

**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 PROPOSED PLAN OF COMPROMISE OR
ARRANGEMENT WITH RESPECT TO
BRAKE PRO, LTD.**

MONITOR'S FOURTH REPORT TO THE COURT

A. INTRODUCTION

BDO Dunwoody Limited (the "Monitor") was appointed Monitor of Brake Pro, Ltd. (also referred to as "Brake Pro", the "Applicant" or the "Company") by an Initial Order of the Honourable Mr. Justice Stinson of the Ontario Superior Court of Justice on 24 July 2007 (the "Initial Order"), pursuant to the application (the "Application") to the Court by the Applicant for protection from its creditors under the *Companies' Creditors Arrangement Act* (the "CCAA"). The Applicant was granted protection for an initial period of 24 days until 17 August 2007 (the "Stay Period").

The Application was made on notice to the Applicant's major secured creditor, Wachovia Capital Finance Corporation (Canada) ("Wachovia" or the "Bank"), which did not oppose the Initial Order. Pursuant to the Initial Order, Wachovia is an unaffected creditor.

On 23 July 2007, Brake Pro entered into a Forbearance Agreement with the Bank (the "Forbearance Agreement"), pursuant to which Wachovia agreed to extend credit to Brake Pro through the CCAA process subject to various conditions, typical to asset based banking arrangements. These conditions included a requirement that all funds paid to Brake Pro be paid to a designed bank account ("the Lock Box") and that Wachovia would make advances based on draw requests from Brake Pro, which requests would be conditional upon Brake Pro being in

compliance with the conditions of the Forbearance Agreement, including a lending formula based on the amount and eligibility of accounts receivable and inventory. Because the largest part of Brake Pro's business was based on selling into the United States, the lending formula included adjustments related to fluctuations in the relative value of Canadian and United States currencies.

In addition to the Stay Period, the Initial Order authorized Brake Pro and the Monitor to undertake a sale process (the "Sale Process") whereby the assets of the Company would be marketed for sale as a going-concern.

By Order dated August 17, 2007, Justice Spence granted an extension of the stay of proceedings established in the Initial Order, to October 1, 2007. On October 1, 2007, Justice Campbell granted a further extension of the stay of proceedings to October 15, 2007 (the "Second Extension Order") to determine if a going-concern sale was possible and, in the alternative, for the Company, with the assistance of the Monitor, to prepare a winding-up plan. On October 12, 2007, Justice Siegel granted a further extension to October 25, 2007 (the "Third Extension Order") to enable the Company, with the assistance of the Monitor, to negotiate, if possible, an en-bloc sale of the assets of the Company. As well, on October 15, 2007, Justice Siegel granted an order (the "October 15 Order") approving the sale of certain inventory to BRF Precision Inc. ("BRF").

The purpose of this report is to advise the Court on the following:

- (a) Brake Pro's activities since the last report of the Monitor;
- (b) The Monitor's activities to date;
- (c) The filing by the Monitor of the Second Supplement to its Third report; and
- (d) Brake Pro's planned activities during the requested extension of the Stay Period to November 8, 2007.

This Report is filed in order to recommend in favour of:

- Brake Pro's request for an extension of the Stay Period to November 8, 2007;
- The sale of additional inventory to BRF;

- The further amendment of paragraph 18(e)(ii) of the initial Order to permit the sale of inventory at such prices and on such terms as the Company may negotiate and the Bank and the Monitor may agree, without further approval of the Court; and
- the distribution to the Bank of the proceeds of the sale of certain inventory to BRF authorized by the October 15 Order, and all proceeds of sale of additional inventory to BRF for which authorization is sought herein.

