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Celebrations bring destruction

An Srey Nich, 10, shovels through scorched debris at her family's home, which was destroyed by fire in Phnom Penh's Meanchey district over the Khmer New Year weekend. A careless homeowner has been blamed for a fire that razed 10 homes in the district on Saturday, one of three weekend blazes caused by candles or incense, according to a fire department official. HONG MENEA

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Leopard's fishy business

Tom Brennan and Don Weinland

IN SIHANOUKVILLE, just north of Cambodia's only deep-water port, stands the headquarters of Chenla Seafood. A uniformed guard stands watch at the gate, which opens on to manicured grounds and a two-building facility that houses what will likely become the country's premier seafood processor.

A few kilometres up the hill and away from the water lies the former plant of Nautisco Seafood Manufacturing, which once held the mantle soon to be captured by Chenla. In sharp contrast to its successor,

Nautisco's facilities show significant wear. The black mould overtaking the factory walls and tall grass covering the yard give the impression the factory has not been used in years.

In fact, operations ceased only last November. And the link between the rise of the first and the collapse of the second, according to Nautisco Seafood's majority shareholders, is Leopard Capital, the Kingdom's bellwether private-equity firm.

A criminal case is playing out in the Phnom Penh courts in which Leopard, a minority stakeholder in Nautisco Seafood, is being charged with breach of trust and fraud in causing the company's collapse. The majority

shareholders, a small group of Canadians who control Nautisco Seafood through a parent company called Nautisco Inc, claim Leopard sought to intentionally sink the seafood processor, capture its assets through a series of complex debt deals, then launch a competitor, Chenla.

The *Post* first reported the legal dispute between the two parties on January 30, less than two years after Leopard Capital's initial investment in Nautisco Seafood.

At the time, Leopard Capital Cambodia managing partner Scott Lewis threatened to sue *The Phnom Penh Post* if it ran the story.

But further investigation over the

past couple of months has revealed that Nautisco Seafood suffered deep and sustained financial problems for much of its operating history, and that Leopard appeared to use that misfortune to its advantage.

Bullish prospects

The investment firm first bought into Nautisco Seafood in May, 2010, purchasing a 34.18 per cent stake for US\$1.6 million, the *Post* reported that month.

Documents obtained in recent weeks, however, show Nautisco Seafood, which launched in September 2009, earned just \$34,407 in rev-

enues through the close of the year, indicating Leopard saw significant upside in the business.

Indeed, Leopard chief executive Douglas Clayton said as much to the *Post* after the deal.

"We are bullish on Cambodia's prospects to break into the global seafood trade," Clayton wrote in an email at the time.

But according to the criminal complaint filed by Nautisco Seafood, \$4 million in start-up capital from the company's early investors was not enough to overcome a host of issues hindering prof-

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itability, including human-resource problems, a limited supply of raw materials and challenges in meeting the international food-safety standards necessary to gain access to key export markets.

Even after Leopard's investment, those problems continued to get worse.

'Going concern'

By October, 2010, "the company was facing severe financial problems", according to the criminal complaint filed by Nautisco Seafood. Two lines of credit worth \$500,000 taken from Cambodia's Advanced Bank of Asia the previous summer seemed to do little to improve operations.

Lionel Letessier, an Indonesia-based consultant hired by Leopard to survey the plant, noted in a later report obtained by the *Post* that "process flow, [quality control], sanitation, product quality, maintenance, etc, must absolutely be improved".

Despite this list of inefficiencies, though, Letessier said he doubted they would explain the company's "huge losses", which were more likely a product of "high-level mismanagement".

Nautisco Seafood's former chief executive, Peou Sambath, declined to comment for this story, as did officials from Leopard Capital and majority shareholder Nautisco Inc.

But some former employees and brokers that supplied raw shrimp to the company pointed to a culture of nepotism at Nautisco Seafood that allegedly gave rise to shady business practices.

"They lost profits because they had a lot of people from the same families working there, and they were corrupt," Hak Houern, a procurement officer, told the *Post*.

