



NO. S-073456
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 *BUSINESS CORPORATIONS ACT*, S.B.C. 2002, c. 57

AND

IN THE MATTER OF

TUAN DEVELOPMENT INC.

THIRD REPORT OF THE MONITOR

MACKAY & COMPANY LTD.

October 09, 2007

INTRODUCTION

1. On May 18th, 2007, upon the ex parte application made by Tuan Development Inc. (the Petitioner or Tuan), Tuan obtained protection from its creditors under the *Companies' Creditors Arrangement Act*, R.S.C. 1985 c. C-36, as amended, (the "CCAA").
2. The CCAA proceeding is governed by orders of this Court dated May 18, 2007 (as amended by order made May 28, 2007) (the "Initial Order"), a further order dated May 31, 2007, and the order dated June 8, 2007 (the "Stay Order"). The Stay Order extended the Stay Period under the Initial Order to October 15, 2007 and authorized Tuan to borrow from Gibraltar Mortgage Ltd. ("Gibraltar") DIP Financing of up to \$13,500,000. Pursuant to the Initial Order, Mackay & Company Ltd. was appointed as the monitor in this CCAA proceeding.
3. The purpose of this third report of the Monitor (the "Third Report") is to, *inter alia*, provide this Honourable Court with an update in respect of the following:
 - The current impasse between Gibraltar and Tuan with respect to funding and the effects on the project of this impasse;
 - Insurance issues relating to the site fire of July 9, 2007;

- Tuan's actual cash flow for the period of August 1, 2007 to September 30, 2007; and,
- A summary of restructuring efforts to date.

TERMS OF REFERENCE

4. In preparing this Third Report, the Monitor has relied upon unaudited financial information prepared by Tuan, Tuan's records and discussions with management of Tuan. An examination of Tuan's financial forecast as outlined in the Canadian Institute of Chartered Accountants ("CICA") Handbook has not been performed. Future orientated financial information relied upon in this report is based on management's assumptions regarding future events and actual results achieved will vary from this information and the variations may be material.

BACKGROUND

5. Detailed information regarding the background of Tuan and its CCAA proceedings is contained in Tuan's Petition to the Court dated May 18, 2007, the Court Orders dated May 18, 2007, May 28, 2007, May 31, 2007, and June 8, 2007 and the First and Second Reports of The Monitor. These documents have been posted by the Monitor on its website at <http://www.mackayco.ca/tuan.html>.

CURRENT IMPASSE BETWEEN GIBRALTAR AND TUAN

6. As stated in the Second Report of the Monitor, Gibraltar's counsel sent a letter dated August 3, 2007 to the Monitor's counsel advising that Gibraltar will not be making any further advances under the DIP Facility except for up to \$20,000 for security to Tuesday August 7th and up to \$40,000 in remuneration owing to Tuan's non-management employees.
7. Since that time, the respective counsel of both Tuan and Gibraltar have exchanged communications outlining the terms under which each party would like to continue the completion of Tuan's main project, but no agreement has been reached. It is the Monitor's understanding that the impasse relates to each party having incongruent demands regarding decision making authority. Gibraltar desires the appointment of a Chief Restructuring Officer ("CRO") with decision making authority, and Tuan desires that the restructuring be completed by a committee that is comprised of representatives of Tuan and Gibraltar, and the appointed CRO, with such committee having the decision making authority. A Court application had been set for October 11, 2007 to appoint a CRO and to in effect resolve this issue, but we understand that that application will not be proceeding.
8. Since the letter of August 3, 2007, Gibraltar has advanced further funds up to September 30, 2007 in the amount of \$222,337.19 as protective disbursements. The procedure surrounding these payments has involved Tuan submitting draw requests to the Monitor, with the Monitor in turn passing these requests to Gibraltar along with

comments. Gibraltar then decided which amounts it would advance as protective disbursements, these amounts were then advanced to the Monitor who in turn issued cheques directly to the payees. These procedures were required by Gibraltar and were a condition of the funding.

9. The advances described above fall into the following general categories: Tuan non-management employee payroll, Tuan management payroll (with the exception of Brian Hauff), tradespersons working on a contractual basis, utilities, site security, worker's compensation, rubbish removal, and professional fees.
10. The construction of the cottage units has not been completed due to insufficient funds. We have made visits to the site approximately twice per month. During our visits, we have noted that the tradespersons have not been fully utilized due to lack of supplies. However, we also noted that Tuan's management has attempted to keep the remaining site staff as busy as possible under the circumstances by completing exterior site work where possible. We also note that most additional work will require funding and that the on site crew can not be fully productive until this funding occurs.

