RSM Richter Inc.
2, Place Alexis Nihon
Montréal (Québec) H3Z 3C2
Téléphone : (514) 934-3497
Télécopieur : (514) 934-3504
www.rsmrichter.com

RSM Richter Inc.

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL
No.: 500-11-041238-110

S U P E R I O R C O U R T
(Commercial Division)
The Companies' Creditors Arrangement Act

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT,* R.S.C. (1985), c. C-36 WITH RESPECT TO:

HART STORES INC. / MAGASINS HART INC., a legal person having its head office at 900 Place Paul-Kane, in the City and District of Laval, Province of Québec, H7C 2T2 and a place of business at 7852 Boulevard Champlain in the City and District of Montreal, Borough of LaSalle, Province of Quebec, H8P 1B3

Debtor

-and-

RSM RICHTER INC., a duly incorporated legal person having its principal place of business at 2 Place Alexis-Nihon, in the city and district of Montreal, Quebec, H3Z 3C2

Monitor

FIRST REPORT OF THE MONITOR ON THE STATE OF THE DEBTOR'S FINANCIAL AFFAIRS
September 27, 2011

INTRODUCTION

1. On August 30, 2011, Hart Stores Inc. (hereinafter referred to as "Debtor" or "Hart Stores") filed with the Quebec Superior Court, a Motion for the Issuance of an Initial Order pursuant to Section 11 of the *Companies' Creditors Arrangement Act,* R.S.C. 1985, C-36, as amended (the "CCAA"). In this regard, the Honourable Jean-Yves Lalonde, J.S.C. rendered the Initial Order appointing RSM Richter Inc. ("Richter") as monitor (the "Monitor").

2. On September 28, 2011, the Debtor will present a Motion for an Order Extending the Stay Period (as defined in the Initial Order) up to and including November 4, 2011 and amending the Initial Order.

3. This First Report of the Monitor has been prepared in order to inform the Court on the following:

   A. General Information about the Debtor

   B. Events leading to the CCAA filing

   C. Debtor's restructuring measures

   D. Operations

   E. Cash flow projections

   F. Activities of the Monitor

   G. Motion to extend the Stay Period and amendments to the Initial Order

4. We inform the Court that the Monitor has not conducted an audit or investigation of the information that was provided by the Debtor and that accordingly, no opinion is expressed regarding the accuracy, reliability or completeness of the information contained within this report. The information contained herein is based on unaudited financial information provided to the Monitor by the Debtor's management as well as obtained through discussions with the Debtor's management and employees.

5. The cash flow projections appended to this report were prepared by the Debtor's management and are based on underlying financial assumptions. The Monitor cannot provide an opinion as to the accuracy, completeness or reliability of these projections. As the cash flow projections relate to future events, which are indeterminable by nature, variances will occur, which may be material. Accordingly, the Monitor does not express an opinion regarding the likelihood of materialization of these cash flow projections.

6. All amounts reflected in this report are stated in Canadian currency unless otherwise noted.

A. GENERAL CORPORATE INFORMATION

7. The Debtor was constituted by a Certificate of Amalgamation issued pursuant to the Canada Business Corporations Act (the "CBCA") on October 25, 1984. However, it traces its history to the founding by Mr. Harry Hart of the original Hart Department Stores opened in Rosemère in 1960.

8. The Debtor is a Canadian public company, listed on the Toronto Stock Exchange. The trading of the shares has been suspended pending the resolution of the present situation. The Debtor operates a chain of 92 mid-sized department stores in Eastern Canada, providing men's women's and children's apparel and footwear, as well as linens, housewares, furniture, electronics, appliances, toys and giftware.

9. Hart Stores are situated in secondary and tertiary markets throughout Ontario, Québec, Newfoundland and Labrador, New Brunswick and Nova Scotia and operate under the names "Hart", "Géant des Aubaines" and "Bargain Giant".