B. EXECUTIVE SUMMARY

In summary, the Monitor reports as follows:

- The Company has sold inventory in the normal course of business, and continues to collect accounts receivable. All proceeds of receivables collected and of this sale of inventory in the normal course have been deposited to the Company's Lock Box account, as authorized by the Initial Order.
- As reported below, the Company has negotiated a sale of a quantity of finished goods inventory to BRF outside of the normal course of business, for which court approval is sought;
- The Company with the assistance of the Monitor and the Bank's consultants, Lissner Associates Limited, has initiated a winding-up process to realize on the assets of the Company for the benefit of the creditors. This includes the sale of further inventory out of the ordinary course of business to current customers, on such terms and at such prices as can be negotiated. The Company seeks an order herein authorizing such sales;
- The Company is seeking the distribution of the proceeds of the sale of inventory to BRF to the Bank;
- The Company and the Monitor sought a going-concern or en-bloc offer for the assets. Several parties had expressed interest and two offers were received for the intellectual property, the machinery and the equipment of the Company. The Company, with the consent of the Bank, is negotiating a transaction with one of the parties, which transaction

will be presented to this Honourable Court for its approval, as soon as negotiations are finalized; and

- The Monitor has filed a Second Supplement to its Third Report, disclosing the fact that Brake Pro is unable to pay about \$460,000 of post filing obligations owed to some 100 different creditors. This has come about due to the fact that an unexpected and rapid increase in the Canadian dollar materially decreased the amount that Brake Pro had contemplated would be available to it under its lending agreements with Wachovia.

Terms of Reference

The information contained in this report has been obtained from the accounting records of Brake Pro and is based on discussions with, and representations made by management, including in particular Mr. Russ Armer, President.

The Monitor assumes no responsibility or liability for any loss or damage occasioned by any party as a result of the circulation, publication, re-production or use of this report. Any use which any party, other than the Court, makes of this report, or any reliance on or decision made based on it, is the responsibility of such party.

Capitalized terms not otherwise defined are as defined in the Initial Order and/or in the Affidavit of Russell Armer, sworn 23 July 2007. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars.

C. BACKGROUND

As previously reported, Brake Pro and the Monitor pursued the marketing timetable established in agreement with Wachovia. A number of interested parties were identified and information was distributed. Four potential purchasers submitted expressions of interest or letters of intent. Two potential bidders conducted substantial due diligence while a third was interested in conducting due diligence but was unable to meet the deadline. Notwithstanding the extensive due diligence conducted, no binding offers were submitted by the September 19, 2007 deadline. As a result, a condition of the Forbearance Agreement was not met.

During the period following the Initial Order, the Company continued to conduct its business, within the parameters of the Forbearance Agreement. During the first number of weeks operating under the CCAA, the Company exceeded forecast with respect to its income and expenses. Unfortunately, starting on or about September 10, 2007 the Canadian dollar appreciated rapidly against the US Dollar. As a result, over a two week period, the borrowing availability from Wachovia was reduced by some \$400,000. The Company was then unable to meet many of its obligations, and was unable to purchase new raw materials.

On September 25, 2007, Wachovia advised that due to Brake Pro's defaults it would no longer support the Company to maintain operations. The Company determined that, in the circumstances, it had no choice but to shut down the plant and lay off all employees.

Many of the Company's suppliers had put the Company on COD, after the commencement of the CCAA proceedings. Others did not, because it was logistically impractical for them to administer COD arrangements, or because they were willing to extend credit in view of the Company's ongoing financial arrangements with the Bank. However, as set out above, the rapid rise of the Canadian Dollar, as against the US Dollar, led to a resultant significant reduction in lending availability which left the Company unable to pay all liabilities incurred since the Initial Order, and unable to continue in business.

The Bank has advised that it wishes the Company to continue to pursue its efforts to self-liquidate through the CCAA process. Notwithstanding the lack of any further borrowing availability, the Bank has agreed to fund certain Company obligations, including employee salaries, wages and expenses up to and including the shut down on September 25, 2007, as well as other ongoing expenses required to be paid by the Company after September 25, 2007, while the Company undertakes a liquidation process. Some of these obligations have already been paid, and others will be funded out of the sales proceeds and liquidation efforts. The Bank has specifically agreed to fund, as part of the expenses going forward, employee wages and vacation pay for all employees retained by the Company to assist with the liquidation, as well as rent and other expenses necessary to maintain the premises during the liquidation process.