Chour Kenghung, a shrimp broker operating in Sihanoukville, claimed Nautisco Seafood had nearly gone bankrupt at one point "due to its nepotism and inside corruption".

A lawyer for Nautisco Inc claimed the company's investigation into corruption allegations showed that a top procurement official at Nautisco Seafood had taken bribes from shrimp brokers looking to secure their relationship with the company.

The investigation also allegedly revealed that the official gave little consideration to the size and quality of shrimp purchased and paid above-market rates for the raw supply.

While that may explain, at least in part, Nautisco Seafood's excess loss of cash, the *Post* was unable to substantiate the claims through its interviews with a number of the company's shrimp suppliers and former employees.

What is revealed in the company's financial statements from 2010, obtained by the *Post*, is that very little of the growing debt load was

put towards improving the efficiencies and capabilities of the company. Only about \$81,000 was spent that year on property, plant and equipment, despite net cash of \$1.3 million generated from short-term loans and proceeds from shareholders. Much of the rest of the cash seems to have gone to procurement of raw supply, which for whatever reason failed to translate into profits for the company.

At a board meeting on November 7, an agreement was reached where Leopard officials would engineer a loan "with the stated aim of preventing the company from becoming insolvent", according to the criminal complaint.

Two days later, the board voted to push forward with a refinancing plan to prevent insolvency, and accepted a new line of credit with ABA worth up to \$900,000. In December, Nautisco Seafood tapped another \$500,000 from the bank.

Nautisco Seafood finished 2010 with a net loss of \$1.2 million for the year, according to Morison Kak & Associates, the independent auditor that prepared the company's financial statements that year.

In its report, which was also obtained by the *Post*, Morison Kak said the projected \$5 million in sales for 2011 would "at best ensure the break-even point", putting Nautisco in danger of not meeting its debt obligations the following year. "Without shareholders' financial support or any substantial cash injection, the company cannot continue as a going concern," the report said.

'True intention'

The start of 2011 brought with it an important question for Nautisco Seafood Manufacturing, according to its majority shareholders, beyond just the failing operations. Was Leopard Capital acting in the company's best interests?

The criminal complaint alleges that Leopard was not. In addition to charging higher interest on loans made to Nautisco Seafood than the company received from other banks, the majority shareholders claim Leopard also began to charge interest on the cash collateral it put up to back those other loans.

In addition, Leopard allegedly demanded Nautisco Seafood grant the investment firm full title and ownership of newly purchased equipment up to \$150,000 in the event of default as security for the cash collateral.

A similar move to acquire assets is said by the majority shareholders to have taken place in June, when Leopard Cambodia Fund, which was linked to Leopard Capital, issued \$200,000 to Nautisco Seafood at zero per cent interest. But the money came with the condition that all inventories at the time of the loan and any purchased thereafter be used as security in the event of default.

The complaint alleges the board of directors did not ap-



A Nautisco Seafood Manufacturing Ltd truck on the grounds of the company's Sihanoukville processing plant. PHOTO SUPPLIED

prove the loan, and that it was agreed upon only by CEO Peou Sambath, who also served as chairman of the board of directors, and Leopard Cambodia managing partner and Nautisco Seafood director Scott Lewis.

Nautisco Seafood sought as much as \$1.25 million in credit throughout 2011, with Leopard Capital fronting a significant amount of cash collateral with conditional agreements. These moves show that Leopard's "true intention [was] to drive the company into financial distress unnecessarily and thus acquire ownership at a low price", according to the criminal complaint.

To that end, Nautisco's lawyers say, Leopard entered into a side deal with ABA to purchase all the bank's loans to Nautisco without board approval or the knowledge of the majority shareholder. This, in effect, made Leopard the company's biggest creditor, a fact that was confirmed to the *Post* by Scott Lewis in January.

"The minority shareholder then threatened to immediately call in the loans to [Nautisco Seafood] in an attempt to extort more money from the majority shareholder, Nautisco Inc," the complaint alleges.

