

COURT FILE NUMBER

25-2299607

COURT

COURT OF QUEEN'S BENCH OF ALBERTA

JUDICIAL CENTRE

CALGARY

APPLICANTS

**IN THE MATTER OF THE *BANKRUPTCY AND
INSOLVENCY ACT, RSC 1985, c B-3***

**AND IN THE MATTER OF THE DIVISION I PROPOSAL
1031084 ALBERTA LTD.**

**FIRST REPORT OF THE PROPOSAL TRUSTEE TO
COURT SUBMITTED BY KPMG INC. DATED
OCTOBER 6, 2017**

ADDRESS FOR SERVICE AND
CONTRACT INFORMATION OF
PARTY FILING THIS DOCUMENT:

PROPOSAL TRUSTEE

KPMG Inc.
Suite 3100, Bow Valley Square II
205 - 5th Ave SW,
Calgary, Alberta T2P 4B9
Ryan Adlington
Tel: (403) 691-8504
radlington@kpmg.ca

COUNSEL

Torys LLP
525 – 8th Avenue SW,
46th Floor Eighth Avenue Place East
Calgary, Alberta T2P 1G1
Kyle Kashuba
Tel: (403) 776-3744
kkashuba@torys.com

Table of Contents

	<u>Page</u>
1. INTRODUCTION	4
2. BACKGROUND	5
3. CASH FLOW FORECAST	8
4. LEASE DISCLAIMER.....	10
5. ADMINISTRATIVE CONSOLIDATION.....	10
6. ADMINISTRATION CHARGE.....	11
7. PROPOSAL TRUSTEE’S RECOMMENDATION.....	11

Listing of Appendices

- Appendix "A" - Cash Flow Statement
- Appendix "B" - Management's Representation Letter

1. INTRODUCTION

1. On October 2, 2017, 1031084 Alberta Ltd. (“**Alberta Co**”) filed a Notice of Intention to Make a Proposal (the “**NOI**”), pursuant to Section 50.4(1) of the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 as amended (the “**BIA**”). On October 3, 2017, 623735 Saskatchewan Ltd. (“**Saskatchewan Co**”, and collectively with Alberta Co, the “**Company**”) filed an NOI pursuant to the same legislation (collectively with Alberta Co’s NOI filing, the “**NOI Proceedings**”). KPMG Inc. (“**KPMG**”) was appointed as proposal trustee (the “**Proposal Trustee**”) in the NOI Proceedings.
2. The NOI provides Alberta Co with a stay of proceedings until November 1, 2017 and a stay of proceedings for Saskatchewan Co until November 2, 2017 (the “**Initial Stay Period**”).

Purposes of the Report

3. The purpose of the First Report of the Proposal Trustee (the “**First Report**” or this “**Report**”) is to provide this Honourable Court with the Proposal Trustee’s views on the following matters:
 - a) A summary of certain background information about the Company;
 - b) The objectives of the NOI Proceedings and the creditors of the Company;
 - c) The Company’s statement of projected cash flow for the 13-week period from October 1, 2017 to December 30, 2017 (the “**Cash Flow Forecast**”);
 - d) The Company’s request for Administrative Consolidation of the estates of Alberta Co and Saskatchewan Co; and
 - e) The Company’s request for the approval of an Administrative Charge as defined in Affidavit #1 of Danny Mysak (the “**Mysak Affidavit**”).

Restrictions and Scope Limitation

4. In preparing this First Report and making the comments herein, the Proposal Trustee has been provided with, and has relied upon certain unaudited, draft and/or internal financial information, Company records, Company prepared financial information and projections, discussions with management and employees of Alberta Co and Saskatchewan Co, doing business as Spareparts, and information from other third party sources (collectively, the “**Information**”). Except as described in this Report:

