

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE COMPANIES' CREDITORS
ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

AND DOMENICO SARAFINO AS A PERSON INTERESTED IN THE MATTER OF A
PLAN OF COMPROMISE OR ARRANGMENT OF HYDRX FARMS LTD.,
CANNSCIENCE INNOVATIONS INC. AND SCIENTUS PHARMA INC.

(the "Applicants")

FIRST REPORT OF THE MONITOR

INTRODUCTION

1. On March 22, 2021, the Applicants brought an application (the "CCAA Application") before this Court returnable on March 22, 2021, seeking an initial order pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 as amended ("CCAA") to, among other things, obtain a stay of proceedings to allow them an opportunity to obtain funding to restructure the affairs of the company or to market the company for sale.
2. On March 22, 2021, the Court granted an initial order in these proceedings (the "Initial Order") that, among other things, appointed Schwartz Levitsky Feldman Inc. ("SLF") as monitor of the Applicants in these CCAA proceedings (in such capacity, the "Monitor"), and granted a stay of proceedings for the initial 10-day period (the "Stay Period").
3. The Court scheduled a comeback motion to be heard on March 31, 2021 (the "Comeback Motion").

PURPOSE

4. The purpose of this first report of the Monitor (the “**First Report**”) is to provide information to the Court on:
 - a. the Applicants’ operations since granting the Initial Order;
 - b. the Monitor’s activities since its appointment;
 - c. the Applicants’ motion for approval of:
 - i. the Administration Charge (as defined and described below);
 - ii. the return of a machine to C-Tech Innovations Ltd.; and
 - iii. an extension of the Stay Period to May 3, 2021
 - d. the Monitor’s recommendations with respect to the above.

TERMS OF REFERENCE

5. In preparing this First Report, and making comments herein, the Monitor has been provided with, and has relied upon, unaudited financial information, books and records prepared by the Applicants, discussions with management of the Applicants (“**Management**”), and information from other third-party sources (collectively, the “**Information**”). Except as described in this Report in respect of the Applicants cash flow forecast:
 - a. the Monitor has reviewed the Information for reasonableness, internal consistency and use in context in which it was provided. However, the Monitor has not audited or otherwise attempted to verify the accuracy or completeness of such information in a manner that would wholly or partially comply with Generally Accepted Auditing Standards (“**GAAS**”) pursuant to the Chartered Professional Accountants Handbook and, accordingly, the Monitor expresses no opinion or other form of assurance contemplated under GAAS in respect of the Information; and
 - b. some of the information referred to in this First Report consists of forecasts and projections. An examination or review of the financial forecast and projections, as outlined in the Chartered Professional Accountants Handbook, has not been performed.
6. Future oriented financial information referred to in this First Report was prepared based on Management’s estimates and assumptions. Readers are cautioned that since projections are

based upon assumptions about future events and conditions that are not ascertainable, the actual results will vary from the projections, even if the assumptions materialize, and the variations could be significant.

7. Unless otherwise indicated, the Monitor's understanding of factual matters expressed in this Report concerning the Applicants' and their business is based on the Information, and not independent factual determinations made by the Monitor.
8. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars.

BACKGROUND

9. Hydrx Farms Ltd. ("Hydrx") is a private corporation incorporated under the Canada Business Corporations Act on April 29, 2014.
10. Hydrx has two wholly owned subsidiaries, Scientus Pharma Inc. ("Scientus Pharma") and CannScience Innovations Inc. ("CannScience"). Scientus Pharma was incorporated on the premise that it would be the go forward corporation name of Hydrx if the business ever went public and CannScience was acquired in March 2017 principally for its patents. Neither company has carried on any active business while owned by Hydrx.
11. Hydrx is a vertically-integrated biopharmaceutical company with a focus on developing and commercializing pharmaceutical grade cannabinoid derivative products.
12. The company was approved by Health Canada as a Controlled Dry Substance Licensed Dealer in October of 2016 and subsequently received a Licensed Product Cultivation License in September of 2017 which was subsequently amended to include among other things:
 - a. cultivation;
 - b. the sale of dried flowers;
 - c. the processing of capsules and oils;
 - d. the sale of capsules and oils; and
 - e. the processing and sale of edibles and extracts.
13. Hydrx operates out of a 46,000 square foot facility which it owns at 1130 Champlain Court, Whitby, Ontario.

UPDATE ON THE APPLICANTS' OPERATIONS

14. Since the date of the Initial Order, the Applicants have focused on trying to maintain and restart existing operations as well as pursuing expressions of interest from various parties to buy or refinance the Applicants.

