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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 OILSANDS QUEST INC., OILSANDS QUEST SASK INC., OILSANDS QUEST TECHNOLOGY INC., 1291329 ALBERTA LIMITED, STRIPPER ENERGY SERVICES INC., and TOWNSHIP PETROLEUM CORPORATION	
DOCUMENT	**FIRST REPORT OF THE MONITOR** **DECEMBER 15, 2011**	
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**MONITOR** ERNST & YOUNG 1000, 440 - 2nd Avenue SW Calgary, Alberta T2P 5E9 Attention: Neil Narfason / Orest Konowalchuk Telephone: 403-206-5067 / (403) 206-5698 Fax: 403-206-5075 Email: Neil.Narfason@ca.ey.com Cassie.Hern@ca.ey.com **COUNSEL** Borden Ladner Gervais LLP Barristers & Solicitors Centennial Place, East Tower 1900, 520 – 3rd Avenue SW Calgary, Alberta T2P 0R3 Attention: Patrick T. McCarthy, Q.C. / Josef G. A. Krüger, Q.C. Phone: (403) 232-9500 / (403) 232-9563 Fax: 403-266-1395 Email: pmccarthy@blg.com jkruger@blg.com	

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INTRODUCTION

1. On November 29, 2011, Oilsands Quest Inc., Oilsands Quest Sask Inc., Oilsands Quest Technology Inc., 1291329 Alberta Limited, Stripper Energy Services Inc., and Township Petroleum Corporation (collectively "Oilsands Quest" or the "Company") sought and obtained protection from their creditors under the Companies' Creditors Arrangement Act, R.S.C. 1985 c. C-36, as amended, (the "CCAA") pursuant to an order of this Honourable Court (the "Initial Order").

2. Pursuant to the Initial Order, Ernst & Young Inc. was appointed monitor of the Company (the "Monitor").

3. The purpose of this first report (the "First Report") of the Monitor is to provide this Honourable Court with the Monitor's comments in respect of the following:

    a) A brief operational update;

    b) The notices issued to creditors regarding the granting of the Initial Order;

    c) An update on the restructuring plan;

    d) The Company's proposed retention plan;

    e) The revised cash flow projections (the "Revised Cash Flow Projections") from December 12, 2011 to February 28, 2012 (the "Forecast Period");

    f) The Monitor's comments regarding the Company's request for an extension of the stay period; and

    g) The Monitor's recommendations.

4. Capitalized terms not defined in this First Report are as defined in the Initial Order.

5. All references to dollars are in Canadian currency unless otherwise noted.

BACKGROUND

6. The Company is a development stage company which holds certain permits, licenses and leases in Alberta and Saskatchewan allowing it to explore and develop natural resource properties. To date the Company has not received any revenue from any of its natural resource properties, and none of its projected resources have been classified as proved reserves. The Company expects that significant additional exploration and development activities will be necessary to establish proved reserves, and, if reserves are proven, to develop the infrastructure necessary to facilitate production from its natural resource properties.

7. The Company's oil sand leases in Alberta and Saskatchewan (collectively the "Oilsands Assets") are:

   a) Axe Lake, SK;
   b) Wallace Creek, AB;
   c) Raven Ridge, AB; and
   d) Eagles Nest, AB.

8. The Company has 19 employees and contractors.

9. Further background for the Company and its operations is contained in the materials filed in support of the application for the Initial Order including the November 28, 2011 affidavit of Mr. Garth Wong (the "November 28 Wong Affidavit"). This document, together with other information regarding this CCAA proceeding, has been posted by the Monitor on its website at: www.ey.com/ca/oilsandsquest.

TERMS OF REFERENCE

10. In preparing this First Report, the Monitor has relied upon unaudited financial information, company records and discussions with management of the Company.

The Monitor has not performed an audit, review or other verification of such information. An examination of the financial forecast as outlined in the Canadian Institute of Chartered Accountants Handbook has not been performed. Future orientated financial information relied upon in this report is based on management's assumptions regarding future events and actual results achieved will vary from this information and the variations may be material.

OPERATIONAL UPDATE

11. Following the granting of the Initial Order, there have been no material changes in the Company's operations. It has maintained its full workforce and has generally enjoyed the support of its critical vendors.

12. The Company's actual cash flow results for the first two weeks of these CCAA proceedings have been in line with the cash flow projections which were attached as Exhibit D to the November 28 Wong Affidavit.

