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COURT COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE CALGARY
APPLICANT NATIONAL BANK OF CANADA, IN ITS CAPACITY
AS ADMINISTRATIVE AGENT
RESPONDENTS TWIN BUTTE ENERGY LTD.
DOCUMENT **FOURTH REPORT OF FTI CONSULTING CANADA
INC., IN ITS CAPACITY AS COURT APPOINTED
RECEIVER AND MANAGER OF TWIN BUTTE
ENERGY LTD.**

February 13, 2017

ADDRESS FOR SERVICE AND
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INTRODUCTION

1. On September 1, 2016 (the “**Date of Appointment**”), FTI Consulting Canada Inc. was appointed as receiver and manager (the “**Receiver**”) of all of the assets, undertakings and properties (the “**Property**”) of Twin Butte Energy Ltd. (“**Twin Butte**” or the “**Company**”) pursuant to an Order of the Honourable Madam Justice Romaine (the “**Receivership Order**”).
2. The Receivership Order authorized the Receiver, amongst other things, to manage, operate and carry on the business of the Company, to market any or all the Property including advertising and soliciting offers to purchase the Property, and to make such arrangements or agreements as deemed necessary by the Receiver.
3. On October 11, 2016, an order (the “**SISP Order**”) was granted approving the Receiver’s proposed sales and investor solicitation process (“**SISP**”), which was attached as Appendix A to the Second Report of the Receiver. The SISP Order also authorized the Receiver to engage CIBC World Markets (“**CIBC**”) and Peters & Co. Limited (“**Peters**”) (collectively “**Selling Agents**”) as selling agents to market all of the assets and properties of Twin Butte in accordance with the terms of the SISP.
4. On January 19, 2017, an order (the “**Sale Approval and Vesting Order**”) was granted approving a purchase and sale agreement (“**HOC PSA**”) dated December 23, 2016 between the Receiver and Henenghaixin Operating Corp (“**HOC**”). The HOC PSA contemplated the en bloc sale of all of Twin Butte’s oil and gas assets to HOC. The Receiver continues to work with HOC with respect to closing the HOC PSA in accordance with its conditions.
5. The Receiver’s reports and other publically available information in respect of these proceedings (the “**Receivership Proceedings**”) are posted on the Receiver’s website at <http://cfcanada.fticonsulting.com/twinbutte> (the “**Receiver’s Website**”).

6. The purpose of this report ("**Fourth Report**") is to advise this Honourable Court with respect to the Receiver's intention to terminate certain agreements that were listed as excluded contracts in Schedule G of the HOC PSA. The agreements the Receiver is proposing to terminate are as follows:

(a) Silverdale 02-06-049-27 W3M oil batter well effluent processing and water disposal agreement ("**DPDG Agreement**") dated October 1, 2011 between Secure Energy Services Inc. ("**Secure**") and Emerge Oil & Gas Inc. ("**Emerge**"). (Emerge is a predecessor of Twin Butte). A copy of the DPDG Agreement is attached as Appendix A to the Receiver's confidential supplement to this Fourth Report ("**Confidential Supplement Report**").

(b) Non-competition agreement ("**Non-Compete Agreement**") dated October 1, 2011 between Secure and Emerge. A copy of the Non-Compete Agreement is attached as Appendix B to the Confidential Supplement Report.

(Collectively the Non-Compete Agreement and the DPDG Agreement are referred to as the "**Secure Agreements**").

TERMS OF REFERENCE

7. In preparing this Fourth Report, the Receiver has relied upon unaudited financial information, other information available to the Receiver and, where appropriate, the Company's books and records and discussions with various parties (collectively, the "**Information**").

8. The Receiver has prepared this Fourth Report in connection with the Receiver's Application dated February 22, 2017. This Fourth Report should not be relied on for other purposes.

9. Information and advice described in this Fourth Report that has been provided to the Receiver by its legal counsel, Norton Rose Fulbright Canada LLP (the “**Receiver’s Counsel**”), was provided to assist the Receiver in considering its course of action, is not intended as legal or other advice to, and may not be relied upon by, any other person.
10. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian Dollars.

