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COURT COURT OF QUEEN'S BENCH OF ALBERTA

JUDICIAL CENTRE CALGARY

APPLICANT OEL PROJECTS LTD.

DOCUMENT **FIRST REPORT OF THE PROPOSAL TRUSTEE
BDO CANADA LIMITED
MAY 22, 2020**

ADDRESS FOR
SERVICE AND
CONTACT
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PARTY FILING THIS
DOCUMENT

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**FIRST REPORT OF THE PROPOSAL TRUSTEE
BDO CANADA LIMITED
MAY 22, 2020**

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INTRODUCTION

1. On May 20, 2020 (the “**Filing Date**”), OEL Projects Ltd. (“**OEL**” or the “**Company**”) filed a Notice of Intention to Make a Proposal (the “**NOI**”) pursuant to the *Bankruptcy and Insolvency Act* (the “**BIA**”). BDO Canada Limited consented to act as trustee (the “**Proposal Trustee**”) of the proceedings.
2. On May 8, 2020, OEL’s parent company, McIntosh Perry Consulting Engineers Ltd. (“**McIntosh Perry**”), issued a formal demand letter and *Notice of Intention to Enforce Security* (the “**Demand Notice**”) to OEL in respect of OEL’s obligations to McIntosh Perry in the amount of approximately \$9.2 Million pursuant to the terms of an *Amended and Restated Promissory Note* dated April 1, 2017 and a *General Security Agreement* dated April 1, 2017 (collectively the “**McIntosh Perry Security**”).
3. OEL subsequently consented to the immediate enforcement of the McIntosh Perry Security and the appointment of a Receiver.
4. On May 26, 2020, OEL is scheduled to make an application to the Court of Queen’s Bench of Alberta (the “**Court**”) seeking approval of a sale of substantially all of its assets (other than certain excluded assets) to McIntosh Perry Energy Ltd. (“**MPEL**”), a related entity also owned by McIntosh Perry, pursuant to an *Asset and Share Purchase Agreement* dated May 21, 2020 (the “**ASPA**”).
5. The purpose of this report (the “**First Report**”) is to provide the Court with:
 - Background information in respect of the business and affairs of OEL;
 - The results of the Proposal Trustee’s review of OEL’s financial position;
 - Details in respect of the proposed transaction with MPEL (“**Proposed Transaction**”) and the Proposal Trustee’s analysis thereof; and
 - The Proposal Trustee’s recommendation in respect the Proposed Transaction.

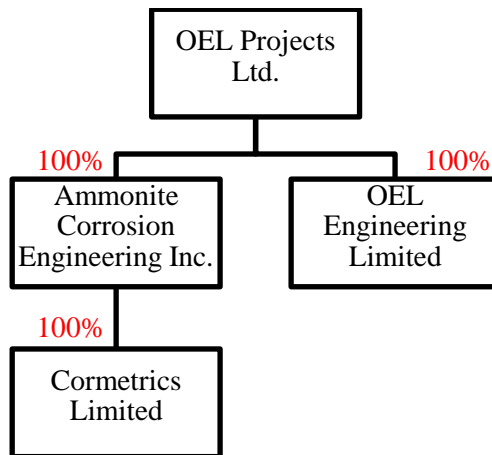
TERMS OF REFERENCE

- 6. In preparing this First Report, the Proposal Trustee has necessarily relied upon unaudited financial information and records of OEL and its subsidiaries, supplemented by discussions with representatives of the Company (collectively “**Management**”). The Proposal Trustee has not performed an audit or other verification of such information and accordingly, the Proposal Trustee expresses no opinion or other form of assurance in respect of such information.

BACKGROUND

Corporate Structure and Business Operations

- 7. OEL is a privately held company incorporated in the Province of Alberta. McIntosh Perry acquired 100% of the voting shares of OEL as of October 2016.
- 8. McIntosh Perry is controlled by various entities of the Signal Hill Equity Partners group (“**Signal Hill**”). OEL is the 100% shareholder of two subsidiaries which also results in an indirect ownership interest in a third entity. The organizational structure of OEL and its subsidiaries is as follows:



- 9. OEL, originally founded in 1971, operates from two leased premises in Calgary and provides full service engineering, design, procurement and facility construction management services to the Western Canadian oil and gas industry.

