

COURT FILE NUMBER 1601-11708

COURT COURT OF QUEEN'S BENCH OF ALBERTA

JUDICIAL CENTRE CALGARY

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

AND IN THE MATTER OF A PLAN OF ARRANGEMENT OF
QUATTRO EXPLORATION AND PRODUCTION LTD.

DOCUMENT **FIRST REPORT OF MONITOR
HARDIE & KELLY INC. IN ITS CAPACITY AS MONITOR OF
QUATTRO EXPLORATION AND PRODUCTION LTD.
SEPTEMBER 30, 2016**

ADDRESS FOR SERVICE AND CONTACT
INFORMATION OF PARTY FILING THIS DOCUMENT

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**FIRST REPORT OF THE MONITOR
HARDIE & KELLY INC.
SEPTEMBER 30, 2016**

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INTRODUCTION

1. On August 10, 2016, (the “NOI Filing Date”), Quattro Exploration and Production Ltd. (“Quattro” or the “Company”) commenced restructuring proceedings (the “BIA Proceedings”) by filing a Notice of Intention to Make a Proposal (the “NOI”) pursuant to the *Bankruptcy & Insolvency Act*, R.S.C. 1985, c. B-3, as amended (the “BIA”). Hardie & Kelly Inc. (“HKI”) consented to act as proposal trustee.
2. Pursuant to the BIA, the filing of the NOI provided the Company with an automatic 30-day stay of proceedings through to September 9, 2016.
3. On September 6, 2016, HKI filed a report (the “Pre-Filing Report”) with the Court of Queen’s Bench of Alberta (the “Court”) in contemplation of the Company’s September 8, 2016 application pursuant to Section 11.6(a) of the *Companies’ Creditors Arrangement Act*, R.S.C. 1985 c. C-36, as amended (the “CCAA”) seeking to, *inter alia*, continuing its restructuring proceedings from the BIA to the CCAA.
4. On September 8, 2016, the Court granted the Company’s application and issued an Order (the “Initial Order”) providing certain relief to the Company, including continuing its BIA Proceedings under the CCAA, extending the stay of proceedings originally established under the BIA Proceedings through to October 8, 2016, and appointing HKI as monitor (the “Monitor”).
5. On September 27, 2016, Quattro made an application to the Court (the “Extension Application”) for an extension of the stay of proceedings through to November 30, 2016.

PURPOSE

6. The purpose of this report (the “First Report”) is to provide information to this Honourable Court with respect to:
 - a. The notice issued by the Monitor to Quattro’s creditors informing them of the Company’s CCAA proceedings;
 - b. An operational update;
 - c. The Company’s financial performance since the date of the Initial Order;
 - d. The Company’s revised cash flow forecast for the period September 26 to December 12, 2016;
 - e. The interim financing secured by the Company;
 - f. The Company’s restructuring activities; and
 - g. The Company’s request for an extension of the Stay through to November 30, 2016 and the Monitor’s recommendation thereto.

TERMS OF REFERENCE

7. In preparing this First Report, the Monitor has been provided with, and has relied upon unaudited financial information, books and records of the Company, and discussions with the Company’s management (“Management”). Except as described in this First Report, the Monitor has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of such financial information in a manner that would wholly or partially comply with Generally Accepted Assurance Standards (“GAAS”) pursuant to the Chartered Professional Accountants Canada Handbook and, accordingly, the Monitor expresses no opinion or other form of assurance contemplated under GAAS in respect of such information.
8. Some of the information referred to in this First Report consists of forecasts and projections. An examination or review of any financial forecast and projections, as outlined in the Chartered Professional Accountants Canada Handbook, has not been performed.

