Executive summary

Deloitte & Touche LLP ("Deloitte") was contracted by the Department of Fisheries and Aquaculture to conduct a review of Ocean Choice International's ("OCI" or the "Company") operation in Marystown. The review conducted looked at the historical operation of the plant and opportunities available to the Company to improve sustainability and profitability. This report focuses on two main areas:

I. Review of the historical financial information provided by OCI to comment on their fiscal losses from 2008 to 2010, as they pertain to their primary groundfish operations in Marystown; and
II. Completion of financial projections for the primary groundfish operations as presented by OCI along with any additional opportunities that were identified through our review process.

It was determined that OCI has acted in accordance with sections 3.4.1 and 3.2.3 of the Implementation Agreement relating to the operation in Marystown. There were no material differences discovered in the Company's financial reporting. However, it must be noted, the variance analysis conducted does not constitute any type of assurance.

Based on the supplied income statements of the Marystown plant, OCI's Earnings Before Interest, Tax, Depreciation and Amortization ("EBITDA") losses are approximately $1.2 million, $2.9 million and $6.2 million for 2008, 2009 and 2010 respectively. EBITDA was calculated as per section 3.2.2 of the Implementation Agreement. While information prior to 2008 wasn't available from OCI, another report from the Government on the Marystown operations dated February 2006 showed an EBITDA loss of approximately $8.2 million in 2004, approximately $5.1 million in 2005 and a projected EBITDA loss of approximately $2.5 million in 2006. It appears from a historical perspective that the groundfish operations in Marystown have been an unprofitable venture for many years.

The analysis of the Marystown operations shows that there were significant EBITDA losses incurred by OCI since 2008. The main causes for the EBITDA losses were fluctuations in foreign exchange and fuel costs. In addition, increase in selling expenses, cost of sales, increases in overhead and a decrease in other income also contributed to the EBITDA losses.

For the Marystown operations, a $0.01 change in the United States (U.S.) dollar exchange rate creates an impact of approximately $0.3 million to the bottom line of the Marystown plant. Due to the considerable changes in the exchange rate over the last few years, it has become difficult for senior management of OCI to predict future results. Since 2008, the Canadian dollar has decreased as low as approximately $0.80 and has averaged approximately $0.93 against the U.S. dollar. OCI has experienced average rates of approximately $0.93 in 2008, $0.88 in 2009 and $0.97 in 2010 in this business segment. As per OCI, the negative impacts of a weaker U.S. dollar have been partially offset by an increase in average selling price. However, due to the export nature of the industry, a weaker U.S. dollar creates a negative impact on the Company's bottom line.

Rising fuel costs have also created a negative impact on the Company's operations. After a global economic downturn in 2008, which brought a decrease in the cost of fuel, the costs have continued to rise and are now approaching early 2008 levels. The Company's fuel usage has been relatively consistent over the last 3 years. The increase in fuel cost from 2008 and 2010 was almost $1.25 million. As fuel costs continue to rise and approach the 2008 levels, the Company can reasonably expect a rise in their fuel expense, directly impacting the Company's net income. Fuel represents approximately 26% of the landed cost. A $0.01 per litre change in the fuel cost can impact the business segment profitability by approximately $52,000.

Within this report, several scenarios were tested to determine the likely financial outcome. These scenarios include:

- Exporting 100% of the frozen at sea landings;
- Creating 18 weeks of in-plant processing for the Marystown facility which represents 25% of the landings, approximately 7 million lbs., and export the remainder;
- Moving 25% of the total landings, approximately 7 million lbs. to a facility in Fortune for processing and exporting the remainder; and
- Various situations for a potential EBITDA break even operation.

Based on information provided by OCI and under the current economic conditions, any substantial improvements to the operations or increased plant efficiency would be unlikely to result in a profitable EBITDA for Marystown plant. Although labour and fixed overhead costs at Marystown plant are significantly higher compared to Fortune plant, any reasonable reductions in these costs would not materially impact the plant profitability.

The following was the scope of work and the outcomes of the review.

Scope Point	Section in Document
a) Review all capital expenditures for the fiscal years 2008-2010 and determine if they are in accordance with Section 3.4.1 of the Implementation Agreement.	• Historical Observations- Capital Expenditures
Outcome: Based on procedures performed, there were no material errors or exceptions found.	
b) Verify that OCI is compliant with the requirements of the Implementation Agreement regarding the harvesting of groundfish and landing in specified product forms.	• Historical Observations- Product Forms
Outcome: Based on the letter issued by DFO and DFA, OCI is fully compliant with the conditions for harvesting of groundfish and landing in specified product forms, as outlined in the Implementation Agreement.	
c) Review and summarize the losses experienced by OCI from its harvesting and processing activities related to Marystown for the fiscal years 2008 to 2010. The consultant will discuss results with management of OCI and perform a high level variance analysis on the results explaining the differences year over year and corroborate the major differences where information or supporting documentation can be supplied by OCI. The consultant will not be required to provide any type of audit assurance on the results of operations or financial position of OCI's Marystown operations.	• Historical Observations – Marystown Processing Operation
Outcome: Foreign exchange and fuel costs were major factors contributing towards the EBITDA losses experienced by OCI for the past 3 years. Adding to the EBITDA losses were increases in other costs and decreases in other income. These EBITDA losses have been $1.2 million, $2.9 million and $6.2 million for 2008, 2009 and 2010 respectively.	
d) Provide a summary of any fiscal losses incurred by the Marystown processing facility prior to the fiscal year 2008. Indicate the level of assurance provided by OCI on each fiscal loss (i.e. audit, review, internal financial statements, etc).	• Historical Observations – Marystown Processing Operation
Outcome: OCI entered into an agreement with FPI to purchase the assets of the Marystown operation in December of 2007 and hence the Financial information prior to 2008 was not available. Additional	

