

CANADA  
PROVINCE OF QUEBEC  
DISTRICT OF QUEBEC  
DIVISION NO.: 01-MONTRÉAL  
COURT NO.: 500-11-041229-119  
ESTATE NO.: 41-1532467

SUPERIOR COURT  
(Bankruptcy and Insolvency)

IN THE MATTER OF THE BANKRUPTCY OF:

**M. Haddad Sportswear Inc.**

a duly incorporated legal person having its head office  
and principal place of business at 701- 333, Chabanel,  
Montréal, Quebec H2S 1L6

**Debtor**

and

**RSM Richter Inc.**

**Trustee**

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### TRUSTEE'S REPORT TO THE FIRST MEETING OF CREDITORS

The purpose of this Report is to apprise the Creditors as to the affairs of the bankrupt as well as to the current status of the administration of the M. Haddad Sportswear Inc. Estate (hereinafter the "Debtor"). We caution the readers that certain information contained in this Report is based upon Management representations as well as the data reflected in the unaudited books and records of the Debtor. The Trustee has not conducted an audit and has not reviewed in detail the books and records of the Debtor. Consequently, the Trustee expresses no opinion whatsoever with respect to the reliability or completeness of such information.

#### 1. Events Leading to the Bankruptcy

- (1) The Debtor's business was the importing and manufacturing of women's clothing, mainly with respect to swimwear.
- (2) Over the past few years, the Debtor sustained important financial pressures from its clients. Some of the clients, including Walmart decided to purchase their goods directly from Asia, others such as Sears imposed increased rebates or as in the case of The Bay, transferred all of the credit risk to the Debtor by changing the supply terms and conditions to sales on consignment.
- (3) On or about July 18, 2011, Management came to the conclusion that it was unable to maintain the viability of its operations under such stringent financial terms. Consequently, most of the employees were terminated as at that date.

- (4) However, Management only informed its primary secured lender, Scotia Bank ("Bank") of this situation one month later, namely, on or about August 20, 2011.
- (5) On August 24, 2011 the Bank, as the first ranking secured creditor on inventory and receivables, informed the Debtor of its intention to enforce its securities and as a result, issued its notice under Section 244 of the *Bankruptcy and Insolvency Act*.
- (6) On August 25, 2011, the above-mentioned Debtor filed a Notice of Intention to Make a Proposal.
- (7) During the stay period provided by the Notice of Intention, Management attempted to interest a potential purchaser to acquire the assets and pursue the operations of the business.
- (8) Unfortunately, these efforts were fruitless and the Debtor had no choice but to declare bankruptcy on September 19, 2011.
- (9) The Trustee promptly instituted a formal sales process ("Sales Process") to dispose of the Debtor's assets.
- (10) As a result, 69 potential purchasers across Canada and the US were identified by the Trustee. This included auctioneers, suppliers and competitors.
- (11) Through this process, 10 parties demonstrated an interest and proceeded in performing a due diligence verification.
- (12) Finally, two offers were submitted to the Trustee by liquidators.
- (13) Both offers are insufficient to pay in full the secured debt, therefore not allowing for the payment of a dividend to Unsecured Creditors.
- (14) No offer has yet been accepted for the sale of the assets. The Trustee is awaiting the feedback and consent of the Bank and other secured lenders.
- (15) The Trustee has obtained an independent legal opinion on validity of the security held by the Bank. This opinion confirms that its securities are valid and opposable to the Trustee.

## 2. STATEMENT OF AFFAIRS

The Debtor by its president has declared his assessment of the "actual" value of the Debtor's assets and liabilities. The following summarizes the information contained in the Debtor's Statement of Affairs:

### Liabilities

Secured Creditors (book value \$2,625,870)	\$	446,933
Deemed Trusts		43,040
Preferred Creditors		23,361
Unsecured Creditors		3,462,908
		<u>3,976,242</u>

### Assets

Inventory		329,500
Accounts receivable		82,433
Other assets		35,000
		<u>446,933</u>
<b>Deficit</b>	<b>\$</b>	<b><u>3,529,309</u></b>

## 3. ASSET (net book value)

### a) Inventories (\$1,668,152)

Inventories consisted of piece-goods and finished goods, having an initial apparent book value of \$1,668,512. However, the foregoing amount was not substantiated as the Debtor had no perpetual inventory system. The valuation of \$329,500, reflected above, was the "net estimated realizable value" based on a physical count allegedly performed by the Debtor but it was impossible to determine the date on which the count was performed. Moreover our cursory review of the inventory indicated that quantities and descriptions of the items on the inventory list which had been provided to us were erroneous. Accordingly, a new count was performed between September 21 and September 26, 2011 by a representative of the Trustee.

