

Court File No. 32-1494254

**ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)**

**IN THE MATTER
OF THE NOTICE OF INTENTION TO MAKE A PROPOSAL
OF PARLAY ENTERTAINMENT INC.**

**FOURTH REPORT OF THE BDO CANADA LIMITED,
AS PROPOSAL TRUSTEE
July 25, 2011**

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Appendix A Cash Flow Results for the Period July 1 to July 15, 2011

1. Introduction and Background

1.1 Introduction

- 1.1.1 Parlay Entertainment Inc. ("**Parlay**" or the "**Debtor**") is a public company listed under the Toronto Stock Exchange. Parlay and is one of the pioneers and technology leaders in the online gaming industry. As the inventor and holder of Internet bingo patents, Parlay was the first company in the world to develop and deploy its award winning software along with value added Parlay Game Services ("**PGS**") managed solutions based in Alderney and North America. PGS includes hosting services, shared games and, in the case of PGS Europe, pooled liquidity across the European marketplace. Parlay's head offices are located in Oakville, Canada. Parlay and its subsidiaries are licensed or certified to conduct business in Alderney, the United Kingdom and the Isle of Man.
- 1.1.2 Parlay's revenues declined from \$8.5 million in 2008 to \$3.4 million in 2009 and to \$2.9 million for the year-ended December 31, 2010.
- 1.1.3 This substantial decrease in revenues was a product of increased regulation of the on-line gaming industry in the USA, the world-wide recession reducing discretionary spending and increased competition.
- 1.1.4 Despite management's efforts to reduce costs, substantial losses were incurred in 2010 of \$2.4 million.
- 1.1.5 Management's belief is that the present revenue levels do not represent a sustainable business model for a public company with the accompanying accounting, regulatory and legal costs.
- 1.1.6 As set out in the First Report of the Proposal Trustee dated May 2, 2011, there are no registrations against Parlay pursuant to the Ontario Personal Property Security Act.
- 1.1.7 On May 4, 2011 Parlay filed a Notice of Intention to Make a Proposal (the "**NOI**") under the *Bankruptcy and Insolvency Act* Canada (the "**BIA**"). BDO

Canada Limited was named as the Proposal Trustee (the "**Proposal Trustee**").

- 1.1.8 Parlay's management initiated the NOI for the purpose of selling the business operations to a third party. On April 25, 2011, Parlay entered into a \$500,000 Debtor-In-Possession Credit Facility (the "**DIP Facility**") with M Projects Assets S. A. (the "**DIP Lender**" or "**M Projects**").
- 1.1.9 By order of this Honourable Court dated May 9, 2011 (the "**May 9 Order**"), a first ranking charge for the professional fees and disbursements of the Proposal Trustee and Parlay's legal counsel in the amount of \$200,000 against the assets of Parlay was approved. In addition, the May 9 Order also approved the DIP Facility and a second ranking charge of up to \$500,000 against the assets of Parlay, which was a condition of the DIP Facility. A copy of the May 9 Order is attached as Exhibit 3 to the Affidavit of David Callander sworn July 22, 2011 (the "**Affidavit**").
- 1.1.10 As described in the second report of the Proposal Trustee dated May 27, 2011, M Projects submitted an agreement to purchase the assets of Parlay by way of a stalking horse bid (the "**Asset Purchase Agreement**"). The Asset Purchase Agreement includes a Break-Up Fee of \$50,000 and the Expense Reimbursement of up to \$50,000 and a Minimum Overbid of \$37,500. A copy of the Asset Purchase Agreement is attached as Exhibit 7 to the Affidavit.
- 1.1.11 By order of this Honourable Court dated June 3, 2011 (the "**June 3 Order**"), the Proposal Trustee was authorized to market and sell the assets of Parlay, bidding procedures (the "**Bidding Procedures**") were approved, and Parlay was authorized to enter into the Asset Purchase Agreement. The June 3 Order also provided a third ranking charge as security for potential break up fees of M Projects, and a fourth ranking charge as security for directors and officers of Parlay (the "**Director's Charge**"), as well as granting a 45 day extension to the period for filing a Proposal. A copy of the June 3 Order is attached as Exhibit 5 to the Affidavit.
- 1.1.12 By order of this Honourable Court dated July 13, 2011 (the "**July 13 Order**") Parlay was granted a 45 day extension for filing a proposal until

September 1, 2011. The July 13 Order also vacated the Director's Charge. A copy of the July 13 Order is attached as Exhibit 8 to the Affidavit.

