

**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 OR ARRANGEMENT
OF PRISZM INCOME FUND, PRISZM CANADIAN OPERATING TRUST,
PRISZM INC. AND KIT FINANCE INC.

(the "Applicants")

FACTUM OF THE APPLICANTS
(returnable April 29, 2011)
(Motion to Extend Stay Period, Amend KERP, and Grant Franchisor Charge)

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TO: **ATTACHED SERVICE LIST**

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(returnable April 29, 2011)
(Stay Extension, KERP Amendment, and Franchisor Charge)

PART I - INTRODUCTION

1. On March 31, 2011, Priszm Income Fund ("**Priszm Fund**"), Priszm Canadian Operating Trust ("**Priszm Trust**"), Priszm Inc. ("**Priszm GP**"), and KIT Finance Inc. ("**KIT Finance**") (and together with Priszm Fund, Priszm Trust and Priszm GP, the "**Applicants**") were granted protection from their creditors pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "**CCAA**") by order of the Honourable Mr. Justice Morawetz (the "**Initial Order**"). The stay of proceedings and other benefits of the Initial Order were extended to Priszm LP. Priszm Fund, Priszm Trust, Priszm GP, Priszm LP and Kit Finance will be referred to collectively herein as the "**Priszm Entities**".

2. The Prizm Entities now seek the following relief:
 - (a) An extension of the Stay Period (as defined in paragraph 14 of the Initial Order) until and including June 30, 2011;
 - (b) Approval of amendments to the key employee retention plans as set out in the Affidavit of Deborah J. Papernick, sworn April 21, 2011 (the “April 21 Affidavit”); and
 - (c) Approval of a charge (the “Franchisor Charge”) in favour of Yum! Restaurants International (Canada) LP (the “Franchisor”) on the Property (as defined in the Initial Order) as security for the continuing fees payable pursuant to the Franchise Agreement (as defined in the April 21 Affidavit).
3. This relief will allow the Prizm Entities to continue their efforts to secure a going concern solution for their business, their approximately 6,500 employees and numerous suppliers, landlords and other creditors and maximize recovery for the Prizm Entities’ stakeholders.

PART II - THE FACTS

4. The facts with respect to this motion are more fully set out in the April 21 Affidavit. All capitalized terms used but not defined herein have the meaning ascribed to them in the April 21 Affidavit.

5. Prizm LP is a franchisee of the Franchisor and is Canada's largest independent quick service restaurant operator. Prizm LP operates 428 KFC, Taco Bell and Pizza Hut restaurants.

April 21 Affidavit, Motion Record, Tab 2 at paras. 3 and 4.

6. In fiscal years 2009 and 2010, the Prizm Entities experienced same store sales declines; as a result, financial performance was below prior years' performance and budgeted expectations.

April 21 Affidavit, Motion Record, Tab 2 at para. 4.

7. On September 5, 2010, Prizm Fund breached a covenant under its senior secured indebtedness with Prudential Investment Management, Inc., and each Prudential affiliate a party thereto (collectively, "**Prudential**"), failed to make certain payments required thereunder, and remains in non-compliance today.

April 21 Affidavit, Motion Record, Tab 2 at para. 5.

8. Prizm Fund failed to make an interest payment of \$0.975 million due on December 31, 2010 in respect to its subordinated debentures due June 30, 2012 and remains in default of its interest payment obligation.

April 21 Affidavit, Motion Record, Tab 2 at para. 6.

9. The Prizm Entities have also ceased paying certain obligations to the Franchisor as they come due, including continuing fees since December 2010. Prizm LP has defaulted in its obligation to complete contractually required upgrades to a number of restaurants.

April 21 Affidavit, Motion Record, Tab 2 at para 7.

CCAA Proceedings

10. Following various unsuccessful efforts to restructure or refinance their debt, the Prizm Entities sought and were granted CCAA protection. FTI Consulting Canada Inc. was appointed as monitor of the Prizm Entities (the “**Monitor**”) in this CCAA proceeding.

April 21 Affidavit, Motion Record, Tab 2 at para. 8.