9. Unless otherwise stated, all monetary amounts noted herein are expressed in Canadian dollars.

NOTICE TO CREDITORS

10. The Monitor issued notice of the CCAA proceedings (the “Creditor Notice”) to all known creditors as represented by the Company. Creditors were directed to the Monitor’s website (the “Website”) to obtain a copy of the Initial Order and a listing of the known creditors as represented by Management. The Creditor Notice encourages creditors to refer back to the Website regularly for updates as to the status of the proceedings. A copy of the Creditor Notice is attached as Appendix “A”.
11. Pursuant to the terms of the Initial Order and the CCAA, the Monitor published a notice of the CCAA proceedings (the “Newspaper Notice”) in the *National Post* on September 13, 2016 and September 20, 2016. A copy of the form of the Newspaper Notice is attached as Appendix “B”.
12. Pursuant to the terms of the CCAA, the Monitor filed with the Office of the Superintendent of Bankruptcy (the “OSB”) *Forms 1 and 2* containing certain prescribed information regarding the proceedings.

OPERATIONAL UPDATE

13. Following the granting of the Initial Order, there have been no material adverse changes in the Company’s operations. The Company has reported total average daily production of approximately 1,400 BOE from the operations for the month of August 2016, including both operated and non-operated properties. According to Management, this is consistent with past production levels as adjusted for seasonal maintenance interruptions.
14. To date, Management, with the assistance of the Monitor, has been able to communicate with suppliers and make mutually satisfactory arrangements to ensure the uninterrupted supply of goods and services to the Company.

FINANCIAL PERFORMANCE

15. Included as Exhibit “S” to the Affidavit of Mr. Leonard Van Betuw sworn on September 2, 2016 (the “Initial Van Betuw Affidavit”) filed prior to the commencement of the CCAA proceedings, was a cash flow forecast (the “Initial Forecast”) for the period August 29 to November 27, 2016 (the “Initial Forecast Period”).
16. A variance analysis of the Company’s actual receipts and disbursements over the period August 29 to September 25, 2016 versus the corresponding period in the Initial Forecast is set out in the following table.

	August 29 - September 25, 2016			Notes
	Actual	Forecast	Variance	
Receipts				
Production revenues	2,427	683,473	(681,046)	a)
Miscellaneous	3,129	47,600	(44,471)	b)
	5,556	731,073	(725,517)	
Disbursements				
Royalties	-	(25,200)	25,200	
Production and operating	(316,696)	(558,888)	242,192	c)
Transportation	-	(73,032)	73,032	
General and administration	(177,559)	(230,000)	52,441	d)
Restructuring	(124,154)	-	(124,154)	e)
	(618,409)	(887,120)	268,711	
Investing				
Interim financing	300,000	130,000	170,000	f)
Capital expenditures	(27,500)	(150,000)	122,500	g)
Sale of assets	-	-	-	
	272,500	(20,000)	292,500	
Financing				
Interest payments	(54,794)	(64,798)	10,004	
	(54,794)	(64,798)	10,004	
Increase in cash	(395,148)	(240,845)	(154,302)	
Cash - beginning	569,016	637,487	(68,471)	h)
Cash - closing	173,868	396,642	(222,773)	

17. The Company experienced negative cash flow of approximately \$395,000 over the period August 29 to September 25, 2016, which was a variance of approximately \$150,000 compared to the Company's projections. The Monitor offers the following comments:

- a. Oil and gas revenues related to August production are received in September and were forecast by the Company to be received during the week ending September 25, 2016, as revenues are generally paid on the 25th of each month. However, revenues were received the following day on September 26th as a result of September 25th falling on a weekend, causing a negative cash variance within the period.

The Monitor notes that, according to Management, revenues were forecast conservatively; however, revenue deposits received on September 26th totalled \$562,795, which is nearly \$120,000 lower than forecast. The Company has indicated that the variance relates to:

- i. The pricing obtained for August production was significantly lower than the previous month's pricing, which was used as the basis for forecasts; and
 - ii. Certain transportation charges were netted from sales revenues by the purchasers, therefore actual sales are somewhat higher than the deposit amounts would suggest.
- b. The variance in Miscellaneous Receipts is a timing difference relating to funds being held in Court pursuant to garnishees that have yet to be released to the Company.
 - c. Actual operating costs include royalties and transportation expenses. Together, payments for royalties, operating expenses and transportation have totalled approximately \$340,000 (or 52%) lower than forecast. According to Management, this variance resulted from the fact that operating expenses were estimated to be paid as incurred given the uncertain impact of these proceedings and the potential that suppliers

would alter the Company's ongoing payment terms. Such accelerated payment terms did not materialize to the extent forecast, resulting in timing delays, with these timing differences to be reversed in subsequent periods.

