COURT FILE NUMBER	1201-05287
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
APPLICANT	**HSBC BANK CANADA**
DEFENDANT	**X-TREME ENERGY GROUP INC.**
DOCUMENT	**THIRD REPORT OF ERNST & YOUNG INC. IN ITS CAPACITY AS RECEIVER AND MANAGER OF X-TREME ENERGY GROUP INC.**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**Norton Rose Canada LLP** 400 3rd Avenue SW, Suite 3700, Calgary, Alberta T2P 4H2

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INTRODUCTION

1 On April 30, 2012, the Court of Queen's Bench of Alberta issued an order appointing Ernst & Young Inc. ("**EYI**") as Receiver and Manager (the "**Receiver**") of X-Treme Energy Group Inc., now 1627090 Alberta Ltd., ("**X-Treme**").

2 EYI, in its capacity as Receiver of X-Treme, filed its first report to this Honourable Court on July 5, 2012 (the "**First Report**").

3 EYI, in its capacity as Receiver of X-Treme, filed its second report to this Honourable Court on November 1, 2012 (the "**Second Report**").

PURPOSE OF THIS REPORT

4 The purpose of this report (the "**Third Report**") is to update this Honourable Court with respect to counsel for the Receiver's review of the security held by HSBC Bank Canada ("**HSBC**").

SECURITY OF HSBC

5 In the course of the Second Report, particularly at paragraph 63, the Receiver stated:

> Counsel to the Receiver has completed a review of the first ranking security held by HSBC over the assets of X-Treme and has advised the Receiver that it is satisfied that it ranks in priority to all other creditors subject to the qualifications referenced in this Second Report.

6 It was subsequently determined that counsel for the Receiver had completed a partial security review with respect to certain interests however, had not completed a fulsome or final written review of the security held by HSBC.

7 Counsel for the Receiver appeared before this Honourable Court on November 7, 2012 and advised of its oversight as it related to having completed a final review of the HSBC security. Counsel for the Receiver further advised this Honourable Court that it would forthwith be preparing a review of the HSBC security.

8 Counsel for the Receiver prepared a Security Review dated December 3, 2012 a complete copy of which was provided to counsel for HSBC, Borden Ladner Gervais LLP, and to counsel for ADT Petroservicios, S.A. De C.V. ("**ADT**"), Peacock Linder & Halt LLP, in early December, 2012.

9 A copy of the Security Review is attached to this Third Report as Schedule "A".

10 As referenced in the Security Review, ADT commenced an action in the Court of Queen's Bench (the Amended Statement of Claim filed by ADT is attached to the Security Review as Schedule "C") against various parties including X-Treme and HSBC. The action relates to the alleged breach of certain contracts for the fabrication and financing of drilling rigs in Mexico. ADT has sought various forms of relief against the Defendants and has particularly sought against HSBC a

declaration that any indebtedness of X-Treme to HSBC is equitably subordinated to the indebtedness of X-Treme to ADT.

11 The Security Review prepared by counsel for the Receiver considered that ADT proceeding and contains a detailed review of the law with respect to equitable subordination.

RECOMMENDATION

12 Counsel for each of the Receiver, HSBC and ADT has agreed to a form of **Order** regarding the interim distribution of funds (the "Interim Distribution Order") currently held by the Receiver following the sale of the core business assets of X-Treme (as is more particularly described in the Second Report of the Receiver).

13 The Receiver recommends that the Court approve the Interim Distribution Order.

All of which is respectfully submitted this 24th day of January, 2013.

ERNST & YOUNG INC.
IN ITS CAPACITY AS RECEIVER AND MANAGER OF X-TREME ENERGY GROUP INC. AND NOT IN ITS PERSONAL CAPACITY

Neil Narfason, CA•CIRP
Senior Vice-President

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On January 1, 2012, Macleod Dixon joined Norton Rose OR to create Norton Rose Canada.

Memorandum

From	NORTON ROSE CANADA LLP	Date	December 3, 2012
		Our Ref	01128610-0051
To	ERNST & YOUNG INC.		

REVIEW OF LOAN DOCUMENTS GRANTED TO HSBC BANK CANADA (THE "LENDER") BY X-TREME ENERGY GROUP INC. ("XEG"), X-TREME BITS AND DOWNHOLE TOOLING LTD. ("TOOLING") AND X-TREME ENERGY RENTALS LTD. ("RENTALS")

I. EXAMINATION OF DOCUMENTS

At your request and on your behalf, we have reviewed certain security and related documents as outlined below:

1. Facility Letter Agreement dated February 10, 2010 between the Lender, as lender, and XEG, as borrower;

2. Facility Letter Agreement dated May 21, 2010 between the Lender, as lender, and XEG, as borrower;

3. Facility Letter Agreement dated September 14, 2010 between the Lender, as lender, and XEG, as borrower;

4. Line of Credit by Way of Current Account Overdraft Agreement dated December 18, 2009 granted by XEG in favour of the Lender;

5. General Security Agreement dated December 18, 2009 granted by XEG in favour of the Lender (the "**XEG GSA**");

6. $6,500,000 Demand Collateral Mortgage dated December 18, 2009 granted by XEG in favour of the Lender (the "**Mortgage**");

7. General Assignment of Rents dated December 18, 2009 granted by XEG in favour of the Lender (the "**General Assignment of Rents**");

8. Security Over Cash, Credit Balances and Deposit Instruments By Third Party dated September 23, 2010 granted by XEG in favour of the Lender (the "**XEG Deposit Security Agreement**");

9. Guarantee dated May 25, 2010 granted by Toolings in favour of the Lender;

10. General Security Agreement dated May 25, 2010 granted by Toolings in favour of the Lender (the "**Toolings GSA**");

11. Guarantee dated June 4, 2010 granted by Rentals in favour of the Lender;

12. General Security Agreement dated June 4, 2010 granted by Rentals in favour of the Lender (the "**Rentals GSA**"); and

13. PPSA Search Results with respect to the Loan Parties.

The documents in paragraphs 1-12 inclusive are referred to collectively as the "**Loan Documents**", and the documents in paragraphs 5, 8, 10 and 12 are referred to collectively as the "**Security Documents**". XEG, Rentals, Toolings and 1627090 Alberta Ltd. ("**1627090**") are collectively referred to as the "**Loan Parties**". Unless otherwise defined in this memorandum, capitalized terms have the meanings given to them on **Schedule "A"** hereto.

II. SEARCHES

The registration particulars against the Loan Parties as disclosed by our searches under the PPSA are summarized in **Schedule "B"** hereto. We note that in addition to the registrations in favour of the Lender, (i) there are other registrations against XEG, some of which may be purchase money security interests, as well as two registrations in favour of the Worker's Compensation Board and (ii) there is one registration against Toolings that may be a Purchase Money Security Interest.

III. QUALIFICATIONS AND ASSUMPTIONS

This security review is subject to the qualifications and assumptions set out in **Schedule "C"** hereto.

IV. SUMMARY OF CORPORATE HISTORY

On September 1, 2011, XEG, Toolings and Rentals amalgamated to form X-Treme Energy Group Inc. ("**Amalgamated XEG**") (the "**Amalgamation**"). We note that the Lender's registrations against each of Toolings and Rentals were not updated at the Alberta Personal Property Registry to reflect the name change of Toolings and Rentals to Amalgamated XEG. However, as reflected in Schedule "B" hereto, the only registrations against Toolings and Rentals are registrations in favour of the Lender (other than registration number 10093027948 against Toolings in favour of Sissons Enterprises Corp. and Tank Direct, the particulars of which are summarized in Schedule "B" hereto).

Further, on September 6, 2012, Amalgamated XEG changed its name to 1627090 Alberta Ltd. (the "**Name Change**"). We note that the Lender's registration against XEG, Toolings and Rentals were not updated to reflect the Name Change. However, as reflected in Schedule "B" hereto, there are no registrations against 1627090.

V. SALE APPROVAL AND VESTING ORDER

The Lands were transferred to P & O XEG Assets Ltd. (the "**Purchaser**") on August 21, 2012 as a result of the registration at the LTO of that certain Sale Approval and Vesting Order by Justice T.H. McMahon of the Court of Queen's Bench pronounced July 5, 2012 at Calgary, Alberta, as amended by an Amended Sale Approval and Vesting Order by Justice William A. Tillman of the Court of Queen's Bench pronounced August 17, 2012 (collectively, the "**Order**"). The Order was registered at the LTO as Instrument No. 122 272 988.

The Order approved a certain asset purchase agreement and the sale of certain assets which include the Lands (the "**Purchased Assets**") from Ernst & Young Inc. (the "**Receiver**"), in its capacity as Court-appointed Receiver of the assets, undertakings and property of Amalgamated XEG, to the Purchaser. The Order provides that upon the delivery of a certified copy of the Order to the Registrar of Land Titles for the South Alberta Land Registration District (the "**Registrar**") and a written request from the Receiver or the Receiver's counsel to do so, the Registrar shall: (a) cancel certificates of title to the Lands; (b) issue a new certificate of title to the Lands in the name of the Purchaser or its nominee (the "**New Title**"); and (c) discharge any and all encumbrances from the New Title that are not listed in Schedule "B" to the Order. The encumbrances listed in Schedule "B" of the Order do not include the Mortgage or the General Assignment of Rents and, accordingly, they were discharged from title to the Lands upon registration of the Order. The Order provides that the Receiver will hold the proceeds from the sale of the Purchased Assets, less closing costs of the Receiver (the "**Net Proceeds**") pursuant to the terms of the Order and that the Net Proceeds stand in place and stead of the Purchased Assets and any Claimants may assert their Claims against the Net Proceeds with the same right and priority that the Claimants had against the Purchased Assets immediately prior to the sale of the Purchased Assets, as if the Purchased Assets had not been sold and remained in the possession and control of Amalgamated XEG. The Order provides that the Net Proceeds can not be disbursed by the Receiver unless an order allowing for a disbursement of the Net Proceeds is issued by the Court. For purposes of this paragraph, "Claimants" and "Claims" each have the meaning ascribed thereto in the Order.

VI. LITIGATION COMMENCED BY ADT PETROSERVICIOS, S.A. DE C.V. ("ADT")

ADT commenced an action in the Alberta Court of Queen's Bench (Court File No. 1101-12738) against each of XEG, the former President and Chief Executive Officer of XEG, Brian Edward Gibbs ("**Gibbs**"), the Lender, Axiom Oilfield Services Ltd. and an unidentified corporate entity (the "**ADT Action**"). The ADT Action can, in general terms, be summarized as follows:

1. In or about 2009, ADT and XEG participated together as a joint venture and consortium for the purposes of bidding on a project to supply five drilling rigs to Pemex Exploracion Y Produccion ("**Pemex**") in Mexico.