5. The Proposal Trustee has reviewed the information for reasonableness, internal consistency and use in the context in which it was provided. The Proposal Trustee has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of the Information in a manner that would wholly or partially comply with generally accepted assurance standards, and accordingly The Proposal Trustee expresses no opinion or other form of assurance in respect of the Information.
6. In view of the purpose of the First Report, some of the financial information herein may not comply with generally accepted accounting principles.
7. Some of the information referred to in this First Report consists of forecasts and projections, which were prepared based on management's estimates and assumptions. Such estimates and assumptions are, by their nature, not ascertainable and as a consequence no assurance can be provided regarding the forecasted or projected results. Indeed, the reader is cautioned that the actual results will likely vary from the forecasts or projections, even if the assumptions materialize, and the variations could be significant.
8. The Proposal Trustee has prepared this First Report in its capacity as a court appointed officer in support of the motion described in section 7 of this Report. The reader is cautioned that this Report may not be appropriate for any other purpose and consequently should not be used for any other purpose.
9. Unless otherwise stated, all monetary amounts noted herein are expressed in Canadian dollars.
10. Capitalized terms not otherwise defined herein are as defined in the Company's application materials, including the Mysak Affidavit filed in support of this application. The First Report should be read in conjunction with the Mysak Affidavit as certain information contained in the Mysak Affidavit has not been included herein to avoid unnecessary duplication.

2. BACKGROUND

11. Spareparts is a private sunglasses, watch, and accessories store with national presence (with 21 locations across Canada as at the dates of the filing of the NOI Proceedings). Of the 21 stores nationwide, 4 locations are operating under Saskatchewan Co and the remaining 17 stores are under Alberta Co. All of Spareparts' 21 store locations are leased.

12. While the Company's head office is located in a leased premises at 213 Avenue C S, Saskatoon, Saskatchewan, the locality of both Alberta Co and Saskatchewan Co, based on the analysis provided in the Mysak Affidavit, is Alberta.
13. Although there are two entities that were set up for the operations of Spareparts, the Company operates as a single, integrated economic unit.
14. As described in the Mysak Affidavit, the growing competition in the market and the general challenges in the retail marketplace have led the Company into challenges in its working capital management. The Company has defaulted on various financial and other covenants with their secured creditors, Royal Bank of Canada ("RBC") and BDC Capital Inc. ("BDCC"). Both RBC and BDCC have agreed to forbear from enforcing their rights and remedies, subject to certain terms and conditions, to permit the Company to pursue a restructuring.
15. On October 2, 2017 and October 3, 2017, respectively, Alberta Co and Saskatchewan Co each filed an NOI, to allow the Company to downsize its store footprint through disclaimers of certain leases at its underperforming stores, and to restructure its business, potentially through the completion of a Sales and Investment Solicitation Process (the "SISP").
16. The Company's business affairs, financial performance and position, as well as the causes of its insolvency, are detailed in the Mysak Affidavit and are hence not repeated in the First Report. The Proposal Trustee has reviewed the Mysak Affidavit, has discussed the same with Mr. Mysak, and is of the view that the Mysak Affidavit provides a fair summary thereof.

OBJECTIVES OF THE NOI PROCEEDINGS

17. The primary objectives of the NOI Proceedings are to:
 - a) Ensure the on-going operations of the Company;
 - b) Restructure the Company's operations, including the proposed closure of the underperforming stores and lease disclaimers in respect thereof;
 - c) Restructure the debts of the Company to ensure the Company has adequate working capital to continue its operations; and

- d) Complete a transaction arising from a SISP to be proposed and approved by this Honourable Court. It is anticipated that the proposed SISP will contemplate a stalking horse credit bid by a party related to the Company.

CREDITORS

Secured creditors

18. The Proposal Trustee understands the following:

- a) The Company entered into a secured revolving operating loan (the “**Operating Loan**”) and several non-revolving term loans (the “**Non-Revolving Loans**”) with RBC in October 2016 (the “**RBC Facilities**”), whereby RBC has provided the Operating Loan and a Non-Revolving Loan to Saskatchewan Co and 11 Non-Revolving Loans to Alberta Co. The Operating Loan is used to support daily working capital requirements for both Saskatchewan Co and Alberta Co.
- b) The outstanding loan balance, as at October 2, 2017, was approximately \$3.92 million.
- c) The RBC Facilities are secured by a first charge over all the assets of Saskatchewan Co, Alberta Co and 101268550 Saskatchewan Ltd. (“**101**”, shareholder of Saskatchewan Co and owned by Mrs. Terra Mysak), with cross-guarantees between Alberta Co and Saskatchewan Co, and additional guarantees from 101 and the ultimate owners, Mr. Danny Mysak and Mrs. Terra Mysak.
- d) Alberta Co also entered into a financing agreement with BDCC (a wholly owned subsidiary of BDC) on October 4, 2016 (the “**BDCC Facility**”). The BDCC Facility was for the purpose of tenant leasehold improvements in 2016 and 2017, working capital growth, and replenishment of working capital. The outstanding loan balance for the BDCC Facility, as at October 2, 2017, was approximately \$960,000.
- e) The BDCC Facility is secured by a general security agreement over all the assets of Saskatchewan Co, Alberta Co and 101, with cross-guarantees between the two primary entities and additional guarantees from 101 and the owners.
- f) According to the personal property registry searches conducted in respect of the two primary companies, other secured creditors include Steelcase Financial Services Ltd. (for Saskatchewan Co and Alberta Co) and Element Financial Corporation (for

