

# Management's Discussion and Analysis (“MD&A”)

The following discussion and analysis of Enerchem International Inc. (“Enerchem” or the “Company”) for the year ended December 31, 2009 should be read in conjunction with the audited annual consolidated financial statements, including the accompanying notes and supplemental material contained in the Company’s Annual Report and the Annual Information Form. This MD&A focuses on key statistics from the financial statements of the Company and pertains to known risks and uncertainties relating to the oilfield services industry in the Western Canadian Sedimentary Basin (“WCSB”) where the Company operates. This discussion should not be considered all inclusive, as it excludes unanticipated changes that may occur in general economic, political, environmental and industry conditions. Additional information relating to the Company is available on the System for Electronic Document Analysis and Retrieval (“SEDAR”) at [www.sedar.com](http://www.sedar.com) and the Company’s website at [www.enerchem.com](http://www.enerchem.com). This MD&A was prepared effective March 9, 2009.

## Forward Looking Statements

Certain statements contained in this MD&A constitute forward-looking statements. These statements relate to future events or future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "target", "intend", "could", "might", "should", "believe" and other similar expressions. These statements speak only as of the date of this MD&A and the Company does not undertake to publicly update these forward-looking statements except in accordance with applicable securities laws. In particular, this MD&A contains forward-looking statements pertaining to the following:

- crude oil and natural gas production levels;
- projections of market prices and costs;
- projections of crude oil and natural gas industry activity levels, including drilling activity and the type of drilling activity in the WCSB;
- expectations of cash flows and the Company’s ability to finance its operating activities;
- expectations of EBITDA;
- expectations of sources of funds to fund future capital expenditures;
- the ability to operate efficiently and profitably;
- the effect of the global financial crisis on the business;
- expectations of future current ratios for the Company
- the necessary annual return on average capital employed to maintain cost of capital at economic levels;
- expected changes of management information systems and processes and the effect on future operations;
- the effect of management's just-in-time approach to inventory management on future margins;
- expectations of financial results and sales volumes in 2010;
- timing and length of the annual plant shut down;
- the Company’s 2010 capital expenditure program;
- supply and demand for the Company’s products and services; and
- general political and economic circumstances.

Readers are cautioned that the foregoing list is not exhaustive. Forward-looking statements or information are based on a number of factors and assumptions which have been used to develop such statements and information but which may prove to be incorrect. Although management of the Company believes that the expectations reflected in such forward-looking statements or information are reasonable, undue reliance should not be placed on forward-looking statements

because the Company can give no assurance that such expectations will prove to be correct. In addition to other factors and assumptions which may be identified in this document, assumptions have been made regarding: activity in the WCSB; the general stability of the economic and political environment; the effect of market conditions on demand for the Company's products and services; the Company's policies with respect to acquisitions; the ability to obtain qualified staff, equipment and services in a timely and cost efficient manner; the ability to operate the Company's businesses in a safe, efficient and effective manner; the performance and characteristics of various business segments; the effect of current plans; the timing and costs of pipeline, storage and facility construction and expansion; future oil and natural gas prices; currency, exchange and interest rates; the regulatory framework regarding royalties, taxes and environmental matters in the jurisdictions in which the Company operates; and the ability of the Company to successfully market its products and services.

The actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth under the section entitled "Risk Factors" in the Annual Information Form for the year ended December 31, 2009 and later in this MD&A. The Annual Information Form and the Annual Report are available on SEDAR at [www.sedar.com](http://www.sedar.com).

## Financial Highlights

<b>Results of Operations</b> (\$ thousands except per share amounts)	For the years ended December 31		
	<b>2009</b>	2008	2007
Revenues	<b>105,471</b>	115,797	80,300
Net loss for the year	<b>(30)</b>	(1,901)	(4,481)
Net loss per share			
Basic	<b>0.00</b>	(0.13)	(0.29)
Diluted	<b>0.00</b>	(0.13)	(0.29)
EBITDA <sup>(1)</sup>	<b>1,242</b>	2,398	4,073
EBITDA per share <sup>(2)</sup>	<b>0.08</b>	0.16	0.27
<b>Financial position</b>			
Total assets	<b>72,533</b>	63,338	64,926
Working capital <sup>(3)</sup>	<b>17,780</b>	13,915	15,991
Purchase of property, plant and equipment	<b>1,205</b>	4,134	9,118
Total bank indebtedness	<b>368</b>	3,448	-
Shareholders' equity	<b>49,590</b>	49,597	51,844
Number of shares (thousands)			
Outstanding, end of year	<b>15,007</b>	15,027	15,253
Average, during the year <sup>(4)</sup>	<b>15,171</b>	15,177	15,293

(1) EBITDA is a non-GAAP measure and is defined below under the Section "Use of Non-GAAP Measures" in this MD&A.

