Q.B.G. No. 1461 of 2009

C A N A D A)
PROVINCE OF SASKATCHEWAN)

IN THE QUEEN'S BENCH
JUDICIAL CENTRE OF SASKATOON

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

AND IN THE MATTER OF A PROPOSED PLAN OF ARRANGEMENT FOR THE CREDITORS OF BIG SKY FARMS INC., DRYCAST SYSTEMS INC. and BIG SKY MANAGEMENT CONSULTING CORP.

SEVENTH SUPPLEMENTARY AFFIDAVIT OF CANUTE TAGSETH

I, **CANUTE TAGSETH**, of the City of Saskatoon, in the Province of Saskatchewan, Chartered Accountant, **MAKE OATH AND SAY THAT**:

1. I am employed as the Chief Financial Officer of the Applicant, Big Sky Farms Inc., such that I have personal knowledge of the facts and matters hereinafter deposed to, except where stated to be based upon information and belief, and where so stated I do verily believe the same to be true.

2. I make this Sixth Supplementary Affidavit to supplement the Affidavit sworn by me on October 29, 2009; the Supplementary Affidavit sworn by me on November 2, 2009; the Second Supplementary Affidavit sworn by me on December 4, 2009; the Third Supplementary Affidavit sworn by me on December 8, 2009; the Fourth Supplementary Affidavit sworn by me on December 16, 2009; the Fifth Supplementary Affidavit sworn by me on December 29, 2009 (the "Fifth Supplementary Affidavit") and the Sixth Supplementary Affidavit sworn by me on February 7, 2010 (the "Sixth Supplementary Affidavit"), each of which Affidavits have been filed on behalf of Big Sky Farms Inc., Drycast Systems Inc. and Big Sky Management Consulting Corp. (collectively, "**Big Sky**") in support of these proceedings.

3. I have reviewed the Notice of Motion on behalf of Big Sky Finishers (No. 1) Inc. ("Finishers") dated February 18, 2010 (the "Finishers Notice of Motion"), together with the Affidavit of John Beckton sworn on February 18, 2010 (the "Beckton Affidavit") and filed in support of the Finishers Notice of Motion.

4. I make this Seventh Supplementary Affidavit in reply to the allegations contained in the Beckton Affidavit.

5. Big Sky has obtained approval of its creditors and this Honourable Court for an Amended and Restated Plan of Compromise and Arrangement dated February 8, 2010 (the "Plan").

6. Words and phrases in this Seventh Supplementary Affidavit which begin with capital letters but which are not expressly defined herein are intended by me to have the meanings which are ascribed to such words and phrases in the Plan.

<u>Disclaimer of The Subject Agreements By Big Sky</u>

7. Big Sky Farms Inc. was a party to the following three agreements with Finishers, (the "Subject Agreements"), namely:

(a) a contract Finishing Agreement (the "Contract Finishing Agreement") between Finishers and Big Sky Farms Inc. dated May 16, 2003 whereby Finishers has agreed to finish hogs owned by Farms for a term ending June 30, 2018 (subject to earlier termination in certain circumstances, as provided for in the Contract Finishing Agreement), a copy of which Contract Finishing Agreement comprises Exhibit "B" to the Beckton Affidavit;

(b) an Option Agreement (the "Option Agreement") between Finishers and Big Sky Farms Inc. dated May 16, 2003 pursuant to which Finishers has a put option to sell to Big Sky Farms Inc. two large-scale hog finishing barns and related land, facilities and equipment located near Ogema, Saskatchewan (the "Project"), and pursuant to which Big Sky Farms Inc. has a call option to repurchase the Project from Finishers at the expiry of the term of the Contract Finishing Agreement (or, at the option of Finishers, on one year's notice at any time after June 10, 2009) at the depreciated book value of the barns at the time of sale, subject to certain adjustments as provided in the Option Agreement, a copy of which Option Agreement comprises Exhibit "C" to the Beckton Affidavit; and

(c) an Indemnity agreement (the "Indemnity Agreement") between Finishers and Big Sky Farms Inc. dated May 16, 2003 pursuant to which Big Sky Farms Inc. has agreed to indemnify Finishers, along with its directors, officers and certain related persons, against certain claims or losses resulting from environmental activity pertaining to the Project, a copy of which Indemnity Agreement comprises Exhibit "D" to the Beckton Affidavit.