1.2 Purpose

2.1.1 The purpose of this Report of the Proposal Trustee is to:

- (a) advise the Court as to the status of Parlay's operations and cash flow results since the date of the last report;
- (b) advise the Court as to the status of the process to market and sell the assets of Parlay; and
- (c) recommend approval of the completion of the Asset Purchase Agreement.

2. Sales Process

2.1.2 Pursuant to the June 3 Order, the Proposal Trustee initiated a sales and marketing process (the "**Sales Process**") to invite offers to purchase the assets of Parlay on a going concern basis.

2.1.3 The timelines for the Sales Process are as follows:

- (a) July 18, 2011 - deadline for receipt of Qualified Bids (the "**Bid Deadline**")
- (b) July 25, 2011 - auction sale, if applicable
- (c) August 2, 2011 - sale approval hearing at Court
- (d) August 4, 2011 - anticipated closing of approved sale.

2.1.4 As described in previous reports, the Proposal Trustee prepared an online data room, an information package, and conditions of sale (the "**Information Package**") to invite offers to purchase the assets of Parlay.

The Information Package was distributed to interested parties who signed a confidentiality agreement with the Proposal Trustee. A copy of the Information Package is attached as **Appendix E**.

- 2.1.5 Because of the specialized nature of Parlay's business, the Proposal Trustee placed an advertisement on the internet with Gaming Intelligence (www.gamingintelligence.com). This website serves as a news and marketing hub for the online gaming industry.
- 2.1.6 In addition to the advertisement placed online, the Proposal Trustee contacted a further 105 companies including parties identified by management of Parlay, as well as parties who were known to the Proposal Trustee as operating in industries the same as or similar to Parlay.
- 2.1.7 The Sales Process has resulted in 17 parties contacting the Proposal Trustee regarding the assets of Parlay. Confidentiality Agreements were signed by 9 of the parties, who were provided the Information Package and granted access to the online data room.
- 2.1.8 By the Bid Deadline, no bids were received for the assets of Parlay. The only bid for the assets of Parlay is the pre-existing Asset Purchase Agreement with M Projects.

3. Asset Purchase Agreement

- 3.1.1 The June 3 Order approved Parlay entering into the Asset Purchase Agreement with M Projects. Pursuant to the terms of the Asset Purchase Agreement, M Projects will:
 - (a) pay cash Proceeds of \$500,000 less amounts outstanding under the DIP Facility;
 - (b) offer employment to twenty six (26) Parlay employees (the "Transferred Employees") on closing;

- (c) assume Parlay's liabilities to the Transferred Employees, including severance and termination obligations; and
- (d) carry on the business and assume certain customer contracts of Parlay.

3.1.2 The assets to be purchased are on an "as is, where is" basis and include the following (estimated values as of May 16, 2011):

- (a) accounts receivable valued at approximately \$100,000, subject to adjustment on closing;
- (b) all of the software development inventory of Parlay with a net book value of approximately \$10,000;
- (c) all of Parlay's equipment, which has a net book value of approximately \$616,000;
- (d) certain customer contracts, intellectual property, business records, regulatory approvals, customer lists, and goodwill; and
- (e) the shares of Parlay Games Limited, a wholly owned subsidiary of Parlay.

3.1.3 All Parlay property which is not included in the assets purchased by M Projects will remain with Parlay and include:

- (a) cash and cash equivalents;
- (b) accounts receivable, which exceed \$100,000;
- (c) certain excluded customer contracts
- (d) intercompany rights and claims other than with Parlay Games Limited;
- (e) rights to tax refunds; and

(f) shares of all subsidiaries other than Parlay Games Limited.

3.1.4 In addition, management of Parlay are dealing with parties who have expressed interest in purchasing the public shell of Parlay.

