

**IN THE COURT OF QUEEN'S BENCH OF ALBERTA  
JUDICIAL DISTRICT OF CALGARY**

**IN THE MATTER OF THE PROPOSAL OF  
DEEP CREEK OIL & GAS INC.**

**TRUSTEE'S THIRD REPORT -  
DISALLOWANCE OF THE CLAIM OF SEMCANADA CRUDE COMPANY**

**August 28, 2009**

Deep Creek Oil & Gas Inc.  
Trustee's Third Report  
Alger & Associates Inc.  
August 28, 2009

**DEEP CREEK OIL & GAS INC.**

**LISTING OF EXHIBITS**

**TO THE THIRD REPORT OF THE TRUSTEE**

1. Deep Creek Oil & Gas Inc. Proposal, dated June 18, 2009
2. Minutes of First Meeting of Creditors for Deep Creek Oil & Gas Inc., dated July 2, 2009
3. Order approving Deep Creek Oil & Gas Inc. Proposal and Sale of Davey Lake, dated July 23, 2009
4. Davey Lake Property Oil Production, Sales to non-SemCanada Crude Company purchasing for the period November 2008 to July 2009
5. Deep Creek Oil & Gas Inc. Proof of Claims in the CCAA proceedings of SemCanada Crude Company
6. Reconciliation of Prepayment and Product Delivery between SemCanada Crude Company and Deep Creek Oil & Gas Inc. for the period June 2008 to October 2008
7. Court Order regarding funds owed to SemCanada Crude Company, dated March 5, 2009
8. SemCanada Crude Company Statement for Crude Oil supplied in March 2009
9. Letter from Osler, Hoskin, &Harcourt LLP on behalf of SemCanada Crude Company informing of Deep Creek Oil & Gas Inc. obligation, dated March 26, 2009
10. National Bank of Canada Bank Statements from July 2008 to May 2009

Deep Creek Oil & Gas Inc.  
Trustee's Third Report  
Alger & Associates Inc.  
August 28, 2009

**DEEP CREEK OIL & GAS INC.**

**LISTING OF EXHIBITS CON'T...**

**TO THE THIRD REPORT OF THE TRUSTEE**

11. National Bank of Canada Loan Statements from July 2008 to March 2009
12. Bank of Nova Scotia March Bank Statement
13. Loan agreement between Keele Mezzanine Limited Partnership and Deep Creek Oil & Gas Inc.
14. Keele Mezzanine Limited Partnership Loan Statement for the period from November 2008 to March 16, 2009
15. National Bank of Canada Loan and Security Agreement
16. SemCanada Crude Company Proof of Claim, dated July 15, 2009
17. Trustee Disallowance Letter, dated July 20, 2009
18. Consent Order Re: Appeal of Disallowance, dated August 5, 2009
19. Letter from Osler, Hoskin, & Harcourt LLP on behalf of SemCanada Crude Company, request for additional information, dated August 14, 2009
20. Letter from Parlee McLaws LLP to Osler, Hoskin, & Harcourt LLP, dated August 27, 2009
21. Reconciliation of information requested and supplied in this report
22. Supplemental Trustee Disallowance Letter of the Claim of SemCanada Crude Company, dated August 27, 2009

### **Preface**

1. The Trustee's Third Report ("Trustee's Report") will provide the Court with information in the following major areas:
  - a) The Proposal of Deep Creek Oil and Gas Ltd. ("Deep Creek" or the "Company");
  - b) The history of the transactions between SemCanada Crude Company ("SemCanada") and Deep Creek;
  - c) The SemCanada Claim; and
  - d) The disallowance of the SemCanada claim.

### **Disclaimer and Limitations of Report**

2. The information contained in the Trustee's Report was obtained from the records of Deep Creek and various other sources. The information was not audited nor otherwise verified by the Trustee as to its accuracy or completeness, nor has it necessarily been prepared in accordance with generally accepted accounting principles and the reader is cautioned that this report may not disclose all significant matters about Deep Creek. Accordingly, we do not express an opinion or any other form of assurance on the information presented herein. The Trustee may refine or alter its observations as further information is obtained or is brought to its attention after the date of the Trustee's Report.
3. The Trustee assumes no responsibility or liability for any loss or damage occasioned by any party because of the circulation, publication, reproduction, or use of the Trustee's Report. Any use that any party makes of this report, or any reliance on or decisions to be made based on it is the responsibility of such party.

