

DISTRICT OF: NOVA SCOTIA
DIVISION NO: 01 – HALIFAX
COURT NO: 2021 Hfx No. 503367

PRE-FILING REPORT OF DELOITTE RESTRUCTURING INC.
IN ITS CAPACITY AS PROPOSED RECEIVER OF
3304051 NOVA SCOTIA LIMITED

JANUARY 20, 2021

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1.0 INTRODUCTION AND PURPOSE OF THIS REPORT

- 1.1 Deloitte Restructuring Inc. ("**Deloitte**") understands that an application has been made before the Supreme Court of Nova Scotia in Bankruptcy and Insolvency (the "**Court**") by Canadian Imperial Bank of Commerce ("**CIBC**"), for an Order (the "**Receivership Order**") appointing Deloitte as an interlocutory receiver (the "**Receiver**") to exercise the power and duties set out in the Receivership Order, without security, of certain of the assets, properties and undertakings (collectively, the "**Property**") of 3304051 Nova Scotia Limited operating as Hefler Forest Products ("**Hefler**").
- 1.2 Deloitte was retained by CIBC to act as its financial consultant to review the operations and financial position of Hefler on August 4, 2020 (the "**Consulting Engagement**"). As part of the Consulting Engagement, Deloitte has worked with CIBC and its legal counsel, Burchell's LLP ("**Burchell's**"), with regard to the proposed receivership, as discussed below.
- 1.3 Deloitte is a licensed insolvency trustee within the meaning of section 2 of the BIA and has consented to act as Receiver in these proceedings in the event that the Court grants the relief sought by CIBC. Deloitte has prepared this pre-filing report as proposed Court-appointed Receiver of Hefler (the "**Proposed Receiver**") to provide background to the Court for the pending receivership application and the relief being sought as part of the application (the "**Pre-Filing Report**").
- 1.4 Deloitte has engaged Wickwire Holm ("**Wickwire**") to act as the Proposed Receiver's independent legal counsel.
- 1.5 The purpose of this Pre-Filing Report is to provide information to the Court with respect to:
 - a) Hefler's current financial position (including assets, liabilities and security interests), causes of financial difficulty and Hefler's immediate cash resources.
 - b) The outcome of Deloitte's review of Hefler's operations.
 - c) A summary of Hefler's significant creditors.
 - d) The results of Hefler's sale and investment solicitation process.
 - e) The results of CIBC issuing its ten-day notice to enforce its security.
 - f) Wickwire's preliminary review of the validity and enforceability of CIBC's security.
 - g) Deloitte's consent to act as Receiver should the Court see fit to grant the Receivership Order as requested by CIBC.

2.0 TERMS OF REFERENCE

- 2.1 In preparing this Pre-Filing Report, Deloitte has been provided with, and has relied upon, unaudited, draft and/or internal financial information, Hefler's books and records, discussions with management, and information from third-party sources (collectively, the "**Information**"). Except as described in this Report:
 - a) Deloitte has reviewed the Information for reasonableness, internal consistency and use in the context in which it was provided. However, Deloitte has not audited or otherwise attempted to verify the accuracy or completeness of the Information in a manner that would wholly or partially comply with Canadian Audit Standards ("**CAS**") pursuant to the Chartered Professional Accountants Canada Handbook and, accordingly, the Proposed

Receiver expresses no opinion or other form of assurance contemplated under CAS in respect of the Information.

- b) Deloitte has prepared this Report in its capacity as Proposed Receiver to provide background to the Court for its consideration of the relief being sought. Parties using this Report other than for the purposes outlined herein are cautioned that it may not be appropriate for their purposes.

