Company A

Collateral Examination

As of October 31, 2008

Distribution:

	Line Management:	Account Officer SVP SVP
	Credit:	SVP
	Other:	
Risk Rating:		6.5 at previous exam
Examination Dates:		12/3/08-12/5/08, 12/9/08
Line of Business:		ABL
Type of Exam:		Recurring
Exam Frequency Per SAM:		4 times per annum

Recommended Exam Frequency per Commercial Field Exam ("CFE"): 4 times per annum

Commercial Field Services
Collateral Examination Report

Customer Name: **Company A**

Customer Address: **123 Some St. Anywhere, NY**

Telephone Number: **555-555-5555**

Contact Person: **Ima Controller**

Email Address: **imacontroller@companya.com**

Type of Business: **Manufacturer**

Fiscal Year End Date: **12/31/08**

Legal Entity of Borrower: **S Corp**

Type of Annual Financial Statement Provided: Audited

State of Incorporation: **Delaware**

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General

<u>Business Description/Background:</u>

Company A (the "Company" or "Co A") manufactures nail enamels in bulk for cosmetic companies. The Company is headquartered in Paterson, NJ with its affiliate Company B All manufacturing and operations for Co A are located at facilities located in Patterson, NJ. The Company sells to major cosmetic companies including Avon, L'Oreal, Revlon, Del Laboratories, Estee Lauder and O.P.I. (a distributor to nail salons). The Company specializes in developing custom formulas in order to meet the specific needs of customers. All products are produced to customer specifications.

<u>Current/Proposed Credit Facility:</u>

Company A has been a customer of Lending Bank since September 2005. The parent company for Co A (Co A Holdings, Inc.) acquired Company B ("Co B") in October 2007. Co B is presently financed by Webster Bank. The Borrower has requested that SOV consider financing both companies as co-borrowers under one line of credit.

Below are highlights of the proposed revolving credit facility for both Co A and Co B.

- Commitment: $9MM
- Advance Rates: 85% of eligible AR
  50% of eligible Inventory
- Sublimit: $3,250M on Inventory
- Reporting: Full dominion, with weekly reporting

<u>Specific Credit/RM/Field Exam Concerns:</u>

The RM was contacted prior to the start of field work. No specific concerns were discussed or mentioned. The RM did mention the need for a combined (Co B and Co A) borrowing base. Both a combined borrowing base and a consolidating borrowing base are presented in this report. All other comments, tables etc. presented are for Co A only.

Examination Highlights

- The AR general ledger to balance sheet reconciliation includes two liability accounts for rebate programs payable to customers. The total of these liability accounts is $93M. The examiner has recommended these items as ineligible;
- The proof of cash and the analysis of bank deposits show approximately $662M of Co A AR cash being deposited into the company's operating accounts. Cash other then SOV advances into the operating accounts are payments received from Co A Europe ($812M) as well as some customers that continue to remit to the old address ($662). Per management, the deposits made to the Commerce bank are transferred to the Lending Operating account. For August and September the deposits below were all made to the Lending

account, for October, $261M (all Co A Europe) was deposited to Commerce, the balance went to the Lending Account.

Below is a breakdown of the receipts:

August
Co A Europe: $160M
Other Customers: $361M

September
Co A Europe: $100M
Other Customers: $166M

October
Co A Europe: $551M
Other Customers: $135M

"Other" customers for the three months were mostly foreign and include:

- L'Oreal USA/Maybelline ($169M)
- The East Asiatic (Thailand) PLC ($402M, foreign)
- Ina Trading ($5M, foreign)
- Elibo Company ($85M, foreign).

The examiner recommends that Co A be instructed to forward all AR cash directly to the lockbox account and to not deposit these monies into the operating account. If a customer continues to remit to the TD North account then these monies should be forwaded to the lock box and not the operating account.

- Co A availability calculated by the examiner was $1,935M. This is $166M under the availability calculated buy the Company. The difference is caused by the examiner's recommendation to reserve for the rebate accruals, customer deposits, make and hold inventory and the inventory at outside processors.
- Co A and Co B combined net availability calculated by the examiner totaled $1,756M, This is $1,067M under the company's calculation of $2,823M. ***Please note that the Co B availability presented and included in the combined availability is from the survey. Both the Co B and Co A amounts are as of 10/31/08; however, the Co B portion of the initial borrowing base reported to Lending was prepared subsequent to the amounts presented here.*** The difference is caused by:
    - $178M of additional inventory ineligibles recommended by the examiner for results of the cost test on Co B, a reconciliation difference noted on Co B, $30M for inventory at an outside processor

$44M for labor and overhead on Co B, and $76M for make and hold inventory noted on Co A
  - $1,150M of additional AR ineligibles including: $94M for accrued rebates, $924M for foreign AR and $126M for customer deposits.
- The AR aging as of 10/31/08 is consistent with the prior period. Total AR is 3% higher than it was as of 10/31/07.
- Sales for the 12 months ended 10/31/08 are 0.8% above sales for the 12 months ended 10/31/07.
- Dilution shows some deterioration going from 0.5% to 2.6%; however, the source of the credits causing the increase is cash that is removed from customer deposits and applied to the AR. The examiner included these items as dilutive because the transactions (the “move” from customer deposits to AR) take place approximately 1 week after the invoice is generated. Since the collateral reported to SOV will be reduced by the credits and not the cash previously received, the examiner has included these items as dilutive. The examiner has also recommended ineligibles for the customer deposits as potential contras. Should SOV decide to enact this recommendation, the examiner recommends that these credits then be treated as non-dilutive.
- AR remains concentrated. Del Labs accounts for 28% of total AR, and Drocosca (a foreign account) accounts for 12.2%. The top ten customers account for 75.5% of total AR.
- The company does not have a perpetual inventory system. Full physicals are performed quarterly.
- During the tour of the storage and manufacturing facilities, the examiner noted that there is make and hold inventory.
- Total AP has increased from $2,402M as of 10/26/08 to $3,671M as of 10/31/07. Per management, the increase was due to increased orders received for November and December.

