

Action No. 0901-07221

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

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

AND IN THE MATTER OF MAHALO ENERGY LTD.

ELEVENTH REPORT OF THE MONITOR
ALGER & ASSOCIATES INC.

OCTOBER 12, 2010

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INTRODUCTION

1. On May 21, 2009, Mahalo Energy Ltd. (“Mahalo” or the “Company”) filed a petition pursuant to the provisions of the *Companies’ Creditors Arrangement Act* (“CCAA”) in the Court of Queen’s Bench of Alberta (the “Court”). On May 22, 2009 the Court granted an order (the “CCAA Initial Order”), which, amongst other things, appointed Alger & Associates Inc. (“Alger”) as Monitor (“Monitor”) of Mahalo.
2. The Monitor’s previous reports provided this Honourable Court with information on Mahalo’s affairs, sale of the Company’s assets, updates on Mahalo’s restructuring efforts and applications for extensions of the stay period to October 15, 2010.
3. Copies of certain relevant information related to these proceedings, including the Initial Order, the Petition, the supporting affidavits, the Stay Extension Orders and the Sale Approval and Vesting Order, may be obtained from the Monitor’s website (www.alger.ca/engagements.htm).
4. All defined terms from the Monitor’s previous reports are applicable to this report.
5. The purpose of the Monitor’s Eleventh Report is to provide this Honourable Court with:
 - a. Updated information on Mahalo’s operations since the filing of the Monitor’s Tenth Report;
 - b. Summary of Actual vs. Budgeted Cashflow for the period ending October 1, 2010;
 - c. Projected Cash Flow for the Period ended November 19, 2010;
 - d. Issues that have arisen regarding the completion of the Plan of Arrangement that require an Order from this Honourable Court; and
 - e. The Monitor’s recommendations regarding Mahalo’s seeking of an Order from this Honourable Court.

Limitations of Report

6. The information contained in this report has been obtained from the records of Mahalo and is based upon discussions with and representations made by management.

POST CCAA OPERATIONS

Actual Cash Flow for period ended October 1, 2010

7. Attached as Exhibit 1 is a detailed analysis of Mahalo's actual versus budgeted cash flow for the period ended October 1, 2010. A summary comparison of the actual versus budgeted cash flow for this period is as follows:

Mahalo Energy Ltd. Actual vs. Budgeted Cash Flow For the Period May 22, 2009 to October 1, 2010	Budget	Actual	Difference
Opening Cash on hand	59,798	59,798	-
Cash Receipts	3,676,978	3,507,895	(169,083)
Cash Disbursements	<u>(3,584,604)</u>	<u>(3,554,606)</u>	<u>29,998</u>
Closing Cash on Hand	152,173	13,087	(139,085)

8. The actual cash receipts for the period were less than budgeted primarily because the Alberta Crown Royalty Deposit of approximately \$189,000 was not received.
9. The actual cash disbursements for the period were less than budgeted as professional and consulting fees payments have been deferred until completion of the CCAA Plan of Arrangement.

Expenditure Variances in Excess of Budget Thresholds

10. Pursuant to Clause 26 (b) of the CCAA Initial Order, as amended, line item expenditure variances greater than 10% of the budgeted expenses (15% on a three week average basis) are required to be reported to the Lenders.
11. There were no line item variances in excess of the above thresholds.

Projected Cash Flow for period ending November 19, 2010

12. The Company has prepared a cash flow budget for the period ending November 19, 2010, which is attached as Exhibit "2" to this report. A summary of the cash flow budget for this period is as follows:

Mahalo Energy Ltd.	
Budgeted Cashflow Summary	
Period ending November 19, 2010	
Opening cash on hand	\$13,087
<u>Cash Receipts</u>	
Deposits and Receivable collections	25,000
Gross Over-riding Royalty	10,000
	35,000
<u>Cash Disbursements</u>	
Payroll, Consultants and related	(36,000)
Other G&A	(6,000)
	(41,000)
Closing cash on hand	\$6,087

13. The following are the explanations for the budgeted figures:

Cash Receipts

Deposit receipts: Mahalo anticipates the receipt of \$25,000 from the partial release of the royalty deposit held by the Alberta government.

