

**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 KK PRECISION INC. (the "**Applicant**")

**FIRST REPORT OF**  
**RICHTER ADVISORY GROUP INC.**  
**IN ITS CAPACITY AS MONITOR OF**  
**KK PRECISION INC.**

June 24, 2014

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monitor of KK Precision Inc. dated June 24, 2014

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**RICHTER**

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**KK PRECISION INC.**

**FIRST REPORT OF RICHTER ADVISORY GROUP INC.,  
IN ITS CAPACITY AS MONITOR OF  
KK PRECISION INC.**

**JUNE 24, 2014**

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FIRST REPORT OF RICHTER ADVISORY GROUP INC.  
In its capacity as Monitor of KK Precision Inc.

June 24, 2014

**Introduction**

1. On May 30, 2014, the *Ontario* Superior Court of Justice (Commercial List) (the "Court") issued an order (the "Initial Order") granting KK Precision Inc. (the "Company") protection pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "CCAA"). Pursuant to the Initial Order, Richter Advisory Group Inc. ("Richter") was appointed the Company's monitor (the "Monitor"). The Initial Order provided the Company with, *inter alia*, a stay of proceedings until June 29, 2014 (the "Stay Period"). The proceedings commenced by the Company under the CCAA are herein referred to as the "CCAA Proceedings".
2. The principal purpose of the CCAA Proceedings is to allow the Company to implement an orderly wind-down of its operations. The orderly wind-down includes production activities for a period of time to, among other things, permit key customers the opportunity to source alternative supply, and to carry out a process to solicit offers from interested parties to purchase the Company's business and/or assets with a view to maximizing value for all stakeholders.

**Purposes of this Report**

3. The purpose of this report ("Report") is to provide information to this Court in respect of the following:
  - (a) The Company's activities since the issuance of the Initial Order;
  - (b) The Accommodation Agreement dated June 24, 2014 between the Company, Siemens Energy Inc. ("Siemens"), Bank of Montreal and BMO Capital Partners (together, the "Lenders") (the "Siemens Accommodation Agreement");

- (c) The Accommodation Agreement dated June 19, 2014 between the Company and Pratt & Whitney Canada Corp. ("Pratt"), (the "Pratt Accommodation Agreement" and together with the Siemens Accommodation Agreement, the "Accommodation Agreements");
- (d) The Monitor's activities since the issuance of the Initial Order;
- (e) The Company's actual cash flows for the period from May 10, 2014 to June 13, 2014, including a comparison of actual to forecast results;
- (f) The process commenced by the Company to solicit offers for the Company's business and/or assets (the "Solicitation Process");
- (g) The Company's request for an extension of the Stay Period to September 19, 2014; and
- (h) Recommend that this Honourable Court make an order:
  - Ratifying the Solicitation Process;
  - Approving the Siemens Accommodation Agreement;
  - Approving the Pratt Accommodation Agreement;
  - Approving the redaction of the sensitive commercial information in the Accommodation Agreements and sealing the unredacted Accommodation Agreements together with the schedules attached thereto; and
  - Granting the Company's request for an extension of its stay of proceedings from June 29, 2014 to September 19, 2014.

#### **Terms of Reference**

4. In preparing this Report, the Monitor has relied on unaudited financial information prepared by the Company's representatives, the Company's books and records, discussions with management and discussions with the Company's advisors. The Monitor has not conducted an audit or other verification of such information.
5. Unless otherwise stated, all monetary amounts noted herein are expressed in Canadian dollars.



### The Company's Activities since the Issuance of the Initial Order

6. Details of the Company's activities since the commencement of the CCAA Proceedings are set out in the affidavit of Garth Wheldon sworn June 24, 2014, filed in support of the Company's motion returnable June 25, 2014 (the "June 24 Wheldon Affidavit").
7. A summary of the Company's activities include:
  - (a) Meeting and corresponding with employees regarding the CCAA Proceedings;
  - (b) Continuing to manufacture component parts and supply goods to Rolls-Royce Canada Limited and Rolls-Royce Power Engineering PLC (together, "Rolls Royce") in accordance with the terms of an accommodation agreement between Rolls Royce and the Company approved in the Initial Order (the "Rolls Royce Accommodation Agreement");
  - (c) Preparing weekly production reports for Rolls Royce in accordance with the Rolls Royce Accommodation Agreement;
  - (d) Meeting and corresponding with the Company's other customers, including Siemens and Pratt, to address current production requirements and develop workable schedules for the production of customer parts taking into consideration the Company's available resources;
  - (e) Negotiating the Accommodation Agreements (as discussed further below);
  - (f) Communicating with the new landlord for the Company's premises located at 104 Oakdale Road, Toronto, Ontario (the "Premises"), 2215225 Ontario Inc. ("2215225" or the "Landlord") regarding the Company's lease, which expires on September 30, 2014;
  - (g) Communicating with key suppliers to secure goods and services during the CCAA Proceedings and to address payment terms;
  - (h) Responding to calls and enquiries from creditors and other stakeholders regarding the CCAA Proceedings;
  - (i) Reporting receipts and disbursements;
  - (j) Making payments to suppliers for goods and services received following the issuance of the Initial Order;