However, due to the lack of funds, the Company has been unable to pay various other post-filing liabilities incurred since the Initial Order. As reported in the Monitor's Second Supplement to the Third Report, Appendix I, as at October 16, 2007, the Company has calculated that these liabilities total approximately \$460,000 to some 100 creditors. Attached hereto as Exhibit "A" is a copy of the Monitor's second supplement to its Third report and a letter which the Monitor has sent to all creditors with post filing claims which Brake Pro is not able to pay. This letter was mailed on Monday, October 22, 2007 and the Second Supplement was posted on the BDO website on the same date.

Based on the information available to the Monitor, it appears that there is likely to be a shortfall to the Bank, and accordingly it seems there will be no funds available for the second secured creditor, or for the unsecured creditors.

D. BRAKE PRO'S ACTIVITIES SINCE THE ISSUANCE OF THE THIRD EXTENSION ORDER

With the consent of the Bank, the Company called back a small number of employees on a day-to-day basis in order to maintain the computer and accounting systems, to maintain the security of the plant, negotiate and collect accounts receivables, and organize the inventory and machinery and equipment for a potential sale.

With the assistance of the Monitor and the Bank's consultants, Lissner Associates Limited, The Company has initiated a winding-up process to realize on the assets of the Company for the benefit of its creditors (the "Process"). This Process, which has been reviewed by Wachovia, includes the ongoing collection of Accounts Receivable by the Company and the marketing of the Inventory to customers of the Company on such terms and at such prices as the Company can obtain in the circumstances. In order to permit this Process to proceed, the Company is seeking authorization by the Court to sell the inventory of the Company on such terms and at such prices as it may negotiate, with the consent of the Bank and the Monitor, without specific Court approval for each transaction. The Company is asking that it be permitted to do so

notwithstanding paragraph 18(e)(ii) of the Initial Order, which limits sales outside the normal course to the amount of \$100,000 per transaction, or \$500,000 in the aggregate.

As of October 19, 2007, the Company had collected some \$1,390,000 from the accounts receivable and had sold inventory at market prices to customers. These funds have been paid into the bank account for the Lock Box arrangement maintained in favour of Wachovia as permitted by the provisions of the Initial Order.

By the October 15 Order, Justice Siegel authorized the sale of certain inventory to BRF. Such authorization was required as it exceeded the threshold for such sales outside the normal course of business provided for at paragraph 18(e)(ii) of the Initial Order. All of the inventory sold pursuant to this transaction was located in Ontario. Attached hereto as Exhibit "B" is a copy of the October 15 Order.

A portion of the funds received from the sale of inventory to BRF authorized by the October 15 Order has been segregated by the Company, so as to comply with paragraph 5 of the October 15 Order, which provides that the sale Proceeds shall be held pending a further Order of the Court as to their distribution. A portion of these proceeds were distributed to the Bank inadvertently by transferring it to the Bank after depositing to the Lock Box account. The Company now requests authorization to distribute all of these proceeds of this sale to BRF to Wachovia. A legal opinion as to the validity of Wachovia's security in Quebec and Ontario with respect to the proceeds sought to be distributed is being prepared by Monitor's counsel, and a supplementary report will be filed prior to or at the time of the return of this motion with respect to this opinion.

As well, the Company and the Monitor had been seeking either a going-concern or an en-bloc offer for the assets. The Monitor and the Company worked with several parties with interest in various types of assets. As at the time of preparing this report, two offers have been received for the intellectual property and the machinery and equipment of the Company. Additionally, one offer was received for all assets en bloc, but that offer was rejected as the price offered was considered to be too low. With the concurrence of the Bank, the Company, with the assistance of the Monitor, is finalizing a transaction with one of the other two parties, subject to Court

approval. It is anticipated that an order requesting approval of this transaction will be sought as soon as the transaction has been finalized, which is expected to occur very shortly.

