



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)

**FIFTH REPORT OF THE MONITOR – DOYLE SALEWSKI INC.
February 10, 2005**

I. 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 "CCA"). 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. ("DSI") was appointed as monitor (the "Monitor") of the Applicants.
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" of the order.
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"). The terms of the Initial Order were

further extended to December 13, 2004 by order of the Honourable Mr. Justice Farley dated October 6, 2004. On December 13, 2004 there was a further extension by the Honorable Madam Justice Lax. Copies of previous orders are contained in our prior four reports, save and except the most recent order of the Honourable Madam Justice Lax which is enclosed as **Appendix "A"**.

4. Further background information is outlined in the Monitor's previous reports which are available on the Monitor's web-site www.doylegroup.ca.

II. Purpose

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

- i. the status of the Applicants' current financial position, operations, and restructuring efforts since the Monitor's fourth report dated December 8, 2004 (the "Fourth Report"); and
- ii. the Applicants' motion to extend the terms of the Initial Order to February 23, 2005.

III. 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. 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.

IV. The Applicants' Current and Projected Financial Position and Status of Operations

9. The Applicants have been proceeding in good faith and with due diligence in continuing to restructure their operations. Some of the most significant events since the Fourth Report are described below.

(i) Current and Projected Financial Position

10. Enclosed as **Appendix "B"** is a Statement of Receipts and Disbursements of the Applicants for the period December 6, 2004 to February 5, 2005.

11. As at February 5, 2005, the Applicants' cash flow position is \$513,217.89. Based on the cash projection submitted in the Fourth Report projecting a bank balance of \$627,540.51, this is a shortfall of \$114,322.62 from the submitted budget.

12. The cash shortfall can be attributed to several reasons, including:

- (i) Shortfall in sales by corporate stores due to weather and store closures;
- (ii) Lower royalties of 241 Pizza ® due to call centre issues;
- (iii) Additional outlays required for the call centre which were not budgeted.

13. Specific deviations from budget which are included in the variances noted in **Appendix "B"** are detailed as follows:

(i)	Shortfall in Collection of 241 Royalties Due to Call Centre Issues	(58,145.00)
(ii)	Robin's Royalties shortfall (timing difference)	(39,000.00)
(iii)	Collection of Robin's SAF Arrears (Volume Rebates) not in budget	55,108.00
(iv)	Actual Robin's Collections of SAF (Volume Rebates) less than budget	(17,227.00)
(v)	Net Cash Loss in Corporate Store Sales	(66,000.00)
(vi)	Outlay for Call Centre Not Budgeted	(63,449.00)
(vii)	Adfund Outlay Budgeted but not Taken	50,000.00
(viii)	Insurance – timing difference	23,799.00
	Amount Summarized	(114,914.00)
	Other	591.38
	Net Ending Cash Variance	(114,322.62)

14. Notwithstanding the shortfall in the time period projected since our last report, the Applicants have performed better than anticipated from the outset of the filing of the CCAA.

15. Enclosed as **Appendix "C"** is a cash forecast prepared by the Applicants for the period February 6, 2005 to March 31, 2005. The forecast projects a positive cash balance for the Applicants for the time period.

16. The Applicants are up to date with all their post filing obligations and are in position to maintain same during the proposed extension period.

(ii) Status of Operations

17. At this stage of the CCAA proceedings, the Applicants have continued their operations and have maintained the integrity and functionality of their businesses. As noted above, the cash flow for operations is overall positive and is projected to be satisfactory for the proposed extension period.

18. 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, Dawn Food, have now been resolved. The latter is continuing to provide products to the Applicants and a new agreement has been reached.

(iii) Directors and Officers Insurance

19. The Applicants were successful in securing directors and officers insurance through to February 28, 2005. As such, it is anticipated that the CCAA process will have terminated on or before that date and no further insurance will be required.

(iv) Arrears of Wages – Mr. Robert MacDonald

20. As at July 1, 2003, a severance liability in the amount of \$562,920 had been set up in the books of Afton Food Group Inc. on behalf of Mr. Robert MacDonald (Contract Marketing). This liability reflects salary, bonus and vacation pay earned under the employment agreement between Mr. MacDonald and Afton Food Group Inc. However, this excludes any potential pension and health benefit obligations that may accrue to the benefit of Mr. MacDonald.

21. Payments made by the Applicants from July 15, 2003 to July 31, 2004 reduced the obligation by \$67,708 to \$495,212. On July 7, 2004, Mr. MacDonald submitted an additional claim for outstanding wages in the amount of \$110,865. These wages were earned prior to June 20, 2003. This amount increases Mr. MacDonald's claim to \$606,077 as at July 2004.

22. The Monitor was notified of the claims by correspondence dated August 13, 2004 from Mr. MacDonald's counsel, Mr. Eversley. The correspondence is enclosed as **Appendix "D"**. These amounts do not reconcile to the general ledger balances which have been provided to the Monitor. Should this issue become of relevance to the court, the Monitor will have to do further research.

23. As the liability had arisen prior to the CCAA proceedings and the claim is unsecured, the Monitor and its counsel are of the opinion that this not a claim to be paid by the Applicants at this time. Payment would only be expected to be considered if there are funds in excess of secured creditor claims. The Monitor and the Applicants believe this to be highly unlikely.

(v) 241 Pizza ® Call Centre

24. As set out in the Fourth Report, the Applicants reached an agreement with a new call centre, Call Cast, to service the 241 Pizza ® franchisees. As reported to this Honourable Court, a number of significant problems ensued and management undertook corrective action.

25. Difficulties continued through December 2004 and January 2005. A royalty moratorium was offered to the franchisees which have affected the Applicants' cash flow.