Availability:

Below is the 10/31/08 combined availability for Co A and Co B, as prepared by the examiner and the company.

(000's)		Audit Calculation	Company Calculation	Variance $	%
(a)	Accounts Receivable per the 10/08 aging.	$ 8,353	$ 8,353	$ -	0.0%
	Ineligibles				
(b)	Foreign	1,937	1,013	924	91.2%
(c)	Past Due > 90 days from invoice date	510	513	(3)	-0.6%
(d)	Customer Deposits	126	-	126	0.0%
(e)	Inter-company	20	-	20	0.0%
(f)	CB's/Partially Pad	9	-	9	0.0%
(g)	20% Concentration	-	-	-	0.0%
(h)	40% Concentration - Del Labs	-	-	-	0.0%
(i)	Contra	-	20	(20)	-100.0%
(j)	Rebates	94	-	94	0.0%
	Total Ineligibles	$ 2,696	$ 1,546	$ 1,150	74.4%
	Eligible Accounts Receivable	$ 5,657	$ 6,807	$ (1,150)	-16.9%
(k)	Advance Rate	85.0%	85.0%	85.0%	0.0%
	Available Accounts Receivable	$ 4,808	$ 5,786	$ (978)	-16.9%
(l)	Inventory as of 10/08	$ 6,249	$ 6,249	$ -	0.0%
	Ineligibles				
(m)	WIP	228	228	-	0.0%
(n)	Make and hold	76	-	76	0.0%
(o)	Labor and OH	44	-	44	0.0%
(p)	Supplies	39	39	-	0.0%
(q)	O/S Processor	30	-	30	0.0%
(r)	Reconciliation	15	-	15	0.0%
(s)	Cost Test FG's	13	-	13	0.0%
(t)	Slow moving/Obsolete	-	-	-	0.0%
	Total Ineligible	$ 445	$ 267	$ 178	66.7%
	Eligible Inventory	$ 5,804	$ 5,982	$ (178)	-3.0%
(u)	Advance Rate	50.0%	50.0%	50.0%	0.0%
	Available Inventory	$ 2,902	$ 2,991	$ (89)	-3.0%
	Collateral Availability	$ 7,710	$ 8,777	$ (1,067)	-12.2%
	Less Outstanding Revolver	5,954	5,954	-	0.0%
	Excess (Deficit) Availability	$ 1,756	$ 2,823	$ (1,067)	-37.8%

Below is the consolidating availability as prepared by the examiner.

(000's)	Consolidating Borrowing Base- Audit	Co A	Co B	Total
(a)	Accounts Receivable per the 10/08 aging.	$ 5,603	$ 2,750	$ 8,353
	Ineligibles			
(b)	Foreign	1,015	922	1,937
(c)	Past Due > 90 days from invoice date	327	183	510
(d)	Customer Deposits	39	87	126
(e)	Inter-company	-	20	20
(f)	CB's/Partially Pad	-	9	9
(g)	20% Concentration	-	-	-
(h)	40% Concentration - Del Labs	-	-	-
(i)	Contra	-	-	-
(j)	Rebates	94	-	94
	Total Ineligibles	$ 1,475	$ 1,221	$ 2,696
	Eligible Accounts Receivable	$ 4,128	$ 1,529	$ 5,657
(k)	Advance Rate	85.0%	85.0%	85.0%
	Available Accounts Receivable	$ 3,509	$ 1,300	$ 4,808
(l)	Inventory as of 10/08	$ 5,025	$ 1,224	$ 6,249
	Ineligibles			
(m)	WIP	146	82	228
(n)	Make and hold	76	-	76
(o)	Labor and OH	-	44	44
(p)	Supplies	-	39	39
(q)	O/S Processor	30	-	30
(r)	Reconciliation	-	15	15
(s)	Cost Test FG's	-	13	13
(t)	Slowmoving/Obsolete	-	-	-
	Total Ineligible	$ 252	$ 193	$ 445
	Eligible Inventory	$ 4,773	$ 1,031	$ 5,804
(u)	Advance Rate	50.0%	50.0%	50.0%
	Available Inventory	$ 2,387	$ 516	$ 2,902
	Collateral Availability	$ 5,895	$ 1,815	$ 7,710
	Less Outstanding Revolver	3,960	1,994	5,954
	Excess (Deficit) Availability	$ 1,935	$ (179)	$ 1,756

(a) Gross AR and the corresponding ineligibles for both Co A and Co B are per the 10/31/08 detailed Accounts Receivable agings.
(b) Per the SAM, past due invoices are defined as any invoice 90 or more days old.
(c) Per the SAM, any customer that is not located in the U.S. or Canada is to be considered ineligible. Below are the top ten foreign accounts for Co A and Co B:

Co A

Customer	**Total A/R**	**P/D A/R**	**LC/Insurance**	**Reserve**
DROCOSCA	684	72		612
ELIBO CO.	114			114
ELIAN GROUP	75			75
THE EAST ASIATIC (THAILAND) PLC	63			63
EUROPEAN PERFUME WORKS CO. L.L.C	62			62
INTEX INTERNATIONAL, S.A.	40			40
J VAN RESOURCES	38			38
LUMINEYE NAILCRAFT INNOVATIONS	22			22
PERMAQUIM SA	22			22
ANDEAN MINING & CHEMICAL	24	11		13
Total Analyzed	1,144	83		1,061
Not Analyzed	45	1		44
Total	1.189	84		1,105

Co B

Customer	**Total A/R**	**P/D A/R**	**LC/Insurance**	**Reserve**
BISSU COSMETICOS SA DE CV	214		-	214
LABORATORIOS DAROSA, S.A.	127			127
COLOMER MEXICO	84	8		76
AGENCIAS INTERNACIONALES	70			70
ESCOS, S.R.L.	67			67
UNION CHEMICAL IND. CO., LTD.	64			64
UNION CHEMICAL IND. (SHANGHAI)	53			53
LABORATORIOS "CROM." C.POR A.	31			31
MAPRIN REPRESENTACIONES	39	10		29
PERMAQUIM S.A	28			28
Total Analyzed	777	18		759
Not Analyzed	167	4		163
Total	944	22		922

(d) Customer deposits represent cash received from customers and not applied to the AR aging. The cash is held in a liability account until it is applied to open AR. The amount held on Co A is the balance in the customer deposit liability account. The amount held for Co B is the customer deposit liability account balance, less amounts received from foreign customers.

(e) Inter-company AR is the balance due to Co B from Co A Enterprises. This amount is treated as a contra on the Company prepared Borrowing Base.

(f) For Co B, the examiner noted $12M of eligible invoices that had $3M of cash applied to them. As the remaining balance may represent disputed amounts, the examiner has recommended that the partially paid invoices be reserved for. For Co A, all partially paid invoices noted by the examiner were due from ineligible accounts, therefore no reserve is recommended.

(g) Per the SAM there is 20% concentration limit on amounts due from customers other then Del Labs. The examiner did not note any concentrations in excess of 20% of the total AR balance for either Co B or Co A.
(h) Per the SAM there is 40% concentration limit on amounts due from Del Labs. As of 10/31/08 the balance due from Del Labs was 28% o the total AR on Co A and 14% of the Co B total AR.
(i) The examiner did not note any contras other than Co A. The examiner has reserved for the Co A Contra AR under "Inter-company," see (e) above.
(j) Per the general ledger to balance sheet reconciliation for AR. The company has accrued $94M for rebates payable to customers.
(k) Per the SAM the proposed AR advance rate is 80%
(l) Per the Company's roll forward of the 9/30/08 physical inventory.
(m) WIP is derived from the company's 9/30/08 physical and the roll forward of total AR The component percentages noted as of 9/30/08 are applied to total inventory to arrive at the WIP amount.
(n) Per the examiners physical review of Co A finished goods inventory. The amount recommended is an estimate as the company does not have a perpetual. During the examiners review of inventory, make and hold inventory was observed. The examiner estimated that approximately ½ of the finished goods on hand were make and hold product. Due to customer specificity of the finished goods inventory, the examiner recommends reserving for approximately 50% of the finished goods.
(o) Per the Company's summary, the total Co B inventory balance f $1,224M includes $44M for burden. The labor and overhead burden is not included in he Co A inventory balance.
(p) Per the Company's summary, the total Co B inventory balance f $1,224M includes $39M for supplies.
(q) Per Co A management, approximately $30M of inventory is located offsite at Penn Color at any given time.
(r) Per the examiners reconciliation of the 9/30/08 physical inventory to the general ledger for Co B
(s) Per the results of the Co B cost test. The carrying costs of the finished goods inventory @ 9/30/08 are approximately 10% above the current costs.
(t) The Company maintains inventory reserves for both Co B and Kirke; however the gross inventory amount shown is net of the respective reserves; therefore, no reserve is necessary.
(u) Per the SAM the proposed inventory advance rate is 50%
(v) Per the Company's general ledgers and borrowing bases for 10/31/08.

Conclusions/Recommendations:

Overall the Company's collateral performance appears to be consistent with the prior year's performance; however, the lack of a reliable inventory perpetual system remains a concern. To help mitigate this risk, the examiner recommends that at least 2 of the quarterly physicals be observed by Lending. The examiner further recommends that SOV schedule field exams to coincide with the Company's quarterly physical counts so that they can be observed by bank personnel/agents.

Rating:

Accounts Receivable:	Satisfactory
Inventory:	Marginal
Books & Records:	Satisfactory

Due to the lack of a perpetual the examiner has assigned a marginal rating to the inventory.

Accounts Receivable:

General:

The Company sells to cosmetic manufacturers and distributors. Selling terms are generally net 30, net 45 or net 60. Discounts are generally not offered; however, if there is a very large order or if a customer takes product in excess of the amount ordered, discounts may be offered. The Company's aging is based on invoice date and consists of aging buckets of 0-30, 31-60, 61-90 and over 90.

The Company does not maintain credit files. Most customers have long established relationships with the Company. If there is a new customer, trade references are obtained and the customer (if the references check out) is given a small credit limit.