- d. Actual general and administrative expenses were approximately \$50,000 (or 23%) lower than forecast. According to Management, this variance is a result of:
 - i. Timing delays stemming from the fact that not all general and administrative expenses were paid as incurred as forecast, with these timing differences to be reversed in subsequent periods; and
 - ii. Reduction of its staff by three individuals.
- e. The Company has paid approximately \$125,000 in respect of restructuring expenses which were not forecast in the period. Approximately \$100,000 of this relates to a retainer paid to Durham Capital, a financial advisor retained by the Company.
- f. The Company borrowed an additional \$150,000 in interim financing above the amount forecast. These funds were largely used to fund the retainer to Durham Capital, which had not been contemplated in the Company's projections.

In addition, the interim lender did not deduct fees from the initial funding tranche as anticipated, which is expected to reverse in subsequent periods.

- g. Actual capital expenditures related to a planned work-over were \$122,500 (or 82%) lower than forecast. Management advises that the project was delayed such that it is not yet complete. In addition, Management has indicated that the project is under-budget and therefore only a further \$87,500 is expected to be paid in future weeks.
- h. The opening cash balance reported in the Initial Forecast did not match the Company's actual bank balance. Therefore, a portion of the variance in the actual closing cash balance as compared to the forecast relates to this

disparity.

18. The Monitor has identified certain invoices paid by the Company that relate to the period prior to the NOI date. Many of these payments related to outstanding employee and contractor wages and expenses which appear to be consistent with existing compensation policies and were therefore specifically permitted pursuant to paragraph 8 of the CCAA order.

However, the Monitor identified four payments totalling approximately \$42,000 that did not appear to meet this criteria:

- a. Three cheques which had been sent to suppliers prior to the NOI date cleared the Company's account after the NOI date. According to Management, two of the cheques related to crown leases which would be required to be paid; and
 - b. A payment on account of pre-NOI consumption was made to a utility provider which the Company believed would shut off service in the absence of a payment.
19. The Monitor has also identified five payments totalling \$50,000 which were made either directly to Quattro's President and CEO Leonard Van Betuw or to credit card companies on behalf of Mr. Van Betuw. Management advises that the payments relate to legitimate Company expenses incurred by Mr. Van Betuw after the NOI Filing Date and were paid in a manner consistent with existing compensation policies related to employee or contractor expenses and were therefore specifically permitted pursuant to paragraph 8 of the CCAA order.

The Monitor has requested supporting information from the Company in order to verify the validity of the transactions. Management indicated shortly before the filing of this report that it has collected detailed information which is available for the Monitor's review. The Monitor intends to review this information as soon as possible and will provide a further update to this Court regarding these transactions.

CASH FLOW FORECAST

20. Management prepared an updated cash flow forecast for the period September 26 to December 25, 2016 (the “September 27th Forecast”) which was attached as Exhibit “A” to the Affidavit of Leonard B. Van Betuw sworn on September 27, 2016 in connection with Quattro’s Extension Application.

However, after review of the September 27th Forecast with the Monitor, the Company issued a revised forecast for the reduced period of September 26 to December 12, 2016 (the “September 29th Forecast”), which was attached as Exhibit “A” to the Supplemental Affidavit of Leonard B. Van Betuw sworn on September 29, 2016.

The September 29th Forecast can be summarized as follows:

	September 26 - December 12, 2016
Receipts	
Production revenues	2,070,183
Miscellaneous	47,600
	2,117,783
Disbursements	
Royalties	(56,800)
Production and operating	(1,485,769)
Transportation	(244,969)
General and administration	(690,000)
Restructuring	(275,000)
	(2,752,538)
Investing	
Interim financing - Tranche 1	830,000
Interim financing - Tranche 2	
Capital expenditures	(87,500)
Sale of assets	-
	742,500
Financing	
Interest payments	(129,595)
	(129,595)
Increase (Decrease) in cash	(21,850)
Cash - beginning of period	173,868
Cash - end of period	152,018