GORR: Mahalo has retained a GORR on the sale of the Canadian assets sold to the Purchaser.

Disbursements

Payroll, consultants: the payroll and consultants costs reflect the personnel required to help administer the remaining Canadian activities.

Other G&A: costs for external consultants, professionals, rent, and other G&A.

14. Due to the timing of their receipt of the budget to November 19, 2010, the budget has not yet been formally approved by the Lenders. However, it is hoped that formal approval will be received prior to the Court application to extend the CCAA Stay.

Remaining Assets

Deposits

15. The current remaining deposit balance is approximately \$189,000, representing an Alberta Crown Royalty deposit.
16. The Company does not believe that it will receive the full refund of this deposit before the November 19, 2010 expiry of the CCAA stay extension being sought by Mahalo, but believes that it will receive a partial release of this deposit. As referenced above, the Company projects it will be able to fund operations until the closing of the subscription for shares by Alpine as contemplated in CCAA Plan. The Monitor considers this assessment reasonable. Any remaining deposit balances owed are to be assigned to the Lenders under the CCAA Plan.

GORR

17. The GORR retained by the Company from the sale of the remaining Canadian properties will remain with the Company under the CCAA Plan.

Creditor Matters

Pre-CCAA Creditors

18. Various pre-CCAA creditors have contacted the Monitor. All such creditors have been informed of the terms of CCAA Initial Order.
19. Additional creditors that were not included in Mahalo's vendor listings have contacted the Monitor and have been provided with the required information and have also been included in the CCAA claims process.

Post-CCAA Creditors

20. Mahalo has paid all of its operating expenses on a current basis, with the exception of certain professional fees, which fees are covered by the administration charge under the Initial CCAA Order. These fees will be paid from the proceeds of the Investment Agreement under the terms of the Plan of Arrangement.

CCAA PLAN OF ARRANGEMENT

Sanction Order

21. On September 16, 2010, this Honourable Court granted the Sanction Order being sought by the Company in order to complete the CCAA Plan of Arrangement.

Investment Agreement Closing Issues

22. Since the obtaining of the Sanction Order on September 16, 2010, various issues have arisen with respect to the completion of the Investment Agreement and related Plan of Arrangement. The following are relevant excerpts from the October 12, 2010 affidavit of David Burton, Mahalo's President and CEO, a copy of which will be posted at www.alger.ca, regarding these issues:
 - a. In recent discussions, certain of the Regulatory Authorities have advised Mahalo's corporate counsel that they will not grant the CTO Revocation Orders, or the Non-

Reporting Issuer Order, until such time as Mahalo has issued Class A shares and Class B shares and redeemed its common shares all in accordance with the terms of the Investment Agreement and the Plan. Accordingly, the condition precedent found at Article 6.1(p) of the Investment Agreement cannot be met prior to closing.

- b. The position taken by the Regulatory Authorities creates a circular problem as follows:
 - i. The Regulatory Authorities will not grant the CTO Revocation Orders and the Non-Reporting Issuer Order without Mahalo issuing its new classes of shares and redeeming its common shares;
 - ii. Mahalo will not issue the Class A shares to Alpine and the Other Investors without receiving the Subscription Price from Alpine; and
 - iii. Alpine will not advance the Subscription Price without the Regulatory Authorities issuing the CTO Revocation Orders and the Non-Reporting Issuer Order.
- c. Mahalo and Alpine have agreed to solve this problem by closing the Investment Agreement in escrow. Alpine will advance the Subscription Proceeds and Mahalo will issue the Class A shares and these proceeds and shares will be held in escrow by the escrow agent pending receipt of the CTO Revocation Orders and the Non-Reporting Issuer Order.
- d. If for any reason the Regulatory Authorities do not grant these Orders, the Subscription Price will be returned to Alpine, and the Class A shares will not be delivered. The precise terms of the escrow arrangement are contained in the draft Escrow Agreement attached as Exhibit A to the October 12, 2010 affidavit of David Burton.
- e. The Regulatory Authorities have not offered any guarantee or assurance that they will grant the CTO Revocation Orders and/or the Non-Reporting Issuer Order - even after Mahalo issues its new classes of shares and redeems its common shares. However, based upon the advice received from counsel, Mahalo has no reason to believe that these Orders will not be forthcoming once these steps have occurred. Mahalo also

