

**IN THE SUPREME COURT OF BRITISH COLUMBIA
IN BANKRUPTCY AND INSOLVENCY**

BETWEEN:

CIBT Finance (2017) Corp.

Applicant

and

KGIC Inc. and

674143 B.C. Ltd., Cornerstone Academic College of ESL, Teacher Training and Testing Preparation Inc., Cornerstone Language School Ltd., KGIC Business College (2010) Corp., KGIC Business College (BC) Corp., KGIC Language College (2010) Corp., KGIC Language College (BC) Corp., MTI Community College Ltd., Pan Pacific Career College Inc., Pan Pacific College (Toronto) Ltd., Pan Pacific College Inc., PGIC Career College Inc., PGIC Toronto Inc., PGIC Vancouver Studies Inc., PGIC Victoria Studies Inc., Study English in Canada Inc., Study English in Canada (Vancouver) Inc., Upper Career College of Business & Technology (Vancouver) Inc., Upper Career College of Business & Technology Inc., Urban International School Inc., Victoria International Academy of Teacher Training Ltd., Western Town Business College Ltd. and Western Town College Toronto Inc.

Respondents

APPLICATION UNDER SECTION 47(1) OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, C. B-3, AS AMENDED AND SECTION 39 OF THE *LAW AND EQUITY ACT*, R.S.B.C. 1996 C.253, AS AMENDED.

**FIRST REPORT OF BDO CANADA LIMITED, IN ITS
CAPACITY AS COURT APPOINTED INTERIM RECEIVER**

2 February 2017

TABLE OF CONTENTS

BACKGROUND	3
PURPOSE OF THIS REPORT.....	3
CONDUCT OF THE RECEIVER.....	4
RECEIVER'S FINDINGS AND DETERMINATIONS	6
RECEIVER'S GO FORWARD PLAN	8
RECOMMENDATIONS.....	9
Exhibits	
Receiver's Estimated 2017 Cash-flow Projection - Pre-Appointment	A
Interim Manager's Estimated 2017 Cash-flow Projection - 1 February 2017	B

BACKGROUND

1. On 25 January 2017, by order of this Honourable Court (the “Order”), BDO Canada Limited (“BDO” or the “Receiver”) was appointed Interim Receiver of KGIC Inc. and its subsidiaries (collectively the “KGIC Group”).
2. KGIC Inc. through its operating subsidiaries, operates a number of private career and language colleges through several brands in British Columbia and Ontario. The principal brands are “King George International College” which provides language training in Victoria, Vancouver, Surrey and Toronto and “MTI Community College” which provides career training in Vancouver, Surrey, Burnaby and Chilliwack. The Receiver has determined that the KGIC Group currently has some 1,600 students and 342 employees in 18 campuses.
3. On 25 January 2017, CIBT Finance (2017) Corp. (“CF2017”) took an assignment of the Bank of Montreal’s (“BMO”) debt of approximately \$13 million and issued S.244 Notices to enforce its security. For reasons, outlined in the motion material for the Order, CF2017 applied to the Honourable Court for an order appointing an Interim Receiver in order to protect and preserve the assets.

PURPOSE OF THIS REPORT

4. The purpose of this First Report of the Receiver (the “First Report”) is
 - a. to report on
 - i. the conduct of the Receivership over the period from 25 January 2017 to 2 February 2017, as described in this First Report;
 - ii. the Receiver’s findings and determinations to date;
 - iii. the Receiver’s preliminary views on a possible resolution; and
 - b. to seek
 - i. an order expanding the Receiver’s powers in Paragraph 12 of the Order to permit the termination of staff in order to reduce costs;

- ii. an order permitting the Receiver to terminate premise leases in order to reduce costs, and
- iii. an order approving the actions of the Receiver as outlined in this report.