21. The Monitor provides the following comments on the September 29th Forecast:
- a. Revenues to be received the week of October 24, 2016 have been reduced as compared to the Initial Forecast, which Management advises is due to a reduction in pricing as well as a reduction in volumes related to oil production that was not converted into sales within the month. Despite the reduction in pricing forecasts, Management has indicated that revenues received in the week of November 21, 2016 have been held constant with the Initial Forecast as the additional volumes produced but not sold in the previous month will be sold during this period;
 - b. Forecast operating expenses and G&A expenses appear to be consistent with the Company's Initial Forecast. As a result of the significant variances that have occurred to date which were largely attributed to timing differences, the expenses included in the September 29th Forecast necessarily include payment of accounts payable and accrued liabilities relating to those variances.

Management has indicated that the September 29th Forecast anticipates that payment terms will be consistent over the remaining forecast period; however, the Monitor notes that any significant acceleration of payment terms could result in actual expense payments being higher than forecast during the period;

- c. The September 29th Forecast does not include any proceeds from asset sales as a result of the deadlines for any transactions pursuant to the sale and investor solicitation process (the "SISP") falling outside the forecast period;
- d. According to the September 29th Forecast, the Company will be able to fund its operations and restructuring efforts while maintaining a positive cash balance with the assistance of additional draws, up to the full amount of the remaining available interim financing provided for operations, on the Interim Facility (as later defined).

INTERIM FINANCING

22. The Initial Order authorized Quattro to enter into an interim financing agreement (the “Interim Facility”) with its principal lender, Business Development Bank of Canada (“BDC”).
23. The Interim Facility of \$1,250,000 is comprised of:
 - i. Tranche 1 - \$1,000,000 – towards operations, and
 - ii. Tranche 2 - \$250,000 – towards a sale and investor solicitation process.
24. To date, the Company has borrowed \$150,000 under Tranche 1 and \$150,000 under Tranche 2. As mentioned previously, according to the September 29th Forecast, the Company expects to draw on the remainder of the Tranche 1 facility by the end of the forecast period.
25. One of the underlying conditions of the Interim Facility was the provision of a business plan to BDC by September 23, 2016. The Monitor understands that the Company and BDC have informally agreed to extend the deadline to September 30, 2016, although BDC has not provided a formal waiver of the default. As of the time of the issuance of this report, the Monitor understands the business plan has not yet been delivered but Management advises that it is continuing to work with its advisors and anticipates it will meet this deadline.

RESTRUCTURING ACTIVITIES

Sale and Investor Solicitation Process

26. The Initial Order directed the establishment of a SISP, which Management anticipates will form the basis for the Company’s restructuring plan. The basis of the SISP is to seek a transaction (or multiple transactions) culminating in a sale of certain assets and/or financial restructuring alternatives.
27. Pursuant to the terms of the SISP, the Company has engaged two financial advisors with distinct roles as follows:

- NRG Divestitures Inc. – in respect of the solicitation of offers for the sale of some or all of the Company’s assets; and
 - Durham Capital – in respect of the solicitation of investment and or financing restructuring alternatives.
28. The significant timelines established within the SISP which is being conducted in two phases are as follows:
- a. Non-binding indications of interest being due by October 31, 2016 (the “Phase I Bid Deadline”);
 - b. The deadline for Qualified Phase II Participants to then deliver a Qualified Bid shall be November 28, 2016 (the “Phase II Bid Deadline”);
 - c. The deadline for finalizing a definitive agreement(s) with a successful bidder(s), subject only to Court approval, shall be December 19, 2016; and
 - d. The target date for Court approval of any transaction(s) shall be no later than January 20, 2017.

Claims Process

29. As of the date of the Pre-Filing Report, it was anticipated that the Company would be seeking the establishment of a formal claims process; however, prior to the Company’s initial CCAA application, the Company, in consultation with the Monitor, ultimately determined that it was not cost-effective to begin a claims process at this stage of the proceedings. As a result, this relief was not sought at the initial CCAA application and the Initial Order does not provide for the establishment of a formal claims process.
30. The Monitor understands the Company intends to seek an order establishing a claims process after it has reviewed initial results of the SISP, but prior to completion of any transaction resulting from the SISP.