(2) Calculated as EBITDA divided by the basic weighted average number of shares outstanding during the year.

(3) Calculated as current assets less current liabilities.

(4) Represents the weighted basic average number of shares outstanding during the year.

## Use of Non-GAAP Measures

This MD&A contains references to certain financial measures that do not have any standardized meaning prescribed by Canadian Generally Accepted Accounting Principles (“GAAP”), and may not be comparable to similar measures presented by other companies. These measures are provided to assist investors in determining the Company’s ability to generate cash from operations and to provide additional information regarding the use of its cash resources. These financial measures are identified below:

- Cash provided by operations is derived from the Company’s consolidated statement of cash flows and represents cash provided by operating activities before changes in non-cash components of working capital. Cash provided by operations is provided as supplemental information because management believes it provides investors with additional information regarding the Company’s ability to generate funds to finance operations and its capital requirements.
- EBITDA represents earnings from operations before interest expense, taxes, depreciation, amortization, accretion expense, and write-downs. It is used by management internally to measure the performance of the business as a whole. EBITDA is presented as supplemental information because management believes it is a widely used financial indicator of the Company’s operating profitability and performance before the effects of capital investment and financing decisions.
- EBITDA per share represents EBITDA divided by the basic weighted average common shares outstanding.

Cash provided by operations (\$ thousands)	For the years ended December 31	
	2009	2008
Cash provided by operations	5,734	2,895
Deduct: Changes in non-cash components of working capital	1,098	3,891
Net cash provided by (used in) operating activities	4,636	(996)

EBITDA (\$ thousands)	For the years ended December 31	
	2009	2008
EBITDA	1,242	2,398
Deduct (add): Amortization	2,600	2,508
Interest	15	107
Loss on write-down of plant equipment	-	2,129
Income taxes	(1,343)	(445)
Net loss	(30)	(1,901)

## Overview of the Company’s Operations

Enerchem fractionates and distributes hydrocarbon fluids designed for use in the fracturing (FracSol™) and drilling (DrillSol™) of crude oil and natural gas wells as well as solvents (WaxSol™) used to resolve production and processing problems for downstream producers. The Company’s energy marketing group purchases crude oil and crude derived fractions for the Company’s feedstock requirements and for resale. Through its wholly owned subsidiary, acquired on May 1, 2006, Millard Trucking Ltd. (“Millard Trucking”), the Company provides fluid transportation and related oilfield services. FracSol™, DrillSol™, and WaxSol™ together will be referred to as “hydrocarbon fluids” or “HCF” throughout this MD&A.

The Company's fractionation facilities are located in Alberta near Sundre and Slave Lake. The Slave Lake Plant is connected to a major pipeline through a Company owned Lease Automatic Custody Transfer system ("LACT") and lateral pipeline and the plant is further pipeline connected to a small producer from whom a portion of its feedstock requirements are met. Millard Trucking is located in the town of Sundre. In addition, the Company maintains finished goods inventory in several locations including a dedicated facility in Grande Prairie, Alberta. The Company's business is conducted principally in Western Canada. The Company's common shares trade on the Toronto Stock Exchange under the symbol "ECH".

The Company's activities are divided into three distinct business segments:

- *Oilfield services*, which represents the manufacture and sale of HCF;
- *Energy marketing*, which represents the purchasing, gathering and marketing of crude oil and crude oil by-products to refiners and other customers; and
- *Transportation services*, which represents the operations of Millard.

