ALGER & ASSOCIATES INC.
Formerly Collins Barrow Limited

#400, 602 - 11 Avenue SW
Calgary, Alberta T2R 1J8
T 403 298 5800
F 403 296 2988

Information Paper
Bankruptcy and Insolvency Issues Related to the Beef Industry
July, 2004

With the current state of the beef industry in this country, caused predominantly by the discovery of BSE in a Canadian cow in May, 2003, but being exacerbated by ongoing drought conditions in Western Canada, issues related to the bankruptcy and insolvency of the industry's participants are likely going to be on the increase in the near future. As a result, it would be wise for affected parties to be knowledgeable of some of the unique issues related to this industry. The purpose of this paper is to provide readers with an overview of the unique issues related to this industry and in particular those areas that would have an impact on the bankruptcy or insolvency of this industry's participants.

This paper is historical in nature and is intended as a reference material for interested parties. It is not meant to be a substitute for legal advice, which the reader should seek before considering an appropriate course of action. To the extent that the reader has any questions on this paper, please contact either Michael Costello or Sharon Stapley, whose contact details are contained at the conclusion of this paper.

This paper is organized as follows:

I. Overview of the Beef Industry

The beef industry is divided into two main areas, the upstream area, comprising the breeding, raising and feeding of the cattle (commonly referred to as "producers") and the downstream area, comprising the slaughtering of these cattle and the further processing of the carcass beef (commonly referred to as "processors").

The upstream area represents the largest segment in terms of number of participants, with literally thousands of full-time ranchers as well as part-time farmers engaged in the breeding, raising and feeding of the 16 million head of cattle in the country, 6 million of whom reside in Alberta. The downstream area on the other hand is comprised of relatively few players, particularly the meat packing sector, in which 80-90% of the country's production comes from five major meat packing companies (the classic definition of an oligopoly), the two largest being subsidiaries of multi-billion dollar US-owned conglomerates.

a. Upstream Participants ("Producers")

i. Cow-Calf Operators ("Ranchers") – these participants represent the bulk of the industry in terms of numbers, ranging from large ranches with hundred or even thousands of cattle located on thousands of acres of ranchlands to small-scale hobby farmers with just a few head of cattle located on small acreages. The economics of this segment of the cattle industry involve a base herd of breeding cows used for producing calves on an annual basis, with the bulls either owned by the operator or "rented" from others or alternatively artificially inseminated at specialized breeding operations. These calves, referred to in this circumstance as "feeder cattle", unless retained as "replacement" cows or sold for breeding purposes in which case they are referred to as "breeding cattle", thus represent the annual cash crop required to fund these operations, supplemented by the recoveries available from the "culling" of the cows and bulls in the herd.

Culling is the process of disposing of the cattle that the rancher/farmer deems as being unproductive or as too risky of retaining for future breeding purposes. These cattle are sold to slaughter-houses for the making of ground beef and other related products, given that the meat from these animals is not tender enough for prime cuts of beef. The volume of culling can also be influenced by the desire of the rancher/farmer to grow or retract the size and/or quality of their herd and quite often the decision is influenced by economics (i.e. the cost of feed). Similarly, the amount of calves that are sold off annually as a cash crop versus being retained for replacing the cattle culled from the breeding herd is often dictated by the ranchers/farmers desire to grow or retract the size of their herd.

ii. Breeders – these participants are much smaller in number than the cow-calf operators with their focus being upon the provision of Purebred breeds of cattle (e.g. Charolais, Angus, Hereford etc.) for the cow-calf operators to utilize in order to improve the quality of their herd and resulting calves. The economics of this segment involves the sale or rental of the bulls for breeding purposes and/or the sale of the semen to cow-calf operators via an artificial insemination facility, with quality of production being the key to success.

iii. Feedlot Operators – these participants are again, like breeders, much smaller in number than cow-calf operators and range from small feedlots with feeding capacities in the hundreds of head to large feedlots with capacities in the tens of thousands of head. The economics of this industry involve the production of feed components (e.g. barley, hay, silage) from the farm lands associated with these feedlots and the sale of this feed, related products (e.g. medicine and feeding supplements) and yardage (i.e. labour and capital costs) to customers who place their cattle in the feedlot, also known as "custom-feeding". These customers are often cow-calf operators who "background" their cattle at these feedlots for the fall/winter for ultimate return to the ranchers/farmers own grasslands the following spring, but can often be customers who "finish" their cattle there, meaning that they are fed for purposes of reaching slaughter-weight with the ultimate intention of selling the "finished" animal to a meat-packer. The feedlot operator, to the extent that they have the capital, can quite often also be the customer for the "feeder" cattle and thus assume the risk of ownership of these cattle.

