

No. S117081
Vancouver Registry

IN THE SUPREME COURT OF BRITISH COLUMBIA
IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985,
c. C-36, AS AMENDED

AND

IN THE MATTER OF THE *CANADA BUSINESS CORPORATIONS ACT*,
R.S.C. 1985, c. C-44

AND

IN THE MATTER OF STERLING SHOES INC. and STERLING SHOES GP INC.

NINTH REPORT OF THE MONITOR
ALVAREZ & MARSAL CANADA INC.

December 7, 2012

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1.0 INTRODUCTION

- 1.1 Alvarez & Marsal Canada Inc. ("**A&M**" or the "**Monitor**") was appointed as Monitor pursuant to the order (the "**Initial Order**") pronounced by this Honourable Court on October 21, 2011 (the "**Order Date**") on the application of Sterling Shoes Inc. ("**Sterling**") and Sterling Shoes GP Inc. ("**Sterling GP**") (together, the "**Petitioners**") under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "**CCAA**"). The proceedings brought by the Petitioners under the CCAA will be referred to herein as the "**CCAA Proceedings**". The Petitioners and Sterling Shoes Limited Partnership (the "**Partnership**") will be referred to herein as the "**Petitioner Parties**" or the "**Company**".
- 1.2 On April 2, 2012, on the application of the Petitioner Parties, this Honourable Court made an order (the "**Claims Process Order**") approving among other things, a claims process (the "**Claims Process**") for the determination of the nature and quantum of claims against the Petitioner Parties.
- 1.3 On October 11, 2012, this Honourable Court approved an extension of the Stay Period to January 11, 2013.
- 1.4 On December 12, 2012, the Petitioner Parties will bring a notice of application (the "**Notice of Application**") to this Honourable Court seeking an order permitting them to make one or more distributions to the creditors of Sterling GP and the Partnership (the "**Distribution Order**").
- 1.5 In support of the Notice of Application, the Petitioner Parties are relying on the Tenth Affidavit of Mr. Daniel Gumprich (Sterling's Chief Financial Officer), sworn December 4, 2012 (the "**Gumprich #10 Affidavit**").
- 1.6 The Initial Order, together with the Notice of Application, the Gumprich #10 Affidavit and select motion material and other documentation filed in the CCAA, are posted on the Monitor's website at www.alvarezandmarsal.com/sterling.

2.0 PURPOSE OF REPORT

- 2.1 This is the Monitor's ninth report (the "**Ninth Report**") and it has been prepared to provide this Honourable Court and the Company's stakeholders with:
 - a) an update on the Claims Process generally, including an estimate of the potential distributions to creditors and the timing thereof should the Distribution Order sought by the Petitioner Parties be granted;

- b) a review of the Company's cash receipts and disbursements for the period ended December 1, 2012; and
- c) the Monitor's comments and recommendations regarding the application for the Distribution Order and other matters.

3.0 TERMS OF REFERENCE

- 3.1 In preparing this report, A&M has necessarily relied upon unaudited financial and other information supplied, and representations made to us, by certain senior management of the Company ("Management"). Although this information has been subject to review, A&M has not conducted an audit nor otherwise verified the accuracy or completeness of any of the information prepared by Management or otherwise provided by the Petitioner Parties. Accordingly, A&M expresses no opinion and does not provide any other form of assurance on the accuracy of any information contained in this report, or otherwise used to prepare this report.
- 3.2 Unless otherwise stated, all monetary amounts contained in this report are expressed in Canadian dollars.

4.0 UPDATE ON THE CLAIMS PROCESS

- 4.1 On April 2, 2012, this Honourable Court granted the Claims Process Order, the key elements of which, along with details of the Claims Process, are described in the Fourth and Seventh Reports of the Monitor dated March 29, 2012 and June 12, 2012, respectively, and are not repeated herein.

Summary of Creditor Claims Filed to Date

- 4.2 A summary of creditor claims filed as at December 5, 2012 is set forth in the following table. All claims received to date are reflected in the table below.