10. The regional distribution of the stores is as follows:

• Québec	58 stores
• Ontario	16 stores
• New Brunswick	5 stores
• Nova Scotia	2 stores
• Newfoundland and Labrador	11 stores

11. The Debtor leases premises for each of its department stores, which range in size from 16,000 square feet to 45,000 square feet with an average store size of 26,000 square feet.

12. As of the date hereof, the Debtor had approximately 1,609 active employees, including 1,460 sales associates in the stores, 78 warehouse employees and 71 head office staff.

13. The Debtor's 220,000 square foot head office and distribution center is located in Laval, Québec and is leased from a related entity.

14. We refer this Court to the Debtor's Motion for the Issuance of an Initial Order dated August 30, 2011, for further details with respect to the Debtor's operations and corporate structure.

B. EVENTS LEADING TO THE CCAA FILING

15. The following table summarizes the financial results for the past 3 fiscal years ended January 29, 2011 (based on the Debtor's audited consolidated financial statements).

Hart Stores Inc.
Historical Annual Financial Results
For the fiscal years ended

(000's)	F2009	F2010	F2011
	Audited	*Audited*	*Audited*
Sales	**$ 175,086**	**$ 179,462**	**$ 174,692**
Cost of sales and expenses	169,880	174,259	173,665
Operating earnings	**5,206**	**5,203**	**1,027**
Financial charges	925	602	746
Amortization	2,872	3,696	2,922
Other expenses (income)	(350)	(1,602)	-
Earnings (losses) before income taxes	1,759	2,507	(2,641)
Income taxes	563	922	(929)
Net earnings (losses)	**$ 1,196**	**$ 1,585**	**$ (1,712)**

16. As shown in the above table, for the fiscal year ended January 29, 2011, Hart Stores reported a net loss of $1.7M compared to net earnings of $1.6M in fiscal 2010. The sales decreased by 2.7% from fiscal 2010 to fiscal 2011, with same-store sales decreasing by 4.4% during the same period.

17. The Debtor's management attributes the overall negative results of fiscal 2011 to the reduced consumer spending observed in the 3rd and 4th quarters resulting from the economic downturn at the time. In addition, the Debtor explains the decrease in net earnings by the impact of lower value in same-store sales, higher salaries due to minimum wage increases and additional costs related to the implementation of a new point-of-sale and inventory merchandising system.

18. The following table summarizes the financial results for the first and second quarters of fiscal 2012 (based on the Debtor's unaudited consolidated financial statements).

Hart Stores Inc. Historical Quarterly Financial Results						
(000's)	1st Quarter (May 1, 2011)		2nd Quarter (July 31, 2011)		YTD July 31, 2011	
	F2011	F2012	F2011	F2012	F2011	F2012
	Unaudited	*Unaudited*	*Unaudited*	*Unaudited*	*Unaudited*	*Unaudited*
Sales	**$ 35,041**	**$ 29,695**	**$ 45,941**	**$ 38,707**	**$ 80,982**	**$ 68,402**
Cost of sales and expenses	36,548	33,600	44,951	38,926	81,499	72,526
Operating earnings	**(1,507)**	**(3,905)**	**990**	**(219)**	**(517)**	**(4,124)**
Financial charges	165	249	194	279	359	528
Amortization	674	767	689	801	1,363	1,568
Earnings (losses) before income taxes	(2,346)	(4,921)	107	(1,299)	(2,239)	(6,220)
Income taxes	(916)	(1,427)	35	(377)	(881)	(1,804)
Net earnings (losses)	**$ (1,430)**	**$ (3,494)**	**$ 72**	**$ (922)**	**$ (1,358)**	**$ (4,416)**

19. As shown in the above table, the sales and net earnings for the first two quarters of fiscal 2012 continued to decline significantly as compared to the previous year. For the first quarter ended May 1, 2011, the Debtor recorded sales of $29.7M, representing a 15% decrease in comparison to sales of $35M for the same period in previous year. Consequently, the net loss was $3.5M compared to a net loss of $1.4M in previous year. For the second quarter ended July 31, 2011, sales continued to decline resulting in a 16% decrease in sales as compared to last year and a further increase in net loss.

