# TAB 1

Court File No. 03-CL-5145

*ONTARIO*
**SUPERIOR COURT OF JUSTICE**
Commercial List

BETWEEN:

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 or Plans of Compromise or Arrangement of Ivaco Inc. and the Applicants listed in Schedule "A"

Applicants

**AFFIDAVIT OF BRIAN M. DENEGA**
**(Sworn October 13, 2006)**

I, BRIAN M. DENEGA, of the City of Toronto, in the Province of Ontario, MAKE OATH AND SAY:

1. I am a Senior Vice-President of Ernst & Young Inc., the Monitor of the Applicants appointed by this Honourable Court by Order dated September 16, 2003 as amended from time to time. As such, I have personal knowledge of the matters set forth in this Affidavit. To the extent I do not have personal knowledge, I have set out the source of my information and in all such cases I verily believe the matters set out to be true.

2. It has been over three years since the Applicants filed in September 2003 and almost two years since the sale to Heico closed and put the estates in substantial funds. The unsecured creditors of Ivaco, identified by a court-approved process, have not seen a single cent.

3. But for the issues that Heico only now seeks to raise in its Statement of Claim, the Monitor would soon be in a position to seek court approval of a partial distribution, even without the sums that will eventually be paid by Heico.

4. As described below, there is substantial overlap between the amounts now claimed by Heico and the working capital adjustments claimed by the Sellers. It is not clear what, if any, claim Heico asserts against the Ivaco estates absent a finding by KPMG in favour of Ivaco, in whole or in part.

5. Subsection 5.12 of the APAs provides, among other things, that the Sellers may distribute up to 60% of the Estimated Cash Amount to their creditors and that the purchaser shall have no claim against such amounts, nor may it protest the proposed distribution at any court hearing held for the purposes of seeking approval of a distribution. The APAs also provide for additional amounts to be distributed unless they are subject to a bona fide dispute. This subject is also addressed in the Order of the Honourable J. Farley dated March 21, 2005, which provides as follows:

> 1. THIS COURT DECLARES that pursuant to the terms of each APA, each of the Selling Parties is to have available to it for distribution to its respective creditors, all funds paid by Heico to each of them, respectively, pursuant to each APA, except that Ivaco Inc. shall not be entitled to distribute $2,050,500 ("Residual Holdback Amount") and that amount shall be held by the Monitor, subject to the terms of paragraph 3 of this Order.

6. Absent an agreed or court-ordered allocation of the Heico claim among the Ivaco estates and between cash on hand and the working capital claims asserted by the Ivaco estates, an interim distribution to creditors could be delayed even further, to the very real prejudice of Ivaco's creditors.

7. The body of Ivaco creditors, which includes numerous individuals and small businesses that can ill afford further delay and partial recovery, are facing just that as a result of the proposed claim by Heico.

8. I have reviewed the Affidavit of Stanley H. Meadows sworn September 29, 2006 (the "Meadows Affidavit"). He argues in the Meadows Affidavit that it is Ivaco that is responsible for any delay and further that delay does not prejudice the large corporations that are the creditors of Ivaco. In my previous affidavits, I attempted to set out the objectively demonstrable facts as to what has occurred in the period post-closing and I will leave the argument as to the appropriate conclusion that follows from those facts as to responsibility for delay and the motives of the parties to counsel.

9. The new matters contained in the Meadows Affidavit to be addressed are:

   (a) The claim Heico seeks to advance against the Ivaco estates and the conditions that the Monitor seeks from this Honourable Court if there is to be an order lifting the CCAA stay;

   (b) The rejection by Heico of the method for addressing the privilege issue set out in my previous affidavit;

   (c) The refusal by Heico to volunteer financial information;

   (d) The rejection by Heico of the proposal to jointly instruct KPMG to prepare its report using as the alternative bases the only two interpretations of the APAs proffered by the parties; and

   (e) The request by Heico in paragraph 1(c) of the Statement of Claim that the scope of documentary production include every single document created in the period September 15, 2003 to November 30, 2004.

10. Before addressing these matters, I believe it necessary to address the allegations of "deliberate misrepresentation" that Heico seeks to advance in its draft Statement of Claim. I am advised by counsel, Peter F.C. Howard of Stikeman Elliott LLP, that there are cost consequences of making and failing

to establish such a serious allegation. I believe it is important to state at the outset however that if the Monitor had observed any deliberately misleading conduct by Ivaco it would have considered that it was its duty to report it to this Honourable Court. The Monitor observed no such conduct and made no such report. The Applicants, the Chief Restructuring Officer, Randy Benson, and their counsel were completely open and forthcoming at all times with information and their business rationale for acting in a particular manner. In addition, where the Monitor considered that information ought to be made available to stakeholders, the Applicants never sought to influence or dissuade the Monitor in any way we considered inappropriate or other than in accordance with their duty to act in the best interests of the business and maintain high standards of integrity.

