

**IN THE COURT OF QUEEN'S BENCH OF ALBERTA
IN BANKRUPTCY & INSOLVENCY
JUDICIAL DISTRICT OF EDMONTON**

**IN THE MATTER OF THE PROPOSAL OF
TRANSGLOBAL COMMUNICATIONS GROUP INC.**

Trustee's Report

Introduction and Purpose

Transglobal Communications Group Inc. ("Transglobal", the "Company") filed a Notice of Intention to Make a Proposal ("NOI") on May 20, 2008, and Meyers Norris Penny Limited consented to act as Trustee. A Cash Flow Projection was filed on May 30, 2008 and an Order granting an extension for the time for filing the Proposal to July 7, 2008 was granted on June 19, 2008. Copies of the June 19, 2008 Order granting the extension and the Trustee's Report dated June 17, 2008 (the "First Report") were mailed to the creditors on July 2nd, 2008.

It is our view that Transglobal will not be in a position to file a definitive Proposal by July 7, 2008.

Stone Sapphire Litigation

Subsequent to the First Report a decision was rendered on the application for reconsideration of the summary judgment heard in April 2008; and it is the Trustee's understanding that the Court refused the reconsideration application, upholding the original summary judgment. Counsel for the Company has advised that Transglobal has instructed counsel to appeal the decision.

It is also our understanding that prior to the decision being rendered, Stone Sapphire Ltd. sought to have the stay of proceedings lifted as against Transglobal, such that the \$1.53M in Court could be paid to them, however, this application was denied at the same time the decision to uphold the original summary judgment was issued. HSBC takes the position that they hold security over those funds by virtue of their General Security Agreement executed with the Company. On May 23, 2008, HSBC appeared in Court and obtained an Order authorizing them to bring an application for determination of its claim and the

priority to the funds in Court. The date for the hearing of this application has been set for August 15, 2008.

Secured Creditors

As indicated in the First Report, our review of the Company's banking activity indicates that two Business Development Bank of Canada ("BDC") term loan payments, totaling approximately \$8,500, were directly debited from the Company's account in June 2008. Also as indicated in the First Report, the Company's counsel advises that management has had discussions with BDC and that the payments are to be stopped while the stay of proceedings is in place.

As indicated in the First Report, our review of the Company's banking activity indicates that two cheques were written on May 27, 2008 to Chrysler Credit totaling approximately \$2,000. In addition to these payments one cheque was written to Key Equipment Financing (the lessor of the Company's computers) for \$2,955.14 on June 25, 2008. All of these payments appear to be post NOI obligations.

Assets

Accounts Receivable

The Company reports Accounts Receivable as at June 25, 2008, totaling \$81,465 CAD and \$2,303,786 USD, for a combined CAD total of \$2,536,785 (using an exchange rate of \$1.065776 CAD/USD). This balance has declined \$412,323 CAD from the June 13, 2008 balance stated in the First Report. We also note that the Company's cash position from June 13, 2008 to June 25, 2008 has increased by approximately \$141,000 CAD. As reported previously, we note that \$745,013 CAD (using an exchange rate of \$1.065776 CAD/USD) is reported to be due from Stone Sapphire Limited, a customer with whom the Company is currently involved in litigation, and is also listed as a creditor at the time of the filing of the Notice of Intention. Accordingly, it is our opinion that it is unlikely this account would be collected in the normal course.

Of the remaining balance of \$1,791,772 (\$2,536,785 - \$745,013), \$848,399 (or 47%) is less than 60 days outstanding, \$236,273 (or 13%) is 61 - 120 days outstanding, and \$707,100 (or 40%) is greater than 120 days outstanding. We have reviewed these accounts with management, and the Company anticipates that for the most part the accounts are fully collectable, with the potential of some returned product from four of the 25 creditors listed. However, we note that three additional accounts receivable were also listed as creditors at the time of the filing of the Notice of Intention, and accordingly, may assert a right of set-off. The potential set-off pertaining to these three accounts total \$218,111 CAD.

