay any Prepetition Employee Obligations before such amounts are due and payable, and this Final Order shall not be deemed to allow the Debtors to accelerate any payment of any amounts of Prepetition Employee Obligations that may be due and owing by the Debtors.
3. Notwithstanding any other provision of this Final Order and absent further order of the Court, (i) payments to Employees on account of Prepetition Employee Obligations shall be limited by sections 507(a)(4) and (a)(5) of the Bankruptcy Code and capped at the amount afforded priority by those statutory subsections; and (ii) the Debtors are not authorized to “cash out” unpaid vacation days upon termination/resignation of an employee in excess of the caps provided by section 507(a)(4) or (a)(5) of the Bankruptcy Code unless applicable state law requires such payment.

4. The Debtors may only make material changes or modifications to their Compensation and Benefits Programs or introduce any new employee compensation or benefit plans or programs in prior consultation with the DIP Lender.

5. The Debtors shall maintain a matrix or schedule of amounts paid pursuant to the Non-Insider Severance Program, the Insider Severance Program, and the Insider Severance Packages, subject to the terms and conditions of this Final Order, including the following information: (a) the title of the claimant paid; (b) the amount and date of the payment to such claimant; and (c) the total amount paid to the claimant to date. The Debtors shall provide a copy of such matrix or schedule to the U.S. Trustee, counsel to the DIP Lender, and any statutory committee appointed in these Chapter 11 Cases every 30 days beginning upon entry of this Final Order.

6. Pursuant to section 362(d) of the Bankruptcy Code, Employees are authorized to proceed with their Workers' Compensation Claims (if any) in the appropriate judicial or administrative forum, and the Debtors are authorized to continue the Workers' Compensation Policies and pay the Workers' Compensation Claims. This modification of the automatic stay pertains solely to pursuing Workers' Compensation Claims.

7. The Debtors are authorized to reissue payment for the Prepetition Employee Obligations and to replace any inadvertently dishonored or rejected payments. Further, the Debtors are authorized to reimburse any expenses that Employees may incur as a result of any bank's failure to honor a prepetition check.

8. The Banks are authorized, when requested by the Debtors, in the Debtors' discretion, to honor and process checks or electronic fund transfers drawn on the Debtors' bank accounts to pay Prepetition Employee Obligations authorized to be paid hereunder, whether such

checks or other requests were submitted prior to, or after, the Petition Date, provided that sufficient funds are available in the applicable bank accounts to make such payments. The Banks may rely on the representations of the Debtors with respect to whether any check or other transfer drawn or issued by the Debtors prior to the Petition Date should be honored pursuant to this Final Order, and any such Bank shall not have any liability to any party for relying on such representations by the Debtors, as provided for in this Final Order.

9. The Banks are hereby authorized to continue to service and administer the Bank Accounts as accounts of the Debtors as debtors in possession without interruption and in the usual and ordinary course, and to receive, process, honor and pay any and all checks and drafts drawn on, or electronic transfer requests made on, the Bank Accounts after the Petition Date by the holders or makers thereof, as the case may be; provided, however, that any check drawn or issued by the Debtors before the Petition Date may be honored by a Bank if specifically authorized by order of this Court.

10. Nothing in this Final Order (i) is intended or shall be deemed to constitute an assumption of any agreement pursuant to section 365 of the Bankruptcy Code or an admission as to the validity of any claim against the Debtors; (ii) shall impair, prejudice, waive or otherwise affect the rights of the Debtors or their estates with respect to the validity, priority or amount of any claim against the Debtors and their estates; (iii) shall impair, prejudice, waive, or otherwise affect the rights of the Debtors and their estates with respect to any and all claims or causes of action; or (iv) shall be construed as a promise to pay a claim.

11. The Debtors are authorized to take any and all actions necessary to effectuate the relief granted herein.

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

13. This Court shall retain jurisdiction with respect to all matters arising from or related to the implementation of this Final Order.