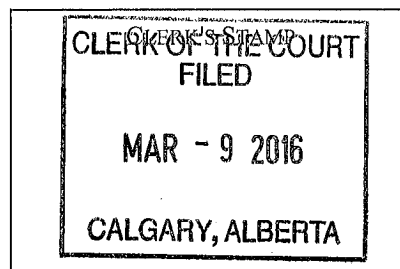


FORM 49
[RULE 13.19]



COURT FILE NUMBER 1601 - 03113
COURT COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE CALGARY

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

**AND IN THE MATTER OF THE COMPROMISE
OR ARRANGEMENT OF QUICKSILVER
RESOURCES CANADA INC., 0942065 B.C. LTD.
and 0942069 B.C. LTD.**

DOCUMENT **AFFIDAVIT**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT
BENNETT JONES LLP
Barristers and Solicitors
4500, 855 - 2nd Street S.W.
Calgary, Alberta T2P 4K7

Attention: Chris Simard / Kevin Zych
Tel No.: 403-298-4485 / 416-777-5738
Fax No.: 403-265-7219 / 416-863-1716

AFFIDAVIT OF J. DAVID RUSHFORD

Sworn on March 8, 2016

I, J. David Rushford, of the City of Calgary, in the Province of Alberta, SWEAR AND SAY THAT:

1. I am the Senior Vice President and Chief Operating Officer of each of Quicksilver Resources Canada Inc. ("**Quicksilver Canada**" or "**QRCI**"), 0942065 B.C. Ltd. ("**LNG Co**") and 0942069 B.C. Ltd. ("**LNG SubCo**"), and together with Quicksilver Canada and LNG Co, the "**Applicants**") and I am also a director of each of the Applicants. As such I

FORM 49
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CLERK'S STAMP

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have personal knowledge of the matters hereinafter deposed to, save where stated to be based on information and belief, in which case I verily believe the same to be true.

2. All references to dollar amounts contained herein are to Canadian Dollars unless otherwise stated.

I. RELIEF REQUESTED

3. This Affidavit is made in support of an Application by the Applicants for an Order (the "**Initial Order**") pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "**CCAA**"), among other things:

- (a) declaring that the Applicants are companies to which the CCAA applies;
- (b) staying all proceedings and remedies taken or that might be taken in respect of the Applicants or any of their property, except as otherwise set forth in the Initial Order or otherwise permitted by law, including staying any remedies to attempt to remove Quicksilver Canada as the operator of joint venture assets;
- (c) authorizing the Applicants to carry on business in a manner consistent with the preservation of their property and business;
- (d) appointing FTI Consulting Canada Inc. as Monitor (the "**Monitor**") of the Applicants in these proceedings;
- (e) granting the Administration Charge (defined below), the Directors' Charge (defined below), the KERP Charge (as defined below) and the LNG Co Interim Lenders' Charge (as defined below);
- (f) approving Quicksilver Canada's Key Employee Retention Plan ("**KERP**"), as described herein;
- (g) authorizing Quicksilver Canada to, with the consent of the Monitor, pay for goods and services supplied to Quicksilver Canada by certain Critical Suppliers (as defined below) prior to the date of the Initial Order;

- (h) authorizing the Applicants to pay interest and other costs which may become due and owing under the terms of Credit Facility (as defined below), including the costs of the Agents' legal counsel and other consultants and advisors (collectively, the "**Agent's Advisors**") engaged for these proceedings.
- (i) approving the engagement letter entered into between Houlihan Lokey Capital, Inc. (the "**Financial Advisor**" or "**Houlihan**") and Quicksilver Canada effective September 14, 2015 (the "**Financial Advisor Engagement Letter**");
- (j) approving the services agreement entered into between Quicksilver Canada and QRI effective March 4, 2016 (the "**Services Agreement**");
- (k) authorizing Quicksilver Canada to advance funds to LNG Co by way of an interim lending arrangement;
- (l) sealing on the Court file the Westcoast Agreement (defined below), certain agreements related to the KKR Transaction (defined below), the Confidential KERP Documents (defined below); and
- (m) deeming service of the Application for the Initial Order to be good and sufficient.

II. BACKGROUND

A. Quicksilver Group

- 4. An organization chart of the Applicants and their Canadian and U.S. affiliates (collectively, the "**Quicksilver Group**") is attached as **Exhibit "1"** to this my Affidavit. For clarity, Quicksilver Canada, LNG Co and LNG SubCo are the only Applicants in these proceedings.
- 5. Quicksilver Canada is a wholly-owned subsidiary of Quicksilver Resources Inc. ("**QRI**"), the ultimate parent company of the Quicksilver Group. The Quicksilver Group has operations in both the United States and Canada.

6. LNG Co is a wholly-owned subsidiary of Quicksilver Canada, and LNG SubCo is a wholly-owned subsidiary of LNG Co.
7. QRI, which is not an applicant in these proceedings, is a public company whose common shares were traded on the New York Stock Exchange under the ticker symbol "KWK" until January, 2015. QRI's common shares then traded on the OTC market under the ticker symbol "KWKA" until March 17, 2015. The shares of QRI have traded on the OTC pink market under the symbol "KWKAQ" since that date.
8. On March 17, 2015, QRI and thirteen (13) of its direct and indirect subsidiaries in the Quicksilver Group (collectively, the "**Chapter 11 Debtors**"¹) filed for voluntary relief under chapter 11 of title 11 of the United States Code, 11 U.S.C. §§ 101-1532 in the United States Bankruptcy Court for the District of Delaware (the "**U.S. Court**"). Quicksilver Canada, and its direct and indirect subsidiaries (collectively with Quicksilver Canada, the "**Quicksilver Canada Group**", which includes LNG Co and LNG SubCo) are not included in the Chapter 11 filing, and the Applicants have no present intention to seek recognition of these proceedings in the United States or elsewhere. Quicksilver Canada has two subsidiaries, Makarios Midstream Inc. and 1622834 Alberta Ltd., that are not Applicants in these proceedings.

B. Quicksilver Canada

9. Quicksilver Canada is a corporation amalgamated under the *Business Corporations Act*, R.S.A. 2000, c.B-9, as amended on January 1, 2009 (the "**ABCA**"). A copy of Quicksilver Canada's certificate and articles of amalgamation are attached as **Exhibit "2"** to this my Affidavit.
10. Quicksilver Canada's principal executive office is located at 2000, 125 – 9th Avenue, S.E., Calgary, Alberta T2G 0P6. Its registered office is located at 4500, 855 – 2nd Street S.W., Calgary, Alberta T2P 4K7.

¹ The Chapter 11 Debtors are: Quicksilver Resources Inc. (QRI), Barnett Shale Operating LLC, Cowtown Drilling, Inc., Cowtown Gas Processing L.P., Cowtown Pipeline Funding, Inc., Cowtown Pipeline L.P., Cowtown Pipeline Management, Inc., Makarios Resources International Holdings LLC, Makarios Resources International Inc., QPP Holdings LLC, QPP Parent LLC, Quicksilver Production Partners GP LLC, Quicksilver Production Partners LP, and Silver Stream Pipeline Company LLC.

11. Quicksilver Canada (including its predecessor companies) and its joint venture partners were the first commercial producers of coalbed methane in Canada. Quicksilver Canada continues to explore for and develop unconventional gas resources in Alberta and British Columbia.