20. On a cumulative basis, as at July 31, 2011, sales were down 16% reaching $68.4M in comparison to sales of $80.9M for the same period last year (there were 92 stores in operation as at July 31, 2011 compared to 90 at the end of the same period the previous year). The Debtor recorded a net loss of $4.4M for the 26-week period ended July 31, 2011 compared to $1.4M in fiscal 2011, a significant deterioration of its financial performance.

21. Per management, the unusually cold spring weather and the resulting decrease in customer traffic were the most important factors responsible for the decrease in sales in the first quarter of fiscal 2012. In addition, management believes that the cold weather also greatly impacted many weather-related categories of inventory including fashion and seasonal products.

22. Therefore, a number of the Debtor's stores are not profitable, or are at the very least underperforming, and the cost of maintaining these stores only adds to the Debtor's rising losses. Furthermore, the Debtor's current overheard structure is not in line anymore with its reduced business volume.

23. The Debtor's decline in sales, compounded by inventory purchases made in anticipation of better sales have led to a significant build-up of excess inventory that may be difficult to sell in the ordinary course of business (the "Excess Inventory"). The Debtor's inventory increased from $53.6M as at January 29, 2011 to $66.4M as at July 31, 2011 ($58.2M as at July 31, 2010). The current level of inventory is approximately $66.5M.

24. Consequently, from January 29 to July 31, 2011 (end of 2nd quarter), the Debtor's indebtedness towards Wells Fargo Capital Finance Corporation Canada ("Wells Fargo" or "DIP Lender"), its principal secured lender, increased from $13.5M to $28.3M, while accounts payable and accrued liabilities increased from $14.9M to $23.5M. As a result, the indebtedness as at July 31, 2011 shows a significant negative variance from its actual level of the previous year.

25. As of the date of the CCAA filing, the Debtor's indebtedness is as follows:

Hart Stores Inc. List of Creditors As of August 30, 2011		
(000's)		
Secured creditors	$	29,133
Unsecured creditors		26,718
Total	**$**	**55,851**

26. While the Debtor sought to refinance its affairs with another lender, its efforts had been unsuccessful and the Debtor's Board of Directors concluded that it would not be able to refinance its affairs under the current circumstances.

27. Therefore, the Debtor's Board of Directors decided that the best course of action was to seek the protection of the Court to restructure its affairs under the CCAA.

C. DEBTOR'S RESTRUCTURING MEASURES

28. The following is a summary of the Debtor's restructuring initiatives that are presently being implemented or are being contemplated by management:

Closing of underperforming stores

- Pursuant to a detailed analysis of individual store contribution, the Debtor has identified, on a preliminary basis, approximately 23 store locations which impair Hart Store's profitability (hereinafter referred to as the "Closing Stores"). As per the Debtor's management, additional stores may be closed as it finalizes the store profitability analysis.

- For the Closing Stores, the Debtor requested the Monitor's assistance to initiate a process to solicit bids for the purpose of selecting an expert independent liquidator, on an exclusive basis, for the liquidation of inventory and furniture and fixtures located at the Closing Stores (the "Inventory Sale Process").

- The Inventory Sale Process began on September 16, 2011 and to date, ten liquidators have signed a confidentiality agreement and have been granted access to a virtual data room maintained by the Monitor. The virtual data room contains select financial information concerning the Closing Stores. Those parties signing a confidentiality agreement have also received a "Request for Proposal" and an "Agency Agreement" outlining selected terms and conditions on which bidders should submit proposals. The bid submission deadline is October 5, 2011 at 2:00 PM Eastern time.

- In parallel to the Inventory Sale Process, the Debtor has requested the Monitor's assistance to conduct a process for the assignment of the leases and, to the extent desired by the prospect party, the sale of furniture and fixtures relating to the Closing Stores (the "Lease Sale Process").

