

**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 PLAN OF COMPROMISE AND
ARRANGEMENT OF SKLAR-PEPPLER FURNITURE CORPORATION**

**APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT
ACT*, R.S.C. 1985, c. C-36, AS AMENDED**

**SECOND REPORT OF THE MONITOR
DATED OCTOBER 4, 2006**

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APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT*
ACT, R.S.C. 1985, c. C-36, AS AMENDED

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

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ARRANGEMENT OF SKLAR-PEPLER FURNITURE CORPORATION
APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT
ACT*, R.S.C. 1985, c. C-36, AS AMENDED

**SECOND REPORT OF THE MONITOR
DATED OCTOBER 4, 2006**

1. On August 8, 2006, Sklar-Pepler Furniture Corporation (the "Applicant") filed for and obtained protection from its creditors under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "CCAA") pursuant to the Order of this Honourable Court dated August 8, 2006 (the "Initial Order"). Pursuant to the Initial Order, BDO Dunwoody Limited was appointed as the monitor of the Applicant (the "Monitor") in this CCAA proceeding.

Purpose

2. The purpose of this Second Report of the Monitor (the "Second Report") is to advise the Honourable Court with respect to:

- (a) the activities of the Applicant from September 1, 2006, the date of the Monitor's First Report (the "First Report") to the date of the Second Report;
 - (b) the activities of the Monitor from September 1, 2006, the date of the First Report to the date of the Second Report, to request a hearing for the approval of the Monitor's fees and costs and those of its legal counsel, and to request an administrative charge on the assets of the Applicant as security for such fees and costs;
 - (c) the Applicant's cash flows for the period of October 2, 2006 to December 1, 2006; and,
 - (d) the Applicant's request for an extension of the Stay Period to November 30, 2006.
3. Capitalized terms not defined in this Second Report are defined in the Initial Order. All references to dollars are in Canadian currency unless otherwise noted.

Terms of Reference

4. In developing this Second Report, the Monitor has relied upon unaudited Applicant prepared financial information, Applicant records and discussions with management of the Applicant, as represented by Mr.

Robert Tweedy, the Applicant's President and sole director, Mr. Bill Malisch, the acting Chief Operating Officer, and Ms. Karima Alarakhia, the acting Controller. The Monitor has not performed an audit or other verification of such information. An examination of the financial forecast as outlined in the Canadian Institute of Chartered Accountants ("CICA") Handbook has not been performed. Future oriented financial information relied upon in this Second Report is based upon management's assumptions regarding future events, and actual results achieved will vary from this information and the variation may be material.

5. The Monitor assumes no responsibility or liability for loss or damage occasioned by any party as a result of the circulation, publication, reproduction or use of this report and any use which any party, other than a Court, makes of this report or any reliance on or decision taken based upon it, is the responsibility of such party. The Monitor is relying on the accuracy of the representations made to it by the Applicant. The Monitor is further relying on the accuracy of the books, records and reports of the Applicant which have been supplied to the Monitor by the Applicant in these proceedings.

Background

6. The Applicant is a corporation incorporated pursuant the *Business Corporations Act (Ontario)*. It is one of Canada's leading branded suppliers of residential upholstered furniture and occasional tables. The Applicant supplies retailers both in Canada and the United States of America.
7. The Applicant owns 100% of Sklar-Peppler of America Inc. ("SPA"). SPA is a U.S. holding company that owns 100% of the shares of Associated Furniture Manufacturers Inc. ("AFM") in Portland, Oregon. AFM primarily manufactures "Sklar-Peppler" branded products for the Applicant. SPA and AFM are not included in the reorganization under the CCAA and we understand they are to continue to carry on business in the ordinary course.
8. The Applicant's principal lender is National Bank of Canada ("National Bank") which has continued to extend credit facilities to the Applicant during this restructuring. In addition, NatExport/Sodex ("Sodex"), a division of National Bank, has also continued to provide an accounts receivable factoring facility to the Applicant during these CCAA proceedings.

Court Proceedings

9. On September 5, 2006 the Applicant sought and received an Order, which extended the Stay Period under the Initial Order to September 21, 2006.
10. On September 20, 2006, the Applicant attended at 9:30 a.m. before the Court to seek an interim extension of the Stay Period to the next available 10:00 a.m. open Court appointment at which time the Applicant's Motion for a further extension of the stay until November 30, 2006 could be heard on a full record. The Monitor attended Court on September 20, 2006 and consented to the proposed interim extension to October 6, 2006, which was granted by the endorsement of Justice Lederman.