C. LNG Co

12. LNG Co is a corporation incorporated under the *Business Corporations Act*, SBC 2002, c. 57, as amended on June 1, 2012 (the "BCBCA"). A copy of LNG Co's certificate of incorporation is attached as **Exhibit "3"** to this my Affidavit.
13. LNG Co's principal executive office is located at 2000, 125 – 9th Avenue, S.E., Calgary, Alberta T2G 0P6. Its registered office is located at 2200, 1055 West Hastings Street, Vancouver, BC V6E 2E9.
14. In May 2013, LNG Co purchased a former paper mill site located in Campbell River, British Columbia with the intent to begin feasibility studies to develop, build and operate natural gas liquefaction, storage and on-loading facilities, called "Discovery LNG".
15. LNG Co is the beneficial owner of the lands and rights of way relating to Discovery LNG, and it also directly holds the contracts, permits, licenses and leases (including water lot leases) related to Discovery LNG.

D. LNG SubCo

16. LNG SubCo is a corporation incorporated under the BCBCA. A copy of LNG SubCo's certificate of incorporation is attached as **Exhibit "4"** to this my Affidavit.
17. LNG SubCo's principal executive office is located at 2000, 125 – 9th Avenue, S.E., Calgary, Alberta T2G 0P6. Its registered office is located at 2200, 1055 West Hastings Street, Vancouver, BC V6E 2E9.
18. LNG SubCo holds the lands and three associated rights of way relating to Discovery LNG as bare trustee for its parent company, LNG Co, the beneficial owner of such lands and rights of way.

E. Directors and Officers

19. The executive officers of Quicksilver Canada are:
 - (a) Glenn Darden - President and Chief Executive Officer;
 - (b) J. David Rushford - Senior Vice President and Chief Operating Officer;
 - (c) Robert W. McGregor – Vice President, Finance
 - (d) David Haugen – Vice President, Engineering;
 - (e) Tony Kuehne – Vice President, Marketing and Business Development; and
 - (f) Levonne L. Louie – Vice President, Land.
20. The executive officers of each of LNG Co and LNG SubCo are Mr. Darden, Mr. Rushford, Mr. Kuehne and Mr. McGregor.
21. The board of directors of each of the Applicants is comprised of two directors, being myself and Mr. Darden. Mr. Darden is also a director of QRI, and all other members of the Quicksilver Group for which there are directors. Mr. Darden is also an officer of QRI and all other members of the Quicksilver Group for which there are officers.

F. Employees

22. Quicksilver Canada currently has 75 employees, all of whom are employed in Canada. Neither LNG Co nor BC SubCo has any employees.
23. Quicksilver Canada does not offer a pension plan to any of its employees, but it does match its employees' contributions to their registered retirement savings plans up to certain maximum amounts. Quicksilver Canada's monthly expense in respect of such contributions equals approximately \$35,000, and all such amounts have been paid current.

III. BUSINESS OF THE APPLICANTS

A. Quicksilver Canada

24. Quicksilver Canada is an independent gas exploration, development, and production company with operations exclusively in Canada. All reserves, producing properties and exploration prospects of the Quicksilver Canada Group are located in Alberta and British Columbia.
25. As of December 31, 2015, Quicksilver Canada had approximately:
- (a) 150 billion standard cubic feet ("**MMcf**") of estimated net proved reserves (determined in accordance with the requirements of the U.S. Securities and Exchange Commission), of which substantially all were gas and approximately 99% were classified as producing; and
 - (b) 662,962 million gross (465,026 million net) acres of land.

(i) Principal Properties and Certain Key Agreements

Horn River

26. As of December 31, 2014, Quicksilver Canada held approximately 126,500 net acres in the Horn River basin of northeast British Columbia, of which virtually all is leased for 10-year terms (the "**Horn River Asset**"). Proved resources in the Horn River Asset at that date were 66.5 billion cubic feet of natural gas equivalents ("**Bcfe**"). There is approximately 13 trillion cubic feet ("**Tcf**") of total resource potential. Average net production was 32 MMcf per day in 2014 from the Horn River Asset.
27. All of Quicksilver Canada's surface and mineral rights in the Horn River Asset are pursuant to agreements with the B.C. Crown and various municipalities.
28. In 2012, Quicksilver Canada drilled an eight-well pad in the Horn River Asset and those eight wells have been the Quicksilver Group's highest producing wells to date. The Quicksilver Group believes that the Horn River Asset contains the most prolific wells in

its portfolio, however continued capital development will require substantial amounts of capital. In total, Quicksilver Canada has 19 wells associated with the Horn River Asset.

29. Quicksilver Canada generates significant negative cash flow in respect of the Horn River Asset, primarily as a result of the precipitous decline in natural gas prices over the past few years, which resulted in certain of Quicksilver Canada's obligations becoming financially onerous and uneconomic, as described below. Because of these factors, the Horn River Asset is currently not producing and all wells are shut-in.

(A) KKR Agreements

30. In December 2011, the Quicksilver Canada Group entered into various agreements among themselves and with 0927530 B.C. Unlimited Liability Company ("**KKR Newco**"), a subsidiary of Kohlberg Kravis Roberts & Co. L.P. ("**KKR**"), as described below (collectively, the "**KKR Transaction**").
31. As part of the KKR Transaction, the Maxhamish Pipeline and the Fortune Creek compressor assets were transferred by Quicksilver Canada to a newly-formed partnership named the Fortune Creek Gathering and Processing Partnership (the "**Partnership**"). Initially, KKR Newco contributed \$125 million and Quicksilver Canada contributed the Maxhamish Pipeline and the compressor assets to the Partnership, respectively, each in exchange for a 50% partnership interest pursuant to a Contribution Agreement dated December 23, 2011 among Quicksilver Canada, the Partnership and KKR Newco. Quicksilver Canada also received a cash payment from the Partnership in an amount equal to approximately \$112 million (being the \$125 million contribution by KKR Newco, less certain amounts required to complete work on the Maxhamish Pipeline and the compressor assets). A copy of the Contribution Agreement is now shown to me and marked as **Exhibit "5"** to this my Affidavit.
32. On December 23, 2011, Quicksilver Canada transferred its 50% partnership interest and \$3 million in cash to Makarios Midstream Inc. ("**MMI**"), a wholly-owned subsidiary of Quicksilver Canada, in exchange for 1,000 shares in the capital of MMI. However, Quicksilver Canada remained bound by the Contribution Agreement and the Gathering

Agreement. The partners of the Partnership are now MMI and KKR Newco. MMI has no business assets other than its 50% interest in the Partnership and a small amount of cash (\$26,000).

33. Pursuant to the Contribution Agreement, Quicksilver Canada agreed, among other things:
 - (a) subject to a limited deferral rate, to spend the cumulative sum of \$300 million on drilling in the area over the three (3) years starting in 2012;
 - (b) to repurchase certain compression assets from the Partnership on either January 1, 2016 or May 1, 2018 for a purchase price of \$33 million; and
 - (c) to enter into a take-or-pay Gathering Agreement with the Partnership.
34. The Gathering Agreement dated December 23, 2011 that was entered into by Quicksilver Canada and the Partnership is now shown to me and marked as **Exhibit "6"** to this my Affidavit.
35. Pursuant to the Gathering Agreement, Quicksilver Canada has an obligation to pay a monthly fee to the Partnership comprised of the following:
 - (a) a transportation fee based on (raw gas) amounts actually shipped, made up of (i) a fixed capital component, and (ii) an operating component to be determined based on the annual operating cost for the Maxhamish Pipeline divided by the annual throughput for the Maxhamish Pipeline; and
 - (b) during the first ten (10) years of the term of the Gathering Agreement, a take-or-pay component based on the amount, if any, by which the total revenue from transportation fees from all shippers on the Maxhamish Pipeline (including Quicksilver Canada, which is currently the only shipper on the Maxhamish Pipeline) for a given month falls below the revenue requirement for such month. The total amount that would be payable to the Partnership in respect of the take-or-pay fee from the beginning of 2014 until the end of the initial term in 2021 is currently estimated by Quicksilver Canada to be approximately \$142 million.