8. For reasons more particularly described below in paragraphs 9 to 49 hereof, on February 4, 2010, Big Sky Farms Inc. caused to be served upon Finishers a "Notice by Debtor Company to Disclaim or Resiliate an Agreement" dated February 4, 2010 (the "Notice of Intention to Disclaim") whereby Big Sky Farms Inc. gave notice to Finishers of the intention of Big Sky Farms Inc. to disclaim the Subject Agreements. A copy of the Notice of Intention to Disclaim comprises Exhibit "A" to the Beckton Affidavit.

Hog Industry Market Conditions

9. The North American hog industry has recently gone through an extended period of tremendous economic upheaval as a result of more than thirty consecutive months of negative returns to hog producers.

10. This extended period of negative returns to hog producers has had a severe impact upon the Western Canadian hog industry, as manifested by the receivership, bankruptcy or insolvency of Saskatchewan hog producers such as Stomp Pork Farm Ltd., Fairway Farms Ltd. and Big Sky Farms Inc. and Alberta hog producers such as Great Plains Farms Ltd.

11. Stomp Pork Farm Ltd. restructured under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA") in 2008. Attached and marked as Exhibit

"A" to this Affidavit is a true copy of the Amended *Ex Parte* Initial Order obtained by Stomp Pork Farm Ltd. under the CCAA on March 27, 2008.

12. By means of an Order of this Honourable Court dated May 29, 2009, a receiver was appointed of certain assets, property and undertaking of Stomp Pork Farm Ltd. and Stomp Pork Farm (U.S.A.) Inc. Attached and marked as Exhibit "B" to this Affidavit is a true copy of the receivership order described in this paragraph.

13. In December of 2008, Fairway Farms Ltd., a Saskatchewan hog producer, became bankrupt. Attached and marked as Exhibit "C" to this Affidavit is documentation pertaining to the bankruptcy of Fairway Farms Ltd.

14. On December 20, 2007, the Court of Queen's Bench of Alberta appointed an interim receiver of a hog production operation located near Medicine Hat, Alberta known as Great Plains Farms Ltd. ("Great Plains"). By Order dated August 12, 2008, the Court of Queen's Bench of Alberta authorized the interim receiver to sell the land, buildings and equipment of Great Plains, including three hog finisher barns containing total aggregate capacity for 6,000 hogs. Attached and marked collectively as Exhibit "D" to this Affidavit are true copies of the Alberta Court Orders pertaining to Great Plains described in this paragraph, together with the September 2, 2008 Information Memorandum pertaining to the sale by the interim receiver of the land, buildings and equipment of Great Plains.

The Response of Big Sky Farms Inc. To Industry Market Conditions

15. In order for hog production companies such as Big Sky Farms Inc. to be successful, they are required to be cost competitive not only in the context of Canada, but in the context of all of North America.

16. The hog industry competes globally for market share. The Canadian hog industry is largely impacted by the currency exchange rates that exist between Canada and the United States. The price that Big Sky Farms Inc. receives for a finished animal is derived from a US dollar formula base price, as determined by U.S. packers. The Canada-United States exchange rate currently has a very significant impact upon the

operations of Big Sky Farms Inc., with every one cent movement in the exchange rate amounting to nearly one million dollars in annual fluctuations in revenue. The appreciation of the Canadian dollar against the U.S. dollar over the last several years is a reality with which all Canadian companies have had to live.

17. While the revenue of Big Sky Farms Inc. is impacted by the appreciated value of the Canadian dollar (a factor over which Big Sky Farms Inc. has no control), Big Sky Farms Inc. can control its costs.

18. Big Sky Farms Inc. is one of the most cost competitive companies within the hog industry, as measured by benchmarking through industry analysts such as "Agristats". "AgriStats" is a North American hog industry analyst and benchmarking company which generates financial data from 24 North American hog production companies representing over 1.7 million sows. The "AgriStats" report includes three prominent Canadian hog production companies in addition to Big Sky Farms Inc., being Hytek, Puratone and Maple Leaf Agri Farms.

19. Big Sky Farms Inc. continues to challenge its existing cost structure against industry standards and its peers throughout North America.

Reduction of the Canadian Sow Herd

20. The Canadian hog industry went through a tremendous growth period starting in the early 1990's and continuing for the ensuing ten to fifteen years. As a result, the Canadian sow herd grew to over 1.6 million sows at its peak in 2006.

21. In 2010, the size of the Canadian sow herd has now been reduced to approximately 1.3 million sows (a reduction of approximately 19% since its 2006 peak).

