

## **Buyer unveils lawsuit against South Ocean**

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The embattled South Ocean Golf & Beach resort has been named as the centrepiece defendant in a lawsuit filed by a potential buyer against its holding company and Canadian pension fund owner, alleging that they violated an exclusivity agreement regarding the hotel's purchase that was signed earlier this year.

The plaintiffs, L&M Specialities and Case Financial, are alleging breach of contract, breach of fiduciary duties and fraudulent inducement against the South Ocean Development Company and its ultimate owner and financial backer, the Canadian Commercial Workers Industry Pension Plan (CCWIPP). They are seeking \$100 million damages, plus interest, costs and legal fees.

### **Defendants**

Also named as defendants are two leading CCWIPP executives, Eugene Fraser and Cliff Evans, who are both named as officers of the South Ocean Development Company, and Allen & Company, a Florida firm that is acting as a broker for the pension fund in finding a buyer for the South Ocean property.

The crux of the legal dispute, which was filed in the US district court for the southern district of Florida on November 9, is a contract that South Ocean entered into with L&M earlier this year, which allegedly gave the latter and its subsidiaries an exclusivity period to conduct due diligence and conclude the resort's purchase.

L&M alleged that the Letter of Intent it entered into for South Ocean's purchase was really "an attempt to deflect the Financial Services Commission of Ontario's (FSCO) investigation into the investment by CCWIPP in the property held by South Ocean [the resort]. South Ocean, [George] Allen and Allen & Company knew or should have known of this".

The FSCO has been investigating CCWIPP's investment activities for two years, the lawsuit alleged, and in May this year produced a damning report that said it had a "special concern" about the investments made in South Ocean and also the British Colonial Hilton, which the pension fund is also the financial backer for.

## **Demanded**

The FSCO demanded that CCWIPP's Board of Trustees conduct "a complete independent due diligence review" of their investments in the British Colonial Hilton and South Ocean resorts to determine, among other issues, whether all funds advanced to the resorts since December 2000 are "recoverable".

The Commission's report, a copy of which has been seen by The Tribune, details that over an 18-month period between June 14, 2001, and December 22, 2003, CCWIPP advanced a total of almost \$20 million to the British Colonial Hilton and South Ocean resorts.

Over that period some \$11.638 million was sent to South Ocean's holding company, the South Ocean Development Corporation, through Propco 34, the investment vehicle which acts as the 'in' company for CCWIPP to funnel funds to that property.

The South Ocean resort has been closed since July 2004, due to the heavy financial losses it had incurred for CCWIPP, with all 79 workers and 16 managerial staff laid off.

The pension fund said the closure would enable it to upgrade South Ocean, located in southwestern New Providence, from two to four-star status, but in reality it has been searching for a buyer through Allen & Co for many months.

The Florida lawsuit against the resort and its owner was filed by Michael and Lawrence Schaffer, who own L&M and are also chief executive and president respectively of Case Financial.

They alleged that they had a business relationship with CCWIPP "for many years", with the pension fund investing in Case Financial both as a shareholder and holder of a \$2.5 million debenture.

Mr. Schaffer alleged that in March 2005, he met with Evans and a purported associate, John Irvine, to discuss South Ocean's sale. He agreed that Case Financial would acquire it for \$25 million in a mixed cash and equity deal, either acting alone or by forming a consortium. The Letter of Intent was signed on March 21.

## **Reveals**

The Letter of Intent reveals that L&M and its partners would enter into a joint venture agreement with South Ocean Development Company to purchase the hotel for \$25 million, via a new holding vehicle.

The total value of the deal would be \$25 million, with CCWIPP getting \$10 million in cash and a 25 per cent equity stake in the new holding vehicle. The deal would have included the hotel properties, remaining 40-year lease on the golf course, and improvement rights to a marina and casino gaming licence.

Conclusion of any deal would have depended on the \$15 million mortgage that South Ocean had with Scotiabank (Bahamas) being in good standing.

The lawsuit claimed: "Due to the pending FSCO investigation, Evans, on behalf of himself, South Ocean and CCWIPP, required another Schaffer entity to enter into a Letter of Intent with South Ocean for the property."

Fraser allegedly signed the Letter of Intent, which allowed L&M and Case Financial to perform due diligence on South Ocean, examining its "financing, accounting and business records", as well as all contracts and the casino licence that kicks in when the resort gets up to a certain room size.

After the signing, L&M alleged that it and its subsidiaries brought various investor groups to the Bahamas to inspect South Ocean in April 2005.

The Letter of Intent allegedly prevented the defendants from soliciting other buyers between March 18, 2005, and May 31, 2005, but the lawsuit claimed that this exclusivity period was "breached".

The lawsuit alleged that in May 2005, South Ocean, CCWIPP and the other defendants approached investors from Toronto and others, who had previously been introduced to the Bahamian resort by Schaffer and his companies, and "falsely informed them that.... the Letter of Intent had been terminated".

They then allegedly attempted to sell the resort to the Toronto-based investors, who are not named in the lawsuit. Then, during May 2005, Schaffer and his companies alleged that Evans approached them to immediately pay back the \$2.5 million worth of debentures that CCWIPP held in Case Financial. This was sparked by the FSCO probe.

## **Debentures**

In return for paying back the debentures, South Ocean and CCWIPP allegedly agreed to extend the exclusivity period until January 31, 2006. An exchange of letters over the exclusivity period allegedly followed, but the lawsuit alleged that Schaffer was "induced" to hand over the agreement on the debenture repurchase before the extension agreement was "fully executed".

The lawsuit alleged: "The original Letter of Intent provided that plaintiffs had until June 31, 2005, to negotiate and execute a definitive agreement. However, on June 1, 2005, plaintiffs through Schaffer were falsely informed by CCWIPP, South Ocean, Evans and Fraser that Allen had sold the property, and therefore plaintiffs could not go forward to negotiate and enter into a definitive agreement under the original Letter of Intent, that South Ocean would not sign the extension agreement.....and further that no extension of the Letter of Intent would be honoured."

The debentures agreement was allegedly never returned.

South Ocean's closure was the culmination of the 'Right-Sizing Programme' report on South Ocean, written by Warren Adamson, president of the Caribbean Hotels Division for PRK Holdings, a company through which CCWIPP funds the resort.

The Adamson report said: "South Ocean's accumulated deficit as at December 31, 2002, as per its audited financial statement, was \$26 million. This deficit includes losses of \$4.7 million and \$3.5 million for the 2002 and 2002 fiscal years, respectively. The anticipated loss for fiscal 2003 is \$7 million of which \$5 million will be cash provided by [CCWIPP], the balance of \$2 million being non-cash expenses. "In fact, the anticipated loss for the 2003 fiscal year will exceed forecasted revenues..... To put another perspective on the extent of the loss situation, the \$5 million cash subsidy required of [CCWIPP] for 2003 will exceed the total annual payroll (including all payroll benefits and gratuities collected from guests and paid over to employees) of the entire resort operation."

The Adamson report said that based on figures to August 31, 2003, South Ocean's ADR was 84 per cent below the required rate to generate a reasonable return on the pension fund's investment. The hotel needed to generate an ADR of \$438 on its then 39.5 per cent occupancy, rather than the \$69.10 ADR it was actually achieving.

In addition, for the eight months to August 31, 2003, South Ocean's operating losses were 40 per cent higher than for the same period in 2002.