believes that closing the Investment Agreement in escrow is the only viable option to allow it to finish implementing its Plan. The Monitor concurs with this position.

- f. In the event the Regulatory Authorities do not grant the Orders requested, there will be no possibility of any transaction that monetizes Mahalo's tax attributes for the benefit of its creditors. Mahalo will either be wound up or further advice and directions will be sought to realize upon any remaining assets for the benefit of the Lenders (i.e. there will be no recovery for unsecured creditors in this event).

Seeking of Order

23. In order to complete the above closing of the Investment Agreement in escrow Mahalo is seeking an Order from this Honourable Court permitting:
 - a. Mahalo and Alpine to close the Investment Agreement in escrow on the terms and conditions set out in the Escrow Agreement attached as Exhibit A to the October 12, 2010 affidavit of David Burton (the "Escrow Agreement"); and
 - b. Mahalo to be able to redeem the Class A shares issued to Alpine and the Other Investors in accordance with the terms of the Escrow Agreement, notwithstanding s. 36(2) of the *Business Corporations Act*, R.S.A. 2000, c. B-3, as amended.

Plan of Implementation

24. Subject to the Order being granted by this Honourable Court and the fulfillment or waiver of the conditions contained in the Escrow Agreement, Mahalo will implement the CCAA Plan in accordance with its terms.

EXTENSION OF STAY PERIOD

25. The current stay period expires on October 15, 2010 and Mahalo will be applying for a further extension to November 19, 2010. The extension is necessary for Mahalo to:
 - Obtain the Orders outlined above;

- Close the Investment Agreement in escrow;
 - Fulfill the terms of the Plan of Arrangement.
26. Mahalo has continued to act in good faith and with due diligence to work on a restructuring plan to the benefit of its creditors and shareholders.

Recommendation

27. The Monitor is of the opinion that an extension of the stay period is appropriate in the circumstances and recommends that the Court grant the extension of the stay to the November 19, 2010 date contained in Mahalo's application and further that the Court grant the Order required to allow Mahalo to complete the closing of the Investment Agreement in escrow.

Respectfully submitted on this 12th day of October, 2010.

Alger & Associates Inc.

In its capacity as Court Appointed Monitor of
Mahalo Energy Ltd., and not in its personal capacity.



Per: Guy W.L. Odhams
Senior-Vice President

Mahalo Energy Ltd. Cash Flow Budget vs. Actual,
Canadian Operations during CCAA process May 22, 2009 to October 1, 2010

