

CANADA
PROVINCE OF QUEBEC
DISTRICT OF MONTREAL
No cour : 500-11-052107-170
No dossier : 41-2219514

SUPERIOR COURT
(Commercial Division)
Bankruptcy and Insolvency Act

IN THE MATTER OF THE PROPOSAL OF:

FREEMARK APPAREL BRANDS INC.
FREEMARK APPAREL BRANDS TEC INC.
FREEMARK APPAREL BRANDS ESP INC.
FREEMARK APPAREL BRANDS USA INC.

legal persons duly incorporated under the laws of
Canada, having their principal places of business at
5640 Pare Street, Mount Royal, Quebec, H3B 1M1

Debtors

-and-

RICHTER ADVISORY GROUP INC.

Trustee

**REPORT OF THE TRUSTEE ON THE FINANCIAL SITUATION
OF THE DEBTORS AND ON THE PROPOSAL**
(Sections 50(5) and 50(10)(b) of the *Bankruptcy and Insolvency Act*)

1. The purpose of the First Meeting of Creditors is to consider the joint proposal filed on July 24, 2017 (hereinafter the "Proposal") by Freemark Apparel Brands Inc., Freemark Apparel Brands TEC Inc., Freemark Apparel Brands ESP Inc. and Freemark Apparel Brands USA Inc. (hereinafter referred collectively as the "Debtors" or the "FAB Group").
2. Pursuant to Sections 50(5) and 50(10)(b) of the Bankruptcy and Insolvency Act, and in order to assist the ordinary unsecured creditors (hereinafter the "Unsecured Creditors") in considering the Proposal, the Trustee is hereby submitting its report on the financial situation of the Debtors and on the Proposal.
3. All the capitalized terms that are not otherwise defined herein shall have the meaning ascribed thereto in the Proposal.
4. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars.