36. Although Quicksilver Canada's take-or-pay obligation under the Gathering Agreement is owed to the Partnership (a 50% interest of which is owned by MMI, as described above), the Quicksilver Canada Group does not receive 50% of the take-or-pay payments made by Quicksilver Canada to the Partnership. The Partnership Agreement provides, among other things, that any Available Cash Flow (as defined in the Partnership Agreement) of the Partnership for a fiscal quarter will be first paid to KKR Newco provided that there are any Unrecovered Balances in respect of any Capital Pool (each as defined in the Partnership Agreement). Currently, the remaining Unrecovered Balance in respect of the Maxhamish Pipeline Capital Pool was \$105,697,793. Accordingly, there is no expectation that any Available Cash Flow will flow from the Partnership to MMI or to the Quicksilver Canada Group in the near term.
37. MMI and the Partnership are parties to an Operating Agreement dated December 23, 2011, a copy of which is now shown to me and marked as **Exhibit "7"** to this my Affidavit. Pursuant to the Operating Agreement, MMI was engaged by the Partnership to operate and maintain all of the assets of the Partnership, and assumed responsibility for the performance of the Partnership's obligations as operator under the Gathering Agreement. The Partnership agreed to reimburse MMI for expenses incurred in providing such services.
38. In turn, Quicksilver Canada and MMI entered into a Services Agreement dated December 23, 2011, a copy of which is now shown to me and marked as **Exhibit "8"** to this my Affidavit. Pursuant to the Services Agreement, Quicksilver Canada agreed to provide certain services to MMI to allow MMI to fulfill its obligations under the Operating Agreement. MMI agreed to pay Quicksilver Canada a monthly fee for each service provided, based on the fully-loaded direct cost of such service plus 5%.
39. All resources in the Horn River Asset are owned by Quicksilver Canada (as opposed to any other entity in the Quicksilver Canada Group, the Partnership, KKR Newco or KKR). The Maxhamish Pipeline and certain compression assets are owned by the Partnership.
40. Other material agreements related to the KKR Transaction are:

- (a) the December 23, 2011 Partnership Agreement entered into between Quicksilver Canada (subsequently assigned to MMI as described above) and KKR Newco, which is now shown to me and marked as **Exhibit "9"** to this my Affidavit;
 - (b) the December 23, 2011 Gas Processing Agreement entered into between Quicksilver Canada and the Partnership, which is now shown to me and marked as **Exhibit "10"** to this my Affidavit;
 - (c) the December 23, 2011 Guaranty granted by QRI to the Partnership, which is now shown to me and marked as **Exhibit "11"** to this my Affidavit; and
 - (d) the March 13, 2014 First Amending Agreement entered into between Quicksilver Canada, the Partnership, KKR Newco, MMI and QRI, which is now shown to me and marked as **Exhibit "12"** to this my Affidavit.
41. Given the extended depressed natural gas price environment, Quicksilver Canada's obligations under the KKR agreements have proven to be extremely financially onerous and the arrangements are not economically viable in the current circumstances or the foreseeable future. As described in greater detail below, the agreements were entered into at a time when Quicksilver Canada expected to be able to grow and scale its business such that its obligations under the agreements would have proven to be commercially reasonable. However, for the reasons described herein, that was not possible. The Maxhamish Pipeline only ever achieved a throughput of approximately 100 MMcfd raw gas out of a nominal rated capacity of 400 MMcfd. The throughput in this pipeline subsequently dropped to 40 MMcfd, as no additional development was conducted.
42. QRCI did not make an approximately \$1.6 million payment due to the Partnership at the end of June 2015 and has not made subsequent monthly payments of the same amount pursuant to the Gathering Agreement. As a result, among other things, the following rights accrued or will accrue to the Partnership: (i) the Partnership may discontinue transporting Quicksilver Canada's gas until all amounts owing are repaid (although, production was previously shut-in on March 8, 2015 due to the termination of a third-party gathering and processing agreement); (ii) if the non-payment continues for more

than 90 days after a written demand therefor, subject to certain existing contracts for the sale of gas, the Partnership may enforce the lien granted by Quicksilver Canada to the Partnership on the natural gas belonging to Quicksilver Canada while it is in the Maxhamish Pipeline and in the Partnership's possession; (iii) the Partnership has certain set-off rights against Quicksilver Canada; (iv) if the non-payment continues for the greater of 180 days and 60 days following a written notice by the other partner, Quicksilver Canada is not entitled to receive partnership distributions or vote with respect to partnership matters until the non-payment is cured and the Partnership may be dissolved or Quicksilver Canada's interest in the Partnership may be purchased by the other partner; and (v) the Operating Agreement could be terminated by the Partnership.

43. As at the date hereof, neither KKR, KKR Newco or the Partnership has sent Quicksilver Canada any written notices regarding the past due amounts, which amounts bear interest compounded monthly at prime plus 2%.
44. A number of the agreements relating to the KKR Transaction have provisions requiring the parties thereto to keep the agreements and the terms thereof confidential, and accordingly the Applicants are asking that all the agreements related to the KKR Transaction (contained in Exhibits "5" – "12" of this Affidavit) be sealed on the Court file.

(B) Westcoast Agreement

45. Until March, 2015, Quicksilver Canada received field gathering and treatment services from Westcoast Energy Inc. ("**Westcoast**" or "**Spectra**") pursuant to an Agreement for New Raw Gas Transmission and Treatment Services dated February 27, 2009 between Quicksilver Canada and Westcoast, doing business as Spectra Energy Transmission (the "**Westcoast Agreement**"). A copy of the Westcoast Agreement, including the Westcoast General Term and Conditions and Westcoast's Toll Schedules for Raw Gas Transmission and Treatment Services, is now shown to me and marked as **Exhibit "13"** to this my Affidavit. The Westcoast Agreement has a provision requiring the parties thereto to keep the agreement and the terms thereof confidential, and accordingly the Applicants are asking that the Westcoast Agreement be sealed on the Court file.

46. Pursuant to the Westcoast Agreement, Spectra provided firm transmission and treatment services to Quicksilver Canada based on specified volumes on a take-or-pay basis. Quicksilver Canada was obligated to pay a monthly fixed price fee which is payable regardless of the volumes Quicksilver Canada actually delivered to Spectra for transmission and treatment, which have been substantially lower than the volumes contemplated by the take-or-pay obligation.
47. A letter of credit in the amount of \$33 million was issued to Spectra, which amount was based on a 12- month rolling average receivables calculation.
48. Given the factors described above, Quicksilver Canada's obligations under the Westcoast Agreement were financially onerous and uneconomic. On February 27, 2015, Quicksilver Canada did not make a payment to Spectra that was due under the Westcoast Agreement.
49. On March 2, 2015, Spectra sent a letter to Quicksilver Canada advising of the remedies that Spectra might exercise pursuant to the non-payment. A copy of that letter is attached as **Exhibit "14"** to this my Affidavit.
50. On March 4, 2015, Spectra sent a letter to Quicksilver Canada advising that Spectra would suspend service under the Westcoast Agreement on March 8, 2015, if the non-payment was not remedied. A copy of that letter is attached as **Exhibit "15"** to this my Affidavit.
51. On March 9, 2015, Spectra sent a letter to Quicksilver Canada advising that Spectra would terminate the Westcoast Agreement on March 19, 2015, if the non-payment was not remedied. A copy of that letter is attached as **Exhibit "16"** to this my Affidavit.
52. On or about March 19, 2015, Spectra terminated the Westcoast Agreement and drew down the full face amount of the \$33 million letter of credit. Quicksilver Canada did not and does not believe that Spectra was legally entitled to draw down the entire amount of the letter of credit and it has reserved all of its rights, entitlements and remedies in that regard. Quicksilver Canada will consider addressing the improper draw down of the letter of credit in these proceedings. Attached as **Exhibits "17"** and **"18"** to this Affidavit are

copies of correspondence exchanged between Quicksilver Canada's counsel and Spectra's counsel on March 19, 2015 with respect to the termination, draw on the letter of credit and associated issues.

