

IN THE MATTER OF THE BANKRUPTCY OF
HMV Canada Inc.
of the City of Toronto, in the Province of Ontario

**TRUSTEE'S REPORT TO THE FIRST MEETING OF CREDITORS
ON PRELIMINARY ADMINISTRATION**

I BACKGROUND

HMV Canada Inc. (“**HMV**” or the “**Company**”) was a leading audio and visual entertainment retailer, specializing in music, DVD, Blu-ray, and other media-related products. The Company was incorporated in 1998 under the *Business Corporations Act* (Ontario) and was also registered extra-provincially to carry on business in Alberta, British Columbia, Saskatchewan, Manitoba, Quebec, New Brunswick, Nova Scotia, Newfoundland and Labrador and Prince Edward Island. The Company originated as a subsidiary of the U.K.-based HMV Retail Ltd. In June 2011, HMV Retail Ltd. sold the Company and the assigned the rights to the “HMV” brand in Canada to U.K.-based Hilco Capital Limited, an affiliate of HUK 10 Limited.

As of January 2017, HMV operated 102 leased retail locations across Canada, as well as two leased warehouse and distribution centers in Mississauga, Ontario. The Company’s head office was located at Unit 110, 5401 Eglinton Avenue West in Etobicoke, Ontario. HMV employed approximately 1,280 individuals across Canada, the majority of which were part-time employees at the Company’s retail locations. The Company ceased operations and terminated all of its remaining employees on or before April 28, 2017.

On January 27, 2017, on application by HUK 10 Limited (“**HUK10**” or the “**Lender**”), the Ontario Superior Court of Justice (Commercial List) (the “**Court**”), issued an order (the “**Receivership Order**”) appointing Richter Advisory Group Inc. as receiver (the “**Receiver**”) of the assets, undertakings and properties of HMV to exercise the powers and duties set out in the Receivership Order. Concurrently, the Court also granted an order (the “**Approval Order**”) approving the agency agreement entered into among the Company, the Receiver and a contractual joint venture comprised of Gordon Brother Canada ULC and Merchant Retail Solutions ULC (together, the “**Agent**”) dated January 26, 2017 (the “**Agency Agreement**”), pursuant to which, among other things, the Agent was authorized to conduct a sale of the Company’s inventory and furniture, fixtures and equipment (the “**Liquidation Sale**”).

The Liquidation Sale was completed on April 15, 2017 upon the Agent vacating the final two HMV retail store locations. On June 2, 2017, the Agent and the Receiver, on behalf of itself and HMV, signed off on the final reconciliation as required by the Agency Agreement, and the Agent made payment to the Receiver on the final net amounts owing to HMV on the same date.

The Receiver filed two reports with the Court (the “**Receiver’s Reports**”), which among other things, provided the Court with information relating to the receivership proceedings, described the Receiver’s activities and conduct, the results of the Liquidation Sale, the proposed distribution to HUK10 on account of its indebtedness with the Company, the Receiver’s receipts and disbursements and a summary of the

security opinion prepared by Gowling WLG (Canada) LLP (“**Gowling WLG**”), independent counsel to the Receiver in this matter. Copies of the Receiver’s Reports and orders granted by the Court can be obtained from Richter’s website at <http://www.richter.ca/Folder/Insolvency-Cases/H/HMV-Canada-Inc>.

On June 19, 2017, the Court issued an order approving the application for bankruptcy made by HUK10 and appointing Richter as the trustee in bankruptcy (the “**Trustee**”), subject to affirmation by the creditors at the first meeting of creditors or substitution by another trustee by the creditors.

On June 23, 2017, notice of the first meeting of creditors, a list of creditors, a proof of claim form and a proxy were sent to all known creditors of the Company. On June 29, 2017, notice of the bankruptcy and the first meeting of creditors was published in the National Post.

The activities of the Trustee since its appointment have primarily consisted of statutory work in accordance with the provisions of the *Bankruptcy and Insolvency Act* (Canada) (the “**BIA**”).

II CAUSES OF BANKRUPTCY AND FINANCIAL POSITION

The Company had incurred significant net losses, each year from 2013 through to 2016. By 2016, the net loss for the eleven month period ending November 30, 2016 had reached approximately \$15.9 million.