### The Proposal of Deep Creek

4. In early to mid March 2009, Deep Creek discussed and then met with Alger & Associates Inc. to review various options available to the Company due to its current financial situation and recent discussions with their operating lender, the National Bank of Canada ("NBC").
5. On March 19, 2009, Deep Creek filed a Notice of Intention to Make a Proposal ("NOI") pursuant to the *Bankruptcy and Insolvency Act* and Alger & Associates Inc. (the "Trustee") consented to act as Trustee.
6. On April 16, 2009 and May 29, 2009, Deep Creek was granted extensions in order to file the Proposal. On June 18, 2009, Deep Creek filed a Proposal, attached as Exhibit 1 to this report.
7. On July 2, 2009, Deep Creek held a Creditors' Meeting to vote on the Proposal and the minutes of the Creditors' Meeting are attached as Exhibit 2 to this report. As indicated in the minutes, the Proposal was accepted by more than the required statutory majority of creditors in both the number of creditors and dollar value of claims.
8. On July 23, 2009, Deep Creek obtained a Court Order from the Honorable Justice Hawco approving the Proposal and the sale of Deep Creek's interest in the Davey Lake property. A copy of the Order granted is attached as Exhibit 3. The Order included a clause holding back the amount of \$149,037.45 until the matter of the SemCanada claim, discussed below, was adjudicated. The sale of Davey Lake closed on July 29, 2009.
9. The Company is continuing operations in the normal course and has met all of the obligations required by the Proposal with the exception of the payment of cash and shares to the creditors, which is pending the resolution of the claim of SemCanada.

### History of the SemCanada and Deep Creek transactions

10. In early 2008, Deep Creek held an 18.5% working interest in an oil and gas property known as Davey Lake and located in Alberta. Deep Creek took over operatorship of Davey Lake in early July 2008. The initial working interest was owned prior to any advance payments by SemCanada.
11. The Company's interest in the property was increased in November 2008 to 80.5% by purchasing the interest of the operator, financed by Keele Capital Mezzanine Limited Partnership ("Keele"). Keele was familiar with the property as the existing lender to the operator of Davey Lake.
12. We are advised by management of Deep Creek that the transaction was almost entirely funded by way of debt provided by Keele. The small amount of cash required to complete the transaction was taken from the Bank of Nova Scotia account and transferred into the National Bank of Canada account. In addition, as noted in Paragraph 15, the last payment received from SemCanada was September 25, 2008 and the funds used in operations long prior to the completion of the purchase of the additional interest in Davey Lake.
13. During 2008, the Davey Lake property regularly supplied oil to SemCanada. During the period from July 2008 to July 2009, all crude oil production from Davey Lake was sold to either SemCanada or Acme. Attached as Exhibit 4, are the purchase statements for all oil production not sold to SemCanada from November 2008 to date for the Davey Lake property.
14. On July 22, 2008, SemCanada made an application for, and received protection from its creditors under the *Companies Creditors Arrangement Act* ("CCAA"). According to the books and records of Deep Creek as at July 22, 2009, SemCanada owed \$296,757 to Deep Creek, as operator of Davey Lake. In addition, SemCanada Energy Company owed an additional \$113,206. Deep Creek filed proof of claims relating to amounts owed for gas and oil production, respectively. These claims are attached as Exhibit 5.

