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District of	Ontario
Division No.	09 – Mississauga
Court No.	32-1756215
Estate No.	32-1756215

## TRUSTEE'S PRELIMINARY REPORT

IN THE MATTER OF THE BANKRUPTCY OF  
CANUSA PRODUCTS INC.  
OF THE CITY OF MISSISSAUGA, IN THE PROVINCE OF ONTARIO

### Section A – Background

Canusa Products Inc. (“Canusa” or the “Company”) operated as a magazine and book publisher focusing on health, fitness, nutrition and lifestyle and distributed globally. Canusa was incorporated in 1999 and carried on business as Robert Kennedy Publishing (not to be confused with Robert Kennedy Publishing Inc., a separate legal entity that is not in bankruptcy and that has changed its name recently to Tosca Reno Media Inc.).

The five magazine titles published by Canusa were: *Oxygen*, *MuscleMag International*, *Clean Eating*, *Reps* and *American Curves*.

There were 52 active titles in the book publishing division at the Company. These books were authored by Robert Kennedy, Tosca Reno Kennedy (“Tosca Kennedy”) and certain authors who were at arm’s length to Canusa. As discussed further below, the Company published the books but did not own all of the intellectual property related to the publications (e.g. copyrights, trademarks, etc.).

On the 7<sup>th</sup> day of June, 2013, Canusa’s sole director, Tosca Kennedy, filed an assignment for the general benefit of creditors and Deloitte & Touche Inc. was appointed as trustee (“Trustee”).

The publishing business was not continued by the Trustee; to maximize value of the assets of the Company, a timely sale needs to be achieved.

The Trustee understands that the following factors contributed to the insolvency:

- a) the illness and death of the Company's founder, Robert Kennedy, in April 2012, and the resulting impact that this has had on the Company;
- b) unfavourable industry trends for printed magazines;
- c) the cost of a settlement of a dispute in early 2013 with a significant advertiser;
- d) lower than expected renewals of subscriptions due to difficult transition to a new subscription service provider in early 2013;
- e) costs relating to the closure of a retail venture for MuscleMag International brand;
- f) commitment to a significant lease for a large distribution centre in Mississauga, which was significantly in excess of current corporate needs; and
- g) significant distributions to Robert and Tosca Kennedy relative to recent cash-flow and profitability.

## Section B - Assets

### *Intellectual Property and Related Assets - Magazines*

Although Canusa is the publisher of the five magazines, it does not own all of the intellectual property related to the magazines. In particular, there are various copyrights, moral rights of authors and trademarks that are not owned by Canusa. The situation is complicated by a lack of documentation that establishes precisely what rights Canusa has with respect to the magazines and the related intellectual property. For example, there is a lack of written license agreements that establish the scope and terms of the rights that Canusa has in this regard. The Trustee is continuing its review of the Company's books and records in order to identify the assets of the Company, including greater clarity as to the ownership and rights relating to the magazines and books published by the Company.

At this time, the Trustee understands that:

- The Canadian trademarks for *Oxygen* and *MuscleMag International* are held in the testamentary estate of Robert Kennedy. *Clean Eating* and certain other U.S. and Canadian trademarks are held by Tosca Reno Media Inc. (previously Robert Kennedy Publishing Inc.) These entities are not bankrupt and their assets do not form part of the estate of Canusa.
- Canusa owns the brand names *Reps* and *American Curves*.
- Certain international licences are held by Canusa.
- The subscriber lists are property of Canusa.
- Domain names associated with the business are property of Canusa; however, these may have limited use and value without the necessary rights from the various rights-holders to continue to use the content that populated these sites prior to bankruptcy.

The sale of a magazine (or book) publisher in Canada is subject to the *Investment Canada Act* and may require ministerial review if the purchasers are not Canadian. This, combined with the limited rights that Canusa holds with respect to the intellectual property in question, complicates any attempt to realize on these assets.

Based on the foregoing, it would appear that marketing the Canusa magazine assets and the related intellectual property together as a package would be the most successful strategy for maximizes recoveries. However, due to the divided ownership of the intellectual property and the uncertainty as to the extent of Canusa's rights thereto, the Trustee intends to market the assets of the Company, such as they are, individually on a lot-basis in addition to an *en bloc* basis, to garner interest.

The Trustee has had preliminary discussions with counsel for Tosca Reno Media Inc. with respect to a possible resolution of the various claims and rights regarding the magazines and books in question, which resolution would see consideration flow to the estate in exchange for an assignment by the Trustee of its rights, if any, in respect thereof. The Trustee intends to discuss this further with the inspectors of the estate, once appointed.

### ***Book Division***

Based on the Trustee's review to date, it appears that there are only 5 written agreements for the 52 active titles.