2. ADT, XEG and Pemex entered into an agreement entitled "Asset Purchase and Services Agreement for the Acquisition of Five New Rigs, with a Capacity of 750-HP, including their Installation, Pre-start-up, Start-up and Maintenance for the Northern Division" (the "**Pemex Contract**"). In connection with the Pemex Contract, ADT and XEG entered into a Joint Participation Agreement (as amended) (the "**JPA**").

3. XEG and Gibbs represented and agreed that XEG would obtain financing for the purpose of financing the fabrication and construction of the rigs contemplated in the Pemex Contract (the "**Rig Financing**").

4. The Lender provided the Rig Financing which was guaranteed by ADT pursuant to a Limited Recourse Guarantee made as of June 15, 2010 (the "**Limited Recourse Guarantee**"). As a consequence of the Limited Recourse Guarantee, ADT also granted to HSBC a Floating Lien Pledge Agreement, an Irrevocable Security, Administration and Source of Payment Trust Agreement and a Collection Rights Assignment Agreement (collectively the "ADT **Security Agreements**").

5. Pursuant to the JPA, ADT advanced to XEG the sum of USD $11,221,130.00, paid $5,000,000.00 to third party subcontractors on behalf of XEG and incurred other costs with respect to construction of the Rigs contemplated in the Pemex Contract.

6. ADT alleges that XEG, in breach of its contractual obligations and representations to ADT, failed to deliver the rigs in accordance with the Pemex Contract and used amounts advanced by ADT, including the Rig Financing, for purposes other than the fabrication and construction of the Rigs

contemplated in the Pemex Contract. It is also alleged that XEG engaged in misrepresentation and fraud, induced breach of contract and breached its fiduciary duties and duty of good faith, among other things, to ADT.

7. ADT alleges that the Lender knew or ought to have known that XEG had diverted and converted funds, including the Rig Financing, advanced by ADT for improper purposes. ADT further alleges that the Lender actively participated in a scheme to divert funds, including the Rig Financing, advanced by ADT for improper purposes. ADT further alleges that the Lender breached its duty of care to ADT in that HSBC knew or ought to have known that XEG and Gibbs were participating in a conspiracy to defraud ADT.

In the ADT Action, ADT seeks the following relief against the Lender:

1. A declaration and judgment that each of the Limited Recourse Guarantee and the ADT Security Agreements are of no force and effect.

2. A declaration and judgment that ADT is released from each and all of its obligations under each of the Limited Recourse Guarantee and the ADT Security Agreements.

3. A declaration and judgment that the Lender is vicariously liable for the acts of its employees and agents.

4. In the alternative, a declaration and judgment that the Limited Recourse Guarantee does not apply to and ADT has not guaranteed any Rig Financing applied by XEG for improper purposes.

5. Further, or in the alternative, a declaration that any indebtedness of XEG to the Lender is equitably subordinated to the indebtedness of XEG to ADT.

A copy of the Amended Statement of Claim filed by ADT is attached as **Schedule "C"** hereto.

The only substantive evidence tendered by ADT to date is the Affidavit of Willem Bauke (Bob) Postma filed September 28, 2012 in the ADT Action (**Schedule "D"**). The only evidence filed by ADT in the XEG receivership action is two affidavits of a legal assistant attaching corporate searches and correspondence amongst counsel.

VII. EQUITABLE SUBORDINATION

The doctrine of equitable subordination enables a court to subordinate a creditor's claim or interest when the creditor has acted inequitably and harmed its debtor or the debtor's other creditors.

Michael MacNaughton and Sam Rappos summarized the current state of the doctrine of equitable subordination in Canada in the following terms:

> [...] Although the case law has been uneven, it appears that Canadian courts are generally open to considering the applicability of the doctrine to the facts before it. That being said, it is unlikely that a court will use the doctrine to simply adjust claims merely because the court perceives a result as being inequitable. The jurisprudence supports the argument that it will be necessary for a claimant to convince the court that the facts of the case are so offensive that it warrants the intrusion of the Court using equitable principles. [...] [C]ourts have regularly held that the facts before it did not satisfy the court that a party had engaged in sufficiently inequitable conduct to warrant the use of the doctrine. As a result, it may be difficult for claimants to satisfy the inequitable conduct threshold.

> Whether a court utilizes equitable principles will depend on whether there are statutory provisions that determine priority amount competing creditors. [...] Ontario courts have confirmed that courts may use equitable principles to determine the priority amongst competing creditors where no statutory priority determination exists. However, such cases do not necessarily recognize the doctrine of equitable subordination in Canada per se, as the courts did not consider it necessary to consider the three-party equitable subordination test.[1]

In *Canadian Deposit Insurance Corp.* v. *Canadian Commercial Bank*, the Supreme Court of Canada declined to opine on whether or not the doctrine had a rightful place in Canadian Insolvency law but referred to the three part test for equitable subordination set out in the American case of *Re: Mobil Steel*:

> ...(1) the claimant must have engaged in some type of inequitable conduct; (2) the misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant; and (3) equitable subordination of the claim must not be inconsistent with the provisions of the bankruptcy statute...[2]

On the basis of our research, we have identified a number of Canadian cases that have substantively considered claims of equitable subordination.

(i) Unsuccessful Canadian Claims of Equitable Subordination

National Bank of Canada v Merit Energy Ltd.

A number of underwriters (the "**Underwriters**") entered into an underwriting agreement with Merit. The Underwriters then "entered into Subscription and Renunciation Agreements with Merit for the purchase of the Flow-Through Shares"[3]. Merit, however, "did not incur CEE [Canadian Exploration Expense] as anticipated" and, "[a]s a result, those Flow-Through Shareholders, who anticipated tax deductions based on $15 million of CEE, were potentially faced with a tax problem".

Merit, PricewaterhouseCoopers, the Underwriters and the Directors and Officers of Merit were all sued by the Flow-Through Shareholders. PWC was specifically sued for misrepresentation.

Justice LoVecchio considered the following issues:

1. Are the claims of the Flow-Through Shareholders subordinate to the claims of Merit's unsecured creditors?

2. Are the claims of the Underwriters, the Directors and Officers and [PWC] subordinate to the claims of Merit's unsecured creditors?

Having found that the Flow-Through Shareholders' claims were, "in substance claims for the return of the equity investment and accordingly [could not] rank with Merit's unsecured creditors"[4], Justice LoVecchio concluded that the Underwriters' and Directors and Officers claims against Merit were creditors' claims which ranked with Merit's other unsecured creditors[5]. PWC's indemnity claim was also found to be a

[1] Michael J. MacNaughton and Sam P. Rappos, "Equitable Subordination in Canadian Insolvency Law" in Janis P. Sarra ed., *Annual Review of Insolvency Law 2008* (Toronto: Carswell, 2009) at 169-170.
[2] *Canadian Deposit Insurance Corp. v. Canadian Commercial Bank (1992)*, 16 C.B.R. (3d) 154 at para. 91.
[3] *National Bank of Canada v. Merit Energy Ltd.*, 2001 ABQB 583, aff'd 2002 ABCA 5, at para. 16.
[4] *Ibid* at para. 55
[5] *Ibid* at para. 72

creditor's claim ranking with Merit's other unsecured creditors[6]. In so finding, Justice LoVecchio considered the principles of equitable subordination:

> In *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, the Supreme Court of Canada expressly left open the question of whether equitable subordination formed part of Canadian insolvency law, but expressed its opinion as to the applicable test as developed in the United States:
>
> > ...(1) the claimant must have engaged in some type of inequitable conduct; (2) the misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant; and (3) equitable subordination of the claim must not be inconsistent with the provisions of the bankruptcy statute...(p. 420)
>
> An application of these criteria would lead to the conclusion that **equitable subordination would not apply in this case, even if it was part of Canadian law**.
>
> Although the Trustee suggested that the Underwriters may have "participated" in the misrepresentation, there is **no evidence before me of inequitable conduct on their part.** It is perhaps significant that the Flow-Through Shareholders have not alleged any such misconduct as against the Underwriters, but rather they have only advanced the statutory causes of action available to them under securities legislation.
>
> **As there is no evidence of inequitable conduct on the part of the Underwriters, there can be no corresponding injury to Merit's other creditors, or enhancement of the Underwriters' position.**
>
> Finally, **the application of equitable subordination of the Underwriters' claims in this case would be inconsistent with the established priority scheme contained in the BIA**. The United States Supreme Court addressed this third requirement of consistency in *United States v. Noland* [footnote omitted]:
>
> [t]his last requirement has been read as a "reminder to the bankruptcy court that although it is a court of equity, it is not free to adjust the legally valid claim of an innocent party who asserts the claim in good faith merely because the court perceives the result as inequitable"
>
> This statement encapsulates what the Trustee is asking to the Court to do: subordinate the claims of the Underwriters, who have asserted their claims under their indemnities as they are entitled to do, merely because the result may be perceived as inequitable. The words of the US Supreme Court are consistent with the view that **equitable subordination is an extraordinary remedy that ought to be employed only where there is some misconduct on the part of the claimant. The statutory scheme of distribution in the BIA must be paramount, and if it is to be interfered with, it should only be in clear cases where demonstrable inequitable conduct is present**.[7]
>
> [emphasis added]

[6] *Ibid* at para. 80
[7] *Ibid* at para. 67

I. Waxman & Sons Ltd. (Re)

In *I. Waxman & Sons Ltd. (Re)*, 89 O.R. (3d) 427, fourteen unsecured trade creditors ("**UTC**") claimed that their position should take priority over the claim of Morris Waxman ("**Morris**"), a judgment creditor[8]. The court characterized the issues before it as follows:

1. How should Morris Waxman's claim be characterized? Is it in the nature of debt or equity?

2. If it is in the nature of debt, should it nonetheless be subordinated to the claims of the UTC?[9]

Having concluded that Morris' judgment was a debt claim "properly provable in bankruptcy", the court considered whether or not Morris' claim "should be subordinated to the claims of the UTC"[10]. With respect to the UTC's claim of equitable subordination, the court stated:

> [33] There is of course a danger associated with taking a doctrine divorced from its legal home and applying it to Canada's statutory bankruptcy regime unencumbered with deep knowledge of the origin, development and legal system from which it originated. Canadian legal commentary has been critical of decisions promoting the doctrine absent a deeper familiarity with the American experience. [citation omitted] On the other hand, a vibrant legal system must be responsive to new developments in the law and the need for reform. Jurisprudence from other jurisdictions often provides the impetus or basis for much needed legal developments.
>
> [34] That said, **in the United States, although not the case originally, there is nonetheless a statute that expressly supports the application of such a doctrine. In Canada, no such express statutory approbation exists.** Furthermore, as pointed out by Reilly J. in *Unisource Canada v. Hongkong Bank of Canada*, **many of the principles associated with equitable subordination have already been incorporated into the *BIA*.** It seems to me that the importation or application of a doctrine such as equitable subordination should respond to a lacuna in our law. The Supreme Court has left open the question of whether such a doctrine should be recognized in Canada. Certainly the case before me does not establish the need for such a doctrine. **Even if such a doctrine does exist, the three parts of the test referred to in *Canadian Deposit Insurance Corp. v. Canadian Commercial Bank* have not been met.** There is no legitimate basis on which to subordinate Morris' claim on the grounds of inequitable conduct. Furthermore, in my view, his conduct has not resulted in any injury to the UTC or conferred an unfair advantage on Morris[11].
>
> [emphasis added]

Harbert Distressed Investment Fund, L.P. v. General Chemical Canada Ltd.