Activities of the Applicant

11. Attached hereto as **Schedule "1"** to this Report is the Applicant's cumulative cash flow (Projected to Actual) for the period from August 7, 2006 to September 22, 2006.
12. For the 7 weeks ended September 22, 2006, the Applicant reports a positive cash flow of approximately \$267,000. However, this positive cash flow includes \$475,000 advanced under the Subdebt loan facility. Accordingly, the Applicant's net cash flow from operations for this period is in fact negative by approximately \$208,000.

13. Although the Applicant's cash receipts have been lower than had been projected, cash disbursements have also been lower despite unanticipated chargebacks by Sodex totaling approximately \$171,000, and the payment of pre-filing vacation pay, Goods and Services Tax ("GST") and Retail Sales Tax reportedly totaling approximately \$33,000.
14. The Monitor has been advised by the Applicant's management that the lower cash disbursements can be attributed to lower inventory purchases than had been projected, and to a deferral of certain payments such as pension benefit contributions and rent at the Ajax facility, which facility is owned by a corporation controlled by Mr. Malisch.
15. On September 27, 2006 Canada Revenue Agency ("CRA") completed an audit of the Applicant's source deductions and determined an indebtedness of approximately \$276,000.
16. The Monitor is advised that the discussions between the Applicant and its trade union with respect to how various outstanding concerns of that trade union will be dealt with in these CCAA proceedings, continue with some progress being made.

Activities of the Monitor

17. Pursuant to the Initial Order, the Monitor's responsibilities were essentially restricted to those set out in section 11.7 of the CCAA. Accordingly, the Monitor has had limited involvement with the Applicant or with respect to overseeing the business and affairs of the Applicant.
18. As previously reported, the Monitor continues to relay all requests it receives for information from creditors to the Applicant's counsel. The Monitor understands that these requests are being met by the Applicant.
19. The Monitor has not received any material complaints about the operation of the business of the Applicant since its appointment at the commencement of these CCAA proceedings.
20. The Monitor has met with senior management of the Applicant and is in communication with them. The Monitor has made a number of visits to the Applicant's place of business and has requested various financial and other information from the Applicant.
21. In addition, the Monitor has set up weekly appointments with the management of the Applicant at which time the Monitor reviews outstanding issues and seeks additional information from the Applicant.

22. As reported in the First Report, there have been some inadequacies in the flow of financial information from the Applicant to the Monitor since the commencement of these CCAA proceedings. During the month of August, the information provided was incomplete and inaccurate. However, information provided during September has improved, so as to address concerns raised previously. Accordingly, the quality of financial information provided to the Monitor, on a weekly basis, has continued to improve during the month of September; however, the timeliness of its provision still continues to be an issue.
23. The Monitor is advised that the Applicant collects the accounts receivable of AFM, purchases inventory from AFM and funds the operations of AFM; however, the Monitor has not been fully provided with the particulars of such receipts, inter-company purchases and transfer payments, so as to make a determination as to the net cost or benefit of such transactions to the Applicant.
24. The Monitor continues to seek further financial information from the Applicant. At the time of drafting this report, the Monitor has not been furnished with any operating forecasts of the Applicant, for the post-filing period, and has not been furnished with any Statements of Income and Expenses, or any Statements of Assets and Liabilities, for the post-filing period, although the Monitor has requested same (The Monitor is advised

that August 2006 internal Financial Statements have recently been prepared and are to be sent to the Monitor shortly). Accordingly, the Monitor is unaware as to the profits earned, or losses incurred by the Applicant, in the period after August 8, 2006.