15. Subsequent to the filing of protection under CCAA, Deep Creek agreed to continue to supply oil to SemCanada, on a prepaid basis. This arrangement continued until the end of October 2008, when Deep Creek stopped supplying SemCanada with crude oil production. The last payment by SemCanada to Deep Creek was made on September 25, 2008.
16. A reconciliation of the payments and supply of oil transactions, prepared by SemCanada, is attached as Exhibit 6 to this report. This reconciliation was reviewed and has been agreed by the Company. The net amount owed by Deep Creek for advance payments received after the CCAA filing was \$159,891.
17. During mid to late 2008, the Company faced several financial difficulties including: non-payment of the pre-CCAA SemCanada account receivable, lower commodity prices, and unsuccessful drilling activities. Deep Creek was unable to repay the advance payments made by SemCanada.
18. During late 2008 and early 2009, SemCanada continued discussions to collect the outstanding amount without success. We understand from the management of Deep Creek, that SemCanada discussed the financial difficulties facing Deep Creek.
19. On March 5, 2009, Deep Creek consented to an Order in favour of SemCanada. The Order, amongst other things:
  - a) Confirmed the amount owed to SemCanada;
  - b) Required Deep Creek to supply oil from Davey Lake;
  - c) Required Deep Creek to immediately pay any outstanding balance if the oil supplied from Davey lake did not pay out the amount in full by July 4, 2009; and
  - d) Acknowledged that the amount owed to SemCanada was held in trust by Deep Creek.

A copy of this Order is attached as Exhibit 7 to this report.

20. As previously discussed, in early to mid March 2009, Deep Creek met with Alger & Associates Inc. to discuss various options available to the Company due to its current financial situation and on March 19, 2009, Deep Creek filed a NOI.
21. After the NOI, the Company supplied certain production in late March 2009 to SemCanada in accordance with the March 5, 2009 Court Order whilst reviewing the situation with the Trustee and Keele. Attached as Exhibit 8, is a copy of the production shipped to SemCanada in March 2009.
22. On March 26, 2009, SemCanada's legal counsel informed the Trustee that certain excess advance payments made by SemCanada to Deep Creek for oil purchases were held in trust by Deep Creek and the Trustee had an obligation to protect the trust monies held on SemCanada's behalf. A copy of this letter is attached as Exhibit 9 to this report. A copy of this letter was sent to Keele by the Trustee on March 26, 2009.
23. The Trustee discussed this situation with the secured creditor, Keele, who advised the Company that production must be shipped where sales proceeds would generate future cash flow. Therefore, due to the stay in place and discussions with Keele, Deep Creek halted shipments to SemCanada.
24. On March 31, 2009, the legal counsel for SemCanada was informed that Deep Creek would no longer be supplying crude oil from battery legal described as 06-034-28W4. This decision not to supply the production was made by Company management, and not any one specific individual.
25. The Trustee took the position that there was a stay in place and informed SemCanada's legal counsel that at the time of the March 5, 2005 Court Order and NOI there were no funds, trust or otherwise, in the Company's possession. The Company relied on a revolving demand loan in favour of National Bank of Canada ("NBC").

### Deep Creek Cash and Loan Positions

26. The Company had two bank accounts as follows:
  - a) National Bank of Canada ("NBC") – This account was established for the operating line of credit and is where the oil and gas revenue from Davey Lake was exclusively received and the majority of operating expense paid. All SemCanada advance payments were made to this account.
  - b) Bank of Nova Scotia ("BNS") – This account was opened in Kelowna, where the officers of the Company reside, and is used for holding proceeds from the sale of shares and oil production from the Farrow property. Once funds reach a certain balance they are transferred to the NBC account.
27. The line of credit arrangements allowed the Company to make deposits and write cheques from the NBC bank account. When the balance in the bank account reached \$25,000, the balance was automatically transferred to reduce the operating loan. Conversely, when the balance became negative funds were transferred from the operating loan account to a maximum of \$800,000.
28. The NBC bank statements for the months of July 2008 to May 31, 2009 are attached as Exhibit 10. The NBC demand loan statements for the period July 2008 to March 2009 are attached as Exhibit 11. As mentioned in Paragraph 35, the NBC loan was assumed by Keele in late March 2009. The NBC bank and loan statements for the month of March 2009 were previously provided to the legal counsel for SemCanada.
29. Based on review of the NBC statements at March 5, 2009, which was the date of the Court Order, the loan balance was at the maximum level of \$800,000 and the balance in the bank account was overdrawn by \$24,216. At the date of the NOI, the loan balance remained at \$800,000 and there was a balance in the bank account of \$49.
30. The BNS bank statement for the month of March 2009, a copy of which is attached as Exhibit 12, was previously provided to SemCanada's legal counsel.