The Ontario Superior Court of Justice (Commercial List) likewise declined to apply equitable subordination in *Harbert Distressed Investment Fund, L.P. v. General Chemical Canada Ltd.*, [2006] O.J. No. 3087. General Chemical Canada Ltd. ("**General Chemicals**") was a wholly owned subsidiary and creditor of the American General Chemical Products Industrial Inc. ("**Industrial**") which entered Chapter

[8] *I. Waxman & Sons Ltd. (Re)*, 89 O.R. (3d) 427, aff'd 2010 ONCA 447.
[9] *Ibid* at para 17.
[10] *Ibid* at para 27.
[11] *Ibid* at paras. 33-34

11 protection pursuant to the U.S. *Bankruptcy Code*. JP Morgan Chase Bank was Industrial's "initial debtor in possession ('DIP')"[12]; this role was subsequently taken over by the Plaintiff, Harbert.

Harbet advanced $9 million to JP Morgan Chase Bank which was used to retire its revolving line of credit and Industrial emerged from Chapter 11 protection.

General Chemicals, however, began to have financial troubles and entered into CCAA protection. Despite General Chemical's "active efforts" to try to sell the company, ongoing environmental issues effectively prevented the sale[13]. Specifically, by-products of General Chemical's manufacturing of calcium chloride were sent to a Soda Ash Settling Basin ("**SASB**"), a contaminated site which was expressly excluded from Herbert's security.

General Chemicals had been operating under a "Provincial Certificate of Approval" from the Ministry of the Environment ("**MOE**") when it entered CCAA proceedings. The CCAA order permitted the MOE and Her Majesty in right of Ontario to, *inter alia*, continue to exercise their powers under environmental legislation.

In addition to its environmental issues, General Chemicals was also having difficulties with maintaining proper funding for its pension plans and had outstanding payments to the plans for a total of $4,290,300.

When it became evident that the restructuring was not going to be successful, the CCAA proceedings were terminated and an interim receiver (PricewaterhouseCoopers ("**PWC**")) was appointed pursuant to section 47 of the *BIA*. Morneau Sobeco Limited (the "**Administrator**") was appointed administrator of General Chemical's pension plans.

In response to PWC "moving to request the court's authorization to make an interim distribution of $3.75 million" to Harbert, the Administrator took "the position that even if Harbert [was] a secured lender, with priority over the Administrator, the equities require the subordination of Harbert's security to the position of the Administrator, and thus of the pension plans"[14].

After setting out the American test cited by the Supreme Court in the *CDIC* Case, the Court stated:

> [92] It should be remembered, however, that **equitable subordination has been used sparingly by Canadian courts**. Inequitable conduct requires the court to conduct a broad inquiry into the conduct of the parties to determine what is right and just in all the circumstances. **The test is a "sense of simple fairness." [citation omitted] Equitable subordination is not used, however, to "adjust the legally valid claim of an innocent party who asserts the claim in good faith merely because the Court perceives the result as inequitable." [citation omitted] The court must therefore be careful not to approach the question on the basis of who the competing creditors are (i.e., the "innocent and vulnerable" employees, as opposed to the "sophisticated and wealthy" lender), but rather by the nature of their respective claims.**[15]
>
> [emphasis added]

With respect to the first part of the American test for equitable subordination, specifically whether or not the claimant had engaged in some sort of inequitable conduct, the Court stated:

[12] *Harbert Distressed Investment Fund, L.P. v General Chemical Canada Ltd.*, [2006] O.J. No. 3087 at para 7.
[13] *Ibid* at para 15.
[14] *Ibid* at paras 2 and 90.
[15] *Ibid* at para 92.

> [93] In support of its position concerning "inequitable conduct", the Administrator relies on the fact that as a result of the March 31, 2004 transaction, Harbert become the controlling shareholder of Industrial, General Chemical's parent. The Administrator claims that the Harbert $9 million advance was used to pay off Industrial's DIP loan, rather than directly benefit General Chemical. It says that as a result it would be inequitable for Harbert to be given priority over General Chemical's assets, when General Chemical did not benefit from the advance on the Revolver. To allow this would be at the expense of the members and retirees of the pension plans.
>
> [94] The essence of the Administrator's claim in relation to this part of the test is that General Chemical had no benefit from the Harbert loans. As I have already stated, the evidence does not bear this out. I am persuaded on the basis of Appendices "C" and "D" to the Monitor's twelfth report to the court (attached to the Interim Receiver's first report to the court), that General Chemical itself took draws on the Revolver [the revolving line of credit], quite apart from the $9 million draw used to repay the Industrial DIP loan. That being the case, General Chemical did benefit from the loans.[16]

Despite finding that it would be "inequitable for Harbert to be given priority for its loans to General Chemical"[17], which was sufficient to conclude that equitable subordination was not applicable, the Court continued to examine the next two branches of the American test: whether or not the conduct resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant, and whether or not the claim is inconsistent with the provisions of the bankruptcy statute. With respect to the second and third branches of the American test, the Court stated:

> [96] As to the requirement for injury to creditors or an unfair advantage to Harbert, the Administrator says that the true nature of the Harbert loans gives Harbert an unfair advantage over the other General Chemical creditors. There is no question that as first secured lender, Harbert has an advantage over the other creditors. That is the nature of having this kind of security. **It is true that the interests of General Chemical's innocent and vulnerable employees and pensioners will be adversely affected by Harbert's priority. I cannot see, however, that Harbert's advantage is an *unfair* advantage, of the sort contemplated by the case law.** This part of the argument must fail as well.
>
> [97] Lastly, equitable subordination is only permitted where it would not run contrary to the statutory scheme in the *Bankruptcy and Insolvency Act*. **As the Administrator points out, Canadian courts have shown a willingness to apply the principle of equitable subordination where the ranking provisions of the BIA are not applicable.** [citation omitted] As the court put it in *Bulut,* the court will not apply the doctrine of equitable subordination to alter a *statutory* scheme for determining priorities among creditors. Here, if the Administrator had a lien, the issue of priority between its security and Harbert's would lie outside the BIA. The BIA does not set out a scheme of priorities among secured creditors; it merely says that secured creditors are to be paid in priority to unsecured creditors.[emphasis added]
>
> [98] While the Administrator could meet the third branch of the test, its failure to meet the other two is sufficient to defeat the claim for equitable subordination. As a result, **I do not view this as an appropriate case to employ the doctrine of equitable subordination**.[18]
>
> [emphasis added]

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[16] *Ibid* at paras 93-94.
[17] *Ibid* at para 95.
[18] *Ibid* at paras 96-98.

(ii) Successful Canadian Claims of Equitable Subordination

Bulut v. Brampton (City)

The Ontario Court of Appeal upheld a motion judge's application of the doctrine of equitable subordination in *Bulut v. Brampton (City)*, 185 DLR (4th) 278. In this case, however, there was no legislation applicable to the facts that contained sections pertaining to the priority of claims. The appeal arose out of the bankruptcy of two companies, Everingham Brothers Limited ("**Everingham**") and 764388 Ontario Limited operating as Royal Spas ("**Royal Spas**"). Everingham, a manufacturer of stainless steel cookware, owned a commercial premise ("**Tilbury**") from which Royal Spas leased space. Both Royal Spas and Everingham were owned by Nicholas Bulut and his family, who was also the president of the companies. Sun Life Assurance Company of Canada, a respondent, held the first mortgage to Tilbury in the amount of $2,250,000. Bulut was a secured creditor of Everingham in the amount of approximately $650,000. One of the appellants, 1236517 Ontario Ltd. ("**123**") was a secured creditor of Royal Spas in the approximate sum of $1,500,000.

Everingham defaulted on the Sun Life mortgage in January 1996 and a court granted possession of Tilbury to Sun Life. At this time, both Everingham and Royal Spas had significant amounts of equipment in Tilbury. In May 1997, a bailiff acting on behalf of the City of Brampton levied restraint on Everingham's personal property due to arrears in business taxes in the amount of approximately $80,000. Everingham and Royal Spas sought an order so that they could retrieve their property from Tilbury. A form of order was entered into that permitted Everingham and Royal Spas access to Tilbury in exchange for the payment into court of $35,000 (included occupancy costs) by May 15, 1997. The order resulting from an application of Everingham and Royal Spas to extend that deadline resulted in an order containing the following paragraph, which the court considered to be of central importance:

> 5. THIS COURT ORDERS that if the Plaintiffs [Everingham and Royal Spas] fail to make the payment referred to in paragraph 3 of the Order of the Defendant [Sun Life] shall be at liberty to exercise its right under the writ of possession herein and <u>that any arrears in payment of occupancy costs shall be a charge on the said equipment, inventory and trade chattels in the same manner and to the same extent as a landlord's distress</u> subject to any rulings as to the entitlement and priorities of the parties...[19]
>
> [court's emphasis]

Following Everingham's filing of a Notice of Intention to file a proposal with the official receiver pursuant to the *BIA*, Sun Life applied for and was granted an order containing the following:

> THIS COURT ORDERS AND DECLARES that <u>Sun Life has a charge on the assets of Everingham in the possession of Sun Life on the Premises (the "Assets") and that Sun Life shall be entitled to distrain against the Assets in accordance with the terms of the Occupation Order</u>...[20]
>
> [court's emphasis]

Everingham failed to file a proposal and became bankrupt on October 17, 1997. On October 23, 1997, Bulut and 123 served Sun Life with a notice of their intention to exercise their security interests in accordance with the Ontario *Personal Property Security Act*, RSO 1990, c P-10. Sun Life refused to recognize such. The assets of Everingham and Royal Spas were eventually sold to an interim receiver and the proceeds paid into court. Royal Spas made a voluntary assignment in bankruptcy in on March 31, 1998. Bulut and 123 (collectively, the "**Appellants**") brought the appeal against orders made

[19] *Bulut v. Brampton (City)*, 185 DLR (4th) 278 at para 10.
[20] *Ibid* at para 12.

following a motion for a declaration that their security interest had priority over the occupancy costs payable to Sun Life.