Saskatchewan Co). Management advised that these registrations were related to the various equipment leased by the Company.

Unsecured creditors

19. According to the Company’s books and records, as at October 2, 2017, Management estimates that accrued and unpaid unsecured obligations totalled approximately \$2,243,154.08, which consists of \$2,243,154 in trade payables, \$123,879 in professional fees and \$1,180,048 in tenant leasehold improvements payables.

3. CASH FLOW FORECAST

20. The Company, with the assistance of the Proposal Trustee, has prepared a cash flow forecast of its receipts and disbursements for the period from October 1, 2017 to December 30, 2017. The detailed Cash Flow Forecast is attached as Appendix “A” to this Report and is summarized below:

1031084 ALBERTA LTD. and 623735 SASKATCHEWAN LTD.	
Consolidated 13-week Cash Flow Forecast	
For the period October 1 to December 30, 2017	
\$' unaudited	13 Weeks
Receipts	
Sales	5,623,318
Sales tax collected	607,318
Total receipts	6,230,637
Disbursements	
Occupation costs	1,026,603
Salaries, wages and benefits	810,385
Inventory payments	2,620,000
Source deductions and WCB	252,403
Tax remittances	67,657
Bank charges	47,447
Insurance	4,540
Telephone and utilities	18,534
Overhead costs	37,217
Marketing expenses	28,117
Webshop costs	9,750
Contingency	65,000
Total disbursements	4,987,651
Net cash flow before professional fees and payments to secured creditors	1,242,986
Professional fees	235,000
Loan repayments - principal and interest	-
Total professional fees and payments to secured creditors	235,000
Net cash flow after professional fees and payments to secured creditors	1,007,986
Opening balance	939,723
Ending balance	1,947,709

21. The Cash Flow Forecast estimates that the Company will be generating approximately \$1 million during the period of projection.
22. The Proposal Trustee has reviewed the Cash Flow Forecast to the standard required by section 50.4(2) of the *BIA*. Section 50.4(2) requires the Proposal Trustee to review the debtor's cash flow statement as to its reasonableness and to file a report with the Office of the Superintendent of Bankruptcy on the Proposal Trustee's findings. The Canadian Association of Insolvency and Restructuring Professional's Standards of Professional Practice include a standard for proposal trustees fulfilling their statutory responsibilities under the *BIA* in respect of a proposal trustee's report on the Cash Flow Forecast.
23. Our review consisted of inquiries, analytical procedures and discussion related to information supplied to us by certain of the management and employees of the Company. Since hypothetical assumptions need not be supported, our procedures with respect to them were limited to evaluating whether they were consistent with the purpose of the Cash Flow Forecast. We have also reviewed the support provided by management of the company for the probable assumptions, and the preparation and presentation of the Cash Flow Forecast.
24. Based on our review, nothing has come to our attention that causes us to believe that, in all material respects:
 - a) the hypothetical assumptions are not consistent with the purpose of the cash-flow statement;
 - b) as at the date of this Report, the probable assumptions developed by management are not suitably supported and consistent with the plans of the Company or do not provide a reasonable basis for the cash-flow statement, given the hypothetical assumptions; or
 - c) the cash-flow statement does not reflect the probable and hypothetical assumptions.
25. Since the Cash Flow Forecast is based on assumptions regarding future events, actual results will vary from the information presented even if the hypothetical assumptions occur, and the variations may be material. Accordingly, we express no assurance as to whether the Cash Flow Forecast will be achieved.
26. The Cash Flow Forecast has been prepared solely for the purpose described on the face of the Cash Flow Forecast, and readers are cautioned that it may not be appropriate for other purposes.