BACKGROUND TO THE SECURE AGREEMENTS

11. Emerge (a company acquired by and subsequently amalgamated with Twin Butte in 2012), originally sold a facility known as the Silverdale 02-06-049-27W3 Oil Battery (“**Silverdale Facility**”) to Secure pursuant to the terms of an asset purchase agreement dated September 11, 2011 (the “**Silverdale Facility PSA**”).
12. The Silverdale Facility’s operation is comprised of receiving, processing and treating fluids produced from oil and gas wells, separating clean oil from waste fluids and then terminaling/transporting clean oil and disposing waste fluids.
13. Pursuant to the Silverdale Facility PSA, Secure and Emerge agreed to enter into the Non-Compete Agreement whereby Emerge agreed not enter into similar businesses that would compete with the Silverdale Facility for a term of seven (7) years (expiring in October 1, 2018, or approximately 20 months from now).
14. Emerge also entered into the DPDG Agreement in relation to the Silverdale Facility. Further details with respect to the Non-Compete Agreement and the DPDG Agreement are provided below.

SUMMARY OF SECURE AGREEMENTS

Non-Compete Agreement

15. After Emerge sold the Silverdale Facility to Secure, the respective companies entered into the Non-Compete Agreement. The Non-Compete Agreement was entered into to protect the Silverdale Facility business from competition by Emerge in order for Secure to receive the full benefit of the Silverdale Facility until the expiry of the Secure Agreements.
16. Through the Non-Compete Agreement, Emerge (and its affiliates or successors) agreed not to build or buy a facility that provides similar services to the Silverdale Facility for a term of seven years in a set restricted geographic area. The seven year term commenced on October 1, 2011 and ends October 1, 2018. The restricted geographic area covers approximately 59 townships (“**Restricted Area**”).

DPDG Agreement

17. The DPDG Agreement governs an arrangement whereby Emerge would deliver all of the fluid it produces from its oil wells in a designated area to the Silverdale Facility to be treated, processed, terminaled, transported and/or disposed of (collectively “**Processing Services**”). The Processing Services were to be provided by Secure to Emerge at set rates. In exchange, Secure would be afforded various other benefits including a right of first refusal to purchase any of Emerge’s current or future suspended or abandoned wells to be used as disposal wells and a gross overriding royalty as further described below.
18. The following provides a high level summary of the major terms of the DPDG Agreement:
 - (a) Term commenced on October 1, 2011, continues for seven (7) years thereafter until terminated by either party providing 30 days written notice. Earliest termination date is October 1, 2018.
 - (b) The major business terms of the DPDG Agreement are as follows:

- i. Dedication (“**Dedication**”) of reserves created by clause 308 of the DPDG Agreement. The Dedication clause requires Twin Butte to deliver all of the well effluent and oilfield waste product produced (“**Produced Fluid**”) from Twin Butte wells within a dedicated area (“**Dedicated Area**”) to the Silverdale Facility for processing, treatment and transport/disposal. The Dedicated Area covers approximately 2.7 townships.
- ii. Secure to process, treat, terminal and transport/dispose of the Produced Fluid Emerge delivers to the Silverdale Facility at set rates as described in Exhibit C of the DPDG Agreement.
- iii. Gross overriding royalty (“**GORR**”) created by clause 311 of the DPDG Agreement. The GORR clause gives Secure a GORR on any third party produced water (“**Third Party Produced Water**”) that is disposed of down Twin Butte owned disposal wells in the Dedicated Area and Restricted Area (as defined in the Non-Compete Agreement and described in further detail below). The GORR is calculated as 20% of the disposal revenue Twin Butte generates for the disposal of Third Party Produced Water down Twin Butte wells in the Dedicated Area and Restricted Area.
- iv. Right of first refusal (“**ROFR**”) created by clause 310 of the DPDG Agreement. The ROFR clause grants secure the first right, but no obligation, to purchase any 100% Twin Butte owned suspended or abandoned well, including any disposal wells, for aggregate consideration of \$1.00 plus assumption of environmental liabilities located within the Restricted Area.