NOTICE TO CREDITORS (THE "NOTICE")

13. Pursuant to the terms of the Initial Order, the Monitor:

    a) Published the Notice in the Calgary Herald on December 3, 2011;

    b) Made the Initial Order publicly available on the Monitor's website effective November 29, 2011;

    c) On December 6, 2011 mailed the Notice to every known creditor identified to it by the Company (the "Known Creditors") as having a claim of more than $1,000; and

    d) Prepared a list showing the names and addresses of the Known Creditors and made the list publicly available on the Monitor's web site effective December 8, 2011.

14. The Notice also advised that if a creditor was unable to obtain a copy of this Order from the Monitor's website, it could request a copy be delivered.

RESTRUCTURING

15. On August 13, 2010 Oilsands Quest engaged TD Securities Inc. ("TD") as a financial advisor to explore strategic alternatives for enhancing shareholder value. The agreement with TD was amended on February 8, 2011 (the August 13, 2010 and the February 8, 2011 TD agreements are collectively referred to as the "Original TD Agreement").

16. Oilsands Quest plans to revitalize the strategic alternatives process and further amend its engagement of TD to allow TD to assist in identifying and analyzing potential strategic alternatives available with respect to Oilsands Quest's Oil Sands Assets, establish a solicitation process ("SP") for Court approval and, if approved by the Court, lead the SP. Negotiations regarding the terms of that amended engagement are ongoing.

17. Oilsands Quest expects that it will seek Court approval of the terms of the amended engagement of TD in January 2012.

KEY EMPLOYEE RETENTION PLAN

18. As set out in the December 14, 2011 Wong Affidavit filed in support of the Oilsands Quest's application returnable on December 20, 2011, the Company is seeking this Honourable Court's approval of a proposed key employee retention plan for a limited number of its employees (the "2012 KERP"). The intention of the KERP is to ensure that those employees considered essential to the continuation of the operations and a successful restructuring are retained (the "Key Employees").

19. The Companies' ability to successfully reorganize depends on the continued employment, active participation and dedication of the Key Employees who possess the knowledge, experience and skills necessary to support the Company's day-to-day operations. The Key Employees are particularly crucial to meeting the Company's U.S. public reporting requirements. Certain of them also have extensive experience with, and knowledge of the geological structure of the

Oilsands Assets, which will be essential to supporting the proposed solicitation process.

20. As well, the active job market in Alberta and Saskatchewan currently provides other viable employment options for the Key Employees. The Key Employees have been anxiously awaiting details of the 2012 KERP and many have concerns with respect to job security and compensation. Finding suitable replacements for any departing Key Employees could be difficult and costly due to costs associated with executive search firms, relocation expenses and bonuses as well as a perceived need, in light of the Company's situation, to pay above-market salaries to interest good quality prospects. In addition, the loss of certain Key Employees could create further stability concerns, potentially leading to additional departures and creating a momentum of attrition.

Methodology in developing the KERP

21. In early 2011 Oilsands Quest established a retention program for its employees for fiscal 2001 (the "F11 Retention Plan"). The F11 Retention Plan is described in the November 28, 2011 Wong Affidavit. Under that program employees were able to receive up to 75% of their base salary if they stayed with the Company under the earlier of December 31, 2011 or a significant sale.

22. The bonuses for Key Employees under both the F11 Retention Plan and the proposed 2012 KERP were established by Oilsands Quest's senior management based on the following factors:

    (i) The nature of the employees' job requirements and experience;

    (ii) The employees' relevance to a successful restructuring; and

    (iii) The estimation of the cost and risk that without appropriate incentives the Key Employees would seek alternate employment.

Summary of KERP

23. The proposed 2012 KERP covers seven Key Employees and assumes a total payment of approximately $603,250.

24. The basic terms of the KERP can be summarized as follows:

a) Key Employees who remain with the Company until the earlier of the Company's exit from the CCAA (defined as date when the CCAA process is terminated by the Court) or December 31, 2012 will receive a bonus of 50% of their base salary; and

b) The 2012 KERP will be payable in two instalments, one in July 2012 and the second in January 2013.

December 31, 2012 has been selected as an end date for payment of the 2012 KERP because it allows for the retention of staff throughout the next critical phases of the CCAA process and will allow the Company to meet its regulatory obligations.

25. Payments of bonuses under the 2012 KERP will only be made if, at the relevant date the Key Employee:

(i) has not voluntarily resigned or been terminated for cause; and

(ii) has fulfilled his or her employment obligations to the Company.