- The Lease Sale Process has just commenced (September 22, 2010). The Debtor identified 31 potential interested parties to whom the Monitor sent a solicitation. Interested parties that will sign the confidentiality agreement will be granted access to a virtual data room maintained by the Monitor. The virtual data room contains specific information relating to the leases and furniture and fixtures of the Closing Stores. The offer submission deadline for expressions of interest is October 14, 2011.

Liquidation of Excess Inventory in continuing stores

- The Debtor's management is in process of implementing a liquidation strategy relating to the slow moving and obsolete inventories in the Continuing Stores (the "Excess Inventory Liquidation Process"). It is currently contemplated by the Debtor to discuss and negotiate with the successful liquidator/bidder the Excess Inventory Liquidation Process which would commence subsequent to the commencement date of the Inventory Sale Process.

- The Debtor's management will seek the assistance of the chosen liquidator to complete the following steps:

    - Identification of the Excess Inventory;
    - Preparation of the inventory in Continuing Stores and from warehouse;
    - Determination of the pricing, mark-down and advertising strategy; and
    - Implementation of an internal communication plan for logistics.

Operating and overhead expenses reduction

- Management, with the assistance of the Monitor, is in the process of completing its analysis and identification of potential cost reduction initiatives at the stores and head office levels coupled with measures to stimulate sales and gross margin, including:

    - Reduction in the number of advertising circulars and optimization of circular distribution;
    - Review of hour's optimization at the store level;
    - Optimization of transportation activities between warehouse and stores;
    - Headcount reductions following the store closures;
    - Elimination of visual store merchandisers' position;
    - Implementation of internal processes to control costs; and
    - Various sales and gross margin improvement initiatives.

- The Company has already begun implementing some of these corrective measures.

Refinancing

- The Debtor re-initiated discussions with a number of chartered banks and asset-based lenders with a view to refinance the Debtor's affairs. To date four lenders have been approached by the Debtor and discussions are progressing.

Business plan

- The Debtor is currently incorporating all of the above mentioned initiatives and corrective measures into a revised business plan and financial model in order to determine its financing requirements for its continuing operations as well as to assist it in seeking available funding for the purpose of submitting a plan of arrangement to its creditors.

D. OPERATIONS

29. Pursuant to the filing of the CCAA, the Debtor, with the assistance of the Monitor, implemented a detailed communication plan addressing the information needs of suppliers, landlords and employees. The Debtor also issued a press release advising of the CCAA proceedings.

30. The Debtor has been in communication with certain suppliers affected by the CCAA filing and, to date, has been successful in maintaining a continued supply of goods and services to its business, either on a cash on delivery basis or on negotiated terms.

31. Certain creditors have exercised alleged rights of retention relating to the receipt of goods purchased by the Debtor. In this regard, the Debtor is negotiating with these suppliers in order to ensure the release of these goods and the continuing receipts of merchandise.

E. CASH FLOW PROJECTIONS

DIP Financing

32. The Initial Order authorized the Debtor to enter into an interim financing (the "Post-Filing DIP Financing") with Wells Fargo pursuant to the DIP commitment letter filed in support of the Initial Order (the "DIP Commitment Letter"), thereby creating a charge in favour of the DIP Lender over the Debtor's property (as more fully described in the Initial Order). As per the terms of the DIP Facility, which expires on November 4, 2011, any receipts must be applied against the Pre-Filing Revolver Loan while disbursements must be funded through the Post-Filing DIP Financing, up to a maximum of $20M.

33. Pursuant to the DIP Commitment Letter, the Debtor submitted to the DIP Lender the following:

- On September 20, 2011, a detailed 13-week cash flow projections outlining the store closures and the strategy relating thereto;
- Daily monitoring schedules;
- Daily drawdown certificates;
- Weekly borrowing base certificates;
- Weekly actual receipts and disbursements with comparison to the cash flow projections;

- Information requested by the DIP Lender from time to time; and
- A letter dated September 26, 2011 outlining elements of the proposed restructuring plan which encompass both a refinancing transaction and a transaction with respect to 23 stores that the Debtor has decided to close, Excess Inventory and leases associated with the Closing Stores.

