

District of ONTARIO
Division No. 09 - Toronto
Estate No. 31-2504280
Court No. 31-2504280

ONTARIO
SUPERIOR COURT OF JUSTICE
IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF THE PROPOSAL OF
TOONBOX ENTERTAINMENT LTD.
OF THE CITY OF TORONTO,
IN THE MUNICIPALITY OF METROPOLITAN TORONTO,
IN THE PROVINCE OF ONTARIO.

AND

District of ONTARIO
Division No. 09 - Toronto
Estate No. 31-2504276
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ONTARIO
SUPERIOR COURT OF JUSTICE
IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF THE PROPOSAL OF
THE NUT JOB 2 PRODUCTIONS INC.
OF THE CITY OF TORONTO,
IN THE MUNICIPALITY OF METROPOLITAN TORONTO,
IN THE PROVINCE OF ONTARIO.

AND

Court File No. CV-19-618364-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

BETWEEN:

PACIFIC MERCANTILE BANK

Applicant

- and -

THE NUT JOB 2 PRODUCTIONS and TOONBOX ENTERTAINMENT LTD.

Respondent

SECOND REPORT OF THE PROPOSAL TRUSTEE AND INTERIM RECEIVER
June 21, 2019

INTRODUCTION

1. On April 10, 2019 Pacific Mercantile Bank (“PMB”) brought Applications for Bankruptcy Orders against Toonbox Entertainment Ltd. (“Toonbox”) and The Nut Job 2 Productions Inc. (“Nut Job”, and collectively, the “Companies”), returnable May 7, 2019.
2. PMB brought a further application for the appointment of an Interim Receiver to preserve the assets of the Companies, until such time as Bankruptcy Orders were issued. On April 18, 2019, by Order of the Honourable Mr. Justice Haaney of the Ontario Superior Court of Justice, BDO Canada Limited (“BDO”) was appointed as Interim Receiver of all assets, undertakings and properties of the Companies (the “Interim Receiver”). The Order is attached to BDO’s First Report, dated May 27, 2019, as Appendix “I”.
3. The Companies and PMB subsequently agreed that an orderly sale of assets “*en bloc*” would maximize realization and, accordingly, the Applications for Bankruptcy Orders were adjourned to June 4, 2019 to allow the Companies to file Proposals under the *Bankruptcy and Insolvency Act* (“BIA”).
4. On April 28, 2019, the Companies each filed a Proposal, naming BDO as the proposal trustee (the “Proposal Trustee”). A copy of each respective Proposal, together with each Certificate of Filing dated April 29, 2019, is attached to BDO’s First Report as Appendix “II” and Appendix “III”. Lipman Zener Waxman PC (“LZW”) act as counsel to the Proposal Trustee/Interim Receiver.
5. On May 21, 2019 separate First Meetings of Creditors were held for each of Toonbox and Nut Job. Both meetings were adjourned *sine-die* pending the outcome of the proposed sale process of the assets of the Companies. Copies of the Reports of Trustee on Proposal and Supplementary Report of Trustee on the Companies’ proposals are attached to BDO’s First report as Appendix “IV”.
6. By its First Report, BDO as Proposal Trustee/Interim Receiver advised this Honourable Court of its activities to the date of the Report, described the assets and Toonbox and Nut Job

and detailed a proposed sales process for the assets, which it wished to initiate, requested authorization to consolidate the proposal proceedings of Toonbox and Nut Job for administrative purposes, requested approval of a \$200,000 Administration Charge, and asked for approval of its Report and the conduct and activities of the Proposal Trustee/Interim Receiver, as described in its Report.

7. In paragraphs 15. to 17. of its First Report, BDO indicated that the Companies were subject to co-production agreements with Redrover Co. Ltd. (“Redrover”), which had funded various of the animations produced.
8. Immediately after issuance of its First Report, BDO became aware that the relationship between the Companies and Redrover is considerably more complicated than had first been realized.
9. Accordingly, prior to attending at Court, the parties (being Redrover, BDO and PMB), agreed to defer requesting approval of a proposed sales process until the agreements between the Companies and Redrover could be better understood, issues of ownership of assets determined, and an accounting obtained from Redrover for monies potentially owing by it to Toonbox, or claimed by Redrover as owing to it by Toonbox.
10. By Order of the Honourable Mr. Justice Conway, dated June 6, 2019 the Court provided the relief sought by the Proposal Trustee, being the consolidation of the proposal proceedings of each of Toonbox and Nut Job for administrative purposes, the provision of a \$200,000 Administration Charge, and approval of the conduct and activities of the Proposal Trustee, as set out in the First Report. A copy of the Order is attached hereto as Appendix “I”.