As reported previously, certain of the Company's Accounts Receivable are insured by Export Development Canada ("EDC") to a maximum coverage of \$3,000,000 USD. We have reviewed recent documents pertaining to the Accounts Receivable Insurance Policy, and note that USD accounts are insured to a maximum of 90%, subject to restrictions pertaining to credit limits and credit term periods which have been determined on an individual account basis. We also note from our review that it does not appear that CAD accounts are insured by EDC. We have compared the Accounts Receivable listing as at June 25, 2008 to the listing of current USD credit approvals, and estimate that of the USD accounts, approximately \$1,020,569 USD receivables are eligible for insurance. Accordingly, we estimate that based on insurance coverage of 90%, \$918,512 USD would be collectable through the Company's insurance policy. According to management, premiums for EDC insurance are up to date and Accounts Receivable continue to be insured

Inventory

Management has provided an Inventory Valuation Report as at June 30, 2008, which values the Company's inventory at \$1.72M at average cost which is approximately \$180,000 less than the inventory value for May, 2008. Consolidated financial statements for the year ended December 31, 2007 reports inventory totaling \$555,000, valued at lower of cost or net realizable value. Management advises that a large number of inventory returns occurred in the current fiscal period, specifically pertaining to one of the Company's largest unsecured creditors, QVC Inc. The Trustee is unaware at this time what realization could be anticipated from the Company's inventory on a liquidation basis.

Post-Filing Operations

Subsequent to the Company's filing of a Notice of Intention on May 20, 2008, Transglobal has continued to carry on business. Sales for May, 2008 are reported to total approximately \$939,218. Sales were projected to total \$1,158,951 in May, 2008 which is a negative variance of approximately \$220,000 or 19%. Sales for June 2008 are reported to total approximately \$1,362,047. Sales were projected to total \$1,155,609.62 which is a positive variance of approximately \$206,438 or 18%. Management advises that sales in May are at a lower level than the same time period last year due, primarily in their opinion, to customers ordering closer to their "in store" dates in order to consolidate freight and reduce costs. Management advises that this trend has been taking place over the past few years as retailers look to reduce costs by facilitating more of the shipping and warehousing process in China, where costs such as labour and overhead are substantially lower than in the US.

As previously reported, the Company is continuing to pay for some goods and services on a cash basis; however, certain creditors have continued to operate with Transglobal on credit terms, which, management advises they are adhering to.

The Company continues to utilize a payroll service in Canada and in the United States, which ensures that staff who are currently employed are paid on a regular basis, and all payroll deductions are remitted. We are advised by management that employees in the Hong Kong office are also being paid on a current and regular basis.

Further to the First Report, management continues to negotiate the terms of a new lease for the Company's premises in Edmonton. As indicated in the First Report, management had anticipated having the new lease in place for July, 2008 however negotiations have taken longer than expected. It is our understanding from management that the Company and the landlord have reached a verbal agreement to reduce the current space occupied by two thirds and the rent will be reduced by approximately \$8,000 per month. The Company will be required to complete some small renovations that are expected to cost no more than \$7,500.

Payment of Pre NOI Debts

Yun Choy Ltd.

Yun Choy Ltd. is a supplier in China that supplies manufactured goods for the Company and was reported to be owed \$374,209 at the NOI. We believe that this amount was understated as all invoices had not yet been rendered to the Company.

Management now advises that Yun Choy Ltd. has been paid \$453,822.28 USD for debts outstanding prior to the filing of the NOI as a result of transfers from irrevocable letters of credit. Letters of credit were issued by Dollar Tree Stores Inc. (a customer of the Company) pertaining to purchase orders placed with the Company, for goods to be manufactured by Yun Choy Ltd. The letters of credit contain a transfer clause that allows the Company (as the beneficiary) to transfer a set portion of the letter of credit to another beneficiary (in this case Yun Choy Ltd.). The issuance of the transfer is similar to the Company issuing a separate letter of credit directly to Yun Choy Ltd., in that once it is initiated it is irrevocable unless the beneficiary of the transfer (Yun Choy Ltd.) consents. Management advises that the set up of these transfers, as well as the shipment of the finished product, were completed prior to the filing of the NOI, and that a letter of credit was required in order to do business with Yun Choy Ltd. Yun Choy Ltd., however, did not remit its paper work to redeem their portion of the letter of credit until after the filing of the NOI. The actual payments to the Company and to Yun Choy Ltd. from the letters of credit took place after the filing of the NOI due to the time required to redeem the letters of credit. Management advises that they have been successful in recovering additional amounts due to some late shipments by Yun Choy Ltd as the letters of credit

contained conditions whereby late fees could be levied on late shipments. While prior business practices of the Company would have been not to pursue collecting these charges, in an effort to improve profitability, the Company has ensured all charges have been collected where possible. In reviewing the Company's bank statements the Trustee has been able to identify late fee charges in the amount of \$35,154 being collected during the period of June 19 to June 23, 2008.

Zhe Jiang Ruyi Gifts & Crafts Co.

Zhe Jiang Ruyi Gifts & Crafts Co. ("Ruyi") is another supplier of manufactured goods to the Company located in China. The Trustee notes that Ruyi was not listed as a creditor at the time the NOI was filed.

