



Court File No. 04-CL-5491

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

**COMMERCIAL LIST**

**IN THE MATTER OF THE COMPANIES'  
CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-  
36, AS AMENDED**

**AND IN THE MATTER OF A PLAN OF COMPROMISE  
OR ARRANGEMENT OF AFTON FOOD GROUP LTD.,  
AFTON FOOD GROUP INC., JOINT TECHNOLOGIES  
INC., KEDARD HOLDINGS LTD., ROBIN'S FOODS  
INC., MRS POWELL'S (CANADA) INC., 241 PIZZA  
(1997) INC., RUFFAGE INTERNATIONAL INC.,  
CYBERSENSATIONS CAFÉ INC., MRS. POWELL'S,  
INC. and KIDSPORTS CAPITAL CORPORATION AND  
OTHER APPLICANTS LISTED ON SCHEDULE "A"**

(the Applicants)

**THIRD REPORT OF THE MONITOR – DOYLE SALEWSKI INC.  
October 1, 2004**

**I. INTRODUCTION, PURPOSE AND QUALIFICATIONS**

***Introduction***

1. On July 16, 2004, Afton Food Group Ltd. and certain of its subsidiaries (collectively, the "Applicants") filed for, and obtained, protection from their creditors under the *Companies' Creditors Arrangement Act*, R.S.C. 1985 c. C-36 (the "CCAA"). The terms of this proceeding are governed by an order of this court dated July 16, 2004 (the "Initial Order"). Pursuant to the Initial Order, Doyle Salewski Inc. ("DST") was appointed as monitor (the "Monitor") of the Applicants. A copy of the Initial Order is attached as Appendix "A".

2. By order dated July 27, 2004 of the Honourable Mr. Justice Nordheimer, the Initial Order was amended *nunc pro tunc* to include the companies listed in Schedule "A". A copy of the July 27, 2004 order is attached hereto as Appendix "B".

3. The terms of the Initial Order were extended by order of the Honourable Madam Justice Hoy on August 13, 2004 (the "August 13, 2004 Order"). A copy of the August 13, 2004 Order is attached hereto as Appendix "C".

4. Further background information is outlined in the first report of the Monitor dated July 23, 2004 (the "First Report"), the supplement to the First Report dated July 16, 2004 and the second report of the Monitor dated August 11, 2004. As noted in the First Report, copies of Monitor's reports and the court orders issued to date are available on the Monitor's web-site [www.doylegroup.ca](http://www.doylegroup.ca).

*Purpose*

5. The purpose of this third report of the Monitor (the "Third Report") is to provide information to the court in connection with the following:

- (a) the status of the Applicants' operations, restructuring efforts and cash flow since the Second Report as at September 25, 2004;
- (b) to summarize the process proposed by the Monitor to solicit purchasers or investors for the Applicants' businesses;
- (c) to obtain the court's approval for the Applicants' retainer of Capitalink, L.C. ("Capitalink") and to provide a charge for Capitalink's fees and expenses;
- (d) the Applicants' request that the court authorize them to disclose to prospective investors and/or purchasers Personal Information (as defined in this report) with respect to the Applicants' employees, subject to the restrictions contemplated in this report; and
- (e) the Applicants' motion to extend the terms of the Initial Order to December 13, 2004.

*Qualifications*

6. The information contained in this report has been obtained from the records of the Applicants and is based on discussions with, and representations made by, management of the Applicants and other professional advisors retained in this matter.

7. The financial information of the Applicants has not been audited, reviewed or otherwise verified by the Monitor as to its accuracy or completeness, nor has it necessarily been prepared in accordance with generally accepted accounting principles and the reader is cautioned that this report may not disclose all significant matters about the Applicants. Accordingly, the Monitor does not express an opinion or any other form

of assurance on the financial or other information presented herein. The Monitor may refine or alter its observations as further information is obtained or is brought to its attention after the date of this report.

8. The Monitor assumes no responsibility or liability for any loss or damage occasioned by any party as a result of the circulation, publication, reproduction or use of this report. Any use that any party makes of this report or any reliance on or decisions that are made based on this report are the sole responsibility of such party. All dollar amounts identified in this report are expressed in Canadian dollars, unless otherwise specified.

## II. RECENT DEVELOPMENTS

### A. The Applicants' Current Financial Position, Restructuring Efforts, and Status of Operations

#### *Current Financial Position*

9. Attached as Appendix "D" is the original consolidated cash flow projection dated July 15, 2004 prepared by the Applicants and filed in connection with the Initial Order.

10. Attached as Appendix "E" is the revised consolidated cash flow projection dated July 15, 2004, which was presented to the court at the initial application hearing on July 16, 2004 (the "July 16, 2004 Cash Flow").

11. Attached as Appendix "F" is a consolidated cash flow projection dated August 11, 2004 which was presented to the court at the August 13, 2004 hearing (the "August 11, 2004 Cash Flow").