The Appellants conceded (1) that because Sun Life was a secured creditor, priority would be decided outside of the *BIA*; (2) that the *PPSA* was not applicable; and (3) that a judge could make a charging order giving priority over other secured creditors.

In the majority judgment, the Court of Appeal agreed with the motion judge's decision that Bulut's and 123's "misconduct" prevented them from obtaining priority over Sun Life. The motion judge had found that there was:

> '...evidence of a continuing and concerted course of action between and among Mr. N. Bulut and Mr. S. Bulut and their respective corporations, including [123] herein, in delaying the payment of occupancy costs relating to the personal property of Royal Spas and Everingham in respect of which Messrs. Bulut and their respective corporations now claim an interest as second parties, and which personal property Sun Life has effectively warehoused for one year at the cost of $1,305.00 per day'[21].

The Court of Appeal found that "the motions judge's reasons for applying equitable principles to give Sun Life priority over Bulut and [123] [were] sound"[22] and then outlined some of the factors supporting its conclusion which are set out in full below:

> [81] First, the Bulut family were the principals and directing minds of Everingham, Royal Spas and 123 Co. One does not need to pierce corporate veils to agree with the motions judge's description of "Mr. N. Bulut, Mr. S. Bulut and their respective corporations."
>
> [82] Second, Everingham had a huge mortgage from Sun Life. It defaulted on this mortgage in January 1996. Bulut acquired the major part of his security interest in Everingham (approximately $550,000 of a total interest of $650,000) after Everingham's default on the mortgage. Similarly, 123 Co. acquired its security interest in Royal Spas (approximately $1,500,000) in May 1997. Royal Spas was a tenant of Everingham. It is obvious that Bulut and 123 Co. acquired their security interests with full knowledge that Everingham and Royal Spas were in serious financial trouble, especially vis-à-vis Sun Life.
>
> [83] Third, Sun Life's security interest in the personal property at Everingham's premises was obtained in a court proceeding launched by Everingham and Royal Spas in which they sought to obtain their personal property (i.e. equipment and inventory) from Everingham's premises. On May 1, 1997, Nicholas Bulut, the President of both Everingham and Royal Spas, swore an affidavit in support of the motion. At the time Bulut was a secured creditor of both Everingham and Royal Spas. In his affidavit, Bulut spoke on behalf of Everingham and Royal Spas. However, importantly, he also spoke explicitly in his capacity as holder of security interests in the personal property of Everingham and Royal Spas. Bulut stated:
>
>> 15. ... The items of personal property are owned by Everingham and Royal Spas and Everingham and Royal Spas are lawfully entitled to possession of such property. The items of personal property belonging to these corporations are themselves secured under a General Security Agreement. I, Nicholas Bulut, hold the security interest in these items of

[21] *Ibid* at para 79.
[22] *Ibid* at para 80.

> personal property belonging to Everingham and Royal Spas. I am content, Royal Spas is content and Everingham [footnote omitted] is content if the items of personal property simply are released to all three of us and we can sort out our respective interests in the personal property.

> [84] In other words, Bulut was openly representing not only Everingham and Royal Spas, but also himself in his capacity as holder of security interests in the personal property of Everingham and Royal Spas. He was seeking relief from the court in both of these capacities.
>
> [85] Fourth, the motions judge provided Everingham, Royal Spas and Bulut with the relief they sought, provided Everingham and Royal Spas paid occupancy costs of $1,305 per day from April 25, 1997 to the date on which the personal property was removed. This order was not appealed. Yet, almost immediately, the companies stopped making occupancy cost payments. Further, the companies made no serious efforts to remove their personal property. In short, the companies and Bulut (explicitly) and 123 Co. (by strong and fair inference) sought relief from the court, obtained it, did not appeal the court order — and then promptly ignored it.[23]

With respect to equitable subordination, the Court of Appeal specifically stated:

> [87] [...] It is true, as Rosenberg J.A. notes, that the motions judge's orders resemble the doctrine of equitable subordination and that the Supreme Court of Canada and this court have expressly left open the question of whether this doctrine should be introduced into Canadian law: see Canada Deposit Insurance Corp. v. Canadian Commercial Bank, [1992] 3 S.C.R. 558 (S.C.C.); and Olympia & York Developments Ltd. v. Royal Trust Co. (1993), 14 O.R. (3d) 1 (Ont. C.A.).
>
> [88] There is a crucial difference between those cases and this appeal. In those cases, the issue before the courts was whether the doctrine of equitable subordination should be introduced into statutory regimes for determining priorities between creditors. There is, as the courts recognized, a serious issue as to whether courts should modify explicit priorities created by statute, even if the modification arose through the application of equitable principles.
>
> [89] The situation in the present appeal is entirely different. No statutory regime, including the BIA and the PPSA, determines the priority issue as between Sun Life and Bulut and 123 Co. That issue must be determined under common law principles. In that context, there is nothing wrong with a motions judge doing what common law judges have done for centuries, namely considering common law and equitable principles together in an attempt to reach a fair result. That is what the motions judge did on these motions.[24]

Oppenheim v. J.J. Lacey Insurance Ltd.

The Newfoundland and Labrador Supreme Court - Trial Division, extensively discussed equitable subordination in *Oppenheim v. J.J. Lacey Insurance Ltd.*, 2009 NLTD 148 ("***Oppenheim***").

J.J. Lacey Insurance Limited ("**Lacey**") was a body corporate licensed as an insurance broker, and its affiliate, Hiland Company Limited ("**Hiland**") was a body corporate licensed as an insurance company.

[23] Ibid at paras 81-85
[24] Ibid at paras 87-89

At some point, an investigation into both Lacey and Hiland's accounts was undertaken and irregularities were discovered. As a result, Hiland's license as an insurance company was cancelled and a provisional liquidator was appointed ("**Hiland's Provisional Liquidator**"). Following a petition by Hiland's Provisional Liquidator, KPMG was appointed Trustee in Bankruptcy of Lacey. Hiland's Provisional Liquidator thereafter filed a proof of claim pursuant to section 8(1) of the *BIA* for $1,647,939 and an unsecured claim in the amount of $2,910,459.

The Plaintiff Lloyd's, for whom Lacey had acted as an insurance broker and agent, was an unsecured creditor of Lacey's and "appealed the decision of the trustee of Lacey to allow the proof of Hiland in the bankruptcy of Lacey"[25]. Lloyd's statement of claim alleged that Lacey and Hiland, "by their directors, officers, servants and agents, unduly and unlawfully and maliciously and lacking *bona fides* conspired and agreed together, one with the other, or with persons unknown to":

> 1) submit false, inaccurate and misleading information to Lloyd's for the purposes of obtaining, without authorization, and to convert to their own use or the use of directors, officers or shareholders, the benefit of premiums otherwise due and owing to Lloyd's on policies issued pursuant to the Binding Authority Agreements;
>
> 2) submit false, inaccurate and misleading information to Lloyd's, the purpose of which was to mislead, misstate and otherwise mislead Lloyd's as to the true nature of the potential exposure to Lloyd's from the issuance of insurance policies pursuant to the Binding Authority Agreements;
>
> 3) misled Lloyd's as to the premiums written and the potential exposure incurred as a result of the generation of policies of insurance pursuant to the Binding Authority Agreements aforesaid; and
>
> 4) conceal from Lloyd's a true reflection of the insurance risks that Lloyd's, by operation of law, was otherwise obliged to provide cover notwithstanding the failure of the Defendants to remit the premiums.[26]

Having found that "frauds were perpetrated" by, among other things, Lacey and Hiland and assuming that the Hiland's claim was for a legitimately incurred debt, the Court considered whether the debt "could be postponed in favour of the debts of other creditors of Lacey until these creditors receive their full entitlement in the Lacey bankruptcy"[27]. More specifically, the Court questioned "whether the codified scheme of distribution of assets of a bankrupt, under the BIA, can be modified by a court on the basis of equitable principles, in particular the proposed notion of equitable subordination"[28]. The Court went on to quote extensively from an article entitled "Transplanting Equitable Subordination: The New Free-Wheeling Equitable Discretion in Canadian Insolvency Law" (2002) 36 Can. Bus. L.J., 36 by Professor G.W. Telfer:

> [40] Professor Telfer states that there is no statutory provision in the BIA that expressly permits the application of equitable subordination. However, he points out that **under section 183 of the BIA courts exercising jurisdiction in Canada are "invested with such jurisdiction at law and in equity as will enable them to exercise original, auxiliary and ancillary jurisdiction in bankruptcy"**.
>
> [41] At page 55 of his article Professor Telfer summarizes the conflicting positions in Canadian legal commentary regarding the doctrine. He states:

25 *Oppenheim v. J.J. Lacey Insurance Ltd.*, 2009 NLTD 148 at para 5.
26 *Ibid* at para 6.
27 *Ibid* at para 32.
28 *Ibid.*

> Beyond the precise legal authority for the doctrine, Canadian commentators have also taken up the normative debate of whether such judicial intrusion into commercial affairs is desirable. Some authors assert that there are instances "where the facts are so compelling that fairness dictates some adjustment of priorities".[citation omitted] Bankruptcy courts require the discretion in equity "to subordinate the claim of a creditor whose conduct prejudiced an estate".[citation omitted] On a general level, the failure to intervene with an equitable remedy may "permit conduct which is morally offensive to go unpunished and, indeed to be rewarded."[citation omitted]
>
> Poised against the argument in favour of intervention stands the need for commercial certainty in commercial lending. Departure from the legal scheme of priorities "in favour of a discretionary scheme simply aggravates the uncertainty of result".[citation omitted] If courts resorted to equitable remedies, including equitable subordination, the effect would be to alter the priority scheme of the provincial personal property security legislation. This would subvert the PPSAs' purpose, which is to provide a statutory scheme to give certainty and predictability to secured transactions. The introduction of a discretionary regime, it is argued, would create costly litigation, drive up the cost of credit and make reorganizations more difficult as parties jockey to alter legal priorities.

The Court considered the three requirements for a successful claim of equitable subordination as set out in the American jurisprudence and cited by the Supreme Court in CDIC and concluded that (1) *inter alia*, Hiland and Lacey had "engaged in a form of inequitable conduct", and (2) that such conduct injured Lloyds and "conferred a unfair advantage on Hiland"[29]. In other words, the first two branches of the American test had been met.