- (k) Consulting with the Monitor to develop the Solicitation Process (as discussed further below);  
and
- (l) Working with the Monitor to satisfy information requests of Prospective Purchasers (as defined below) as well as both scheduling and overseeing site visits for Prospective Purchasers to view and inspect the Company's machinery/equipment.

#### **The Accommodation Agreements with Siemens and Pratt**

8. The Company, with the assistance of the Monitor, has been negotiating the Accommodation Agreements that would ensure continued production of component parts for both Siemens and Pratt during the CCAA Proceedings and provide Siemens and Pratt the time necessary to transition the supply of component parts sourced from the Company to alternate suppliers.
9. Certain of the key business terms addressed by the Siemens Accommodation Agreement and the Pratt Accommodation Agreement are summarized below:
  - (a) Confirmation of the amount of accounts receivable owed by Siemens and Pratt respectively to the Company;
  - (b) Expedited payment for amounts owed by Siemens and Pratt to the Company;
  - (c) Confirmation that the Company will continue to produce and ship component parts to Siemens and Pratt during the period of the Accommodation Agreements, including revised pricing for same;
  - (d) Confirmation that the Company will sell to Siemens and Pratt certain raw materials and work-in-process (unfinished) inventory used in the production of their respective component parts;  
and
  - (e) Limitations on Siemens and Pratt's setoff rights against the Company.
10. The Monitor is supportive of the Company's motion for approval of the Accommodation Agreements for the following reasons:
  - (a) They provide a mechanism to maximize the value of the Company's accounts receivable and inventory;

- (b) They provide a framework for the Company to continue to produce component parts for Siemens and Pratt that should allow them to secure alternative production without disruption;
  - (c) They provide a means to fund the Company's operations during the CCAA Proceedings, including the costs of these proceedings; and
  - (d) They provide the framework for the Company to execute an orderly wind-down of its business, including providing the stability required to meet its enhanced short-term production plan and secure payment for component parts shipped in the pre and post-filing periods.
11. A redacted copy of the Siemens Accommodation Agreement (without schedules) and the Pratt Accommodation Agreement (without schedules) are attached as Exhibits "B" and "C" to the June 24 Wheldon Affidavit. As the Accommodation Agreements and the schedules attached thereto include certain sensitive commercial and competitive information, the Company has requested that the unredacted Accommodation Agreements and the schedules attached thereto be filed with the Court on a sealed and confidential basis. In the circumstances, the Monitor believes that it is appropriate for the unredacted Accommodation Agreements and the schedules attached thereto to be filed with the Court on a confidential basis and sealed until further Order of this Court.

**The Monitor's Activities since the Issuance of the Initial Order**

12. Since the date of the Initial Order, the Monitor's activities have included:
- (a) Arranging for notice of the CCAA Proceedings to be published in the Monday, June 9, 2014 edition of the National Post, as required pursuant to the Initial Order;
  - (b) Sending a notice, within 5 days of the issuance of the Initial Order, of the CCAA Proceedings to all known creditors of the Company;
  - (c) Establishing a website at [www.richter.ca/en/insolvency-cases/k/kk-precision-inc](http://www.richter.ca/en/insolvency-cases/k/kk-precision-inc), where all materials filed with the Court, and all orders made by the Court in connection with the CCAA Proceedings, will be available in electronic form;
  - (d) Implementing procedures for the monitoring of the Company's cash flows and for ongoing reporting of variances to the Cash Flow Forecast (as hereinafter defined);

- (e) Assisting the Company in preparing communications to its employees regarding the CCAA Proceedings and participating in a meeting with the Company's management team and employees on June 2, 2014 to discuss the CCAA Proceedings, including its impact on employees;
- (f) Assisting the Company in preparing its weekly report to Rolls Royce in accordance with the terms of the Rolls Royce Accommodation Agreement, including an analysis of the production status for component parts to be delivered to Rolls Royce;
- (g) Collecting and dispersing monies received, in trust, from Rolls Royce to the Company in accordance with the terms of the Rolls Royce Accommodation Agreement;
- (h) Assisting the Company in its discussions and negotiations with both Siemens and Pratt regarding the terms of the Accommodation Agreements;
- (i) Considering processes to market the Company's business and/or assets for sale and assisting the Company in developing the Solicitation Process and communications with interested parties;
- (j) Attending frequently at the Company's premises and meeting with the Company's management team to discuss the Company's operations and the CCAA Proceedings;
- (k) Corresponding and communicating extensively with the Company and its legal counsel;
- (l) Corresponding and communicating with the Lenders and their legal counsel;
- (m) Responding to calls and enquiries from creditors and other stakeholders regarding the CCAA Proceedings; and
- (n) Preparing this Report.