The Trustee understands that the principal causes of the Company’s financial difficulties can be summarized as follows:

- (a) The Lender had supported the Company with additional financing since December 2014, and had agreed to defer cash payments, including scheduled principal and interest payments since November 2014. The Company lacked sufficient liquidity to address normal operating costs along with servicing its debt obligations owing to the Lender. In addition, there was no indication that HMV would be able to secure alternative financing to repay HUK10 in full, given its financial results and financial position;
- (b) The Company and its major suppliers were unable to reach an agreement, on mutually acceptable terms, to sustain HMV’s operations and support a recovery. Not having come to satisfactory arrangements with the major suppliers, the Company was projected to incur another loss in 2017 and require at least an additional \$5 million to sustain operations. The Lender was not prepared to continue to advance additional funds to the Company on that basis, and a withdrawal of its support would result in a material adverse change for the Company; and
- (c) The major suppliers all significantly reduced or stopped their supply of inventory to the Company, and with no viable alternative supply arrangement, the Company would have run out of inventory in the near future.

III FINANCIAL POSITION/ASSETS

As detailed in the Statement of Affairs, the Company did not have any realizable assets as at the date of bankruptcy as substantially all of its assets were sold through the Liquidation Sale, and the proceeds were in the possession of the Receiver and subject to the receivership proceedings and secured claims of

HUK10. In addition, based on the amounts realized to date from the Company's assets, HUK10, will likely suffer a significant shortfall on its security. Accordingly, it is unlikely that there will be any monies available to fund a distribution to unsecured creditors of the Company.

IV SECURED CREDITORS

The Company's primary secured lender was HUK10 who was owed approximately \$40.0 million as of the date of bankruptcy and prior to any distributions from the Receiver. On June 19, 2017, the Court granted an order authorizing and directing the Receiver to make an interim distribution in the amount of \$31,975,000 to HUK10 in respect of its secured claim against HMV.

The Receiver has obtained an independent legal opinion on HUK10's security from Gowling WLG, supported by separate independent legal opinions from law firms (the "**Additional Law Firms**") arranged by Gowling WLG in those provinces where Gowling WLG does not have offices in Canada, namely from additional legal counsel in the provinces of Saskatchewan, Manitoba and each of the Atlantic provinces. In these opinions to the Receiver, Gowling WLG and each of the Additional Law Firms, as applicable, have opined that the security documents executed and delivered by HMV in favour of HUK10 are (i) valid and enforceable in accordance with the terms thereof, subject to the standard assumptions, qualifications and limitations contained in the opinions, and (ii) create a valid security interest and hypothec in the assets of HMV to secure the payment and performance of indebtedness and obligations owed to HUK10.

V SECURITY FOR UNPAID WAGES – S.81.3 CLAIMS

The Trustee is not aware of any potential claims pursuant to section 81.3 of the BIA.

As previously noted, all of the Company's employees were terminated on or before April 28, 2017, and any amounts owed to the Company's former employees for wages and/or vacation pay are being addressed in the concurrent receivership proceedings.

The Receiver will continue to comply with the provisions of the *Wage Earner Protection Program Act* and related regulations, where applicable.

VI PREFERRED CREDITORS

The Company's Statement of Affairs indicates that there were no known preferred creditors as at the date of bankruptcy.

VII UNSECURED CREDITORS

The Company's Statement of Affairs indicates that there are approximately 317 unsecured creditors with claims totalling approximately \$81.2 million.

VIII PROVABLE CLAIMS

As at 3:00PM on the date of this report, the Trustee has recorded Proof of Claims filed, as follows:

	Number	Amount (\$)	Proxy in Favour of Trustee
Secured	-	-	-
Unsecured	51	6,925,256.86 ⁽¹⁾	12
TOTAL	51	\$6,925,256.86	12

Note (1): Two creditors filed claims claiming a priority for a portion of the claim amount. For purposes of this report, the entire amount of each claim has been shown as unsecured until the Trustee investigates these claims further.

IX PREFERENCE PAYMENTS AND TRANSFERS UNDER VALUE

The Trustee has not performed a review of the Company's books and records, with respect to potential fraudulent preferences, settlements or transfers at undervalue, as defined in the BIA. It is the intention of the Trustee to discuss the scope of its review with the inspectors to be appointed at the first meeting of creditors.

X TRUSTEE'S FEES

In consideration for consenting to act in these proceedings, HUK10 has agreed to provide a deposit to the Trustee in the amount of \$50,000 (the "**Deposit**") to guarantee payment of the Trustee's fees and disbursements for statutory work in accordance with the provisions of the BIA, including the fees and disbursements of its legal counsel.

Further information relating to the receivership or bankruptcy proceeding may be obtained from our website at <http://www.richter.ca/Folder/Insolvency-Cases/H/HMV-Canada-Inc>.

Dated at Toronto, Ontario, this 7th day of July, 2017.

RICHTER ADVISORY GROUP INC.,
in its capacity as Trustee of the estate of
HMV Canada Inc.,
and not in its personal capacity



Paul van Eyk, CPA, IFA, CIRP, LIT