53. Depending on whether or not Spectra was entitled to fully draw the letter of credit, the potential claim of Spectra against Quicksilver Canada, based on the aggregate fixed charges aggregate under the Westcoast Agreement, may be as high as \$136 million.

Horseshoe Canyon

54. Quicksilver Canada has operations in central Alberta primarily focused on a coalbed methane development from the Horseshoe Canyon, a shallow formation between 200 and 1,000 meters deep.
55. As of December 31, 2015, Quicksilver Canada held approximately 338,523 net acres in the Horseshoe Canyon in Alberta (the "**Horseshoe Canyon Asset**"). Proved resources in the Horseshoe Canyon Asset at that date were 150 Bcfe, of which substantially all was natural gas. There is approximately 270 Bcfe of resource potential. Average net production was 42.5 MMcf per day in the first quarter of 2016 from the Horseshoe Canyon Asset.
56. Horseshoe Canyon is one of the lowest cost, unconventional gas resource plays in North America. It is also the most studied and technologically advanced coalbed methane play. Most of the wells Quicksilver Canada has in the area are vertically drilled.
57. The Horseshoe Canyon Asset has over 2,900 gross (1,400 net) producing wells.
58. Quicksilver Canada's surface and mineral rights in the Horseshoe Canyon Asset are held pursuant to agreements with freehold owners, the Alberta Crown and various municipalities.
59. The Horseshoe Canyon Asset is the largest dry coal bed methane play in North America and it is generally considered one of the most successful coal bed methane gas plays in the Western Canadian Sedimentary Basin.

60. Quicksilver Canada generates positive cash flow from the Horseshoe Canyon Asset.

Northwest Alberta Shale Assets

61. Quicksilver Canada also owns shale-oil exploration acreage in northwest Alberta of approximately 32,800 net acres, of which Quicksilver Canada has a 100% working interest (the "**Shale Assets**"). The land is encumbered only by Alberta Crown royalties and the security granted to the Agent in connection with the Credit Facility (all as defined below).
62. The reserve mix of the Shale Assets are estimated to be split 30% and 70% between gas and liquids.
63. The acreage is held under license with the earliest expiration in the third quarter of 2016, and Quicksilver Canada must drill 1 vertical and 3 horizontal wells to validate licenses to continue them as 5-year leases.
64. All of Quicksilver Canada's surface and mineral rights with respect to the Shale Asset are pursuant to agreements with the Alberta Crown.
65. Quicksilver Canada incurs only minimal expenses in respect of the Shale Assets.

B. LNG Co and LNG SubCo

Discovery LNG

66. As referred to above, in May 2013, LNG Co purchased a former paper mill site located in Campbell River, British Columbia with the intent to begin feasibility studies to develop, build and operate natural gas liquefaction, storage and on-loading facilities, called Discovery LNG. LNG SubCo holds the lands and three associated rights of way as bare trustee for LNG Co, the beneficial owner of such lands and rights of way. In addition to being the beneficial owner of the lands and rights of way, LNG Co directly holds the contracts, permits, licenses and leases related to Discovery LNG.
67. The 1,200 acre Discovery LNG site, which was formerly occupied by a subsidiary of Catalyst Paper Corporation, is classified as a brownfield redevelopment site and zoned as heavy industrial land with deep-water access.
68. Quicksilver Canada's intention was for the potential project to undergo a feasibility study and once complete, and upon regulatory approval, to construct a facility that would convert produced natural gas primarily from British Columbia into LNG for export to Pacific Rim markets in Asia. Discovery LNG is expected to provide the facilities for liquefying natural gas, LNG storage and carrier on-loading facilities. The Horn River Basin Asset and Discovery LNG were being marketed in Asia as a fully-integrated upstream and downstream resource and liquefaction project.
69. The Quicksilver Canada Group believes the site is an attractive option for redevelopment as an LNG export facility. On June 30, 2015, Quicksilver Canada received a 25-year, 20-Mtpa LNG export license, which is subject to approval of the Governor in Council. A copy of the June 30 letter decision from the National Energy Board is attached as **Exhibit "19"** to this my Affidavit
70. There are, however, environmental issues associated with Discovery LNG arising from the site's prior use, and both Quicksilver Canada and LNG Co provided comprehensive environmental indemnities in favor of Catalyst Paper in connection with the purchase of the property.

71. LNG Co has conducted a full Phase 2 environmental site assessment to reclassify the site as a low-risk industrial site which will allow for a future project description to be filed with the BC Environmental Assessment office, to redevelop the site for LNG.
72. As described in greater detail below, the Discovery LNG property (and therefore LNG Co and LNG SubCo) does not generate any revenue (as it is in the planning stage) and is reliant upon advances from Quicksilver Canada for funding. As LNG Co and LNG Subco have no employees, Quicksilver Canada employees perform services for LNG Co and LNG Subco.

C. Bank Accounts and Cash Management

73. The Applicants' primary bank is Bank of Nova Scotia, at which they maintain Canadian dollar and U.S. dollar accounts.
74. Quicksilver Canada manages a centralized cash management system for all of the entities in the Quicksilver Canada Group (including LNG Co and LNG SubCo), whereby Quicksilver Canada lends cash on an unsecured inter-company basis to its subsidiaries as needed. As at the date hereof, LNG Co owes Quicksilver Canada \$5 million. LNG SubCo does not owe Quicksilver Canada anything.
75. It is anticipated that the Applicants will continue to use the existing cash management system and will continue to maintain the bank accounts and arrangements already in place during the CCAA proceedings. This approach will minimize any disruption to business operations as the Applicants seek to restructure. The cash management system includes the necessary accounting controls to enable the Applicants, as well as their creditors, the Monitor and this Honourable Court, to trace funds through the system and ensure that all transactions are adequately documented and readily ascertainable.
76. During the CCAA proceedings, Quicksilver Canada intends to continue to lend cash to LNG Co and LNG SubCo as needed to fund expenses related to Discovery LNG. Such amounts, which are included in the cash flow referred to below, are expected to be approximately \$1.5 million annually, with property taxes of approximately \$400,000 and the water lot leases of approximately \$150,000 being the two largest components, and

continuing to run the landfills that are located at the site being another significant component.

77. Quicksilver Canada believes that continuing to lend cash to LNG Co to pay such expenses is in the best interest of Quicksilver Canada and its creditors in order to preserve the value of Discovery LNG, an asset of a wholly-owned subsidiary of Quicksilver Canada. Discovery LNG also has the potential to be leveraged into a fully integrated upstream/downstream LNG investment opportunity to monetize the Horn River Asset.
78. Quicksilver Canada is proposing, as described in detail below, that post-filing advances to LNG Co and LNG SubCo be secured by way of a Court-ordered charge (the LNG Interim Lenders' Charge, as defined below). As set out in the cashflow forecast, it is anticipated that approximately \$260,000 would need to be advanced by Quicksilver Canada to LNG Co and LNG SubCo in the first 13 weeks of this proceeding.

