Of No. S209201
Vancouver Registry

IN THE SUPREME COURT OF BRITISH COLUMBIA

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT,*
R.S.C. 1985, c. C-36, AS AMENDED

AND

IN THE MATTER OF MOUNTAIN EQUIPMENT COOPERATIVE AND
1314625 ONTARIO LIMITED

PETITIONERS

SECOND REPORT OF THE MONITOR

ALVAREZ & MARSAL CANADA INC.

OCTOBER 19, 2020

A&M
ALVAREZ & MARSAL

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APPENDICES

1.0 INTRODUCTION

1.1 On September 14, 2020, Mountain Equipment Cooperative and 1314625 Ontario Limited (together, the "**Petitioners**" or "**MEC**") were granted an initial order (the "**Initial Order**") by the Supreme Court of British Columbia to commence proceedings (the "**CCAA Proceedings**") under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "**CCAA**"). Among other things, the Initial Order afforded MEC an initial stay of proceedings up to and including September 24, 2020 (the "**Stay Period**") and appointed Alvarez & Marsal Canada Inc. ("**A&M**") as monitor of MEC (the "**Monitor**") during the CCAA Proceedings.

1.2 On September 22, 2020, the Petitioners filed an application (the "**Comeback Application**") to, among other things, seek an amended and restated initial order (the "**ARIO**") and sale approval and vesting order (the "**SAVO**") to approve the sale transaction (the "**Sale Transaction**") contemplated by the asset purchase and sale agreement between the Petitioners and 1264686 B.C. Ltd. (the "**Original Purchaser**") dated September 11, 2020 (the "**APA**") for the sale of the Purchased Assets and to vest all of the Purchased Assets in the Original Purchaser's permitted assignee free and clear of any Encumbrances other than Permitted Encumbrances, as such capitalized terms are defined in the APA

1.3 On September 24, 2020, this Honourable Court granted an extension of the Stay Period from September 24, 2020 to September 28, 2020 to allow for the Comeback Application to be heard on September 28, 2020.

1.4 During the period from September 28, 2020 through to October 1, 2020, in addition to hearing the Comeback Application of the Petitioners, the Court heard applications by Plateau Village Properties Inc. and Midtown Plaza Inc. (together, the "**Landlords' Application**"), Kevin Harding and Save MEC (together, the "**Members' Application**"), and the BC Co-op Association and Mutuals Canada (the "**Public Intervenors' Application**").

1.5 On October 2, 2020, this Honourable Court dismissed the orders sought under the Landlords' Application, Members' Application and Public Intervenors' Application and granted the following orders sought by the Petitioners:

a) the ARIO which amended and restated the Initial Order to, *inter alia*:
   i. extend the Stay Period to November 3, 2020;
   ii. authorize an increased maximum amount of borrowing under the Interim Financing Facility to $100 million;

iii. approve a key employee retention plan and grant a charge against the assets of the Petitioners in an amount not to exceed $778,000 to secure the Petitioners' obligations thereunder; and

b) the SAVO.

1.6 On October 16, 2020, the Petitioners filed an application seeking approval of an assignment order (the "**Assignment Order**") to assign all of the rights and obligations of the Petitioners under certain Remaining Contracts (subsequently defined) to the Original Purchaser's assignee, 1266524 B.C. Ltd. (the "**Purchaser**"). As a condition of the assignment of the Remaining Contracts, all monetary defaults shall be paid by the Purchaser (the "**Cure Costs**") to the counterparties to the Remaining Contracts.

1.7 Further information regarding these CCAA Proceedings, including the Initial Order, the ARIO, affidavits, reports of the Monitor and all other Court-filed documents and notices are available on the Monitor's website at www.alvarezandmarsal.com/mec (the "**Monitor's Website**").