The "finished goods" inventory reflected the necessity for substantial downward adjustments. The "raw material" inventory consisted in rolls of fabric, for which, we were unable to determine the cost.

As discussed above both categories of inventory were subject to a Sale Process, the offers received with respect thereto pale in comparison to the alleged "book value and/or net estimated liquidation value reflected in the Statement of Affairs.

**b) Accounts Receivable (\$510,789)**

Our review of the accounts receivable listing, indicated that the accounts receivable records were not up to date and that numerous customer payments had not been applied. Pursuant to our review, we have estimated the "reliable" accounts receivable at \$82 K. We have further identified accounts, totaling \$428 K, of a doubtful nature.

RSM Richter Inc., as Agent for the Bank is presently endeavoring to collect the receivables.

**c) Other Assets (\$63,000)**

Other assets include manufacturing equipment and shelving and a used vehicle, namely a 2007 Cadillac SRX. The foregoing is subject to the security of Investissement Quebec.

**4. LIABILITY**

**a) Secured Creditors**

**Scotiabank:**

As at the date of bankruptcy, the books and records of the Debtor reflected indebtedness to Scotiabank, of approximately \$2,000,000. The Bank holds the following valid security:

- (i) Conventional hypothecs without dispossession dated April 23, 2010 on inventories;
- (ii) Security under section 427 of the *Bank Act*, covering inventories as well as accounts receivables.

As previously stated, the Trustee has obtained a legal opinion on the validity and opposability of the security from the firm of Woods s.e.n.c.r.l.

**Investissement Quebec**

Investissement Québec holds first ranking security on all other assets of the Debtor. As at the date of bankruptcy, the books and records of the Debtor reflected indebtedness to Investissement Québec of \$391,250. Investissement Québec holds the following valid security:

- (i) Conventional hypothec without dispossession dated March 4, 2005;
- (ii) Conventional hypothec without dispossession dated December 6, 2007;
- (iii) Conventional hypothec without dispossession dated November 25, 2008.

**Business Development Bank of Canada**

Business Development Bank of Canada holds security that ranks after Investissement Quebec. As at the date of bankruptcy, the books and records of the Debtor reflected indebtedness to Business Development Bank of Canada of \$234,620 owing. The Business Development Bank of Canada holds the following valid security:

- (i) Conventional hypothec without dispossession dated November 4, 2005;
- (ii) Conventional hypothec without dispossession dated November 26, 2007.

**b) Deemed Trusts**

The books and records reflect unremitted deductions at source, totaling \$43,040.

**c) Preferred Creditors**

The books and records reflect amounts owing to the landlord, Groupe Dayan, totaling \$23,362.

**d) Unsecured Creditors**

The books and records reflect amounts owing to unsecured creditors totaling \$1,283,971 (excluding the unsecured portion of the secured claim). The Trustee has not yet received sufficient proofs claims to determine the accuracy of this amount.

**5. SUMMARY OF THE PRELIMINARY ADMINISTRATION**

**a) Books and Record**

The books and records of the Debtor were not up-to-date at the date of bankruptcy. These have not been updated since April 2011. The Trustee took possession of the books and records of the Debtor for future references.

**b) Security and protective measures**

Since September 19, 2011, the Trustee has performed the following:

- Inventory of the assets;
- Changing of locks on doors giving access to the premises;
- Insured the assets of the Estate;
- Occasional presence of a representative of the Trustee on the premises.

**c) Reviewable Transactions and Preferential Payments**

The Trustee is presently reviewing the books and records to determine whether payments were made that could be considered as a reviewable transaction and shall report its findings to the inspectors of the Estate.

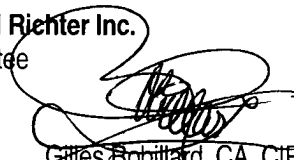
**6. EXPECTED REALIZATION AND PLANNED DISTRIBUTION**

Based upon the information on hand, the realization will be insufficient to provide a dividend to unsecured creditors. It is apparent that the secured creditors will suffer a shortfall in this matter.

DATED AT MONTRÉAL, this 5<sup>th</sup> day of October, 2011

**RSM Richter Inc.**

Trustee

Per:   
Gilles Robillard, CA, CIRP  
Administrator of the Bankruptcy