Orders are received by the customer service department. The customer service department ensures that the order is within the customer's credit limit and that the customer is in good standing (i.e. not on credit hold). If the customer's status if clear, the order is accepted and sent to production. Production personnel will check the order and the required ingredients to ensure that all necessary components and/or raw materials are available. If an item is not available a requisition is prepared to either purchase the needed raw material or produce the needed component. Once all ingredients are obtained the item(s) are produced and shipped to the customer.

In most cases samples are sent to the customer prior to the shipment of the completed order. Since the customer approves the sample, returns are minimal. Per the examiners review of credits, credits are issued to apply cash received in advance.

Accounts Receivable Reconciliation:

Collateral Reconciliation

			Amount
Bal. Per Lender:	**10/31/2008**		$ 5,327
Less Cash I/T:	10/30 and 10/31	269	
	Adjustments per proof of cash	(586)	
	Adjustments per 11/12 BBC	38	
Total Subtractions:			(279)
Adjusted Lender Balance:			$ 5,606
Balance per the Aging:			$ 5,603
Difference: (1)			$ 3

(1) As the aging is below the collateral balance, SOV should monitor the collateral reconciliations. If the same difference appears in the collateral reconciliation for November, the collateral should be adjusted.

Aging to General Ledger Reconciliation

		Amount
Aging Date:	**10/31/2008**	$ 5,247
Balance per G/L		$ 5,246
Difference:		$ 1

General Ledger to Balance Sheet Reconciliation

			Amount
G/L Date:	**9/30/2008**		$ 5,246
Additions:	Inter-Co Co B (1)	510	
Total Additions			510
Subtractions:	CM Reserve (2)	52	
	Rebate Program (3)	69	
	Rebate Program DEL (3)	24	
	Allowance for Doubtful Accts	26	
Total Subtractions			171
Adjusted G/L Balance:			$ 5,585
Balance per Balance Sheet:			$ 5,584
Difference:			$ 1

(1) Amounts due from Co B are maintained in a separate GL account.
(2) Per management, the company accrues this balance to cushion any impact should a large credit need to be issued in the future..

(3) The examiner has not recommended these items as ineligible as they represent potential offsets to AR.

Accounts Receivable Aging Spreads:

	Oct-08		Oct-07	
	Amount	Pct	Amount	Pct
0-30	$ 2,652	47%	$ 2,313	43%
31-60	1,750	31%	1,590	29%
61-90	676	12%	1,109	20%
Over 90	525	9%	427	8%
Total	**$ 5,603**	**100%**	**$ 5,439**	**100%**

AR for the period ended 10/31/08 is consistent with the prior period ending 10/31/07. Current AR total $5,603M which is $164M or 3% greater than the total AR for 10/31/07.

Accounts Receivable Concentrations:

Customer	City & State	D & B	% Total A/R	Total	0-30	31-60	61-90	Over 90
DEL LABS	Uniondale, NY	LNR	27.9%	$1,565	$533	$578	$53	$401
DROCOSCA	Foreign		12.2%	684	142	367	103	72
O.P.I.	North Hollywood CA	NL	11.0%	614	556	57	-	1
VERA INTERNATIONAL (combined)	New Windsor, NY	1R3	8.1%	452	154	155	143	-
AMERICAN INTERNATIONAL	Los Angeles, CA	1R3	4.1%	227	225	2	-	-
JORDANA COSMETICS	Los Angeles, CA	1R3	2.9%	165	98	67	-	-
MARKWINS BEAUTY PRODUCTS	City of Industry, CA	1R3	2.9%	163	46	80	37	-
ORLY INTERNATIONAL	Van Nuys, CA	1R3	2.8%	156	31	84	41	-
MARKWINS INT'L CORP.	City of Industry, CA	1R3	1.9%	108	-	-	77	31
THE NEW MILANI GROUP, INC.	Los Angeles, CA	2R4	1.7%	97	22	48	27	-
Total Top Ten Accounts Receivable Concentrations			**75.5%**	**$4,231**	**$1,807**	**$1,438**	**$481**	**$505**
Not Analyzed			24.5%	1,372	845	312	195	20
Total Accounts Receivable			**100.0%**	**$5,603**	**$2,652**	**$1,750**	**$676**	**$525**

AR is fairly concentrated, with 51.1% of the total due from the top three customers. The company's largest customer, Del Labs, accounts for 27.9% of total AR; well below the 40% concentration limit imposed by SOV.

Accounts Receivable Statistics:

	12 Month Comparison		Change	
	Current	**Prior**	**Amount**	**Pct**
Sales	$ 29,464	$ 28,793	$ 671	2.3%
Collections	28,130	27,457	674	2.5%
Dilution	786	339	446	131.5%
Dilution %	2.7%	1.2%	1.5%	125.0%
Turnover	63.0	66.5	(3.5)	-5.3%

	6 Month Comparison		Change	
	Current	**Prior**	**Amount**	**Pct**
Sales	$ 15,923	$ 15,606	$ 317	2.0%
Collections	14,730	14,585	145	1.0%
Dilution	420	84	336	398.0%
Dilution %	2.6%	0.5%	2.1%	420.0%
Turnover	65.2	68.1	(2.9)	-4.3%

	3 Month Comparison		Change	
	Current	**Prior**	**Amount**	**Pct**
Sales	$ 7,907	$ 7,767	$ 140	1.8%
Collections	7,491	7,119	372	5.2%
Dilution	337	33	304	909.0%
Dilution %	4.3%	0.4%	3.9%	975.0%
Turnover	64.5	68.8	(4.3)	-6.2%

Sales

For the twelve, six and three month periods ended 10/3108 gross sales have shown modest increases when compared to similar periods ending 10/31/07. However, net sales (gross sales less dilution) were flat or lower when comparing the periods ended 10/31/08 to 10/31/07:

- For the 12 months ended 10/31/08 net sales totaled $28,678M which is $225M or 0.8% more than the net sales for the 12 months ended 10/31/07.
- For the 6 months ended 10/31/08 net sales totaled $15,503M which is $18M or 0.1% less than the net sales for the 12 months ended 10/31/07.
- For the 3 months ended 10/31/08 net sales totaled $7,570M which is $164M or 2.1% less than the net sales for the 12 months ended 10/31/07.