The Trustee faces significant constraints in selling the book division *en bloc*. These constraints include: reversion of authors' rights, payment of royalties on ongoing sales and a possible inability to assign the copyright without the permission of the author. In addition, the author has a statutory right of first refusal to purchase book inventory. There are further potential constraints with respect to trademarks.

The book inventory is principally comprised of approximately 150,000 units, representing approximately \$550,000 in net book value. The inventory is located at Canusa's consignment customer, National Book Network, Inc. in the U.S., and there are approximately \$533,000 of Accounts Receivable due from NBN (net of returns reserve). In addition, there are approximately 40,000 units of book inventory on Canusa's premises. Inventory and Accounts Receivable balances in aggregate are disclosed later in this report.

As is customary in the publishing industry, returns can significantly erode Accounts Receivable collections, and there are numerous possible set off claims that might be asserted. For example, if a title is non-active then any retailer can return the book for a period of 12 months. Therefore, the collection of Accounts Receivable is uncertain

### ***Equipment and Furniture***

The Trustee has completed the physical count of the equipment and furniture on-site.

As rent is currently running at approximately \$75,000 per month, it is important to sell the equipment and furniture on an expedited basis, in order to disclaim the lease and bring the obligation to pay rent to an end. The Trustee has satisfied itself that there is no value in the lease and that there is unlikely to be any person willing to take an assignment of the lease and the obligations thereunder. The Trustee is investigating the feasibility of removing the equipment and furniture to a storage site rather than continuing to occupy the premises.

### ***Inventory and Accounts Receivable***

There is bulk paper and work-in-progress held at Quad / Graphics Inc. at a book value of approximately \$800,000. However, Quad / Graphics Inc. and the paper supplier, Gould are significant creditors and realizing on this asset will be difficult.

As of the date of bankruptcy, the total accounts receivable (including books) is over \$1,000,000.

### ***Other assets***

The Company has certain prepaid expenses and deposits totaling \$367,000 that are likely to have limited value.

The Trustee has reviewed the last tax return and it appears that Canusa has not participated in a provincial program for media publishers. The Trustee will review the viability with former employees and external accountant representatives. At this time, it does not appear that the Company is owed any material refunds from taxation authorities.

Currently, the Trustee is holding approximately \$233,000 in its trust account.

### ***Proposed realization process***

The Trustee intends to recommend to the inspectors of the estate, once appointed, that it be authorized and directed by the inspectors to proceed with a realization of the assets referred to above, as follows:

- 1) Equipment and Furniture – list prepared – deadline of July 5, 2013, for selection of auctioneer – sale and exit by July 25, 2013;
- 2) Magazine business and Book Division – due to the constraints disclosed above, the Trustee will formalize the realization strategy with the inspectors and estate counsel; and
- 3) Accounts Receivable collections – ongoing

## **Section C - Secured Creditors**

Based on the Trustee's review, there are no secured creditors having general security agreements over Canusa's property. Notwithstanding that there are two outstanding registrations of security interests pursuant to the *Personal Property Security Act* (Ontario), there is no debt outstanding to the parties in question. There are certain creditors holding limited security over specific assets of the Company, as more particularly set out in the Statement of Affairs.

One of the Secured Creditors, Blue Chip Leasing Company, was notified by the Trustee that their collateral was in the possession of an unpaid photographer as a result of a transaction completed by the Company in April, 2013.

CDS Global, Inc., the subscriber service provider based in Iowa, has filed a secured proof of claim for USD\$151,420.63, citing an Artisan's Lien over the subscriber list. The Trustee will be seeking legal advice on this matter and will review the matter further with the estate inspectors, once appointed.

There were 96 employees based on the Company records. On June 26, 2013, the Trustee held a workshop with the employees to assist with the claims, including Wage Earner Protection Program claims. The Trustee estimates that the value of priority claims of employees pursuant to section 81.3 of the *Bankruptcy and Insolvency Act* is approximately \$164,000, which is in priority to the unsecured creditors.

Based on the Trustee's review to date, it appears that there is no deemed trust amount due for source deductions.

## **Section D - Conservatory and Protective Measures**

The Trustee attended the premises on Friday June 7, 2013, to meet with employees and take possession and control of the Canusa property. The Trustee engaged a security firm to attend and to monitor the property and the parties attending and leaving the property on the first day and over the first weekend following the commencement of the bankruptcy proceedings.

The locks were changed externally and to certain areas within the premises to control the access to the property.

The Trustee confirmed insurance coverage as a named insured and changed the loss payee to the estate.

Due to the potential value of the intellectual property of the business, the Trustee worked with the technology contractor to lock-out previous systems users to prevent unauthorized access to images and materials.

The Trustee did not continue the business and notified key stakeholders and suppliers about the bankruptcy on a timely basis.