27. Management's representation on the Company's Cash Flow Forecast is attached to this Report as Appendix "B". In its representations, the Company has indicated that the assumptions underlying the Cash Flow Forecast are appropriate in the circumstances.

4. LEASE DISCLAIMER

28. The Company, with the assistance of its advisors and in consultation with the Proposal Trustee, has concluded that a restructuring focusing on profitable stores, while vacating unprofitable locations, will maximize value for all stakeholders.
29. To date, Alberta Co, with the assistance of the Proposal Trustee, has identified seven stores that are to be closed (the "**Closing Stores**"). Management has disclaimed the leases at the Closing Stores as at October 2, 2017.
30. Management is in the process of redistributing all the inventory from the Closing Stores to the stores that will remain opened.
31. In addition to the Closing Stores, Saskatchewan Co has also disclaimed the two leases of the Company's warehouse on October 4, 2017.

5. ADMINISTRATIVE CONSOLIDATION

32. As noted in the Mysak Affidavit, Alberta Co and Saskatchewan Co operate as a single, integrated economic unit, and it will not be in the Company's interest to segregate the operations of each of the entity for the purpose of the NOI Proceedings.
33. The Proposal Trustee agrees that it would be in the best interest of the restructuring process and all stakeholders affected thereby if the estates are consolidated administratively for the purposes of efficiency and cost optimization.
34. The Proposal Trustee has reviewed the Mysak Affidavit and is also of the view that the analysis of the locality of the debtors provided in the Mysak Affidavit, stating that the locality of the Company is in Alberta, is a fair summary thereof.

6. ADMINISTRATION CHARGE

35. The Company is seeking approval of an Administration Charge over all of the property, assets and undertakings of Alberta Co and Saskatchewan Co in priority to all other security interests, trusts, liens, charges and encumbrances, claims of secured creditors, statutory or otherwise, in an amount not to exceed \$300,000, in favour of the Proposal Trustee, Torys LLP and McCarthy Tétrault LLP's in order to secure payment of their respective reasonable fees and disbursements incurred at their standard rates and charges.
36. In the event that the Company does not file proposals or if the proposals filed are not approved by the Company's creditors or the Court, then Alberta Co and Saskatchewan Co will be deemed to have made assignments in bankruptcy. KPMG would be named Trustee in Bankruptcy and would have to comply with certain statutory duties. If the assets of the Company are fully encumbered by secured claims, then without the benefit of the Administration Charge, KPMG would be at risk of non-payment of its fees.
37. The secured creditors, most directly impacted by the proposed charge, either consent to or do not oppose the granting of the charge.

7. PROPOSAL TRUSTEE'S RECOMMENDATION

38. Based on the foregoing, the Proposal Trustee respectfully recommends that this Honourable Court issue an order:
- a) Approving the transfer of the estate of Saskatchewan Co from Saskatchewan to Alberta and approving the Administrative Consolidation of Alberta Co and Saskatchewan Co; and
 - b) Approving the Administration Charge.

This Report is respectfully submitted this 6th day of October, 2017.

KPMG Inc.

**In its capacity as Trustee under the Notice of Intention to
Make a Proposal of 1031084 Alberta Ltd. and 623735 Saskatchewan Ltd.,
and not in its personal capacity**



Per: Ryan J. Adlington
Senior Vice President



Per: Pinky Law
Vice President

APPENDIX “A”

Cash Flow Forecast

1031084 ALBERTA LTD. and 623735 SASKATCHEWAN LTD. (collectively, the "Company")
 Consolidated 13-week Cash Flow Forecast for the period October 1 to December 30, 2017
 \$' unaudited