Dilution

Dilution for the comparable periods has increased; however, per the examiners analysis of credit memos, credits are generally issued to apply the customer deposits. When cash is received the Company debits cash and credits the customer deposit liability account. As this cash is applied the Company debits the liability account and credits AR. Per the examiners review the cash in advance is applied on average 6.125 days after the invoices is generated.

Turnover

Turnover has shown a modest improvement for the 12, 6and 3 month periods ended10/31/08 when compared to the same periods ending 10/31/07.

Credit Memo Test ($000's):

As noted in the dilution comments, credits are issued to move cash received in advance from the customer deposit liability account to the trade AR. All credits reviewed by the examiner were issued for this reason.

Analysis Summary		**Reason**	**Number**	**Amount**	**Percentage**	**Lag Days**
Beg Date:	1-Aug	Move CIA to AR	8	$ 261	100.0%	4.5
End Date:	31-Oct					
Total Amount Issued	$ 337	**Total Analyzed**	**8**	**$ 261**	**100.0%**	**4.5**
Total Number Analyzed	8					
Total Amount Analyzed	$ 261					
Percent Analyzed	77.5%					
Weighted Issue Lag	4.5					
Total Lag	4.5					

Credit and Collections:

The Company does not maintain credit files. Most customers are long standing and well known by the company. If the company does get a new customer, trade references are required and reviewed prior to shipping the customer. Credit limits are normally low; with increases occurring only after the customer has built up a history with the Company.

If customers become past due, cash in advance may be required along with a payment made against past due balances prior to new shipments being made.

Accounts Receivable Past Due Analysis ($000's):

The examiner selected 12 accounts with material past due and critical balances. A summary of the results appears below. For the balances analyzed, it appears that all of the past due and critical amounts are collectible.

	Critical		Past Due	
Reason	Amount	Percent	Amount	Percent
Subsequently Paid	$ 292	53.1%	$ 210	40.4%
Slow/Extended Terms	258	46.9%	310	59.6%
Total Analyzed	$ 550	**100.0%**	$ 520	**100.0%**
Total Analyzed	$ 550	81.4%	$ 520	99.0%
Not Analyzed	126	18.6%	5	1.0%
Total Per Aging	$ 676	100.0%	$ 525	100.0%

Shipping/Proof of Service Test ($000's):

The examiner selected 28 invoices totaling $1,016M, or 18.1% of the total AR balance. The examiner noted the following with regards to the invoice/shipping test:

	Number	Amount	Pct
Signed and Dated BOL	16	$ 557	55%
Subsequent Payment	7	338	33%
E-mailed Verified	5	122	12%
Items Verified	28	$ 1,016	100%
Invoices Tested	28	$ 1,016	100%

Verifications ($000's):

As shown above, the examiner verified the 12 invoices selected for the shipping test that were not supported by a signed and dated bill of lading. The ABO unit does not presently conduct verifications on this account.

Cash Review

Cash Application Testing:

The examiner selected 9 deposits totaling $2,843M and traced totals applied to AR to the deposits to the lock box account. No exceptions were noted. From these 9 deposits, 18 payments totaling $574M or 8% of cash received during the period of 8/1/08-10/31/08 were reviewed. All payments were applied properly and timely

Audit Period Status

	Number (1)	Amount	Pct.
Collected	18	$ 573	100%
CM / W/O	1	1	0%
Total Tested (1)	**18**	**$ 574**	**100%**

Verification

Check	16	$ 1,704	297%
Deposit Slip	14	2,565	447%
Bank Stmt	9	2,943	513%
Total Tested (1)	**18**	**$ 574**	100%

(1) If one or more invoices were partially collected, credited or written off, the sum of the categories will be greater than the number tested.

Analysis of Bank Deposits:

Below is the analysis of bank deposits. As can be seen the company will at times deposit AR cash into the operating account.

Source	Aug-08	Sep-08	Oct-08	Total	% of Total
Lending	$959	$711	$ 1,257	$ 2,927	27.3%
Co A AR (1)	521	266	426	1,213	11.3%
Lending to Cover Checks	1,959	2,292	2,324	6,575	61.4%
Total	$ 3,439	$ 3,269	$ 4,007	$ 10,715	100.0%
Total per Bank	3,439	3,269	4,008	10,716	
Variance	$-	$-	$(1)	$(1)	

(1) Difference in October between the deposited amount and the applied amount (see below) is cash received on 10/30 and 10/31/08. This cash was received and applied in October, but not deposited until November.