Allocation of the cost of the 2012 KERP

26. The cost of the 2012 KERP is to be allocated amongst two of the Oilsands Quest entities based on an estimate of the percentage of time spent by the Key Employees in respect of each entity, drawn from weekly time summaries. Based on historical allocation rates, it is anticipated that approximately 71% of the 2012 KERP bonus will be allocated to Oilsands Quest Inc. the with the remaining 29% of the 2012 KERP bonus being allocated to Oilsands Quest Sask Inc.

2012KERP review and analysis

27. The Monitor compared Oilsands Quest's proposed 2012 KERP with similar programs authorized in recent CCAA and Chapter 11 filings (the "Benchmark Data"). The Monitor's analysis indicated that Oilsands Quest's proposed 2012 KERP terms and the total payments are consistent with the Benchmark Data.

28. The Monitor believes that the proposed 2012 KERP is reasonable and that it is critical to ensuring that key personnel are retained to maintain the Company's business and operations and to develop and finalize a restructuring plan.

29. The Company proposes that the retention payment amounts payable in July 2012, amounting to approximately $301,625, will be transferred to the Company's counsel in January 2012, to be held in trust. The remainder of the payments due under the 2012 KERP would be secured under the Administration Charge in the Initial Order, as discussed in the December 14 Wong Affidavit.

REVISED CASH FLOW FORECAST THROUGH FEBRUARY 28, 2012

30. The Company, with the assistance of the Monitor, has prepared a forecast for the period December 12, 2011 to February 28, 2012 (the "Forecast Period") which are attached as Exhibit A to the December 14 Wong Affidavit (the "Forecast"). Management has prepared the Forecast based on the most current information available.

31. The table below summarizes cash flow for the Forecast Period:

Consolidated cash flow forecast		December 12, 2011- February 28, 2012
RECEIPTS		
Camp Service		1,100,000
Alberta Road Maintenance		976,144
Main Road Maintenance		466,145
GST collected		127,114
Total receipts		2,669,403
DISBURSEMENTS		
Corporate recurring G&A		714,840
Corporate payroll and benefits		739,503
Insurance		374,000
Operating Expenses		2,974,656
Land tenure		66,512
Litigation		-
Strategic alternatives process		-
CCAA professional fees		320,000
GST paid		230,637
Total disbursements (before interest payments)	**$**	**5,420,149**
Foreign exchange gains / (losses)		-
NET CASH FLOWS	**$**	**(2,750,745)**
OPENING CASH	$	3,408,237
NET CHANGE IN CASH FLOWS		(2,750,745)
ENDING CASH	$	657,492

32. As summarized above, the Company is projecting total cash receipts of approximately \$2.7 million against cash disbursements of approximately \$5.4 million, resulting in a net decrease in cash of approximately \$2.7 million during the Forecast Period.

33. The Monitor has reviewed the assumptions supporting the Forecast and believes the assumptions to be reasonable.

34. Significant assumptions made by the Company's management with respect to the Forecast are:

a) Oilsands Quest revenues relate to a camp rental agreement and two road maintenance agreements with Cenovas;

b) GST collected is based on 5% of Cenovus billings;

c) Corporate recurring G&A costs are based on recent historical results and includes directors' fees and expenses and professional fees;

d) Payroll amount is based on average pay periods and includes 50% of the 2012 KERP to be placed in trust;

e) Insurance is an estimate for the Directors' and Officers' insurance; and

f) Operating expenses are based on camp and road usage agreements with Cenovus.

35. Based on the Company's assumptions, the Forecast indicates that the Company will continue to have sufficient available cash to meet its current obligations through the Forecast Period.

THE COMPANY'S REQUEST FOR AN EXTENSION OF THE STAY PERIOD

36. Pursuant to the Initial Order, as amended, the Stay Period expires on December 21, 2011. The Company is seeking an extension of the Stay Period to and including, February 17, 2012 (the "Stay Extension").

37. The Stay Extension is necessary to allow the Company to finalize the terms of TD's engagement, and develop and conduct an SP.

38. In the Monitor's view, the Company is acting in good faith and with due diligence.

RECOMMENDATIONS

39. The Monitor recommends that this Honourable Court approve:

a) the KERP; and

b) the Stay Extension.

Dated at Calgary, this 15th day of December, 2011.

ERNST & YOUNG INC.
in its capacity as
Monitor of Oilsands Quest

Neil Narfason, CA•CIRP, CBV
Senior Vice-President

Cassie Hern, CA
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