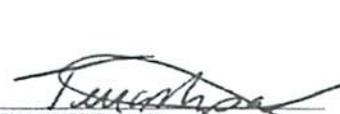
For the week:	Notes	Week 1	Week 2	Week 3	Week 4	Week 5	Week 6	Week 7	Week 8	Week 9	Week 10	Week 11	Week 12	Week 13	Total
		Oct 1 - 7	Oct 8 - 14	Oct 15 - 21	Oct 22 - 28	Oct 29 - Nov 4	Nov 5 - 11	Nov 12 - 18	Nov 19 - 25	Nov 26 - Dec 2	Dec 3 - 9	Dec 10 - 16	Dec 17 - 23	Dec 24 - 30	13 weeks
Receipts															
Sales	3	140,709	140,709	140,709	140,709	244,700	322,694	322,694	322,694	471,643	844,015	844,015	844,015	844,015	5,623,318
Sales tax collected	3	15,197	15,197	15,197	15,197	26,428	34,851	34,851	34,851	50,937	91,154	91,154	91,154	91,154	607,318
Total receipts		155,905	155,905	155,905	155,905	271,128	357,545	357,545	357,545	522,580	935,168	935,168	935,168	935,168	6,230,637
Disbursements															
Occupation costs	4	382,823	-	-	-	301,049	-	-	-	342,731	-	-	-	-	1,026,503
Salaries, wages and benefits	5	97,887	-	108,276	-	80,077	-	103,400	-	113,133	-	139,143	-	168,469	810,385
Inventory payments	6	25,000	25,000	25,000	25,000	115,000	160,000	160,000	165,000	235,000	420,000	425,000	420,000	420,000	2,620,000
Source deductions and WCB	7	32,073	34,528	300	29,626	80	28,117	300	37,057	80	-	40,317	-	49,925	252,403
Tax remittances	8	-	-	-	-	-	-	-	16,935	9,593	-	-	41,129	-	67,557
Bank charges	9	13,985	-	-	-	8,880	-	-	-	24,582	-	-	-	-	47,447
Insurance	9	-	-	1,513	-	-	-	1,513	-	-	-	1,513	-	-	4,540
Telephone and utilities	9	-	-	6,178	-	-	-	6,178	-	-	-	6,178	-	-	18,534
Overhead costs	9	6,889	1,350	3,050	1,350	6,139	1,350	2,300	1,350	6,139	1,350	2,300	1,350	2,300	37,217
Marketing expenses	9	704	704	704	704	1,224	1,613	1,613	1,613	2,358	4,220	4,220	4,220	4,220	28,117
Webshop costs	9	750	750	750	750	750	750	750	750	750	750	750	750	750	9,750
Contingency		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	65,000
Total disbursements		565,111	67,332	150,770	62,430	518,198	196,830	281,055	227,705	739,365	431,320	624,421	472,449	650,664	4,587,651
Net cash flow before professional fees and payments to secured creditors		(409,206)	88,573	5,135	93,476	(247,070)	160,715	76,490	129,840	(216,785)	503,848	310,747	462,719	284,505	1,242,986
Professional fees	10	75,000	-	-	-	45,000	-	-	-	115,000	-	-	-	-	235,000
Loan repayments - principal and interest		-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total professional fees and payments to secured creditors		75,000	-	-	-	45,000	-	-	-	115,000	-	-	-	-	235,000
Net cash flow after professional fees and payments to secured creditors		(484,206)	88,573	5,135	93,476	(292,070)	160,715	76,490	129,840	(331,785)	503,848	310,747	462,719	284,505	1,007,986
Opening balance		939,723	455,517	544,090	549,225	642,700	350,630	511,345	587,835	717,675	385,890	889,738	1,200,485	1,663,204	939,723
Ending balance		455,517	544,090	549,225	642,700	350,630	511,345	587,835	717,675	385,890	889,738	1,200,485	1,663,204	1,947,709	1,947,709

Notes to the cash flow forecast:

- The Consolidated Cash Flow Forecast (the "Cash Flow Forecast") was prepared by the Company, with the assistance of KPMG Inc. acting in its capacity as Proposal Trustee under the Notice of Intention to make a Proposal (the "NOI"). The Company has prepared the Cash Flow Forecast on a consolidated basis due to the nature of their operations which are comingled and intertwined.
- The Cash Flow Forecast is based on unaudited information, solely for the purpose of projecting cash receipts and disbursements of the Company during the NOI. The Cash Flow Forecast was prepared primarily based on historical trends. The actual timing and amount of receipts and disbursements may vary from the Cash Flow Forecast and the variances may be material.
- Sales have been forecasted monthly primarily based on historical trends. The sales are prorated by the day to determine the weekly forecast.
- Occupation costs include rent payments (including base rent, common area maintenance and taxes). Assumed leases for 9 locations to be disclaimed in early October.
- Salaries, wages and benefits relate to the Company's sales and administrative employees and are paid on a bi-weekly basis. To date, 13 employees have been laid off and approximately 43 layoffs will occur after store closures are completed.
- Inventory payments refers to amounts used to purchase inventory. The Cash Flow Forecast does not include any payment of accounts payable arrears for the period before the filing of the NOI.
- Source deductions and WCB include necessary remittances related to Salaries, wages and benefits.
- Tax remittances include GST, HST and other provincial taxes accrued subsequent to the commencement of the NOI.
- Operating costs include bank charges, insurance, telephone and utilities, marketing expenses, webshop costs and other miscellaneous operating expenses.
- Professional fees include payments to the Company's legal counsel, the Proposal Trustee and its legal counsel.

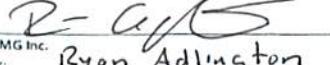
Dated October 5, 2017.


 1031084 ALBERTA LTD.
 Per:


 623735 SASKATCHEWAN LTD.
 Per:

DANIEL MYSAK: Director

TERRA MYSAK: Director


 KPMG Inc.
 Per: Ryan Adlington
 Senior Vice President

APPENDIX “B”

Management’s Representation Letter

District of: Saskatchewan
Division No. 02 - Saskatoon
Court No. 23-2299690
Estate No. 23-2299690

- FORM 30 -
Report on Cash-Flow Statement by the Person Making the Proposal
(Paragraphs 50(6)(c) and 50.4(2)(c) of the Act)

In the matter of the proposal of
623735 Saskatchewan Ltd.
of the City of Saskatoon, in the Province of Saskatchewan

I, 623735 Saskatchewan Ltd., have developed the assumptions and prepared the attached statement of projected cash flow of the insolvent person, as of the 5th day of October 2017, consisting of the period from October 1st to December 30th 2017.

The hypothetical assumptions are reasonable and consistent with the purpose of the projection described in the notes attached, and the probable assumptions are suitably supported and consistent with the plans of the insolvent person and provide a reasonable basis for the projection. All such assumptions are disclosed in the notes attached.

Since the projection is based on assumptions regarding future events, actual results will vary from the information presented, and the variations may be material.

The projection has been prepared solely for the purpose described in the notes attached, using a set of hypothetical and probable assumptions set out in the notes attached. Consequently, readers are cautioned that it may not be appropriate for other purposes.

Dated at the City of Saskatoon in the Province of Saskatchewan, this 5th day of October 2017.



623735 Saskatchewan Ltd.
Debtor

TERRA MYSAK - Director

Name and title of signing officer

District of: Alberta
Division No. 02 - Calgary
Court No. 25-2299607
Estate No. 25-2299607

- FORM 30 -
Report on Cash-Flow Statement by the Person Making the Proposal
(Paragraphs 50(6)(c) and 50.4(2)(c) of the Act)

In the matter of the proposal of
1031084 Alberta Ltd.
of the City of Calgary, in the Province of Alberta

I, 1031084 Alberta Ltd., have developed the assumptions and prepared the attached statement of projected cash flow of the insolvent person, as of the 5th day of October 2017, consisting of the period from October 1st to December 30th 2017.

The hypothetical assumptions are reasonable and consistent with the purpose of the projection described in the notes attached, and the probable assumptions are suitably supported and consistent with the plans of the insolvent person and provide a reasonable basis for the projection. All such assumptions are disclosed in the notes attached.

Since the projection is based on assumptions regarding future events, actual results will vary from the information presented, and the variations may be material.

The projection has been prepared solely for the purpose described in the notes attached, using a set of hypothetical and probable assumptions set out in the notes attached. Consequently, readers are cautioned that it may not be appropriate for other purposes.

Dated at the City of Saskatoon in the Province of Saskatchewan, this 5th day of October 2017.



1031084 Alberta Ltd.
Debtor

DANNY MYSAK Director
Name and title of signing officer