2.2 Unless otherwise stated, all dollar amounts contained in this Report are expressed in Canadian Dollars.

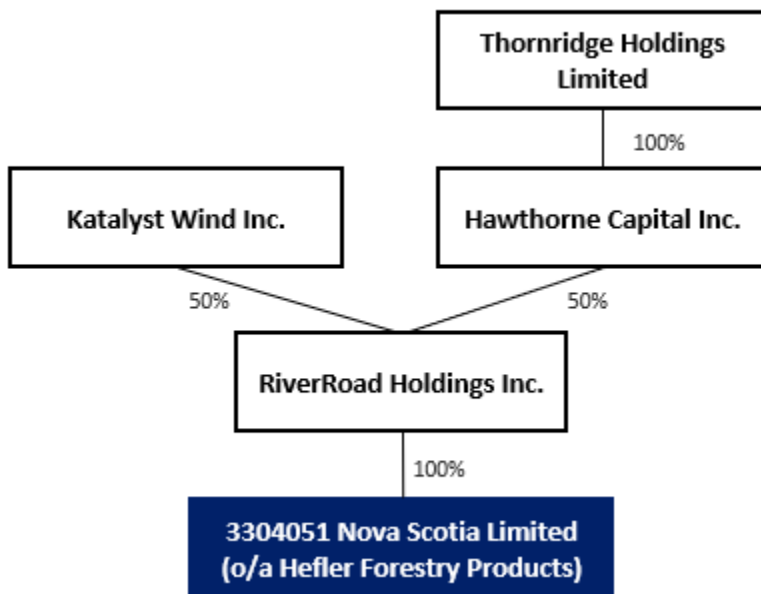
2.3 This Report has been prepared with reference to the Affidavit of Kyle Lane sworn on January 18, 2021 (the "**Lane Affidavit**") in this matter, a copy of which will be filed separately with the Court by CIBC.

2.4 This Report should be read concurrently with the Lane Affidavit for further context and background regarding Hefler and the activities leading up to CIBC's application for the Receivership Order.

3.0 OVERVIEW OF HEFLER

3.1 Hefler is a privately held Canadian corporation with operations located in Middle Sackville, Nova Scotia. Hefler was formed in March of 2017 when Hawthorne Capital Inc. ("**Hawthorne**") and Katalyst Wind Inc. ("**Katalyst**") incorporated RiverRoad Holdings Inc. ("**RiverRoad**") to acquire the Hefler assets from a CCAA proceeding.

3.2 At the commencement of the Consulting Engagement, the ownership structure of Hefler was as follows:



3.3 On or around September 28, 2020, a transaction occurred whereby Hawthorne purchased Katalyst's equity interest in RiverRoad and thus became the sole shareholder of Hefler.

- 3.4 Hefler operates a 3.1MW biomass power plant (the “**Plant**”) that generates and sells energy to Nova Scotia Power (“**NSP**”) under a power purchase agreement (the “**PPA**”) and standard small generator interconnection and operating agreement (the “**Operating Agreement**”) at predetermined rates contained within the Province of Nova Scotia’s Community Feed-in Tariff program (the “**COMFIT**”). In addition to the Plant, Hefler has also operated a sawmill intermittently since acquiring the assets.
- 3.5 Since the commencement of operations in 2017, Hefler has incurred operating losses of \$8.6 million resulting in negative EBITDA of \$5.4 million, and has relied on capital injections from its shareholders and restructured terms from CIBC.
- 3.6 During the Consulting Engagement, Management advised Deloitte that the main factors hindering Hefler’s performance were:
- Biomass input prices being significantly in excess of what Management had projected during its due diligence.
 - Biomass consumption rates, a measure of the amount of input required to produce a MW, significantly exceeded Management’s expectation.
 - Poor operating results at the sawmill caused by inefficient equipment, limited management experience and high input costs.
 - Annual repairs and maintenance significantly exceeded Management’s expectations.
 - Utility costs, specifically water consumption rates, exceeded Management’s expectations.
- 3.7 At the date of this Report, Hefler employs approximately 14 employees and the Plant is run under the supervision of a Class One Power Engineer. In the past, Hawthorne and Katalyst have provided both strategic and financial oversight to Hefler.
- 3.8 Deloitte has been advised by Thornridge that during the week of January 15, 2021 the sole director of Hefler, being C. Robert Gillis, resigned, along with the officers, being Jason Weston and Candice Blaney (the “**Resignations**”). Since the Resignations, the Plant has been left without any stewardship or funding to continue operations.
- 3.9 As at January 14, 2021 (the date of the most recent internal financial statements of Hefler), a summary of the balance sheet is as follows:

