

Action No. 1003 05560
Bankruptcy Action No. 24-115359

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

IN THE MATTER OF THE
BANKRUPTCY AND INSOLVENCY ACT,
R.S.C. 1985, c. B-3, AS AMENDED

AND THE
COMPANIES' CREDITORS ARRANGEMENT ACT,
R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR
ARRANGEMENT OF COW HARBOUR CONSTRUCTION LTD.

SEVENTH REPORT TO THE COURT
SUBMITTED BY DELOITTE & TOUCHE INC.
IN ITS CAPACITY AS MONITOR

May 27, 2010

INTRODUCTION AND PURPOSE OF THIS REPORT

1. On April 7, 2010, Cow Harbour Construction Ltd. ("CHC" or the "Company") filed and obtained protection from its creditors under the *Companies' Creditors Arrangement Act* ("CCAA") pursuant to an Order rendered by this Honourable Court (the "Initial Order").
2. The Initial Order provides, inter alia, for the following:
 - a. No proceeding or enforcement process in any court or tribunal shall be commenced or continued against or in respect of the Company or its property, or affecting the Company's business operations and activities until and including May 3, 2010 (the "Stay Period").
 - b. All persons having agreements with the Company for the supply of goods and services must continue to provide goods and services in the normal course of business.
 - c. No person shall discontinue, fail to honour, alter, interfere with, repudiate, resiliate, cancel, terminate or cease to perform any right, renewal right, contract, agreement, license or permit in favour of or held by the Company, except with the written consent of the Company and the Monitor, or with leave of the Court.
 - d. The appointment of Deloitte & Touche ("Deloitte") as monitor of the Company under the CCAA.
3. On April 29, 2010, the Court rendered a judgment extending the Initial Order and the Stay Period until May 21, 2010.
4. On May 21, 2010, the Court rendered a judgment extending the Initial Order and the Stay Period until June 4, 2010.

5. This Report (“Seventh Report”) covers:
 - a. Update on the Syncrude contract and potential impact on future revenues.
 - b. Fleet equipment maintenance issues.
 - c. Update on the Chief Restructuring Advisor contract terms.
 - d. Funds segregated in accordance with paragraph 10 of the Order dated May 21, 2010.

6. In preparing this Report, the Monitor has relied upon unaudited interim financial information, the Company’s records and discussions with management of the Company, their financial and legal advisors, and Syncrude’s representatives. While the Monitor has reviewed the information, some in draft format, submitted in the abridged time available, the Monitor has not performed an audit or other verification of such information.

7. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars. Capitalized terms not defined in this Report are as defined in the previous reports of the Monitor.

8. Copies of the Monitor’s Reports, including a copy of this Seventh Report, the motion record in this CCAA Proceeding and further reports of the Monitor will be available on the Monitor’s website at www.deloitte.com/ca/cowharbour. The Monitor has also established a toll free telephone number that is referenced on the Monitor’s website so that parties may contact the Monitor if they have questions with respect to the Company’s restructuring or the CCAA.

CONTRACT WITH SYNCRUDE

9. As previously mentioned by the Monitor, and as shown on the Updated Cash Flow Statement attached to the Monitor’s Fifth Report, Syncrude represents the sole source of revenues for the period between May 15 and October 1, 2010, with monthly revenues varying between \$14.65 million and \$15.65 million. Revenues are obtained from two mine sites, referred to as the Aurora site and the Base Mine site.

10. On May 21, 2010, the Monitor's Sixth Report was filed in order to advise this Honourable Court that there was rumored that Syncrude may have curtailed the overburden removal contract work being performed by CHC on Syncrude's Aurora site.
11. As outlined in the Monitor's Sixth Report, the Monitor advised this Honourable Court that we would follow this matter closely and report to this Honourable Court as soon as we had relevant information from CHC's management and Syncrude. In order to get clarification on the Syncrude situation, we held various discussions with Mr. Adrian Lake, Contract Manager at Syncrude. A summary of these discussions is included in the following paragraphs.