Sterling Shoes Limited Partnership and Sterling Shoes GP Inc. Summary of Creditor Claims As at December 5, 2012 (\$000's)							
Nature of Claim	Number of Claims Received	Allowed Claims	Amount of Allowed Claims (\$000's)	Number of Notices of Dispute Unresolved	Amount of Notices of Dispute (\$000's)	Total Number of Claims	Gross Amount of Claims (\$000's)
Pre-filing Claims	412	407	\$14,514	1	\$18	408	\$14,532
Restructuring Claims:							
Employee Claims	163	158	2,112	4	357	162	2,469
Landlord Claims	68	22	1,098	38	14,698	60	15,796
Director and Officer Claims	-	-	-	-	-	-	-
Total	643	587	\$17,724	43	\$15,073	630	\$32,797

Pre-Filing Claims and Employee Restructuring Claims

- 4.3 Since the date of the Monitor's Eighth Report, six additional Pre-Filing Claims have been allowed by the Company totalling \$124,000. In addition, four previously disputed claims have been resolved and allowed in the aggregate amount of \$179,000.
- 4.4 To date, 163 Restructuring Claims (as defined in the Claims Process Order) have been filed by former employees, including two by senior executives of the Company.

Landlord Restructuring Claims

- 4.5 68 Landlords whose leases were terminated by the Company as part of the restructuring process filed Restructuring Claims. 46 of those claims were disallowed or revised, in response to which 38 Notices of Dispute ("**NOD**") were filed. All 38 claims in respect of which NOD's were filed (the "**Disputed Landlord Claims**") remain in dispute.
- 4.6 As noted in the Monitor's Eighth Report, the Company made offers to all landlords having Disputed Landlord Claims in order to resolve those claims. Seven of the landlords accepted that offer. With a view to assisting the Company in resolving the remaining Disputed Landlord Claims, on or about October 10, 2012, the Monitor delivered a letter to each of the remaining landlords (the "**Remaining Landlords**") seeking certain additional information, including:
 - a) particulars of any new leases entered into (either on a temporary or permanent basis), including the term, the base rent and the additional rent; and
 - b) details of efforts to re-let the premises and an estimate of the time required to secure a long-term tenant.
- 4.7 The response from the Remaining Landlords to this letter was, for the most part, comprehensive. Following its initial review of the information provided, the Monitor had a number of additional questions to which it sought answers directly from the Remaining Landlords. As a result of the foregoing efforts, significant progress has been made in assessing the Disputed Landlord Claims.
- 4.8 After discussions between the Company and the Monitor and consideration of the additional information provided by the Remaining Landlords, it is expected that the Company will make a revised offer to the Remaining Landlords in order to resolve their claims. The Company expects to resolve a number of the remaining Disputed Landlord Claims in the near future, in which case those Remaining Landlords could be included in the first distribution to creditors, which is expected to be made in or about late January.

Director and Officer Claims

- 4.9 To date, no claims have been filed against any Directors or Officers of the Petitioners.

5.0 UPDATED CCAA CASH FLOW STATEMENT AND VARIANCE ANALYSIS

- 5.1 The Company previously filed with this Honourable Court a weekly cash flow forecast for the period ending January 12, 2013 (the “**January 2013 Cash Flow Statement**”), which has been reviewed by the Monitor.
- 5.2 As part of the Monitor’s ongoing oversight and monitoring of the business and financial affairs of the Company, the Monitor has undertaken regular reviews of the Company’s actual cash flow in comparison to that forecast by Management.
- 5.3 The Company’s actual cash receipts and disbursements for the 59 week period from October 16, 2011 to December 1, 2012 as compared to the January 2013 Cash Flow Statement are set out as an Appendix “A”.
- 5.4 In summary, the Company has experienced a net favourable cash flow variance of \$77,000 for the 9 week period since the last forecast was updated by Management. The key components of the net favourable variance relate primarily to unexpected receipts, including unexpired insurance premiums, and a favourable variance in respect of professional fees.
- 5.5 As at December 1, 2012, the Company had a closing cash balance of \$14.1 million, all of which is held in its accounts, except for \$500,000 which is held by the Monitor as security for the Administrative Charge. Other monies previously held in trust by the Monitor totalling \$3.0 million were released to Town Shoes Limited (“**Town**”) as part of the settlement of the final working capital adjustments pursuant to the terms of the sales transaction between Sterling and Town.
- 5.6 The Company is current in its payment of wage obligations and also with the CRA and given the funds on hand this is not expected to change prior to any distribution to creditors.

