

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

**IN THE MATTER OF THE PROPOSAL OF
CLOTHING FOR MODERN TIMES LTD.
A COMPANY DULY INCORPORATED IN THE PROVINCE OF ONTARIO WITH A
HEAD OFFICE IN THE CITY OF TORONTO
IN THE PROVINCE OF ONTARIO**

FIFTH REPORT OF THE PROPOSAL TRUSTEE

NOVEMBER 2, 2011

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INTRODUCTION

1. On June 27, 2011, Clothing for Modern Times Ltd. (“**CMT**” or the “**Company**”) filed a Notice of Intention to Make a Proposal (“**NOI**”) under Section 50.4 of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, as amended (the “**BIA**”). A. Farber & Partners Inc. (“**Farber**”) was appointed as Trustee in the Proposal of the Company (the “**Proposal Trustee**”). A copy of the Certificate of Filing a Notice of Intention to Make a Proposal is attached hereto as **Appendix “A”**.
2. CMT is an Ontario-incorporated company that designs, produces and markets trendy apparel styles under the retail businesses: Urban Behavior (“**UB**”), Costa Blanca (“**CB**”) and Costa Blanca X (“**CBX**”), with a head office premises located at 300 Supertest Road, Toronto.
3. At the time of filing the NOI, the Company employed 1,682 employees, of which approximately 1,316 are hourly retail employees.
4. CMT has experienced declining sales and reduced profit margins over the past three years attributed mainly to the poor economic climate for retail operations and the entry of direct competitors in the Canadian marketplace.
5. On June 24, 2011, the Company’s primary secured lender, Roynat Asset Finance, a Division of Roynat Inc. (“**Roynat**”) demanded repayment of its loans and issued a Notice of Intention to Enforce Security under Section 244 of the BIA. CMT consented to the immediate enforcement of Roynat’s security.

6. Roynat, CMT and other related entities to CMT, as guarantors, entered into a forbearance agreement dated June 24, 2011 (the “**Forbearance Agreement**”), whereby Roynat agreed to forbear from taking certain actions under its security and agreed to maintain its credit facilities pursuant to the Roynat Loan (as defined below), subject to the terms and conditions contained in the Forbearance Agreement. Roynat has extended the Forbearance Agreement on numerous occasions with the current extension terminating on November 5, 2011.

7. Pursuant to Orders of the Honourable Madame Justice Hoy dated July 11 and 22, 2011 (the “**July Orders**”), the Court approved, *inter alia*, (i) the post-filing advances and Over-Advances to the Company by Roynat, (ii) a super-priority charge in favour of Roynat to secure payment of the money advances by Roynat post-filing, (iii) an Administration Charge to secure the reasonable fees and disbursements of CMT’s legal and financial advisors, the Proposal Trustee and its legal counsel; (iv) a process for the removal of fixtures, (v) a process for the marketing and sale of the UB and CBX businesses; (vi) a charge in favour of certain of CMT’s real property landlords, and (vii) two extensions of time for CMT to file a proposal to its creditors, the last extension expiring on September 12, 2011. Copies of the July Orders are attached hereto as **Appendix “B”**.

8. On September 12, 2011, CMT sought and obtained an eleven-day extension of time to September 23, 2011 to file a proposal in order to review the offers received and continue negotiations with a prospective purchaser.

9. On September 23, 2011 (the “**September Order**”), CMT sought and was granted an extension of time to file a proposal for 45 days until November 7, 2011. In addition, pursuant to the July Orders and September Order, the Court approved a self-liquidation plan by CMT of a total of 41 stores (the “**Liquidation Stores**”) identified for closure and a key employee retention and incentive plan (“**KERP**”) for certain key employees employed in the Liquidation Stores. A copy of the September Order is attached hereto as **Appendix “C**”.
10. The Proposal Trustee has reviewed the sworn affidavit of Chris Johnson dated November 1, 2011 (the “**Johnson Affidavit**”), in support of the Company’s motion.

PURPOSE OF THIS REPORT

11. The purpose of this Fifth Report of the Proposal Trustee (“**Fifth Report**”) is to:
- a) support the Company’s request to seek approval of the Asset Purchase Agreement (the “**Sale Agreement**”) between 7951388 Canada Inc. (“**795**”) and CMT for the going concern sale of the UB business and assets, including the leases of 12 UB locations;
 - b) support the Company’s request to vest title to the purchased assets described in the Sale Agreement in and to 795 free and clear of all claims and encumbrances;
 - c) support the Company’s request to seek approval of the Asset Purchase Agreement (the “**Midtown Agreement**”) between Boathouse West Inc. and CMT for the sale of the lease, leasehold interests and fixtures of the

UB store located at Midtown Plaza, in the City of Saskatoon, Saskatchewan (the “**Midtown Store**”)

- d) advise the Court and comment on the Company’s request for approval to self-liquidate inventory and fixtures at twenty-five additional stores (the “**Additional Stores**”);
- e) support the Company’s request to seek approval to extend the KERP to the Key Store Employees (as defined in the First Report) employed at the Additional Stores; and
- f) recommend that the Company be granted a 45-day extension to December 22, 2011 for the filing of its Proposal pursuant to the BIA.

DISCLAIMER

12. Farber has relied upon the financial records and financial statements of CMT, as well as other information supplied by management, accountants, auditors and financial advisors to CMT. Our procedures and enquiries did not constitute any audit or review engagement. Farber assumes no responsibility or liability for loss or damage occasioned by any party as a result of the circulation, publication, re-production or use of this Fifth Report. Any use which any party, other than Court, makes of this Fifth Report or any reliance on or a decision made based upon it is the responsibility of such party.

