VTECH/LEAPFROG MERGER INQUIRY

Summary of hearing with Morgan Stanley on 19 October 2016

LeapFrog's financial situation, re-structuring and liquidation

1. Morgan Stanley told us that it was contacted by the board of LeapFrog after LeapFrog had received an unsolicited offer from a potential buyer. Thereafter, Morgan Stanley was engaged to provide financial advisory services in connection with an evaluation of strategic alternatives, including a potential sale of the company. Morgan Stanley told us that among the alternatives they considered was whether or not the opportunity existed to raise a significant amount of incremental equity capital in order to help fund the business. Morgan Stanley was not asked to advise on LeapFrog's credit facility or on other types of debt financing alternatives and did not engage in discussions with LeapFrog's creditors on LeapFrog's behalf.

2. Morgan Stanley said that LeapFrog was losing a substantial amount of money and a significant investment of capital would have been required to maintain the business. It highlighted that some of the potential interested parties it contacted expressed concern as to whether LeapFrog could be turned around to create a profitable and self-funding enterprise.

3. Morgan Stanley told us that it had reviewed projections prepared by LeapFrog's management concerning the company's cash balances during calendar year 2016. The management projections showed that LeapFrog would not have sufficient liquidity available from its cash balances and under its existing credit facility to fund its operations as soon as the summer 2016.

4. [✂]

5. Morgan Stanley said that the toy market is highly seasonal and typically has a significant build of inventory and receivables through the summer and leading up to the Christmas selling season. Morgan Stanley stated that the projections provided by LeapFrog's management suggested that the amount of cash the company had and estimated availability under its credit facility was not sufficient to fund the LeapFrog business as soon as the summer of 2016.

6. [✂]

7. Morgan Stanley noted that during the course of conversations they were having with prospective buyers, one potential buyer indicated [✂] that the potential buyer could potentially be interested in an asset acquisition of the company’s brand, toy business and interactive reading business but had no interest in the tablet business. Further, according to Morgan Stanley, the amount of money this potential buyer was willing to pay for the toy business and brand was not sufficient to maintain a standalone sustainable tablet business.

Potential purchasers

8. Morgan Stanley explained that in assessing how actionable proposals received from interested parties were, it relied on its experience as a firm involved in executing merger and acquisition transactions and that the factors that were considered include, among other things, how far along the interested party was in its due diligence, access to financing, timing and certainty (eg receipt of any required regulatory, governmental or other approvals).

9. For example, a party that had submitted a proposal indicated that the proposal was subject to approvals by several government and regulatory agencies and as a result its timeline to receive the necessary approvals and complete the transaction would be at least five to six months. Morgan Stanley explained that this timing was a significant consideration in the context of a company that based on management’s forecasts did not have sufficient liquidity to survive the summer.

10. Morgan Stanley confirmed that [✂] was the interested party that submitted a proposal on 23 December 2015 to purchase LeapFrog and a revised proposal on 29 January 2016. The revised proposal dated 29 January proposed to invest capital in a new class of stock that would have resulted in [✂] becoming the majority owner of LeapFrog and was not a bid to purchase the company. [✂]

11. Morgan Stanley said that it had not created a ranking of ‘next best bids’ after VTech’s offer. Given the financial situation of LeapFrog, Morgan Stanley continued to pursue every available option as long as it could and to the extent available until a definitive transaction was reached.

12. Morgan Stanley said it was important to recognise that [✂] revised proposal was submitted without a marked up contract and only provided very high level supporting information for their proposal. Morgan Stanley stated that there were incremental risks to the revised proposal. In particular, Morgan Stanley explained that the revised proposal was subject to further due diligence and

they had not provided a detailed proposal in the form of a marked-up contract as to how the investment would actually work, as well as the risks of requiring a shareholder vote, which the VTech offer did not require. These factors were considered in the context of the advice given by Morgan Stanley to the LeapFrog board.

13. [✂]

14. [✂]

15. Morgan Stanley said that [✂] had requested three weeks to complete due diligence and negotiate and document a transaction following its second proposal of 29 January. In its second proposal, [✂] also requested a period of exclusivity [✂]

16. Morgan Stanley said that conversations with the Class B shareholders took time and were difficult negotiations. [✂]

17. With respect to [✂], which withdrew its bid in November 2015, Morgan Stanley said that [✂] was in conversations with LeapFrog for a long period of time and was the party that initially submitted an indication of interest which led to the company deciding to retain Morgan Stanley. [✂] had marked up the merger agreement, exchanged multiple drafts and engaged in advanced negotiations. [✂] indicated that in addition to the cost of purchasing the company, the resources required to turnaround and stabilise the LeapFrog business were substantial and it was not willing to accept the business risk associated with turning around the company. Morgan Stanley said that following the decision to withdraw its proposal, [✂] indicated that it might be prepared to purchase select assets from LeapFrog in the even that LeapFrog entered bankruptcy.

18. Morgan Stanley could not speculate on whether other parties would have been successful in acquiring LeapFrog or some of its assets in the event that VTech withdrew its bid. Morgan Stanley told us that it viewed one of its primary responsibilities as helping LeapFrog avoid the pending liquidity crisis it would have faced. Morgan Stanley highlighted that it recommended to the LeapFrog board that all ongoing channels of communication should be pursued, rather than focusing on one bidder. [✂] This was also the reason why Morgan Stanley maintained contact with a number of parties right up until VTech purchased LeapFrog.

Views on the merger

19. Morgan Stanley told us that it was pleased that it found a transaction that saved LeapFrog from a pending liquidity crisis.