Summary of discussions with Syncrude

12. Syncrude confirmed that they are still working with the Company on an ongoing basis. For example, reclamation work is still ongoing at the Base Mine site. The reason Syncrude curtailed the overburden removal contract work is because, for the time being, they now have the required level of exposed oil sands. Neither safety issues involving the Company nor the quality of their work were factors.
13. Mr. Lake confirmed that it is difficult to do mid-term and even short-term planning in the type of business CHC is in. At this time, there is no overburden removal type work scheduled to be completed by a subcontractor at the Aurora site, but the situation could change within the next month. However, as mentioned in our Sixth Report, there is also a possibility that all overburden removal type work going forward could be completed by Syncrude with their own equipment.
14. It is our understanding that the Contract Mining Services contract signed in November 2009 between Syncrude and the Company (the "Contract") does not guarantee minimum monthly revenues. The Contract states that the maximum contract value is approximately \$440 million over five years. Total revenues based on this contract could be less, or it could be higher, depending on Syncrude's needs in the future. Mr. Lake confirmed that any overburden removal or reclamation work to be completed at the Aurora site by the Company will be done in accordance with the Contract.
15. As it relates to special projects not covered by the Contract, the Company needs to submit a bid the same way as any other company providing services. In order to obtain these special projects,

the Company needs to meet various conditions, one of which is a financial stability condition. Based on our discussions, Syncrude did not confirm that meeting the financial stability condition is precluded given that the Company is currently under CCAA. Syncrude maintains that the Company is still required to allow Syncrude to review financial information to allow for assessment of the Company's financial stability condition.

16. Based on information received from Syncrude, the Company has approximately \$35 million of approved release orders as at May 21, 2010. In essence, from discussions with Syncrude, we understand this to mean that the Company has approved orders (similar to an order book) at this time, which could allow them to generate future revenues for the period between May 22, 2010 and December 31, 2010, to an approximate maximum of \$35 million. As mentioned before, when Syncrude approves a release order, it does not mean that the Company is guaranteed to generate revenues equal to the total value of the approved release order. However, the release order could subsequently be increased if Syncrude needs additional services from the Company. These adjustments are frequent in this type of business and the Company's management confirmed that they are currently having discussions with Syncrude in order to get additional revenues from outstanding approved release orders.
17. Based on the above, it is difficult for the Company to prepare a cash flow projection, with substantial support confirming the reasonableness of the projections. However, at this time and based on the recent information received by the Monitor, we have requested that the Company prepare an amended cash flow projection with more conservative assumptions.
18. It is the Monitor's intention to meet with the CFO and the CEO of the Company in order to prepare this amended cash flow and report to this Honourable Court before June 4, 2010.

FLEET EQUIPMENT MAINTENANCE

19. On May 25, 2010, the Monitor was advised that Ground Force Mechanical & Rental Services ("Ground Force"), who were acting as a maintenance sub-contractor for the Company, were asked to leave Syncrude's Aurora site. The Monitor's understanding is that Ground Force was handling various maintenance tasks for the Company and more specifically, the maintenance on the shovels.

20. Considering that fleet maintenance is a sensitive issue for lessors, the Monitor held various discussions with representatives of the Company, Ground Force, and Syncrude. Based on those discussions, our understanding is as follows:

- a. Various meetings and discussions took place over the past few weeks concerning the safety performance of Ground Force at the Syncrude Aurora site. It is our understanding that Ground Force was removed from the Syncrude Aurora site for repeated safety infractions.
- b. In order to reinstate Ground Force on the Syncrude Aurora site, the Company and Ground Force had to implement various safety measures.
- c. Those safety measures were reviewed by Syncrude representatives and were subsequently approved (the "Approved Safety Measures"), which enabled Ground Force to go back to work for the Company at the Syncrude Aurora site.
- d. On May 25, 2010, representatives of the Company requested that Ground Force leave the Aurora site immediately because they believed that the Approved Safety Measures were not being adhered to. According to the Company's representatives, this action was necessary in order to avoid any shutdown of CHC's operations by Syncrude due to the violation of the Approved Safety Measures.
- e. Ground Force's representative is of the opinion that they did follow the Approved Safety Measures and do not understand why they were requested by the Company to leave the Aurora site.
- f. Syncrude's representatives confirmed to the Monitor that the removal of Ground Force from the Aurora site was requested by the Company. This was not a decision made by Syncrude. According to the representative of Syncrude, Ground Force is still an approved sub-contractor by Syncrude and, consequently, can return to the Aurora site upon request of the Company.

21. The Monitor is raising this matter because the fleet maintenance is an important consideration, and Ground Force was taking an active part in the fleet maintenance activities, and more specifically, on the maintenance of the shovels.
22. The Monitor had a discussion with Mr. Wally Herritt, General Manager of Maintenance at CHC, in order to determine who will complete the maintenance work, which Ground Force has completed in the past. Based on this discussion, Mr. Herritt believes that the Company has employees who can perform this type of work.
23. At this time, the Monitor does not have information that would cause us to believe that the Company will not be able to handle the fleet maintenance work, which was previously performed by Ground Force, especially if we consider the reduction of the level of activity due to the absence of overburden removal work at this time.