2.0 PURPOSE

2.1 This second report (the "**Second Report**") has been prepared by the Monitor to provide information to this Honourable Court in respect of the following:

a) the activities of the Monitor since the First Report of the Monitor dated September 24, 2020 (the "**First Report**");

b) an overview of assignments or amendments of real estate leases and contracts that the Petitioners have pursued either by consent and/or by way of the Assignment Order;

c) a comparison of actual receipts and disbursements compared to the CCAA Cash Flow Forecast appended to the Pre-filing Report of the Monitor dated September 13, 2020 (the "**Pre-filing Report**") during the period September 15, 2020 to October 11, 2020; and

d) the recommendations of the Monitor in respect of the foregoing, as applicable.

2.2 The Second Report should be read in conjunction with the supporting affidavit of Philippe Arrata sworn October 15, 2020 and the First Report. Background information, including capitalized terms not defined herein, are contained in the Initial Order, the ARIO, the SAVO, and the Monitor's previous reports, and have not been repeated herein.

3.0 TERMS OF REFERENCE

3.1 In preparing this report, A&M has necessarily relied upon unaudited financial and other information supplied, and representations made to it, by certain senior management of MEC

("**Management**") and the Purchaser's legal counsel, Fasken Martineau DuMoulin LLP. Although this information has been subject to review, A&M has not conducted an audit nor otherwise attempted to verify the accuracy or completeness of any of the information prepared by Management or otherwise provided by the Petitioners or other third parties. Accordingly, A&M expresses no opinion and does not provide any other form of assurance on the accuracy and/or completeness of any information contained in this Second Report, or otherwise used to prepare this Second Report.

3.2 Certain of the information referred to in this Second Report consists of financial forecasts and/or projections prepared by Management and the Purchaser. An examination or review of financial forecasts and projections and procedures as outlined by the Chartered Professional Accountants of Canada has not been performed. Readers are cautioned that since financial forecasts and/or projections are based upon assumptions about future events and conditions that are not ascertainable, actual results will vary from those forecasts and/or projected and the variations could be significant.

4.0 ACTIVITIES OF THE MONITOR

4.1 The activities of the Monitor since the First Report have included the following:

Review of CCAA Court Materials

a) reviewing draft Court application materials and providing comments to MEC's legal counsel;

Reviewing Materials in Connection with Advancing the Sale Transaction

b) reviewing documentation, in consultation with MEC and its legal counsel and the Monitor's legal counsel, in respect of assigned Real Property Leases, Material Contracts, Personal Property Leases and corresponding Cure Costs;
c) holding discussions with MEC's legal counsel, Management, the Special Committee, and the MEC Board in respect of matters related to the Sale Transaction;
d) reviewing the draft net working capital adjustments forecast at closing of the Sale Transaction and attending to discussions with Management regarding same;

Monitoring of Cash Receipts & Disbursements

e) reviewing and approving the weekly covenant threshold reporting required pursuant to the terms of the Restructuring Support Agreement between the Lenders and MEC dated September 11, 2020 (the "**RSA**") and attending to weekly meetings with FTI, advisor to the Agent, and Management;

f) reviewing weekly funding requests under the Interim Financing Facility prepared by Management and attending to discussions regarding same;

Statutory and Other Responsibilities

g) posting filed court materials and other relevant information as they become available to the Monitor's Website;

h) preparing this Second Report;

Communication Matters

i) conducting ongoing discussions with the Monitor's legal counsel, Management, the Petitioners' legal counsel, financial advisor to the Agent, and other stakeholders, among others, to discuss various matters;

j) attending to various discussions with the members of the MEC Board, Management, and the Petitioners' legal counsel regarding the process of communications to employees, vendors, MEC members and other interested parties;

k) reviewing draft communications prepared by Management in respect of employee terminations as well as follow up communications;

Creditor and Other Stakeholder Matters

l) receiving approximately 359 telephone and email inquiries as of October 11, 2020 from trade creditors, MEC members, employees and other parties. The Monitor continues to track and log these inquiries and has addressed the queries where required;

m) holding discussions and liaising with Management, the MEC Board, and the Special Committee in respect of the CCAA Proceedings and related matters generally;

n) holding discussions with Management, the Special Committee and counsel to MEC to discuss handling of member and customer data in accordance with privacy laws and regulations; and

Other Matters

o) coordinating and holding discussions with Management regarding transition and post-closing matters.