4. Approval of the Asset Purchase Agreement

4.1.1 Pursuant to section 65.13 of the BIA, an insolvent person in respect of whom a NOI is filed, may not sell assets outside of the ordinary course of business unless authorized to do so by a court. In deciding whether to grant the authorization, the court is to consider, among other things:

4.1.1.1 **“Whether the process leading to the proposed sale was reasonable in the circumstances”** - Parlay’s Bidding Procedures and Sales Process were approved by the Court. The 45 days to carry out the Sale Process allowed for Parlay’s assets to be reasonably exposed to the market. The Asset Purchase Agreement was used as a stalking horse to allow Parlay to continue operations with some certainty to suppliers, customers and employees that Parlay will be sold and its operations will continue while helping to maximize the realizations for creditors.

4.1.1.2 **“Whether the trustee approved the process leading to the proposed sale”** - the Proposal Trustee recommended the Sales Process and the Bidding Procedures which were approved by the June 3 Order.

4.1.1.3 **“Whether the Proposal Trustee filed with the court a report stating that in their opinion the sale would be more beneficial to creditors than a sale under a bankruptcy and the effects of the proposed sale on creditors and other interested parties”** - as described in this Report, the Asset Purchase Agreement along with the support of the DIP Lender allowed Parlay to continue operations. Without this support, Parlay would not have been able to continue as a going concern, and Parlay’s operations would

have shut down. In a bankruptcy, the customers of Parlay would not have received ongoing support and as a result, Parlay's contracts would have little or no value in a liquidation sale by a bankruptcy trustee. The public shell would have no value. The ongoing operations and the sale pursuant to the Asset Purchase Agreement have provided, and will continue to provide benefits to creditors, customers and other stakeholders of Parlay, including:

- (a) Transferred Employees have continued to be employed and will be offered continuing employment and their employment obligations will be assumed by M Projects;
- (b) suppliers have been paid in the post filing period;
- (c) customers have been supported in the post-filing period and will be continued to be supported; and
- (d) shareholders may benefit from the sale of Parlay's public shell.

4.1.1.4 **"The extent to which creditors were consulted"** - creditors were referred to the Proposal Trustee's website to access copies of the Trustee's Reports, motion materials and Court Orders. The majority of Parlay's creditors consist of employees who were made aware of status of the Sales Process by both the management of Parlay and the Proposal Trustee.

4.1.1.5 **"Whether the consideration to be received is reasonable and fair taking into account their market value"** - a formal valuation of the going-concern value of Parlay is a difficult undertaking as significant cash losses have been incurred in the last 12 to 18 months as a result of decreasing revenues. The Proposal Trustee is of the view that the best means to determine value of this type of business with these poor financial results is to expose it to the market. A rigorous effort was undertaken and numerous parties

were contacted. The Sales Process exposed Parlay's assets to the market over a 45 day period. Several parties examined the data room but ultimately there were no other bidders. This provides sufficient comfort in the circumstances that the value achieved is fair and reasonable. As described above, due to the specialized nature of the assets, there would be little or no value in a liquidation scenario.

4.1.2 In summary, the Proposal Trustee believes that the issues to be considered by the court in order to approve the sale of Parlay's assets to the Asset Purchase Agreement pursuant to section 65.13 of the BIA have been met.

5. Cash Forecast and Results to Date

5.1.1 Management of Parlay prepared an updated cash flow forecast (the "Updated Forecast") for the period of July 1 to September 2, 2011, which was included in the Third Report of the Trustee dated July 5, 2011.

5.1.2 The Proposal Trustee has monitored the Debtor's business operations and cash flow up to and including the period ending July 15, 2011. During this period Parlay's cash receipts are below receipts forecast in the Updated Forecast by \$148,000 due to timing differences, and disbursements have been less than the disbursements forecast in the Updated Forecast by \$92,000 due to timing differences as well as savings due to contingency disbursements which were forecast but not needed. In summary, the actual cash position as at July 15, 2011 is below forecast by \$56,000. The DIP Lender has continued to support Parlay's cash requirements.

5.1.3 Parlay's management has advised the Proposal Trustee that Parlay is continuing to operate its business in the ordinary course and wages and source deductions are being paid as due.

5.1.4 A copy of the actual results compared to forecast for the period July 1, 2011 to July 15, 2011 is attached hereto as **Appendix A**.

6. Conclusion and Recommendations

6.1.1 The Proposal Trustee believes that Sales Process, approved by the Court and carried out by the Proposal Trustee was reasonable in the circumstances.