11. The Initial Order granted a stay of proceedings up to and including April 29, 2011, or such later date as this Court may order.

April 21 Affidavit, Motion Record, Tab 2 at para. 25.

12. Since the commencement of the CCAA proceedings, the Prizm Entities have continued operating their business as a going concern.

April 21 Affidavit, Motion Record, Tab 2 at para. 17.

13. The Prizm Entities have also been working diligently to move the Soul Transaction (described below) to closing and to advance the Sales Process (described below).

April 21 Affidavit, Motion Record, Tab 2 at para. 17.

Soul Transaction

14. In September 2010, the Prizm Entities commenced a sales process in an effort to divest some of their restaurants, which resulted in an agreement of purchase and sale with Soul Restaurants Canada Inc. (the “**Purchaser**”) with respect to the sale of 232 (subsequently reduced to 231 with no corresponding reduction in the purchase price) operating restaurants in Ontario, British Columbia and Quebec (few outlets), as amended (the “**Soul Agreement**”).

April 21 Affidavit, Motion Record, Tab 2 at para. 19.

15. Since the commencement of the CCAA proceedings, the Prizm Entities have engaged in extensive negotiations with the Purchaser and worked diligently to move the transaction contemplated by the Soul Agreement (the “**Soul Transaction**”) to closing. As a result, the Prizm Entities expect to bring a motion to Court seeking approval of the Soul Agreement and the Soul Transaction shortly.

April 21 Affidavit, Motion Record, Tab 2 at para. 20.

Sales Process

16. Prizm LP, Prizm GP, Kit Finance and Prudential entered into an agreement dated February 1, 2011 (the “**Sales Process Agreement**”) pursuant to which the Prizm Entities agreed to conduct a sales process for the Prizm Entities’

restaurants not forming part of the Soul Transaction (the “**Remaining Restaurants**”) and to use their best commercial efforts to comply with the sale process described in the Sales Process Agreement.

April 21 Affidavit, Motion Record, Tab 2 at para 21.

17. On February 10, 2011, Prizm Fund retained Canaccord Genuity (“**Genuity**”) to act as financial advisor and sales agent in connection with the potential sale of some or all of its Remaining Restaurants and commenced the sales process.

April 21 Affidavit, Motion Record, Tab 2 at para. 22.

18. A number of expressions of interest were received by the Prizm Entities on or before March 22, 2011, the deadline set out in the Sales Process Agreement.

April 21 Affidavit, Motion Record, Tab 2 at para. 23

19. The Prizm Entities continue to work diligently with Genuity, the Monitor and Prudential to implement the sales process. The process has been amended and the Prizm Entities expect to bring a motion to Court seeking approval thereof shortly.

April 21 Affidavit, Motion Record, Tab 2 at para. 24

20. The stability provided by the stay of proceedings is critical for the Prizm Entities’ continuance of their daily operations and sales efforts.

April 21 Affidavit, Motion Record, Tab 2 at para. 27.

Key Employee Retention Plans

21. Prior to the commencement of the CCAA proceedings and in order to ensure retention of key personnel while the Prizm Entities attempted to refinance, restructure and sell their business, the Prizm Entities offered 41 key personnel retention bonuses (the “KERPs”).

April 21 Affidavit, Motion Record, Tab 2 at para. 33.

22. As security for their obligations under the KERPs, the Prizm Entities established trusts in favour of the KERP participants.

April 21 Affidavit, Motion Record, Tab 2 at para. 37.

23. Under the terms of the KERPs, in order to receive the incentive bonuses, the KERP participants cannot have resigned, been terminated with cause or have failed to perform their duties and responsibilities diligently, faithfully or honestly.

April 21 Affidavit, Motion Record, Tab 2 at para. 38.

24. Since March 31, 2011, three of the KERP participants have resigned from the Prizm Entities. As a result, those participants have forfeited their entitlement to their KERPs. In order to attempt to minimize the risk of further departures during this critical time, the Prizm Entities would like to reallocate the funds which have been forfeited by the KERP participants who have resigned to

certain of the remaining KERP participants (none of whom are members of senior management) as additional incentives to continue their employment with the Priszm Entities.