3304051 Nova Scotia Limited (o/a Hefler Forestry Products)
Summary balance sheet
As at January 14, 2021

Current assets	
Accounts receivable	405,514
HST receivable	21,663
Inventory	121,982
Prepaid assets and deposits	98,225
Total current assets	647,384
Deferred financing costs	4,834
Investment tax credits	45,337
Property, plant and equipment	5,376,986
Total assets	6,074,541

3304051 Nova Scotia Limited (o/a Hefler Forestry Products)
Summary balance sheet
As at January 14, 2021

Current liabilities	
Bank indebtedness	1,526,970
Accounts payable and accrued liabilities	917,835
Current lease obligations	32,970
Term loan payable	5,097,778
Total current liabilities	7,575,553
Canada Emergency Business Account	40,000
Lease obligations	8,302
Due to shareholders	5,035,723
	12,659,578
Shareholders' equity	
Common shares	1,950,000
Deficit	(8,535,037)
Total shareholders' equity	(6,585,037)
Total liabilities and shareholders' equity	6,074,541

- 3.10 Pursuant to the terms of a credit agreement dated March 30, 2017 (as amended, the "**Credit Agreement**"), Hefler maintains a \$1.2 million demand operating facility, a term instalment loan with a balance of \$5.3 million and a \$10 thousand credit card facility. At the date of this Report the cumulative indebtedness owing to CIBC is approximately \$6.6 million.
- 3.11 As security for the Hefler obligations and liabilities to CIBC under the Credit Agreement, Hefler executed, among other things, a general security agreement, an assignment of the PPA and Operating Agreement, and a mortgage on its lands and buildings. In addition, Thornridge and Katalyst have executed joint and several guarantees in favour of CIBC in the amount of \$3 million and Hawthorne and Katalyst have executed a joint and several guarantee in favour of CIBC in the amount of \$900 thousand. RiverRoad executed an unlimited guarantee in favour of CIBC, including a pledge of the Hefler shares.
- 3.12 Since late November, CIBC has funded the Hefler operations via excess borrowings under the operating line, including the funding of \$36 thousand of payroll on January 19, 2021.

4.0 DELOITTE'S PRIOR INVOLVEMENT WITH HEFLER

- 4.1 On August 4, 2020, CIBC engaged Deloitte under the Consulting Engagement to perform an independent business review with respect to Hefler's affairs and financial position, including an assessment of CIBC's collateral position. As part of the Consulting Engagement, Deloitte undertook the following:
- a review and assessment of Hefler's financial position and historical operating results;
 - a review and assessment of Hefler's financial forecasts, including projected cash flows, and the reasonableness of the underlying assumptions and future operating outlook, including consideration of the various options available to Hefler;
 - a review and assessment of Hefler's business plan and future business prospects and the financial impact of this plan on the future viability of Hefler;