D. Intercompany Services

79. As a wholly-owned subsidiary of QRI, Quicksilver Canada has traditionally had certain corporate services provided to it by QRI. Such services included US GAAP reporting (since Quicksilver Canada was included in the consolidated statements of the Quicksilver Group), internal audit, certain budgeting services, internal legal, cash management, debt service, hedge analysis, certain information technology, certain human resource functions, certain insurance and others.
80. In anticipation of these proceedings, and in particular in light of the fact that QRI is a significant creditor of the Applicant (as discussed below), Quicksilver Canada determined that it would be appropriate to formalize the relationship by which Quicksilver Canada receives intercompany services from QRI. Accordingly, on March 4, 2016, Quicksilver Canada and QRI entered into a Services Agreement, a copy of which is attached as **Exhibit "20"** to this my Affidavit (the "**Services Agreement**").
81. The payments required to be made by Quicksilver Canada to QRI under the Services Agreement are expected to be minimal. They are included in the cash flow forecast

referred to below, and I understand that the Monitor believes that the quantum of the payments is reasonable having regard for the services Quicksilver Canada will receive under the Services Agreement (most likely less than \$10,000 per month).

IV. CURRENT CIRCUMSTANCES

82. As required under U.S. securities laws and permitted under applicable Canadian securities laws, the Quicksilver Group's public financial reporting is done on a consolidated basis in accordance with U.S. generally accepted accounting principles. A copy of the Quicksilver Group's unaudited consolidated monthly financial statements over the last year are attached as **Exhibit "21"** to this my Affidavit.

83. Attached as **Exhibit "22"** is the unaudited consolidated balance sheet for the Quicksilver Canada Group as at December 31, 2015. The key contributor to the Quicksilver Canada Group is Quicksilver Canada.

A. Assets

84. As at October 31, 2015, the Quicksilver Canada Group had total assets with a book value of approximately \$252 million. The assets included current assets of approximately \$36 million, and non-current assets of approximately \$216 million.

85. Current assets included primarily cash (approximately \$26 million) and inventory and other current assets (approximately \$9 million).

86. Non-current assets included primarily property and equipment (approximately \$211 million) and other assets (approximately \$6 million).

B. Liabilities

87. As at December 31, 2015, the liabilities on Quicksilver Canada Group's balance sheet totalled approximately \$712 million.

Credit Facility

88. Pursuant to an Amended and Restated Credit Agreement dated as of December 22, 2011, QRI, as parent, and Quicksilver Canada, as borrower, are party to a secured credit facility originally scheduled to mature on September 6, 2016 but accelerated and terminated on March 17, 2015 (the "**Credit Facility**") with a syndicate of banks led by JPMorgan Chase Bank N.A., Toronto Branch, as Administrative Agent (the "**Agent**"). A copy of the Amended and Restated Credit Agreement (with amendments, but excluding the lengthy exhibits and schedules appended thereto) is attached as **Exhibit "23"** to this my Affidavit.
89. LNG Co and LNG SubCo are not obligors under the Credit Facility.
90. The Credit Facility is secured against, among other things, the assets of Quicksilver Canada, including all of its real property and personal property, but excluding certain specified excluded collateral. The shares of LNG Co owned by Quicksilver Canada are included in the security. The security was granted pursuant to a Demand Debenture dated as of September 6, 2011 by Quicksilver Canada in favor of the Administrative Agent. A copy of the Demand Debenture is attached as **Exhibit "24"** to this my Affidavit.
91. The Credit Facility is guaranteed by QRI and certain of its affiliates, namely, Cowtown Pipeline Management, Inc., Cowtown Pipeline Funding, Inc., Cowtown Gas Processing L.P. and Cowtown Pipeline L.P. pursuant to a Guaranty dated as of December 22, 2011. A copy of the Guaranty is attached as **Exhibit "25"** to this my Affidavit.
92. Concurrently with Quicksilver Canada and QRI entering into the Credit Facility, QRI entered into a Credit Facility with JPMorgan Chase Bank, N.A., as Global Administrative Agent, and the banks and other financial institutions party thereto as lenders and the other agents party thereto (the "**US Credit Facility**"). As security for its obligations under the US Credit Facility, its guarantee of the Credit Facility and certain swap and hedging transactions and bank product obligations as provided therein, QRI and certain of its affiliates granted security over, among other things, certain shares and securities, including 65% of the shares of Quicksilver Canada, to the Global Administrative Agent,

for its benefit and the benefit of the Canadian Administrative Agent. None of the Applicants are obligors under the US Credit Facility.

93. The Canadian Administrative Agent and the Global Administrative Agent entered into an Intercreditor Agreement dated as of December 22, 2011. Article 3 of the Intercreditor Agreement provides a mechanism to address how the Canadian Administrative Agent and the Global Administrative Agent share proceeds received under the Credit Facility and the US Credit Facility. A copy of the Intercreditor Agreement is attached as **Exhibit "26"** to this my Affidavit.
94. As at the date hereof, Quicksilver Canada has drawn approximately CAD \$80.6 million and approximately USD \$18.4 million under the Credit Facility. In addition, Quicksilver Canada has issued various letters of credit under the Credit Facility. The total amount currently outstanding under the Credit Facility is approximately CAD \$106.4 million.
95. Quicksilver Canada intends to make monthly interest payments under the Credit Facility during these proceedings, and such interest payments are accordingly included in the cash flow forecast referred to below.
96. On March 17, 2015, Quicksilver Canada reached an agreement with the Agent regarding a forbearance for a period up to and including June 16, 2015 of any default under the Credit Facility arising due to the Chapter 11 filing by the Chapter 11 Debtors. The forbearance has subsequently been extended on multiple occasions and is currently set to expire on April 1, 2016.
97. The Applicants have agreed to pay the reasonable fees and disbursements of the advisors to the Agent (the "**Agent's Advisors**") during the course of these proceedings.

Intercompany Debt

98. Quicksilver Canada is indebted to QRI in the principal amount of approximately USD \$413.3 million in respect of funded debt (the "**Intercompany Debt**"). The Intercompany Debt does not include trade payables or other amounts owing by Quicksilver Canada to QRI. The Intercompany Debt was advanced by QRI to Quicksilver Canada as follows:

- (a) On October 8, 2010, QRI advanced approximately USD \$243.6 million;
 - (b) On May 1, 2013, QRI advanced approximately USD \$147.1 million; and
 - (c) On March 11, 2014, QRI advanced approximately USD \$22.6 million.
99. Each of the advances were used by Quicksilver Canada to repay existing third party debt, either debts owing by Quicksilver Canada under the Credit Facility or debts owing by Quicksilver Canada to other non-Quicksilver Group creditors. Quicksilver Canada's cash flow from operations was historically sufficient to fund operations but insufficient to also fund its intensive capital program. Accordingly, Quicksilver Canada borrowed these funds from QRI to fund its capital program.
100. The letter agreements pursuant to which QRI advanced the Intercompany Debt to Quicksilver Canada are attached as **Exhibit "27"** to this my Affidavit. Interest on the Intercompany Debt accrues at 2% per annum and is to be paid quarterly, although Quicksilver Canada stopped paying interest in April 2015. Quicksilver Canada does not intend to make interest payments on the Intercompany Debt during these proceedings, and such interest payments are therefore not included in the cash flow forecast referred to below.
101. The Intercompany Debt is unsecured and is governed generally by an Amended and Restated Global Intercompany Note dated October 7, 2011, a copy of which is attached as **Exhibit "28"** to this my Affidavit.

V. EVENTS LEADING TO APPLICANTS' CURRENT CIRCUMSTANCES

A. General

102. Several key factors have resulted in the current financial position of Quicksilver Canada, including the sustained decline in gas prices, operational challenges, and an inability to consummate a transaction with respect to the Horn River Asset, all of which taken together have not permitted Quicksilver Canada to grow quickly enough to achieve the scale required to make its Horn River Asset, and the associated arrangements with KKR and Spectra, economic. In addition, QRI's significantly leveraged balance sheet has

exacerbated issues for Quicksilver Canada, in particular given that QRI is also a party to the Credit Facility.