MONITOR'S ACTIVITIES TO DATE

15. Since the granting of the Initial Order, among other things, the Monitor has been:
 - a. assisting the Applicants in their communications with stakeholders;
 - b. responding to calls and emails received from creditors and other parties with respect to these CCAA proceedings;
 - c. reviewing the Hydrx receipts and disbursements; and
 - d. participating in discussions with Management with respect to the cash flow forecasts prepared by the Applicants.
16. The Applicants' weekly cash flow forecast for the period March 22, 2021 to June 25, 2021 (the "**Cash Flow Forecast**") as appended to the Pre-Filing Report of the Proposed Monitor dated March 22, 2021 (the "**Pre-Filing Report**") has been updated to remove interest payments as they are stayed by the Initial Order. The updated Cash Flow Forecast is attached as Appendix "A" to this First Report. Given the limited number of business days that have elapsed since the date of the Pre-Filing Report, the Applicants do not anticipate any other material change in the weekly Cash Flow Forecast. The Cash Flow Forecast shows that with the \$500,000.00 available from the "Restart Group", the Applicants will have sufficient liquidity during the first 13 weeks of the CCAA Proceedings. The Restart Group is a group of individuals related to the Applicants who have agreed to finance the company during the CCAA period. The Monitor will continue to work with the Applicants to review actual receipts and disbursements and any variances, if any from the Cash Flow Forecast and provide an update to the Court in its next report.
17. The Monitor has established a case website at www.slfinc.ca (the "**Monitor's Website**"). All court documents and certain other documents will be posted on the Monitor's Website. Further, the Monitor has arranged for a toll-free hotline phone number, 1-844-572-2235 for calls related to this matter and an e-mail address insolvency@slf.ca for e-mail correspondence with the Applicants creditors and other parties related to the CCAA Proceedings.

18. Pursuant to the Initial Order, the following notices have been posted on the Monitor's Website, and/or sent to the Applicants' stakeholders since the date of the Initial Order:
- a. On March 24, 2021, the Monitor posted a copy of the CCAA application materials, the Proposed Monitor's Report and the Initial Order.
 - b. On March 24, 2021, the Monitor sent a notice by email and prepaid ordinary mail about the CCAA proceedings, the toll-free telephone number and the Monitor's email address (the "Notice to Creditors") to all known creditors who have a claim against the Applicants of more than \$ 1,000.00 (the "Known Creditors"), as per information provided by the Applicants. A copy of the Notice to Creditors was also posted on the Monitor's website;
 - c. On March 26, 2021, the Monitor posted on the Monitor's Website a list showing the names of the Known Creditors and amounts owing per the Applicants' books and records; and
 - d. On March 27, 2021, the Monitor published the Notice to Creditors in the Globe and Mail (National Edition).

ADMINISTRATION CHARGE

19. The Restart Group has agreed to provide initial funding of up to \$250,000.00 for professional fees in these CCAA Proceedings.
20. The Restart Group seeks an Administration charge for this amount in priority to all other charges against the Applicants' current and future assets, undertakings and properties (the "Administration Charge")
21. It is proposed that Administration Charge will secure the fees of the Monitor, counsel to the Applicants and the Monitor's independent counsel over at least the next 30 day period. Professional fee obligations secured by the Administration Charge will be paid in the ordinary course from funding provided by the Restart Group and subject, ultimately, to the approval of this court.

C-TECH INNOVATION LTD.

22. Hydrx holds a purchase money security interest over a machine from C-Tech Innovations Ltd. for which it owes in excess of \$ 500,000.00. Hydrx's future plans do not include use of the machine and the Applicants wish to return the machine (the "Machine") to the manufacturer to reduce/extinguish the outstanding debt.

STAY EXTENSION

23. The Stay Period is currently set to expire on March 31, 2021. The Applicants are requesting an extension of the Stay Period until May 3, 2021.
24. The Monitor is of the view that the requested extension of the Stay Period is appropriate for the following reasons:
 - a. the Applicants require the extension in order to evaluate expressions of Interest received and consider their options.
 - b. the Applicants continue to operate in good faith and with due diligence since the date of the Initial Order.
25. Based on the Cash Flow Forecast for the period March 22, 2021 to June 25, 2021, the Monitor is of the view that the Applicants will have sufficient liquidity to fund their operations which includes funding from the Restart Group.