Management advises that in June, 2008, \$211,986.13 CAD has been paid to Ruyi for debts incurred prior to the filing of the NOI. The Company advises that the supplier ceased work on all existing orders and refused to complete these orders until payment of all outstanding invoices was received. Management advises that Ruyi is in the process of completing numerous orders for different customers of the Company and as such made a decision to remit payment in order to ensure that production continued.

Natexport

Natexport (a division of National Bank) provided pre-shipment financing to the Company and was listed as having a debt outstanding of \$400,000 at the NOI.

It is the Trustee's understanding that Natexport filed a claim with Export Development Canada ("EDC") for amounts owed to them by the Company. EDC paid the claim to Natexport in the amount of \$440,397.49 USD and subsequently took an assignment of debt dated June 20, 2008. EDC has provided the Trustee with a copy of the Assignment of Debt and confirmed that Natexport's claim has been paid.

Colorado Distribution Group

Colorado Distribution Group owns warehouse space utilized by the Company in the United States. Management advises that the Colorado Distribution Group has refused to ship product or advise of inventory levels stored within their warehouses until the Company pays the \$4,386.36 debt outstanding at the NOI. Management is considering paying this debt in order to have goods worth approximately \$7,000 shipped to a customer. The Trustee notes that based upon the Company's June 30, 2008 inventory report, approximately \$21,621.00 USD in inventory is currently stored with the Colorado Distribution Group so payment of the \$4,386.36 would allow shipment of another \$14,261 (\$21,621 - \$7,000) of inventory.

Business Plan

Management is continuing to review all operating processes in light of the former controller's alleged misappropriation of Transglobal's assets, and in order to implement reductions where possible concerning production costs and administrative overhead. Management has hired a temporary controller and is in the process of interviewing applicants as a permanent hire to assist with the financial management and reporting requirements.

Further to the First Report, we are advised by management that they are currently in detailed discussions with four separate lenders, namely Maple Trade Finance Inc, Royal Bank of Canada, RBC Capital Markets and Century Services Inc. with respect to refinancing of the Company's operating loans and pre-shipment financing and that two of the lenders are expected to offer term sheets in the near future. Management is confident that should it be determined that HSBC has priority to the funds currently held in Court, and the funds are made available to HSBC, that the proposed financing (in particular with Maple Trade Finance Inc.) will be sufficient to pay HSBC in full and secure additional funding for operations and the funding of a Proposal to its creditors. While the Company continues to discuss financing options, management advises that it has also entered into preliminary discussions with a competitor regarding the sale of the Company.

Further to the First Report, the Company expects to receive some recovery of funds alleged to have been misappropriated by the former Controller. Since the filing of the First Report there have been some examinations for discovery, however, the timing for the resolution of the claim is still uncertain.

An extension of time will enable the Company to continue to operate during its peak season while implementing cost saving measures; to continue discussions with potential lenders concerning refinancing; to continue discussions with potential purchaser(s) of the Company; and may permit sufficient time to determine the priority to the approximate \$1.53M USD currently held in Court. All of these steps will enable management to present a more comprehensive and definitive Proposal to its creditors than Transglobal could at the present time.

With regard to the August 15, 2008 Court Hearing to determine entitlement to the \$1.53M USD currently held in Court, the Company is currently weighing the effect of the Court's decision to award the monies to either HSBC or Stone Sapphire Ltd. and how it will subsequently impact the structure of its proposal.

Subsequent to the June 17, 2008 First Report, the Trustee has continued to request financial information for the purposes of monitoring on a weekly basis. While the Company has provided the required information, it has not been submitted on a weekly basis, rather the bulk of the information was received between July 2 and 3, 2008. Management attributes this to the lack of a controller, the recent departure of their book


keeper and competing priorities being placed on management. Management advises that with the recent hiring of a temporary controller, the financial information should be provided in a more timely manner.

It is our opinion that:

- a) Despite the Company not forwarding the monitoring information to the Trustee on a weekly basis the Company has and continues to act in good faith and with due diligence in formulating a Proposal,
- b) The Company would likely be able to make a viable Proposal if an extension was granted, and
- c) No creditor will be materially prejudiced if an extension is granted and the Company continues to act in good faith.

DATED this 4th day of July, 2008.

Meyers Norris Penny Limited
in it's capacity as Trustee in the Division I Proposal of
Transglobal Communications Group Inc.
and not in it's personal capacity



Grant Bazian, CIRP, Trustee
Senior Vice President