PURPOSE OF REPORT

11. This is the Second Report of the Proposal Trustee/Interim Receiver (the “Second Report”) for both Companies’ estates. The purpose of the Second Report is to:
 - a) provide this Court with information regarding:

- (i) the activities of the Proposal Trustee/Interim Receiver from the date of the First Report to the date of the Second Report, being June 22, 2019; and
 - (ii) the complexity of the relationship between the Companies and Redrover; and
- b) respectfully request that this Court grant an order that:
- (i) requires Redrover to forthwith supply the Proposal Trustee with a Property Proof of Claim and supporting evidence to establish Redrover's ownership entitlement to various animations and other assets in the possession of the Companies, and to forthwith supply the Proposal Trustee with an accounting of all monies owing by the Companies and Redrover to each other ; and
 - (ii) approves this Second Report and the conduct and activities of the Proposal Trustee/Interim Receiver described herein.

DISCLAIMER

12. In preparing this Report, the Proposal Trustee/Interim Receiver has relied upon unaudited financial information prepared by the Companies' representatives, the Companies' books and records and discussions with the Companies' representatives. The Proposal Trustee/Interim Receiver has not performed an audit or other verification of such information.

BACKGROUND

13. Toonbox was incorporated on June 19, 2008 and operated as an animation studio, producing various computer-animated films. Mr. Hong Kim is Toonbox's controlling shareholder and director. Toonbox is a holding company which owns various production companies, including Nut Job.

14. Nut Job was incorporated on April 5, 2013 and is a wholly owned subsidiary of Toonbox. Nut Job was an animation studio and produced the film “The Nut Job 2: Nutty by Nature” (the “Film”).
15. On December 19, 2017 Nut Job entered into a loan agreement with PMB in the amount of US\$8,170,705, secured by a general security agreement in favour of PMB (the “Loan”). Toonbox guaranteed the payment of the loan to PMB.
16. Nut Job was eligible to claim various provincial and federal refundable tax credits for the production of the film (the “Tax Credits”).
17. Nut Job was to use the Tax Credits to repay PMB in full. Pursuant to the Loan agreement with PMB the funds generated from the Tax Credits were to be kept in a separate trust account in favour of PMB, and paid over as soon as possible. Nut Job did not comply with the terms of the PMB Loan Agreement. Instead, the refunded Tax Credits were co-mingled with Toonbox’s funds and allegedly used by Toonbox to fund other ongoing film productions and operations.
18. The Loan matured on March 19, 2019 and Nut Job failed to repay it.
19. On March 20, 2019, having no funds to finance the continuation of business, the Companies ceased operations and Toonbox’s employees were terminated. At the time of the cessation of operations, Toonbox had approximately 40 active and 10 non-active employees.

ACTIVITIES OF PROPOSAL TRUSTEE/INTERIM RECEIVER from May 28 to June 21, 2019

Redrover Co. Ltd.

20. In 2013, Toonbox entered into a co-production agreement with Redrover pursuant to which Redrover financed various co-productions being produced by the two parties. Redrover owned the films, and Toonbox produced the films. Pursuant to the agreement, the “net receipts” from the exploitation of the films were to be shared on a 50/50 basis between Toonbox and Redrover. Toonbox advises that it has been unable to obtain an accounting

relating to the gross and net receipts from the films and that Redrover has not made any payments to Toonbox.

21. Management of Toonbox has advised the Proposal Trustee/Interim Receiver that in 2017 Redrover suspended its funding to Toonbox on all ongoing projects. Toonbox and its counsel have advised the Proposal Trustee/Interim Receiver that Toonbox made numerous attempts to contact Redrover to obtain an accounting, and clarity with respect to Redrover's reasons for the suspension of funding.
22. The Proposal Trustee/Interim Receiver was recently contacted by Lerner's LLP ("Lerner's"), counsel to Redrover. Lerner's advised the Proposal Trustee/Interim Receiver that Redrover is a significant creditor of Toonbox. Accordingly, the Proposal Trustee/Interim Receiver and LZW have reviewed various agreements between Toonbox and Redrover which have become available to the Proposal Trustee/Interim Receiver from the records of the Companies. The Proposal Trustee/Interim Receiver agreed to work co-operatively with Lerner's to exchange information to determine the rights and duties of the parties pursuant to the various productions, and amounts that may be owed by either party to the other.
23. The Proposal Trustee/Interim Receiver located a number of Co-Production Agreements between Redrover and Toonbox which indicated that Toonbox produced certain animations on behalf of Redrover, which then owned 100% of the productions, in exchange for financing the costs of production. Toonbox agreed to pay over to Redrover any Tax Credits it received from the Canadian federal and/or provincial governments for having produced the animations. In addition to being paid the production costs, Toonbox was to receive 50% of any "net receipts" earned by Redrover on the marketing and distribution of such productions. In most but not all cases, separate production companies were incorporated by Toonbox for each separate animation, such as the production of the "Nut Job 2: Nutty by Nature" film, for which The Nut Job 2 Productions Inc ("Nut Job") was incorporated.

24. The first Nut Job film was apparently produced for Redrover by a separately incorporated production company called Nut Job Inc. It appears that Toonbox was entitled not only to 50% of the “net receipts” generated by Redrover, but also to television production rights related to the “Nut Job” franchise. Additionally, 50% of the ownership rights to the first Nut Job film were to revert to Toonbox after 5 years (with the five year period expiring in June of 2019).
25. The various co-production agreements entered into with Redrover are complex, and were summarized for the Proposal Trustee/Interim Receiver by LZW. This information, received after the release of the First Report of the Proposal Trustee/Interim Receiver, was shared with the Companies, PMB and Redrover and led to agreement between the parties to defer a sales process until the complexities of the relationship between the Companies and Redrover could be better understood, and possibly reconciled.