22. In order to encourage further reductions in the size of the Canadian sow herd, the Government of Canada has introduced the Hog Farm Transition Program (the "HFTP"), whereby a fund of Seventy-Five Million ($75,000,000.00) Dollars has been made available by the Government of Canada to Canadian hog producers who empty

their hog barns and completely idle their hog production facilities for a period of three years.

23. The HFTP is administered by the Canadian Pork Council. Attached and marked collectively as Exhibit "E" to this Affidavit is a true copy of documentation pertaining to the HFTP derived from the website of the Canadian Pork Council at www.cpc-ccp.com.

24. Retraction of the sow herd also occurred in the United States, but not to the extent that it has occurred in Canada.

25. As a result of this significant reduction in the size of the Canadian sow herd, thirty consecutive months of negative returns for Canadian hog producers and the appreciation of the Canadian dollar against the U.S. dollar, there is excess hog finishing capacity in Canada. Most of the available hog finishing spaces are located in Western Canada.

The Cost of Available Hog Finishing Spaces in the U.S. & Canada

26. Big Sky currently contracts hog finishing spaces in Canada and in the State of Iowa in the United States.

27. Hog finishing spaces are currently available in Iowa at an average annual price of $32.00 (U.S.) per space. Such contract prices include the costs of all labour, operating costs and manure removal.

28. There is an initial transportation cost for Canadian hog producers such as Big Sky to relocate their existing hog finishing capacity to hog finishing facilities in Iowa. However, even after such initial transportation costs are factored in, the total aggregate overall cost to Canadian hog producers such as Big Sky to relocate their hog finishing capacity to hog finishing facilities in Iowa is substantially less than the costs which Big Sky would be required to pay to Finishers under the Contract Finishing Agreement. These substantial cost savings which can be derived by Canadian hog producers such as Big Sky are a result of lower contract prices

available in Iowa, lower feed costs in Iowa and reduced transportation costs to slaughter facilities in Iowa.

29. Hog finishing spaces are currently available in Canada at annual prices ranging between $36.00 to $40.00 per space. Such contract prices include the costs of all labour, operating costs and manure removal.

Cost of Hog Finishing Spaces To Big Sky Farms Inc. Under The Subject Agreements

30. The base price paid by Big Sky Farms Inc. to Finishers under the Subject Agreements is One Hundred and Four Thousand ($104,000.00) Dollars per month (the "Finishers Base Price"). The Finishers Base Price includes all operating costs, save and except for the cost of manure removal.

31. In addition to the Finishers Base Price, Big Sky Farms Inc. pays to Finishers under the Subject Agreements a crystallized hog marketing incentive payment of $1.50 per hog (the "Marketing Incentive Payment"), which amounts to an additional cost to Big Sky Farms Inc. of approximately $8,550.00 per month. This amount of $8,550.00 per month is calculated at 24,000 hog spaces x 95% utilization x 3 turns x $1.50 per hog for 12 months = $8,550.00 per month.

32. When the Finishers Base Price ($104,000.00) is added to the monthly cost of the Marketing Incentive Payment ($8,550.00), the total monthly costs to Big Sky Farms Inc. to obtain hog finishing services from Finishers under the Subject Agreements is $112,550.00 per month or $1,350,600.00 annually. When this total annual cost of $1,350,600.00 is divided by the 24,000 hog finishing spaces supplied to Big Sky Farms Inc. under the Subject Agreements, the annual cost to Big Sky Farms Inc. of a hog finishing space provided to it by Finishers amounts to $56.28.

33. In addition, Big Sky Farms Inc. pays for annual manure removal costs of $9.75 per hog finishing space. When these manure removal costs are factored in, the annual net cost to Big Sky Farms Inc. of a hog finishing space provided to it by Finishers under the Subject Agreements amounts to $66.03 per hog finishing space.

Fair Market Value of Hog Production Facilities Owned By Finishers

34. As described above, the Option Agreement contains a "Put Option", pursuant to which Finishers has a put option (the "Put Option") to sell to Big Sky Farms Inc. two large-scale hog finishing barns and related land, facilities and equipment located near Ogema, Saskatchewan (the "Project"), and pursuant to which Big Sky Farms Inc. has a call option to repurchase the Project from Finishers at the expiry of the term of the Contract Finishing Agreement (or, at the option of Finishers, on one year's notice at any time after June 10, 2009) at the depreciated book value of the barns at the time of sale, subject to certain adjustments as provided in the Option Agreement.