April 21 Affidavit, Motion Record, Tab 2 at para. 39.

25. It is believed that the amount of the forfeited funds is significantly less than the cost which would result from the disruption to ongoing operations if these employees left and had to be replaced.

April 21 Affidavit, Motion Record, Tab 2 at para. 40.

26. The Monitor is supportive of the proposed reallocation.

April 21 Affidavit, Motion Record, Tab 2 at para. 41.

Franchisor Charge

27. As described further in the April 21 Affidavit, Priszm LP has withheld payment of continuing fees payable to the Franchisor since December 7, 2010 and continues to do so.

April 21 Affidavit, Motion Record, Tab 2 at para. 42.

28. The Franchisor has agreed to defer collection of post-filing continuing fees accruing from March 31, 2011 to May 20, 2011 and waived any claim to interest in respect of such fees. In consideration of the deferral, the Priszm

Entities have agreed to grant (subject to Court approval) a charge in favour of the Franchisor to secure payment of such post-filing continuing fees.

April 21 Affidavit, Motion Record, Tab 2 at para. 44.

29. It is proposed that the Franchisor will be paid the post-filing continuing fees (not including interest) that relate to a particular outlet at the time of closing of the sale of such outlet. To the extent that any outlet is closed without a sale as a going concern, the Franchisor will be paid any deferred post-filing continuing fees (not including interest) that relate to those unsold outlets from retained proceeds of sale of other outlets.
30. The Franchisor Charge will rank behind the Administration Charge and the Critical Supplier Charge and ahead of the DIP Charge and the Directors' Charge (as such terms are defined in the Initial Order).

April 21 Affidavit, Motion Record, Tab 2 at para. 44.

31. It is not expected that the Franchisor Charge will have any detrimental effect on the beneficiaries of the DIP Charge or the Directors' Charge due to the corresponding increase in cash flow and the waiver of interest payable with respect to such fees. Further, the deferral makes the potential need to draw down on the DIP Amendment (as defined in the Initial Order) less likely.

April 21 Affidavit, Motion Record, Tab 2 at para. 45.

32. The DIP Lender (as defined in the Initial Order) has consented to the granting of the Franchisor Charge.

April 21 Affidavit, Motion Record, Tab 2 at para. 46.

PART III - ISSUES AND THE LAW

33. The issues on this motion are as follows:
- (a) Should the Court grant an extension of the Stay Period?
 - (b) Should the Court approve the amendment to the KERPs?
 - (c) Should the Court grant the Franchisor Charge?

Extension of the Stay Period

34. Pursuant to s. 11.02 of the CCAA, the Court may extend the stay of proceedings with respect to a debtor company where (a) circumstances exist that make the order appropriate; and (b) the applicant has acted and is acting in good faith and with due diligence.

CCAA, s. 11.02(2), 11.02(3)

35. The Stay Period expires on April 29, 2011. An extension of the Stay Period up to and including June 30, 2011 is necessary to give the Prizm Entities time to move the Soul Transaction to closing and advance the sales process.

April 21 Affidavit, Motion Record, Tab 2 at paras. 26-27.

36. In *Re Canwest Global Communications Corp.*, Justice Pepall granted an extension of the stay of proceedings for a group of debtors that were continuing to work with their stakeholders. She found that the extension would provide the necessary stability to allow the debtors to continue working towards a resolution that would result in the continuation of their businesses as a going concern. The factors which supported her decision were (a) the cashflow forecast indicated that the debtors had sufficient cash resources to operate throughout the extension of the stay period, (b) the monitor supported the extension, (c) there was a lack of opposition to the motion and (d) the debtors had acted and were continuing to act in good faith and with due diligence.

Re Canwest Global Communications Corp., [2009] O.J. No. 4788 (S.C.J.) [*Canwest I*], at para. 43, Applicants' Book of Authorities, Tab 1.