6.0 APPLICATION FOR A DISTRIBUTION ORDER

- 6.1 The Company is applying to this Honourable Court for the Distribution Order, which would authorize it to make one or more distributions to creditors having Allowed Claims (as defined in the Claims Process Order) against Sterling GP or the Partnership.
- 6.2 The Company does not intend to make any interim or final distributions to the creditors of Sterling (for greater clarity, and as defined at section 1.1, Sterling refers to Sterling Shoes Inc.),

which are primarily the holders of \$25.8 million in convertible debentures and accrued interest, as Sterling has no assets of value (as noted in the Monitor's Eighth Report) and, accordingly, no funds are available for distribution. Similarly, there will be no distribution to the shareholders of Sterling.

- 6.3 If the Distribution Order is granted, and barring any unforeseen issues, the Company plans to make an interim distribution to the holders of Allowed Claims against Sterling GP or the Partnership in or about late January 2013.
- 6.4 The Company does not propose to make any interim distributions to holders of disputed claims, being the Remaining Landlords and a small number of employees. The Company will withhold from any distributions sufficient funds to make pro rata distributions to holders of disputed claims against Sterling GP or the Partnership based on (i) the amounts of such claims as set forth in the applicable Proof of Claim or Landlord Proof of Claim (as those terms are defined in the Claims Process Order), and (ii) the total amount available for distribution to all creditors of Sterling GP and the Partnership.
- 6.5 Should any of the outstanding disputed claims be resolved, the holders of such claims will then be included in any future distributions.
- 6.6 The Company will also withhold from any interim distributions sufficient funds to cover the anticipated administration costs to the completion of the CCAA Proceedings.
- 6.7 The Monitor is of the view that it is in the interests of all creditors of the Company to make an initial distribution as soon as possible, and, if appropriate, further interim distributions, rather than wait until a later date when all outstanding disputed claims have been settled. Given the intention to hold back funds as described above, the Monitor sees no prejudice to any stakeholder in making distributions in accordance with the terms of the proposed Distribution Order.

Potential Distributions to Unsecured Creditors

- 6.8 The Monitor has performed an analysis to determine the range of potential recoveries by creditors of Sterling GP and the Partnership. It is estimated that as at January 12, 2013, the Company will have cash on hand in the amount of approximately \$13.75 million (refer to section 9.1 and Appendix "A" of the Monitor's Eighth Report). Again, this is an estimate only, and the amount may change.

- 6.9 As summarized in the table below, depending on the aggregate amount of the outstanding disputed claims (once resolved), the Monitor's calculations indicate a potential distribution to creditors in the range of 40% to 62% of their claim.

Sterling Shoes Limited Partnership Estimated Potential Recoveries to Creditors (\$000's)		
	High \$	Low \$
Total Estimated Proceeds Available for Distribution as at January 12, 2013	<u>13,750</u>	<u>13,250</u>
Total Estimated Claims:		
Pre-filing claims	14,500	14,500
Restructuring claims		
Landlords	5,200	15,800
Employees	<u>2,400</u>	<u>2,500</u>
Total Estimated Claims	<u>22,100</u>	<u>32,800</u>
Estimated Potential Recovery Percentage	<u>62%</u>	<u>40%</u>

- 6.10 The total estimated claims used in the low case above are based on the total amount of Allowed Claims and total amount of outstanding disputed Claims as set out in the summary of creditor claims in section 4.2. Any change in the status of any claim may have an impact on the potential distribution to creditors.
- 6.11 Based on the total amount of the outstanding disputed claims, the Monitor is of the view that any distribution made in or about late January 2013 should be no more than \$5.0 million (or approximately 25% of the total Allowed Claims). This will ensure a sufficient holdback of funds to make distributions in respect of the disputed claims as well as to fund administration costs. If a sufficient number of the outstanding disputed claims are resolved before the first distribution, it is possible that the total amount of that distribution would increase.