iv. Cattle Brokers – these participants, which include auction marts, are fewer still in number and essentially involve fulfilling a middleman role between and amongst the various segments above as well as the meat packing companies who require cattle for their slaughter facilities. These participants generally earn their revenue on a per head transaction basis, but can take ownership of the cattle between the seller and the ultimate buyer in which case the risks of ownership are present.

b. Downstream Participants ("Processors")

i. Meat Packers – these participants are very few in number, but very large in volume, with Canada's two largest being Cargill Foods and Lakeside Packers, both subsidiaries of multi-billion dollar US-owned conglomerates that can each process 4,000 to 6,000 head of cattle per day. Numerous small abattoirs swell the numbers somewhat, but very little of the volumes. These participants can generally be broken down into two segments, both of which are often integrated given the economics associated with the combination of these two separate, but related operations.

1. Slaughterhouses/Abattoirs – this is the segment where the cattle realize that they should have read the fine print on the "free food" contracts they implicitly agreed to at the feedlot. These operations involve the purchase of live cattle, their slaughter and the sale of the primary carcass beef

product, as well as the secondary "credit" products, including hides, offal (i.e. edible internal organs such as hearts, liver, brain, tongue etc.) and rendering (i.e. pretty well everything else).

2. Boxing/Boning Operations – boxing operations process the carcass into whole primal cuts (i.e. loins, ribs, chuck etc.), which are then vacuum packaged and placed into 40-60 pound boxes for sale to butchers, supermarkets and other further processors. Boning operations process the older "culled" cattle carcasses by stripping the bones from these animals and producing the boneless beef product that is then used in the production of ground beef and other products (e.g. sausages etc).

ii. Butchers/Supermarkets/Further Processors

These participants, who are larger in number than the meat packers, take the carcass beef or, more often than not, the boxed and boned beef product and create steaks, roasts and ground beef for the retail and food service markets. Further processors will use these products to create valued-added products for the same markets (e.g. sausages, patties, corned beef, fajita beef etc.).

II. Unique Issues Associated With the Beef Industry

Because much of the Producer area of the beef industry falls within the Bankruptcy and Insolvency Act ("BIA") provisions for farmers, fisherman and aquaculturists, there are various unique treatments for such parties. Firstly, a farmer who conducts their operations personally (as opposed to through a corporation) cannot be petitioned into bankruptcy, they can only voluntarily assign themselves into bankruptcy. Similarly, under section 48 of the BIA a creditor cannot petition for a receiving order against a farmer who conducts their operations personally (as opposed to corporately). Finally, there are various super-priorities under section 81.2 of the BIA that are available to farmers which can severely impact the realization of creditors, these super-priorities relating mainly to unpaid goods provided by these farmers.

In addition to the BIA provisions, there are various additional Acts that can have an impact upon the beef industry, including:

a. Farm Debt Mediation Act – this Act, a copy of which is contained in the annotated copy of the BIA, provides for certain differences in administration for insolvent farmers, including the appointment of an administrator, a stay of proceedings against the farmer's creditors, the appointment of a mediator by the administrator, an extended 15 business day notice period for secured creditors, a guardian for the farmer's assets and the existence of an appeal board to adjudicate cases. The practical effect of this Act is that it provides increased protections for farmers who are legitimately attempting to "save their livelihood", subject to numerous pre-conditions in order for these farmers to be able to enjoy the benefit of these protections.

b. Livery Stable Keepers Act – this Act provides for protection similar to that provided by a mechanic lien for a mechanic in that the stable keeper enjoys a lien over the animals it is feeding and caring on behalf of third parties until these costs are paid for in full. This Act also provides for the right of the stable keeper to recover these costs via a sale of these animals, subject to various pre-conditions. The practical effect of this Act is that creditors who, but for this Act, would be regarded as unsecured creditors by the secured creditors, enjoy in fact super-priority over these secured creditors.