11. Without necessarily asking this Honourable Court to make findings to this effect, the Monitor approaches this unpleasant situation on the following basis:

(a) Its duty to the estates is to finalize and effect the collection of monies from Heico as soon as reasonably practicable and the current situation is intolerable for the creditors of Ivaco;

(b) It is required to assess the merits or otherwise of the causes of action that Heico alleges, in consultation with the major creditors of the estates including the Informal Advisory Committee and the pension creditors;

(c) There is a very real prospect based on the experience to date that Heico will use all avenues available to it to extend the final resolution of matters and therefore steps which might otherwise be available in normal litigation such as pleadings motions, motions to disqualify and protracted discovery are not optimal by reason of the delay resulting from these steps;

(d) In view of the fact that Heico now seeks to make extremely serious allegations at this late stage in the proceedings and if Heico's object is not delay it could have no legitimate objection especially in the context of insolvency proceedings in the event it is determined that the stay should be lifted, to an expedited schedule to get to a trial on the merits and other conditions to protect the legitimate interests of creditors of Ivaco.

**A. Timing of the Statement of Claim and Impact on the Estates**

12. The Notice of Objection filed by Heico, which is Exhibit 2 to my Affidavit dated September 11, 2006, is dated January 11, 2005. It appears from the Documents provided on September 13, 2006 that Stanley Meadows accessed them on or before January 13, 2005. There is a substantial overlap between the matters raised in the Statement of Claim and the issues raised in the Notice of Objection and Initial Submissions in the working capital dispute. A table of concordance setting out the parallels is attached as Exhibit "A" to this my Affidavit. It appears that Heico knew of most if not all of the matters it alleges in the Statement of Claim from at the latest January 2005.

13. I have been present or been informed of what occurred at the approximately 10 attendances (including 9:30 appointments) before this Honourable Court where Heico and the Monitor, on behalf of the Applicants, have appeared since April 2005. At no time before September 12, 2006 did Heico ever indicate that it was planning or even contemplating a separate court claim with respect to the working capital issues. It is my belief, based on these facts and our experience with Heico to date, that in the absence of paragraphs 48 to 50 of my Affidavit of September 11, 2006, Heico would not have surfaced these allegations and the claim of set-off until after KPMG had delivered its working capital report.

14. The Meadows Affidavit makes reference to certain pension disputes that are outstanding. While it is accurate to say that these matters are extant, for these purposes, it is important to note that the existence of these disputes does not

prevent an interim distribution to the creditors. The fact that the entities remain outside of bankruptcy and/or receivership necessitated discussions with the relevant tax authorities to obtain their agreement that any distribution would not attract a liability upon the Monitor that would itself be met by the Monitor's charge. These discussions have taken some time but, as at September 2006, the Monitor had obtained or is about to obtain sufficient assurances from these authorities that its plan was to pursue an interim distribution of at least 30% in two of the three estates, of course on notice to the Service List and the taxing authorities. The potential impact of asserting a $75,000,000 contingency in each estate is obvious - Heico will undoubtedly assert that there can be no distribution until that claim is finally determined or allocated by agreement or court order or at least allocated as described above (with the effect that the real creditors of the Ivaco entities are held hostage).

## B. Assessment of the Statement of Claim, Methods of Dealing With It and the Working Capital Dispute

15. In the Meadows Affidavit at paragraph 78, Mr. Meadows sets out an extract from one of the interviews of Randy Benson, the former CRO of the Applicants. KPMG has interviewed 16 individuals on 19 separate days (some individuals more than once) in the circumstances set out in my Affidavit of September 11, 2006.

16. The interview of Mr. Meadows was to be the last interview before the next and final steps in the protocol (written submissions), which should have led to the KPMG report on or before the end of November, 2006. The interview process is not finished pending determination of the privilege issue and Mr. Meadows' ability to provide further "information" to KPMG from the Documents.

17. In assessing the claims to be advanced in the proposed Statement of Claim, the Monitor has access to the substantial body of information and documents generated by the KPMG process.