10. On May 20, 2020, the Company formally terminated 20 employees who had previously been temporarily laid off (the “**Former Employees**”) in contemplation of the filing of the NOI and the Proposed Transaction. The Proposal Trustee understands that the Former Employees were paid all outstanding wages, salaries, commissions and/or compensations.
11. MPEL has 34 remaining employees (the “**Current Employees**”). The Proposal Trustee understands that MPEL has offered employment to all of these individuals and that MPEL will assume any accrued vacation pay obligations in respect of the Current Employees.
12. Ammonite Corrosion Engineering Inc. (“**Ammonite**”), which was acquired by OEL in 2014, is based out of Calgary provides corrosion prevention and mitigation programs and solutions to customers in the oil and gas industry. Ammonite operates from leased premises and has two full employees.
13. Cormetrics Limited (“**Cormetrics**”) is also based out of Calgary and provides failure analysis, corrosion testing chemical programs guidance and field investigations to the oil and gas industry. Cormetrics currently has four employees.
14. The Proposal Trustee understands that OEL Engineering Limited is a dormant entity with no assets.

Secured and Priority Creditors

15. The books and records of OEL reflect an obligation to McIntosh Perry of approximately \$9.2 Million. As discussed above, this obligation is secured pursuant to the McIntosh Perry Security. The Proposal Trustee’s legal counsel has undertaken an independent review of the McIntosh Perry Security and provided an opinion that it is valid and enforceable.

16. A recent search of the Alberta Personal Property Registry also indicates a subsequent security registration to that registered by McIntosh Perry in favour of Canadian Imperial Bank of Commerce (“CIBC”). The Proposal Trustee understands that CIBC’s registration relates to a credit facility that McIntosh Perry and its subsidiaries, including OEL, have in place with CIBC.
17. The Proposal Trustee understands that there is a subordination agreement in place between CIBC and McIntosh Perry pursuant to which OEL’s obligations to McIntosh Perry are subordinated to CIBC’s security interest. The Proposal Trustee has not incurred the expense of having its legal counsel review CIBC’s security or the subordination agreement and is proceeding on the assumption that the McIntosh Security is subordinate to CIBC as both CIBC and McIntosh are supportive of the Proposed Transaction with the payment of the sales proceeds to be directed to CIBC.
18. The Proposal Trustee understands that the Company is current with its payroll remittance obligations to Canada Revenue Agency (“CRA”) such that it is not anticipated that CRA would advance a deemed trust claim in this regard.
19. As set out earlier in this First Report, Management has advised the Proposal Trustee that the Former Employees of OEL have been paid all outstanding wages, salaries, commissions and/or compensations and that MEPL will assume the vacation pay obligations in respect of the Current Employees. Consequently, there would be no claims that would otherwise be afforded a security interest in current assets pursuant to Section 81.4 of the BIA.

Current Financial Status

20. As discussed in further detail in the next section of this First Report, OEL has a significant working capital deficiency in excess of \$3 Million. Given its revenue generating activities are exclusively dependent on the Western Canadian oil and gas industry and in light of the depressed nature of that industry over the last number of years, OEL has been struggling financially and has been dependent on McIntosh Perry for assistance funding its operations.

21. The Proposal Trustee understands that McIntosh Perry, and Signal Hill as its parent, are not prepared to advance funding to OEL in light of OEL's current circumstances leading to the Demand Notice being issued by McIntosh Perry.
22. In light of OEL being insolvent, having no ability to satisfy its ongoing and future obligations and in consideration of the Demand Notice, OEL filed the NOI and will be making an application to Court seeking approval of the Proposed Transaction.

FINANCIAL POSITION

OEL Projects Ltd.