The Court stated that in a non-insolvency situation, it was "more than satisfied that the common law of equity would subordinate the claim of Hiland to the claim of Lloyd's as against Lacey"[30]. However, the Court had to consider whether or not subordinating Hiland's claim would be inconsistent with the *BIA*:

> [53] **Would I, by equitably subordinating the claim of Hiland to the claim of Lloyd's as against the bankrupt estate of Lacey, be doing something inconsistent with the provisions of the BIA?** Sections 136-141 of the BIA set out the scheme of distribution of the assets of a bankrupt and section 141 specifies that subject to the BIA all claims proved in a bankruptcy shall be paid ratably. This means that the priority of claims set out in section 136 and following sections will have priority over general creditors. However, general creditors are to be paid ratably. By applying equitable subordination to the unsecured claim of Hiland in the bankruptcy of Lacey, would I be doing something which is inconsistent with the provisions of the Bankruptcy statute? Clearly by subordinating the claim of one unsecured creditor to the claims of all other unsecured creditors, I would not be bringing into bankruptcy matters the chaos envisaged by Chadwick, J. in AVEO or Matticks. **While indeed the scheme of distribution in the BIA may have as objects the avoidance of litigation and promotion of expeditious distribution, in my view equitable subordination of the claim of Hiland in this particular matter does not interfere significantly with these objects nor does it have the effect of challenging or interfering with secured creditors because we are dealing only with the rights of unsecured creditors relative to each other.** It is true that by allowing the doctrine of equitable subordination to apply to unsecured creditors *inter se* that litigation about postponing the claims of unsecured creditors would result in

[29] *Ibid* at para 51.
[30] *Ibid* at para 52.

the delay of the distribution of dividends from the bankrupt estate to such disputing creditors. However, it would only delay distribution to the creditor who is sought to be found subordinate. All other unsecured creditors would receive their dividends as they would have received them in the ordinary course of events. Trustees in bankruptcy would simply determine their preliminary distributions based upon the challenged unsecured claim not being subordinated but would not distribute the dividend to that impugned unsecured creditor but would distribute to all other unsecured creditors their ratable share. After the subordination challenge was litigated a trustee could simply adjust payouts in accordance with the result of the subordination litigation. **If the subordination argument were unsuccessful, the harm caused to the creditors sought to be subordinated could be mitigated by solicitor and client costs and interest at the statutory rate from the time of the initial dividend, such interest being chargeable against the creditor seeking the subordination.** None of the chaos envisaged by Chadwick, J. would result in such a situation.

[54] I am therefore satisfied that **the three-part test for equitable subordination as postulated by Iacobucci, J. in CCB is appropriate to be applied in the circumstances of this matter** and conclude that the claim of Hiland in the bankruptcy of Lacey is to be subordinated until all other unsecured claims have been satisfied. **In doing so I see no inequity being caused.** It has been argued that to allow equitable subordination would punish the creditors of the insolvent estate of Hiland, principally policy holders. In my view, this is not an appropriate consideration. The creditors of Hiland have no status in the bankruptcy of Lacey. The creditor of Lacey is Hiland itself, not the creditors of Hiland. Hiland the corporation participated in a fraud against Lloyd's. **The creditors of Hiland should not be indirectly rewarded by the criminal activity of the Hiland corporation**. **Thus, I see no inequity in postponing the claim of Hiland to the other unsecured creditors of Lacey**. **I acknowledge that there is difficulty in limiting the scope of equitable subordination but I cannot defer from finding unfair conduct simply because such conduct is generally difficult to define**. In the case at bar, it is not at all difficult to find unfair, unconscionable and criminal activity on the part of Hiland, Gillingham and Lacey. Difficulty in limiting the scope of the doctrine should not stop courts from expanding the law so that the law responds to those clear cases where right-thinking persons can clearly and easily discern oppressive unfairness as having occurred.

[emphasis added]

VIII. FINDINGS

Based upon and subject to the foregoing and to the qualifications set forth in **Schedule "E"** hereto, we have found that:

1. Each of the Loan Documents (other than the Mortgage and the Assignment of Rents) constitutes a legal, valid and binding obligation of each Loan Party that is a party thereto and is enforceable against such Loan Party in accordance with its terms.

2. Immediately prior to registration of the Order at the LTO and the transfer of the Lands to the Purchaser on August 21, 2012 as a result of the Order, each of the Mortgage and the Assignment of Rents constituted a legal, valid and binding obligation of Amalgamated XEG and was enforceable against Amalgamated XEG in accordance with its terms.

3. The XEG GSA creates in favour of the Lender a valid security interest under the laws of Alberta in any XEG GSA Collateral to which the PPSA applies and in which 1627090 has rights and secures payment and performance of the XEG Obligations. By operation of law, as a result of the

Amalgamation and the Name Change, the obligations of XEG prior to the Amalgamation and the Name Change are now the obligations of 1627090.

4. The XEG Deposit Security Agreement creates in favour of the Lender a valid security interest under the laws of Alberta in any XEG Deposit Collateral in which the PPSA applies and to which XEG has rights and secures payment and performance of the XEG Obligations. By operation of law, as a result of the Amalgamation and the Name Change, the obligations of XEG prior to the Amalgamation and the Name Change are now the obligations of 1627090.

5. Subject to the findings under the heading "Summary of Corporate History" above, registration has been made in all public offices provided for under the laws of Alberta or the federal laws of Canada applicable therein where such registration is necessary to preserve, protect or perfect the security interests created by the XEG GSA in the XEG Collateral to which the PPSA applies.

6. The Toolings GSA creates in favour of the Lender a valid security interest under the laws of Alberta in any Toolings Collateral to which the PPSA applies and in which 1627090 has rights and secures payment and performance of the Toolings Obligations. By operation of law, as a result of the Amalgamation and the Name Change, the obligations of Toolings prior to the Amalgamation and the Name Change are now the obligations of 1627090.

7. Subject to the findings under the heading "Summary of Corporate History" above, registration has been made in all public offices provided for under the laws of Alberta or the federal laws of Canada applicable therein where such registration is necessary to preserve, protect or perfect the security interests created by the Toolings GSA in the Toolings Collateral to which the PPSA applies.

8. The Rentals GSA creates in favour of the Lender a valid security interest under the laws of Alberta in any Rentals Collateral to which the PPSA applies and in which 1627090 has rights and secures payment and performance of the Rentals Obligations. By operation of law, as a result of the Amalgamation and the Name Change, the obligations of Rentals prior to the Amalgamation and the Name Change are now the obligations of 1627090.

9. Subject to the findings under the heading "Summary of Corporate History" above, registration has been made in all public offices provided for under the laws of Alberta or the federal laws of Canada applicable therein where such registration is necessary to preserve, protect or perfect the security interests created by the Rentals GSA in the Rentals Collateral to which the PPSA applies.

10. Immediately prior to registration of the Order at the LTO and the transfer of the Lands to the Purchaser on August 21, 2012 as a result of the Order, the Mortgage and the General Assignment of Rents were registered at the LTO against title to the Lands and the Mortgage constituted a first charge on the Lands, subject to the encumbrances set out in **Schedule "F"** hereto.

11. It is our opinion that the Security Documents of the Lender currently ranks in priority to all other creditor claims as against XEG assets generally subject to certain specific registrations set out in Schedule "B".

12. It is our current information that at least some of the Defendants in the ADT Action have filed Statements of Defence however, no Affidavits of Records have been delivered nor has Questioning pursuant to the Alberta *Rules of Court* commenced. We are not in a position to provide a firm opinion with respect to the claims advanced in the ADT Action and, in particular, whether a Court would equitably subordinate the Lender's secured position to ADT. To date however, it is our view that the evidence tendered to date by ADT does not satisfy the test for

equitable subordination as described by the Supreme Court of Canada in *Canadian Deposit Insurance Corp.* so as to reorganize the registered security set out herein.

IX. RELIANCE

This security review relates exclusively to the Loan Documents and is rendered solely for the use of the addressee hereof and may not be relied on by any other parties for any other purpose without our prior written consent.

SCHEDULE "A"

DEFINITIONS

In this security review:

(a) **"Collateral"** means, collectively, the Rentals Collateral, the Toolings Collateral and the XEG Collateral;

(b) **"Lands"** means, collectively, the lands situate in Alberta and legally described as follows:

(i) Plan 0624793, Block 71, Lot 17, Excepting Thereout All Mines and Minerals;

(ii) Plan 0624793, Block 71, Lot 18, Excepting Thereout All Mines and Minerals;

(iii) Plan 0420312, Block 71, Lot 14, Excepting Thereout All Mines and Minerals;

(iv) Plan 0420312, Block 71, Lot 15, Excepting Thereout All Mines and Minerals;

(v) Plan 7921753, Block 71, Lot U1, Excepting Thereout All Mines and Minerals; and

(vi) Plan 7921753, Block 71, Lot 3, Excepting Thereout All Mines and Minerals;

(c) **"LTO"** means the Land Titles Office (Alberta);

(d) **"PPSA"** means the *Personal Property Security Act* (Alberta);

(e) **"Rentals Collateral"** has the meaning ascribed to the term Collateral in the Rentals GSA;

(f) **"Rentals Obligations"** has the meaning ascribed to the term Obligations in the Rentals GSA;

(g) **"Toolings Collateral"** has the meaning ascribed to the term Collateral in the Toolings GSA;

(h) **"Toolings Obligations"** has the meaning ascribed to the term Obligations in the Toolings GSA;

(i) **"XEG Collateral"** means, collectively, the XEG GSA Collateral and the XEG Deposit Collateral;

(j) **"XEG Deposit Collateral"** has the meaning ascribed to the term Deposits in the XEG Deposit Security Agreement;

(k) **"XEG GSA Collateral"** has the meaning ascribed to the term Collateral in the XEG GSA; and

(l) **"XEG Obligations"** has the meaning ascribed to the term Obligations in the XEG GSA.

SCHEDULE "B"

ALBERTA PPR SEARCH RESULTS

SEARCH RESULTS

1. **1627090 Alberta Ltd. (as of November 23, 2012)**

No Results Found.

