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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 REGIONAL MUNICIPALITY OF TORONTO,
IN THE PROVINCE OF ONTARIO.**

SUPPLEMENTARY REPORT OF TRUSTEE ON PROPOSAL

**TO THE CREDITORS OF
TOONBOX ENTERTAINMENT LTD.**

The following information is provided to assist creditors in evaluating the Company's affairs and the Proposal. Please note we have not audited or reviewed the Company's books and records and, as a result, we are not able to express an opinion concerning the accuracy of the information contained herein. The following information originated from the Company's books and records that were made available to us, as well as from our discussions with the Company and management.

Further to our prior report to creditors dated May 7, 2019, concerning the Proposal filed by Toonbox Entertainment Ltd. (the "Company") on April 29, 2019, the Trustee has prepared this supplementary report to creditors to report on additional findings that came to the Trustee's attention prior to the first meeting of creditors that is to be held on May 21, 2019.

We are advised by Pacific Mercantile Bank, the largest unsecured creditor, that they will be seeking an adjournment of the creditors meeting and shall be directing the Trustee to proceed to court for an order to approve the Sale Process.

An adjournment will also give the Trustee additional time to access amounts owing to employees, as discussed later in this report

Franchise rights and intellectual property rights

The Company reports to own franchise rights and intellectual property rights (collectively "Rights") in some of its produced films. The following is list of productions the Company worked on prepared based on information obtained from the books and records as well as Mr. Hong Kim ("Hong"), the Company's controlling shareholder. The Company does not necessarily own Rights in all of the productions: (the "Films"):

- The Nut Job
- The Nut Job 2



- The Nut Job 3
- Spark aka Bana Royale
- Pirate Cat
- Beet Party
- Bolts & Blip
- Grimmlings
- Once upon a Zodiac
- Far Fetched
- The Gods Must be Crazy

Films co-produced with Redrover

The Company engaged in co-production and distribution agreements (“Agreements”) with RedRover Co. Ltd. (“Redrover”) pursuant to which, *inter alia*, Redrover was responsible for financing the following films:

- The Nut Job
- The Nut Job 2
- The Nut Job 3
- Spark aka Bana Royale
- Pirate Cat
- Beet Party
- Bolts & Blip

The Company in turn agreed to be responsible for the production of the films by incorporating a production company (“Prodco”) for each of the above mentioned films as a separate wholly-owned subsidiary of the Company; Prodco was to render production services to the Company and Redrover pursuant to the terms of a Production Service Agreements between the Company, Redrover and Prodco.

The Agreements are being reviewed by Lipman, Zener, Waxman, the Trustee’s independent legal counsel, as well as Cassels Brock, which represent Pacific Mercantile Bank.

Pursuant to the Agreements the net receipts from the exploitation of the films were to be shared on an equal basis (i.e. 50% to the Company and 50% to Redrover). Net funds from the exploitation of the films were to be received and distributed by Redrover. The Agreements required Redrover to keep accurate and complete books and records relating to the gross revenue and net receipts and the Company had a right to inspect such books and records. Hong advised that Redrover did not disclose or provide the Company with the accounting relating to the gross and net receipts and did not make any payment of the net proceeds belonging to the Company. As a result, Hong advises the Company is unable to estimate how much in net receipts the Company is entitled to.

Hong advises that in 2017 Redrover suspended its funding to the Company on all ongoing projects due to frequent changes in Redrover’s management. The Company and the Company’s solicitors made numerous attempts to contact Redrover with the intent of obtaining clarity with respect to Redrover’s rationale for the funding suspension. All attempts to contact Redrover were unsuccessful.



The following film summaries were prepared based on Hong's comments, the Company's books and records and information obtained independently from the Company's external accountant and solicitor:

The Nut Job:

The Nut Job was the first co-production produced together with Redrover. Hong advised that the production was successful based on the available box office information; however, no share of the net proceeds was received by the Company from Redrover. The film was released in January 2014. Hong advised that Redrover owned 100 percent of the Rights in The Nut Job for five years after the release date. Since January 2019, 50 percent of the Rights were reverted back to the Company. There are no uncollected tax credits available to the Company. The Company might have a claim for the share of the net proceeds against Redrover but, as mentioned previously, this information is not available to the Company.

The Nut Job 2:

Following the success of The Nut Job, the Company and Redrover agreed to produce a second installment of the series called The Nut Job 2. The second film did not generate as much interest and resulted in much lower receipts than expected. The film was released in August 2017. Hong advises that Redrover owns 100 percent of the Rights. The Company is entitled to receive approximately \$300,000 in tax credits.

The Nut Job 3:

The third installment of the series, The Nut Job 3, is a production that was not finalized or released. Production was suspended due to non-payment of the agreed funding amounts by Redrover. Hong advises that Redrover owns 100 percent of the Rights of this film. He further advises that while Redrover has the right to produce feature films, the Company has the right to produce TV shows connected to the Nut Job franchise.