35. If exercised by Finishers today, the Put Option would require Big Sky Farms Inc. to purchase the Project from Finishers for approximately $4,833,207.00 (as evidenced by Finishers financial statement documents posted on SEDAR as at Deecmber 30, 2009). If exercised by Finishers at the end of the term of the Option Agreement, the Put Option would require Big Sky Farms Inc. to purchase the Project from Finishers for approximately $1,800,000.00.

36. Fair market values of Western Canadian hog production units and hog finishing facilities have dropped considerably as a result of the protracted downturn in the hog market. As more particularly described below in paragraphs 37 to 41 hereof, there is currently excess hog finishing space for sale throughout Saskatchewan and Manitoba and recent transactions have yielded significantly lower fair market values for hog finishing facilities.

37. The receivership of Stomp Pork Farm Ltd. has resulted in numerous hog production units and hog finishing facilities located throughout Saskatchewan that are currently empty and available for purchase.

38. The finishing barns owned by Leroy Agra Pork in the vicinity of Leroy, Saskatchewan (containing 40,000 hog finishing spaces) were recently sold to Hytek in May of 2009 for approximately $2,000,000.00 (or $50.00 per hog finishing space).

39. Pursuant to an Order of this Court, Big Sky recently concluded the sale of its Treherne, Manitoba hog facility for $600,000.00. Based upon the assumption that half of the sale price of the Treherne facility can be allocated to the hog finishing barn and the other half can be allocated to the breeding farrowing barn comprising the Treherne facility, the cost of the 5,600 hog finishing spaces represented by this sale amounted to $300,000.00/ 5,600.00 or $53.57 per hog finishing space.

40. There is a 10,000 space hog finisher barn located in the District of Ponteix, Saskatchewan (the "Ponteix Barn") which was recently purchased by New Generation Pork Finishing Inc. ("New Generation") for $400,000.00. Attached and marked as Exhibit "F" to this Affidavit is a true copy of the Certificate of Title to the Ponteix Barn. Based upon a purchase price of $400,000.00 paid by New Generation to acquire the 10,000 hog finishing spaces in the Ponteix Barn, New Generation paid approximately $40.00 per hog finishing space for the Ponteix Barn.

41. Attached and marked as Exhibit "G" to this Affidavit is a true copy of the Certificate of Title to the land and buildings pertaining to the three 2,000 space hog finisher barns located near Medicine Hat, Alberta and previously owned by Great Plains. I have determined from my review of this Certificate of Title, and I believe it to be true, that the land, buildings and equipment previously owned by Great Plains (including 6,000 hog finishing spaces) were purchased for $230,000.00 (or approximately $38.33 per hog finishing space). Although the purchaser of the Great Plains facility was affiliated with the previous ownership group of Great Plains, this transaction appears to be reflective of the current reduced market value of Western Canadian hog finishing facilities.

42. Based upon my calculations of its present day net value, the Project owned by Finishers which Big Sky Farms Inc. could have been required by Finishers to purchase from Finishers pursuant to the Put Option has a fair market value of no more than approximately $1,200,000.00.

Other Considerations

43. As noted in the Beckton Affidavit, Big Sky has contractual commitments to deliver hogs to various Canadian packers and U.S. packers. However, Big Sky currently has excess hog production capacity beyond the levels required to meet these contractual commitments. The hog finishing capacity of the Finishers barns has no bearing whatsoever on the ability of Big Sky to meet these contractual commitments to deliver hogs to Canadian packers and U.S. packers.

44. On page 6 of the Offering Memorandum for Finishers which comprises Exhibit "E" to the Beckton Affidavit (the "Finishers OM"), it is clearly stated that an investment in the securities of Finishers "*involves a significant degree of risk*". It is there noted that the securities of Finishers are "*speculative*" and "*may be appropriate only for investors who are prepared to have their money invested for a long period of time and have the capacity to absorb a loss of some or all of their investment*".

45. On pages 7, 8 and 9 of the Finishers OM comprising Exhibit "E" to the Beckton Affidavit, prospective investors in Finishers were cautioned that the success of the Project and of a subscriber's investment in the securities of Finishers was, to a significant degree, dependent upon the continuing ability and financial condition of Big Sky Farms Inc. to perform its obligations to Finishers under the Subject Agreements, which in turn was subject to a number of risks, including "Fluctuations in Agricultural Commodity Prices and Currency Values"; "Export Markets"; "Domestic Markets"; "Public Concerns with Large Scale Hog Production"; "Expansion Risks"; "Environmental Risks"; "Hog Disease Risks" and "Liquidity, Capital Resources and Contractual Obligations".