c. Crop Payments Act – this Act deems the lessor, vendor or mortgagee of a property to be the owner of the share from the sowing of the crops on this property until the share of the crops or the proceeds of the sale of the share have been delivered into the possession of the lessor, vendor or mortgagee. The practical effect of this Act is that it provides these latter parties with a priority claim over other parties, such as the lessee, purchaser or mortgagor, subject to a maximum under the Act of a one-third share of the crop.

d. Livestock & Livestock Products Act – this Act, which contains numerous sections, deems under sections 7 and 8 that title to livestock does not pass to a buyer who is a licensed livestock dealer (as defined under this Act, but encompassing most feedlots, cattle brokers and slaughterhouses) until such time as that dealer has made payment for these livestock. The practical effect of these sections of the Act is that cattle in the possession of a licensed livestock dealer may not in fact be legitimately owned by those dealers if payment has not been made for them.

e. Possessory Liens Act – this Act provides for protection similar to that provided to the stable keeper above, but for items being stored and cared for by a bailee. This Act provides the bailee with a lien over the items stored and cared for on behalf of third parties until the costs incurred by the bailee are paid for in full. This Act also provides for the bailee's right to recover these costs via a sale of the items stored and cared for, subject to various pre-conditions. The practical effect of this Act is that creditors who, but for this Act, would be regarded as unsecured creditors by the secured creditors, enjoy in fact super-priority over these secured creditors.

III. <u>Bankruptcy & Insolvency Act (BIA) Issues</u>

Based on the outline in section II of some of the unique issues and Acts involving the beef industry, the following are some of the key items to be aware of when considering the bankruptcy and insolvency issues of each of the industry's participants as outlined previously in section I:

a. Upstream Participants ("Producers")

This area of the industry has been the one suffering the most severe consequences associated with the BSE discovery in May, 2003 as the available supply of cattle after this date greatly exceeded the demand for the product, which slumped dramatically due to the fact that international markets, which comprised approximately 40% of the market for Canadian cattle production, banned the import of Canadian cattle and beef products after this BSE discovery.

With domestic consumption unable to consume the excess and with available slaughter processing capacity in Canada being well behind finished cattle production capability, the price for live cattle has fallen to unprecedented levels over the past year, affecting each of the participants negatively given the domino effect associated with reduced finished cattle prices.

The key bankruptcy and insolvency issues associated with the participants in this area of the beef industry involves the ability of participants to sustain their operations in the face of a reduced price environment, which will require a strong equity position, as well as the ability to avoid selling assets at depressed prices (i.e. the key to making a small fortune in this area of the industry will be to start with a large one at least for the short-term) and if these depressed price sales are necessary, the key will be to ensure eligibility for government support programs, such as the BSE Recovery Program and CAIS/NISA, in order to cushion the effect of these depressed prices.

i. Cow-Calf Operators (Ranchers) – these participants have felt the effect of reduced demand primarily from the price of cull cows and bulls plummeting by over 50% (see "Slaughter Cow & Bull Prices – 2003/04" chart), a logical outcome given that BSE is associated with older "culled" cattle, but also from a reduced demand and therefore reduced prices for calves as pessimism abounds in the feeder cattle industry (see "Feeder Cattle Prices – 2003/04" chart). The ability to avoid selling culled cows and bulls in a depressed market environment is likely going to be a factor to long-term success in this sector of the industry. Those operations with non-cattle related revenue sources (e.g. oil and gas surface leases etc.) are also better equipped to weather the economic downturn.

ii. Breeders – these participants have generally been the least negatively effected of those in the upstream area of the beef industry, but as pessimism for the solution to the BSE crisis increases and correspondingly the willingness and ability of the cow-calf operator to demand and procure the services of these breeders, a negative effect on this industry is being felt by these participants (see "Breeding Cattle Prices – 2003/04" chart).

iii. Feedlot Operators – these participants, particularly those with large ownership positions in the cattle themselves, have been the hardest hit of those in the upstream area of the beef industry as the price of finished cattle has fallen by 20-30% from pre-BSE levels (see "Slaughter Cattle Prices – 2003/04" chart), while the cost of production has stayed constant due to drought conditions. Even those feedlots without large cattle ownership positions have witnessed a large drop in feeding revenue as demand for these services decreases and the ability for customers to pay their bills is impaired in the current negative environment.

iv. Cattle Brokers – these participants have likewise been severely negatively effected as their revenue depends largely on a steady volume of cattle in order to earn commission revenue on and with many of the other sectors of the upstream industry on "hold" and a reduced demand for cattle arising from the loss of US markets for cattle, trading volumes have dropped dramatically. Similarly, for those in an ownership position in the cattle, they have experienced a double-whammy as the value of these cattle has decreased dramatically.