Based on the available books and records, the Company is entitled to receive approximately \$1.7 million in interim tax credits. Hong advises that the Company requires certain documentation from Redrover to apply for the tax credits. As mentioned previously, the Company has been experiencing difficulties in contacting Redrover since 2017, therefore no documentation has been received to finalize tax credit applications. Hong has undertaken to assist the Trustee to obtain the required documentation.

Spark aka Bana Royale:

Spark was a small budget film that is reported by Hong to be an unsuccessful production that did not generate any profits. Hong advises that Redrover owns 100 percent of the Rights in this film. The Company has claimed and received all tax credits leaving no value to the Company in this film.

Pirate Cat:

Pirate Cat is a production that is still in development stage at the time of the Proposal filing and has not been finalized or released. Hong advises that Redrover owns 100 percent of the Rights in this film. The Company did not receive the necessary funding from Redrover to complete the production; therefore, no costs were incurred necessary to apply for tax credits.



Beet Party:

Hong advises that Beet Party film was finalized and released leaving Redrover with 100 percent of Rights in this film. All tax credits available to the Company were applied for and received.

Bolts & Blips:

Bolts & Blips were the only TV show series co-produced with Redrover. The Company owns 50 percent of the Rights. All tax credits available to the Company were applied for and received.

Films not co-produced with Redrover

As mentioned previously, the funding from Redrover was suspended in 2017. The Company made numerous attempts to contact Redrover to confirm whether the funding would be restarted. When the Company failed to receive any correspondence from Redrover relating to project funding, the Company suspended the production of films associated with Redrover and decided to engage in new film productions separate from Redrover. The following is a list of films the Company worked on without the co-production agreement with Redrover:

- Grimmlings
- Once upon a Zodiac
- Far Fetched
- The Gods Must be Crazy

The following film summaries were prepared based on Hong's comments and the Company's books and records:

Grimmlings:

Grimmlings is a project that has not reached the development stage. The Company failed to find an investor for this project; therefore, the production did not proceed beyond a sales pitch.

Once upon a Zodiac:

Once Upon a Zodiac is a project that has not reached the development stage. The Company was able to obtain investor interest and engage in a Binding Memorandum of Understanding (the "MOU") dated November 29, 2018, with Beijing JC Family International Media Co. Ltd. (the "JC Family"). Pursuant to the MOU, JC Family is to finance twenty percent of the film budget that was estimated to be \$32 million (USD). MOU is intended as a binding legal agreement that shall expire on June 1, 2019 unless a long form definitive agreement is executed between the parties before the expiry date. Hong advises that the Company does not own the Rights of this production, but sees the value in the MOU.

Far Fetched:

Far Fetched is a project that has been funded by the Company and is in the later stages of development. The Company is eligible to receive approximately \$680,000 in tax credits upon



finalizing the production and obtaining necessary certificates for the tax credit applications. Hong advises that approximately \$50,000 is required to finalize the production and release the film. The Company owns the Rights to this film.

The Gods Must be Crazy:

The Gods Must be Crazy is another project that has not reached the development stage and the Company does not own its Rights. Hong advises that the Company was able to obtain investor interest and has entered into an MOU. The Trustee is awaiting the receipt of the MOU to confirm the details of the agreement.

Funding of operations

After Redrover stopped funding operation the Company financed operations by way of a loan with Pacific Mercantile Bank (“PMB”) in the amount of \$8.17 USD, secured by the film tax credits. In addition Hong borrowed over \$1 million personally from friends to invest into the Company.

Misdirection of Film Tax Credits

As discussed in our first Report to Creditors, The Nut Job 2 received film tax credits in October of 2018 in the amount of approximately \$9.1 million (CDN). The film's tax credits received were to be used to repay PMB, however only \$3.249 million was used for that purpose. The balance of funds were advanced to the Company (Toonbox) to fund operations and to repay shareholder loans to Hong in the amount of \$980,000.

Potential employee claims

According to management, the employees were paid wages, vacation pay and termination/severance pay at the time of their termination when the company ceased operations on March 20, 2019. From our review of the books and records it appears that the employees who were active in the operations at the time the company ceased operations, received the payments from the company. Since the filing of the Proposal some employees have contacted the Trustee to advise that they were not paid their termination and/or severance pay. The Trustee has invited these employees to file a proof of claim. It appears that these employees were on a short term lay-off or otherwise inactive when the company ceased operations.

The Trustee is investigating whether the employees (both active and inactive) received their proper entitlement pursuant to the Employment Standards Act. The Trustee has experienced some challenges as the company's Controller/Operations Manager has not been available to assist the Trustee.

In a bankruptcy the employees would be entitled to claims under the Wage Earner Protection Program Act. The Trustee has discussed this matter with Frank Bennett, the solicitor for the Company. Mr. Bennett has advised that the Company would consider amending the Proposal in order that the employees would receive a similar benefit and therefore would not be prejudiced by the Proposal



We trust that the foregoing adequately explains the current and ongoing circumstances of the Company.

Dated at Mississauga, Ontario this 21st day of May, 2019.



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Trustee
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