103. Natural gas prices have declined precipitously since Quicksilver Canada entered into the KKR Transaction.
104. In addition, in January 2013, the Canadian National Energy Board (the "**NEB**"), an independent agency which regulates international and interprovincial aspects of the oil and gas industries in Canada, recommended against approval of the Komie North Project, a series of contracts between Quicksilver Canada and NOVA Gas Transmission Ltd. (a subsidiary of TransCanada PipeLines Limited) for the construction of a pipeline and meter station in the Horn River Basin. As a result, Quicksilver Canada decided to defer drilling and construction of its natural gas treating facility.
105. These were significant delays that were not anticipated by Quicksilver Canada when the KKR Transaction and the Westcoast Agreement were entered into, for example. As described above, Quicksilver Canada's take-or-pay obligations in connection with the KKR Transaction and the Westcoast Agreement are financially onerous and required sufficient scale in order to be economically viable. That scale could not be achieved as a result of the dramatic drop in gas prices, the recommendation by the NEB with respect to the Komie North Project and Quicksilver Canada's inability to consummate a transaction with respect to the Horn River Asset. As described above, the Maxhamish Pipeline had reached a throughput of approximately 100 MMcfd (maximum) and then an average throughput of around 40 MMcfd out of a nominal rated capacity of 400 MMcfd. Quicksilver Canada has been the only shipper on the line, which was certainly not the intention when the key agreements were put in place.

B. QRI Capital Structure Issues

106. In addition, on February 17, 2015, QRI announced that it had decided not to make the approximately USD \$13.6 million interest payment due that day on its 9.125% senior notes due 2019 (the "**2019 Notes**"). The Applicants are not obligors with respect to the 2019 Notes. A copy of the news release is attached as **Exhibit "29"** to this my Affidavit.

107. Under the terms of the indenture governing the 2019 Notes, QRI had a 30-day grace period before the failure to make the interest payment resulted in an event of default. During the 30-day grace period, QRI had discussions with their creditors but those discussions did not produce an agreement that would enable QRI to effectively address, in a holistic manner, the impending issues adversely impacting its business, including (i) potential springing maturities under certain of its secured credit agreements, (ii) potential near term liquidity shortfalls due to the springing maturities, (iii) potential near term breaches of certain financial covenants resulting from sharp declines in natural gas and NGL prices, and (iv) certain other potential defaults under its credit agreements, including the receipt of an opinion containing a going-concern uncertainty from QRI's auditor. The acceleration of the principal under the 2019 Notes would have resulted in defaults under the terms of other indebtedness of QRI, including the US Credit Facility, and of key importance to Quicksilver Canada, the Credit Facility.
108. The issues affecting QRI and Quicksilver Canada have a significant impact on LNG Co and LNG SubCo given that, as discussed above, the Discovery LNG project does not generate any revenues and Quicksilver Canada has been the sole source of financing to fund expenses.

C. Sale Process

109. In January 2014, QRI retained Houlihan to assist with the evaluation of QRI's options to address its near-term debt maturities, enhancement of its liquidity position, and evaluation of strategic alternatives. A true copy of the Financial Advisor Engagement Letter entered into between Quicksilver Canada and Houlihan is attached as **Exhibit "30"** to this Affidavit.
110. On September 14, 2015, QRI announced the commencement of a marketing and sale process to sell substantially all or a portion of its U.S. and Canadian assets. The U.S. process was run as part of the Chapter 11 Debtors' bankruptcy proceedings in the U.S. Court. The Canadian process (the "**QRCI Sale Process**") ran parallel to, but separate from, the U.S. process and solicited bids for any or all the Quicksilver Canada Group's assets.

111. The original timeline for the QRCI Sale Process was as follows:
 - (a) September 17, 2015 – Announcement
 - (b) November 4, 2015 – Indications of Interest Due
 - (c) December 2, 2015 – Final Term Sheet Due
 - (d) January 21, 2016 – Completion of Documentation / Closing
112. Quicksilver Canada, with the assistance of Houlihan, prepared a confidential information memorandum that was provided to interested parties that executed non-disclosure agreements with Quicksilver Canada.
113. With respect to the QRCI Sale Process, a total of 354 parties were contacted, of which 244 were potential strategic buyers and 110 were potential financial buyers. Of those 354 parties contacted, 43 (25 strategic parties and 18 financial parties) executed a non-disclosure agreement, and 11 (6 strategic parties and 5 financial parties) submitted expressions of interest.
114. Ultimately 6 parties (5 strategic parties and 1 financial party) submitted offers in the QRCI Sale Process. Five of the offers were for the Horseshoe Canyon Asset, and one offer was for Discovery LNG. No bids were received for the Horn River Asset.
115. I believe that Houlihan conducted a thorough and comprehensive canvassing of the market, and I am satisfied that all alternatives and expressions of interest were properly and thoroughly pursued.
116. For information purposes only, on January 27, 2016 the U.S. Court approved a sale by QRI and certain of the Chapter 11 Debtors to BlueStone Natural Resources II, LLC for substantially all of QRI and the other sellers' oil and gas assets. A copy of the U.S. Court Order is attached as **Exhibit "31"** to this my Affidavit. It is anticipated that this sale will close on or prior to March 31, 2016.
117. FTI, the proposed Monitor, has been kept apprised of the progress of the Sale Process.

VI. PROPOSED HORSESHOE CANYON ASSET TRANSACTION

118. Effective March 1, 2016, Quicksilver Canada and CPC Resources ULC entered into an asset purchase agreement with respect to the Horseshoe Canyon Asset (the "**Horseshoe Canyon APA**"). A copy of the Horseshoe Canyon APA (excluding the lengthy schedules) is now shown to me and marked as **Exhibit "32"** to this my Affidavit. The APA contains sensitive commercial information, the disclosure of which would be very harmful to Quicksilver Canada's commercial interests. Therefore, the Applicants are asking that **Exhibit "32"** be sealed on the Court file.
119. The Horseshoe Canyon APA provides for a sale of all of Quicksilver Canada's assets in Alberta (the Horseshoe Canyon Asset and the Northwest Alberta Shale Assets).
120. The Horseshoe Canyon APA contemplates that the sale will be finalized through a CCAA proceeding, and it is conditional on the Court granting an approval and vesting order.
121. For clarity, the Applicants are not seeking any relief with respect to the Horseshoe Canyon APA in this Application. If the Initial Order is granted, the Applicants intend to serve a sale approval application shortly after the granting of the Initial Order, which application will be returnable on a date to be coordinated with the Court at the hearing of this Application.

VII. PLAN OF COMPROMISE AND ARRANGEMENT

122. The Applicants do not currently have a Plan of Compromise and Arrangement ready to present to their creditors. If the Initial Order being sought herein is granted by this Honourable Court, the Applicants intend to use the initial 30-day stay period to advance the following initiatives:
- (a) bring an application, on notice to all interested parties, to seek approval of the Horseshoe Canyon APA;

- (b) close the purchase and sale transaction contemplated by the Horseshoe Canyon APA and receive the sale proceeds therefrom, to be held pending an orderly distribution to their creditors;
- (c) explore any and all possible transactions that could monetize the Horn River Asset and Discovery LNG;
- (d) in connection with possible transactions involving the Horn River Asset and Discovery LNG, hold discussions with the appropriate environmental and regulatory authorities in British Columbia, regarding any potential environmental and regulatory claims regarding those assets;
- (e) move forward with a claims process to identify all creditor claims against the Applicants and their directors; and
- (f) hold discussions with the Applicants' primary creditor groups (the Agent, QRI, Spectra, KKR and the British Columbia environmental and regulatory authorities) to discuss a Plan of Compromise and Arrangement that would allow for the most efficient method of monetizing the assets of the Applicants, determining claims against the Applicants and their directors, and distributing proceeds to creditors.