Reconciliation of Cash Receipts to Lockbox Deposits:

	Aug-08	Sep-08	Oct-08	Total
Gross Credit to A/R	$ 2,779	$ 2,419	$ 2,293	$ 7,491
Less: Discounts	-	-	-	-
Other items	-	-	-	-
Net A/R Collections	$ 2,779	$ 2,419	$ 2,293	$ 7,491
Total per Lock Box	2,922	2,953	2,879	8,754
Variance	$(143)	$(534)	$(586)	$ (1,263)
Co A AR in Oper acct (1)	(521)	(266)	(687)	(1,474)
Inter CO. Co B	401	550	659	1,610
AR Other – ATC	160	100	551	811
AR Other - Silver Ling, Fidelco,	2	12	1	15
Customer Advances	98	113	50	261
Miscellaneous (insurance, fees)	3	2	12	17
Purchases Nitro		23		23
Net Variance	$-	$-	$-	$-

(1) Difference in October between the deposited amount (see above) and the applied amount is cash received on 10/30 and 10/31/08. This cash was received and applied in October, but not deposited until November.

Reconciliation of Lockbox Deposits to Loan Reductions

	Aug-08	Sep-08	Oct-08	Total
Total per Lock Box	2,922	2,953	2,879	8,754
Total Per GE Records	2,906	2,861	2,872	8,639
Variance	$16	$92	$7	$115
DIT from this month (-)	70	85	177	332
DIT from Previous month (+)	(85)	(177)	(184)	(446)
Net Variance	$1	$-	$-	$1

Inventory:

General:

Co A manufactures nail polish. The production process consists of blending bases and alcohols with colorants that are then packaged into fifty five gallon, and five gallon drums and pails and shipped out to the end customers. Components are blends of raw materials that are used in a number of the more popular finished products. Per management raw materials and components can be sold to other manufacturers. Finished goods are made to customer specifications.

The examiner noted the following regarding the control of inventory:

- A perpetual inventory is not maintained by the Company
- Physical inventories are performed quarterly. "Quasi" inventory roll forwards are performed for the months that a physical is not done.
    - The company calculates the change in inventory by calculating the purchases to sales ratio. The change to inventory is a plug number that is derived to keep the purchases to sales ratio at approximately 55%.
- Certain raw material quantities are constantly updated. The company electronically tracks usage and levels of certain raw material chemicals such as Toluene, Butyl and Acetate.
- The unit cost (per pound or gallon) is based on the latest material costs. Labor and Overhead are capitalized and added to the GL as a separate line tem and not incorporated into the unit costs.

Inventory Reconciliations:

Below is the reconciliation of the 9/30/08 physical to the general ledger,

			Amount
Bal. Per Perpetual:	**9/30/2008**		$ 4,757
Additions:			
FG Packaging (1)		34	
Penn Color Processing (2)		28	
Labor and Overhead (3)		263	
Total Additions:			325
Adjusted Perpetual Balance			$ 5,082
Balance per the GL			$ 5,082
Difference:			$ -

(1) Eligible pails and drums, no reserve is necessary
(2) Per management, approximately $30M of inventory s at an offsite processor at any given time. The examiner has recommended a reserve for the inventory that is at the out side processor.
(3) Per review of the company's borrowing base, labor and overhead is not included in the gross inventory assigned; therefore no reserve is necessary.

Below is the reconciliation of the 9/30/08 general ledger amount to the balance sheet.

				Amount
Bal. Per General Ledger:	**9/30/2008**		$	5,082
Excess Obsolete (1)		170		
Total Subtractions:				170
Adjusted GL Balance			$	4,912
Balance per Financials			$	4,912
Difference:			$	-

(1) Per the examiner's review of the borrowing base, the gross inventory amount assigned is net of the excess and obsolescence reserve; therefore, an ineligible amount is not needed.

Inventory Composition and Comparison ($000's):

		Oct-08			Oct-07	
Description		**$Amount**	**Pct.**		**$Amount**	**Pct.**
Raw Materials	$	3,752	71.0%	$	3,173	69.1%
Work in Process		146	2.8%		149	3.2%
Finished Goods		388	7.3%		358	7.8%
Components		666	12.6%		665	14.5%
Packaging		73	1.4%		71	1.5%
L&O		261	4.9%		173	3.8%
Total	**$**	**5,286**	**100.0%**	**$**	**4,589**	**100.0%**

There has been no significant shift in the components and the relative balances when comparing the 10/3/08 inventory to the 1/31/07 inventory. Total inventory has shown a significant increase going from $4,589M as of 10/31/07 to $5,286M as of 10/31/08, an increase of $697M, or 15%. As inventory it predominantly made up of raw materials, most of the increase is caused by an increase to the raw material inventory. Some of this increase is due to the higher price of oil for 2008 compared to 2007. Inventory turns approximately once per quarter, the average price of crude the three months ended 10/08 was $91/bbl, for the three months ended 10/31/07 the average was $71/bbl.

Inventory Locations:

All inventory is located in Paterson N.J.

Inventory Turnover:

Inventory turnover averaged 83 days for the 9 months ended 9/30/08.

Book to Physical Adjustments:

The company performs full physicals once every quarter. The results of the physical do not result in an "adjustment," as the book is not updated for purchases or production during the month. The results of the physical simply become the new inventory amount for that month. In months where there is no physical, the company calculates the change to inventory by comparing purchases to sales. The inventory change amount is determined so that the ratio of the cost of materials remains at approximately 55% of sales.

Per the examiner's gross profit test, the percentage used appears reasonable. The examiner calculated a cost of goods sold percentage of 53% (1-47% gross profit).