23. Management has provided the Proposal Trustee with the most recent unaudited non-consolidated interim Balance Sheet of OEL as at the date of the most recent fiscal year end being March 27, 2020, a copy of which is attached as **Appendix "A"** (the "**OEL Balance Sheet**") to this First Report.
24. The Proposal Trustee has reviewed the Balance Sheet and made inquiries of Management regarding the OEL Balance Sheet and can offer the following comments with respect to its preliminary review of significant line items contained in the Balance Sheet:

ASSETS

- (a) Cash - \$286,000 – the OEL Balance Sheet reflects a book balance of available cash as of March 27, 2020 in the amount of approximately \$286,000.
- (b) Accounts receivable - net - \$916,000 – Management has provided the Proposal Trustee with an aged accounts receivable listing as at March 27, 2020, reflecting gross accounts receivable of approximately \$1.5 Million due from 27 customers net of a provision for bad debts of \$570,000.
- (c) Misc. Accounts Receivable – (\$11,000) – this negative balance representing a net payable is the sum of various small miscellaneous non-customer related balances.

- (d) WIP - \$196,000 – this figure represents engineering hours that have been worked on projects accrued at a standard rate but not yet invoiced.
- (e) Prepaid expenses - \$109,000 – represents the unamortized balances of certain expenses including insurance and annual software licenses.
- (f) Property, Plant & Equipment - net - \$1,463,000 – comprised of a balance of approximately \$1.1 Million in relation to unamortized leasehold improvements and a balance of approximately \$350,000 in respect of unamortized office equipment and computer hardware.
- (g) Intangible Assets - \$109,000 – relates to the unamortized balance of capitalized software expenses.
- (h) Deposits - \$91,000 – balance is primarily composed of security deposits in respect of leased premises.
- (i) Investments – Ammonite - \$2,318,000 – This figure represents the book value of OEL’s 100% ownership interest in Ammonite.
- (j) Goodwill - \$446,000 – relates to the acquisition of Ammonite in 2014.

LIABILITIES

- (k) Accounts Payable & Accrued Liabilities - \$732,000 – this figure is comprised of the following major classifications:
 - *Accounts payable* - approximately \$279,000 owed to approximately 40 suppliers of which the largest individual balance is \$42,000. Management has provided the Proposal Trustee with an aged accounts payable listing to support the reported balance.
 - *Payroll obligations* – approximately \$287,000 related principally to accrued wages and vacation pay due to employees through to March 27, 2020.

- *GST* – approximately \$57,000 in relation to the net GST obligation payable as at March 27, 2020.
 - *Accrued liabilities* – approximately \$58,000 relating to the Company’s health spending account and its external accountants.
 - *Profit sharing* - an accrual of approximately \$51,000 to certain employees.
- (l) MEIP Bonus Payable - Shareholders – \$45,000 – represents a bonus payable to certain employees.
- (m) Lease Inducement – Short Term \$99,000 – short-term unamortized portion of lease inducements.
- (n) Income Taxes Payable - (\$67,000) – this negative liability represents a receivable in respect of a potential income tax refund.
- (o) Lease Inducement – Long Term - \$721,000 – long-term unamortized portion of lease inducements.
- (p) MPCE Note - \$9,151,000 – represents OEL’s secured obligation to McIntosh Perry. As mentioned earlier in this First Report, the Proposal Trustee has obtained an independent security opinion confirming the validity and enforceability of the McIntosh Perry Security.
- (q) Due to Related Party – (\$1,330,000) – this negative balance represents the net amount receivable from various unsecured balances due from/to related parties as follows:
- *McIntosh Perry* – an intercompany advance of approximately \$1.2 Million due from McIntosh Perry.
 - *Cormetrics* – approximately \$558,000 due from Cormetrics pursuant to a shareholder advance.

- *ARA* – Approximately \$516,000 owed to this related entity.

ESTIMATED LIQUIDATION ANALYSIS

25. Since McIntosh Perry and Signal Hill are not prepared to advance money to fund OEL’s operations and with the Demand having being issued by McIntosh Perry, the Proposal Trustee anticipates that McIntosh Perry will appoint a Receiver over OEL in the event that the Proposed Transaction is not approved by the Court. Therefore, the Proposal Trustee has prepared the following estimated liquidation analysis of the Company for purposes of assessing the reasonableness of the consideration payable in the Proposed Transaction:

Schedule of Estimated Realizations			
(000's \$)			
	Balance Sheet	Estimated Realizations	
	as at Mar. 27, 2020	Low	High
Cash	\$ 286,000	\$ 286,000	\$ 286,000
Accounts receivable - net	916,000	549,600	732,800
Income tax refund	67,000		67,000
WIP	196,000	-	-
Prepaid expenses	109,000	-	-
Property, plant and equipment	1,463,000	17,500	35,000
Intangible assets	109,000	-	-
Deposits	91,000	-	-
Investment - Ammonite	2,318,000	-	-
Due from Coremetrics	558,000	-	-
Goodwill	446,000	-	-
Estimated gross realizations		853,100	1,120,800
Less: net secured obligation to McIntosh Perry		(7,933,000)	(7,933,000)
Estimated deficiency before professional fees and costs		<u>\$(7,079,900)</u>	<u>\$(6,812,200)</u>

26. The above analysis has been prepared based on the following assumptions:

(a) Cash – assumes all cash balances would be recoverable in a liquidation scenario.

- (b) Accounts receivable - net – in light of the provision of \$570,000 for bad debts already contemplated by the Company, in the event of a liquidation scenario we have assumed collections ranging from 60% - 80% of the net book value of accounts receivable.
- (c) Income tax refund – we have estimated a range of recoveries from nil to 100% of the anticipated refund.
- (d) WIP – it is assumed that in a liquidation scenario, the Receiver would not be in a position to complete the ongoing projects such that there would be no recoveries derived in relation to WIP.
- (e) Prepaid expenses – based on our experience with attempting to recover prepaid balances in a liquidation scenario, we have assumed zero realizations.
- (f) Property, Plant & Equipment - net – based on our recent experience, we have assumed recoveries ranging between 5% - 10% in relation to the net book value of office equipment and computer hardware and zero recoveries associated with the balance of approximately \$1.1 Million in relation to unamortized leasehold improvements.
- (g) Intangible Assets – we have assumed zero recoveries in relation to the unamortized balance of capitalized software expenses.
- (h) Deposits – based on our experience, we have assumed zero recoveries in relation to deposits as they generally prove to be subject to claims of setoff.
- (i) Investment – Ammonite – the March 27, 2020 unaudited balance sheets of each of Ammonite and its subsidiary Cormetrics, attached as **Appendices “B”** and **“C”** respectively to this First Report. In light of the minimal assets of each entity, we have ascribed no value to the shares of each of these entities.

- (j) Due from Cormetrics – in light of the financial position of Cormetrics as set out on **Appendix “C”**, we have assumed this amount to be unrecoverable.
 - (k) Goodwill – as outlined above, we have ascribed no value to the goodwill recorded in respect of the acquisition of Ammonite.
27. Based on the above assumptions, the Proposal Trustee estimates a gross liquidation value of the Company’s assets ranging from approximately \$853,000 to approximately \$1.1 million before considering any costs associated with realizing on the assets such as professional fees and auction fees (the “**Realization Costs**”).
28. In light of net obligation owing to McIntosh Perry being approximately \$8.0 Million (\$9.2 Million loan less \$1.2 intercompany advance), we estimate that there would be a significant shortfall in the range of \$7 Million experienced from realizations before accounting for the Realization Costs and any priority claims that may prove to be advanced by Canada Revenue Agency or employees. Consequently, there would be no funds expected to be available for unsecured creditors in the event of a liquidation scenario.

PROPOSED TRANSACTION

Terms

29. A copy of the ASPA is attached hereto as Exhibit “N” to the sworn Affidavit of James Johnson (the “**Johnson Affidavit**”) filed in these proceedings, the key terms of which are summarized as follows:
- Purchase price of \$2.6 Million (the “**Purchase Price**”);
 - The assets being acquired (the “**Purchased Assets**”) include:
 - Cash;
 - Accounts receivable;
 - Prepaid expenses and deposits;