37. The Prizm Entities have prepared a revised consolidated cash flow forecast for the period from April 18, 2011 to July 3, 2011 that forecasts the Prizm Entities' receipts, disbursements and financing requirements which indicates that the Prizm Entities will have sufficient cash resources through to June 30, 2011.

April 21 Affidavit, Motion Record, Tab 2 at paras. 28-30.

38. The Monitor supports the motion to extend the Stay Period and the Prizm Entities are unaware of any creditor who opposes this motion. It is not

believed that any creditor will suffer any material prejudice if the Stay Period is extended as requested.

April 21 Affidavit, Motion Record, Tab 2 at paras. 31-32.
First Report of the Monitor dated April 26, 2011, para. 39

39. The Prizm Entities have acted and continue to act in good faith and have been working with due diligence to complete the Soul Transaction and continue the Sales Process.

April 21 Affidavit, Motion Record, Tab 2 at paras. 20, 24 and 31.

40. For the foregoing reasons, it is respectfully submitted that the Stay Period should be extended to June 30, 2011.

Amendment to the KERPs

41. Employee retention plans are designed to facilitate and encourage the continued participation of certain employees, while preserving enterprise value. The KERPs were established and funded prior to the CCAA filing. Similar employee retention programs have been approved by the Courts.

Re Canwest Global Communications Corp., 2009 CarswellOnt 6184 (S.C.J.) [*Canwest II*] at para. 49, Applicants' Book of Authorities, Tab 2.

42. The value of employee retention plans has been recognized in numerous CCAA proceedings, including in *Re Nortel Networks Corp.* and *Re Grant Forest Products Inc.*

Re Nortel Networks Corp., [2009] O.J. No. 1044 (Ont. S.C.J.)
[*Nortel*] at para. 4, Applicants' Book of Authorities, Tab 3.

Re Grant Forest Products Inc. [2009] O.J. No. 3344 (Ont. S.C.J.)
[*Grant Forest*], Applicants' Book of Authorities, Tab 4.

43. In *Grant Forest*, Justice Newbould found that the proposed employee retention plan was appropriate after considering the following factors:

- (a) the monitor supported the employee retention plan;
- (b) the beneficiary of the employee retention plan was likely to consider other employment opportunities if the employee retention plan is not approved;
- (c) the beneficiary of the employee retention plan was crucial to the successful restructuring of the debtor company;
- (d) it would be difficult to find replacement in a timely manner should the beneficiary elect to terminate his employment; and
- (e) the board of directors of the debtor company, in exercising their business judgment, supported the employee retention plan.

Grant Forest at paras. 8-12, 17-19, Applicants' Book of Authorities, Tab 4.

44. In the case at bar, notwithstanding the establishment of the KERPs in their favour, three KERP participants (all non-senior management head office employees) have resigned since the commencement of the CCAA proceedings. The Prizm Entities are concerned that losing additional KERP participants will complicate the daily operations of the Prizm

Entities and jeopardize their ongoing efforts to complete the Soul Transaction and the sales process.

45. As the Prizm Entities are in the very midst of the CCAA proceedings, the resignation of any more KERP participants would be detrimental as it would be difficult to find replacements in a timely manner. Management believes that the amount of the funds forfeited by the resigned KERP participants is significantly less than the cost which would result if the remaining KERP participants left and had to be replaced.
46. The proposed amendment to the KERPs decreases the threat of further resignations by the remaining KERP participants.
47. As stated above, the Monitor supports the proposed amendment to the KERPs.

April 21 Affidavit, Motion Record, Tab 2 at para. 41.

48. For the foregoing reasons, it is respectfully submitted that this Court should approve the proposed amendments to the KERPs.

Granting of the Franchisor Charge

49. The Prizm Entities are also seeking approval of the Franchisor Charge to secure payment of the post-filing continuing fees.