34. The Monitor has been informed that according to the DIP Lender, some milestones and possibly the process that the Debtor is following is not in compliance with the Restructuring Timeline set out in the DIP Commitment Letter.

35. The Debtor disagrees with the view of the DIP Lender and in light of the DIP Lender not intending to take any remedy at this stage, the Monitor has not taken any position with respect to the occurrence or not, of an event of default pursuant to the DIP Commitment Letter.

Period from August 29 to September 25, 2011

36. When the Motion for the Issuance of an Initial Order was filed on August 30, 2011, the Debtor submitted a projected cash flow statement for the initial 30-day period ending on September 29, 2011.

37. It was initially projected that the Debtor was to suffer a cash flow deficiency of approximately $0.5M for the period from August 29 to September 25, 2011. It had been projected that, as at September 25, 2011, the Pre-Filing Revolving Loan and the Post-Filing DIP Financing were to amount to approximately $19.4M and $11.3M, respectively (total of $30.7M).

38. For the period August 29 to September 25, 2011, the Debtor reported a positive net cash flow of $3M, representing a favorable variance as compared to the projected cash flow deficiency primarily due to timing. The Pre-Filing Revolving Loan and the Post-Filing DIP Financing total approximately $18.9M and $7.8M as at September 25, 2011, respectively (total of $26.7M). We refer this Court to **Appendix A** for a copy of the comparative cash flow statement for the period from August 29 to September 25, 2011, including details of the above noted variances.

39. Since the filing of the CCAA, the Debtor is paying its suppliers based on negotiated terms or on cash on delivery basis. The Debtor advises that it has not incurred significant unpaid liabilities since the filing. It, however, addresses later in this report its desired treatment of these post-filing liabilities.

Period from September 26 to November 6, 2011

40. The Debtor presents to this Court its cash flow projections for the period from September 26 to October 23, 2011 (refer to **Appendix B.1**). The cash flow projections for the period from October 24 to November 6, 2011 (refer to **Appendix B.2**) are filed under seal with the Court as the Debtor does not want to disclose the projected realization relating to the Inventory Sale Process in order to preserve the integrity of same. Nonetheless, for the period from September 26 to November 6, 2011 (the "Period") the cash flow projections reflects the following:

- The Debtor projects generating a positive net cash flow of approximately $5.6M during the Period primarily due to the estimated collection of funds resulting from the Inventory Sale Process.
- The Pre-Filing Revolving Loan is projected to be fully repaid as at November 6, 2011.
- The Post-Filing DIP Financing is projected to increase from its present level to $19.9M as at November 6, 2011, without exceeding the $20M maximum borrowing limit.

41. The Debtor's cash flow projections for the Period are based on information and assumptions provided by management based on financial and other information available as of September 27, 2011. The cash flow projections have been prepared using probable assumptions supported and consistent with the plans of the Debtor for the Period, considering the economic conditions that are considered the most probable by management. Since the projections are based on assumptions regarding future events, actual results will vary from the information presented even if the hypothetical assumptions occur, and the variations may be material.

42. The basic assumptions underlying the cash flow projections are that the Debtor will continue to operate the continuing stores in the normal course of business, with the exception of the Excess Inventory Liquidation Process to be conducted and the Inventory Sale Process to be implemented in the Closing Stores.

43. The Debtor is reviewing its operations to identify potential cost reduction initiatives which may be instituted during the Period, if necessary. In this regard, due to the high level of inventory, the Debtor reviewed its outstanding purchase orders for fall / winter 2011 and significantly reduced its purchasing commitments.

44. The assumptions used by the Debtors' management with respect to the cash flow projections appear reasonable.

F. ACTIVITIES OF THE MONITOR

45. On September 7, 2011, in accordance with the Initial Order, the Monitor mailed to all known creditors of the Debtor a notice informing them of the issuance of the Initial Order and of the stay of proceedings. A copy of this notice has been posted on our web site so that creditors may have access to it and a dedicated telephone number and email address have been established.