RECOMMENDATION

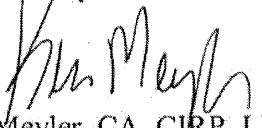
31. The Monitor is satisfied that Management has been acting with due diligence and in good faith in working towards a successful restructuring. The stay extension is required in order for the Company to fully implement the SISP, the process on which Management anticipates the Company's restructuring plan will be based.
32. BDC has advised the Monitor that it is supportive of the Company's application in the circumstances.
33. Consequently, the Monitor is supportive of the Company's application for an extension of the Stay through to November 30, 2016.


All of which is respectfully submitted this 30th day of September, 2016

Hardie & Kelly Inc.

In its capacity as the Monitor of Quattro Exploration and Production Ltd.
and not in its personal or corporate capacity

Per:


Kevin Meyler, CA, CIRP, LIT
Senior Vice President


Charla Smith, CGA, CIRP, LIT
Vice President

APPENDIX “A”

September 13, 2016

To the Creditors of Quattro Exploration and Production Ltd.

Re: Proceedings under the *Companies' Creditors Arrangement Act*

On September 8, 2016, Quattro Exploration and Production Ltd. ("Quattro" or the "Company") made an application to the Court of Queen's Bench of Alberta (the "Court") seeking to transfer its restructuring proceedings initially commenced on August 10, 2016 under the *Bankruptcy and Insolvency Act* (the "BIA Proceedings") to the *Companies' Creditors Arrangement Act* ("CCAA").

On September 8, 2016, the Court granted the Company's application and issued an Order (the "Initial Order") providing certain relief to the Company including an extension of the stay of proceedings originally established under the BIA Proceedings through to October 8, 2016. Claims against the Company for payment of goods and services supplied to Quattro prior to August 10, 2016 continue to be suspended and creditors are prohibited from continuing or taking any actions or exercising any rights or remedies against the Company except with leave of the Court.

A copy of the Initial Order and a list of the names and addresses and amounts due to creditors as provided by Quattro can be found on the Monitor's website (the "Website") at www.insolvency.net/quattro-exploration-production-ltd/ or by contacting the Monitor directly. **You are not required to file a proof of claim at this time.**

Creditors are encouraged to check the Website regularly for updates as to the status of the proceedings as additional materials will be posted to the Website from time to time.

Should you have any questions or concerns please contact Charla Smith, of the Monitor, at 403-536-8506 or at csmith@insolvency.net, or Mr. Michael Bejerman, of Quattro, at michael.b@qxp-petro.com.

Yours truly,

Hardie & Kelly Inc., in its capacity
as Court appointed Monitor of Quattro Exploration and Production Ltd.
and not in its personal capacity


Per: Marc Kelly, CA, CIRP
Senior Vice President

APPENDIX “B”

Court File Number 1601-11708

**IN THE COURT OF QUEEN'S BENCH
OF ALBERTA JUDICIAL CENTRE
OF CALGARY**

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

**AND IN THE MATTER OF
QUATTRO EXPLORATION AND
PRODUCTION LTD.**

On September 8, 2016, upon the application of Quattro Exploration and Production Ltd. (the "Company"), the Court of Queen's Bench of Alberta (the "Court") granted an Order (the "Initial Order") under the *Companies' Creditors Arrangement Act* providing for an initial stay of proceedings through to October 8, 2016. Hardie & Kelly Inc. was appointed as monitor (the "Monitor"). The Initial Order and a list of creditors as estimated by the Company can be accessed by referring to the Monitor's website at www.insolvency.net/quattro-exploration-production-ltd/ (the "Website"). Interested parties are encouraged to check the Website frequently for updates as to the status of the proceedings. For further information contact Charla Smith, of Hardie & Kelly Inc., at 403-536-8506 or by e-mail at csmith@insolvency.net

Hardie Kelly
SUCCESSIONS • INSOLVENCY • TRUSTS

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