ISSUES WITH THE SECURE AGREEMENTS

19. After its appointment the Receiver reviewed the terms of the Secure Agreements and discussed the terms of the Secure Agreements with Twin Butte's management. The Receiver noted that the terms of the agreement were onerous and included restrictive provisions that could potentially affect the overall attractiveness of Twin Butte's oil and gas assets in a sale.
20. Throughout the sale investor and solicitation process ("SISP") it became clear that the Secure Agreements were undesirable to potential purchasers. All of the purchasers that submitted en bloc offers for Twin Butte's oil and gas assets excluded the Secure Agreements. Specifically, the highest bidder, HOC, required the Secure Agreements to be excluded from the HOC PSA.
21. Based on the Receiver's review of the Secure Agreements and the results of the SISP, the Receiver is of the view that, if potential purchasers were required to assume the Secure Agreements, the restrictive nature of provisions contained therein would negatively affect the value of the Twin Butte's assets as the Secured Agreements are generally above market or restrict future development of Twin Butte.

RECEIVER'S ANALYSIS AND INTENTION WITH RESPECT TO THE SECURE AGREEMENTS

22. The Receivership Order empowers the Receiver to terminate agreements or decline to perform them. The Secure Agreements are not being assumed by HOC through the HOC PSA as they are listed as excluded contracts. Therefore, the Receiver and Twin Butte's operations have no further use for the Secure Agreements. In addition, after the HOC PSA closes Twin Butte will no longer have any oil and gas assets and therefore no ability to continue to perform on the Secure Agreements.


23. The Receiver understands that Twin Butte has not been delivering Produced Fluid under terms of the DPDG Agreement nor has Secure been pursuing or enforcing on the terms of the DPDG Agreement since July 2015.
24. The Receiver estimates that, based on current activity levels, if Secure and Twin Butte were to abide by the terms of the Secure Agreements for the remainder of the term, the lost revenue to Secure would total approximately \$700,000 over the remainder of the term. It is uncertain at this time what the lost profit to Secure would be as there would be costs to Secure associated with generating the \$700,000 in lost revenue.
25. The Receiver's Counsel has reviewed the DPDG Agreement giving particular attention to the GORR, Dedication and ROFR. Based on the analysis and reasons identified by the Receiver's Counsel, the Receiver concluded that:
 - (a) the Dedication does not create an interest in land and may be terminated with the DPDG Agreement;
 - (b) the GORR does not create an interest in land and may be terminated with the DPDG Agreement;
 - (c) the ROFR is likely to create an interest in land, but has limited if any commercial value as it provides for the ability for Secure to purchase suspended or abandoned wells in the Restricted Area for \$1.00 plus the assumption of the environmental liability associated with such wells and, accordingly, the Receiver requests the Court's approval of the termination of the DPDG Agreement despite the ROFR.
 - (d) The Non-Compete Agreement does not create an interest in land and therefore it is within the Receiver's powers to terminate the Non-Compete Agreement.

26. Whether or not any clauses within the Secure Agreements create an interest in land, the Receiver's exercise of business judgment favors termination of the Secure Agreements. The Receiver notes that the termination of the Secure Agreements will result in Secure having a claim for damages based on the loss of potential profit for the remaining term (subject to Secure's duty to mitigate). The Receiver intends to seek approval to initiate a claims process upon closing HOC PSA which will provide a platform for Secure to assert a claim and for that claim to be adjudicated.
27. In any event, pursuant to the Sale Approval and Vesting Order, the Assets of Twin Butte are to be transferred to HOC free and clear of all claims with the sales proceeds to stand in the place of the lands and Assets. Further, upon closing the HOC PSA, Twin Butte will cease all operations and will not be in a position to either comply with or contravene the Secure Agreements.


RECEIVER'S REQUEST

The Receiver recommends termination of the Secure Agreements and seeks this Honourable Court's approval of same. All of which is respectfully submitted this 13th day of February, 2017.

FTI Consulting Canada Inc.,
in its capacity as receiver and manager
of the assets, undertakings and properties of
Twin Butte Energy Ltd.



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