46. Since the Initial Order was issued, the Monitor has participated in several meetings and work sessions with the Debtor's management with the view of maintaining and restructuring their operations efficiently. The Monitor is not, however, taking any managerial decisions, same being entirely left to the Debtor's management.

47. The Monitor has been actively involved with the Debtor's management in analyzing various restructuring alternatives, including the preparation of numerous financial projections.

48. The Monitor has devoted time and energy in implementing the Inventory Sale Process and the Lease Sale Process, including the set-up of the respective virtual data rooms and communication with interested parties.

49. The Monitor has assisted management in its analysis of the store profitability and Excess Inventory.

50. In addition, the Monitor has been in constant communication with Wells Fargo, the Debtor's principal secured lender and DIP Lender, in order to keep it apprised of the evolution of the file, of the daily monitoring as well as of the actual weekly financial results in comparison to cash flow projections.

51. The Monitor assisted the Debtor in its dealings with a number of suppliers in order to ensure an uninterrupted flow of goods and services.

52. The Debtor has provided the Monitor with its full cooperation and the Monitor has had unrestricted access to its premises, as well as to the various books and records.

53. The Monitor has implemented procedures to insure a weekly monitoring of the receipts and disbursements, as provided by the CCAA, with a view of performing a weekly comparison and variance analysis of actual results against the Debtor's cash flow projections filed with the application made pursuant to the CCAA.

54. The Monitor, to its knowledge, has been kept informed of the Debtors' major activities and has reviewed the disbursements to ensure that they were related to current commitments.

G. MOTION TO EXTEND THE STAY PERIOD AND AMENDMENTS TO THE INITIAL ORDER

Extension of Stay Period

55. The Debtor's application to extend the Stay Period to November 4, 2011 is reasonable and the Monitor recommends that this Court agrees to it, given inter alia the following factors:

- The requested delay is essential in order to allow time for the Debtor to complete the following:
    - The solicitation of bids under the Inventory Sale Process and Lease Sale Process relating to the Closing Stores;
    - The solicitation of bids under the Excess Inventory Liquidation Process in the Continuing Stores and its implementation;
    - The negotiation with replacement lenders;
    - The identification and implementation of cost reduction initiatives;
    - The renewal of the DIP Financing; and
    - The commencement of discussions with its stakeholders with a view to prepare a plan of arrangement under the CCAA.
- If the extension is granted, we are not aware that any creditor will be materially prejudiced.
- Several suppliers and employees have indicated their support to Hart Stores during the current restructuring process.
- The extension of the Stay Period is supported by Wells Fargo, the Debtor's principal secured lender.
- Several direct and indirect jobs are at stake.
- Since the issuance of the Initial Order, the Debtor has continued to act diligently, in good faith and in the interest of its creditors.
- Since August 30, 2011, the Debtor has continued to pay its employees and suppliers of goods and services on time and/or according to existing agreements.
- If the Initial Order issued by this Court on August 30, 2011 is not extended as requested by the Debtor, there is a strong possibility it will go bankrupt and a liquidation will ensue.

<u>Amendments to the Initial Order</u>

56. The Debtor has filed a Motion seeking the following amendments to the Initial Order:

- Creating a charge in favour of the creditors who have provided the Debtor with goods or services subsequent to the Filing Date (as defined in the Initial Order), and accepted to provide said goods or services on credit or delayed payment terms (the "Post-Filing Supplier Charge").

- Authorizing the payment of quasi-insurance payments, and creating a charge in favour of the insurance financier over the unearned insurance premiums (the "Insurance Charge").

57. The Debtor's application to amend the Initial Order to grant the Post-Filing Supplier Charge is reasonable and the Monitor recommends that this Court agrees to it, given inter alia the following factors:

- Since the Filing Date, many suppliers offered extended credit terms to the Debtor, similar to those in effect prior to the Filing Date, for goods and services sold or provided.

- These flexible credit terms are beneficial to the Debtor and the creditors in general as it allows the Debtor to replenish inventory and results in a better cash flow management and in a greater flexibility in case of unexpected events.