The following is a matrix of the various Acts and whether the various participants would generally expect to benefit from these Acts, would expect to suffer from these Acts, or whether the situation will generally dictate whether they will benefit or suffer from the provisions of these Acts.

LSKA – Livery Stable Keepers Act
CPA - Crop Payments Act
L&LPA – Livestock & Livestock Products Act
PLA - Possessory Liens Act

Participant	**LSKA**	**CPA**	**L&LPA**	**PLA**
Cow-Calf Operator	Suffer	Suffer	Benefit	Both
Breeders	Suffer		Benefit	Benefit
Feedlot – custom only	Benefit	Suffer	Both	Both
Feedlot – cattle-owner	Suffer		Both	Both
Cattle Broker	Suffer		Both	

b. Downstream Participants ("Processors")

In contrast to the upstream area of the beef industry, the downstream area of the beef industry has benefited significantly since the discovery of BSE in May, 2003. The Auditor General of Alberta conducted an investigation into this matter at the request of the Deputy Premier and in his report dated July 27, 2004, which is available at http://www.oag.ab.ca/, he noted that: "*the financial information provided to me shows clearly that the integrated meat packing operations of the three major Alberta-based packers have performed substantially better following the introduction of the Canada Alberta BSE Recovery Program on June 18, 2003, than in the preceding three years*." The report includes a table containing these combined normalized financial results, which illustrates that the above-noted packers have experienced a 281% increase in their combined net earnings before corporate interest and taxes.

In terms of the bankruptcy and insolvency and related Acts issues associated with this area of the beef industry, only the Livestock and Livestock Products Acts is applicable and the effect of this can only be negative if meat-packers have not paid for the finished cattle as the proceeds from the sale of these animals will be subject to a claim by unpaid parties under this Act.

IV. Alger & Associates Inc. experience in the Beef Industry

The firm has expertise in the beef industry, primarily from two individuals:

- Michael Costello, one of our Calgary-based Associates, has in-depth experience in a Vice-President and Chief Financial Officer capacity, including a Chief Restructuring Officer role, with a large publicly traded agri-business company with ranching, feeding and meat packing operations during the 1990's, as well being the firm's lead representative in its current role as trustee for a bankrupt cattle brokerage company.

- Sharon Stapley, our Red Deer based trustee, has been personally involved in the agricultural industry through her experiences raising crops and livestock. Utilizing her insolvency and CCRA knowledge, as well as her hands-on experience and personal contacts, Sharon has made numerous presentations to lenders, lawyers and others regarding bankruptcy and insolvency considerations in the agricultural area.

In addition, the other members of our Corporate team have done numerous receiverships and bankruptcies within the agricultural industry during their professional tenures. The contact details for the members of our Corporate team are:

Bruce Alger, CA•CIRP
P. 403.296.2970
F. 403.296.2988
C. 403.818.0006
E. balger@alger.ca

Barry Hunt, CA
P. 403.296.3082
F. 403.296.2988
C. 403.818.1203
E. bhunt@alger.ca

Colin Christie, CA, CFA
P. 403.296.2974
F. 403.296.2988
C. 403.863.9511
E. cchristie@alger.ca

Guy Odhams, CA•CIRP
P. 403.296.3143
F. 403.296.2988
C. 403.860.8073
E. godhams@alger.ca