The Company's drilling and fracturing fluids are generally used by the crude oil and natural gas industry for deep well drilling and work-over activities that are at well depths greater than 1,850 metres. Enerchem's customers include large multi-national and independent oil and natural gas explorers and producers, as well as smaller independent producers and major, land based drilling contractors with operations in the WCSB. The primary factor influencing demand for the Company's products and services is the level of drilling and work-over activity in the WCSB, which in turn, depends on current and anticipated future oil and natural gas prices and the levels of cash flows allocated by the industry to drilling and work-over activities. Drilling and well service rig counts and drilling rig utilization by depth are leading indicators of anticipated demand for Enerchem's products and services. The following table summarizes average WCSB drilling and well service rig activity and historical commodity prices:

#### Selected Benchmarks<sup>(1)</sup>

	2009	2008	2007
Wells drilled per year (#)	9,351	20,729	19,144
Drilling rig utilization rates (%)	25	47	42
Average rigs utilized by depth			
- less than 1,851 metres (%)	32	36	43
- greater than 1,850 metres (%)	68	64	57
Crude Oil - West Texas Intermediate - year average (US\$ per bbl)	62.28	99.55	72.41
Natural Gas – AECO – year average (Cdn\$ per Mcf)	4.07	8.19	6.45
Canada to U.S. exchange rate – year average (Cdn\$ per \$1.00 USD)	1.14	1.07	1.07

(1) Sources: First Energy Capital Corp., Canadian Association of Oilwell Drilling Contractors, US Department of Energy, and Bank of Canada. All historical averages have been computed using weekday data only.

The trend in the indicators above, with lower average crude oil prices and significantly depressed natural gas prices, created a very difficult environment throughout 2009 in particular for producers weighted heavily to natural gas. Wells drilled in the year dropped by more than half, drilling rigs were retired as the overall utilization rate dropped by almost 50% and many companies that were financed for better economic environments produced poor or very negative results. Enerchem's performance reflected these influences for the early part of 2009 as sales volumes dropped and margins were squeezed. However, a strong balance sheet and management's focused inventory, logistics and margin optimization set the Company up for significant success in the third and fourth quarters of the year.

## **Business Strategy**

Enerchem's distinct business advantage is that its facilities, situated in Alberta, are dedicated to providing a range of hydrocarbon fluids that are consistent in product quality and designed to meet crude oil and natural gas processing and production requirements common to the WCSB. Its business challenge is to ensure the margins it achieves on the sale of its products are sufficient to cover all operating, transportation, selling and general and administrative costs and provide returns on capital. In this regard management's efforts are directed toward:

- Being the low cost producer of quality HCF that provide the best customer value;
- Optimizing infrastructure and facilities capabilities;
- Optimizing fluid transportation arrangements and infrastructure;
- Creating business opportunities and operating synergies through its energy marketing capabilities; and
- Managing capital investment at levels consistent with refineries of similar capability.

In addition, strategic elements of focus to provide long term above average returns to the Company's shareholders include:

- Developing new market segments to establish a more consistent revenue base during seasonal slowdowns in oilfield activity; and
- Identifying and acquiring complementary businesses that are earnings accretive and provide additional opportunities for growth.

## **Risk Factors**

Following are factors which could impact the Company's ability to be successful:

- Crude oil and natural gas prices which influence capital expenditure;
- Seasonal weather patterns and the impact on oilfield activity in the WCSB;
- Access to, and retention of, qualified personnel;
- Competitor product pricing strategies; and
- Access to terminal facilities to manage feedstock and by-product inventory efficiently and effectively.

Additional discussion of the Company's risk factors is provided in detail in Enerchem's Annual Information Form available at [www.sedar.com](http://www.sedar.com).

## **Critical Success Factors**

Enerchem believes the following operational indicators are critical to the success of the business:

- High capacity utilization at each of the Company's fractionation plants and flow-back facility
- High utilization rates for the Company's transportation equipment; and
- Inventory management.

The Company carries a level of fixed operating costs to which each unit produced, sold and transported to the customer contributes a cash margin. At high utilization rates, the total margin delivered covers all fixed and variable costs and provides a return on the fractionation and transportation assets.

Prudent feedstock inventory management requires timely input to the plant process to meet planned sales commitments and minimize the risk inherent in the volatility of crude oil prices. For finished goods inventory a similar focus is appropriate to balance seasonal product sales mix

availability against the risk of margins eroding as crude input prices rise and fall over the processing/sales cycle.

### **Key financial performance indicators:**

The Company monitors and assesses its performance against these critical success factors by tracking the following key financial performance indicators.