5.0 ASSIGNMENT OF LEASES AND CONTRACTS

5.1 Pursuant to the APA, the Petitioners are to use commercially reasonable efforts, as directed by and in cooperation with the Purchaser, to obtain the written consent of the counterparties to the various contracts that are included in the Purchased Assets (where consent to an assignment is required) to the assignment of those contracts to the Purchaser, which include:

a) 16 real property leases, including 15 of MEC's retail locations and the distribution centre located in Brampton, Ontario (the "**Real Property Leases**");
b) 27 assumed contracts, including IT related contracts and agreements with key apparel suppliers (the "**Material Contracts**"); and
c) 59 personal property leases (the "**Personal Property Leases**")

(collectively, the "**Consent Required Contracts**").

5.2 The Purchaser continues to review the Consent Required Contracts and possible additions thereto. The total number of Consent Required Contracts may be updated prior to the hearing to approve same.

5.3 On October 1, 2020, the Petitioners, in consultation with the Purchaser and the Petitioners' legal counsel, delivered to the counterparties to the Consent Required Contracts a letter requesting consent to assignment to the Purchaser and advising that if consent was not obtained, the Petitioners would be required to seek a court order assigning the applicable contract under the CCAA.

5.4 As at the date of this Second Report, the Petitioners have received consents (executed and/or conditional) to assignments or amendments from all the counterparties to the Real Property Leases (the "**Real Property Lessors**") and the Purchaser has correspondingly negotiated and/or is in the process of negotiating amended lease agreements with the Real Property Lessors. In addition to the 16 real property leases, the Purchaser will continue to maintain the 6 owned retail locations and 1 owned distribution centre located in Surrey, British Columbia for a total of 21 retail locations and two distribution centres.

5.5 The Petitioners have not obtained consents for 79 of the Consent Required Contracts, as disclosed in Schedule B of the Assignment Order (the "**Remaining Contracts**") and is seeking approval from this Honourable Court to assign the Remaining Contracts to the Purchaser in accordance with s. 11.3 of the CCAA after which the Purchaser shall pay the applicable Cure Costs.

5.6 The Monitor understands that the relatively large number of consents that remain outstanding is not a result of counterparties opposing the assignment of the Remaining Contracts but rather because no result has been received from those counterparties to date.

5.7 The Monitor is of the opinion that the assignment of the Remaining Contracts appears to be appropriate and commercially reasonable in the circumstances when considering the factors referenced in s. 11.3 of the CCAA. In particular, the Monitor notes the following factors in consideration of its approval of the assignment of the Remaining Contracts which remain subject to this Honourable Court's approval:

a) the Purchaser and their management team have significant experience in the retail industry, as well as experience with corporate transactions and operations in Canada, and ongoing operations are comprised of a significant number of former employees of MEC which will further its efforts to maintain the MEC business as a going concern and honour the on-going obligations under the Remaining Contracts;
b) the assigned Remaining Contracts (which include equipment and supplier agreements as well as critical service contracts) will be utilized in the Purchaser's operations to generate revenue;
c) the assignment of the Remaining Contracts would satisfy the APA and is necessary for the timely closure of the transaction and provides continued employment and/or retention of approximately 91% of active employees and 21 of 22 retail stores;
d) the Purchaser appears to have the ability and financial wherewithal to perform its obligations under the Remaining Contracts, including payment of the Cure Costs. During Phase 2 of the sale and investment solicitation process leading to the Sale Transaction, the Purchaser submitted, as part of its final bid, two letters dated August 28, 2020 and September 11, 2020 outlining its equity commitment and confirming that the source of funding for the Sale Transaction will not require debt financing. The Purchaser through its legal counsel has provided a subsequent letter dated October 16, 2020, as attached as Appendix "**A**", containing additional projected financial information to support its financial position post-closing; and
e) the Petitioners, in conjunction with the Purchaser, have been working diligently and in good faith to obtain consent from the counterparties to the Consent Required Contracts to effect the closing of the Sale Transaction within the timelines contemplated by the APA.