12. As at September 25, 2004, the Applicants experienced net cash flow which is favourable relative to the July 16, 2004 Cash Flow.

13. For the period from July 16, 2004 to September 25, 2004, the Applicants' consolidated cash receipts were \$3,251,522.15 compared to a budget of \$2,833,407.96 representing an increase of \$418,114.19. Management has advised that these variances are due to, *inter alia*:

- (a) account receivable collections from the Robin's Donuts® accounts were budgeted at \$306,000.00 while the actual collections were \$390,746.70, representing an increase of \$84,746.90;
- (b) volume rebate collections are \$468,326.11 compared to a budget of \$385,000.00, representing an increase of \$83,326.11;
- (c) the Applicants received an additional \$50,000.00 in volume rebates, which were earned prior to the CCAA filing, and were not included in the original forecast;

- (d) volume rebates earned by the 241 Pizza® franchisees were \$85,591.02 compared to a budget of \$60,000.00 or an increase of \$25,991.02;
- (e) miscellaneous collections of \$82,175.75 due largely to the receipts of pre-filing and current GST refunds, sale of miscellaneous food inventory and other items;
- (f) management negotiated the sale of a 241 Pizza® franchise; and
- (g) corporate store sales were \$980,511.52 compared to a budget of \$769,000, an increase of \$211,511.

14. The cash disbursements to September 25, 2004 were \$2,438,076.81 compared to a budget of \$2,657,269.02 or a decrease of \$219,192.39. The principal reduction arises due to the following:

- (i) supplier payments are \$169,625 less than forecast; and
- (ii) government payments are under budget by \$108,000.00 due to a variety of factors.

15. Attached as **Appendix "G"** is a copy of the consolidated cash position of the Applicants to September 25, 2004. The net cash position of the Applicants at September 25, 2004 is \$435,301.66 versus a projected shortfall of \$75,026.04. This is a favorable variance of \$510,327.71.

16. The Applicants are projecting a net cash flow balance of \$542,339.18 as at December 31, 2004. Attached as **Appendix "H"** is a consolidated cash flow projection dated October 1, 2004 for the period September 27, 2004 to December 31, 2004.

***Restructuring Efforts***

17. As part of its role as Monitor, DSI has continued to meet with management of the Applicants to discuss and implement restructuring initiatives. Some of the specific actions taken by the Applicants since the Second Report include:

- (a) terminated unprofitable leases;
- (b) terminated under-performing franchises;
- (c) terminated employees;
- (d) continued to develop and source outside financing;
- (e) met with franchisees to address their concerns; and
- (f) considered several merchant banking firms to assist with the investment/sale process.

18. As required under the Initial Order, the Monitor continues to report and consult with Zeifman Partners Inc. ("Zeifman"), the agent for the Applicants' senior lenders, namely Rabobank Nederland, Canadian Branch ("Rabobank"), Credit Union Central of Ontario Limited and Hepcoe Credit Union (collectively, the "Senior Lenders").

19. The Monitor and the Applicants have also consulted with Zeifman, as required, pursuant to the August 13, 2004 Order, with respect to the selection of a merchant banking firm, the particulars of which are discussed below.

*Status of Operations*

20. At this stage of the CCAA proceedings, it appears that the Applicants have stabilized their operations and have continued to maintain the integrity and functionality of their businesses. As noted above, the cash flow for operations is well above forecast and is projected to be satisfactory for the period. Accordingly, management has determined that it does not require a debtor-in-possession facility.

*(a) Matters Raised in the Second Report – Status Update*

21. Management has continued its discussions with certain goods and service providers during the stay period. In general, the Applicants have requested that their suppliers provide credit terms as provided for in the contractual agreements. Customers and suppliers have continued to support and maintain business relations with the Applicants. The issues the Applicants faced with respect to one of their suppliers, Mother Parkers Tea & Coffee Inc., have been resolved for the time being. However, there are outstanding issues with respect to another supplier, Dawn Food Products (Canada) Ltd., which will require further negotiations.

22. On August 10, 2004, the Applicants terminated the franchise and sub-lease agreements of the Saskatchewan franchisees who are listed in the Second Report. Since that time, the Applicants have turned one of these franchises into a corporate store, one has continued as an independent business, and two locations have been closed. Management is actively seeking to re-franchise the location that is being operated as a corporate store as part of the restructuring process.

23. The Applicants have also concluded the North Bay Transaction (the details of which are outlined in the Second Report).

24. The Senior Lenders have maintained their objection to the payment of the directors' professional fees. By letter dated September 22, 2004, the Senior Lenders have advised the Monitor and management that they will not consent to the payment of these fees without Monitor's consent and court approval. The Monitor is, therefore, seeking the court's direction on this matter.