Meeting of June 10, 2019

26. A meeting to advance the issues was held at the offices of BDO and was attended by Mr. Hong Kim, representing the Companies, and representatives of the Proposal Trustee/Interim Receiver and its counsel, and counsel for PMB and Redrover.
27. Lerner as counsel for Redrover indicated that it was in the process of obtaining relevant documentation from Redrover`s corporate head offices located in South Korea, but that additional agreements had already been discovered that appeared to indicate that Toonbox`s entitlement to a return of a 50% ownership interest in the first Nut Job film, and the rights to television productions related to the “Nut Job” franchise, was subject to a \$15 million payment required to be made to Redrover by Toonbox (and such payment has not been made). Additionally, other agreements had been located which may contradict to some degree the agreements already in the possession of the Proposal Trustee/Interim Receiver.

28. Further, counsel for Redrover suggested that Redrover may have an ownership interest in the computer equipment claimed to be owned by Toonbox, as the equipment may have been paid for by Redrover as production costs. Further, it was suggested that the computer equipment probably contains extensive intellectual property, being work product related to the films claimed to be owned by Redrover, and that Redrover and/or the Proposal Trustee/Interim Receiver would need to analyze the electronic information stored in the computer equipment to determine what intellectual property may be claimable by Redrover.
29. The computer equipment of the Companies is presently in storage. In order to enable a review of the intellectual property contained on the servers to take place, the equipment would have to be moved to proper offices and re-connected to electricity and perhaps the internet. The Proposal Trustee/Interim Receiver would incur costs in this regard, but would be prepared to co-operate with Redrover in conducting a review of the electronic records, provided that the cost of such review would need to be borne by Redrover. Additionally, such a review should take place only once Redrover has established its ownership claims and provided the requested accounting of monies owed by or to the Companies.
30. The Proposal Trustee/Interim Receiver has requested that Redrover produce all agreements between Redrover and the Companies, as well as any evidence supporting Redrover`s ownership rights to computer equipment or the information stored thereon. The Proposal Trustee/Interim Receiver and its counsel would need to review such agreements and supporting evidence and also consider the effect of such agreements and other evidence on the sales process. Counsel for Redrover agreed to produce such agreements and evidence, forthwith, but nothing has been received to date.
31. Further, Counsel for Redrover advised that Fintage House (“Fintage”), a collection account management firm located in The Netherlands, had been collecting all revenues related to

the animations produced by the Companies and marketed by Redrover. Fintage apparently emailed regular reports to Redrover, and copied Toonbox with such reports. The Proposal Trustee/Interim Receiver noted that it had not found such reports in the records of the Companies, and Mr. Kim advised he was unaware of such reports, which may have been sent to a previous staff member of the firm, who has recently left Canada. Counsel for Redrover was asked to review the records of Redrover and forward its copies of the reports, and agreed to do so. However, no such reports have been received to date.

32. Specifically, counsel for Redrover was asked by the Proposal Trustee/Interim Receiver to forthwith submit a Property Proof of Claim to evidence its ownership claims, and to submit an accounting for monies received by Redrover from the films, and potentially owing to Toonbox, at least in part. Counsel for Redrover indicated that Redrover has claims against Toonbox for amounts owing to Redrover, including for Tax credits that should have been remitted to Redrover by Toonbox, but were not. For the foregoing reasons, in the opinion of the Proposal Trustee/Interim Receiver it is essential that an accounting be produced right away.
33. Without a determination of Redrover`s ownership of assets represented by the Companies to be owned by them, the proposed sales process of the assets cannot take place.
34. Since no information was received from Redrover by the Proposal Trustee/Interim Receiver since the date of the meeting on June 10, 2019, the Proposal Trustee/Interim Receiver on June 21, 2019 forwarded to counsel for Redrover formal Notices under sec. 81(4) of the *Bankruptcy and Insolvency Act*, requiring Redrover to file Property Proofs of Claim for each of the Companies. Copies of the formal Notices to File Property Proofs of Claim are attached hereto as Appendix"II" and Appendix"III".

CONCLUSION

35. In conclusion, the Proposal Trustee/Interim Receiver requests the approval of this Honourable Court of this Second Report and the activities of the Proposal Trustee/Interim Receiver, as reported herein, and requests that the Court grant an order providing the relief described in paragraph 11(b)(i) of this Second Report.

All of which is respectfully reported, this 21st day of June, 2019.

BDO CANADA LIMITED

In its capacity as Proposal Trustee/Interim Receiver
of Toonbox Entertainment Ltd. and The Nut Job 2
Productions Inc., and not in its personal capacity
Per:



Vince Siciliano, CPA, CGA, CIRP, LIT
Senior Vice President