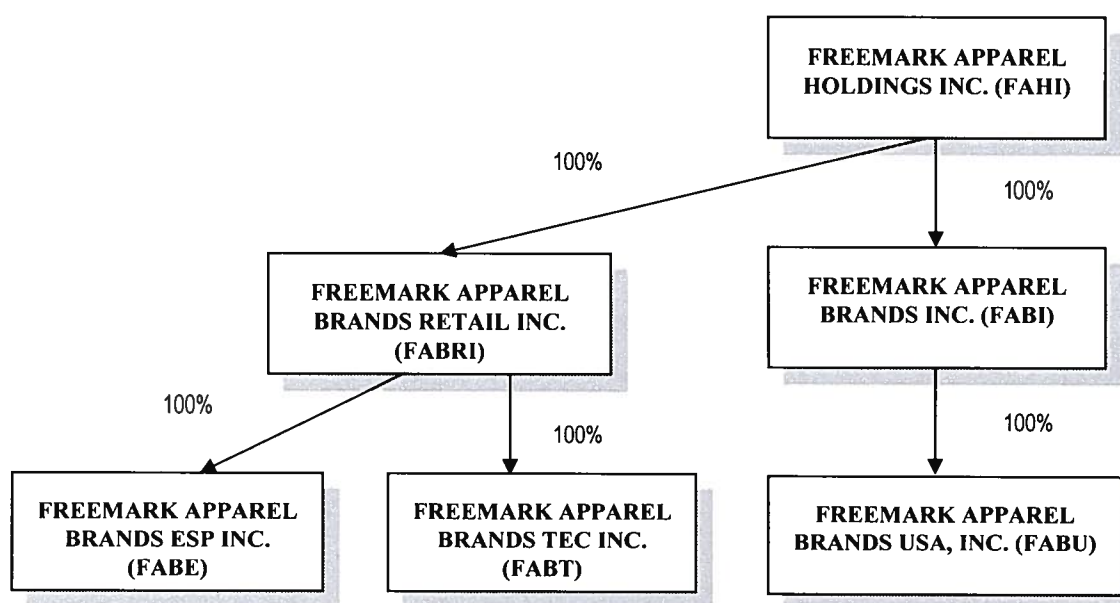
INTRODUCTION

5. On February 17, 2017, each of Freemark Apparel Brands Inc. ("FABI"), Freemark Apparel Brands TEC Inc. ("FABT"), Freemark Apparel Brands ESP Inc. ("FABE") and Freemark Apparel Brands USA Inc. ("FABU") filed a Notice of Intention to Make a Proposal (the "NOI"), the whole as appears in the documents filed in the court records.
6. On February 23, 2017, the court ordered the joint administration of FABI's notice of intention to make a proposal with the notices of intention to make a proposal of FABT, FABE and FABU.
7. On February 24, 2017, documents were sent by regular mail to all creditors of the Debtors, as identified by them, which included a copy of the Debtors' NOI, the whole as appears in the documents filed in the court records.
8. On March 16, 2017, April 27, 2017 and June 9, 2017, the Court granted extensions of time for the filing of a Proposal through to July 24, 2017 in order to allow the Debtors to implement certain restructuring initiatives, and subsequently to pursue and conclude a sale of the assets and business operations of the FAB Group.
9. On July 24, 2017, the Debtors filed a Joint Proposal ("Proposal") to their creditors. We enclose herewith the Proposal made by the Debtors to their creditors, a proof of claim form, a voting form, a proxy and a notice indicating the place and time of the creditors' meeting to address the Proposal.
10. This report summarizes the relevant information and key elements that may assist the Unsecured Creditors in evaluating the Debtors' affairs and the Proposal, presented as follows:
 - a) Overview of the Debtors
 - b) Causes of Insolvency
 - c) Restructuring Initiatives and Sale Transactions
 - d) Financial Information
 - e) Proposal
 - f) Estimated Distribution to the Unsecured Creditors
 - g) Conclusion and Recommendation

11. Additional information related to the overview of the Debtors, causes of insolvency, restructuring measures and asset sale transactions have previously been detailed in reports of the Trustee dated March 7, March 14, April 25, May 9 and June 7, 2017. All prior reports of the Trustee have been filed in the court records and can be found on the Trustee's website at: <http://www.richter.ca/Folder/Insolvency-Cases/F/Freemark-Apparel-Brands>.

OVERVIEW OF THE DEBTORS

12. The organizational chart for the Freemark group of companies, which includes the four Debtors subject to the NOI proceedings and the Proposal, can be represented as follows:



13. At the time of the NOI filing, the FAB Group was a premier retailer of branded apparel, operating since 2004. The business is more fully described as follows:
- FABE and FABT operated 58 retail locations throughout Canada under the following brands: Bench, Scotch & Soda, Esprit & Thread+Copper. FABT operated the Bench, Scotch & Soda and Thread+Copper stores while FABE operated the Esprit stores;
 - FABI operated the wholesale business of the FAB Group in Canada. FABI had long-standing relationships with The Bay, Simons, Winners, Saks Off 5th and many other retailers;
 - FABU operated the wholesale business of the FAB Group in the United States.

14. The Debtors operated their retail and wholesale businesses pursuant to various license agreements with several brands based in Europe: Bench, Scotch & Soda / Amsterdam Couture, Esprit and Garcia.
15. The Debtors' head office and principal distribution center were located in Montreal and, at the time of filing, the Debtors employed approximately 600 employees at the head office, distribution center and retail stores.

CAUSES OF INSOLVENCY

16. Commencing in 2014, the Debtors began experiencing a decline in both sales and profits, which accelerated into a significant downturn in 2016. Management attributes the negative trending to a number of factors including:
 - a) Increasing competition in the marketplace including the recent entry of international retailers not previously present in Canada;
 - b) Overhead cost structure not in line with the declining level of operations;
 - c) Unprofitability of numerous retail locations;
 - d) Unsuccessful launch of the Thread + Copper banner in 2016.

In response to the above-noted challenges, the Debtors attempted to restructure the businesses but ultimately came to the conclusion that a formal restructuring was the only alternative to try and preserve a going concern operation.