CONDUCT OF THE RECEIVER

5. On 25 January 2017, the Receiver entered into an Interim Management agreement with Sprott-Shaw Degree College Corp. (“Sprott-Shaw”) to provide day-to-day management of the KGIC Group.
6. On Thursday 26 January, representatives of the Receiver attended at the head office location of KGIC Inc. at 55 Town Centre Court 8th floor, Scarborough, the premises of the Toronto Institute of Pharmaceutical Technology in Scarborough, a separate private school owned and operated by Dr. Alex MacGregor, CEO of KGIC Inc. and not part of the KGIC Group. Dr. MacGregor objected to the presence of the Receiver and the Interim Manager on the premises of his school. After negotiations, it was agreed that the Receiver and its staff would be allowed on site and that the Receiver would move quickly to relocate the assets of the KGIC Group on site to another location. Space was identified at one of KGIC’s campuses to which the assets have been moved.
7. The mainframe, however, could not be relocated without rewiring by a third party provider. As a result, the KGIC accounting staff had to remain at the Scarborough location until Tuesday 31 January under the supervision of the Receiver, until the relocation could take place.
8. During this period, the Receiver also worked to obtain information so that we could understand the Accounts Payable, outstanding Payroll, Accounts Receivable, and other information required from the system.
9. As well, the Receiver worked with the KGIC staff and the Interim Receiver to set up procedures for approving go-forward purchases, approving payments, cutting cheques and handling cash.
10. The Receiver identified some 60 bank accounts at various banks for the KGIC Group. It appears that each campus or entity had at least two bank accounts (\$CDN and \$USD). While the Receiver moved to stop all payments from these accounts, it quickly learned

that student funds are wired into these account from offshore. From a review of past cash flow, it appears that on average \$50,000 is deposited into these accounts daily. Though the Receiver has opened its own trust accounts, we were advised that foreign recruiting agents would be slow to update their records and that all of the bank accounts should be left open to receive funds. The Receiver has now set up processes to monitor these accounts and to sweep the funds.

11. The Receiver has identified and provided the Order to all of the landlords.
12. The Receiver has obtained a detailed Accounts Payable listing. Total Accounts Payable as at the date of appointment is \$4,164,400. It appears, however, that KGIC's accounting department did not have payee addresses on record. Cheques were cut and sent to the respective campuses which then mailed out the payments. The Receiver is attempting to gather the addresses from the campuses for any future claims process.
13. On or about 19 January 2017, KGIC Inc. abandoned its original head office to move into shared space in Scarborough. The Receiver learned that, though the computer system had been moved, KGIC had abandoned substantial paper records. Following negotiations with the landlord, the Receiver was able to gain access and remove the records to storage. The Receiver has plans to inventory the records.
14. On Thursday 26 January, the Receiver and the Interim Manager held introductory telephone calls with each of the provincial regulators, the Private Training Institutions Branch ("PTIB") in British Columbia and the Ministry of Training, Colleges and Universities ("MTCU") in Ontario and with the accrediting industry association, Languages Canada (collectively the "Regulators"). The purpose of these calls was to advise the Regulators of the Order, introduce the Receiver and the Interim Manager, outline the situation and the immediate plans and to determine if there were any regulatory matters of which we should be aware. Each of the Regulators had its own concerns and was following up on regulatory matters and concerns. Weekly follow up calls are scheduled.
15. Starting on 26 January, the representatives of the Receiver and the Interim Manager have attended at every campus of the KGIC Group to meet with staff, explain the situation and introduce the Interim Manager. The Receiver's general observation was that most employees welcomed the appointment of the Receiver to stabilize operations

and of the Interim Manager, which was known to them as being a respected operator in the industry.

16. The Receiver and the Interim Manager have set in place processes to approve, fund and pay the most urgent post-Appointment obligations. This includes occupancy rent from the date of appointment, an accelerated post-appointment payroll for employees who were not paid by KGIC Inc. in its regular payroll on 27 January and pre-payment of Homestay providers for newly arriving students.

RECEIVER'S FINDINGS AND DETERMINATIONS

17. Based on the KGIC Inc. SEDAR filings, the Receiver anticipated that the KGIC Group would be in serious financial distress. For example, an analysis of the seven reported quarters in 2015 and up-to-and-including Q3 2016, showed that the KGIC Group had lost money in each quarter and had cumulative negative EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization) in excess of \$20 million. As it turns out, the situation on the ground was more severe than the Receiver had anticipated.
18. The Receiver believes, if there had not been the appointment of an Interim Receiver, the KGIC Group was within two or three weeks of collapsing. In broad terms, revenues covered less 65% of costs. January rents totaling \$409,000 had not been paid, and it was not obvious that February rents of some \$437,000 could be funded. About half the employees were paid in the payroll due on 27 January, with a further \$235,000 remaining due. In fact, the management staff had not been paid for the entire month of January. Many students, especially high school aged students, are housed with HomeStay providers. Many of these providers have not been paid for several months, with some \$263,000 owing, and were refusing to take new students, or, worse, turning out students already in their care. Those that were taking new students were demanding payment in advance.
19. Prior to its appointment, the Receiver drafted a cash flow based on KGIC's year-old projection, making some assumptions about eliminated certain marketing and recruiting costs. This projection (Exhibit "A") estimated a negative cash outflow of approximately \$3 million over the period ending 28 April 2017.
20. With the benefit of access to the KGIC Group's financial information, the Interim Manager has prepared a cash flow projection for the same period (Exhibit "B"). This

