

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
(COMMERCIAL LIST)**

**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 OF COMPROMISE OR ARRANGEMENT OF  
THE HARD ROCK PAVING COMPANY LIMITED AND THE COMPANIES LISTED  
ON SCHEDULE "A"**

**AFFIDAVIT OF WILLIAM SCARLETT  
(SWORN JULY 9, 2008)**

I, **WILLIAM SCARLETT**, of the City of Burlington, in the Province of Ontario,  
MAKE OATH AND SAY AS FOLLOWS:

1. I am Senior Territory Manager of Caterpillar Financial Services Limited ("CFSL"), and as such, I have knowledge of the matters hereinafter deposed to. Where my knowledge is based upon information provided to me by others, I have stated the source of the information and I believe it to be true.
2. I make this Affidavit in support of CFSL's position with respect to the motion by the Company returnable July 9, 2008 seeking approval of a sale transaction to Miller Paving Limited, and Waterford Sand and Gravel Limited.
3. The Company is also seeking an extension of the stay of proceedings to permit the Company to complete the sale transaction, to October 10, 2008.
4. It is the position of CFSL that it
  - (a) supports the sale of assets to Miller and Waterford on the terms proposed by the Company for approval by the Court;

- (b) opposes the increase in the administration charge, or in the alternative proposes that the issue of the increase to the administration charge be deferred to permit the parties to discuss the issue, and if not resolved, to return to court to deal with that issue;
  - (c) proposes a short extension of the stay of proceedings for a period of week pending the discussion of the administrative charge.
5. This Affidavit is also supplementary to my affidavits sworn:
- (i) April 28, 2008, in the related receivership proceedings commenced by CFSL against the Applicants;
  - (ii) April 30, 2008, which was filed in response to the within Application for the issuance of an Initial Order under the *Companies' Creditors Arrangement Act* (the "CCAA");
  - (iii) May 12, 2008, in these proceedings which outlines matters which took place between May 2 and May 10, 2008, (collectively, the "Previous Affidavits"), copies of which (without Exhibits); and
  - (iv) Two affidavits sworn June 10, 2008.

## Overview

6. As noted in the Previous Affidavits, CFSL is a secured creditor of Hard-Rock Paving Company Limited ("Hard-Rock Paving", or the "Company") and is owed, as of April 23, 2008, approximately \$31,657,038.38.
7. The other Applicants are guarantors of the indebtedness of Hard-Rock Paving and have given security to CFSL over their assets in support of the guarantees.
8. CFSL has made demand upon Hard-Rock Paving and the other Applicants and has delivered Notices of Intention to Enforce Security (the "NOIs") pursuant to Section 244 of the *Bankruptcy and Insolvency Act* (the "BIA").

9. Pursuant to the Order of the Honourable Mr. Justice Spence dated May 2, 2008, (the “Initial Order”), this Court stayed all proceedings as against the Applicants (the “CCAA Stay”).

10. The Initial Order was issued subject to an endorsement of the Court (the “May 2 Endorsement”) which provides as follows:

“The issuance of this Order is not deemed to be consent to this Order or these proceedings by Caterpillar Financial Services Limited (“CFSL”) and subject to the stay contained in the Order, is without prejudice to the rights of CFSL in the bankruptcy and receivership applications that have been commenced by CFSL (the “CFSL Applications”). The CFSL Applications shall be returnable at the hearing of any motion by the Applicants to seek approval of debtor in possession financing or any extension of the Stay. CFSL is at liberty and this Order is without prejudice to CFSL bringing on the CFSL Applications in response to any motion that is brought in these proceedings on notice to the service list in response to the service of any such motion.”

11. On May 12, 2008, this matter came back on before Justice Spence, wherein CFSL obtained an order amending the Initial Order (the “Amended and Restated Initial Order”), which, among other things, authorized CFSL to provide certain debtor in possession financing to the Company (the “DIP Loan”), over the objection of McLennan Financing Limited, (“McLennan”) who itself sought to provide the Company with DIP financing. Pursuant to the Amended and Restated Initial Order, the Applicants were authorized and empowered to obtain and borrow from CFSL an amount not to exceed \$1,250,000 on terms and conditions set out in a facility letter dated May 7, 2008 (the “Facility Letter”).

12. The Amended and Restated Initial Order also extended the CCAA Stay until June 10, 2008, and authorized a sale process for the Company’s assets (the “Sale Process”).