RESTRUCTURING INITIATIVES AND SALE TRANSACTIONS

17. Following the NOI filing, the Debtors implemented several operational restructuring initiatives which were developed with the assistance of retail, leasing and financial restructuring professionals, including:
 - a) Headcount reductions at the corporate head office, and other overhead rationalizations;
 - b) Closure of unprofitable retail stores, including the wind-down and liquidation of all 10 Thread+Copper stores, and shuttering 5 unprofitable Bench locations;
 - c) Renegotiation of more favorable lease terms for 16 Bench and Esprit stores;
 - d) Operational initiatives to improve retail store profitability;
 - e) Shift in wholesale strategy towards off-price channels.

18. Concurrently with the implementation of these operational restructuring initiatives, the Debtors concluded two separate asset sale transactions during the NOI period, which were reviewed and recommended by the Trustee and approved by the Court:
- a) The Debtors sold to the Scotch and Soda licensor (Scotch & Soda Export B.V.) substantially all the assets related to the brand's retail and wholesale business operations in Canada.
 - On March 8, 2017, the Court issued an Approval and Vesting Order authorizing the transaction, which was concluded by the parties shortly thereafter.
 - The net purchase price paid by Scotch and Soda Export B.V. was \$2 million, of which \$1.3 million was applied as a reduction to the secured indebtedness of HSBC Bank Canada ("HSBC"), and \$0.7 million was retained by the Debtors to provide liquidity for operations.
 - b) Pursuant to a court-approved sale and investment solicitation process conducted by the Trustee, the Debtors concluded a transaction for the sale of substantially all the remaining assets and operations of the FAB Group to 10036331 Canada Inc. (the "Purchaser"), an entity controlled by the majority shareholders of the FAB Group.
 - The purchase price of approximately \$24 million consisted of the repayment in full of the secured indebtedness due to HSBC (\$10.2 million), the assumption of a secured loan due to FAHI (\$11.2 million), and the assumption of accrued employee benefits and post-filing operating liabilities (estimated at \$2.4 million).
 - Following the issuance by the Court of an Approval and Vesting Order on May 16, 2017, the Debtors and the Purchaser completed the transaction on May 19, 2017.
19. As a result of the above noted transactions, the Debtors no longer own any assets and no longer carry on any business activities.

FINANCIAL INFORMATION

20. The following financial data is based upon unaudited financial information prepared by the Debtors' representatives, the Debtors' books and records, and discussions with the Debtors' representatives. The Trustee has not audited, reviewed, or otherwise attempted to verify the accuracy or completeness of such information. This information is submitted solely to assist the reader in assessing the financial position of the Debtors. The Trustee makes no representation or warranty as to the accuracy of said financial information.

Statement of Earnings (Loss)

FAB Group Income statement In thousands	7 mo. ended	12 months ended	
	31-Jan-17 (Unaudited)	26-Jun-16 (Audited)	28-Jun-15 (Audited)
Net sales	\$ 51,015	\$ 71,594	\$ 75,543
COGS	27,059	30,511	33,217
Gross margin	23,956	41,084	42,326
Operating expenses			
Selling	24,829	33,168	31,983
General and administrative	7,541	9,026	9,359
Financial	733	577	492
	33,103	42,770	41,834
Earnings (loss) from operations	(9,147)	(1,687)	492
Other Expenses	-	(561)	(436)
Earning (loss) before income taxes	(9,147)	(2,248)	56
Income tax recovered	(1,154)	(562)	(107)
Net earnings (loss)	\$ (7,993)	\$ (1,686)	\$ 163

21. As noted above, the Debtors reported a combined net loss of \$8.0 million for the 7-months ended January 31, 2017. The FAB Group's cumulative 19-month loss prior to filing the NOI on February 17, 2017 approximated \$9.7 million.

January 31, 2017 Balance Sheet

22. The following table summarizes the Debtors' last month-end balance sheet (by entity and on a combined basis) prior to the February 17, 2017 NOI filing:

FAB Group Balance Sheet as at Jan. 31, 2017 (Unaudited) In thousands	FABE	FABT	FABI	FABU	Total Combined
Assets					
Current assets					
Cash and short-term investments	\$ -	\$ -	\$ -	\$ 38	\$ 38
Accounts receivable	8	549	1,644	405	2,606
Income taxes receivable	-	599	916	-	1,516
Inventory	1,971	11,242	3,980	421	17,615
Prepaid expenses and deposits	18	661	1,208	17	1,904
Intercompany receivable (payable)	(2,362)	(8,382)	10,941	-	198
	(364)	4,669	18,690	881	23,876
Furniture, fixtures, leasehold improvements	813	10,730	1,410	-	12,952
Total assets	\$ 449	\$ 15,399	\$ 20,100	\$ 881	\$ 36,829
Liabilities					
Current Liabilities					
Bank indebtedness	\$ 65	\$ 836	\$ 5,077	\$ -	\$ 5,978
Accounts payable and accrued liabilities	59	5,744	9,892	873	16,568
Income tax payable	-	-	-	8	8
Current portion of obligations under capital leases	194	2,256	183	-	2,632
	318	8,836	15,152	881	25,187
Obligations under capital leases	473	2,460	328	-	3,260
Loans payable, parent company	-	6,000	4,200	-	10,200
Deferred lease inducements	-	986	-	-	986
Deferred lease obligations	20	1,221	-	-	1,240
Total liabilities	810	19,502	19,680	881	40,874
Shareholders' equity					
Capital stock	-	-	2,000	-	2,000
Retained earnings (losses)	(362)	(4,103)	(1,580)	-	(6,045)
	(362)	(4,103)	420	-	(4,045)
Total liabilities and shareholders' equity	\$ 449	\$ 15,399	\$ 20,100	\$ 881	\$ 36,829

Debtors' Statement of Financial Affairs

23. We have summarized the assets and liabilities of the FAB Group as at July 7, 2017, reported on the Debtors' Statement of Financial Affairs. The Debtors have elected to present a joint Proposal for the FAB Group, and as such the Statement of Financial Affairs was prepared on a combined basis.

a) Assets

As a result of the two asset sale transactions outlined in a prior section of this report, the Debtors no longer own any assets or carry on any business activity.

b) Liabilities

Liabilities indicated below are based on the books and records of the Debtors, the Statements of Affairs as of July 7, 2017 and management's representations.

Freemark Apparel Brands Inc.	
Estimated Liabilities - July 7, 2017	
In thousands	
Secured Creditors	\$ -
Preferred Creditors	-
Subsequent Creditors	-
Related Creditors	1,561
Unsecured Creditors	
Trade Creditors	10,254
Landlord damages	8,714
Employees (severance)	215
	<u>19,183</u>
Total	\$ 20,744

Secured Creditors (\$0)

- At the time of the NOI filing, the Debtors had two secured creditors:
 - HSBC, which was owed \$11.0 million; and
 - FAHI, which had made secured loans to both FABI and FABT in the aggregate amount of \$10.7 million, which loans were fully subordinated to the security of HSBC.
- The Trustee engaged independent legal counsel, who provided the Trustee with opinions confirming the validity and enforceability of the security granted by the Debtors in favour of HSBC, as well as the validity and enforceability of the security granted by FABI and FABT in favor of FAHI.
- As a result of the aforementioned asset sales, the indebtedness due to HSBC was repaid in full, while the secured loans owed to FAHI were assumed by the Purchaser as part of the May 19, 2017 transaction. However, the Debtors have not been released of said FAHI claims.

Preferred Creditors (estimated at \$0)

- The Debtors believe that all amounts owing to Preferred Creditors (including employee wages and vacation) have been paid in full. However, it will be determined through the claims process if any creditors will claim preferred status.

Subsequent Creditors (estimated at \$0)

- To the knowledge of the Trustee, all obligations incurred by the Debtors subsequent to the filing of the NOI were either paid by the Debtors post-filing, or assumed by the Purchaser as part of the asset sale transaction concluded on May 19, 2017.

Related Creditors (estimated at \$1.6M)

- FABI (\$1.3M) and FABU (\$0.3M) currently have \$1.6M of unsecured indebtedness owed to Freemark Apparel Brands Group Inc., a company controlled by the majority shareholders of the FAB Group.