25. The Monitor has reviewed the Affidavit sworn by Robert Tweedy dated September 14, 2006 (the "Tweedy Affidavit"). The Monitor is encouraged by the acknowledgment contained therein that the Applicant must supply adequate financial reporting to the Monitor in order to enable the Monitor to perform its mandate. The Monitor endorses Mr. Tweedy's statement that the Applicant will ensure that the Monitor is fully informed of the reorganization process and the Applicant's financial situation.
26. While the Monitor has enjoyed the full cooperation of Mr. Tweedy, there has regrettably been continuous friction with Mr. Malisch pertaining to what he perceives to be excessive professional fees and costs of the Monitor and its Counsel. The Monitor and its Counsel billed an aggregate of \$42,703.53, plus GST, to the end of August 2006 (to August 25, in the case of Monitor's Counsel). At present, \$5,265.74 of that amount remains unpaid. Further, billings totaling \$39,265.51 plus GST, comprising billings of the Monitor to September 22, 2006, and of the Monitor's Counsel to September 12, 2006, were recently forwarded to the Applicant, and have not been paid. Mr. Malisch requested on September 23, 2006 that the

Monitor review operations only on a monthly basis rather than a weekly basis, so as to curtail costs. Further, Mr. Malisch requested that an estimate of costs to be incurred hereinafter be prepared. Accordingly, the Monitor and its Counsel have provided cost estimates to Mr. Malisch on a go-forward basis, and have pointed out that the Monitor has a duty to the Court and the Applicant's stakeholders to properly review the information provided, and to satisfy itself that there are no material adverse changes that need to be reported to this Honourable Court.

27. In the view of the Monitor, the constant frictions pertaining to what the Monitor should or should not do in carrying out its obligations, and the costs related thereto, have noticeably increased the fees and costs beyond what one would normally expect them to be under the circumstances.

28. Paragraphs 26 and 27 of the Initial Order read as follows:

26. THIS COURT ORDERS that the Monitor, counsel to the Monitor and counsel to the Applicant shall be paid their reasonable fees and disbursements, in each case at their standard rates and charges, by the Applicant as part of the costs of these proceedings.

27. THIS COURT ORDERS that the Monitor and its legal counsel shall pass their accounts from time to time, and for this purpose the accounts of the Monitor and its legal counsel are hereby referred to a judge of the Commercial List of the Ontario Superior Court of Justice.

Relying on the above, the Monitor requests that this Honourable Court schedule a hearing for the passing of the Monitor's and its Counsel's accounts.

29. Under the circumstances described in this Report, the Monitor requests an administrative charge be instituted for its fees and costs and those of its Counsel. Initially, the Monitor was led to believe that these CCAA proceedings would be of a short duration and that accordingly, the professional fees would be limited. The Monitor received a retainer towards its fees and costs, and those of its Counsel, from 2072223 Ontario Limited, a company related to the Applicant's current landlord and Mr. Malisch, which retainer has now been exhausted. It now appears that these CCAA proceedings will be more protracted than expected. Although the Monitor and its Counsel are Unaffected Creditors, pursuant to paragraph 41 of the Initial Order, the recurring complaints about professional fees and the apparent extension to the term of this engagement lead the Monitor to now seek the security of an administrative charge.

30. The Monitor requests that the Initial Order be amended to include an administrative charge in favour of the Monitor and its Counsel. It is proposed that the following paragraph, based on the language set-out in paragraph 32 of the model "Long" form of CCAA Initial Order, be inserted as paragraph 27A to the Initial Order:

27A. THIS COURT ORDERS that the Monitor, counsel to the Monitor, if any, and the Applicant's counsel shall be entitled to the benefit of and are hereby granted a charge (the "Administration Charge") on the Property, which charge shall not exceed an aggregate amount of \$●, as security for their professional fees and disbursements incurred at the standard rates and charges of the Monitor and such counsel, both before and after the making of this Order in respect of these proceedings. The Administration Charge shall constitute a first charge on the Property in priority to all security interests, trusts, liens, charges and encumbrances, statutory or otherwise, in favour of any Person.

Projected Cash Flows for the period of October 2, 2006 to December 1, 2006

31. Attached hereto as **Schedule "2"** to this Report, is the Applicant's projected cash flow for the period of October 2, 2006 to December 1, 2006 (the "Extended Cash Flows") as provided to the Monitor by the Applicant on September 29, 2006.
32. Based on our review and discussions with the Applicant's management, the Extended Cash Flows reflect assumptions that the Applicant believes to be reasonable.
33. Despite lower than projected cash receipts during the 7 weeks up to September 22, 2006, the Applicant is projecting higher weekly cash receipts for the next 9 weeks ending December 1, 2006 than had been projected in the earlier cash flow projections. Mr. Malisch has advised the

Monitor that these collection figures represent best estimates, given the ramped up production in September at the Applicant's Ajax facility.