7.0 **OTHER MATTERS**

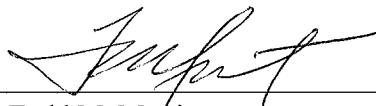
- 7.1 The CFO and the Board of Directors have remained in place to assist with the Claims Process, facilitate distributions and deal with other issues as they arise. The CFO's current employment contract expires on December 31, 2012. The Monitor is advised that the Company intends to extend that contract through to the expiry of the Stay Period. The Monitor is supportive of such an arrangement.

8.0 **MONITOR'S CONCLUSIONS AND RECOMMENDATION**


- 8.1 It is the Monitor's view that the Company and Management continue to act in good faith and with due diligence in advancing the CCAA Proceedings.
- 8.2 The Monitor respectfully recommends that this Honourable Court grant the Distribution Order as sought.

All of which is respectfully submitted to this Honourable Court this 7th day of December, 2012.

**Alvarez & Marsal Canada Inc.,
in its capacity as Monitor of Sterling Shoes Inc.
and Sterling Shoes GP Inc.**



Per: Todd M. Martin
Senior Vice President



Per: Callum D.M. Beveridge
Senior Director

Sterling Shoes Inc. et al.

Actual Consolidated Cash Flow Compared to the January 2013 Cash Flow Statement (Note 1)

For the 59 Week Period from October 16, 2011 to December 1, 2012

	October 16, 2011 to December 1, 2012 (Cumulative)		
(\$000's)	Actual	Forecast	Variance (Note 4)
Gross sales receipts	\$ 52,866	\$ 52,866	\$ -
Cash received on behalf of liquidators (Note 2)	12,870	12,870	-
Inventory liquidation	12,540	12,540	-
Sale of assets	18,323	18,323	-
Receipts (incl. taxes)	96,599	96,599	-
Disbursements			
Vendors	(19,050)	(19,050)	-
Payroll	(13,229)	(13,244)	15
Rent	(8,952)	(8,920)	(32)
Sales tax	(2,779)	(2,711)	(68)
Deposits	(213)	(213)	-
Pre-filing related payments	(1,113)	(1,113)	-
Other	(5,320)	(5,356)	36
Amounts paid to liquidators	(12,089)	(12,089)	-
	(62,745)	(62,696)	(49)
Cash Flow from Operations	33,854	33,903	(49)
CAPEX	(55)	(55)	-
Professional fees	(4,470)	(4,583)	113
Interest / Forbearance fee	(912)	(925)	13
Term Loan	-	-	-
Net Cash Flow	28,417	28,340	77
Bank Position			
Opening bank exposure (Note 3)	(14,270)	(14,270)	-
Closing Bank Position	14,147	14,070	77
Opening balance	\$ (2,344)	\$ (2,344)	-
(Opened) / Cancelled	(721)	(721)	-
Drawn	3,065	3,065	-
LCs	-	-	-
Total Bank Position	\$ 14,147	\$ 14,070	\$ 77

Notes:

- (1) "January 2013 Cash Flow Statement" as defined in and attached to the Eighth Report of the Monitor dated October 9, 2012.
- (2) Cash received on behalf of liquidators and amounts paid to liquidators relate to receipts at stores being liquidated under agency agreements.
- (3) Adjustments to opening balances previously reported include cancellation of certain outstanding cheques post filing.
- (4) The variance is only calculated for the 9 week period from September 30, 2012 to December 1, 2012 and not the 59 week period from October 16, 2011 to December 1, 2012.