INSURANCE ISSUES

11. On or about July 9, 2007, the lodge and pool and fitness centre at the Tuan project were completely destroyed by fire. In the First Report, the Monitor recommended that Tuan be given time to explore its insurance options to determine what relief is available while it continues to complete the cottage units and move towards sale of same. Since this time, the insurance issues have not been resolved.
12. On August 9, 2007, Tuan received a letter from the insurance adjuster, SCM Adjusters Ltd. The letter included text stating

“...there may be grounds to void the Policy on deny liability or coverage under the Policy for any claims, losses or damages advanced by you...”

This letter is attached as Schedule 1 to this Report.

13. On September 4, 2007, Tuan emailed a letter to the insurance adjusters expressing concern with the safety and environmental condition of the lodge and pool fire site.
14. On September 6, 2007, the Monitor attended a meeting concerning the insurance. The meeting was held at the insurance adjuster's office and was attended by Brian Hauff of Tuan, the insurance adjuster, the insurance broker who sold the policy to Tuan, Gibraltar's insurance adviser, and legal counsel representing Gibraltar, Tuan, and the insurer Lloyds of London. The meeting covered many topics including the insurance claim. The meeting was held on a “without prejudice” basis.

15. There is currently no reliable estimate of the amount of the loss. The Monitor understands that Tuan is in the process of drafting a proof of loss on the basis that the lodge and pool will be replaced, and Tuan has advised that it is presently gathering cost estimates to rebuild the facilities. Tuan has indicated that the proof of loss must be reviewed by its counsel before it is released to the Monitor, and has also indicated that it will not file the proof of loss until the Monitor has reviewed it.

16. Tuan has informed the Monitor that:

- a) it has received permission from the insurance adjuster to clean up the site subject to the provision of three cost quotes. The Monitor understands that Tuan has not yet obtained the requested number of quotes. The Monitor also understands that Tuan does not have any funds available to pay for this cleanup;
- b) the insurance adjuster has requested various reports from engineers, architects, and other professionals affiliated with the construction of the lodge and pool, to be used to assist in making a decision on whether to honour the policy. The Monitor understands that Tuan does not have the funds to pay for these reports.

17. It is the opinion of the Monitor that without additional funding, any resolution of the insurance issues will be prolonged.

18. As to the availability of insurance proceeds, the Monitor stated in its Second Monitor's Report that it had no reason to believe the loss due to the fire on July 9, 2007 would not be covered by insurance. This was prior to the insurance adjuster's letter of August 9, 2007 and the meeting of September 6, 2007. The issue of the insurance coverage for the July 9, 2007 fire is unresolved and the site has not been cleaned up.

CASHFLOW MONITORING

19. The Monitor has been reviewing all transactions through Tuan's three bank accounts and Gulf Islands Conference Center Ltd.'s ("GICC") (a related management company whose activities were funded by Tuan) account subsequent to May 18, 2007 and up to September 30, 2007.

20. At July 31, 2007, Tuan had a reconciled balance of \$29,657 in the referenced four bank accounts. In addition, the Monitor held \$37,043 in its trust account with respect to this proceeding. Since that time all new funds from Gibraltar have flowed through the Monitor's trust account for Tuan. As of September 30, 2007:

- a) Tuan / GICC had a reconciled balance of \$10,640 in the four bank accounts; and
- b) the ending balance in the Monitor's trust account was \$42,774. After September 30, 2007, the Monitor disbursed an additional \$40,938 on

October 01, 2007 which left a balance of \$1,836 as of October 01, 2007.

RESTRUCTURING EFFORTS

- **The Plan**

21. Tuan has approached the Monitor in regards to preparing an amended restructuring plan and cash flow to deal with the Material Adverse Change of Monday July 9th, 2007 outlined in the First Report. The Monitor has reviewed a first draft of the cash flow and offered suggestions for inclusion in a final report. Any restructuring plan must include financing. The Monitor is not aware that any source of financing has been obtained to date by Tuan to finance the proposed restructuring.

- **Country Roots**

22. Tuan has not yet come to an arrangement with its major trade supplier Country Roots Furniture who is supplying cabinetry, counter tops and furniture for the fifty cottage units. These materials are required for completion of the cottage units, and they were identified as being a major concern at the beginning of the CCAA process.

23. The Monitor was contacted by the owner of Country Roots during the first week of October 2007. The owner informed the Monitor that Country Roots was insolvent and was considering various options in dealing with its creditors. The owner also informed the Monitor that the balance of the product to be supplied to Tuan was segregated in its warehouse. The Monitor has not verified this information independently. This new information regarding the insolvent state of Country Roots has created an urgency to deal with this situation as losing this furniture in a liquidation would result in substantial additional costs as the majority of the consideration has already been paid to Country Roots and only a fraction of the product has been delivered.