- 34. In general, the cash disbursement figures projected appear reasonable and consistent with the disbursement activities of the first 7 weeks following the date of the Initial Order.

- 35. It appears that based on the cash flow projections prepared by the Applicant, and given the indebtedness to National Bank at September 22, 2006, the Applicant will have sufficient cash available so as to operate during the proposed stay extension period, provided that the value of marginable assets continues to support the borrowing amounts.

The Applicant's Request for an Extension of the Stay Period

- 36. The Monitor has reviewed the application of the Applicant to extend the Stay Period to November 30, 2006.

- 37. The Monitor is unaware of any objection to the proposed extension.

- 38. The Tweedy Affidavit of September 14, 2006, attests that the Applicant is proceeding in good faith and with due diligence.

Recommendation

39. Notwithstanding the concerns set out herein, the Monitor recommends that the proposed extension of the Stay Period to November 30, 2006 be granted.

ALL OF WHICH IS RESPECTFULLY SUBMITTED BY

BDO DUNWOODY LIMITED
in its capacity as Court Appointed
Monitor of the Applicant



Per:
Uwe Manski, FCA, FCIRP
President

SCHEDULE 1.

SCHEDULE 1.

SKLAR PEPLER FURNITURE CORPORATION
CUMULATIVE - PROJECTED TO ACTUAL (in Canadian Dollars)
August 7, 2006 to September 22, 2006

Week of:	Projected	Actual [1]	Variance
	Sep18-22	Sep18-22	Sep18-22
	Week 8	Week 8	Week 8
Cash Outflow:			
Payroll-Whitby(Includes source deductions) [2]	682,100	921,674	(239,574)
Payroll-Portland(Includes source deductions)	316,000	280,945	35,055
Pension benefits	33,000	2,070	30,930
Priority Payables(GST & PST)	100,000	48,125	51,875
Benefits (Portland)	16,000	44,964	(28,964)
Wires(Tables and Cut & Sew)	455,000	159,968	295,032
Raw Materials (includes fabric)	1,800,000	1,693,406	106,594
Freight Cost-Canada & US	77,000	159,894	(82,894)
Freight Cost-Overseas	119,000	55,069	63,931
Miscellaneous Payables	105,000	116,829	(11,829)
Rent & Overhead (Portland)	35,000	52,409	(17,409)
Rent & Overhead (Whitby) [2]	71,000	-	71,000
Rent & Overhead (Ajax)	71,000	92,087	(21,087)
Direct Payments	70,000	31,045	38,955
Loan Interest	35,000	36,583	(1,583)
Professional Fees(National Bank)	13,000	-	13,000
Sodex-Charges	-	170,953	(170,953)
Mgmt fees	-	17,742	(17,742)
Total Cash Outflow	3,998,100	3,883,763	114,337
Cash Inflow:			
Projected Cash Receipts	4,375,000	-	4,375,000
Cash Receipts	-	1,475,662	(1,475,662)
Sodex	-	2,198,409	(2,198,409)
Cr memo	-	1,548	(1,548)
Subdebt loan [3]	-	475,000	(475,000)
Total Cash Inflow	4,375,000	4,150,619	224,381
Net Cashflow	376,900	266,856	110,044
Opening Bank Position as at August 7, 2006 [4]		(3,985,009)	
Adjustment for Changes in Foreign Exchange Rates		44,455	
Closing Bank Position as at September 22, 2006 [4]		(3,673,698)	

NOTES

[1] - Based on the information supplied by the Applicant.

[2] - The "Whitby" description is incorrect, the item relates to the Ajax, Ontario facility.

[3] - Excludes a total of \$125,000 paid as a retainer to the Applicant's legal counsel and the Monitor, as well as consulting fees that are being accrued (\$20,000/mth) for day-to-day managerial services performed by Mr. Malisch.

[4] - Excludes the Subdebt loan and the contingent indebtedness to Sodex relating to factored accounts receivable balances.

SCHEDULE 2.

Sklar Peppler Furniture Corp.