**Cash Flow for the Period from May 10, 2014 to June 13, 2014**

13. The Company's cash flow projection for the period May 10, 2014 to September 19, 2014 (the "Cash Flow Forecast") was filed with the Court as part of the Company's CCAA application materials.

14. A comparison of the Company's budget to actual results for the week ending June 13, 2014 is summarized below:

<b>KK Precision Inc.</b>			
<b>Cash Flow Variance Analysis</b>			
<b>5 Weeks Ended June 13th</b>	<b>Forecast</b>	<b>Actual</b>	<b>Variance</b>
<b>(\$000's)</b>	<b>13-Jun</b>	<b>13-Jun</b>	<b>\$</b>
<b><u>Cash Receipts</u></b>			
Operating Cash Receipts	\$ 2,476	\$ 1,826	\$ (650)
Other	23	-	(23)
<b>Total Cash Receipts</b>	<b>\$ 2,499</b>	<b>\$ 1,826</b>	<b>\$ (673)</b>
<b><u>Cash Disbursements</u></b>			
Operating Expenses	(195)	(100)	95
Payroll & Benefits	(420)	(402)	18
Retention Payments	(23)	(46)	(23)
Rent & Property Taxes	(223)	(223)	-
Utilities & Insurance	(39)	(6)	33
Sales Tax Remittances	-	-	-
Professional Fees	(150)	(55)	95
Other	(123)	-	123
<b>Total Disbursements</b>	<b>\$ (1,173)</b>	<b>\$ (832)</b>	<b>\$ 341</b>
<b>Net Cash Flow</b>	<b>\$ 1,326</b>	<b>\$ 994</b>	<b>\$ (332)</b>
<b>Cash - Opening Balance</b>	<b>\$ 432</b>	<b>\$ 510</b>	<b>\$ 78</b>
<b>Cash - Closing Balance</b>	<b>\$ 1,758</b>	<b>\$ 1,504</b>	<b>\$ (254)</b>

15. As reflected in the above summary table, the Company generated net cash flow of approximately \$994,000 and had approximately \$1.5 million on hand, net of outstanding cheques, as at June 13, 2014.
16. The principal reasons for the unfavourable net cash flow variance are:
- (a) The negative variance of approximately \$673,000 in receipts is due primarily to timing differences related to the delivery of manufactured component parts for Rolls Royce and delays in finalizing the Accommodation Agreements. The Company expects that these negative variance will reverse in the coming months; and
  - (b) The positive variance of approximately \$341,000 in disbursements is due primarily to lower than projected operating expenses and timing differences related to the payment of certain other expenses, including professional fees.

17. The Monitor is of the view that the Company is acting in a manner consistent with its Cash Flow Forecast and there have been no material adverse changes to the Company's operations since the commencement of the CCAA Proceedings.

#### **The Solicitation Process**

18. As noted in the affidavit of George Koulakian sworn May 28, 2014 in support of the Company's CCAA application (the "May 28 Koulakian Affidavit"), as a result of the Company's deteriorating financial position, on December 30, 2013, the Company retained Richter to develop strategic alternatives, which included seeking potential financing, an equity investment and/or going concern sale opportunities.
19. As also noted in the May 28 Koulakian Affidavit, a sales process was launched in February 2014 with a view to identifying an investor and/or buyer for the Company's business (the "Initial Sales Process"). As part of the Initial Sales Process, 57 potential interested parties, including strategic purchasers (competitors, suppliers, companies operating in complementary businesses, etc.) and financial buyers (equity investors with an interest in businesses of a similar profile to the Company) were contacted.
20. Although the Initial Sales Process generated interest from several interested parties, the Initial Sales Process did not result in any firm deal for the Company's business and/or assets.
21. Given the recent completion of the Initial Sales Process and the Company's limited liquidity, the Company, with the assistance of the Monitor, commenced the Solicitation Process as a means of quickly determining whether a transaction that would result in greater than forced liquidation value was available.
22. The purpose of the Solicitation Process is to identify one or more purchasers for the Company's business and/or assets. The objective is to complete a transaction by the end of July 2014, or as soon as possible thereafter. The Solicitation Process is summarized as follows:
  - (a) The Company, in consultation with the Monitor, assembled a list of potential interested parties, including many of the strategic/financial parties that participated in the Initial Sales Process and parties that regularly liquidate assets in insolvency proceedings (collectively, the "Prospective Purchasers");

