

## **Exhibit C**

Estate File Nos. 31-456611  
31-456614  
31-456616  
31-456617

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
(COMMERCIAL LIST)**

**IN THE MATTER OF THE BANKRUPTCY OF  
DB MEDIA DISTRIBUTION INC., DB MEDIA DISTRIBUTION (CANADA),  
CH LLC (CANADA) AND CH SUB LLC (CANADA)**

**FIRST REPORT OF THE TRUSTEE IN BANKRUPTCY**

**INTRODUCTION**

1. On December 9, 2010, DB Media Distribution Inc. ("DB Media"), DB Media Distribution (Canada) ("DB Media Canada"), CH LLC (Canada) ("CH") and CH Sub LLC (Canada) ("CH SUB") (collectively, "DB Media Distribution" or the "Companies") filed an assignment into bankruptcy. Alvarez & Marsal Canada Inc. ("A&M Canada") was appointed as trustee in bankruptcy (the "Trustee") of each of DB Media, DB Media Canada, CH and CH SUB pursuant to certificates of appointment issued by the Office of the Superintendent of Bankruptcy Canada on December 9, 2010.
2. This report of the Trustee is filed to provide this Honourable Court with additional information regarding the Companies and to support the Trustee's motion for an Order of this Honourable Court providing for a procedural consolidation of the bankrupt estates of DB Media, DB Media Canada, CH and CH SUB (the "Procedural Consolidation Order"), and for a separate Order, *inter alia*:
  - a. relieving the Trustee of any obligation to send notice of the bankruptcy and of the first meeting of creditors to such creditors of DB Media Distribution whose claims in the aggregate do not exceed \$100 in the manner prescribed under section 102 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended (the "BIA");

- b. relieving the Trustee of its obligation to include a full list of creditors in the notice of the bankruptcy and of the first meeting of creditors, which the Trustee will send to the creditors with the claims of \$100 or more in the manner prescribed in section 102 of the BIA, and authorizing the Trustee to instead make a one-line entry for the customers and employees and to direct creditors to a website which will contain a complete list of creditors;
  - c. authorizing the Trustee to post a complete list of creditors of DB Media Distribution, including customer names with credit balances, on a dedicated webpage to be set up by the Trustee on its website;
  - d. authorizing the Trustee to redirect DB Media Distribution's book and DVD club websites to a website hosted by the Trustee, which will provide notice of the bankruptcy of DB Media Distribution and provide a link to the Trustee's website containing the statutory notice of the bankruptcy and documents for filing proofs of claim;
  - e. relieving the Trustee of any responsibility to perform any act or take any steps in respect of its obligations under subsections 102(1) and (2) of the BIA as such obligations relate to the creditors noted in paragraph a. above, other than supplying a form of proof of claim and proxy to those creditors upon their request of same; and
  - f. relieving the Trustee of any obligation to take full physical count of the inventory of DB Media Distribution and, otherwise, of any responsibility to perform any act or take any steps in respect of its obligations under subsection 16(3) of the BIA, other than to conduct a spot audit of the inventory.
3. In preparing this report, the Trustee has relied upon unaudited financial information, the books and records of DB Media Distribution, financial information, and analyses prepared by DB Media Distribution, and discussions with management of DB Media Distribution and its parent company, Direct Brands, Inc. (collectively, the "Information"). The Trustee has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of the Information,

and, accordingly the Trustee expresses no opinion or other form of assurance on the Information contained in this report.

4. All references to monetary amounts in this report are in Canadian dollars unless otherwise noted.

## **BACKGROUND**

5. DB Media Canada is a general partnership registered under the laws of the Province of Ontario with general partners CH and CH SUB, being two limited liability companies formed under the laws of the State of Delaware, U.S.A.
6. DB Media is a corporation organized under the laws of the Province of Ontario and is a sister corporation of CH.
7. DB Media Distribution is a direct-to-consumer distributor of books and DVDs in Canada through its various specialty clubs. Prior to the date of bankruptcy, DB Media Distribution sold music compact discs, cassettes and albums to club members, but discontinued this line of its business in December 2008.
8. DB Media Distribution and its predecessor companies have been in business in Canada selling DVDs and music products for over fifty-five years and books for over seventy years. The Companies have an active member base of 229,000 and 147,000 for the book and DVD clubs, respectively.
9. Customers of DB Media Distribution, who were members of its specialty clubs were able to purchase books and DVDs by mail, telephone or on-line. Customers were also able to return books and DVDs to the Companies for credit notes. Credits were applied to the customers' accounts to be used against future purchases. At the date of bankruptcy of the Companies over 72,000 members held unexpired credits ranging in the amounts from less than \$1 to \$2,500.