E. SALE TO BRF PRECISION INC.

Subsequent to the granting of the October 15 Order, the Company negotiated the sale of a substantial quantity of additional inventory to BRF. BRF has offered to purchase finished goods inventory on the same basis as described in the Monitor's (first) Supplement to the Third Report. The inventory in question has a list price of \$194,892.92 and was discounted by 13% for a sale price of \$169,556.84, plus applicable taxes, for a total of \$179,730.25.. Attached hereto as Exhibit "C" is a copy of BRF's Purchase Order

As part of its winding-up Process, as described above, the Company has been circulating lists of its inventory to customers to solicit offers. BRF responded and is eager to close the transaction as early as possible. As this sale to BRF exceeds the threshold contained at paragraph 18(e)(ii) of the Initial Order for sales outside of the ordinary course of business, it is necessary to seek Court approval for this sale.

The Monitor recommends that this Honourable Court approve this sale of inventory. This sale is on the same basis as the first BRF sale approved by the October 15 Order, which is very close to list price and approximately 20% greater than book value. Further, this inventory is held by BRF on consignment at its warehouse premises in Quebec. In the absence of this sale, the Company would have to have this inventory shipped back to its premises, incurring costs without an assurance of being able to sell this inventory elsewhere at prices as attractive as those offered by BRF.

The Monitor is aware that Wachovia sought three liquidation proposals. The BRF offer is greater than the independent liquidation values obtained.

In addition to approving the sale of this further inventory to BRF, the Company is seeking an Order approving the distribution to Wachovia of the proceeds of this sale. As stated above, on

the hearing of this motion on Thursday, a supplementary report will be made available to the Court as to the security of Wachovia.

F. EXTENSION OF THE STAY PERIOD

An extension of the Stay Period to November 8, 2007 will allow the Applicant time to finalize a sale of the machinery and equipment and intellectual property, to finalize arrangements for a realization process, to continue the collection of accounts receivable and the sale of inventory to customers at the best possible prices under the circumstances.

G. RECOMMENDATION

The Monitor reviewed a draft copy of this Report with Brake Pro's management who concurred with the factual content of same.

The Monitor is of the view that Brake Pro is and has been acting in good faith and with due diligence. While the failure to be able to discharge post filing obligations is of concern, it appears that this has occurred unintentionally and is due to unexpected circumstances. Of note is the fact that the amount in issue is almost exactly the same as the reduction in credit availability that occurred due to the currency adjustment. Based on the information currently available, the Monitor believes that creditors would not be materially prejudiced by an extension of the Stay Period and recommends that this Honourable Court approve an extension of the Initial Stay of Proceedings until November 8, 2007.

The Monitor therefore makes this Report in support of an Order:

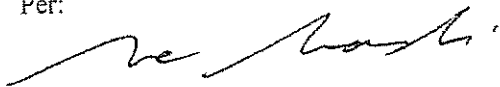
- (a) Extending the stay period to November 8, 2007;
- (b) Approving the sale of finished goods inventory to BRF;
- (c) Amending paragraph 18(e)(ii) of the Initial Order to permit the sale of inventory at such prices and on such terms as the Company may negotiate and the Bank and the Monitor may agree, without further Order of the Court; and
- (d) Authorizing the distribution to the Bank of the proceeds of the sale of inventory to BRF.

All of which is respectfully submitted this 23rd day of October, 2007.

BDO DUNWOODY LIMITED

Monitor

Per:

A handwritten signature in black ink, appearing to read "Uwe Manski". The signature is fluid and cursive, with a long horizontal stroke at the beginning and a small flourish at the end.

Uwe Manski, FCA, FCIRP
President

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BRAKE PRO, LTD.

Court File No. 07-CL-7106

Applicant

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SUPERIOR COURT OF JUSTICE
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Proceeding commenced at Toronto

MONITOR'S FOURTH REPORT TO COURT

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