At December 31	2009	2008	2007
Volumes of refined Hydrocarbon fluids sold	90,448	72,256	62,061
EBITDA <sup>(1)</sup> (000)	\$1,242	\$2,398	\$4,073
Net loss per common share, basic	\$ (0.00)	\$(0.13)	\$(0.29)

(1) EBITDA is a non-GAAP measure and is defined by the Company under the section "Use of Non-GAAP Measures" in this MD&A.

In addition, the Company monitors key areas of operating performance that include but are not limited to, product profitability (margins), product quality and consistency, plant utilization, productivity improvements and waste reduction, market share, logistics efficiency and operating and administrative cost management.

## **Capability to Deliver Results**

### ***Non-Capital Resources***

People are the most critical non-capital resource required in order for the Company to achieve the goals set out in its strategic plan. A formal human resource plan has been implemented in order to ensure the Company maintains high employee morale, productivity and competent skill sets. During 2009, the Company continued to assess and, where appropriate, modify its compensation system to ensure market competitiveness. Management believes that its human resources are appropriate to successfully operate its business and to execute its strategic plan.

### ***Capital Resources***

The Company has the necessary working capital to meet its current obligations and commitments. The Company maintains a fleet of leased field service vehicles and leased premises which represent its off-balance sheet financing arrangements. During 2009, the Company used cash flows from its operating activities to fund capital projects in Sundre and Slave Lake, Alberta. In order to finance future capital expenditure requirements and future growth plans, Enerchem anticipates it will utilize a combination of available cash and cash equivalents, cash flow from operations and, when necessary, its existing credit facilities. Due to the long term nature of its assets and its historical cost of capital, the Company believes that it must provide an annual return of 12% to 15% on average capital employed over the life of its asset base in order to maintain Enerchem's cost of capital at economic levels.

### ***Systems and Processes***

The Company's operational systems and processes are regularly under review by management who continually implement new methods and infrastructure to facilitate increased productivity of its fractionation plants in Slave Lake and Sundre, the transportation assets, the sales force and the finance function. During 2009, through process changes enabled by the activation of the Atlantis lateral pipeline at Slave Lake, significant benefits were realized from the movement of by-products out of the plant. During 2010 changes in management information systems and processes are expected to be a key focus to satisfy current and future needs for more timely and accurate operating and financial information as well as to manage the transition to International Financial Reporting Standards discussed later in this MD&A.

## Seasonality of Operations

The ability to move heavy equipment used for drilling and well work overs in crude oil and natural gas fields in the WCSB is dependent on weather and road conditions. The roads that are travelled are generally not paved and as such present challenges in wet conditions. Exploration and production sites in many of the northern regions of the WCSB are accessible only during the winter months when the ground is frozen hard enough to support the weight of heavy equipment.

The timing and duration of freeze-up and spring break-up has a direct impact on Enerchem's activity levels. Late March through May has traditionally been the Company's slowest period for fluid sales and trucking activity while the peak period is generally from November through February. This timing was consistent during 2009 except that the spring break up ran two to three weeks longer taking until mid-June to see some normal level of activity return. In the third quarter of 2009, sales, in particular of Frac fluids, began to ramp up significantly earlier (July and August) than in past years.

## Selected Annual Information

Selected annual financial information derived from the audited financial statements for the three most recently completed financial years is set forth below and is prepared in accordance with generally accepted accounting principles in Canada:

	For the years ended December 31		
	2009	2008	2007
(\$ thousands except per share amounts)			
Revenues	<b>105,470</b>	115,797	80,300
Net loss from continuing operations	<b>(30)</b>	(1,901)	(4,481)
Net loss per share from continuing operations			
Basic	<b>(0.00)</b>	(0.13)	(0.29)
Diluted	<b>(0.00)</b>	(0.13)	(0.29)
EBITDA, continuing operations <sup>(1)</sup>	<b>1,248</b>	2,398	4,073
EBITDA per share, continuing operations <sup>(2)</sup>	<b>0.08</b>	0.16	0.27
Total assets	<b>72,533</b>	63,338	64,926
Cash provided by operations <sup>(3)</sup>	<b>5,734</b>	2,895	4,563
Cash and cash equivalents	<b>137</b>	196	2,711
Total bank indebtedness	<b>368</b>	3,448	-

(1) Items (1), (2) and (3) above are non-GAAP measures and are defined by the Company under the section "Use of Non-GAAP Measures" in this MD&A.