24. Subsequent to receiving this information, Tuan met with the Monitor and worked out a proposal that it wished to propose to Country Roots to obtain the balance of the furniture and cabinetry that was ordered by Tuan, but still remained in the possession of Country Roots due to a payment dispute between Tuan and Country Roots. The proposal was submitted to Gibraltar as it required funding. As of the date of this report, Gibraltar has not unconditionally committed to such funding.

- **Disclosure Statement**

25. Tuan has prepared a draft version of a new Disclosure Statement which would be required to sell the cottages once they are completed. The draft version does address many issues that needed to be addressed. However, the Monitor notes that much of the information required in the Disclosure Statement can not be finalized until the current financing impasse is resolved. In addition, the current draft version of the

Disclosure Statement is missing several schedules but we anticipate these can be prepared within a reasonable time subject to additional funding.

- **Resolution**

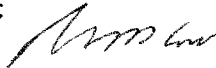
26. Financing is required in order to proceed with Tuan's project. The current impasse means that the project is in substance on hold, and interest costs are continuing to accrue with minimal additional value being added to the project. In addition, the winter season is approaching and preservation/maintenance of the existing cottage units and cleanup of the fire site in the interest of safety and the environment both require funding.

All of which is respectfully submitted this 9th day of October 2007.

MACKAY & COMPANY LTD.

**In its capacity as Court Appointed
Monitor of Tuan Development Inc.**

Per:



Russell Law, CA, CIRP



August 9, 2007

Tuan Development Inc.
The Owners of Strata Plan VIS 4458
Saltspring Island Village Resort
Brian Hauff
Gibraltar Mortgage Ltd.
All Contractors and Subcontractors Associated Directly with the Project
2nd Floor, 1666 West 75th Avenue
Vancouver, BC V6P 6G2

Attention: Brian Hauff

Dear Sirs/Mesdames:

Loss: July 9, 2007
Cover Note: NA072404 and/or BO572NA072404
Our File No.: 53610-9610 SHM

As you know, we are the independent adjusters representing your insurance underwriters, Lloyd's Underwriters (hereinafter referred to as the "Insurer"), with respect to the above-captioned matter.

During the evening of July 9, 2007, at the premises known as the Saltspring Island Village Resort on Saltspring Island, British Columbia, there was a fire loss which destroyed much of the premises and contents and caused a business interruption loss. We understand that you will be presenting a claim to the Insurer and that you are obviously taking the position that the matter is covered by the insurance policy issued by the Insurer (the "Policy").

There is in fact a potential problem with the coverage for this claim. Hence this correspondence.

The Insurer wishes to make it clear that notwithstanding any investigation and fact gathering concerning the loss by the Insurer, there may be grounds to void the Policy or deny liability or coverage under the Policy for any claims, losses or damages advanced by you by reason of:

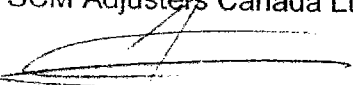
1. The scope of who is an "insured" pursuant to the interim binder or policy.
2. Breaches of the terms and conditions of the Policy, including any Policy condition with respect to the sprinkler system; and/or
3. Some or all of the claims or losses being of a type not falling within the scope of coverage afforded by the Policy; and/or
4. Some or all of the claims or losses falling outside the monetary limits stated in the Policy or to which co-insurance applies; and/or

5. Certain misrepresentations or failure to disclose material information, including representations and information regarding the sprinkler system; and/or
6. Such other grounds as which may presently exist or which may subsequently be discovered and/or which may only come to light as a result of information provided by you.

The Insurer wishes to make it clear that by continuing the investigation and fact gathering into this matter, the Insurer is not in any way representing that it will provide coverage for any claims, losses or damages advanced in this matter. It must be expressly understood that the Insurer is not admitting any obligations under the Policy beyond those expressly contemplated by the Policy, and that the Insurer reserves, and does not waive, the right to deny coverage for any and all of the claims, losses or damages in this matter, to set up any and all defences of non-coverage under the Policy or to challenge the validity of the insurance placement, should it ultimately deem that such positions are appropriate. In addition, it must be expressly understood that the conduct of the investigation, fact gathering or any other action taken or omitted in addressing any claim does not constitute a waiver of any kind. It must also be expressly understood that any information provided to the Insurer may be used by the Insurer to support the voiding of the Policy or a denial of coverage of any claims, losses or damages advanced by you.

You may wish to consult with your own solicitor on coverage in this matter. If you have any questions respecting matters outlined in this letter, we can forward them to the Insurer for comment.

Yours truly,
SCM Adjusters Canada Ltd.



Stuart G. Macdonald
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Executive General Adjuster
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