18. As an example only, in paragraphs 45 and 47(c) of the proposed Statement of Claim, Heico alleges that there were deliberate and unsupported changes to the inventory and trade payables numbers in Ifastgroup LP totalling $8.0 million. It is alleged that these were "deliberate and unsupported changes" that Heico says, in accordance with its interpretation, were neither reasonable nor supportable and were done with the intent of "reducing the amounts of Working Capital shown on Exhibit B and therefore increasing the Purchase Price potentially payable by Heico". The identical item is addressed in Heico's Initial Submission at p. 14 and Annex 2 and KPMG has therefore asked questions about this item of both the CRO, Randy Benson, and the former CFO, Hugh Blakely. This item was also addressed on the cross-examination of Mr. Blakely.

19. The extracts and documents dealing with this item are attached as Exhibit "B" to this my Affidavit with respect to Randy Benson. Exhibit "C" is the cross-examination transcript extracts for Hugh Blakely and Exhibit "D" is Exhibits 7, 8 and 9 to the cross-examination of Hugh Blakely.

20. For example, with respect to the $5 million trade payable adjustment only, the available evidence demonstrates that:

(a) In the months prior to July 2004, the Ifastgroupe division had submitted estimates each month on at least three separate occasions for accounts payable in the area of $2,000,000 to $3,000,000;

(b) The actual level of accounts payable at Ifastgroupe experienced in those prior months had been much higher, in the order of $8,000,000 to $9,000,000;

(c) A low level of accounts payable is not good as a business practice for this business and both the CRO and CFO were trying to instil a business discipline that had previously been absent;

(d) The initial estimate from divisional management for accounts payable for September 30, 2004 was $3.4 million and was adjusted to be $8.4 million;

(e) The adjustment contested by Heico made to accounts payable to increase it accorded with both the historical experience and this business goal;

(f) The adjusted level was actually exceeded by the business for September 30, 2004 as the actual accounts payable level as of that date was $8.526 million; and

(g) The CRO asked the CFO for this adjustment (and for each such adjustment), often in the presence of a representative of the Monitor, whether the CFO was "okay" with the proposed adjustment and the CFO expressly said on each occasion that he was.

21. In paragraphs 34 to 40 of the proposed Statement of Claim, Heico asserts a deliberate non-disclosure misrepresentation tort with respect to the termination of a consignment arrangement by IRM with QIT.

22. The claim does not set out that those facts were fully disclosed in the Monitor's Fifteenth Report dated August 9, 2004 <u>before</u> court approval of the APAs in the presence of Heico's counsel on August 18, 2004 and the subsequent amendment to the APAs dated November 30, 2004. The facts with respect to this matter are summarized in the cross-examination of Hugh Blakely and the Fifteenth Report of the Monitor referenced therein that are appended as Exhibit "E" to this my Affidavit. As court approval is a condition in favour of Heico of the effectiveness of the APAs pursuant to paragraph 7.1(c), Heico's allegation of non-disclosure faces this substantial factual impediment.

23. It is not proposed to multiply examples. The Monitor has available to it similar information and documentation for all the allegations made. It is not intended to waive privilege in any way, however it is the position of the Monitor that the proposed action should be fully defended and not admitted as a valid post-filing claim.

24. The Monitor is also obliged to raise a further consideration. In all the circumstances described in this and previous affidavits, it is the belief of the Monitor, and a possible conclusion open for this Honourable Court, that the conduct of Heico is based on its assessment that the Working Capital Dispute interview evidence, and especially that from Mr. Blakely, was not developing well for it and that its goal is to derail that process for a number of years and compel the estates to seek a resolution unrelated to the legal merits of its claims. The Monitor, in this and previous affidavits, has set out the objective facts that it is aware of that would be relevant to the issue of whether the CCAA stay should be lifted at all in order to allow creditors to assess and advance arguments to that effect on November 7, 2006 if they consider it appropriate.

**C. Alternate Approaches for KPMG**

25. In paragraphs 55 to 63 of the proposed Statement of Claim, under the heading "No Need for Two Alternate Experts Reports", Stanley Meadows provides his argument that the relief we are seeking "is inconsistent with the terms of the APAs" and that to require Heico to pay amounts determined thereunder would be "unfair".

26. Mr. Meadows does not dispute that KPMG has asked questions and requested information that address the two alternative approaches contended for by the Applicants and Heico. The merit or otherwise of the legal

arguments that Mr. Meadows advances in his Affidavit will be addressed by counsel. It should be stressed that the Monitor considers that the approach it contends for is the only appropriate approach for both legal and accounting reasons and its written submissions under the protocol will continue to be advanced on that basis.