Week of:	Oct 2-7		Oct 9-14		Oct 16-20		Oct 23-27		Oct 30-Nov 3		Nov 6-10		Nov 13-17		Nov 20-24		Nov 27-Dec 1		Total
	Week 10	Week 11	Week 11	Week 12	Week 12	Week 13	Week 13	Week 14	Week 14	Week 15	Week 15	Week 16	Week 16	Week 17	Week 17	Week 18	Week 18	Week 18	
Cash Outflow:																			
Payroll-Ajax(Includes source deductions)	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	90,000	810,000
Hourly	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	65,000	325,000
Salary																			140,000
Commission																			30,000
Management	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	45,000	435,000
Payroll-Portland(Includes source deductions)																			200,000
Pension benefits- grouped in payroll																			
Priority Payables(GST & PST)																			
Benefits (Portland)- grouped in Payroll	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	180,000
Wires(Tables and Cut & Sew)	293,000	315,000	315,000	326,000	326,000	326,000	326,000	338,000	338,000	338,000	338,000	360,000	360,000	360,000	360,000	360,000	360,000	360,000	3,016,000
Raw Materials (includes fabric)	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000	360,000
Freight Cost-Canada & US																			
Freight Cost-Overseas(grouped with Freight)	25,000																		25,000
Miscellaneous Payables	35,000																		105,000
Rent & Overhead (Portland)	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	142,000
Rent & Overhead (Ajax)	10,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	5,000	90,000
Direct Payments	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	120,000
Loan Interest and Bank charges	30,000																		180,000
Sears & Brick COOP Advertising	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	60,000
Professional Fees	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	90,000
Sales and marketing expenses	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	90,000
Office and Admin expenses	683,000	616,000	616,000	726,000	726,000	771,000	771,000	673,000	673,000	598,000	598,000	821,000	821,000	820,000	820,000	690,000	690,000	6,398,000	
Total Cash Outflow																			
Cash Inflow:																			
Projected Cash Receipts	650,000	675,000	675,000	675,000	675,000	700,000	700,000	750,000	750,000	750,000	750,000	750,000	750,000	750,000	750,000	800,000	800,000	800,000	6,500,000
Total Cash Inflow																			
Net Cashflow Increase (Decrease)																			
	(33,000)	59,000	59,000	(31,000)	(31,000)	(71,000)	(71,000)	77,000	77,000	152,000	152,000	(71,000)	(71,000)	(70,000)	(70,000)	110,000	110,000	110,000	102,000

End of Week Bank Balance	(4,403,404)	(4,346,404)	(4,346,404)	(4,397,404)	(4,397,404)	(4,468,404)	(4,468,404)	(4,391,404)	(4,391,404)	(4,239,404)	(4,239,404)	(4,310,404)	(4,310,404)	(4,380,404)	(4,380,404)	(4,270,404)	(4,270,404)	(4,270,404)	(4,270,404)
Operating Line, Marnging and Demand Loan	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000
Total Availability On Line	(405,404)	(346,404)	(346,404)	(397,404)	(397,404)	(468,404)	(468,404)	(391,404)	(391,404)	(239,404)	(239,404)	(310,404)	(310,404)	(380,404)	(380,404)	(270,404)	(270,404)	(270,404)	(270,404)
Add:																			
WAM Account	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000
Demand Loan	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000	400,000
Total Availability	394,596	453,596	453,596	402,596	402,596	331,596	331,596	408,596	408,596	560,596	560,596	489,596	489,596	419,596	419,596	529,596	529,596	529,596	529,596
Tables sales	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000	50,000
Units produced a week on average																			
Ajax	800	800	800	850	850	850	850	900	900	900	900	1000	1000	1000	1000	1000	1000	1000	1000
Portland	500	600	600	600	600	600	600	600	600	600	600	600	600	600	600	600	600	600	600
Unit sales	450	450	450	450	450	450	450	450	450	450	450	450	450	450	450	450	450	450	450
	585,000	630,000	630,000	652,500	652,500	652,500	652,500	675,000	675,000	675,000	675,000	720,000	720,000	720,000	720,000	720,000	720,000	720,000	720,000
Total sales excluding freight and taxes	635,000	680,000	680,000	702,500	702,500	702,500	702,500	725,000	725,000	725,000	725,000	770,000	770,000	770,000	770,000	770,000	770,000	770,000	770,000

Accounts receivable collection.
 Collections are based on immediate funding from Sodex for Brick and Sears
 Collections for independents are net 60 day terms at max.
 Since sales are increasing to independent cash receipts will be lagged behind which is why collections don't match sales.

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