13. As set out in the May 2 Endorsement, CFSL currently has bankruptcy and receivership applications outstanding in respect of each of the Applicants. CFSL adjourned the return date for these bankruptcy and receivership applications to June 10, 2008, to coincide with the expiry of the CCAA Stay.

14. Upon the commencement of these proceedings, the Company, with the assistance of the Monitor, had commenced a process for marketing the assets of the Company for sale. CFSL ultimately did not oppose the issuance of the Amended and Restated Initial Order on the understanding that during the following 30 days, the exposure of the Company to the market would determine its viability as a going concern entity, and would determine the value to be placed on its assets.
15. At the expiry of the stay on June 10, 2008, the Company had obtained certain expressions of interest in the assets of the Company, but had not received any firm offers.
16. On return of this matter on June 10, 2008, the Court ordered an extension of the stay of proceedings for 30 days to July 10, 2008, in order to permit the Company to complete the marketing process and obtain any offers for the assets as may be forthcoming from interested parties.
17. The court adjourned the matter to June 12, 2008, to give the parties time to determine who would provide the DIP financing.
18. In light of the extension of the stay of proceedings, CFSL determined that it would offer the Company a second requested DIP facility in the amount of \$1 million. The second DIP facility was approved by the Court on return of the motion on June 12, 2008. \$225,000 of that DIP facility was advanced later that day to the Company.
19. All of the proceeds of the DIP facilities advanced by CFSL have since been used by the Company.

#### **Chronology of Various Events since June 10, 2008**

20. Subsequent to the extension of the stay, the Company continued to pursue its sale process with the assistance of the Monitor. The Monitor undertook negotiations with those parties that had expressed interest in the assets of the Company, and sought to obtain firm offers from each of them.

21. In the meantime, the Company continued to operate in a reduced capacity.
22. The Company also continued to pursue collections from its customers to support its operations.
23. The collection of receivables is complicated by the fact that most receivables are impressed with trust obligations to subcontractors under the *Construction Lien Act*. KPMG and the Monitor have taken steps to determine the amount by which collected receivables are subject to such trust obligations.
24. By Monday June 16, 2008, it had become clear that the Company had not made sufficient provision in its cash flow for the expenses related to professional services. Though CFSL and KPMG raised this as a concern, no steps were taken by the Company at that time to deal with the issue.
25. It was also clear by June 16, 2008, upon the Company providing its weekly DIP report that the Company's receipts for the week of June 6, 2008 were below forecasts by \$166,000. The net shortfall in cash flow for the week of June 6, 2008 was approximately \$132,000.
26. In the meantime, CFSL was advised by the Company that two going-concern offers were expected to be forthcoming from interested parties.
27. By June 17, 2008, the Company had only \$325,000 in DIP financing left. CFSL sought from the Company to learn what it intended to do if it ran out of cash. CFSL also sought to learn why collections were lower than forecast.
28. By email dated June 18, 2008, KPMG, CFSL's consultant, advised that it had reviewed the Company's weekly report for the week ending June 13, 2008, and noted that expenditures were over budget by \$184,000. KPMG also sought updates regarding its contract with Dufferin Construction, and sought to learn the status of various account collections, including those outstanding with the Ontario Ministry of Transportation. CFSL and KPMG were advised that these matters had not yet been resolved.

29. By email dated June 26, 2008, the Company delivered its weekly financial report. This report noted for the first time that as a result of the underestimate of professional fees, it would be seeking an increase in the administration charge or a further DIP in the amount of \$125,000.
30. The Company set a deadline for final offers for its assets of June 27, 2008.
31. By email dated June 27, 2008, the Monitor delivered to CFSL copies of the offers received by the Company and a summary comparison of the offers. It was clear that all offers received would result in a substantial shortfall to the secured lenders of the Company, CFSL and GE.
32. A conference call with the Company and the Monitor to discuss was held on the morning of June 30, 2008. During that conference call, the Monitor and the Company confirmed that none of the offers received were sufficient to pay out the secured lenders in full.
33. During the week of June 30, 2008, the parties took steps to analyze the various offers in order evaluate their positions.
34. After analyzing its security position and considering its options, CFSL determined that it would support the transaction with Miller and Waterford, and advised the Company and the Monitor of this fact on Friday July 4, 2008.
35. The Monitor has delivered a report advising that it recommends acceptance of the Miller/Waterford offers, and the Company is also seeking court approval and acceptance of the offer.
36. CFSL does not support any additional financing to the Company through an extended CCAA process. CFSL is therefore supportive of an immediate closing of the transaction, as it appears that the Company has extremely limited cash to sustain itself as an operating concern beyond only a few days.
37. With respect to the extension of the stay of proceedings, it appears that after closing the transaction, there will need to be continued collection of accounts receivable of the

Company, for the benefit of creditors. It is CFSL's position that such receivables, together with the proceeds of sale to Miller/Waterford should be paid to the Monitor to be held pending a distribution motion, or alternatively pending the appointment of a receiver.