46. The current financial status of Big Sky resulted from a number of factors described above. While the higher than market prices paid by Big Sky to Finishers under the Subject Agreements are not the primary cause of Big Sky's current financial difficulties, they are a contributing factor as they have eroded profitability of Big Sky

47. and have significantly impaired cash flow of Big Sky over the years. At present, the payments which Big Sky is required to make to Finishers pursuant to the Subject Agreements are significantly above market rates and create a very significant impairment of the cash flow of Big Sky. Such an impairment to the cash flow of Big Sky puts in jeopardy the ability of Big Sky to implement the Plan. In particular, Big Sky has future banking covenants which must be met by it in order to maintain the support of its Senior Secured Lenders, and in turn, in order to ensure its viability. Any costs that are not competitive or are above current available market pricing (such as the costs required to be paid by Big Sky to Finishers pursuant to the Subject Agreements) erode the ability of Big Sky to remain in compliance with these covenants and to perform its obligations under the Plan and under the Restructuring Transactions described in the Plan.

48. Finishers is not the only counterparty to a contract with Big Sky which Big Sky has been required to disclaim or to re-negotiate in order to be in a position to complete its CCAA restructuring. In particular, Big Sky was a party to a long-term lease agreement (the "PHPLP Lease Agreement") with Prairie Hog Production Limited Partnership ("PHPLP") in regard to a finisher barn and two nursery barns. During these CCAA proceedings, Big Sky determined that the rates which it was required to pay to PHPLP under the PHPLP Lease Agreement were significantly above market rates for comparable facilities. As a result, Big Sky gave notice to PHPLP of its intention to re-negotiate the terms of the PHPLP Lease Agreement. After a lengthy negotiation process, Big Sky was able to conclude and enter into a re-negotiated lease agreement with PHPLP on more competitive terms to replace the PHPLP Lease Agreement. Because the nature of the facilities leased by Big Sky from PHPLP differ significantly from the Project owned by Finishers which is the subject of the Subject Agreements, I have not exhibited a copy of this revised lease agreement with PHPLP to this Affidavit.

Negotiations Between Big Sky Farms Inc. & Finishers

49. Big Sky has communicated with and been in discussions with Finishers regarding the need to renegotiate the Subject Agreements dating back to August of 2008. Meetings between Big Sky and Finishers to discuss re-negotiation of the Subject Agreements were held at Big sky's office on August 14, 2008 and on September 22, 2009. In addition, and continuously from the date of the commencement by Big Sky Farms Inc. of these proceedings under the CCAA until the present date, Big Sky Farms Inc. has been engaged in dialogue and negotiations with Finishers, with a view to re-negotiating the terms and conditions of the Subject Agreements to prices reflective of current market values. For reasons best known to Finishers, no mention is made in the Beckton Affidavit of the fact of these extensive negotiations between Big Sky Farms Inc. and Finishers having taken place.

50. By letter dated February 11, 2010, Finishers, by its counsel, requested of Big Sky Farms Inc., by its counsel, that Big Sky Farms Inc. provide written reasons for the decision by Big Sky Farms Inc. to deliver the Notice of Intention to Disclaim, as required by section 32(8) of the CCAA. By letter dated February 16, 2010, Big Farms Inc. delivered to Finishers a description of these reasons. Attached and marked collectively as Exhibit "H" to this Affidavit are true copies of the correspondence described in this paragraph. For reasons best known to Finishers, no mention is made in the Beckton Affidavit of these items of correspondence.

51. For the reasons described above, Big Sky Farms Inc. has concluded that the price paid by it to Finishers for hog finishing services under the Subject Agreements is far in excess of prices charged in comparable contracts that could be entered into today. The hog industry is and will remain a very competitive business and companies like Big Sky are faced with the new reality of today's market place. The Subject Agreements between Finishers and Big Sky Farms Inc. were made at a time of continued growth in the hog industry and contracts of this nature go well beyond what would be considered normal in today's market environment.

52. I make this Seventh Supplementary Affidavit in reply to an application by Finishers for relief more particularly described in the Finishers Notice of Motion.

SWORN BEFORE ME at the City of Saskatoon, in the Province of Saskatchewan, this 8th day of March, 2010.)	
A Commissioner For Oaths in and for the Province of Saskatchewan. - Being a Solicitor My Commission Expires Jan 31/2011	CANUTE TAGSETH

This Affidavit was delivered by:

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