Inventory Test Counts:

Test counts were not performed as the company does not have a perpetual inventory and the prior physical was performed approximately 70 days prior to the field exam. The examiner did take a tour of the manufacturing and storage facilities and noted the following:

- Approximately ½ of the finished goods on hand appeared to be make and hold inventory. Company personnel confirmed that on occasion, Co A will make inventory and hold it for the customer until the customer can take it. The inventory is not billed until it is shipped. The examiner has recommended a reserve for 50% of finished goods as all inventory is made to customer specification. In addition, there is no contractual obligation for customers to take inventory that is produced in quantities that exceed the amount ordered.
- The storage facilities appeared to be approximately 60%-80% utilized as of the date of the tour (12/9/08). Per company personnel, the inventory was relatively low. This is common for this time of year, as Co A does experience some seasonality, with heavy shipments occurring prior to the holiday season.

Inventory Cost Test:

The examiner selected 20 raw material items and 10 components for the purpose of performing a cost test. The cost test resulted in a nominal 1% net negative variance (carrying cost above verified costs). Due to the small variance, no reserve was recommended by the examiner.

Variance Analysis

	Items	Amount
Negative Variances (1)	12	$ (27)
Positive Variances (2)	16	11

	Amount	Percent
Net Variance (3)	$ (15)	-1.0%
Absolute Variance (4)	38	2.5%

Net Variance Frequency Analysis

	Items	Amt Tested	Percent
Over -10%	1	$ 66.3	4.3%
-5 thru -10%	4	268.5	17.4%
<0 thru -5%	7	248.8	16.2%
0%	2	219.4	14.2%
>0 thru 5%	14	694.5	45.1%
5 thru 10%	2	42.5	2.8%
Over 10%	-	-	0.0%

(1) Negative variances occur when the cost per source documents is below the cost on the Company provided report.
(2) Positive variances occur when the cost per source documents is above the cost on the Company provided report.
(3) The net variance represents the actual sum of the variances.
(4) The absolute variance represents the sum of the absolute value of all variances.

Gross Profit Review:

The examiner selected 28 items from invoices used to perform the invoice shipping test. The gross profit percentage for the items selected was 47%; however, the costs used by the examiner were material costs only. . The company reports a 30% gross profit for the 9 months ended 9/30/08, this included burden costs for direct labor, overhead and other direct costs. If these items are eliminated, the company gross profit would be 45% which is in line with the examiner's results. In addition to the average gross profit percentage of 47%, the examiner noted the following:

- All items tested sold for a profit.
- The minimum gross profit % noted was 27.5%, the maximum was 67.5%
- 23 of the 28 items or 83% of the amount tested had a gross profit in excess of 40%

G/P Test Statistics

G/P Per Company:	30.0%	Items Tested:	28
G/P per Test:	47.0%	Sales $ Tested:	$ 200
Less Cash Dil:	0.0%	Cost $ Tested:	106
Less Misc Dil:	0.0%		
Net G/P Per Test:	47.0%	Avg Price/Unit:	$ 10.20
Min G/P%:	27.5%	Avg Cost/Unit:	5.41
Max G/P%:	65.5%	Avg G/P per unit:	$ 4.80

G/P Frequency Analysis

	Items	Sales Amt	Percent
Less than 0%	-	$ -	0.0%
0%	-	-	0.0%
Over 0% to 10%	-	-	0.0%
Over 10% to 20%	-	-	0.0%
Over 20% to 30%	1	13.14	6.6%
Over 30% to 40%	4	20.13	10.1%
Over 40%	23	167.04	83.4%

Gross Profit by Product

Description	Items	Sales	Cost	Percent
FG Nail Polish	25	$ 187.2	$ 99.7	46.7%
FG Treatment/Clear	2	8.0	3.8	52.5%
FG Base	1	5.1	2.6	49.1%
Total		$ 200.3	$ 106.1	47.0%

Accounts Payable

General

Major vendors include suppliers of chemicals and colorants. Raw material purchases include nitro, resin, pigments and solvents. There are not many sources for key ingredients. Suppliers are chosen by the president of the company and the purchasing department. Major ingredients are tested and sampled prior to purchases being made.

Terms of sale are generally net 60. Purchases are made on open account; the Company does not have any supply/purchase contracts. The Company's aging is based on invoice date and has aging categories of 1-30, 31-60 and over 60. The Company's largest vendor is BP Chemicals. BP Chemicals accounts for 18% of the total AP as of 10/30/08 and 14% of total purchases for the nine months ended 9/30/08.

Accounts Payable Reconciliations:

The AP is reconciled on a monthly basis by the accounting department. The CFO (Sharon Muzeni) reviews the reconciliation. Below are the AP to General Ledger and AP Trade GL account to Balance Sheet reconciliations.

AP Trial Balance to General Ledger Reconciliation

			Amount
Aging Date:	**9/30/2008**		$ 3,777
Additions:			
	Payments open, invoice not	21	
Total Additions			21
	Inter co Co B	32	
Total Subtractions			32
Adjusted Aging Balance:			$ 3,766
Balance per G/L			$ 3,767
Difference:			$ (1)

General Ledger to Balance Sheet Reconciliation

			Amount
G/L Date:	**9/30/2008**		$ 3,767
Additions:			
	Inter-Co. Co B	32	
	Outstanding Checks	581	
Total Additions			613
Subtractions:			
	AP Rebates	33	
Total Subtractions			33
Adjusted G/L Balance:			$ 4,347
Balance per Balance Sheet:			$ 4,347
Difference:			$ -

Accounts Payable Aging Comparison ($000's):

	Current		Prior	
	10/31/2008		10/26/2007	
Description	Amount	Percent	Amount	Percent
0 - 30 PID	$ 1,782	48.5%	$ 1,226	51.0%
31 - 60 PID	1,394	38.0%	693	28.9%
Over 60 PID	495	13.5%	483	20.1%
Total Per Aging	**$ 3,671**	**100.0%**	**$ 2,402**	**100.0%**

Total accounts payable has shown a material increase, going from $2,402M as of 10/26/07 to $3,671M as of 10/31/08.