38. It is CFSL's position that the ultimate extension of the stay of proceedings should only go to August 8, 2008, as recommended by the Monitor. This provides sufficient time to close the transaction. It will likely be appropriate by that time to terminate the CCAA and convert the process into a receivership for final realization and distribution of the balance of the Company's assets, and this will provide sufficient time to deal with issues for winding up the CCAA proceedings.
39. CFSL has not had sufficient opportunity to consider the issue of the requested increase in the administration charge to \$500,000 in priority to CFSL. The issue of an increase in the administrative charge was raised in the Monitor's report served on Friday July 4, 2008. However, CFSL only learned that this would be requested on this motion by the Company when it received the motion record on July 8, 2008. There is no request contained in the notice of motion filed; it is only contained in the affidavit of David Semley. Furthermore, there is no evidence or back up based on a budget that would justify the amount of the increase of the charge.
40. CFSL opposes an increase in the amount of the charge to \$500,000. CFSL proposes that this issue be deferred for a short period of time to permit the parties to discuss the issue. If it cannot be resolved, the parties can return to court to address the matter. The stay of proceedings can be extended for a short period of a week pending these discussions.

### **Response to GE**

41. GE served an affidavit by email at 9:47 p.m. on July 8, 2008, advising for the first time that it opposed the sale to Miller/Waterford, and proposing, alternatively, that it take its equipment out of the sale to Miller/Waterford, or that it offer to buy all of the Purchased Assets on the same terms as Miller/Waterford. Up until that time, GE has supported the

sales process and indicated that it preferred a going concern sale as opposed to a piecemeal asset sale.

42. No offer to purchase or draft agreement of purchase is included in the material served by GE. GE did not participate in the sale process conducted by the Company that has taken place over the last 60 days since the issuance of the Initial Order. Furthermore, for GE to come forward now is not fair to the others who did participate in the process, as it has been privy to all of the offers put forward by the offerors.
43. GE points to the realization and allocation estimates provided by the Monitor. However, these were provided on a without prejudice basis, and the Monitor explicitly advised through their counsel that they were not to be relied upon. The main issues with the estimates prepared by the Monitor are that they do not take into account the fact that the GE obligations are not cross-collateralized across the equipment subject to these obligations. Some equipment has equity, some does not. Furthermore, the Monitor's estimates do not take into account the repayment of the DIP, which attaches to all collateral, including the GE equipment. Finally, the estimates were based on the values attributed to the equipment by the Company, and not by an independent appraiser.
44. GE has stated that it is confident that it can sell its equipment for more than the realizations suggested by the Monitor. However, it has prepared no independent appraisals, and has no basis for demonstrating that a better realization can be made for its equipment than through the sale to Miller/Waterford.
45. The offer to purchase by Miller/Waterford is the best outcome in the circumstances for all stakeholders in this matter. An independent appraisal of the equipment can be obtained in the next week to provide appropriate values for allocation as between the security held by GE and CFSL. With independent third party appraisals, there is no prejudice to GE in selling the equipment to Miller/Waterford.


46. Furthermore, much of the GE financed equipment may have significant equity, to which GE is not entitled, and which would be subject to the claims of other creditors, including CFSL.
47. It is therefore the position of CFSL that there are no grounds for opposing the sale to Miller/Waterford as a going concern, and all parties will be significantly prejudiced if it does not proceed.
48. I therefore swear this Affidavit in response to the Company's motion for, among other things, the approval of the sale to Miller/Waterford, and an extension of the CCAA Stay herein, and for no other or improper purpose.

SWORN before me at the )  
City of <sup>Toronto</sup> Oakville, Ontario )  
this 9th day of July, 2008 )



A Commissioner, etc.

Steven Weisz



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**WILLIAM SCARLETT**