CONCLUSIONS AND RECOMMENDATIONS

26. For the reasons stated above the Monitor supports the relief sought by the Applicants to;
 - i. grant an Administration Charge of \$ 250,000.00;
 - ii. authorize the return of the Machine to C-Tech Innovation Ltd.; and
 - iii. approve the extension of the Stay Period to May 3, 3021.

All of which is respectfully submitted this 29 day of March, 2021.

**SCHWARTZ LEVITSKY FELDMAN INC., in its capacity
as Monitor of the Applicants, and not in
Its corporate or personal capacity.**


Per: Alan Page, CPA, CA, CIRP, LIT

APPENDIX "A"

Appendix —
Unaudited Cash Flow — Prepared by Management

Hydrex From U.S.A.	4 Week Cash Flow Summary														Total
	Week 1 19-Mar	Week 2 26-Mar	Week 3 2-Apr	Week 4 9-Apr	Week 5 16-Apr	Week 6 23-Apr	Week 7 30-Apr	Week 8 7-May	Week 9 14-May	Week 10 21-May	Week 11 28-May	Week 12 4-Jun	Week 13 11-Jun		
CASH IN TRUST															
Receipts		2,000	2,050	4,100	6,000	11,800	12,400	12,400	14,800	14,800	16,300	16,300	16,000	131,600	
Medical Commodity Sales (1)	-	-	6,000	31,500	37,200	27,200	27,300	31,600	31,600	36,400	36,400	36,400	36,400	311,900	
Contract Processing (2)	-	-	-	-	-	-	6,000	6,000	6,000	30,200	16,600	16,600	16,600	718,000	
Retail Sales (3)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Operating Disbursements															
Payroll and Benefits (4)	(9,000)	(9,000)	(9,000)	(9,000)	(12,000)	(12,000)	(12,000)	(12,000)	(11,000)	(12,000)	(12,000)	(12,000)	(11,000)	(144,000)	
Consulting Fees (5)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	(17,000)	
General Labor	(1,000)	(1,000)	(1,725)	(4,060)	(4,060)	(4,060)	(5,046)	(5,046)	(5,481)	(5,481)	(5,460)	(5,460)	(5,460)	(52,227)	
COGS	-	(104)	(1,208)	(7,340)	(5,100)	(5,950)	(5,950)	(6,904)	(7,264)	(7,264)	(7,890)	(7,890)	(8,260)	(66,227)	
Supplies and Raw Materials	(1,800)	(1,800)	-	-	(1,800)	(1,800)	-	-	-	-	-	-	-	(5,000)	
Regulatory Advisor	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(2,625)	(18,125)	
Utilities	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(800)	
Office Administration	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(7,025)	(50,000)	
Other Operating Expenses (6)	(1,000)	-	(12,000)	-	(12,000)	(12,000)	(12,000)	(12,000)	(12,000)	(12,000)	(12,000)	(12,000)	(12,000)	(113,000)	
Capital Expenditures	(26,750)	(26,750)	(32,883)	(30,170)	(33,403)	(31,153)	(30,811)	(31,173)	(31,151)	(32,364)	(32,774)	(32,774)	(31,043)	(193,000)	
Total Operating Disbursements	(50,000)	(50,000)	(115,000)	(115,000)	(115,000)	(115,000)	(110,000)	(110,000)	(108,000)	(110,000)	(110,000)	(110,000)	(108,000)	(700,000)	
Net Cash Inflows / (Outflows)	(26,250)	(78,900)	(45,833)	(19,700)	(10,600)	(27,850)	(4,811)	(5,667)	2,200	13,600	21,425	21,425	21,955	22,955	
Cash															
Beginning Balance	500,000	421,250	342,341	342,510	372,740	253,135	223,980	219,169	274,822	242,321	245,956	247,381	248,806	248,806	
Net Cash Inflows / (Outflows)	(76,250)	(78,900)	(45,833)	(19,700)	(10,600)	(27,850)	(4,811)	(5,667)	2,200	13,600	21,425	21,425	21,955	22,955	
Ending Balance	423,250	342,341	342,510	372,740	253,135	223,980	219,169	219,169	274,822	242,321	245,956	247,381	248,806	271,761	

NOTES
 (1) Existing inventory to be marketed on Hydrex medical sales platform.
 (2) Contract Processing (revenue contracts have been executed and will start production March 15)
 (3) Retail sales commencing following 60 day notification period to Health Canada
 (4) Employees have been laid off or furloughed in 2020
 (5) Key Personnel are contractually engaged as consultants
 (6) Repairs, Reconfigure production line for new contract