cash flow reflects a substantially smaller KGIC Group than the Receiver had projected. Actual payroll is currently 342 individuals, instead of the 426 anticipated, 20% fewer. Even so, this analysis projects a negative cash outflow of \$2.8 million over the same three month period ending 28 April 2017. The effect is a negative cash outflow averaging \$40,000 each and every work day, which the Receiver is having to borrow to fund.

21. The Interim Manager has also reviewed registrations and has projected student enrollment on a weekly basis. At the time of writing, there are 1,536 students. Graduations exceed new enrollments such that only 1,105 students are projected to be enrolled during the week of 28 April 2017. Only after the end of April is total enrollment projected to increase as the number of starts begins to exceed the number of graduations.
22. The Interim Manager, and the KGIC Group campus directors, advise the Receiver that this is in large part because the KGIC Group has not been paying commissions, totaling \$452,000, owing to off-shore recruiting agents, who have therefore been reluctant to send students to KGIC's language schools and because PTIB, the BC provincial regulator, has curtailed the MTI Career Colleges' ability to enroll new students.
23. This projection and the revenue from new students assumes that the schools remain able to recruit students. One of the regulators has suggested informally that the risk to the provincial student support fund has risen, due to the financial position of the KGIC Group, which could result in the stoppage of new student enrollments.
24. The Interim Manager has made a preliminary analysis of the operations of the KGIC Group. It notes that some of the KGIC operations have significant excess capacity. While continuing to offer the same programmes and courses, some campuses within the KGIC Group could be closed. The Receiver notes that some KGIC Group campuses are literally across the street from each other. A restructuring plan has been developed which would result in immediate savings of approximately 20%, chiefly in General and Administration, Rent and Wages, the three biggest costs. The Interim Manager has projected cash flow savings from operations of some \$1.0 million from operations over the three month period to 28 April. As a result the daily negative cash outflow will be reduced to \$27,000.

25. The Interim Manager has reviewed this proposal considering whether any cost reduction programme would adversely affect a possible sale to a third-party. The Receiver does not believe that it will. It is likely that any purchaser would conduct a similar rationalization of costs and might, in fact, expect the Receiver to execute these changes before a transaction. Given the excess capacity at the KGIC Campuses, the Receiver is of the view that a purchaser would prefer to acquire an operation sized for the number of students enrolled with some room for growth, and then build capacity as enrollments grow, rather than acquire significant excess capacity.
26. For these reasons, the Receiver believes that expansion of the Receiver's powers to permit the termination of employees and premises leases will enable the Receiver to reduce negative cash flow without affecting the quality of education to the students or the ultimate value of the assets.

RECEIVER'S GO FORWARD PLAN

27. The Receiver continues to believe that the value of the KGIC Group is best preserved by continuing operations; in particular, by continuing the education of students in the programmes for which they have enrolled.
28. The Receiver believes that a sale to a qualified purchaser which can stabilize and invest in the operations of the KGIC Group is in the best interests of the students.
29. The Receiver has reviewed the state of the KGIC Group, the results of KGIC's own sales effort conducted in 2016 and the likely list of target purchasers. The Receiver has not completed its analysis. However, given the state of the KGIC Group and the limited time that CF2017 may be willing to fund the cash shortfall, a prompt sale is essential.
30. In conversations with the Regulators, the Receiver has been told that a rapid resolution of the situation is desirable. Notwithstanding the insolvency process, the Regulators appear to be willing to stay regulatory action only providing there is rapid progress to a long-term resolution.
31. The Receiver is advised that an affiliate of CF2017 is preparing to submit an offer for all or substantially all of the KGIC Group paid for with the assumption of all or some of the \$13 million of debt held by CF2017. Should this offer be forthcoming, the Receiver will

analyze it against the possible outcomes of a sales process and given the time value of the process relative to the negative cash outflow.

32. The Receiver anticipates reporting to this Honourable Court as soon as practical either recommending an Approval and Vesting Order for a sale as outlined above or for approval of a sales process.