## **PROCEDURAL CONSOLIDATION OF PROCEEDINGS**

10. The value of the assets in the bankrupt estates is insufficient to satisfy claims of the Companies' creditors in full and, to the extent possible, the Trustee is seeking to minimize the cost of administering the bankrupt estates.
11. In its efforts to reduce the expenses associated with the administration of the bankrupt estates, the Trustee is seeking procedural consolidation of the Companies' bankrupt estates to avoid performing, *inter alia*, the following separate actions in respect of each of the bankrupts:
  - a. convening and conducting meetings of creditors and inspectors;
  - b. making, filing, advertising and distributing all filings and notices required under the BIA; and
  - c. appointing separate groups of inspectors.
12. As noted above DB Media Canada is a general partnership with CH and CH SUB being its partners. The Trustee understands that all of the creditors of the partnership are the creditors of DB Media Canada and that there are no direct creditors of either CH or CH SUB. Subsection 43(16) of the BIA provides for possibility of consolidation of bankruptcy proceedings against different partners in the same partnership. While there is no a specific provision in the BIA dealing with procedural consolidation of other types of estates, the courts have done this in the past pursuant to their inherent equitable jurisdiction where there is no prejudice to creditors.
13. A procedural consolidation of the bankrupt estates of the Companies will enable the Trustee to administer the estates as one and to take the actions described in the above paragraph only once, significantly reducing the costs of administration.
14. The procedural consolidation will not result in prejudice to the Companies' creditors. The creditors will be asked to specify in their proofs of claim a particular company or companies against which their claim will be filed.

15. Direct Brands, Inc., one of the largest creditors of the Companies, has consented to the procedural consolidation being sought by the Trustee.

#### **NOTICE OF BANKRUPTCY AND FIRST MEETING OF CREDITORS**

16. At the date of the bankruptcy assignment, DB Media Distribution had amounts owing to unsecured creditors as follows:

Creditors	DB Media \$ Millions	DB Media # of Creditors	DB Media Canada \$ Millions	DB Media Canada # of Creditors
Third party trade and employee amounts	\$2.3	130	\$0.7	40
Intercompany	\$7.6	2	\$4.0	1
Customer credits	\$1.3	49,181	\$0.5	23,190
Total	\$11.2	49,313	\$5.2	23,231

17. The costs of mailing the notice of bankruptcy and first meeting of creditors to all of DB Media Distribution's creditors would be in excess of \$150,000 which is unduly expensive given the total realizable assets of the estates are estimated to be \$1.7 million, which are comprised largely of receivables.
18. The assets of the Companies are mostly comprised of a large inventory of books and DVDs, as well as certain accounts receivable. As more particularly described below, there are stringent licencing restrictions in relation to the inventory of books and DVDs, preventing the Trustee from realizing on such assets and leaving the accounts receivable to be the main stream of revenue for the estates.
19. In order to provide adequate notice of the bankruptcy and of the first meeting of creditors and to administer the estates in a cost effective manner, the Trustee proposes to:
- send a notice of the bankruptcy and of the first meeting of creditors to all known third party creditors, contingent claimants and employees of the Companies whose claims are \$100.00 or more. It is the Trustee's view that due to a large number of creditors, it

would be unduly expensive and extremely voluminous to include a complete list of creditors with each such notice. The Trustee will be seeking authority from this Honourable Court to instead make a one-line entry for the customers and employees on the notice and to direct creditors to a website which will contain a complete list of creditors;

- b. post a complete list of creditors of DB Media Distribution, including customer names with credit balances, on a dedicated webpage to be set up by the Trustee on its website;
- c. publish a notice of the first meeting of creditors in The Globe and Mail at least five (5) days prior to the meeting of creditors in accordance with the provisions of the BIA;
- d. redirect the Companies' book and DVD club websites to a website hosted by the Trustee, which will provide notice of the bankruptcy of the Companies and provide a link to the Trustee's creditor website containing the statutory notice of the bankruptcy and documents for filing proofs of claim; and
- e. if and as practicable, continue to operate the Companies' customer call centre until at least the conclusion of the first meeting of creditors. When customers call into the centre, the staff will be instructed to provide them with information on the bankruptcy;
- f. notify Canada Revenue Agency and other required governmental agencies of the bankruptcy of the Companies and of the first meeting of creditors.