UPDATE ON THE CHIEF RESTRUCTURING ADVISOR CONTRACT TERMS

24. At the April 7, 2010 Court Hearing, the Court requested the Monitor to report on the compensation terms of the Advisor.
25. Paragraphs 7 to 9 of the Monitor's Third Report provided particulars as to the Advisor's contract terms. Paragraph 9 of the Monitor's Third Report states, "In summary, it would appear that if the Company successfully restructures under the *Companies' Creditors Arrangement Act*, the Advisor will receive considerable contingent compensation, whereas if the Company is unsuccessful in its restructuring efforts, the Advisor's fees will be restricted to the daily work fee."
26. At the time of preparing the Monitor's Third Report (April 26, 2010), the Company's sales were robust and the prospects of refinancing of the Company or obtaining of equity were positive. However, in recent weeks there has been a dramatic reduction in revenues, thus refinancing or equity injections appear less likely. Accordingly, a process has been commenced to facilitate a possible sale of the Company's assets. In doing so, a sales committee composed of representatives from various lenders, the Company and the Advisor was formed.

27. The sales committee recommends retaining Ernst & Young Corporate Finance (Canada) Inc. ("E&Y") to assist with the sales process. In addition, the Monitor will provide support in preparing and managing documents, to assist with the sales process. Ordinarily, many of these activities would be performed by the party retained to lead the sales process, which, in this case, is the Advisor. However, it is recognized that as an individual practitioner, the Advisor has limited direct resources and, as such, the Monitor supports the ancillary services being provided by E&Y or some other party on a limited basis.
28. Counsel for one of the significant creditors provided the Monitor's counsel with an email stating, "...is fine with EY on the terms discussed as amongst them and Pat Ross (i.e. limited involvement and Edmonton Rates)." The Monitor has not received input from other creditors regarding their position on retaining E&Y (except those forming the sales committee).
29. Given the reduced revenues of the Company in recent weeks, it may be that the sales process results in what effectively is an orderly disposition of the assets rather than the sale of the Company en bloc, including its management structure. Regardless, the Monitor is of the opinion that the sales process recommended by the sales committee using the protection afforded by the Initial Order provides an opportunity to maximize realizations for the Company and its creditors. This process permits the Company to continue to operate during the sales process, thus making it more appealing to prospective purchasers.
30. On May 25, 2010, the Monitor sent an email (Appendix A) to the Advisor seeking clarification as to how recent events might affect the Advisor's contingent compensation. The reason being that if the CCAA process is used to facilitate an orderly disposition of the Company's assets, it would be informative for interested parties to know how this impacts the Advisor's success fees.
31. Point 1 of Appendix A requests the Advisor to provide a quote as to E&Y's estimated fees. On May 27, 2010, the Advisor provided the Monitor with an email that states, "After reviewing what work has been done by Deloitte, Aroon [E&Y partner] has estimated that it will cost from 250k to 400k for his services." Given that, in conjunction with monitoring activities, the Monitor will perform many of the divestiture tasks such as obtaining and organizing the necessary information, preparing the confidential information summary, managing the due diligence process and certain aspects of the closing process, and that the Advisor is being paid \$2,000 per day for his activities, including divestiture services, the Monitor's initial thoughts are that the E&Y fee estimate of \$250,000 to \$400,000 is high, particularly given our impression that E&Y was to be providing

"limited involvement." The Advisor previously indicated to the Monitor that E&Y's fees would be approximately \$50,000 to provide limited services, which is consistent with the Monitor's senior corporate finance team's understanding of what is required. We recommend that the Advisor provide a detailed work plan that specifically identifies each task to be performed by the Advisor, the Monitor and E&Y so that interested parties can better appreciate the quantum of fees that might be expected in the sales process.