5.8 For the reasons listed above, the Monitor is in support of the assignment of the Remaining Contracts.

6.0 ACTUAL CASH FLOW RESULTS COMPARED TO CCAA CASH FLOW FORECAST

6.1 Pursuant to the RSA and consistent with the ongoing oversight and monitoring of the business and financial affairs of MEC, the Monitor has established a weekly cash flow review protocol with the Petitioners and Management to compare actual cash flows against the CCAA Cash Flow Forecast.

6.2 The Petitioners' actual cash receipts and disbursements compared to the CCAA Cash Flow Forecast during the period from September 15, 2020 to October 11, 2020 (the "**Reporting Period**") is summarized below:

Mountain Equipment Co-operative
Cash Flow Variance Analysis
For the Four Week Period from September 15, 2020 to October 11, 2020
(In CAD$000s)

	For the Four Weeks Ended October 11, 2020		
	Actual	**Forecast**	**Variance**
Receipts			
Sales	$ 22,935	$ 21,776	$ 1,159
Canada Emergency Wage Subsidy	5,604	2,467	3,137
Total receipts	**28,539**	**24,243**	**4,296**
Disbursements			
Merchandise	(15,576)	(17,952)	2,376
Freight and other non-merchandise	(1,731)	(2,418)	687
Wages and salary	(5,723)	(5,729)	6
SG&A	(441)	(3,303)	2,862
Rent and property taxes	(1,015)	(1,319)	304
Sales tax	(2,039)	(2,300)	261
Total disbursements	**(26,525)**	**(33,022)**	**6,497**
Net operating cash flow	**2,014**	**(8,779)**	**10,793**
Other disbursements			
Professional fees	(469)	(1,084)	615
Debt service	(649)	(693)	44
Contingency	(197)	(532)	336
Total other disbursements	**(1,314)**	**(2,310)**	**995**
Net Cash Flow	**$ 700**	**$ (11,089)**	**$ 11,788**
Opening Borrowing Balance	**$ (65,119)**	**$ (71,040)**	**$ 5,921**
Surplus/ deficit	700	(11,089)	11,788
FX adjustment	47	-	47
Net pre-funding	(2,393)	63	(2,456)
Ending Borrowing Balance	**(66,765)**	**(82,066)**	**15,300**
Add: LC / LG Utilization	(2,725)	(3,747)	1,022
Ending Borrowing Exposure	**$ (69,490)**	**$ (85,813)**	**$ 16,322**
Continuity of Interim Financing			
Existing Credit Facility			
Opening balance	$ 65,119	$ 71,040	$ 5,921
Less: cash receipts	(28,539)	(24,243)	4,296
Ending Existing Credit Facility balance	**36,580**	**46,797**	**10,217**
Interim Financing Facility			
Opening balance	-	-	-
Draws (repayments)	27,839	35,332	7,492
Net pre-funding	2,393	(63)	(2,456)
FX adjustment	(47)	-	47
Ending Interim Financing Facility balance	**30,185**	**35,269**	**5,083**
LC / LG utilitization	2,725	3,747	1,022
Total Indebtedness	**$ 69,490**	**$ 85,813**	**$ 16,322**

6.3 During the Reporting Period, MEC experienced a net favorable cash flow variance of $11.8 million primarily as a result of the following:

a) receipts were approximately $4.3 million higher than forecast due to higher than anticipated sales and favorable timing differences with respect to receipt of the Canada Emergency Wage Subsidy;
b) merchandise and freight and non-merchandise costs were collectively $3.0 million lower than forecast due to timing differences;
c) SG&A costs were $2.9 million lower than forecast due to both permanent and timing differences resulting from the deferral and/or discontinuation of certain services; and
d) rent and property taxes and sales taxes were collectively $565,000 lower than forecast due to timing differences.