2. **X-treme Energy Group Inc. (as of November 23, 2012)**

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
X-TREME ENERGY GROUP INC.	WELLS FARGO EQUIPMENT FINANCE COMPANY	2007-Sep-26	07092611669	1 NEW CTX 620V3 GRAZIANO LATHE CIW 100 KVA TRANSFORMER TOGETHER WITH ALL ATTACHMENTS, ACCESSORIES, ACCESSIONS, REPLACEMENTS, SUBSTITUTIONS, ADDITIONS AND IMPROVEMENTS THERETO, AND ALL PROCEEDS IN ANY FORM DERIVED DIRECTLY OR INDIRECTLY FROM ANY DEALING WITH THE COLLATERAL OR PROCEEDS THEREOF, AND WITHOUT LIMITATION, MONEY, CHEQUES, DEPOSITS IN DEPOSIT-TAKING INSTITUTIONS, GOODS, ACCOUNTS RECEIVABLE, RENTS OR OTHER PAYMENTS ARISING FROM THE LEASE OF THE COLLATERAL, CHATTEL PAPER, INSTRUMENTS, INTANGIBLES, DOCUMENTS OF TITLE, SECURITIES, AND RIGHTS OF INSURANCE PAYMENTS OR ANY OTHER PAYMENTS AS INDEMNITY OR COMPENSATION FOR LOSS OR DAMAGE TO THE COLLATERAL OR PROCEEDS OF THE	2013-Sep-26 23	

NORTON ROSE

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
				COLLATERAL.		
X-TREME ENERGY GROUP INC.	STEELCASE FINANCIAL SERVICES LTD.	2008-Jan-29	08012903690	ALL FURNITURE AND EQUIPMENT LEASED OR FINANCED FROM STEELCASE FINANCIAL SERVICES LTD. INCLUDING BUT NOT LIMITED TO THE ITEMS SET FORTH IN MASTER LEASE AGREEMENT NO. 31798 AND ANY MASTER LEASE EQUIPMENT SCHEDULES, INCLUDING PROCEEDS.	2013-Jan-29	
X-TREME ENERGY GROUP INC.	GE CANADA EQUIPMENT FINANCING G.P.	2008-Jun-26	08062641003	ML00151 2007 DOOSAN G 25P FORKLIFT MV - MOTOR VEHICLE 0712000066A 2006 GILDEMEISTER LATHE NEF600 MV - MOTOR VEHICLE	2013-Jun-26	THE GOODS DESCRIBED HEREIN, WHEREVER SITUATED, AND ALL PRESENT AND AFTER-ACQUIRED INTELLECTUAL PROPERTY, INTANGIBLES, ATTACHMENTS, ACCESSORIES, AND ACCESSIONS THERETO AND SPARE PARTS, REPLACEMENTS, SUBSTITUTIONS, EXCHANGES, AND TRADE INS THEREFORE AND ALL RIGHTS, RECEIVABLES AND CHATTEL PAPER DERIVED FROM OR EVIDENCING THE LEASE OR RENTAL THEREOF BY THE DEBTOR TO THIRD PARTIES, AND ALL PROCEEDS RELATING THERETO. PROCEEDS: ALL OF THE DEBTOR S PRESENT AND AFTER-ACQUIRED PERSONAL

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
						PROPERTY WHICH IS DERIVED DIRECTLY OR INDIRECTLY FROM ANY DEALING WITH OR DISPOSITION OF THE ABOVE-DESCRIBED COLLATERAL, INCLUDING, WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, ALL INSURANCE AND OTHER PAYMENTS PAYABLE AS INDEMNITY OR COMPENSATION FOR LOSS OR DAMAGE THERETO AND ALL CHATTEL PAPER, DOCUMENTS OF TITLE, GOODS, INSTRUMENTS, INTANGIBLES, MONEY, AND SECURITIES.
X-TREME ENERGY GROUP INC.	CHRYSLER FINANCIAL DAIMLERCHRYSLER FINANCIAL SERVICES CANADA INC.	2008-Nov-14	08111414717	ALL ATTACHMENTS, ACCESSORIES, ADDITIONS, ALTERATIONS, REPLACEMENTS & REPAIRS (WHETHER PRESENT OR FUTURE) TO THE VEHICLE COLLATERAL. PROCEEDS: ALL CASH AND NON-CASH PROCEEDS OF THE VEHICLE COLLATERAL INCLUDING WITHOUT LIMITATION PROCEEDS DERIVED DIRECTLY OR INDIRECTLY FROM ANY DEALING WITH THE VEHICLE COLLATERAL OR THAT INDEMNIFIES OR COMPENSATE S THE DEBTOR(S) FOR THE DESTRUCTION OR DAMAGE TO OR LOSS OF THE VEHICLE	2013-Nov-14	

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
				COLLATERAL. THE PROCEEDS MAY TAKE THE FORM OF ANY ONE OR MORE OF THE FOLLOWING: GOODS, DOCUMENTS OF TITLE, CHATTEL PAPER, INSTRUMENTS, MONEY, SECURITIES OR INTANGIBLES. ACCORDINGLY, ANY OF THE DEBTOR(S) AFTER-ACQUIRED PERSONAL PROPERTY MAY BE PROCEEDS AND THEREFORE SUBJECT TO THE SECURED PARTY'S SECURITY INTEREST.		
X-TREME ENERGY GROUP INC.	TRAVELERS FINANCIAL CORPORATION HSBC BANK CANADA LEASING	2008-Nov-28	08112840737	ZIPF8000S 44" PLOTTER DIGITAL IMAGING SYSTEM S/N AFP00992 RICOH AFICIO C2000 DIGITAL IMAGING SYSTEM S/N M5085700113 RICOH AFICO C2500 DIGITAL SYSTEM S/N L3685101550 RICOH AFICIO C3500 DIGITAL SYSTEM S/N L8986421272 PANASONIC PHONE SYSTEM OFFICE FURNITURE & ACCESSORIES. ALL EQUIPMENT IS SPECIFICALLY LISTED ON CONTRACT NUMBER C091025 TOGETHER WITH ALL ATTACHMENTS, ACCESSORIES, ACCESSIONS, REPLACEMENTS, SUBSTITUTIONS, ADDITIONS, AND IMPROVEMENTS	2013-Nov-28	

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
				THERETO, AND ALL PROCEEDS IN ANY FORM DERIVED DIRECTLY OR INDIRECTLY FROM ANY SALE AND OR DEALINGS WITH THE COLLATERAL OR PROCEEDS OF THE COLLATERAL AND A RIGHT TO ANY INSURANCE PAYMENT OR OTHER PAYMENT THAT INDEMNIFIES OR COMPENSATES FOR LOSS OR DAMAGE TO THE COLLATERAL OR PROCEEDS OF THE COLLATERAL.		
X-TREME ENERGY GROUP INC.	HSBC BANK CANADA	2009-Dec-22	09122221684	LAND CHARGE	INFINITY	
X-TREME ENERGY GROUP INC.	HSBC BANK CANADA	2009-Dec-22	09122221733	ALL PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY OF THE DEBTOR.	2019-Dec-22	
X-TREME ENERGY GROUP INC.	HSBC BANK CANADA	2010-Apr-22	10042223139	THE ENTIRE RIGHT, TITLE, CLAIM AND INTEREST OF THE DEBTOR IN AND TO ALL MONIES WHICH ARE NOW OR WHICH MAY FROM TIME TO TIME IN THE FUTURE STAND TO THE CREDIT OF THE DEBTOR IN ANY ACCOUNT AT THE BRANCH OF THE SECURED PARTY LOCATED AT 407-8TH AVENUE SW, CALGARY, AB, T2P 1E5 AND ALL PROCEEDS INCLUDING, WITHOUT LIMITATION, ALL GOODS, SECURITIES, INSTRUMENTS, DOCUMENTS OF TITLE, CHATTEL PAPER,	2020-Apr-22	

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
				INTANGIBLES AND MONEY (ALL AS DEFINED IN THE PERSONAL PROPERTY SECURITY ACT, ANY REGULATIONS THEREUNDER AND ANY AMENDMENTS THERETO).		
XTREME ENERGY GROUP INC.	JONMAC ELECTRIC	2011-Ju1-04	11070400666	PEMEX RIG #1043	2013-Ju1-04	
XTREME ENERGY GROUP INC.	ATCO STRUCTURES & LOGISTICS LTD.	2011-Dec-22	11122212232	132074383 200710 X 32 SKID OFFICE MOBILE HOME	2012-Dec-22	ALL EQUIPMENT, FIXTURES, FURNISHINGS, COMPONENTS, PARTS, APPURTENANCES, ACCESSORIES, MODULES, AND OTHER GOODS OR EQUIPMENT OF ANY KIND WHICH MAY FROM TIME TO TIME, BE INCORPORATED OR INSTALLED IN OR ATTACHED TO THE ABOVE DESCRIBED MOBILE HOMES. ALL CAMP FACILITIES SUPPLIED BY THE SECURED PARTY TO THE DEBTOR INCLUDING WITHOUT LIMITATION, THE KITCHEN/DINER COMPLEX, THE RECREATION COMPLEX, ALL DORMITORY UNITS, THE SEWAGE TREATMENT THE WATER STORAGE EQUIPMENT, TELEPHONE SYSTEMS, FIRE ALARM SYSTEMS, UTILIDORS AND HEAT TRACING, UNDERGROUND MECHANICAL, T.V. SYSTEMS,

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
						FENCING, PARKING RAILS AND WALKWAYS. PROCEEDS: GOODS, INVENTORY, CHATTEL PAPER, SECURITIES, DOCUMENTS OF TITLE, INSTRUMENTS, MONEY, INTANGIBLES, AND ACCOUNTS (ALL AS DEFINED IN THE PERSONAL PROPERTY SECURITY ACT) AND INSURANCE PROCEED.
XTREME ENERGY GROUP INC.	DELL FINANCIAL SERVICES CANADA LIMITED	2012-Jan-18	12011824639	ALL DELL AND NON DELL COMPUTER EQUIPMENT AND PERIPHERALS WHEREVER LOCATED HERETOFORE OR HEREAFTER LEASED TO DEBTOR BY SECURED PARTY PURSUANT TO AN EQUIPMENT LEASE 200-5345281-001 TOGETHER WITH ALL SUBSTITUTIONS, ADDITIONS, ACCESSIONS AND REPLACEMENTS THERETO AND THEREOF NOW AND HEREAFTER INSTALLED IN, AFFIXED TO, OR USED IN CONJUNCTION WITH SUCH EQUIPMENT AND PROCEEDS THEREOF TOGETHER WITH ALL RENTAL OR INSTALMENT PAYMENTS, INSURANCE PROCEEDS, OTHER PROCEEDS AND PAYMENTS DUE OR TO BECOME DUE AND ARISING FROM OR RELATING TO SUCH EQUIPMENT.	2013-Jan-18	