Technically insolvent

Leopard newsletters issued in 2010 and 2011 painted the picture of a successful and growing seafood operation, while financial statements and emails showed an increasingly insolvent and ailing company.

"The company is illiquid and thus technically insolvent. There are insufficient funds to ... pay outstanding raw material suppliers or the operating costs and salaries due at the end of August," Leopard consultant Gordian Gaeta wrote in a memo to Nautisco stakehold-

ers last summer. The following month, he proposed winding down the company, according to the complaint, and the board agreed to stop procuring raw materials, sell off inventory and terminate most workers.

A decision was made to halt operations at the Sihanoukville plant from November 4, after a board meeting was held the day before without the participation of the majority shareholder.

Yet Leopard's December newsletter noted only that "local operational challenges" continued to trouble Nautisco

discussions" with Hanwa in Tokyo last October. However, the majority shareholders claim the talks upset Hanwa, and Leopard has since refused to discuss them. Representatives from the Japanese distributor did not respond to email requests for comment.

New seafood factory

As Nautisco floundered during the summer of 2011, the complaint alleges Leopard insisted that shrimp inventory be dramatically increased and moved to the Ocean King

show that Chenla Seafood is a subsidiary of Nautisco HK, and that Scott Lewis is the representative for the latter firm in Cambodia.

Former Nautisco procurement officer Hak Houern said he worked briefly for Chenla in preparation for the company's launch but quit after having disagreements with Leopard management.

"I hear [Chenla] will start to operate their new factory after Khmer New Year," he said.

Questions about Nautisco Seafood chairman and CEO Peou Sambath's responsibility for the company's failure, as well as his relationship with Leopard Capital, remained unanswered. Nautisco Inc officials did respond to questions about their inability to exercise control against minority shareholder Leopard or steer the company to profitability.

As the *Post* reported in January, a Phnom Penh municipal court had ordered a plan of compromise earlier that month and appointed an administrator to handle the proceedings.

The Nautisco Seafood statement at the time defined a plan of compromise as a legal process where the courts act as an unbiased third party to solve the dispute, and "protect the business while a sustainable business plan is developed".

Leopard has appealed that ruling and a hearing is planned in front of Judge Gnung Thul on April 26, sources said. Attempts at an out-of-court settlement have proved unsuccessful.

In Leopard's March, 2012 newsletter, the firm said only that shareholders have been unable to agree on a restructuring plan for Nautisco and that the "disagreement is being addressed through appropriate channels". ADDITIONAL REPORTING BY MAY KUNMAKARA AND YI SOMPHOSE

[Leopard] then threatened to immediately call in the loans in an attempt to extort more money from ... Nautisco Inc

Seafood, but demand continued to be robust.

By the time the December newsletter was issued, Nautisco had no senior management, as the complaint alleges Leopard refused to discuss the renewal of contracts for the company's top positions.

A staff of 600 in August had been reduced to less than 20.

Clandestine discussions

Rumours that Leopard was about to launch its own seafood operations in Sihanoukville circulated among industry insiders at the end of last year.

In mid-December, Nautisco's largest customer, Hanwa Co Ltd of Japan, told Nautisco Seafood chief operating officer Yuriy Kolytkov there was speculation that Leopard would co-operate with local seafood outfit Ocean King, according to the complaint.

The complaint continues, saying Leopard's Gaeta and Lewis engaged in "clandestine

factory for storage. A due diligence report on Nautisco Seafood, conducted by Leopard's finance team, showed a significant drop in that inventory as of October 31 – to just over \$689,000 from \$889,361, a 22 per cent decline.

The report calls the difference "materially significant", citing causes such as cost allocation, spoilage of raw material, inaccurate recording in the accounting system and fraud. Leopard's first mention of a new company came last month, when it stated in another newsletter that Nautisco HK, the Hong Kong affiliate the company used to invest in Nautisco Seafood, "has started a new seafood factory in a leased modern factory in Sihanoukville".

The name of the Sihanoukville entity is not disclosed in the newsletter, but Ocean King's owner told the *Post* last month that Leopard was in fact leasing his plant. Ministry of Commerce documents also