VIII. THE APPLICANTS MEET THE CCAA STATUTORY REQUIREMENTS

A. The Applicants are "Companies" under the CCAA

123. Quicksilver Canada is a corporation incorporated under the ABCA, and each of LNG Co and LNG SubCo is a corporation incorporated under the BCBCA. Accordingly, each of the Applicants is a "company" to which the CCAA applies.

B. The Applicants have Claims Against them in Excess of \$5 Million

124. As discussed above, the Applicants have claims against them well in excess of \$5 million in the aggregate.

C. The Applicants are Insolvent

125. As discussed above, but for the forbearance that Quicksilver Canada has obtained from the Agent, all amounts outstanding in respect of the Credit Facility could become due and owing imminently, and Quicksilver Canada does not have sufficient liquidity to pay those amounts.
126. With respect to LNG Co and LNG SubCo, their sole source of financing is Quicksilver Canada, which is itself insolvent. As such, LNG Co and LNG Subco are unable to pay their current obligations as they become due.

IX. RELIEF SOUGHT

127. The immediate objective of the proposed CCAA proceeding is to effect a sale of the Horseshoe Canyon Assets and the Northwest Alberta Shale Assets, and then to monetize all of the Applicants' other remaining assets. Following those sales, the Applicants' intention is for the CCAA proceeding to be used to identify and resolve all claims against the Applicants and their directors and officers in order to effect an orderly distribution to the Applicants' creditors.
128. On February 29, 2016, the directors of each of the Applicants resolved to grant authority to management to approve the commencement of proceedings under the CCAA.

A. Stay of Proceedings

129. The Applicants require a stay of proceedings to maintain the *status quo* in order to preserve the value of the Applicants and to ensure that no creditor of the Applicants obtains preferred treatment relative to other creditors.

B. Appointment of Monitor

130. I believe that FTI Consulting Canada Inc. is qualified and competent to act as Monitor under the CCAA proceedings of the Applicants. Attached as **Exhibit "33"** to this my Affidavit is a copy of a Consent to Act as Monitor signed by FTI Consulting Canada Inc.

131. I understand that FTI Consulting Canada Inc. will be filing its Pre-Filing Report with this Honourable Court as proposed Monitor in conjunction with the Applicants' request for relief under the CCAA.

C. Payments During CCAA Proceedings and Critical Suppliers

132. During the course of these CCAA proceedings, the Applicants intend to make payments for goods and services supplied post-filing as set out in the cash flow projections referred to below and as permitted by the Initial Order.

133. Additionally, the Applicants have identified a number of parties that are critical to the ongoing operations of the Applicants, and whose continued, uninterrupted provision of goods and services is crucial to allowing the Applicants to continue their business operations and preserve the value of the business operations (the "**Critical Suppliers**").

134. The Applicants seek the Court's approval to continue to pay the Critical Suppliers in the ordinary course of business, including for the provision of goods and services prior to the date of the application for the Initial Order (all such payments to be made in consultation with and under the supervision of the Monitor), provided that the total amount paid to all Critical Suppliers on or after the date of the CCAA Initial Order in respect of amounts incurred prior to the date of the Initial Order shall not exceed \$150,000 (all related to the Horn River Asset).

135. In my view, given the importance of the goods and services provided by the Critical Suppliers, the potential disruption to the Applicants' business operations should the Critical Suppliers not continue to be paid in the ordinary course (and possibly withhold their goods and services while C.O.D. terms or other arrangements were put in place) could be material and could affect the cash flow forecast in a very material and negative way.

136. It is anticipated that the impact of the payments to Critical Suppliers will only be experienced in the first two (2) weeks of the CCAA proceedings, as reflected in the cash flow forecast. After that, the Critical Suppliers will be invoicing for post-Initial Order

goods and services and will be paid for those goods and services in the same manner as all other suppliers.

137. With respect to the Horn River Asset, Quicksilver Canada is subject to certain current compliance requirements with the BC Oil & Gas Commission (the "**BCOGC**"). Because Quicksilver Canada's wells in the Horn River Asset have been shut-in for approximately one year, the BCOGC is requiring Quicksilver Canada to carry out work to implement a "short-term suspension of certain of the wells" and other regulatory compliance work. The necessary operations include the following:
- (a) suspending wells in a more permanent state;
 - (b) repairing leaking bottom assemblies in a number of wells;
 - (c) paying the costs to remove oil-based drilling fluids stored onsite;
 - (d) removing sludge containing normally occurring radioactive material ("NORM") at a small flowback pit utilized for fracturing flowback operations; and
 - (e) maintaining the roads in the area while this work is being performed.
138. Quicksilver Canada estimates the total expenses associated with these operations to be between \$2.7 million and \$3.0 million. Carrying out these operations is necessary to ensure continued compliance with the BCOGC. In my view, carrying out these operations is in the best interests of Quicksilver Canada and its stakeholders. Doing so will maintain and enhance the value of the Horn River Asset, increasing the likelihood of Quicksilver Canada being able to effect a transaction for the Horn River Asset and increasing Quicksilver Canada's realization therefrom. These projected expenses are reflected in the 13-week cash flow statements described below.
139. With respect to the Horseshoe Canyon Asset, the Applicants are requesting an Order that Quicksilver Canada be authorized to continue to pay all operating expenses with respect thereto, whether incurred before or after the date of the Initial Order. These payments are reflected in the cashflow statements attached to this Affidavit. The reason that Quicksilver Canada is seeking this authority is because the Horseshoe Canyon APA

obligates Quicksilver Canada to continue to operate the Horseshoe Canyon asset in the ordinary course until closing, and any such expenditures will be adjusted for in the purchase price to be paid under the Horseshoe Canyon APA.

D. Administration Charge

140. It is contemplated that the Monitor, counsel to the Monitor, counsel to the Applicants, the Agent's Advisors and Houlihan would be granted a first priority Court-ordered charge on the assets, property and undertakings of the Applicants in priority to all other security interests, trusts, liens, charges and encumbrances (the "**Administration Charge**") up to the maximum amount of \$2,500,000 in respect of their respective fees and disbursements. The Applicants believe the Administration Charge is fair and reasonable in the circumstances.
141. The Applicants requires the expertise, knowledge and continuing participation of the proposed beneficiaries of the Administration Charge in order to complete a successful restructuring. I believe the Administration Charge is necessary to ensure their continued participation.

E. Directors' Charge

142. It is contemplated that the Applicants' directors and officers would be granted a second priority Court-ordered charge on the assets, property and undertakings of the Applicants in priority to all other security interests, trusts, liens, charges and encumbrances, but subordinate to the Administration Charge (the "**Directors' Charge**") up to the maximum amount of \$450,000. The Applicants believe the Directors' Charge is fair and reasonable in the circumstances.
143. A successful restructuring of the Applicants will only be possible with the continued participation of the Applicants' directors and officers. These individuals have specialized expertise and relationships with the Applicants' stakeholders. In addition, the directors and officers have gained significant knowledge that cannot be easily replicated or replaced.

144. The Applicants' directors and officers have the benefit of QRI insurance policies (the "**D&O Insurance Policies**") in respect of their potential liability. Although the D&O Insurance Policies insure the directors and officers of the Applicants for certain claims that may arise against them in their capacity as directors and/or officers of the Applicants, coverage is subject to several exclusions and limitations and there is a potential for insufficient coverage in respect of potential director and officer liabilities, in particular because the D&O Insurance Policies are shared with the directors and officers of other companies in the Quicksilver Group. The directors and officers of the Applicants have expressed their desire for certainty with respect to potential personal liability if they continue in their current capacities in the context of a CCAA proceeding.