32. Point 2 of Appendix A requests that the Advisor to clarify that E&Y's fees will be borne out of the Advisor's contingent compensation if the Advisor receives contingent compensation and these fees will be borne by the Company if the Advisor does not receive contingent compensation. Paragraph 8 (iii) of the Advisor's draft First Report to the Court provided to the Monitor on May 26, 2010 confirms this to be the case.
33. Point 3 of Appendix A raises a concern in that should the Advisor receive contingent compensation, the \$2.0 million administration charge per paragraph 34 of the Initial Order would be insufficient to protect amounts owing to the Applicant's counsel, the Monitor, counsel to the Monitor and the Advisor. Thus, for example, if the assets sell for \$250 million, the contingent compensation to the Advisor alone would be \$3.0 million ($\$250 \text{ million} \times 1\% + \$500,000$). The Monitor was previously advised indirectly that the Advisor would allow his contingent component of his fees (i.e., not the daily work fees) to rank behind the entitlement of the other parties. The Advisor has since indicated he is unwilling to do so and that he expects his fees would participate equally. This has caused concerns amongst the Applicant's counsel, the Monitor and counsel to the Monitor as fee arrangements of these parties do not enjoy significant potential contingent compensation in addition to the hourly base fees. The Monitor's counsel is reviewing this matter and will provide further direction to the Monitor.
34. Point 4 of Appendix A requests the Advisor to provide his position on his success fee entitlement if the sales process results in what is effectively an orderly disposition of assets under the CCAA (e.g., piece meal or liquidation scenarios). The Advisor has not responded to this request. The Monitor's reading of the Advisor's March 24, 2010 contract with the Company is that the Advisor might very well be entitled to contingent compensation in this scenario. Thus, for example, if the assets are disposed of by way of an auction under the CCAA for \$200 million, the contingent compensation to the Advisor would be \$2.5 million ($\$200 \text{ million} \times 1\% + \$500,000$). The net

effect being that, under the CCAA, the Advisor is guaranteed significant contingent compensation regardless as to how assets are disposed of.

35. The Court has not requested the Monitor to recommend what might be a reasonable fee for the Advisor given the recent changes in events and the proposed plans of the sales committee, but the Monitor would be willing to do so, if requested.

**FUNDS SEGREGATED IN ACCORDANCE WITH PARAGRAPH 10 OF
THE ORDER DATED MAY 21, 2010**

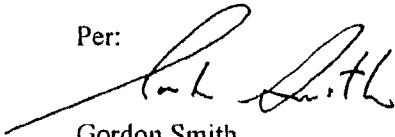
36. At the May 21, 2010 Court Hearing, it was directed that the Monitor should segregate in trust with its counsel, monthly payments from April 1, 2010 which would have been required to be paid by CHC to lessors under:
 - a. those leases in which there the Monitor's counsel has categorized as true leases; and
 - b. those leases which the Monitor's counsel has not been able to categorize as either capital leases or true leases.
37. The Monitor's counsel shall hold such funds in trust pending determination of entitlement thereto under Section 11.01 of the CCAA by Court Order.
38. In accordance with the above, a total amount of \$2,374,770 was transferred to the Monitor's counsel on May 27, 2010. This amount represents the total obligations under the various leases described in Appendix B established by the Company for the period between April 1, 2010 and May 18, 2010.
39. It is the Monitor's intention to request CHC to continue transferring ongoing obligations under these leases to the Monitor's counsel in trust, until the categorization of these leases are finalized.

The Monitor respectfully submits to the Court this, its Seventh Report.

Dated at Edmonton, this 27th day of May, 2010

Deloitte & Touche Inc.
in its capacity as Monitor of
Cow Harbour Construction Ltd.

Per:

A handwritten signature in black ink, appearing to read "Gordon Smith". The signature is written in a cursive style with a long, sweeping underline that extends to the left.

Gordon Smith
Senior Vice-President

Appendix A

Smith, Gordon (CA - Edmonton)

From: Smith, Gordon (CA - Edmonton)
Sent: Tuesday, May 25, 2010 2:03 PM
To: 'Pat Ross'
Cc: 'Chuck Russell'; Mike McCabe; Franco, Martin (CA - Montreal)
Subject: Cow Harbour Construction Ltd.

Pat as discussed yesterday our report to the Court for purposes of the May 28, 2010 Hearing will include an update to our Third Report wherein we will, amongst other matters, comment on the Chief Restructuring Advisor Contract Terms. In order to do so can you respond to the following:

1. Please have Ernst & Young ("E&Y") provide us with a quote as to how much they anticipate their fees will be for the services they are providing. Our reason for this request is that one of the creditors and one of the lawyers involved are sensitive to the fees. Previously you indicated that the E&Y fees would approximate \$50,000 and that is the amount of their requested retainer in their May 18, 2010 letter to you (which is based on hourly fees of \$375 to \$650 per hour, depending on the service provider). Also based on my prior discussion with you, you indicated that this should be sufficient for all of their costs, but I just want to make sure. I do note that page 36 of E&Y's draft May proposal indicates a success fee of 0.25% of the transaction value plus hourly fee charges of \$350 to \$550 per hour (depending on the service provider) however I think this proposal was prepared before the May 18, 2010 letter and simply provided by you for information purposes for yesterday's conference call.
2. During yesterday's conference call you indicated that E&Y's fees will be applied to your success fees, assuming there is a successful restructuring. In the event you do not receive success fees then E&Y's fees will not come out of your fee entitlement (as you will not receive success fees) but rather will be paid directly by Cow Harbour. Please confirm if this is the case.
3. Paragraph 34 of the Initial Order provides for a \$2 million administration charge to secured indebtedness owing to the Applicant's counsel, the Monitor, counsel to the Monitor and the Advisor. This charge appears to be sufficient to satisfy the hourly and daily rate fees of all applicable parties. However in the event there is a sale of the company resulting in success fees to you, then this charge will probably not be sufficient. We expressed this concern to Don MacLean who advises us that you are agreeable that the hourly fees owing to the Applicant's counsel, the Monitor and counsel to the Monitor and the Advisor's daily fee of \$2,000 would rank in priority to any fee success fee entitlement that you would be entitled to. I need you to confirm directly with me that you are in agreement with your success fees ranking behind the noted hourly fees of the Applicant's counsel, the Monitor and counsel to the Monitor and the Advisor's daily fees (\$2,000 per day).
4. Paragraphs 7 to 9 of our Third Report comment on the contract terms of the Advisor. In paragraph 9 we state "...that if the Company successfully restructures under the Companies' Creditors Arrangement Act, the Advisor will receive considerable contingent compensation, whereas if the Company is unsuccessful in its restructuring efforts, the Advisor's fees will be restricted to the daily work fee.". At the time of preparing the Third Report (April 26, 2010), the Company had a rather robust revenue stream such that the likely restructuring efforts were refinancing or a going concern sale to a third party. Recent events such as reduced revenue concerns may affect the going concern sales ability. However the sales process we are undertaking might cause an orderly disposition of assets on a piece meal basis or an outright sale of assets by way of an auction wherein the CCAA process is used to facilitate these other alternatives. What I need from you is your position as to whether you take the position that you are entitled to your success fee structure regardless of the sale process, assuming the CCAA process is used to facilitate the transaction (e.g. in an orderly disposition of assets or an auction). My point being that I need to further elaborate what was meant by "successfully restructures" in our Third Report.

As we need to report to the Court soon, an answer to the above questions by the end of today would be appreciated. If you require clarity as to what I am seeking please call me. Thanks.

Gordon Smith
Partner | Financial Advisory
Deloitte
2000 Manulife Place, 10180 - 101 Street, Edmonton, AB T5J 4E4

Appendix B

APPENDIX B

SUMMARY OF DISPUTED LEASES

Effective date of stay of proceedings	1-Apr-10	Post filing
Lessor	Monthly Payment	Accrual up to May 18, 2010
	\$	\$
Caterpillar Financial (AIG)	21,372.84	32,403.98
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Caterpillar Financial	28,397.86	43,054.82
AIG Commercial Equipment	160,185.00	170,519.52
De Lage Landen Financial Services	150,000.00	387,096.77
Scott Capital Group Inc.	10,469.00	15,872.35
Scott Capital Group Inc.	18,183.33	27,568.27
Scott Capital Group Inc.	5,295.00	5,807.42
Scott Capital Group Inc.	16,717.20	25,345.43
Finning (Canada)	90,000.00	112,258.06
Finning (Canada)	90,000.00	100,258.06
Finning (Canada)	90,000.00	106,258.06
Finning (Canada)	90,000.00	106,258.06
Finning (Canada)	160,000.00	226,236.56
Finning (Canada)	160,000.00	226,236.56
Finning (Canada)	160,000.00	146,236.56
Finning (Canada)	160,000.00	130,236.56
Finning (Canada)	160,000.00	114,236.56
Finning (Canada)	50,000.00	55,698.92
Finning (Canada)	50,000.00	70,698.92
Finning (Canada)	88,000.00	130,296.77
Wajax Industries	16,500.00	25,016.13
Wajax Industries	30,000.00	45,483.87
Wajax Industries	40,000.00	23,225.81
Scott Capital Group Inc.	7,190.00	10,900.97
Heavy Metal Equipment Rentals (Dutchmen Equipment)	20,000.00	5,161.29
	<u>1,893,683.07</u>	<u>2,374,770.30</u>

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