

Court File No.

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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

FIRST REPORT OF THE BDO CANADA LIMITED,
AS PROPOSAL TRUSTEE
May 2, 2011

1. Introduction and Background	3
1.1 Introduction.....	3
1.2 Background	3
1.3 Purpose	4
2. Cash Flow Forecast.....	5
3. Proposed Debtor-In-Possession Financing and Administration Charge	6
4. Summary and Recommendations.....	7

Appendix A	Parlay - Notice of Intention to Make a Proposal
Appendix B	Thirteen Week Cash Flow Forecast
Appendix C	Debtor- In-Possession Credit Facility
Appendix D	PPSA Searches

1. Introduction and Background

1.1 Introduction

1.1.0 On May 2, 2011 Parlay Entertainment Inc. (“Parlay”) filed a Notice of Intention to Make Proposal under the Bankruptcy and Insolvency Act (the “NOI”). BDO Canada Limited has consented to act as Proposal Trustee (“BDO” or the “Proposal Trustee”). A copy of the NOI including the creditors list, BDO’s consent and the Director’s Resolution is attached hereto to as Appendix A.

1.2 Background

1.2.0 Parlay is a public company listed under the TSX Venture Exchange. Parlay 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 a commercial deployment of 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. Some of the world’s best known brands use Parlay solutions. Parlay’s head offices are located in Oakville, Canada. Parlay is licensed or certified to conduct business in Alderney, the United Kingdom and the Isle of Man.

1.2.1 Parlay’s revenues declined from \$8.5 million in 2008 to \$3.3 million in 2009 and to \$2.9 million for the year-ended December 31, 2010.

1.2.2 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.

1.2.3 Despite management’s efforts to reduce costs, substantial losses were incurred in 2010 of \$2.4 million.

1.2.4 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.

1.2.5 A summary of Parlay's balance sheet as February 28, 2011 is presented below (expressed in \$000's):

Assets		Liabilities	
Cash	\$562	Accounts Payable	\$1,317
Accounts Receivable	816	Income taxes payable	64
Prepaid expenses	<u>145</u>	Deferred revenue	<u>407</u>
	1,523		1,788
Fixed Assets	82	Common Stock	4,894
Intangibles	<u>177</u>	Retained deficit	<u><4,900></u>
	<u>\$1,783</u>	Net equity (deficit)	<u><6></u>
			<u>\$1,782</u>

1.2.6 Parlay's management has initiated the NOI for the purpose of selling the business operations to a third party. The party that has offered to provide a Debtor-In-Possession Credit Facility (the "DIP") may also present a Stocking Horse Bid in support of a sales process conducted by the Proposal Trustee.

1.3 Purpose

1.3.0 The purpose of this First Report of the Proposal Trustee is to:

- a) report to the Court on the preliminary Thirteen Week Cash Flow of Parlay;
- b) provide the Proposal Trustee's analysis and recommendation with respect to the proposed DIP; and

- c) Provide the Proposal Trustee's recommendation with respect to the Administration Charge as defined in the proposed form of Order.

2. Cash Flow Forecast

2.1.0 The Chief Financial Officer of Parlay, Mr. David Callander, C.A. has prepared a thirteen week cash flow forecast for the period April 11 to July 8, 2011, attached hereto as Appendix B (the "Forecast").

2.1.1 A summary of the Forecast is provided below:

Receipts

Collection of customer receivables	\$874,250
------------------------------------	-----------

Disbursements

Payroll and related costs	574,968
---------------------------	---------

Rent, internet and other operating costs	91,640
--	--------

Professional Fees	215,000
-------------------	---------

License and Compliance Fees	128,591
-----------------------------	---------

Contingency	<u>110,000</u>
-------------	----------------

	<u>1,120,199</u>
--	------------------

Net Cash Flow	<u><245,949></u>
---------------	------------------------

Opening Cash Balance - April 11, 2011	30,000
---------------------------------------	--------

DIP Financing	<u>500,000</u>
---------------	----------------

Closing Cash Balance - July 8, 2011	<u>\$284,051</u>
-------------------------------------	------------------

2.1.2 The cash inflows from customers are not sufficient to fund the operating costs and professional fees associated with Parlay's restructuring efforts. Though the Proposal Trustee has only conducted a preliminary review of the Forecast, we are of the view that the requirement for the DIP financing is clearly evident.

2.1.3 In addition, there is some uncertainty concerning the timing of receipt of \$400,000 in deposits on the sale of software licenses to two key customers. These receipts are included in the Forecast, but due to the

risk of delays in completing these transactions, the risk of not funding ongoing costs without the proposed DIP is even greater.

3. Proposed Debtor-In-Possession Financing and Administration Charge

3.1.0 The Debtor-In-Possession Credit Facility dated April 25, 2011 is attached hereto as Appendix C and basic terms are as follows:

- a) Maximum \$500,000 credit facility with an initial drawdown of \$250,000 that has been deposited in the Proposal Trustee's bank account;
- b) Maturity Date of 4 months from the date of first advance;
- c) The DIP is conditional upon the Court's approval of the DIP charge which would be subordinate only to the Administration Charge of \$200,000 for the professional and legal fees of the Proposal Trustee, its counsel and Parlay's counsel;
- d) Interest Rate of 8% per annum;
- e) Covenants are mainly limited to cooperation with and disclosure to the DIP Lender and the Proposal Trustee as well as not priming the DIP Lender or filing a Proposal without their consent; and
- f) Events of Default include but are not limited to a negative variance on the Forecast greater than 20% and any other material adverse charge.

3.1.1 In reviewing the terms of the DIP and assessing the financial support required by Parlay, the Proposal Trustee provides the following observations:

- a) As Parlay does not have any secured creditors, the proposed DIP is not priming another party's security interest nor materially prejudicing the position of the unsecured creditors (refer attached PPSA search in Appendix D), also it does not secure pre-filing obligations;
- b) The Forecast clearly indicates the need for DIP financing to ensure that on-going payroll and operating costs are funded;

- c) The term of the proposed DIP coincides with management's timeframe to complete NOI proceedings, namely August 2011;
- d) Parlay's senior management have agreed to continue in their current roles during the NOI proceedings and have indicated they have canvassed major customers and suppliers and those party's are generally supportive of the NOI proceedings;
- e) The value of the software, licenses, intellectual property and other assets should be sufficient to secure the DIP; and
- f) The interest rate for the proposed DIP is relatively low compared to typical DIP financing.

3.1.2 With the proposed DIP providing financing to support the continued operations and a going-concern sales process, the Proposal Trustee is of the view that this is the best means to maximize value for the creditors and possibly even shareholders.

3.1.3 Parlay has also requested an Administration Charge of \$200,000 for fees of the Proposal Trustee, its legal counsel and Parlay's legal counsel. Due to the cash flow constraints of Parlay and the cost of undertaking a sale process in the NOI proceedings, the Proposal Trustee is of the view that the first ranking Administration Charge of \$200,000 is appropriate in these circumstances.

3.1.4 The DIP lender has indicated that they may provide a stocking horse bid to reduce the uncertainty surrounding Parlay conducting a sale process under NOI proceeds. The DIP itself would likely form part of that offer effectively as a credit bid.

4. Summary and Recommendations

4.1.0 The Proposal Trustee recommends and respectfully requests that the Court make an Order approving the proposed DIP and the DIP Charge.

All of which is respectfully submitted this 2nd day of May, 2011.

BDO CANADA LIMITED
Proposal Trustee
Per:

A handwritten signature in blue ink, appearing to read "B. Davidson", with a long horizontal flourish extending to the right.

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