50. The Franchisor Charge will allow the Prizm Entities to defer payment of the March 31, 2011 to May 20, 2011 continuing fees. Similar to a debtor-in-possession financing charge, it will allow the Prizm Entities to preserve going-concern value by decreasing the strain on their cash flow.
51. The Franchisor Charge will facilitate Prizm Entities successfully completing the sales process and closing the Soul Transaction as it will increase their cash flow and reduce the probability of having to draw down on the DIP Amendment (as defined in the Initial Order).

April 21 Affidavit, Motion Record, Tab 2 at para. 45.

52. Section 11 of the CCAA provides that a Court may, subject to the restrictions set out in the CCAA, make any order that it considers appropriate in the circumstances.

CCAA, s. 11

Century Services v. Canada (Attorney General), 2010 SCC 60 [Century Services] at paras. 66-69, Applicants' Book of Authorities, Tab 5.

53. In *Century Services v. Canada (Attorney General)*, Justice Deschamps, speaking for the majority, noted the wide discretion section 11 affords and held that orders granted under that section should advance the policy objectives underlying the CCAA, which is to avoid the social and economic losses that may result from insolvency.

Century Services at para. 70, Applicants' Book of Authorities, Tab 5.

54. It is respectfully submitted that the granting of the Franchisor Charge will advance the policy objectives underlying the CCAA by allowing the Prizm Entities to maximize their chances of completing going concern solutions for their businesses.
55. As stated above, the Franchisor Charge will rank behind the Administration Charge and the Critical Supplier Charge and ahead of the DIP Charge and the Directors' Charge. The beneficiaries of the DIP Charge and the Directors' Charge received notice of this motion and either do not oppose or have consented to the granting of the Franchisor Charge.

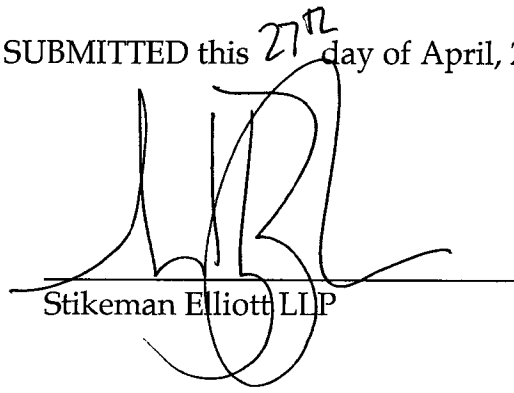
April 21 Affidavit, Motion Record, Tab 2 at para. 45.

56. For the foregoing reasons, it is respectfully submitted that this Court should grant the Franchisor Charge.

PART IV - ORDER REQUESTED

57. The Prizm Entities therefore request an Order, *inter alia*:
- (a) Extending the Stay Period until and including June 30, 2011;
 - (b) Approving certain amendments to the KERPs; and
 - (c) Approving the Franchisor Charge.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 27th day of April, 2011.



Stikeman Elliott LLP

Lawyers for the Prizm Entities

SCHEDULE "A"
LIST OF AUTHORITIES

1. *Re Canwest Global Communications Corp.*, [2009] O.J. No. 4788 (S.C.J.)
2. *Re Canwest Global Communications Corp.*, 2009 CarswellOnt 6184 (S.C.J.)
3. *Re Nortel Networks Corp.*, [2009] O.J. No. 1044 (Ont. S.C.J.)
4. *Re Grant Forest Products Inc.*, [2009] O.J. No. 3344 (Ont. S.C.J.)
5. *Century Services v. Canada (Attorney General)*, 2010 SCC 60

SCHEDULE "B"
RELEVANT STATUTES

Companies' Creditors Arrangement Act
R.S.C. 1985, c. C-36

General power of court

11. Despite anything in the Bankruptcy and Insolvency Act or the Winding-up and Restructuring Act, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

Stays, etc. – other than initial application

11.02 (2) A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,

- (a) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(a);
- (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
- (c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

Burden of proof on application

(3) The court shall not make the order unless

- (a) the applicant satisfies the court that circumstances exist that make the order appropriate; and
- (b) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

Restriction

(4) Orders doing anything referred to in subsection (1) or (2) may only be made under this section.

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Court File No: CV-11-9195-00CL

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