EXHIBIT 1

In Canadian \$

	<u>Cumulative</u>		<u>Variance</u>	
	<u>Budget</u>	<u>Actual</u>	<u>In \$'s</u>	<u>% of budget</u>
Opening Cash on hand	\$ 59,798	\$ 59,798	\$0	0.0%
Canadian Revenue				
GORR Revenue	68,634	51,634	(\$17,000)	-24.8%
Anticipated cash receipt	1,267,288	1,115,205	(\$152,083)	-12.0%
Repayment to Ableco	(256,080)	(256,080)	\$0	0.0%
	-	-		
Production Revenue	315,102	315,102	\$0	0.0%
US receipts	75,324	75,324	\$0	0.0%
	-	-		
Operating Disbursements				
Transaction Costs of Canadian Sale	(100,526)	(100,526)	\$0	0.0%
ERCB Issues	(41,693)	(41,693)	\$0	0.0%
Saskatchewan Environment	(47,299)	(47,299)	\$0	0.0%
Operating Expense	(201,114)	(201,114)	\$0	0.0%
Power prepayment	-	-	\$0	0.0%
	-	-		
Net Revenue	1,079,636	910,552	(\$169,083)	-15.7%
	-	-		
G&A Disbursements				
Canadian Rent	(225,357)	(223,034)	\$2,323	-1.0%
Canadian Payroll and consultants	(1,474,207)	(1,429,295)	\$44,912	-3.0%
Canadian Benefits	(86,593)	(86,593)	\$0	0.0%
Listing fee	(7,875)	(7,875)	\$0	0.0%
Travel	(143,269)	(143,269)	\$0	0.0%
Meals and entertainment	(19,807)	(19,807)	\$0	0.0%
Stationary	(12,007)	(12,007)	\$0	0.0%
Communication	(57,814)	(59,076)	(\$1,262)	2.2%
insurance (assumed paid in USA)	(23,415)	(22,615)	\$800	-3.4%
Computer license rentals	(32,180)	(32,292)	(\$112)	0.3%
Severance/Vacation Pay	(6,000)	(6,000)	\$0	0.0%
Bank Fees	(2,792)	(2,668)	\$124	-4.4%
Other G&A	(113,071)	(120,525)	(\$7,454)	6.6%
Total Disbursements	\$ (2,204,387)	\$ (2,165,056)	\$39,331	-1.8%
Total Cashflow before Management Fee	\$ (1,124,752)	\$ (1,254,504)	(\$129,752)	11.5%
Management fee	1,950,631	1,950,631	\$0	0.0%
Professional Fees:				
Tax return preparation	(12,604)	(13,578)	(\$974)	7.7%
2009 audit	(66,904)	(64,904)	\$2,000	-3.0%
US counsel retainer	-	-	\$0	0.0%
corporate transaction costs	(45,000)	(45,000)	\$0	0.0%
BDP				
Retainer	-	-		
Fees (\$250,000 less Retainer of \$85,000)	(309,410)	(298,238)	\$11,172	-3.6%
Alger				
Retainer	-	-		
Fees (\$160,000 less retainer of 35,000)	(299,587)	(321,118)	(\$21,531)	7.2%
Cash on Hand	\$ 152,173	\$ 13,087	\$ (139,085)	-91.4%

Mahalo Energy Cash Flow Budget

EXHIBIT 2

(CD \$'s except for unit data)	Week ending								Totals
	10/1/10	10/8/10	10/15/10	10/22/10	10/29/10	11/5/10	11/12/10	11/19/10	
Canadian revenue			5,000					5,000	10,000
Collection of receivables									-
Royalty Deposit						25,000			25,000
ERCB deposit									-
Other									-
Operating Disbursements									-
Operating Expense									-
Canadian Rent						(6,000)			(6,000)
Canadian Payroll & consultants			(18,000)				(18,000)		(36,000)
Canadian Benefits									-
Securities Commissions									-
Travel									-
Meals and entertainment									-
Stationary									-
Communication									-
Insurance									-
Computer license rentals									-
Severance/Vacation pay									-
Bank fees									-
Other G&A									-
Sub-total operating disbursements	-	-	(18,000)	-	-	(6,000)	(18,000)	-	(42,000)
Management fee									
Professional Fees:									
2010 Audit									-
2009 Tax Return									-
Corporate Transaction costs/retainers									
BDP									-
Alger & Counsel									-
Cash required	-	-	(13,000)	-	-	19,000	(18,000)	5,000	(7,000)
Cash on Hand - Opening	13,087	13,087	13,087	13,087	87	87	87	1,087	13,087
Cash on Hand - Closing	13,087	13,087	87	87	87	19,087	1,087	6,087	6,087

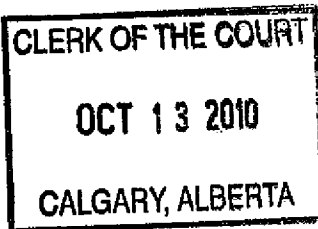
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