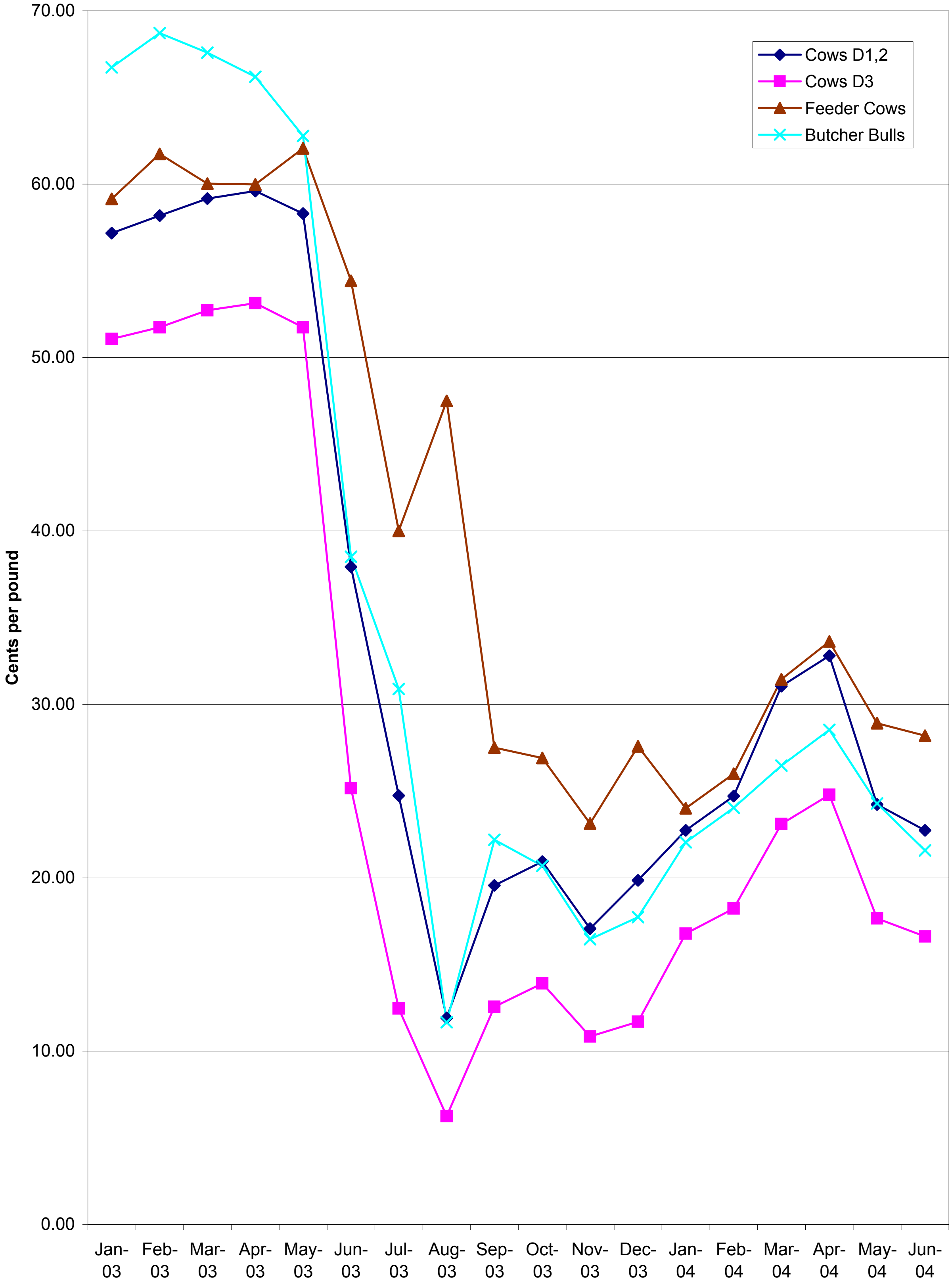
Michael Costello, CA•CBV
P. 403.296.3087
F. 403.296.2988
C. 403.519.0753
E. mcostello@alger.ca