**(b) Recent Developments**

25. The Applicants are in the process of finalizing an agreement with a new call centre, Call Cast, to service its 241 Pizza® franchisees. This proposed agreement would replace the existing call centre host, Opal On Line, at a cost of approximately \$100,000.00. The agreement, which is on commercially reasonable terms, is scheduled to close in November 2004. The existing structure was not providing the franchisees with a suitable level of support. The Monitor has, therefore, authorized, and the Applicants have remitted, a \$20,000.00 deposit to Call Cast. It is anticipated that the new structure will be operating in December 2004.

26. The Monitor has also authorized the payment of a pre-filing obligation to a credit card company. The company in question issued corporate cards to the Applicants' employees. Pursuant to the credit agreement, the employees were held jointly and severally liable for the charges made on the cards. The credit card company also holds a letter of credit with Rabobank.

27. The credit card company advised management that it would either call the letter of credit and cancel the cards or pursue the employees. Payment of this pre-filing obligation was, therefore, in the best interest of all stakeholders and was made with Rabobank's consent.

28. Management is refusing to remit payment for an alleged post-filing obligation to Century Services Inc. The Monitor is seeking the court's direction with respect to this matter.

29. The Senior Lenders have expressed concerns with respect to the status of the Applicants' accounts receivable and rent collections. In response to this concern, which is shared by the Monitor, management is in the process of formulating an action plan for the collection of these amounts.

**B. The Proposed Marketing & Sale Process**

30. Pursuant to the August 13, 2004 Order, the Monitor was authorized to prepare an information package for the purposes of marketing the Applicants' business for sale and soliciting investors.

31. As indicated in the Second Report, the Monitor recommended a sale/investment process proceed on a parallel track with the Applicants' development of a refinancing and restructuring plan.

32. The Monitor also recommended that the Applicants be authorized and empowered (subject to the consent of the Monitor and on consultation with Zeifman) to execute agreements with a merchant bank to assist with the marketing process. A merchant banking firm was identified, and with the Monitor's consent and with due consideration to Zeifman's input, the Applicants have retained Capitalink.

33. The Monitor, therefore, recommends that the going concern sale/investment process proceed as follows:

- (a) the invitations to invest and/or purchase will be issued shortly;
- (b) Capitalink will advise the Monitor in due course of any suitable offers;
- (c) if the marketing process results in an offer that is more beneficial to stakeholders than other options, the Monitor will return to the court as soon as practicable with its recommendations regarding the potential going concern sale or investment; and
- (d) the CCAA stay should be extended to December 13, 2004 to complete any proposed transaction.

**C. Capitalink**

34. With the Monitor's consent, and on consultation with Zeifman, the Applicants retained Capitalink (the "Retainer") to assist the Applicants with the marketing process.

35. To give effect to the Retainer, Capitalink must be provided with a charge for its fees and expenses.

36. The Monitor believes that the Retainer is on commercially reasonable terms and is in the best interests of the Applicants' stakeholders. A copy of the Retainer will be provided to the court at the return of the October 6, 2004 hearing.

**D. Disclosure of Personal Information**

37. In order for the Applicants' business to be marketed on a going-concern basis, it will be necessary to disclose certain information about the Applicants' employees (i.e. job title, years of service, compensation, vacation pay entitlement and other similar job-related information (the "Personal Information")). Prospective purchasers routinely request information of this nature. In this regard, the Applicants will require any recipient of Personal Information to enter into a confidentiality agreement restricting that party's ability to use or retain such information.

38. If the Applicants are not permitted to disclose Personal Information, it may be difficult for the Applicants to obtain and provide this information in a timely manner given the large number of employees involved, thereby potentially impairing the Applicants and thereby Capitalink's ability to market the business on a going-concern basis on an expedited basis.

39. A copy of the form of confidentiality agreement for this engagement is attached hereto as Appendix "T".

**E. Extension of the Stay**

40. Pursuant to the August 13, 2004 Order, the stay period expires on October 13, 2004.

41. An extension to the stay to December 13, 2004 is necessary to enable the Monitor and the Applicants to proceed with the investment/sale process and to be in a position to provide their creditors with a plan of arrangement or compromise.

42. In the Monitor's view, the Applicants are acting in good faith and with due diligence during this CCAA proceeding. The Monitor is further of the view that the extension requested is appropriate in the circumstances.

**III. RECOMMENDATIONS**

43. The Monitor recommends approval of the marketing and sale process detailed herein.

44. The Monitor also recommends that the court approve the Retainer, the amendments to the Initial Order and the minor procedural issues noted in the draft order.

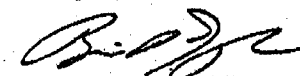
45. The Monitor further recommends that the Applicants be authorized to disclose Personal Information with respect to the Applicants' employees subject to the execution of a confidentiality agreement restricting the use and retention of this information, as well as the restrictions detailed in the draft order.

46. Lastly, the Monitor recommends that the Applicants' request for an extension of the Initial Order to December 13, 2004 be granted.

All of which is respectfully submitted on this 1<sup>st</sup> day of October, 2004.

**DOYLE SALEWSKI INC.**

In its capacity as Monitor of the Applicants



Brian P. Doyle, CA, CIRP  
President