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COURT COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE CALGARY
PROCEEDING IN THE MATTER OF THE NOTICE OF INTENTION TO MAKE A PROPOSAL OF OAN RESOURCES LTD.
DOCUMENT **FIRST REPORT OF THE PROPOSAL TRUSTEE, HARDIE & KELLY INC. JULY 2, 2019**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT

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**FIRST REPORT OF THE PROPOSAL TRUSTEE
HARDIE & KELLY INC.
JULY 2, 2019**

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INTRODUCTION

1. On June 14, 2019 (the “Filing Date”), OAN Resources Ltd. (“OAN” or the “Company”) filed a Notice of Intention to Make a Proposal (the “NOI”) pursuant to the *Bankruptcy & Insolvency Act* (the “BIA”). Hardie & Kelly Inc. consented to act as trustee (the “Proposal Trustee”) of the proceedings.
2. The purpose of this first report (the “First Report”) is to provide the Court of Queen’s Bench of Alberta (the “Court”) with information in respect of the following:
 - a. The background of the Company;
 - b. The Company’s operations since the Filing Date;
 - c. The notices issued by the Proposal Trustee to the Company’s creditors;
 - d. The Company’s initial cash flow forecast;
 - e. The Company’s request to have Crimson Oil & Gas Ltd. (“Crimson”), Highwood Oil Company Ltd. (“Highwood”) and Hudgeon’s Welding declared to be critical suppliers to OAN (the “Critical Suppliers”) and have all payments made to the Critical Suppliers subsequent to the date of the NOI ratified and approved provided all such payments are first approved by the Proposal Trustee, and the Proposal Trustee’s recommendation with respect thereto;
 - f. The Company’s restructuring activities; and
 - g. The Company’s request for an extension of the time required to file a proposal and a corresponding extension of the stay of proceedings (the “Stay”) through to August 28, 2019 and the Proposal Trustee’s recommendation with respect thereto.

TERMS OF REFERENCE

3. In preparing this First Report, the Proposal Trustee has relied upon unaudited financial information, records of the Company and discussions with the Company's management ("Management"). The Proposal Trustee has not performed an audit, review or other verification of such information. An examination of the cash flow information as outlined in the Canadian Institute of Chartered Accountants Handbook has not been performed. Future-oriented financial information relied upon in this report is based on Management's assumptions regarding future events and actual results achieved may vary from this information and the variations may be significant. Accordingly, the Proposal Trustee expresses no opinion or other form of assurance in respect of such information.

COMPANY BACKGROUND

4. OAN is a private company with 36 shareholders headquartered in Calgary, Alberta that was incorporated pursuant to the laws of the Province of Alberta in November 2017.
5. The business of OAN is managed by three full-time and two part-time consultants, who provide consulting services on a month to month basis.
6. OAN carries on business as a producer of oil and gas. Specifically, OAN's primary assets are petroleum and natural gas leases, located in the Panny River area in Northern Alberta (the "PNG Assets"). OAN has ownership interests in six oil wells and is the operator of record with the Alberta Energy Regulator in respect of these wells. OAN's recent average monthly oil production is in the region of 65 bbls/day.

7. The Company's PNG Assets are operated by Crimson acting in its capacity as a contract operator. OAN also relies on Highwood for use of the facilities necessary to bring OAN's production to market, including pipelines and batteries. As discussed in greater detail further in this First Report, the services provided by both Crimson and Highwood are deemed by Management as essential to maintaining the continuity of OAN's operations.

ONGOING OPERATIONS

8. The Company has continued its operations in the ordinary course since the Filing Date. To date, Management, with the assistance of the Proposal Trustee, has been able to communicate with key customers and suppliers to make mutually satisfactory payment arrangements to ensure the uninterrupted supply of goods and services.

CREDITORS

9. The Company classifies the composition of its creditors as of the Filing Date as follows:
 - Secured - 22 debenture holders totalling \$3.3 Million plus accrued interest;
 - Unsecured - 79 creditors with amounts owed totalling approximately \$2.9 Million.
10. Pursuant to S. 50.4(1) of the Act, the Proposal Trustee mailed copies of the NOI, the Trustee's executed consent and the listing of creditors (the "Initial Filing Documents") to all known creditors as represented by the Company. Copies of the Initial Filing Documents have also been posted on the Trustee's website at <https://relieffromdebt.ca/oan-resources-ltd/>.