6.4 As discussed in the Monitor's Pre-filing Report and First Report, MEC has been granted access to an Interim Financing Facility providing near-term liquidity to the Petitioners to operate in the normal course. As at October 11, 2020, MEC has drawn $30.2 million under the Interim Financing Facility.

6.5 Concurrently and in accordance with the terms of the Interim Financing Facility, all cash receipts collected by MEC and totaling $28.5 million during the Reporting Period have been applied against the balance of the Existing Credit Facility. As at October 11, 2020, the balance of the Existing Credit Facility totaled $36.6 million.

6.6 As at October 11, 2020, the combined total indebtedness of the Petitioners to the Lenders was $16.3 million lower than forecast and totaled $69.5 million, including letters of credit and/or guarantees of $2.7 million.

6.7 Since the First Report, the Monitor has continued to review the cash receipts and disbursements of the Petitioners and has been involved in the weekly review of the covenant tests and reporting to the Agent and its advisor, as required under the RSA. Nothing has come to the attention of the Monitor that causes the Monitor to believe that there have been material adverse changes in the cash flow of MEC or that would financially prejudice the stakeholders of MEC.

7.0 RECOMMENDATIONS

7.1 The Monitor respectfully recommends that this Honourable Court grant the Assignment Order being sought by the Petitioners.

*****

All of which is respectfully submitted to this Honourable Court this 19th day of October, 2020.

Alvarez & Marsal Canada Inc.,
in its capacity as Monitor of
MEC and not in its personal or corporate capacity

Todd M. Martin
Senior Vice President

Appendix A

Letter dated October 16, 2020 from Fasken Martineau DuMoulin LLP

FASKEN

Fasken Martineau DuMoulin LLP
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October 16, 2020
File No.: 323434.00001/18295

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Via Email

Howard Gorman
Norton Rose Fulbright Canada LLP
400 3rd Avenue SW, Suite 3700
Calgary, AB T2P 4H2

Dear Mr. Gorman:

Re: Asset purchase agreement dated September 11, 2020 (the "Asset Purchase Agreement") between 1264686 B.C. Ltd (the "Original Purchaser") and Mountain Equipment Co-operative and 1314625 Ontario Limited (together, the "Seller")

As you are aware, we are counsel to the Original Purchaser and counsel to 1266524 B.C. Ltd., a permitted assignee of the Original Purchaser under the Asset Purchase Agreement (the "**Purchaser**"). Capitalized terms used herein and not otherwise defined shall have the meaning ascribed to them in the Asset Purchase Agreement.

Pursuant to the Asset Purchase Agreement, the Seller will be seeking an Assignment Order. In connection therewith, the Seller has requested that the Purchaser provide evidence that it would be able to perform the obligations under the Assumed Contracts which are to be the subject of the Assignment Order.

In this regard, on behalf of the Purchaser, please find attached hereto a projected opening balance sheet for the Purchaser as of November 2, 2020, reflecting an opening availability of not less than $38 million under its various credit facilities, with total liquidity of $47 million including unrestricted cash on the balance sheet, as of November 2, 2020.

Yours very truly,

FASKEN MARTINEAU DuMOULIN LLP

Dylan Chochla

DC/mt
Enclosure

Projected Opening Balance Sheet	
C$s	**Estimated 11/2/2020**
Assets	
Cash	9,500,000
Accounts Receivable	888,640
Inventories	80,268,022
Prepaids & Other	2,148,507
Current Assets	**92,805,169**
PP&E	132,218,793
Investments	191,053
Total Assets	**225,215,015**
Liabilities & Equity	
Accounts Payable	23,372,197
Other Payables	19,806,924
Gift Cards and Returns Allowance	13,187,479
Current Liabilities	**56,366,599**
New Debt	20,000,000
Capital Lease Obligations	36,153,180
Other Liabilities	11,471,609
Total Liabilities	**123,991,388**
Total Equity	101,223,627
Total Liabilities & Equity	**225,215,015**

Projected Liquidity Summary	
Cash	9,500,000
Credit Facility Availability	37,829,025
Projected Total Liquidity	**47,329,025**