Unsecured Creditors (estimated at \$19.2M)

With regards to Unsecured Creditors, we note the following:

- Trade creditors: the amounts reflected above are based on the books and records of the Debtors;
- Landlords: the amounts reflected above represent an estimate of the aggregate amount that could be claimed by landlords pursuant to section 65.2(4)(b) of the Act in respect of damages for resiliated leases, mitigated by certain short term rental agreements entered into for several store locations;
- Employees: the amounts reflected above consist of estimated amounts owing for pay in lieu of notice of termination and severance for certain head office and store employees. All wages and accrued vacation pay were paid to terminated employees upon their departure. The estimated claims of approximately \$215,000 are based upon a recently received government notice and claim filed on behalf of certain employees.

24. Proof of claim forms and Employee Claim Notices (where applicable) will be sent to all known creditors. However, at the present date, the Trustee is unable to determine if the Debtor's records are consistent with those of its creditors. Upon reception of the proofs of claim, the Trustee will review them and deal with any discrepancies for purposes of collocation of claims.
25. The Trustee cautions that these amounts may change as proofs of claims are filed and such changes may be significant.

PROPOSAL

26. The Trustee notes that the following is only a summary of the terms of the Proposal. Creditors are advised to read the Proposal for complete details of the terms of the Proposal.
27. The terms of the Proposal provide that a payment of \$225,000 will be remitted to the Trustee by FAHI (hereinafter referred as the "Debtors' Shareholder") within 10 days following the approval of the Proposal by the Court, for distribution to the Debtors' creditors.
28. The Proposal applies only to Unsecured Claims, Preferred Claims (if any) and Employee Claims. For further clarity, the Proposal does not apply to Secured Claims, or to Subsequent Claims and Proposal Expenses which are to be assumed by third parties.
29. According to the terms of the Proposal, the following amounts must be paid in priority:
 - a) Crown claims that could be subject to a demand under Section 224 (1.2) of the *Income Tax Act*, or under any substantially similar provision of provincial legislation, shall be paid in full, within six months of the approval of the Proposal by the Court, or as may otherwise be arranged with the Crown;
 - b) Amounts owing to employees (past and present) and that they would have been entitled to receive under Section 136(1)(d) of the Act if the Debtors had been declared bankrupt on the date of the approval of the Proposal, shall be paid in their entirety immediately after the approval of the Proposal;
 - c) Preferred Claims, as described in paragraph 136 the Act, being such claims directed by the Act to be paid in priority to all other claims in the distribution of the property of a bankrupt, excluding the employee claims noted in the b) above. The Preferred Claims, without interest or penalty, shall be paid in their entirety in priority to Unsecured Claims within thirty (30) days of the approval of the Proposal by the Court or as may be otherwise arranged with the Preferred Creditors.

As noted in the following section, these priority amounts are expected to be Nil.

30. The amount available after payment of the above-mentioned amounts ("Net Amount") shall be paid to the Trustee within 10 days of the Approval of the Proposal. Each of the Unsecured Creditors shall receive in full and final payment of its Unsecured Claim, without interest or penalty, the following amounts:
 - a) The lesser of one thousand dollars (\$1,000) or the amount of its Proven Claim; and

- b) A pro-rata share, calculated on the basis of the remaining amount of its Proven Claim, of the balance of the Net Amount after payment of the amounts defined in a) above.

The funds shall be disbursed by the Trustee within (i) sixty (60) days after the Approval for all the Unsecured Creditors other than the Employee Creditors and (ii) fifteen (15) days of the receipt by the Trustee of the required governmental confirmations in respect of the Employee Creditors;

31. Conditional upon the acceptance by the creditors of the Proposal and to the approval thereof by the Court, the Related Creditors waive and renounce (i) to any right to prove in whole or in part any Unsecured Claims they may have and (ii) to any dividend that is or could be payable to them under the Proposal.
32. Subject to the terms of the Proposal, each Unsecured Creditor with a Proven Claim equal to or less than \$1,000 shall be deemed to have voted in favour of the Proposal. Likewise, any employee that has not filed a proof of claim prior to the first meeting of creditors shall be deemed to have voted in favour of the Proposal in an amount equal to his Employee Claim.

ESTIMATED DISTRIBUTION TO UNSECURED CREDITORS

33. In the event that the creditors reject the Proposal, the Debtors will automatically be bankrupt. The following information serves to advise the creditors of the Trustee's estimate as to the distribution to creditors under the Proposal in comparison to the estimated distribution under a bankruptcy scenario.