CASH FLOW FORECAST

11. Management, with the assistance of the Proposal Trustee, has prepared an initial cash flow forecast (the "Initial Forecast") for the period June 24 to September 22, 2019 (the "Initial Forecast Period").

12. On June 24, 2019, the Proposal Trustee filed the following documents with the Office of the Superintendent of Bankruptcy (the “OSB”):

- the Initial Forecast as prescribed by s. 50.4(2)(a) of the BIA, a copy of which is attached as Appendix “A”;
- the *Trustee’s Report on Cash Flow Statement* as prescribed by s. 50.4(2)(b) of the BIA, a copy of which is attached as Appendix “B”; and
- the *Report on Cash Flow Statement by the Person Making the Proposal* as prescribed by s. 50.4(2)(c) of the BIA, a copy of which is attached as Appendix “C”.

13. A summary of the Initial Forecast is as follows:

Receipts	-
Production revenues	416,000
	<u>416,000</u>
Disbursements	
Royalties (Fairfax GORR and Gunnarr NPI)	(2,586)
OPEX	-
Payments to Critical Suppliers for pre-filing debt	(244,422)
Current Expenses	-
Effluent Transportation and Handling	(13,973)
Field Operators	(18,250)
Repairs and Maintenance	(14,850)
Micromotion Sales Meter	(1,495)
Surface and Mineral Lease Rentals	(11,682)
Drilling and Property Taxes	(14,564)
Software	(462)
Fuel and Lubricants	(1,063)
Transportation	(4,250)
G&A	-
Management Consulting	(58,170)
Rent and parking	(20,193)
Software, phone, internet	(8,141)
Other consultant expenses	(2,315)
Restructuring	(100,000)
	<u>(516,416)</u>
Net cash inflow (outflow)	(100,416)
Cash - beginning	116,004
Cash - closing	<u>15,588</u>

14. The Initial Forecast reflects negative cash flow of approximately \$100,000 over the Initial Forecast Period, projecting an estimated cash balance of only approximately \$16,000 at September 22, 2019. The Proposal Trustee offers the following additional comments in respect of the Initial Forecast:
- The Initial Forecast contemplates pre-filing payments of approximately \$244,000 to the Critical Suppliers. Further detail in respect of the Critical Suppliers and the Proposal Trustee's recommendation in respect of the Company's pending application to seek the Court's approval to deeming the classification of the Critical Suppliers as appropriate and to have all payments made to the Critical Suppliers subsequent to the date of the NOI ratified by the Court is discussed further on in this First Report; and
 - The forecasted restructuring costs of approximately \$100,000 relate to an estimate of the fees and expenses of the Company's legal counsel, the Proposal Trustee and the Proposal Trustee's legal counsel over the Initial Forecast Period.
15. The Proposal Trustee is satisfied that the Initial Forecast is reasonable in the circumstances; however, we wish to highlight that a significant amount of unanticipated or unforeseen expenses are likely to tax the Company's ability to fund its ongoing post-filing expenses from its cash flow.

CRITICAL SUPPLIERS

16. As discussed above, Management has advised that it is of the opinion that the following three vendors who are each owed amounts as of the Filing Date are critical to maintaining the day to day operations, ongoing cash flow and the safety of field operations.
- OAN is party to an "Effluent Handling Agreement" and a "Contract Operating Agreement" with Crimson. Pursuant to these agreements, among other things, Crimson acts as the on-site operator of OAN's wells and then processes OAN's production for subsequent transportation and further processing. OAN does not have the personnel, equipment or

facilities to operate its own wells or conduct its own processing. Further, the location of OAN's wells and pipelines means that there are no alternative operators/processers for OAN to use other than Crimson. The books and records of the Company indicate that Crimson is owed approximately \$59,000 as of the Filing Date;