31. The BNS Bank Statement identifies cash balances of \$11,234 and \$16,706 as at March 5 and March 19, 2009, respectively. However, these amounts related to sale of shares and production revenue from the Farrow property, another property owned by Deep Creek. There were no funds from Davey Lake production in this account.

#### **Keele Loan**

32. In November 2008, Deep Creek purchased the previous operator's interest in the Davy Lake property. The purchase was financed by a Non-Revolving Bridge Loan with Keele. The amount owed to Keele was \$2.6 million.
33. The security agreement provided Keele with security over all assets, second only to the NBC's fixed and floating security over all the Company's current and future properties. Attached, as Exhibit 13, is a copy of the loan agreement.
34. During the period of November 2008 to March 16, 2009, the Company made various interest payments to Keele. Attached as Exhibit 14 is a copy of the Keele loan statements showing these payments.
35. On March 24, 2009, Keele purchased and assumed NBC's loan.

#### **NBC Loan**

36. NBC was the operating lender for the Company. A copy of the loan documents are attached as Exhibit 15 to this report.

#### **Disallowance of the SemCanada Claim**

37. On July 15, 2009, the Trustee received SemCanada Crude Company's ("SemCanada") proof of claim, which is attached as Exhibit 16 to this report.
38. The claim was reviewed and the Trustee determined that the claim should be disallowed as a trust claim. Attached, as Exhibit 17, is a copy of the disallowance letter sent on July 20, 2009.

39. On July 28, 2009, counsel for SemCanada sent an e-mail advising that SemCanada would appeal the Trustee's disallowance of their claim.
40. On August 5, 2009, all parties agreed to a Consent Order in regard to the disallowance of the SemCanada claim to be heard on September 2, 2009. A copy of the Consent Order is attached as Exhibit 18 to this report.
41. On August 14, 2009, SemCanada's legal counsel sent a letter requesting additional information before the Court Hearing on September 2, 2009. Attached, as Exhibit 19 is a copy of that letter.
42. On August 27, 2009, the Company's legal counsel responded to the request for information, a copy of which is attached as Exhibit 20. The letter advised that information that was considered relevant to the disallowance of their client's claim would be provided in the Trustee's report.
43. A reconciliation of the information requested by the legal counsel to SemCanada to the information and exhibits contained in this report is summarized in Exhibit 21 to this report.
44. On August 27, 2009, the Trustee sent an amended disallowance claim to SemCanada and its legal counsel, advising that the Trustee believed that the Court Order of March 9, 2009 may be a fraudulent preference given the filing of a NOI by Deep Creek on March 19, 2009. A copy of this letter is attached as Exhibit 22.

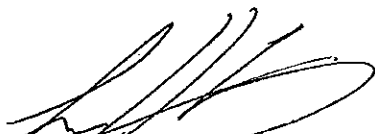
### Conclusion

45. The Trustee has disallowed the Trust claim of SemCanada for the reasons set out in the Notice of Disallowance and Supplemental Notice of Disallowance. If the Trustee's disallowance is upheld, SemCanada's claim will be admitted as an unsecured claim and processed through the proposal as approved by Justice Hawco.

Deep Creek Oil & Gas Inc.  
Trustee's Third Report  
Alger & Associates Inc.  
August 28, 2009

Respectfully submitted on this 28<sup>th</sup> day of August 2009.

Alger & Associates Inc., Trustee

  
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Guy Odhams

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Action No. 25-1179833

2009

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OF ALBERTA  
JUDICIAL DISTRICT OF CALGARY

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IN THE MATTER OF THE PROPOSAL  
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DEEP CREEK OIL & GAS LTD.

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TRUSTEE'S THIRD REPORT -  
DISALLOWANCE OF THE CLAIM OF  
SEMCANADA CRUDE COMPANY  
Volume 1 of 2

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