Accounts Payable Concentrations ($000's) Invoice Date Basis:

Vendor	Terms	% Total A/P	Total	0 - 30 PID	31 - 60 PID	Over 60 PID
T.N.C. Industrial Co., LTD.	Net 60	17.8%	$654	$0	$319	$335
BP Chemicals, INC.	Net 60	11.1%	409	237	172	-
Kama International Corp.	Net 30	9.2%	336	169	167	-
Oxea Corporation	Net 30	8.0%	295	295	-	-
Eckart Cosmetic Colours, LLC	2%B 2% 10, Net 60	4.6%	168	145	23	-
Penn Color, Inc.	Net 60	4.4%	162	73	89	-
EMD Chemicals Inc.	1% 10, Net 60	4.4%	160	74	86	-
KCI Limited	Net 60	4.1%	151	-	151	-
Vototantim GmBH	60 days BL date	3.7%	135	-	43	92
Tri State Steel Drum Corp.	Net 30	2.8%	104	80	24	-
Total Top Ten Accounts Payable Concentrations		**70.1%**	**$2,574**	**$1,073**	**$1,074**	**$427**

The AP is fairly concentrated with 70% of the total due from the top ten vendors; however, there are multiple suppliers available for all products needed in the production process.

A/P turnover/Vendor Payment Test:

The examiner selected 15 checks totaling $6,405M or 15% of the amount disbursed for te period of August 2008 through October 2008 and noted the following:

- 13 of the checks were for trade vendors. The average number of days between the invoice date and the cleared date was 58 days
- 2 of the checks were for non-trade vendors. The average number of days between the invoice date and the cleared date for the non trade items was 32 days.

Other:

Bank Account Review and Bank Reconciliations:

The examiner reviewed the bank reconciliations for the Lending Lock Box, Lending operating and Commerce bank operating accounts. Other then Co A cash receipts being deposited into both the Lending and Commerce operating accounts, no unusual items were noted.

Cancelled Check/Wire Review:

The examiner requested the underlying documentation for the 15 payments selected in the vendor payment test (see above). All payments were supported by check remittance advices and vendor invoices. The examiner did not note any discrepancies between the remittance advice, the check amount and the invoices being paid.

Insurance:

Below is a summary of the Company's major insurance policies:

Types of Coverage	Insurer	Policy Number	Limits	Expiration Date	Adequate?	Loss Payee
General Liability	Greenwich Insurance Co.	GEC000247008	$1MMOcc, $2MM Aggregate	4/21/09	yes	Lavial Ltd (Certificate holder)
Automobile Liability	Greenwich Insurance Co.	AEC000247108	$1,000M	4/21/09	yes	Lavial Ltd (Certificate holder)
Excess/Umbrella Liability	American Guarantee and Liability Ins	AUC3807735-04	$25,000M	4/21/09	yes	Lavial Ltd (Certificate holder)
Property Insurance - 6th St.	Underwriters At Lloyds	AMR23074	6,317M - Building	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)
Property Insurance - 6th St.	Underwriters At Lloyds	AMR23074	$5,000M - Flood	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)
Property Insurance - 6th St.	Underwriters At Lloyds	AMR23074	$5,000M - Earthquake	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)
Property Insurance - 11th St.	Underwriters At Lloyds	AMR23074	9,252M - Business Income	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)
Property Insurance - 11th St.	Underwriters At Lloyds	AMR23074	1,363M - Building	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)
Property Insurance - 11th St.	Underwriters At Lloyds	AMR23074	$5,000M - Flood	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)
Property Insurance - 11th St.	Underwriters At Lloyds	AMR23074	$5,000M - Earthquake	4/21/09	yes	StanCorp Mortgage Investors, LLC (additional interest)

Taxes:

The person that handles taxes was not available during the field visit; therefore taxes were not reviewed during the field work. The appropriate documentation was to be scanned and e-mailed to the examiner for review, but to date these have not yet been received.

The examiner did review bank statements for the period of July 2008 through October 2008 and noted ADP impounds hitting the bank statement for the payment or payroll taxes.

Accrued and Deferred Assets and Liabilities:

Per the SAM: there is currently an open dispute between the French Government and Co A's affiliate; Co B, which remains unresolved. Co B currently has a $2MM note due to SNPE, Inc. which bears interest at 7% payable semi-annually and the Company is currently not paying interest until their disagreement is resolved. Lending will closely monitor this situation and will not move forward until an acceptable resolution is reached in order to protect the best interests of the Bank.

Data Processing System/Environment:

The company utilizes two major software systems; Platinum and Macola. The general ledger and financial systems as well as the AP subsystem are maintained in Macola. AR and inventory subsystems are maintained in Platinum. Operational processes such as ordering and manufacturing are also maintained/performed in Platinum.