- Office furniture and equipment;
 - Intellectual property rights;
 - Shares of Ammonite;
 - Certain contracts associated with revenue generating projects (the “**Assumed Contracts**”); and
 - Books and records.
- In the event any Assumed Contracts are not assignable and consent has not been obtained from the respective counterparty, OEL will:
 - from the closing time of the Proposed Transaction until the earlier of:
 - (i) the Assignment Outside Date (as defined in the Johnson Affidavit); or (ii) such time as the required approval or consent to its assignment, or an Assignment Order pursuant to section 84.1 of the BIA has been obtained, hold the respective Assumed Contract in trust for MEPL and will pay over to MEPL any proceeds collected therefrom; and
 - upon written request of MEPL, make application to the Court for an Assignment Order pursuant to Section 84.1 of the BIA;
 - The Purchased Assets are being acquire on an “*as is, where is*” basis;
 - MPEL will offer employment to the 34 Current Employees and will assume responsibility for all unpaid vacation pay with the individuals executing a release of liability in favour of OEL;
 - The ASPA is conditional upon Court approval; and
 - The Proposed Transaction is scheduled to close upon the granting of an Approval and Vesting Order.

30. McIntosh Perry has issued to OEL an irrevocable direction to pay directing and authorizing OEL to distribute \$2,383,000 from the sales proceeds directly to CIBC.

Proposal Trustee's Assessment

31. Section 65.13 of the BIA provides that an insolvent person filing an NOI may not sell or dispose of assets outside the ordinary course of business unless authorized to do so by the Court.

32. Section 65.13 also provides for various procedural requirements to be followed and certain criteria to be taken into account by the Court when considering whether to approve any proposed transaction, for which the Proposal Trustee provides its comments below.

33. As mentioned earlier in this First Report, the PPR Search references secured registrations by McIntosh Perry and CIBC. Both parties have been put on notice of the application seeking to approve the Proposed Transaction in accordance with Section 65.13(3) of the BIA.

34. Section 65.13(4) provides for the Court to consider, among other things, certain factors for which the Proposal Trustee has the following comments:

- (a) The Proposal Trustee is of the view that the process leading up to the Proposed Transaction was reasonable in the circumstances for the following reasons:

i. The Purchase Price is reasonable in comparison to the Proposal Trustee's assessment of the liquidation value of the Purchased Assets;

ii. Given the significant estimated shortfall from realizations as it relates to secured interests in the Purchased Assets and the nature of the Purchased Assets themselves, the Proposal Trustee is of the view that it is unlikely that incurring the costs associated with administering a public marketing process in respect of the Purchased Assets would

yield sufficient funds to otherwise render funds available for unsecured creditors;

iii. Notwithstanding the above, the Company no longer has the ability to fund its operations or the time available to administer a protracted public sales process in light of the Demand having been issued by McIntosh Perry; and

iv. CIBC and McIntosh Perry, the parties holding secured interest in the Purchased Assets, are supportive of the Proposed Transaction.

- (b) The Proposal Trustee was aware of the process leading up to the Proposed Transaction and approved of it in the circumstances.
- (c) The Proposal Trustee is of the view that the Proposed Transaction will result in net proceeds greater than would be anticipated were the Purchased Assets liquidated in a bankruptcy proceeding as the Purchase Price is greater than the Proposal Trustee's estimated gross realizations as outlined earlier in this First Report even before considering the costs of realization.
- (d) As set out above, CIBC and McIntosh Perry, are aware of and supportive of the Proposed Transaction. In light of the significant estimated shortfall as it relates to secured interests in the Purchased Assets, the Proposal Trustee is of the view that unsecured creditors do not realistically have any financial standing such that they should be consulted.
- (e) The Proposed Transaction will result in a shortfall to all of the Company's creditors which the Proposal Trustee is of the view would otherwise be the same result in a receivership or bankruptcy proceeding. It is also worth noting that the Proposed Transaction contemplates a significant number of individuals being able to maintain employment.