20. If the statutory notice of the bankruptcy and of the first meeting of creditors is mailed to creditors with claims equal to or greater than \$100.00, then the vast majority of third party trade creditors and approximately 2,600 customers comprising an estimated 24% of credit amounts would receive notice.

#### **INVENTORY COUNT**

21. As noted above, a large portion the assets of the Companies is comprised of books and DVDs. There are approximately 465,000 DVDs and over 100,000 Health and Harmony items. The Trustee has been advised by the management of the Companies that that a full count of this inventory would take about 2 full days with about 100 employees counting. No shipping would occur in those two days. The Trustee has not yet had a chance to get an estimate from a third party inventory firm.
22. Such assets are subject to the terms of the licences between various recording studios/publishers and the Companys' parent, Direct Brands, Inc. (the "Head Licences"). Such licences contain express restrictions in terms of the scope of permitted distribution and sale of the licensed products. Notwithstanding that there is no written sublicense between Direct Brands, Inc. and the Companies, the Trustee's counsel's view is that there is an implied sublicense and, therefore, the Companies would be restricted from selling the inventory on the basis as set out in the Head Licences. Accordingly, any distribution or sale outside of the scope permitted under the Head Licences would constitute a breach of its terms. Given that the Trustee cannot acquire better rights than a bankrupt, the Trustee would not have the right to resell the inventory outside of the scope of the permitted distribution and sale terms contained in the Head Licences.
23. Given the above, during the first meeting of the inspectors of the Companies' estates, the Trustee expects to request authorization from the inspectors to return the inventory to Direct Brands, Inc. in exchange for the reduction of its debt, which is approximately \$1.4 million owing from DB Media and \$3 million owing from DB Media Canada.
24. Given the massive volume of inventory units, the trustee expects that taking a physical count of the inventory will involve a substantial expense.
25. The Trustee is of a view that due to the nature of the inventory and given that there will be limited realization from such inventory, the cost of taking physical count of such inventory will be unduly expensive and not in the best interests of the Companies' estates and their stakeholders.



26. Nonetheless, the Trustee intends to conduct a spot audit of such inventory.

**Recommendation**

27. The Trustee respectfully requests and recommends that the Procedural Consolidation Order be made by this Honourable Court in the form attached to the within Notice of Motion.

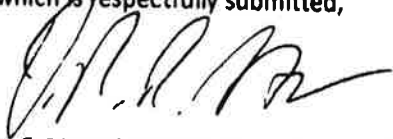
28. The Trustee also respectfully requests and recommends that a separate order be made by this Honourable Court, *inter alia*:

- a. relieving the Trustee of any obligation to send notice of the bankruptcy and of the first meeting of creditors to such creditors of DB Media Distribution whose claims in the aggregate do not exceed \$100 in the manner prescribed under section 102 of the BIA;
- b. relieving the Trustee of its obligation to include a full list of creditors in the notice of the bankruptcy and of the first meeting of creditors, which the Trustee will send to the creditors with the claims of \$100 or more in the manner prescribed in section 102 of the BIA, and authorizing the Trustee to instead make a one-line entry for the customers and employees and to direct creditors to a website which will contain a complete list of creditors;
- c. authorizing the Trustee to post a complete list of creditors of DB Media Distribution, including customer names with credit balances, on a dedicated webpage to be set up by the Trustee on its website;
- d. authorizing the Trustee to redirect DB Media Distribution's book and DVD club websites to a website hosted by the Trustee, which will provide notice of the bankruptcy of DB Media Distribution and provide a link to the Trustee's website containing the statutory notice of the bankruptcy and documents for filing proofs of claim;
- e. relieving the Trustee of any responsibility to perform any act or take any steps in respect of its obligations under subsections 102(1) and (2) of the BIA as such obligations relate

to the creditors noted in paragraph a. above, other than supplying a form of proof of claim and proxy to those creditors upon their request of same; and

- f. relieving the Trustee of any obligation to take full physical count of the inventory of DB Media Distribution and, otherwise, of any responsibility to perform any act or take any steps in respect of its obligations under subsection 16(3) of the BIA, other than to conduct a spot audit of the inventory.

All of which is respectfully submitted,

A handwritten signature in black ink, appearing to be 'J. P. R. B.', written in a cursive style.

**Alvarez & Marsal Canada Inc.** in its capacity  
as trustee in bankruptcy of DB Media  
Distribution Inc., DB Media Distribution  
(Canada), CH LLC (Canada) and  
CH SUB LLC (Canada) and not in  
its personal or corporate capacity