- Pursuant to certain assignments and name changes, OAN is a party to a "Processing Agreement" with Highwood. Under this agreement, OAN's production (once processed at the Crimson facilities) is transported through a pipeline owned by Highwood to facilities owned by Highwood (including a battery) for further processing and/or storage by Highwood. OAN does not have the personnel, equipment or facilities to carry out this work itself, and the location of OAN's wells and pipelines makes any other service provider to be impractical. The books and records of the Company indicate that Highwood is owed approximately \$173,000 as of the Filing Date; and
- An individual, Mr. David Hudgeon, operating as Hudgeon's Welding, is a consultant to OAN who acts as OAN's field operations manager. Specifically, Mr. Hudgeon is responsible for overseeing all technical and safety aspects of OAN's field operations and also for coordinating amongst OAN's other contract service providers. Mr. Hudgeon has provided such services to OAN since its inception and because of Mr. Hudgeon's intimate knowledge of OAN's operations, Management is of the opinion that the time, cost and delay associated with replacing Mr. Hudgeon would seriously undermine OAN's ability to restructure and maintain continuity of operations. The books and records of the Company indicate that Mr. Hudgeon is owed approximately \$13,000 as of the Filing Date.

17. The Company will be seeking the Court's authorization to designate these vendors as critical suppliers and to make payments of the arrears. The Proposal Trustee is supportive of same in the circumstances.

RESTRUCTURING EFFORTS

18. The Proposal Trustee is satisfied that Management has been acting with due diligence and in good faith since the Filing Date by:
- Responding to the Proposal Trustee's information requests on a timely basis;
 - Preparing the Initial Cash Flow; and
 - Holding preliminary discussions with legal counsel and the Proposal Trustee in regard to potential alternatives with respect to the structure of a proposal.

RECOMMENDATIONS

19. The Proposal Trustee is of the view that the Company's application for a further extension of the Stay to August 28, 2019 is warranted to allow the Company the opportunity to continue to work towards developing the framework of a viable Proposal as the Proposal Trustee is satisfied that:
- Management has been acting in good faith and with due diligence with a view towards ultimately preparing a proposal for presentation to its creditors; and
 - No creditor would be materially prejudiced if a further extension of the Stay is granted.

20. The Proposal Trustee supports the recognition of the Critical Suppliers and the authorization of the contemplated payments thereto as set out in this First Report.

All of which is respectfully submitted this 2nd day of July 2019.

Hardie & Kelly Inc.
in its capacity as the Proposal Trustee of OAN Resources Ltd.
and not in its personal capacity

Per:

Marc Kelly
Senior Vice President



APPENDIX “A”

OGN Resources Ltd
Cash Flow Forecast
(Unaudited - prepared by management)

Notes regarding assumptions:

1. Net oil sales revenues from sales of crude oil. Revenue from prior month is followed on the 25th day of the current month. Amount of revenue has been estimated based on: Pricing is based on forecast price information provided by Argus, which markets and sells the Company's oil. Production is forecast net of crown royalties taken in June, by analyzing historical production and applying appropriate decline factors for each well, which is an industry accepted and common means of production forecasting.
2. Gross Overriding Royalty (GORR) to Petro Energy has typically been recorded, but not paid due to lack of cash and contract information for entry. This is intended to be paid going forward. GORR APN has no amount owing in June and subsequent estimated.
3. There are payments to key suppliers of Joint Interest Billing (JIB) for periods prior to June '14, 2019 as follows. Failure to pay these amounts could result in an inability to produce and sell OGN production.
 - Highwood Oil Company (HOC) owns an oil battery in which OGN produces oil. HOC provides oil processing facilities.
 - Highwood Oil Company (HOC) owns a processing facility which provides oil processing, water disposal, and tail facilities to the Rainbow marketing pipeline. They also own the pipeline which OGN production passes through.
4. Processed oil and effluent which passes through batteries, separators, and processing facilities are charged on a fixed rate per m3 of fluid. This is invoiced by way of Joint Interest Billing 60-90 days after it is incurred.
5. Citron Oil & Gas provide contract field operations services to July well including field servicing, which is invoiced by way of Joint Interest Billing 60-90 days after it is incurred.
6. Estimated monthly cost for wellbore based on industry averages. It is assumed that this will be required to be paid on a COD basis.
7. Average monthly cost for use of gas services to monitor production rates, wellbore, bottom hole pressure, and wellhead pressure. It is assumed that this will be required to be paid on a COD basis.
8. Expected annual charges for Surface and Mineral Leases, permits to the Government of Alberta.
9. Annual drilling costs of \$4,231.06 and annual property taxes of \$10,302.32.
10. Remaining monthly payments to PetroEnergy for Cost Control and Well Data.
11. Costs well pump lubricants, based on historical and industry averages. It is assumed that this will be required to be paid on a COD basis.
12. Helicopter transportation to wells as needed access is winter only. This is for a cost incurred past July and expected to be settled in July.
13. Certain management salaries are waived in July and August in order to ensure funds are available to meet cash flow obligations. This plan has been agreed to by members of the management team.
14. Monthly rent for office based on contractual amount, plus monthly parking based on contract which will be cancelled August will be last month of parking given the notice period required.
15. Monthly charges for accounting software, Cloud and Backup services, external and phone, including 24-hour phone service.
16. Bi-monthly payments to consultants for regulatory filings and production accounting services, and June expense for consultant required travel to the field.
17. Anticipated payments to legal counsel and Proposal. Trustee retained to propose proceedings.