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
				PROCEEDS: ALL PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY.		
TOUGH ENOUGH DRILLING INC. XTREME ENERGY GROUP INC.	GE CANADA EQUIPMENT FINANCING G.P.	2012-Mar-14	12031413073	2012 X-TREME 350T TOP DRIVE WITH SERIAL NUMBER 48726 CIW HPU UNIT WITH SERIAL NUMBER 1001 2012 DETROIT DIESEL 12V2000 ENGINE WITH SERIAL NUMBER 5352010179 C/W PAC RIM ELSA 8722615001.	2016-Mar-14	THE GOODS DESCRIBED HEREIN, WHEREVER SITUATED, AND ALL PRESENT AND AFTER-ACQUIRED INTELLECTUAL PROPERTY, INTANGIBLES, ATTACHMENTS, ACCESSORIES AND ACCESSIONS THERETO AND SPARE PARTS, REPLACEMENTS, SUBSTITUTIONS, EXCHANGES AND TRADE-INS THEREFOR, AND ALL RIGHTS, RECEIVABLES AND CHATTEL PAPER DERIVED FROM OR EVIDENCING THE LEASE OR RENTAL THEREOF BY THE DEBTOR TO THIRD PARTIES, AND ALL PROCEEDS RELATING THERETO. PROCEEDS: ALL OF THE DEBTOR'S PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY WHICH IS DERIVED DIRECTLY OR INDIRECTLY FROM ANY DEALING WITH OR DISPOSITION OF THE ABOVE-DESCRIBED COLLATERAL, INCLUDING, WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, ALL INSURANCE AND OTHER

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
						PAYMENTS PAYABLE AS INDEMNITY OR COMPENSATION FOR LOSS OR DAMAGE THERETO AND ALL CHATTEL PAPER, DOCUMENTS OF TITLE, GOODS, INSTRUMENTS, INTANGIBLES, MONEY AND SECURITIES.
XTREME ENERGY GROUP INC.	1289200 ALBERTA LTD.	2012-May-11	12051118386	HTMKAZPX7H405296 2007 INTERNATIONAL 4300 4X2 MOTOR VEHICLE	2013-May-11	THE GOODS DESCRIBED HEREIN, WHEREVER SITUATED, AND ALL PRESENT AND AFTER-ACQUIRED INTELLECTUAL PROPERTY, INTANGIBLES, ATTACHMENTS, ACCESSORIES AND ACCESSIONS THERETO AND SPARE PARTS, REPLACEMENTS, SUBSTITUTIONS, EXCHANGES AND TRADE-INS THEREFOR, AND ALL RIGHTS, RECEIVABLES AND CHATTEL PAPER DERIVED FROM OR EVIDENCING THE LEASE OR RENTAL THEREOF BY THE DEBTOR TO THIRD PARTIES, AND ALL PROCEEDS RELATING THERETO. PROCEEDS: ALL OF THE DEBTOR'S PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY WHICH 15 DERIVED DIRECTLY OR INDIRECTLY FROM ANY DEALING WITH OR DISPOSITION OF

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
						THE ABOVE-DESCRIBED COLLATERAL, INCLUDING, WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, ALL INSURANCE AND OTHER PAYMENTS PAYABLE AS INDEMNITY OR COMPENSATION FOR LOSS OR DAMAGE THERETO AND ALL CHATTEL PAPER, DOCUMENTS OF TITLE, GOODS, INSTRUMENTS, INTANGIBLES, MONEY AND SECURITIES.
X-TREME ENERGY GROUP INC.	WORKERS' COMPENSATION BOARD/COLLECTION UNIT	2012-Jul-16	12071621280	ALL PRESENT AND AFTER-ACQUIRED PROPERTY AND ALL PROPERTY USED IN CONNECTION, PURSUANT TO WCB ACT S129	INFINITY	ACCT# 1540915
X-TREME ENERGY GROUP INC.	WORKERS' COMPENSATION BOARD/COLLECTION UNIT	2012-Jul-16	12071621422	ALL PRESENT AND AFTER-ACQUIRED PROPERTY AND ALL PROPERTY USED IN CONNECTION, PURSUANT TO WCB ACT S129	INFINITY	WCB ACCOUNT 5302530
TOUGH ENOUGH DRILLING INC. X-TREME ENERGY GROUP INC.	GE CANADA EQUIPMENT FINANCING G.P.	2012-Sep-21	12092110276	2012 DETROIT DIESEL 12V2000 ENGINE WITH SERIAL NUMBER 5352006512 C/W PAC RIM	2016-Sep-21	THE GOODS DESCRIBED HEREIN, WHEREVER SITUATED, AND ALL PRESENT AND AFTER-ACQUIRED INTELLECTUAL PROPERTY, INTANGIBLES, ATTACHMENTS, ACCESSORIES AND ACCESSIONS THERETO AND SPARE PARTS, REPLACEMENTS,

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
						SUBSTITUTIONS, EXCHANGES AND TRADE-INS THEREFOR, AND ALL RIGHTS, DEBTOR TO THIRD PARTIES, AN DERIVED FROM OR EVIDENCING THE LEASE OR RENTAL THEREOF BY THE DEBTOR TO THIRD PARTIES, AND ALL PROCEEDS RELATING THERETO. PROCEEDS: ALL OF THE DEBTOR'S PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY WHICH IS DERIVED DIRECTLY OR INDIRECTLY FROM ANY DEALING WITH OR DISPOSITION OF THE ABOVE-DESCRIBED COLLATERAL, INCLUDING, WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, ALL INSURANCE AND OTHER PAYMENTS PAYABLE AS INDEMNITY OR COMPENSATION FOR LOSS OR DAMAGE THERETO AND ALL CHATTEL PAPER, DOCUMENTS OF TITLE, GOODS, INSTRUMENTS, INTANGIBLES, MONEY AND SECURITIES. REFERENCE ELSA 8722615001

3. X-treme Bits & Downhole Tooling Ltd. (as of November 23, 2012)

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
X-TREME BITS AND DOWNHOLE TOOLING LTD.	HSBC BANK CANADA	2010-May-21	10052112842	LAND CHARGE	INFINITY	
X-TREME BITS AND DOWNHOLE TOOLING LTD.	HSBC BANK CANADA	2010-May-21	10052112933	ALL OF THE PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY OF THE DEBTOR.	2020-May-21	
X-TREME BITS & DOWNHOLE TOOLING LTD.	HSBC BANK CANADA	2010-Sep-30	10093027916	THE ENTIRE RIGHT, TITLE, CLAIM AND INTEREST OF THE DEBTOR IN AND TO ALL MONIES WHICH ARE NOW OR WHICH MAY FROM TIME TO TIME IN THE FUTURE STAND TO THE CREDIT OF THE DEBTOR IN ANY ACCOUNT AT THE BRANCH OF THE SECURED PARTY LOCATED AT 407 - 8TH AVENUE S.W., CALGARY, AB, T2P 1E5 AND ALL PROCEEDS INCLUDING, WITHOUT LIMITATION, ALL GOODS, SECURITIES, INSTRUMENTS, DOCUMENTS OF TITLE, CHATTEL PAPER, INTANGIBLES AND MONEY (ALL AS DEFINED IN THE PERSONAL PROPERTY SECURITY ACT, ANY REGULATIONS THEREUNDER AND ANY AMENDMENTS THERETO).	2020-Sep-30	

4. X-treme Energy Rentals Ltd. (as of November 23, 2012)

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
X-TREME ENERGY RENTALS LTD.	SISSONS ENTERPRISES CORP. TANKS DIRECT	2010-Feb-09	10020929424	FUEL/OIL STORAGE TANKS, SPILL BOXES AND ALL ACCESSIONS, IMPROVEMENTS OR MODIFICATIONS THERETO, INCLUDING WITHOUT LIMITATION ALL PUMPS, DISPENSING EQUIPMENT, PIPING, NOZZLES, ELECTRICAL SYSTEMS, VALVES, LEASES, CARDLOCK OR KEYLOCK SYSTEMS PROCEEDS: ALL PRESENT AND AFTER ACQUIRED PERSONAL PROPERTY	2020-Feb-09	
X-TREME ENERGY RENTALS LTD.	HSBC BANK CANADA	2010-Jun-07	10060714213	ALL OF THE DEBTOR'S PRESENT AND AFTER-ACQUIRED PERSONAL PROPERTY.	2020-Jun-07	
X-TREME ENERGY RENTALS LTD.	HSBC BANK CANADA	2010-Jun-07	10060714234	LAND CHARGE	INFINITY	
X-TREME ENERGY RENTALS LTD.	HSBC BANK CANADA	2010-Sep-30	10093027948	THE ENTIRE RIGHT, TITLE, CLAIM AND INTEREST OF THE DEBTOR IN AND TO ALL MONIES WHICH ARE NOW OR WHICH MAY FROM TIME TO TIME IN THE FUTURE STAND TO THE CREDIT OF THE DEBTOR IN ANY ACCOUNT AT THE BRANCH OF THE SECURED PARTY LOCATED AT 407 8TH AVE SW, CALGARY, AB, T2P 1E5 AND ALL PROCEEDS INCLUDING, WITHOUT LIMITATION, ALL GOODS, SECURITIES, INSTRUMENTS, DOCUMENTS OF	2020-Sep-30	

DEBTOR(S)	SECURED PARTY	REGISTRATION DATE	REGISTRATION NUMBER	COLLATERAL	EXPIRY DATE	ADDITIONAL INFORMATION
				TITLE, CHATTEL PAPER, INTANGIBLES AND MONEY (ALL AS DEFINED IN THE PERSONAL PROPERTY SECURITY ACT, ANY REGULATIONS THEREUNDER AND ANY AMENDMENTS THERETO).		

SCHEDULE "E"

QUALIFICATIONS AND ASSUMPTIONS

1. **Loan Documents:** With respect to all documents examined by us (including without limitation the Loan Documents), we have assumed that the signatures are genuine, the individuals signing such documents had legal capacity at the time of signing, all documents submitted to us as originals are authentic, and certified, conformed or photocopied copies, or copies transmitted electronically or by facsimile, conform to authentic original documents. We have also assumed that all such documents are complete and that other than the Mortgage and the Assignment of Rents, none of such documents have been amended, superseded, withdrawn, invalidated or cancelled.

2. **Public Records:** We have assumed that the indices and records in all filing systems maintained in all public offices where we have searched or inquired or have caused searches or inquiries to be conducted are accurate and current, and all certificates and information issued or provided pursuant thereto are and remain accurate and complete.

3. **Incorporation.** We have assumed that each party signing the Loan Documents were, at the time of the execution of the Loan Documents duly incorporated, validly existing and in good standing, and that 1627090 presently is duly amalgamated, validly existing and in good standing.