- d) an evaluation of Hefler's significant assets and liabilities and assessment of the current security position of CIBC;
 - e) a review and assessment of Hefler's insurance coverage;
 - f) a review and assessment of the Hefler's material contracts, specifically the power purchase agreement with Nova Scotia Power and any fiber supply contracts;
 - g) a review of the various statutory liens, potential priority payables and any deemed trusts affecting Hefler; and
 - h) in conjunction with Hefler and CIBC, created a sales and investment solicitation process (the "**SISP**").
- 4.2 On or around August 24, 2020, Deloitte delivered its initial findings report (the "**Findings Report**") under the Consulting Engagement to Hefler and CIBC. The key recommendation contained within the Findings Report was the immediate undertaking of a SISP.
- 4.3 In conjunction with Hefler and CIBC, Deloitte identified a number of potential interested parties to contact with respect to the Hefler assets (the "**Interested Parties**"). The Interested Parties consisted mostly of entities involved in the forestry industry; however a number of strategic parties were also contacted.
- 4.4 The outcome of the SISP was the receipt of one offer that was deemed acceptable to both CIBC and Hefler (the "**Offer**"). Subsequent to the receipt of the Offer, both Deloitte and Hefler worked with the proposed purchaser (the "**Purchaser**") to complete its due diligence.
- 4.5 On January 8, 2021, the Purchaser advised Deloitte that as part of its due diligence it had been advised that its business plan for the Plant may not be acceptable under the COMFIT. Additionally, the Purchaser sought to engage an advisor to complete a comprehensive review of the Plant; however, due to travel restrictions under COVID-19, it was likely this would delay any potential closing for several months.
- 4.6 Based on the current financial position of Hefler, and with neither Hawthorne nor CIBC willing to advance further funding, coupled with the outcome of the SISP and the resignation of the director and officers leaving the plant without direction, CIBC determined that the appointment of a Receiver was warranted to protect its security.

5.0 THE CIBC DEMAND

- 5.1 On September 15, 2020, Burchell's, on behalf of CIBC, issued notices of intention to enforce security over Hefler's assets to Hefler and Thornridge, Katalyst and Hawthorne. At the date of this Report, the required ten-day period has expired. CIBC and Hefler entered into a forbearance agreement on September 25, 2020 which remained in effect until January 14, 2021.

6.0 WICKWIRE'S PRELIMINARY SECURITY REVIEW

- 6.1 In preparing this Report, Deloitte engaged independent legal counsel to undertake, among other things, a high-level review of CIBC's loan documents, including the security granted by Hefler in favour of CIBC in connection therewith. At the date of this Report, and based on discussions with Wickwire, the Proposed Receiver is of the initial view that CIBC holds valid and enforceable security against Hefler. To the extent that the Court grants the Receivership Order sought by CIBC in its application, the Proposed Receiver will obtain a formal independent security opinion from Wickwire, a copy of which will be made available to the Court upon request and, in any event, prior to any distribution to CIBC or any other party.

7.0 DELOITTE'S CONSENT TO ACT AS RECEIVER

7.1 As contained within the Lane Affidavit, Deloitte confirms that it is willing to act as Receiver should the Court see fit to grant CIBC's request to appoint a Receiver over Hefler's assets. A copy of Deloitte's consent to act letter is enclosed as Appendix A.

8.0 CONCLUSION

8.1 Based on the foregoing, namely the lack of stewardship at Hefler and the need to secure and protect the value of the underlying assets, Deloitte supports CIBC's request that the Court grant the Receivership Order.

All of which is respectively submitted on January 20, 2021.

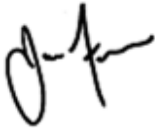
DELOITTE RESTRUCTURING INC.

Acting in its capacity as
Proposed Court Appointed Receiver of 3304051 Nova Scotia Limited
and not in its personal capacity.

Per:



Kurt MacLeod, MBA, CIRP, LIT
Vice President



James Foran
Senior Vice President

PRE-FILING REPORT OF DELOITTE RESTRUCTURING INC.
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APPENDIX A
DELOITTE'S CONSENT TO ACT

January 18, 2021

Kyle Lane
Senior Director, Special Loans
CIBC
25 King Street West, 16th Floor
Toronto, ON M5L 1A2

Dear Kyle,

Subject: 3304051 Nova Scotia Limited ("Hefler")

We understand that CIBC intends to make an application to the Supreme Court of Nova Scotia in Bankruptcy and Insolvency (the "**Court**") for an order (the "**Receivership Order**") appointing Deloitte Restructuring Inc. ("**Deloitte**") as the Court Appointed Receiver/Manager (the "**Receiver**") of Hefler.

Deloitte consents to act as the Receiver pursuant to the draft Receivership Order provided to the Court.

Sincerely,

DELOITTE RESTRUCTURING INC.

Per:



James Foran
Senior Vice President

c: Bruce Clarke, Q.C. (Burchell's)