Proposal

34. Based on the Claims reflected in the Debtors' Statements of Affairs, the amount of the Proposal (\$225,000) would be distributed as follows:

Freemark Apparel Brands Inc. Summary of Proposal	# of Creditors	Estimated Claims	Estimated Distribution	Recovery %
Secured Creditors		\$ -	\$ -	N/A
Preferred Creditors		-	-	N/A
Subsequent Creditors		-	-	N/A
Related Creditors	1	1,560,802	-	0.0%
Unsecured Creditors				
Trade creditors	142	10,254,454	158,926	1.5%
Landlord damages	12	8,713,958	32,956	0.4%
Employees (severance)	35	214,523	33,118	15.4%
Total Unsecured Creditors		19,182,934	225,000	1.2%
Total		\$ 20,743,736	\$ 225,000	

35. It is estimated that the \$225,000 Proposal would represent a 1.2% total recovery to Unsecured Creditors, based upon the estimated claims known to the Trustee. We caution that these amounts may change as proofs of claims are filed and such changes may be significant.
- The Proposal would provide some level of recovery to an estimated 142 unsecured trade creditors, of which approximately 50 would receive in excess of 25% of their claim and 22 would be paid in full;
 - 35 Employee Creditors, with total claims of approximately \$215,000, would receive a total of approximately \$33,000 (15% recovery). Of this group, 8 employees are expected to have their claims paid in full pursuant to the Proposal.

Bankruptcy

36. As previously noted, the Debtors no longer own any assets following the two asset sale transactions concluded during the NOI period. In a bankruptcy scenario, the realization to Unsecured Creditors from the Debtors' estate would therefore be Nil.
37. However, we note that 27 employees whose claim for unpaid severance / notice exceeds \$1,000 would likely recover a greater sum in a bankruptcy scenario, pursuant to the Wage Earner Protection Program Act ("WEPPA"). Under the WEPPA program, which applies in the case of bankruptcy but not in the event of a Proposal, employees may claim up to \$3,400 of unpaid severance and/or pay in lieu of notice.
38. Payment of Employee Claims under the Proposal is expected to be significantly quicker than the timeline for processing and distribution in respect of claims under the WEPPA program.

Other considerations

39. Sections 95 to 101 of the Act will not be applicable to the Proposal. The remedies pursuant to these provisions relate to the recovery of certain amounts under reviewable transactions, preferential treatments and asset disposals.
40. The Trustee has performed a cursory review of the transactions that occurred during the three month period (with unrelated third parties) and 12-month period (for transactions with related parties), prior to the filing of the NOI. Pursuant to our cursory review of these transactions, it appears that same have been concluded in the normal course of business according to historical payment patterns and/or terms of payment made available to the Debtors by the creditors. No material reviewable transaction was noted.

TRUSTEE'S CONCLUSION AND RECOMMENDATION

41. The Proposal presented by the Debtors, which is funded directly by the Debtors' Shareholder, will provide recovery to the Unsecured Creditors of approximately 1.2%. Alternatively, given the fact that the Debtors have no remaining assets, there will be no dividend to Unsecured Creditors in the event of a bankruptcy of the Debtors.
42. Notwithstanding that Employee Creditors in general are expected to realize a greater recovery in a bankruptcy scenario, through a claim under the WEPPA program, acceptance of the Debtors' Proposal is in the best interest of the general body of Unsecured Creditors.
43. Accordingly, the Trustee recommends the Unsecured Creditors vote in favour of the Proposal.

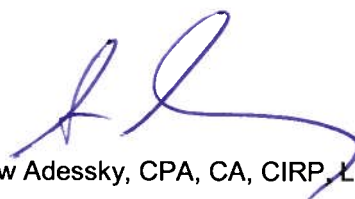
Respectfully submitted at Montreal, this 24th day of July 2017.

Richter Advisory Group Inc.

Trustee



Eric Barbieri, CPA, CA, CIRP, LIT



Andrew Adessky, CPA, CA, CIRP, LIT