- (b) On June 16, 2014, the Company distributed an offer solicitation letter to the Prospective Purchasers detailing the opportunity to purchase the Company's business and/or assets (the "Offer Solicitation Letter"). In addition to the Offer Solicitation Letter, Prospective Purchasers were also provided with a detailed listing of the Company's machinery/equipment, including specifications for same (the "Asset List"). A copy of the Offer Solicitation Letter, including the Asset List, is attached as Exhibit "A" to the June 24 Wheldon Affidavit;
  - (c) Prospective Purchasers interested in obtaining additional information regarding the Company's business will be required to execute a confidentiality agreement;
  - (d) The Company, with the assistance of the Monitor, will facilitate due diligence efforts by, among other things, coordinating meetings between Prospective Purchasers and the Company and/or scheduling site visits to view and inspect the Company's machinery/equipment;
  - (e) Prospective Purchasers are required to submit offers for the Company's assets, en bloc, on or before 5:00 p.m. (Eastern Standard Time) on July 7, 2014;
  - (f) The Company, in consultation with the Monitor, will evaluate all offers and may seek clarifications and/or re-bidding of certain offers;
  - (g) The successful offeror will be required to remove all purchased assets from the Premises by no later than September 30, 2014; and
  - (h) Any sale of the Company and/or its assets will be subject to the approval of this Honourable Court, which will be sought by the Company prior to the end of July 2014 or as soon as practical thereafter, following completion of a definitive agreement.
23. The Monitor notes that the proposed time-frame is condensed but, as noted above, the Company's assets have already been extensively marketed in the Initial Sales Process. In addition, the proposed time frame is necessary to provide the successful bidder with time to coordinate the removal of all purchased assets from the Premises by no later than September 30, 2014, as the Company's lease for the Premises expires on September 30, 2014.
24. As noted in the May 28 Koulakian Affidavit, the lease for the Premises expired on April 30, 2014 and the Company negotiated a lease extension which runs until September 30, 2014. Subsequent to entering into the lease extension, the Premises were sold to 2215225.

25. In consideration of the timeframe to vacate the Premises following the completion of its production activities, which are expected to run until August 31, 2014 at the latest, the Company and the Monitor approached the Landlord regarding a possible one-month lease extension for the Premises. On June 16, 2014, the Landlord informed the Company of the terms upon which it would agree to a one-month lease extension to October 31, 2014, which terms were unacceptable to the Company. On June 19, 2014, the Company was informed by the Landlord that it was not prepared to consider a further lease extension beyond September 30, 2014, as the Landlord had other uses for the Premises that are expected to commence October 1, 2014.
26. As a result, the Monitor believes that the deadlines proposed in the Solicitation Process are reasonable in the circumstances. The Monitor will report back to this Honourable Court if facts or circumstances require the Company or the Monitor to re-evaluate the time periods or the Solicitation Process.

**The Company's Request for an Extension of the Stay of Proceedings to September 19, 2014**

27. The current Stay Period expires on June 29, 2014. The Company is seeking an extension of the Stay Period to September 19, 2014. The Monitor is of the view that the extension to the Stay Period is appropriate in the circumstances and supports the Company's request for an extension of the Stay Period for the following reasons:
  - (a) The Company has acted and is acting in good faith and with due diligence;
  - (b) The granting of the extension should not prejudice any employee or creditor, as the Company is projected to have sufficient funds to pay post-filing services and supplies, as contemplated by the Cash Flow Forecast, which extends to September 19, 2014. The Company is of the view that the Cash Flow Forecast remains appropriate and reflects management's expectation of the Company's receipts and disbursements for the period of the forecast. As a result, a revised cash flow forecast has not been prepared;
  - (c) The Rolls Royce Accommodation Agreement as well as the Siemens Accommodation Agreement and the Pratt Accommodation Agreement contemplate the continued production of component parts by the Company until August 30, 2014;
  - (d) It will allow for the Solicitation Process to be substantially advanced;



(e) The extension would be contemporaneous with the Company's proposed wind-down period;  
and

(f) The Lenders support the extension.

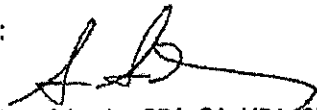
**Monitor's Conclusions and Recommendations**

28. Based on the foregoing, the Monitor respectfully recommends that this Honourable Court make the Order(s) granting the relief detailed in paragraph 3(h) of this Report.

All of which is respectfully submitted this 24<sup>th</sup> day of June, 2014.

**Richter Advisory Group Inc.**  
in its capacity as Monitor of  
**KK Precision Inc.**

Per:



Andrew Adessky, CPA, CA, MBA, CIRP

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