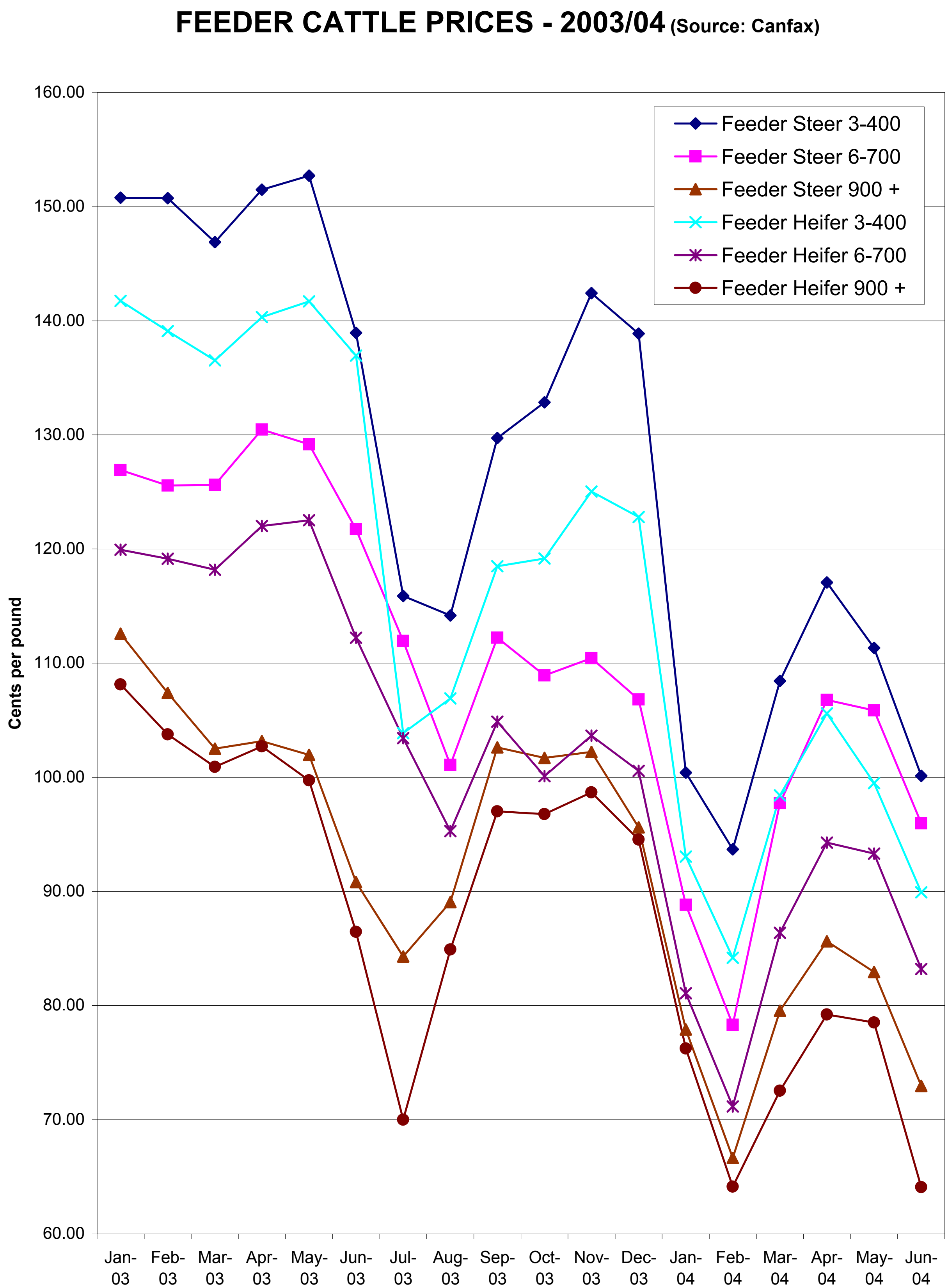
Sharon Stapley, CIRP
P. 403.350.2265
F. 403.346.6120
C. 403.830.0440
E. sstapley@alger.ca

Alternatively, the firm's province-wide toll-free number is 310-8888 and its other toll free numbers are Calgary 1-800-661-8284 and Red Deer 1-877-350-2266.