RECOMMENDATIONS

- 1) The Receiver recommends that this Honourable Court:
 - a) Grant an order expanding the Receiver's powers in Paragraph 12 of the Order to permit the termination of staff in order to reduce costs;
 - b) an order permitting the Receiver to terminate premise leases in order to reduce costs, and
 - c) Approve the actions of the Receiver as outlined in this report.

This Report is respectfully submitted to this Honourable Court as of this 2nd day of February, 2017.

BDO CANADA LIMITED,

In Its capacity as the Court-Appointed Interim Receiver of
KGIC Inc., and not in its personal or corporate capacity

Per:



Jervis Rodrigues, CPA, CA, CFE, CIRP, LIT
Senior Vice-President

EXHIBIT A

18 JANUARY 2017

PRE-APPOINTMENT CASH FLOW PROJECTION

KGIC Inc.
Cash Flow Projection
As of January 18, 2017

	(\$000's)															
Weeks	1	2	3	4	5	6	7	8	9	10	11	12	13	14		
Week Endir	27-Jan	3-Feb	10-Feb	17-Feb	24-Feb	3-Mar	10-Mar	17-Mar	24-Mar	31-Mar	7-Apr	14-Apr	21-Apr	28-Apr	Total	
Receipts																
Tuition	\$ 432	\$ 449	\$ 380	\$ 394	\$ 362	\$ 326	\$ 304	\$ 603	\$ 367	\$ 641	\$ 388	\$ 506	\$ 305	\$ 306	\$ 5,763	
Student loans															-	
Receiver's Certificates															-	
Other															-	
<i>Subtotal</i>	<i>432</i>	<i>449</i>	<i>380</i>	<i>394</i>	<i>362</i>	<i>326</i>	<i>304</i>	<i>603</i>	<i>367</i>	<i>641</i>	<i>388</i>	<i>506</i>	<i>305</i>	<i>306</i>	<i>5,763</i>	
Disbursements																
Commission	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Other direct costs																
Student refunds and relate	22	22	19	20	18	16	15	30	18	32	19	25	15	15	286	
Homestay	60	60	60	60	60	60	60	60	60	60	60	60	60	60	840	
Textbooks				75		75		75		75					300	
Other	12	12	10	11	10	9	8	16	10	17	10	14	8	8	155	
Payroll																
Regular pay		621		612		612		612		612		612		612	4,293	
Employment benefits		22				44				44				44	154	
Other															-	
<i>Payroll Subtotal</i>	<i>-</i>	<i>643</i>	<i>-</i>	<i>612</i>	<i>-</i>	<i>656</i>	<i>-</i>	<i>612</i>	<i>-</i>	<i>656</i>	<i>-</i>	<i>612</i>	<i>-</i>	<i>656</i>	<i>4,447</i>	
Rent					582	430		582				582			2,176	
Office and G&A																
Utilities, union dues, Gov't	15	15	15	15	15	15	15	15	15	15	15	15	15	15	210	
Other G&A	10	10	10	10	10	10	10	10	10	10	10	10	10	10	140	
Insurance			23				23				23			23	92	
Overseas office	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Other															-	
Interest/Bank charges			35				35				35				105	
Professional fees	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Travel	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Advertising and promotion	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Other															-	
Total disbursements	119	762	172	803	695	1,271	166	1,400	113	865	172	1,318	108	787	8,751	
Operating cash inflow/(outflow)	313	(313)	208	(409)	(333)	(945)	138	(797)	254	(224)	216	(812)	197	(481)	(2,988)	
Cash balances																
Beginning cash	-	313	-	208	(201)	(534)	(1,479)	(1,341)	(2,138)	(1,884)	(2,108)	(1,892)	(2,704)	(2,507)		
Operating cash inflow/(outflow)	313	(313)	208	(409)	(333)	(945)	138	(797)	254	(224)	216	(812)	197	(481)	(2,988)	
Ending cash balance	\$ 313	\$ -	\$ 208	\$ (201)	\$ (534)	\$ (1,479)	\$ (1,341)	\$ (2,138)	\$ (1,884)	\$ (2,108)	\$ (1,892)	\$ (2,704)	\$ (2,507)	\$ (2,988)	\$ (2,988)	
Monthly Net Cash Flow				\$ (534)				\$ (1,574)					\$ (880)			

Key Assumptions:

1 This cash flow does not include payments to the existing payables, and only covers ongoing weekly expenses.

2 Based on KGIC's January 18, 2016 Cash Flow Projection. Recruiting costs (Commissions, Travel, Advertising) and professional fees have been eliminated.