THE SALES PROCESS AND SALE AGREEMENT

13. Pursuant to the Johnson Affidavit, the Company, with the assistance of RSM Richter Inc. (“**Richter**”), has been extensively negotiating with the prospective purchaser, 795, an entity incorporated for the purpose of this transaction by YM Inc. (“**YM**”), for the sale of the UB business and assets.
14. The Proposal Trustee has been kept updated on the progress of the negotiations with YM and has offered its assistance where it has been requested by the Company.
15. The Company has completed its negotiations with YM and has entered into the Sale Agreement, subject to approval of this Honourable Court, for the going concern sale of the UB business and assets.
16. Details of the Sale Agreement are summarized in the Johnson Affidavit. The Company is requesting an order sealing the Sale Agreement until completion of the transaction, which is contemplated to be January 16, 2012 (the “**Closing Date**”), as it contains commercially sensitive information that would be prejudicial to the Company and its stakeholders, should it be disclosed at this time. The Proposal Trustee concurs with the Company’s request for an order sealing the Sale Agreement.
17. The Proposal Trustee has reviewed and agrees with the Company’s reasons for the Court to approve the Sales Process as detailed in paragraph 19 of the Johnson Affidavit.

SELF-LIQUIDATION OF ADDITIONAL STORES

18. The Company, as part of the restructuring plan, has determined that it is in the best interests of the stakeholders to liquidate underperforming stores. In furtherance of this plan, the Company has identified the Additional Stores that it intends to liquidate. The Company has advised the Proposal Trustee that it intends to send Notice of Lease Disclaimers for the Additional Stores in accordance with section 65.2 of the BIA.
19. The Additional Stores include a number of UB stores that do not form part of the Sale Agreement. The Company expects to complete its inventory liquidation at these stores by the Closing Date. A complete listing of the Additional Stores is detailed in the Johnson Affidavit.
20. The Company intends to liquidate and remove the fixtures in the Additional Stores in accordance with the guidelines approved in the Order of the Honourable Court dated July 22, 2011. In addition, the Company seeks approval to extend the KERP to the key employees of the Additional Stores.

MIDTOWN AGREEMENT

21. The Johnson Affidavit provides a summary of the Midtown Agreement, which is conditional on landlord's consent of an assignment of the lease and an order of this Honourable Court vesting title to the purchased assets free and clear of all claims and encumbrances.
22. While the Midtown Agreement is in the process of being finalized by the parties, the Company has advised the Proposal Trustee that this store location does not form part of the Sale Agreement with 795 and the purchase price offered far exceeds any value

that may be derived if the location was disclaimed in the same manner as the Additional Stores. The Proposal Trustee agrees with the Company's observations.

STAY OF PROCEEDINGS

23. The current extension of the stay of proceedings expires on Monday, November 7, 2011.

24. The Company has advised the Proposal Trustee that it expects that the proceeds from the UB business and liquidation of underperforming stores will be sufficient to pay out Roynat, and the second and third ranking secured creditors (as defined in the First Report of the Proposal Trustee) have advised CMT that they are prepared to support a basket proposal to unsecured creditors. The Proposal Trustee concurs with these observations.

25. The Company has substantially completed its restructuring. The Company's request for an extension to commence discussions with its largest unsecured creditors is an essential step in the process of formulating and finalizing a viable proposal. Determining the level of support for a proposal is for all practical purposes a responsible approach to this phase of the Company's restructuring efforts. Without an extension of the stay, however, the Company will be deemed bankrupt to the detriment of its stakeholders, including employees, unsecured creditors and landlords at the remaining CB locations.

26. The Proposal Trustee is satisfied that the Company has acted and is acting in good faith and with due diligence in the proceeding to date and, if the extension being

sought is granted, will allow the Company time to commence discussions with its largest unsecured creditors with a view to determining creditor support for a proposal.

27. The Proposal Trustee is not aware of any creditor who would be materially prejudiced if the extension of the NOI stay period being requested by the Company to December 22, 2011 is granted.

28. The Company has provided the Proposal Trustee with updated cash flow projections for the period ending January 21, 2012. The Company intends to file these cash flow projections with the Court (on a confidential basis to preserve the purchase price under the Sale Agreement) in support of its request for an extension of the time for filing a Proposal. The Proposal Trustee has reviewed the cash flow projections and is satisfied that the Company will continue to operate within the net cash flow projections during this period.

29. At the present time, Roynat is seeking approval from its credit committee to extend the Forbearance Agreement. The Proposal Trustee has not yet been advised of the proposed terms of the Forbearance Agreement but knows of no reason why an extension agreement could not be reached between the Company and Roynat.

RECOMMENDATIONS

30. As a result of the above, the Proposal Trustee respectfully recommends that this Honourable Court:

- a) approve the Sale Agreement between 795 and CMT for the going concern sale of the UB business and assets, including the leases for 12 UB locations;
- b) vest title to the purchased assets described in the Sale Agreement in and to 795 free and clear of all claims and encumbrances;
- c) approve the Midtown Agreement between Boathouse and CMT for the sale of the lease, leasehold interests and fixtures of the UB store located at Midtown Plaza, in the City of Saskatoon , Saskatchewan;
- d) approve the process to self-liquidate inventory and fixtures by the Company at the Additional Stores;
- e) approve the extension of the KERP to the Key Store Employees employed at the Additional Stores; and
- f) grant the Company a 45-day extension of time for the filing of its Proposal pursuant to the BIA until December 22, 2011.

All of which is respectfully submitted this 2nd day of November 2011.

**A. FARBER & PARTNERS INC.
IN ITS CAPACITY AS TRUSTEE *IN RE*
THE PROPOSAL OF CLOTHING FOR MODERN TIMES LTD.**

A. Farber & Partners Inc.