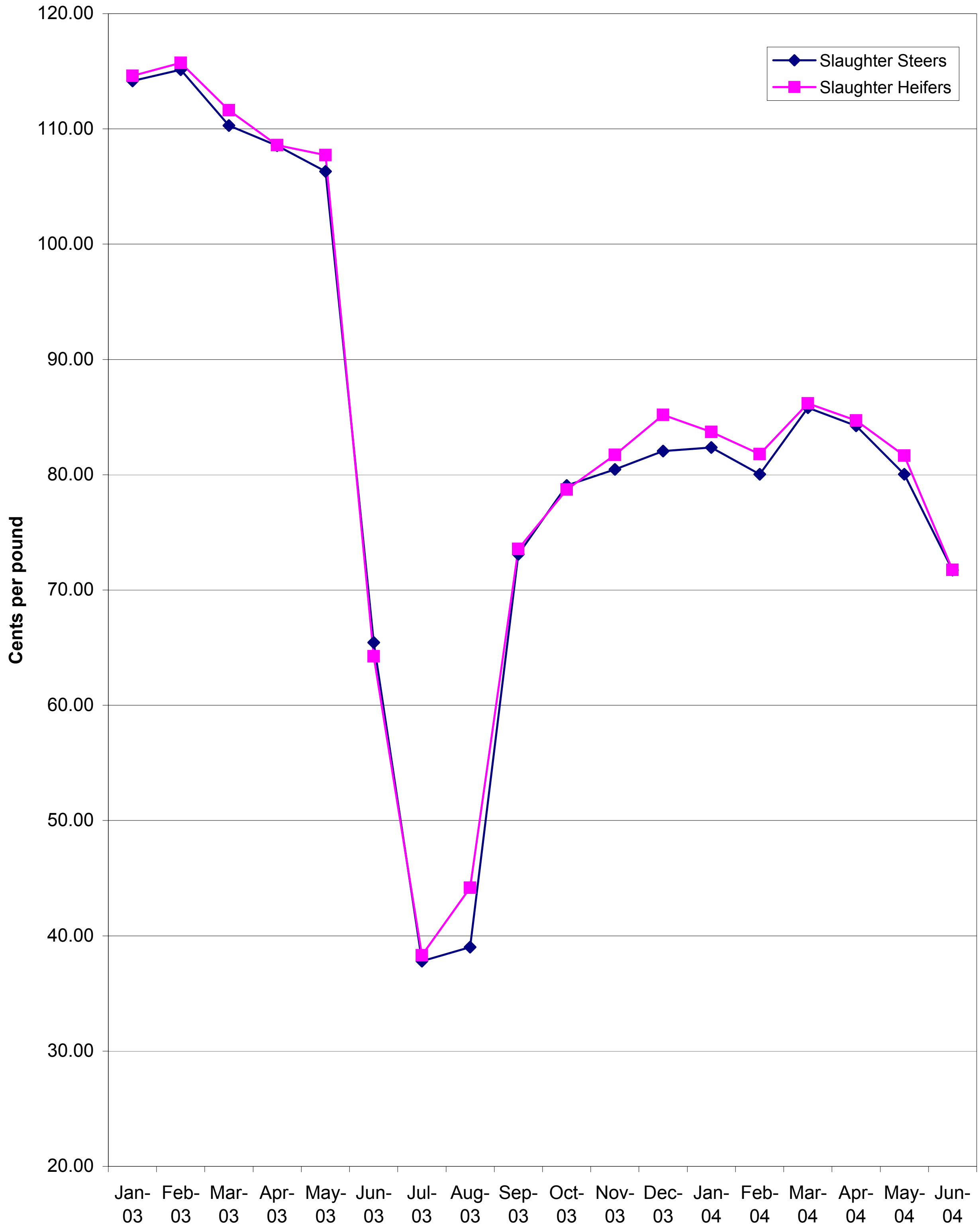
M:\Information Brochures\Information Paper - Beef Industry - July-04.doc

SLAUGHTER COW & BULL PRICES - 2003/04 (Source: Canfax)




FEEDER CATTLE PRICES - 2003/04 (Source: Canfax)
Feeder Steer 3-400
Feeder Steer 6-700
Feeder Steer 900 +
Feeder Heifer 3-400
Feeder Heifer 6-700
Feeder Heifer 900 +
Cents per pound
160.00
150.00
140.00
130.00
120.00
110.00
100.00
90.00
80.00
70.00
60.00
Jan-03
Feb-03
Mar-03
Apr-03
May-03
Jun-03
Jul-03
Aug-03
Sep-03
Oct-03
Nov-03
Dec-03
Jan-04
Feb-04
Mar-04
Apr-04
May-04
Jun-04

SLAUGHTER CATTLE PRICES - 2003/04 (Source: Canfax)



BREEDING CATTLE PRICES - 2003/04 (Source: Canfax)