- While the Debtor is confident that it will be successful in restructuring its affairs, there is no assurance thereof and the Post-Filing Supplier Charge will provide an additional comfort for those suppliers willing to extend credit to the Debtor in case its restructuring plan fails. **However, it is important for the creditors to understand that the Post-Filing Supplier Charge, if created, would rank after the Administration Charge, the DIP Charge and any other secured creditors, present or future, and that there is no guarantee whatsoever as to the full payment of any post-filing liabilities in the event that the Debtor's restructuring plan fails and a liquidation or a bankruptcy ensue**.

- The pre-filing creditors will not be prejudiced by the establishment of the Post-Filing Supplier Charge, as those suppliers extending credit for post-filing goods and services could otherwise ask for payment on a cash on delivery basis. These funds would therefore not be available for distribution to the pre-filing creditors in the event of a liquidation or a bankruptcy.

- The amount of $2M for the Post-Filing Supplier Charge appears reasonable given the proportion of purchases for which creditors actually provide credit to the Debtor in relation to the whole.

- We refer this Court to the Debtor's Motion for the Extension of the Stay Period dated September 27, 2011, for further details with respect to the Post-Filing Supplier Charge.

58. The Debtor's application to amend the Initial Order to grant the Insurance Charge is reasonable and the Monitor recommends that this Court agrees to it, given inter alia the following factors:

- On July 29, 2011, KRG Insurance Brokers ("KRG") confirmed to the Debtor the renewal of the following coverage (the "Financed Policies"):

Affiliated, Policy No. RW5461	Property / Boiler & Machinery
Intact, Policy No. 501240628	Liability / Umbrella
Liberty, Policy No. CMT0686045004	Crime
Liberty, Policy No. DOT0380391007	Directors' & Officers' Liability, including Employment Practices Liability
Eagle, Policy No. 50T0381	Cargo

- On August 9, 2011, KRG invoiced the Debtor for the total amount of the premium $945,799.65 and informed the Debtor that it could finance same.

- On August 10, 2011, KRG and the Debtor entered into a Premium Installment Contract whereby the Premium was to be paid as follows:

    - Down payment of $273,826.04; and
    - Ten (10) instalments totalling $686,445.69 (including $14,472.08 of interest).

- At the time of the entering into the Premium Installment Contract it was clearly the intentions of all that same was to be assigned to Macquarie Premium Funding Inc. ("Macquarie") and that Macquarie would benefit from a first ranking charge over the unearned insurance premiums and dividends with respect to the Financed Polices.

- As of the date hereof the Debtor is being informed that even though the down payment has been received by KRG, the premium in whole or in part has not been paid to the insurers.

- KRG has informed the Debtor that it will not be funding the premium, notwithstanding the term of the Premium Installment Contract and that Macquarie has not consented to the assignment of same to its benefit.

- Macquarie has advised the Monitor that failing the Court to sanction the Debtor's ability to make the payments under the Premium Installment Contract, to create a charge in its favour over the unearned premiums and to authorize its recourses under the Premium Installment Contract in case of a default by the Debtor, Macquarie will not advance funds on behalf of the Debtor.

- In the case that the premiums are not paid by Macquarie or KRG, the Debtor's cash flow projections indicate that it could not make the payment of the premiums in full on their due date without significantly impacting other aspects of the business, thus jeopardizing the coverage under the insurance policies.

- In the event the policies would be cancelled, the Debtor may not be in a position to seek replacement insurance before their cancellation given its current financial situation and the CCAA proceedings.

- The Debtor requires proper insurance coverage to continue operating its business.

- The continued insurance coverage is necessary to protect the Debtor's assets in the event of a claim.

- We refer this Court to the Debtor's Motion for the Extension of the Stay Period dated September 27, 2011, for further details with respect to the Insurance Charge.

Respectfully submitted at Montreal, this 27th day of September, 2011.

RSM Richter Inc.
Court-Appointed Monitor

Benoit Gingues, CA, CIRP