6.1.2 The stalking horse nature of the Asset Purchase Agreement provided certainty and allowed the sale of Parlay's assets to be canvassed to the market.

6.1.3 The Asset Purchase Agreement was the only offer received. The completion of the Asset Purchase Agreement will allow Parlay to continue as a going concern, and will provide ongoing benefits to the Transferred Employees, customers, and suppliers of Parlay. The continuation of Parlay may also allow for a sale of the public shell which will provide a benefit to the shareholders of Parlay.

6.1.4 A liquidation of Parlay's assets will provide little or no recovery to the creditors and other stakeholders of Parlay. The Asset Purchase Agreement is supported by the management of Parlay.

6.1.5 The Proposal Trustee believes that the issues to be considered by the court in order to approve the sale of Parlay's assets to the Asset Purchase Agreement pursuant to section 65.13 of the BIA have been met.

6.1.6 The Proposal Trustee recommends and respectfully requests that this Honourable Court make an Order approving the completion of the sale of Parlay's assets pursuant to the Asset Purchase Agreement.

All of which is respectfully submitted this 25th day of July, 2011.

BDO CANADA LIMITED

Proposal Trustee

Per:

A handwritten signature in black ink, appearing to read 'BFD', with a long horizontal flourish extending to the right.

Blair F. Davidson, CA•CIRP, CBV, CMC
President

Parlay Entertainment Inc.
Cash Flow Results
July 1, 2011 to July 15, 2011

	July 1, 2011 to July 15, 2011		
	Projected \$	Actual \$	Variance \$
Cash Receipts			
<i>Receivables from Customers</i>			
Customer #1 deposit (PEL)	160,000	-	(160,000)
Customer # 2 deposit (PEL)	-	-	-
Smart (15,000 pounds sterling) (PEL)	-	-	-
Intervision (PGL)	-	-	-
Stays in PGL	-	-	-
Video King (PEI)	2,400	-	(2,400)
207 Media (PEI) - rent	3,700	3,672	(28)
207 Media (PEI) RB	8,500	8,417	(83)
207 Media (PEI) managed service fee	3,250	3,218	(32)
Double B (PEL)	24,000	23,800	(200)
Palaces (PML)	-	9,623	9,623
Expekt (PEL)	-	-	-
HST refunds	-	-	-
2010 corporate tax refund	-	-	-
First Nation (PGL)	-	5,000	5,000
Bank interest	-	25	25
	-	-	-
Total Cash Receipts	201,850	53,755	(148,095)
Cash Disbursements			
<i>Overhead Costs</i>			
Payroll - gross	65,000	68,803	(3,803)
Manulife - health benefits	-	6,175	(6,175)
RBC - LTD	-	541	(541)
Expenses - CIBC VISA	-	2,800	(2,800)
Expenses - TD Canada Trust	-	1,250	(1,250)
Rent (gross rent)	16,950	16,950	-
Toronto Maintenance (cleaners)	-	-	-
Telephone - One Connect	3,000	1,065	1,935
Telephone - Bell (all three accounts)	800	537	263
Internet - Blink	3,600	-	3,600
Heenan Blaikie - ongoing fees	101,700	50,850	50,850
BDO - ongoing fees	16,000	-	16,000
BDO - legal fees	10,000	5,000	5,000
MPP Projects Assets S.A. compliance fees	10,000	-	10,000
Contingency	27,000	-	18,931
employee expenses	-	65	-
water	-	74	-
off site back up	-	663	-
consulting fees	-	450	-
repair expenses	-	808	-
Rogers cell phone / blackberry	-	3,650	-
transfer agent fees	-	241	-
Rogers cell phone / blackberry	-	2,118	-
rounding	-	(1)	1
FX movements	-	131	(131)
Total Cash Disbursements	254,050	162,170	91,880
Net Cash from Operations	(52,200)	(108,415)	(56,215)
Opening Balance - Bank balance	212,440	212,440	-
Net Cash from Operations	(52,200)	(108,415)	(56,215)
	160,240	104,025	(56,215)
DIP Advance (Repayment)	-	-	-
Closing Balance - Bank Balance	160,240	104,025	(56,215)
DIP Loan - opening balance	380,557	380,558	380,559
Advance (Repayment)	-	-	-
Drawn	-	-	-
DIP Loan - closing balance	380,557	380,558	380,559