26. Prior conversion issues that dealt largely with the computer hardware and software at both call centre and franchisee sites have largely been resolved. Prior problems associated with Bell Canada have also been corrected.

27. The most significant issue that remains outstanding is with the new call centre still having a shortage of trained personnel to service the demands of its customer 241 Pizza. This ongoing problem has been addressed by Call Cast and the Applicants by engaging the service of another call centre to handle the overflow in demand to take pizza orders during peak times. This has acted as a stop gap measure to reduce the number of lost phone calls and lost orders.

28. Management continues to work with Call Cast to minimize the disruption to the franchise operations and anticipates that Call Cast will be able to conduct call centre operations without any interruptions very shortly.

(vi) Potential Landlord Obligations

29. The Applicants operating under the Robins' trademark have entered into a number of direct leases with various landlords. At the time of CCAA appointment, some landlords had not received payment for the month of July 2004 and/or earlier. As well, some of the cheques by the Applicants were returned as NSF. In addition, there are amounts potentially due to the landlords for % rent and CAM charges (percentage rent and common area maintenance charges) relating to July 16, 2004 and prior. Based on information provided, the Monitor estimates that a potential \$129,000 may be due to landlords for stores that presently remain open. This liability may be reduced by a nominal amount for franchisees that will be responsible to remit their share of CAM and % Rent that have not been paid to date.

30. The Applicants operating under the 241 Pizza Trademark have entered into a number of direct leases with various landlords. However, 241 Pizza ® franchisees remit payment directly to the landlord. As a result, the Applicants are not aware of the status of leases with the tenants until they receive notification of an arrears issue from the landlord. At the time of this report, management tells us that they have two formal notices of arrears as detailed below:

- (i) Rent is being claimed owed to a landlord for an aggregate amount of \$37,238.81. Of the amount claimed, \$16,874.00 accrues prior to July 16, 2004 and a further \$20,364.81 including accelerated rent obligations subsequent to the CCAA filing. The Applicants repudiated the lease

effective at the end of December 2004. The Applicants have not made any payments to the landlord.

- (ii) In January 2005, a landlord notified the Applicants that the franchisee was in arrears of two months rent in the amount of \$12,176.60. The Applicants were notified as named on the lease as the head tenant. The Applicants made arrangements with the franchisee and the landlord that the franchisee would pay \$2,176.60 immediately to the landlord and pay the balance of \$10,000 in three equal installments, with payment commencing on February 15, 2005 and the following two months. The Applicants are not aware whether the franchisee is fulfilling its obligation to the landlord.

31. Accordingly, the Monitor is unaware of the status of currency of payment of leases of certain franchisees notwithstanding the requirement under the Initial Order to pay same.

(vii) Manufacturing and Supply Agreements

32. The Applicants undertook a review of their current Manufacturing & Distribution contracts. The major findings were:

- (i) The remaining term on the contracts range from approximately one year to seven years. In some cases, there is not an expiry date attached to the existing contract.
- (ii) The contracts may provide opportunities to reduce the cost of manufacturing and or distribution if the Applicants can increase its annual volumes over the past year.
- (iii) Some contracts contain cost increases when either there is a slippage in the supplier's gross margin or an increase in either the cost of a commodity or a general cost increase.

33. As the CCAA process provides an opportunity for the Applicants to restructure its business affairs, to date the following has occurred:

- (i) The Applicants have invited their current manufacturing and distributor suppliers to requote their contracts with the Applicants. In some cases, this has allowed the current supplier to maintain business with the Applicants at a lower cost to the Applicants and its Franchisees;
- (ii) The Applicants have also found alternative distributors to distribute certain of their products in Canada. This reduces the number of distributors in both the 241 and Robins' chains. Negotiations formal terms with these distributors are underway.
- (iii) Repudiation letters have been issued to three existing suppliers.
- (iv) An amending agreement with a supplier, Dawn Foods, has been signed. Upon signing the agreement, the supplier remitted approximately \$55,000 in volume

rebates owing to the Applicants prior to the CCAA period that the supplier previously refused to release.

34. When companies change from one supplier to another an orderly transition period usually takes place over a six to ten week period. This process allows for the incumbent to work through its inventory while the new supplier has the time to prepare for the additional business.

V. Restructuring Efforts

35. The Applicants have continued to work diligently with Capitalink and the Monitor to identify a strategic partner and develop a refinancing and restructuring plan. As such, the result of their efforts is a proposed transaction with Loretta Foods, which appears to be acceptable to the Applicants and the senior secured creditor. However, final details of a proposed transaction are still undetermined at the time of writing of this report. Counsel for the Applicants and the Monitor will advise the court directly. The Affidavit of Mr. Bruce Smith is expected to provide details of a proposed transaction to the court.

36. We are satisfied, given the financial and operational condition of the Applicants, that reasonable efforts have been made and that a commercially reasonable transaction is proposed with Loretta Foods.

VI. Extension of the Stay

37. Pursuant to the Order of the Honourable Madam Justice Lax dated December 13, 2004, the stay period expires on February 14, 2005.

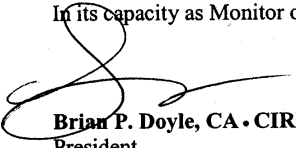
38. An extension of the stay to February 23, 2005 is necessary to enable the Applicants to proceed with an asset purchase agreement with Loretta Foods.

39. 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.

All of which is respectfully submitted on this 10th day of February, 2005.

DOYLE SALEWSKI INC.

In its capacity as Monitor of the Applicants



Brian P. Doyle, CA • CIRP
President