4. **Power and Capacity:** We have assumed that each party signing the Loan Documents had all necessary power and capacity to execute and deliver such documents, as applicable, and perform their respective obligations thereunder.

5. **Authorization:** We have assumed that the execution and delivery of the Loan Documents by each party thereto and the performance by the parties of their respective obligations thereunder have been duly authorized, do not breach any laws and do not violate the terms of any agreements to which each such party is a party. We have also assumed that each party to such documents was not at the time of execution of the Loan Documents and is not bound by any provision in its constating documents or by-laws or by any agreement which would in any way hinder or restrict its powers or the powers of its directors to authorize, execute and deliver the Loan Documents or which would hinder or restrict the applicable party from performing its obligations thereunder.

6. **Requisite Authority:** We have assumed that there are no actions, suits, proceedings or investigations against or affecting any party to the Loan Documents before any governmental authority which purport to affect the legality, validity and enforceability of the Loan Documents and that no authorization, consent or license was required that was not obtained (governmental or otherwise) in connection with the execution and delivery of the Loan Documents and the performance of the obligations thereunder.

7. **Execution and Delivery:** We have assumed that the Loan Documents have been duly executed and delivered by each of the parties thereto.

8. **Conduct of Parties:** We have assumed, notwithstanding the allegations and claim for equitable subordination referenced in the ADT Action, that the conduct of the parties to the Loan Documents has complied with any requirements of good faith and fair dealing and that there has not been any mutual mistake of fact, misunderstanding, fraud, duress or undue influence.

9. **Enforceability:** All opinions which expressly or by necessity relate to enforceability of the Loan Documents are subject to:

(a) applicable bankruptcy, insolvency, winding up, arrangement, liquidation, fraudulent preference and conveyance, debtor protection, reorganization, moratorium, realization laws and other laws and judicial decisions of general application affecting the rights and remedies of creditors generally;

(b) the court's discretion in the future awarding equitable and other remedies, such as specific performance, equitable subordination and injunctive relief, which accordingly may not be available in any particular circumstance;

(c) equitable limitations on and defences against remedies and equitable principles applicable to proceedings at law or in equity, including without limitation the court's power to grant relief from forfeiture, to decline to give effect to provisions accelerating payment of indebtedness and to stay proceedings and execution of judgments;

(d) applicable laws regarding limitations of action;

(e) the court's discretion to decline to hear any action or give effect to an obligation if to do so would be contrary to public policy or if it is not the proper forum to hear such action;

(f) limitations which may be imposed by law or equity on the effectiveness of terms exculpating a party from liability or limiting the liability of a party;

(g) limitations on the right of a creditor to receive immediate payment of amounts stated to be or which may become payable on demand;

(h) limitations on the right of a party to enforce a provision based upon a minor or non-substantive default;

(i) implied obligations requiring good faith, fair-dealing and reasonableness in performance and enforcement of a contract;

(j) rights of indemnity may not be enforceable if they indemnify a party against the party's own negligence or wilful misconduct or the consequences of an unlawful act or penalty, or are against public policy;

(k) the actual receipt by the Loan Parties, or by a third party in accordance with the directions of the Loan Parties, of those sums of money, if any, stipulated in a Loan Document as having been received; and

(l) the following limitations:

  (i) provisions which purport to establish evidentiary standards may not be enforceable or may be limited in application;

  (ii) the *Judgment Interest Act* (Alberta) limits interest on a judgment debt arising under the judgment of an Alberta court to a rate prescribed by regulation from time to time;

  (iii) determinations or demands made in exercise of a discretion may be unenforceable if made in an unreasonable or arbitrary fashion;

  (iv) we express no opinion as to attornment and due on sale provisions as such provisions may be unenforceable;

(v) provisions for recovery of fees and expenses may be restricted by a court to a reasonable amount and legal fees are subject to taxation;

(vi) those provisions in the Loan Documents which provide for a higher rate of interest in respect of any amount in default than would otherwise be payable in respect of such amount or which provide for payment of an amount due to a default or breach as damages which are not a genuine pre-estimate of losses may not be legal, valid, binding or enforceable;

(vii) provisions purporting to allow severance of or restrict the effect of a provision may not be enforceable if such severance or restriction would not accord with public policy or if the severance or restriction would substantially alter the scope or intention of the agreement;

(viii) no opinion is expressed on enforceability of any provision purporting to exclude unwritten variations, amendments, waivers or consents;

(ix) provisions which provide that delay or failure by a party to exercise any right, remedy or option will not operate as a waiver thereof may not be enforceable;

(x) no opinion is expressed on enforceability of any provision in the Loan Documents which purports to constitute a receiver or receiver and manager as the agent of the Loan Parties or to absolve a receiver or a receiver and manager of responsibility for its acts or consent to or ratify future actions by or on behalf of a receiver or receiver manager;

(xi) no opinion is expressed herein as to the validity or enforceability of the security constituted by the Loan Documents against any right, contract, document, lease, agreement, debt, claim or demand which by its terms or pursuant to law is not assignable or is assignable only upon the fulfilment of certain requirements. Without limiting the generality of the foregoing, no opinion is expressed on enforceability of an assignment of:

(1) an existing or future debt due or becoming due from; or

(2) a chose in action in respect of which there is a right of recovery enforceable by action against,

either the Crown in right of Alberta or Canada or a "Provincial Corporation" (as defined in the Financial Administration Act (Alberta));

(xii) remedies exercisable upon default in the Loan Documents must be exercised in good faith and a commercially reasonable manner;

(xiii) the duties and obligations imposed upon lenders and their agents pursuant to sections 16 and 66 of the PPSA;

(xiv) no opinion is expressed on enforceability of provisions purporting to waive offsets, counterclaims or defences;

(xv) we express no opinion as to the waiver of certain rights by the Loan Parties in the Loan Documents with respect to its right to recover insurance proceeds or as to the application of such proceeds; and

(xvi) we express no opinion as to the consequence of the interest rate stipulated in the Loan Documents at any time exceeding the criminal interest pursuant to the *Criminal Code* (Canada).

10. **Priority:** It is our opinion that the Security Documents of the Lender ranks in priority to all other creditor claims as against XEG assets generally subject to certain specific registrations as set out in Schedule "B".

11. **Personal Property Security:**

(a) The validity, perfection and effect of perfection or non-perfection of the security interests created by the Security Documents:

(i) in respect of goods and a possessory security interest in chattel paper, a security, a negotiable document of title, an instrument or money, are, except:

(1) as provided in subparagraph 11(a)(ii) below; and

(2) as to goods which the parties to the security agreement understand are to be kept in another jurisdiction and which are removed to the other jurisdiction within 30 days of the security interest attaching,

governed by the laws of the jurisdiction where such personal property is situate at the time of attachment;

(ii) in respect of:

(1) intangibles;

(2) goods of a type normally used in more than one jurisdiction (if such goods are classified as equipment or inventory leased or held for lease to others); and

(3) non-possessory security interests in chattel paper, securities, negotiable documents of title, instruments or money,

are governed by the laws of the jurisdiction in which the debtor is "located" for the purposes of the PPSA at the time the security interest attaches;

(iii) in respect of investment property is governed by the law, at the time the security interests attach:

(1) of the jurisdiction where the certificate is located if the collateral is a certificated security,

(2) of the issuer's jurisdiction if the collateral is an uncertificated security,

(3) of the securities intermediary's jurisdiction if the collateral is a security entitlement or a securities account, or

(4) of the futures intermediary's jurisdiction if the collateral is a futures contract or a futures account.

(b) except for perfection by registration of the security interests created by the Security Documents in investment property (which is governed by the laws of the jurisdiction where the debtor is located for the purposes of the PPSA), perfection, the effect of perfection or non-perfection and the priority of the security interest created by the Security Documents in investment property is governed by the law:

(i) of the jurisdiction where the certificate is located if the collateral is a certificated security,

(ii) of the issuer's jurisdiction if the collateral is an uncertificated security,

(iii) of the securities intermediary's jurisdiction if the collateral is a security entitlement or a securities account, or

(iv) of the futures intermediary's jurisdiction if the collateral is a futures contract or a futures account.

(c) Perfection of security interests under the Security Documents may not be effective in respect of proceeds (as defined in the PPSA) which are required by the PPSA to contain a serial number description on the financing statement.

(d) No opinion is expressed with respect to the registration or perfection of security interests in any personal property which cannot be perfected by the filing of a financing statement under the PPSA, nor with respect to the validity, registration or perfection of security interests in personal property governed by statutes or laws other than the PPSA, such as (without limitation) ships, copyright, trade marks, patents, industrial designs and other forms of intellectual property, contracts of annuity or policies of insurance (except rights to money or other value payable thereunder as indemnity or compensation for loss of or damage to collateral).

(e) We have assumed none of the parties have agreed to postpone the attachment of any security interests.

(f) A security interest in proceeds is only perfected to the extent proceeds are identifiable and traceable.

(g) No opinion is expressed with respect to any registrations that may be necessary regarding any personal property that is now or which may hereafter be a fixture.

12. **Search Limits and Defects:** Findings which depend on or relate to searches of public registries and offices of record are effective only to the effective times listed in Schedule "B" and are qualified with respect to errors or omissions in the records of or search results provided by such registries and offices. The searches conducted will not reveal:

(a) interests that may have been granted by predecessors or successors in title to the Loan Parties personal property or any part thereof; and

(b) interests in respect of the personal property or any part thereof which are not, or not required to be, registered in the Province of Alberta.

13. **Alberta Law:** All findings herein are limited to the laws of the Province of Alberta and the applicable federal laws of Canada, in each case as in force on the date hereof.

14. **Legal Effect:** Whenever an obligation, act, agreement or instrument is expressed to be "legal, valid and binding" or "enforceable" or words of like effect, we mean that such obligation, act, agreement or instrument is capable of being given legal effect. We express no opinion as to any factors such as financial capacity or title to assets which may make such obligation, act, agreement or instrument unenforceable in fact.

SCHEDULE "F"

ENCUMBRANCES

1. Easement 1005PC registered November 15, 1966
2. Easement 6783UG registered December 17, 1973
3. Caveat 922 091 831 registered April 7, 1992
4. Utility Right of Way 042 028 223 registered January 19, 2004
5. Utility Right of Way 042 028 224 registered January 19, 2004
6. Caveat re: Right of Way Agreement, Etc. 042 072 363 registered February 19, 2004
7. Utility Right of Way 042 083 606 registered February 26, 2004
8. Change of Name re: FortisAlberta Inc. 042 504 115 registered November 18, 2004
9. Utility Right of Way 792 168 155 registered July 18, 1979
10. Utility Right of Way 852 097 637 registered May 15, 1985