F. KERP and KERP Charge

145. Quicksilver Canada has put in place a key employee retention plan for its executive and non-executive employees. The KERP is designed to incentivize key employees to remain in their employment during the anticipated restructuring. Without the retention of key employees, the Applicants' ability to successfully maintain their business operations and preserve asset value in the CCAA proceeding, would be seriously compromised.

146. The key elements of the KERP are:

- (a) non-executive eligible participants will receive payments in three (3) installments:
 - (i) 60% of the bonus amount, less applicable taxes and withholdings, which was paid at the execution of the asset purchase agreement relating to substantially all of the Horseshoe Canyon Asset which occurred on March 1, 2016 ("**Milestone 1**");
 - (ii) 20% of the bonus amount, less applicable taxes and withholdings, to be paid upon the successful closing of the sale contemplated in (i) above ("**Milestone 2**"); and

- (iii) 20% of the bonus amount, less applicable taxes and withholdings, to be paid at the time of the completed transition of all of the assets of Quicksilver Canada ("**Milestone 3**");
- (b) executive eligible participants will receive 100% of the bonus amount, less applicable taxes and withholdings, to be paid at the time of the completed transition of all of the assets of Quicksilver Canada;
- (c) a non-executive participant whose employment is terminated by QRCI without cause after achieving Milestone 1 but before Milestone 2 is achieved, will remain eligible to receive all KERP payments related to Milestone 1 and Milestone 2 subsequent to such termination; provided that any such employee who is offered employment by a purchaser contemporaneously with his/her termination, would not be eligible to receive bonus payments after his/her termination date;
- (d) a non-executive plan participant whose employment is terminated for any reason within 30 days after achieving Milestone 2 will not be eligible to receive the Milestone 3 payment;
- (e) a non-executive plan participant whose employment is terminated by QRCI without cause 31 or more days after achieving Milestone 2, but before Milestone 3 is achieved will remain eligible to receive all bonus plan payments that are related to Milestone 3; provided that any such employee who is offered employment by a purchaser contemporaneously with his/her termination, would not be eligible to receive the Milestone 3 payment;
- (f) any participant who terminates his or her own employment prior to any of Milestone 1, 2 or 3, will not be eligible to receive the bonus payment or payments with respect to such Milestone or Milestones; and
- (g) an executive participant whose employment is terminated by Quicksilver Canada without cause prior to achieving Milestone 3 will remain eligible to receive the Milestone 3 payment; and

- (h) the final component of the KERP is a bonus retention payment plan for certain executive employees, under which bonus payments are payable upon the sale of Quicksilver Canada's interests in the Horn River Asset. That plan has been in place for certain of the executives of Quicksilver Canada since 2013 and has recently been expanded to include two other executives in anticipation of these proceedings, given the need to retain and incentivize the entire executive. Now shown to me and marked as **Exhibit "34"** to this Affidavit is a copy of the letters to the executive employees regarding this bonus retention payment arrangement (the "**Bonus Retention Letters**").
147. Now shown to me and marked as **Exhibit "35"** to this Affidavit is a copy of a spreadsheet that contains details of the names of the key employees, their annual salaries and the retention payment that has been offered to them under the KERP (the "**Confidential KERP Summary**"). The Confidential KERP Summary and the Bonus Retention Letters (collectively, the "**KERP Documents**") contain sensitive commercial information, the disclosure of which would be very harmful to Quicksilver Canada's commercial interests, as well as the privacy interests of Quicksilver Canada's employees. Therefore, the Applicants are asking that the KERP Documents in **Exhibits "34"** and **"35"** be sealed on the Court file.
148. It is contemplated that the beneficiaries under the KERP would be granted a third priority Court-ordered charge on the assets, property and undertakings of the Applicants in priority to all other charges other than the Administration Charge and the Directors' Charge (the "**KERP Charge**") up to the maximum amount of \$1,380,000, which is the maximum that will become payable under the KERP Documents. The Applicants believe the KERP Charge is fair and reasonable in the circumstances.
- G. LNG Co Interim Lenders' Charge**
149. As is noted above, LNG Co and LNG Subco generate no revenue from which to pay their expenses. Rather, they rely on intercompany loans from QRCI to provide cash to meet their expenses. Currently, LNG Co currently owes QRCI \$5 million and LNG SubCo currently owes QRCI \$0, by way of unsecured intercompany loans.

150. As set out in the 13-week cash flow forecast described below (and attached as **Exhibit "36"** to this Affidavit), LNG Co and LNG Subco will require cash during these proceedings to pay their ongoing day-to-day operational expenses and their share of the professional fees and disbursements in connection with the CCAA proceedings, for which they have no source of funding other than QRCI. These funding requirements are estimated to be no more than \$1 million in the next six months, and the short-term expenses are reflected in the 13-week cashflow forecast mentioned below.
151. LNG Co and LNG Subco propose to obtain such funding pursuant to debtor-in-possession advances from QRCI, as required. It is contemplated that QRCI would be granted a Court-ordered charge on the assets, property and undertakings of LNG Co and LNG Subco to secure such advances (the "**LNG Co Interim Lenders' Charge**").
152. The Applicants believe the proposed interim lending arrangement and the LNG Co Interim Lenders' Charge are fair to all stakeholders and are reasonable in the circumstances.

H. Sealing

153. As noted above, various Exhibits to this Affidavit contain sensitive commercial information, the disclosure of which would be very harmful to Quicksilver Canada's and certain of its counterparties' commercial interests, as well as the privacy interests of Quicksilver Canada's employees. Accordingly, as part of this application, the Applicants are requesting that the Exhibits containing the agreements related to the KKR Transaction (Exhibits "5" – "12"), the Westcoast Agreement (Exhibit "13"), the Horseshoe Canyon APA (Exhibit "32") and the KERP Documents (Exhibits "34" and "35") be sealed on the Court file.

X. CASH FLOW PROJECTIONS

154. As noted above, the Applicants' 13-week cash flow forecast is attached as Exhibit "36" hereto. As set out therein, the Applicants' principal uses of cash during the next 13 weeks will consist of the payment of ongoing day-to-day operational expenses, such as payroll,

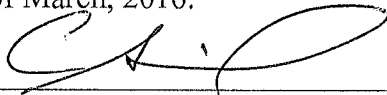
transportation and office related expenses, and professional fees and disbursements in connection with these CCAA proceedings.

155. As at March 11, 2016, the Applicants expect to have approximately \$19.8 million available cash on hand. The Applicants' cash flow forecast projects that, subject to obtaining the relief outlined herein, the Applicants will have sufficient cash to fund their projected costs until the end of the stay period.

XI. CONCLUSION

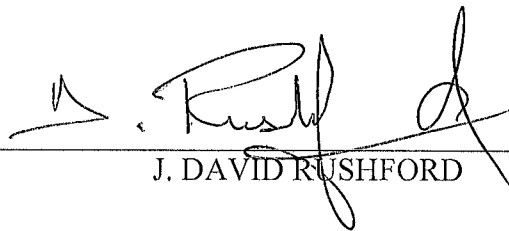
156. I swear this my Affidavit in support of an Application for the relief set out in paragraph 3 of this my Affidavit and for no other or improper purpose.

SWORN (OR AFFIRMED) BEFORE ME)
at Calgary, Alberta, this 8th)
day of March, 2016.)



A Commissioner for Oaths)
in and for the Province of Alberta)

CHRIS SIMARD
Barrister and Solicitor



J. DAVID RUSHFORD