## **Section E – Legal Proceedings**

The Trustee has engaged Torys LLP as estate counsel to provide advice to the Trustee.

There is an ongoing collection action in the U.S. that the Trustee is attempting to resolve to benefit the estate.

## **Section F – Provable Claims**

The Trustee assisted with the preparation of the Statement of Affairs. The unsecured creditor list was prepared using Company information from mid-May, 2013, however have learned that certain provable claims will be higher than set out in the Statement of Affairs.

In addition, there are certain creditors that have been assigned a nominal amount of \$1.00 to facilitate the notices being issued to creditors pending determination of the actual amounts owing to such creditors. The landlord's claim in the Statement of Affairs excludes has not been calculated. .]

As set out in the Statement of Affairs, there are certain creditors that will have significant claims in the estate:

- a) Employees – wages, termination and severance, with amounts to be calculated and proven by employees;
- b) Orlando Corporation – landlord (proof of claim outstanding);
- c) Quad / Graphics Inc. – printer and distribution (approximately USD\$2.3 million asserted to date, subject to the review of this claim by the Trustee);
- d) Gould Paper Corp – paper supplier (approximately USD\$950,000 asserted to date, subject to the review of this claim by the Trustee);
- e) CDS Global Inc. – subscriber service provider (approximately USD\$151,000 claimed as a secured creditor, subject to the review of this claim by the Trustee); and
- f) Subscribers – Approximately 218,000 parties that may have prepaid their digital or magazine subscription; however it is expected that certain of these parties may make claims through their credit cards. Canusa's records indicate that this liability may be as high as \$2.5 million.

The Trustee will consult with its counsel and the inspectors with respect to the consideration of claims and the making of distributions to creditors in due course, if funds are available for distribution.

## **Section G – Transfers at Under Value and Preference Payments**

The Trustee is in the process of reviewing the Company's books and records and the details of the payments to the creditors and payments to related parties in the relevant statutory periods prior to the bankruptcy in order to identify potential preference payments and transactions at undervalue.

To date, there are a number of transactions have been identified requiring further review, including deemed dividends that were declared to eliminate Robert Kennedy's shareholder loan balance of approximately \$1.1 million as of the date of his death. In addition, the shareholder loan receivable from Tosca Kennedy is approximately \$490,000 as of the date of bankruptcy.

The Trustee has discussed a number of related-party transactions with Tosca Kennedy and her counsel, including the fact that there have been no specific royalty payments as against the Company's use of the trademarks, which are beneficially owned by her.

The Trustee will consult with counsel and inspectors on these matters going forward.

## **Section H – Anticipated Realizations and Projected Distributions**

As set out in Sections B, C and F, the viability of an *en bloc* sale of the magazine and book properties is impaired by virtue of the fact that the most valuable brands and trademarks are not owned by the Company, and there are secured parties and potential statutorily preferred creditors that would rank ahead of the general unsecured creditors.

As of the date of this report, the assets have not been exposed to the market and there is uncertainty about the fair market values of the assets due to the issues described herein.

In addition, it is the Trustee's view that this administration is highly complex relative to the value of the property in the estate, including by reason of a lack of commercial agreements between the parties, competing interests between parties, lack of complete ownership of publishing properties, anticipated difficulties with receivables collections and a high operating cost structure of the premises and systems.

The Trustee expects that net proceeds of the estate will be significantly less than the book value of the assets. As information becomes more clear in the next one to two months, we will provide the inspectors with a range of estimated realizations on various assets and overall.

Attached as Appendix 1, is an Interim Statement of Receipts and Disbursements.

## Section I – Other matters

The Trustee's fees will be paid by the estate, however prior to the bankruptcy the Trustee received a guarantee from Tosca Kennedy (limited to \$15,000) in the event that there were no assets available with which to pay its fees.

The Trustee has established a webpage at <http://www.deloitte.com/ca/can-usa> to communicate to employees, creditors, media and other interested parties. Copies of relevant documents, including and court materials, are available at this site.

No bond has been required by the Official Receiver.

Within the premises, the Company has possession of an extensive photograph and slide collection that appears to be subject to a property claim of the estate of Robert Kennedy. The Trustee has granted access to family representatives to review the collection for purposes of making a property claim.

The Trustee has engaged certain former employees to assist with dealing with property claims made by third-parties who have personal property and former employees and contractors with digital personal work product that may be necessary to re-establish their careers.

After the meeting of creditors, to minimize costs, it is expected that the Trustee's activities will be supported by 3 or fewer former employees of Canusa, with a view to focusing on asset realizations to benefit the estate.

Dated at Toronto, Ontario, this 27<sup>th</sup> day of June, 2013



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Trustee