APPENDIX “B”

District of: Alberta
Division No. 02 - Calgary
Court No. 25-2523592
Estate No. 25-2523592

-- FORM 29 --
Trustee's Report on Cash-Flow Statement
(Paragraphs 50(6)(b) and 50.4(2)(b) of the Act)

The attached statement of projected cash flow of OAN Resources Ltd., as of the 24th day of June 2019 has been prepared by the management of the insolvent person (or the insolvent debtor) for the purpose described in the notes attached, using the probable and hypothetical assumptions set out in the notes attached.

Assumptions:

The assumptions are detailed as an attachment to the cash-flow statement

Our review consisted of inquiries, analytical procedures and discussion related to information supplied to us by: the management and employees of the insolvent person or the insolvent person. Since hypothetical assumptions need not be supported, our procedures with respect to them were limited to evaluating whether they were consistent with the purpose of the projection. We have also reviewed the support provided by: management or the insolvent person for the probable assumptions and preparation and presentation of the projection.

Based on our review, nothing has come to our attention that causes us to believe that, in all material respects,

(a) the hypothetical assumptions are not consistent with the purpose of the projection;

(b) as at the date of this report, the probable assumptions developed are not suitably supported and consistent with the plans of the insolvent person or do not provide a reasonable basis for the projection, given the hypothetical assumptions; or

(c) the projection does not reflect the probable and hypothetical assumptions.

Since the projection is based on assumptions regarding future events, actual results will vary from the information presented even if the hypothetical assumptions occur, and the variations may be material. Accordingly, we express no assurance as to whether the projection will be achieved.

The projection has been prepared solely for the purpose described in the notes attached, and readers are cautioned that it may not be appropriate for other purposes.

Dated at the City of Calgary in the Province of Alberta, this 24th day of June 2019.

Hardie & Kelly Inc. - Licensed Insolvency Trustee

Per:



Charla Smith - Licensed Insolvency Trustee
110, 5800 2nd Street SW
Calgary AB T2H 0H2
Phone: (403) 777-9999 Fax: (403) 640-0591

APPENDIX “C”

District of: Alberta
Division No. 02 - Calgary
Court No. 25-2523592
Estate No. 25-2523592

- FORM 30 -
Report on Cash-Flow Statement by the Person Making the Proposal
(Paragraphs 50(6)(c) and 50.4(2)(c) of the Act)

I, OAN Resources Ltd., have developed the assumptions and prepared the attached statement of projected cash flow of the insolvent person, as of the 24th day of June 2019.

Assumptions:


The assumptions are detailed in an attachment to the cash-flow statement

The hypothetical assumptions are reasonable and consistent with the purpose of the projection described in the notes attached, and the probable assumptions are suitably supported and consistent with the plans of the insolvent person and provide a reasonable basis for the projection. All such assumptions are disclosed in the notes attached.

Since the projection is based on assumptions regarding future events, actual results will vary from the information presented, and the variations may be material.

The projection has been prepared solely for the purpose described in the notes attached, using a set of hypothetical and probable assumptions set out in the notes attached. Consequently, readers are cautioned that it may not be appropriate for other purposes.

Dated at the City of Calgary in the Province of Alberta, this 24th day of June 2019.



OAN Resources Ltd.
Debtor



Name and title of signing officer

Name and title of signing officer