Scope Point	Section in Document
information up to 2006 was obtained from another Government report on the Marystown Operations, dated February 2006.	
e) Review and verify that the method used by OCI to allocate overhead, administrative, head office and similar expenses is in accordance with Section 3.2.3 (a) of the Implementation Agreement; attest to the appropriateness of OCI's allocation method; and indicate any significant variances which would have arisen had a different generally-accepted allocation method been adopted.	• Historical Observations – Allocation of Overhead and Other Expenses
Outcome: OCI is compliant with Section 3.2.3 (a) of the Implementation Agreement. No additional information was available from OCI to test significant variances which would have arisen if a different generally-accepted allocation method had been adopted. In 2009 and 2010 the Marystown plant would have realized an EBITDA loss regardless of what allocation method was used.	
f) Complete financial projections to indicate the financial benefits, if any, which could be achieved by implementing each of the following stand alone options proposed by OCI. a. Frozen at Sea (FAS) production (i.e., no in-plant processing); and b. FAS production with in-plant processing at Marystown for 18 weeks annually, and export of all surplus FAS fish.	• Analysis – Scenario 1 and 2
Outcome: Exported Yellowtail provide a higher contribution margin to the operation when compared with in-plant processing. Under current projections for 2012 from OCI, operating the Marystown plant for 18 weeks would result in an EBITDA loss of approximately $2.3 million whereas 100 % export of FAS landings would result in a positive EBITDA of $0.1 million.	
g) Complete a financial analysis to determine the mix of FAS and fillet production necessary to provide a breakeven and profitable EBITDA.	• Analysis – Breakeven Analysis
Outcome: Based on sensitivity analysis in the financial model, a shift in various factors could influence the EBITDA break-even. Under the current projections of OCI this would require 100% export with no onshore processing. To achieve a profitable EBITDA within the Marystown operations, there has to be a significant positive change in the combination of foreign exchange or fuel costs, coupled with improvement in labour efficiency.	
h) Complete a financial analysis to determine the financial benefits, if any, of moving the in-plant processing to a smaller facility with lower fixed overheads.	• Analysis - Scenario 3
Outcome: Based on financial modeling with the information provided by OCI, moving the processing to Fortune would reduce the loss realized by OCI to approximately $0.8 million, compared to $2.3 million noted in f) above for Marystown. The difference between the two facilities is due to a reduction in cost of sales, approximately $1.1 million, and fixed plant overhead, approximately $0.4 million. For the same throughput in each operation, the plant in Fortune would have labour costs approximately $0.7 million less than Marystown.	
i) Complete a financial analysis to indicate the benefits realized, if any, from increasing the allowable export exemption for whole frozen Yellowtail flounder from 380 gm. to 450 gm. in 2010, including the relative contribution provided by the <380 gm. fish and the 380-450 gm. fish.	• Analysis – Future Events and Options
Outcome: Based on financial modeling with the information provided by OCI, contribution margins for the operations increase when the export size exemption is increased from 380 gm. to 450 gm. fish.	
j) Consider and comment on the potential impacts of certain future events on OCI's operations including higher utilization of Yellowtail quotas; tariff elimination under the Canada-European Comprehensive Economic and Trade Agreement (CETA); reopening of an American Plaice fishery on the Grand Banks; and changes in exchange rates.	• Analysis – Future Events and Options
Outcome: Several future events could impact OCI's operation. In the financial projections it is assumed	

Scope Point	Section in Document
that the full yellowtail quota will be utilized. EU tariff elimination will have very little impact on projections due to very low levels of export to that region. According to recent scientific reports there is only a 50% chance of American plaice reopening by 2015 so it was not realistic to include this in the projections. As outlined earlier, exchange rates have the largest influence on changes in financial outcomes.	
k) Report on OCI's employment levels at Marystown (including associated vessel crews) for the fiscal years 2008-2010.	• Historical Observations – Employment levels at Marystown
Outcome: OCI has maintained the required number of employees for the previous three years with an average employment of 422 people per year. OCI has been compliant with Section 3.1.1 of the Implementation Agreement.	