3 Assumes same cash inflow and cost structure as in January 2017

EXHIBIT B
31 JANUARY 2017
POST-APPOINTMENT
CASH FLOW PROJECTION

KGIC Inc., in Interim Receivership
Cash Flow Projection
As of January 31, 2017

Weeks	(\$000's)														Estimated Daily	
	1	2	3	4	5	6	7	8	9	10	11	12	13	14		Total
Week Ending:	27-Jan	3-Feb	10-Feb	17-Feb	24-Feb	3-Mar	10-Mar	17-Mar	24-Mar	31-Mar	7-Apr	14-Apr	21-Apr	28-Apr		70
Receipts																
Tuition	\$ 92	\$ 216	\$ 216	\$ 216	\$ 216	\$ 252	\$ 252	\$ 252	\$ 252	\$ 288	\$ 288	\$ 288	\$ 288	\$ 324	\$ 3,440	
Student loans		50	50	50	50	50	50	50	50	50	50	50	50	50	650	
Receiver's Certificates															-	
Other															-	
Subtotal	92	266	266	266	266	302	302	302	302	338	338	338	338	374	4,090	\$ 58
Disbursements																
Commission	14	32	32	32	32	38	38	38	38	43	43	43	43	49	516	
Other direct costs																
Student refunds and related costs															-	
Homestay/Texbook/Student activity		85	81	78	75	72	70	68	67	65	64	64	63	62	917	
Other															-	
Payroll																
Regular pay			460		460		460		460		460		460		2,758	
Other															-	
Payroll Subtotal	-	-	460	-	460	-	460	-	460	-	460	-	460	-	2,758	
Rent		437	-			437					437				1,310	
Office and G&A																
G&A		19	19	19	19	19	19	19	19	19	19	19	19	19	241	
Insurance			30			30				30				30	120	
Other															-	
Interest/Bank charges	1	2	2	2	2	2	2	2	2	3	3	3	3	3	33	
Professional fees	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Travel	-	8	8	8	8	8	8	8	8	8	8	8	8	8	103	
Advertising and marketing	-	14	14	14	14	14	14	14	14	14	14	14	14	14	182	
Other															-	
One time cash Disbursement																
SSDC Management fee	20	20	20	20	20	20	20	20	20	20	20	20	20	20	280	
Legal & Receivership fee		100				100				100				300		
Pre-Appointment Salary					235									235		
One Time Subtotal	20	120	20	20	255	120	20	20	20	20	120	20	20	20	815	
Total disbursements	35	717	666	173	865	740	631	169	627	202	1,167	170	629	205	6,994	\$ 100
Operating cash inflow/(outflow)	57	(451)	(400)	93	(599)	(438)	(329)	133	(325)	136	(829)	168	(291)	169	(2,904)	\$ (41)
Cash balances																
Beginning cash	-	57	(393)	(793)	(700)	(1,299)	(1,737)	(2,065)	(1,933)	(2,258)	(2,121)	(2,950)	(2,783)	(3,073)		
Operating cash inflow/(outflow)	57	(451)	(400)	93	(599)	(438)	(329)	133	(325)	136	(829)	168	(291)	169	(2,904)	
Ending cash balance	\$ 57	\$ (393)	\$ (793)	\$ (700)	\$ (1,299)	\$ (1,737)	\$ (2,065)	\$ (1,933)	\$ (2,258)	\$ (2,121)	\$ (2,950)	\$ (2,783)	\$ (3,073)	\$ (2,904)	\$ (2,904)	
Monthly Net Cash Flow					\$ (1,299)				\$ (822)					\$ (783)		

Key Assumptions:

- This cash flow covers ongoing weekly expenses.
- Assumes we'll pay the unpaid salary, rent, homestay fee and commission because it's important to maintain a good relationship with these creditors but will not pay any other existing payables
- Assumes that cash inflow in Feb will roughly the same as in Jan 2017 but student start will ramp up gradually in the next few months (see tab "student pop & start" for details)
- Assumes that outstanding student loan is \$ 1.2M of which \$ 50K will be received each week until it's fully paid
- Assumes that commission will be 15% of student payments; Other income (homestay, textbook, activities, etc) will be \$ 324 per student per month, other direct expense will be 70% of other income; Assumes that in the interim period salary and rent will be the same as in Jan 2017; G&A and travel will be 70% of the average of Q3 2016; bank charges will be 0.8% of direct payment from students; ad & promotion will be the same as the average of the first 9 months of 2016