- (f) The Proposal Trustee is of the opinion that the Purchase Price is reasonable based on the Proposal Trustee's liquidation analysis set out earlier in this First Report.
35. Section 65.13(5)(a) of the BIA provides that if a proposed sale or disposition is to a related party that the Court must be satisfied that good faith efforts were made to sell or otherwise dispose of assets to non-related parties. As set out in the Johnson Affidavit, the board of directors of OEL gave consideration to engaging a third party to attempt to consummate a transaction to an unrelated third party. However, it was determined that it would not be feasible to initiate such a process in light of the current market conditions, the cost of administering such a process, the ongoing cash drain that would occur during a process and the risk of employees leaving during such a process thereby jeopardizing any effective going concern value. In light of the foregoing, the Proposal Trustee is of the view that the Company demonstrated good faith efforts in this regard.
36. Section 65.13(5)(b) of the BIA provides that in relation to a sale to a related party, the Court must also be satisfied to that which would be received under any offer that would be made by a third party. In light of the Proposal Trustee's liquidation analysis and the resultant estimated shortfall to the secured creditors, the Proposal Trustee is of the view that this condition is also satisfied.
37. As mentioned earlier in this First Report, the Proposal Trustee's understanding is that all wages and vacation pay due to Former Employees and Current Employees have either been paid or are being assumed by MEPL such that there should be no payments to consider pursuant to consider as prescribed by S.65.13(8) of the BIA.

RECOMMENDATIONS

38. The Proposal Trustee recommends to this Honourable Court that the ASPA be approved and that an Approval and Vesting Order granted for the following reasons:
- (a) The Proposal Trustee is of the view that the Proposed Transaction will result in net proceeds greater than would otherwise be anticipated were the Purchased Assets liquidated in a receivership or bankruptcy proceeding;
 - (b) The Proposed Transaction affords the opportunity for a significant number of individuals to maintain employment; and
 - (c) Based on the Proposal Trustee's liquidation analysis as set out in this First Report, CIBC and McIntosh Perry, as secured creditors, would experience shortfalls from realizations in a liquidation scenario and both parties are supportive of the Proposed Transaction. Consequently, there is no prejudice to unsecured creditors of OEL.
39. The Proposal Trustee further recommends that the Court authorize the proposed distribution to CIBC in light of the Proposal Trustee having obtained an independent security opinion confirming the validity and enforceability of the security granted by OEL to McIntosh Perry.

All of which is respectfully submitted this 22nd day of May 2020.

BDO Canada Limited,
in its capacity as Proposal Trustee of OEL Projects Ltd.
and not in its personal capacity

Per:



Marc Kelly
Senior Vice President

APPENDIX “A”

OEL Projects Ltd.

BALANCE SHEET

(Unaudited)

000's C\$

March 27, 2020

Current assets

Cash	286
Accounts receivable - Net	916
Misc. Accounts receivable	(11)
WIP	196
Prepaid expenses	109

1,495

Property, plant & equipment - Net	1,463
Intangible Assets	109
Deposits	91
Investment - Ammonite	2,318
Goodwill	446

TOTAL ASSETS 5,922

Current liabilities

AP & accrued liabilities	732
MEIP Bonus payable-Shareholders	45
Lease Inducement-short term	99
Interest Payable (MPCE)	

877

Income taxes payable (67)

810

Lease Inducement-long term	721
MPCE Note	9,151
Due to Related Party	(1,330)

8,542

SHAREHOLDERS' EQUITY

Retained earnings / (Deficit)	(3,430)
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(3,430)

TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY 5,922

APPENDIX “B”

Ammonite Corrosion Ltd

BALANCE SHEET (Unaudited)

000's C\$

March 27, 2020

Current assets

Cash	42
Accounts receivable - Net	181
Misc. Accounts receivable	(1)
WIP	56
Prepaid expenses	15

292

Investment - Ammonite/cormetrics	(1,750)
Goodwill	489
TOTAL ASSETS	(969)

Current liabilities

AP & accrued liabilities	76
	<u>76</u>

Due to Related Party	(91)
	<u>(91)</u>

SHAREHOLDERS' EQUITY

Retained earnings / (Deficit)	(953)
	<u>(953)</u>

TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	(969)
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APPENDIX “C”

Cormetrics

BALANCE SHEET (Unaudited)

000's C\$

March 27, 2020

Current assets

Cash	22
Accounts receivable - Net	180

202

Property, plant & equipment - Net	44
Intangible Assets	2

TOTAL ASSETS 248

Current liabilities

AP & accrued liabilities	49
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49

Income taxes payable	(22)
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28

Due to Related Party	(467)
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(467)

SHAREHOLDERS' EQUITY

Retained earnings / (Deficit)	687
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687

TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY 248