**D. Financial Information and Payment into Court**

27. In his Affidavit, Mr. Meadows confirms that the Monitor has requested and Heico refuses to provide information as to the financial position of the parties to the APAs and asset transfers on a confidential basis to the Monitor. I was present on September 12, 2006 before this Honourable Court when counsel for Heico also raised the issue of set-off of amounts determined to be owing by Heico in the working capital dispute to the Applicants as against the claims it makes in the proposed Statement of Claim.

28. The Monitor addresses this refusal to provide financial information in the proposal it makes as to conditions to be attached to an order lifting the stay, if such an order is to be granted. If the stay is not lifted, provision of such information will be addressed in the context of the ancillary orders with respect to privilege and the KPMG process.

**E. The Privilege Issue**

29. Heico has refused the proposal set out in my Affidavit of September 29, 2006. A copy of the October 3, 2006 letter from its counsel to that effect is attached as Exhibit "F" to this my Affidavit. Leaving this issue unresolved means that the interview portion of the KPMG Protocol is not completed and leads to further delay. The Monitor will seek the answers to the questions it has posed in the cross-examinations set by the agreed schedule of September 12, 2006.

30. As requested in the October 3, 2006 letter, appended as Exhibit "G" to this my Affidavit is a list of the documents for which a claim for privilege is apparent with respect to the Documents provided on September 13, 2006.

**F. Scope of Documentary Production**

31. In paragraph 1(c) of the proposed claim, Heico seeks "an order for discovery directing the defendants to produce all documents, books, records and files, in their possession and in the possession of Ernst & Young Inc. as Monitor in the CCAA proceedings commenced by the defendants, including records in electronic form, relating to the operations, business and activities of the defendants during the period from September 15, 2003 to November 30, 2004".

32. In the course of these CCAA proceedings, a multitude of issues have arisen that have nothing whatsoever to do with the working capital issues sought to be raised by Heico. These issues include pension, environmental, claims process, creditor, U.S. subsidiaries, and numerous other unrelated matters. The document request encompasses certainly hundreds of thousands and possibly over a million pieces of paper. The cost of making such production cannot be estimated with any precision but it is safe to say that the cost to the estates if ordered would be very substantial. The lack of any basis for the scope of discovery sought given the limited issues that Heico seeks to raise reinforces the belief I attested to earlier in paragraph 24 of this Affidavit and identifies the need for an order setting the scope of documentary production as a condition of lifting the stay in order to forestall further delay while that scope is settled.

## G. The Order Requested by the Monitor

33. For the reasons set forth above, the Monitor seeks an order dismissing Heico's motions in their entirety and granting the relief sought by the Monitor. In the alternative, with respect to the Heico matter, if it is determined that the stay is to be lifted it ought to be conditional upon orders designed to safeguard the stakeholders' interest in resolving the working capital adjustment dispute and Heico's action as quickly as possible, namely:

(a) An order directing KPMG to include in its report on the working capital adjustment a calculation of the adjustment determined pursuant to the approach specified in each of the initial written submissions of Ivaco and Heico to KPMG provided always that KPMG is to indicate in its report the approach it accepts and the reasons on an accounting basis for such acceptance and the accounting basis as to why the approach not accepted is unsuitable;

(b) An order directing Heico to provide the Monitor (on a periodic ongoing basis), on a confidential basis, with financial information addressing the transfers of assets if any since closing and sufficient in the view of the Monitor acting reasonably to determine whether Heico has the ability to pay any amount ultimately determined to be owing as a working capital adjustment;

(c) In addition to the order requested at subparagraph (b), above, an order directing Heico to pay into court the amount of the working capital adjustment that was acknowledged in its letter of January 10, 2005 plus any additional amount subsequently determined by KPMG to be owing to Ivaco in its report within seven days of the date of the report (assuming the amounts referred to in (a) above are not the same it would be the lower of the two amounts generated);

(d) In the alternative to the orders set forth at subparagraphs (b) and (c), above, an order directing Heico to pay into court $65,258,008 plus interest calculated from December 23, 2004; and

(e) An order directing Heico to pay into court $2,000,000 as security for costs prior to the filing of a defence.

34. The Monitor also will seek conditions, the precise details of which will follow the cross-examinations, but will include:

(a) A set date for an early trial in accordance with the established principles of quick resolution in insolvency matters;

(b) A fixed schedule for pre-trial matters;

(c) An order fixing the scope and dates for documentary discovery; and

(d) An order providing for the utilization of interviews to date as oral discovery and limiting the days of further or additional discovery;

all with a view to achieving the earliest feasible final resolution of the matters Heico seeks to raise in its motions on an urgent basis.

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| Sworn before me at the City of Toronto in the Province of Ontario this 13th day of October, 2006. | |
| A commissioner for taking affidavits | Brian M. Denega |