Other than during the latter portion of the year, oilfield activity levels in the WCSB in 2009 were generally much lower than in 2008, creating a challenging business climate for companies providing products and services to crude oil and natural gas explorers and producers (E&P). In recent history, drilling in the WCSB has been predominantly focused on natural gas activities. During the spring and summer of 2009, North American natural gas inventories increased to well above five year average levels, depressing natural gas prices to the point where E&P companies shut in production and focused drilling activity in western Canada on only the most economic opportunities. As a result, overall drilling rig utilization rates averaged 25% in 2009 compared to 47% and 42% in 2008 and 2007, respectively. The lower drilling activity continued through the first two quarters of 2009, and into quarter three at which time certain companies identified new exploration opportunities, based on horizontal drilling technology, and altered their focus to drilling for crude oil. The technology requires increased volumes of frac fluid, one of Enerchem's products, and the final quarter of the year was a much better one for the Company from the perspective of increased sales volumes at improved margins.

The Company's consolidated revenue in 2009 was 9% lower than 2008, the net impact of higher volumes and lower prices. Approximately 85% of consolidated revenues are derived from the sale of HCF, the prices for which are pegged to posted crude oil prices, introducing a level of volatility in revenues between comparative periods over which management can exercise little control. Volume of product sold is also impacted by demand (general industry conditions) and management's effectiveness in meeting demand with production and appropriate margins.

Enerchem's volume of HCF sold in 2009 was 25% higher than in the prior year in spite of the difficult economic environment of 2009. Through the first two quarters of the year, the Company recorded net after tax losses. That trend was reversed for the latter half of the year ending up with a \$30,000 net loss for the year compared to a reported net loss in 2008 of \$1,901,000. In 2008, the Company recorded significant unfavorable one time charges for the write off of an unsuccessful investment in new heater technology at Sundre (\$2,129,000) and for anticipated restructuring costs driven by the move of the head office to Calgary and significant changes in the executive management of the Company in the second quarter of that year (\$850,000). In 2009, the bottom line benefitted from the recovery of income taxes enabled by the tax rules that provide for the carry back of losses to recover taxes paid in prior periods.

## Results of Operations – Annual Review

### Revenue

Consolidated revenues for the year ended December 31, 2009 decreased by \$10,326,000, or 9%, to \$105,471,000 down from \$115,797,000 for the prior year. Revenues were positively impacted by a 25% increase in volumes of HCF sold in the current year and negatively impacted by the lower average crude oil price in 2009. The increased volumes were delivered in a year during which drilling activity in the WCSB was down significantly from prior years. A discussion of revenues within specific business segments is included in the paragraphs that follow.

**Oilfield services segment.** HCF sales volumes were 25% higher in 2009 when compared to 2008, although revenues were \$7,517,000 lower. The lower 2009 average crude price, the basis on which the Company's product prices are determined, more than offset the volume increase, which was achieved despite the overall lower industry activity levels in 2009. Average margin per cubic metre of HCF sold, a key indicator of Enerchem's success, was 12% lower in 2009 compared to 2008. This change was driven by several factors including the volatility of crude prices, the mix of products sold at different margins, market supply and demand and general industry activity. One of the more significant negative effects on year-over-year margin realized was the carryover into 2009 of high volumes of higher average cost feedstock and HCF inventories. These higher costs in inventory were charged to cost of goods sold during 2009 according to the accounting policies followed by Enerchem. Management spent considerable time and effort changing the operational imperatives to prevent this negative effect in the future.

**Energy marketing segment.** Revenues increased by \$1,049,000, or 3%, to \$34,035,000 in 2009 when compared to 2008, a result of the impact of higher levels of by-product sales which resulted from the increased HCF volumes sold by the Oilfield services segment. The volume increase was partially offset by the lower average crude price, and therefore prices received for crude by-products, in 2009 compared to 2008.

**Transportation Services.** Segment revenues decreased by \$2,704,000, or 15%, to \$15,755,000 in 2009 when compared to 2008. The lower level of industry activity and the resulting competitive pressure on rates drove a 34% reduction in third party revenues in the segment when compared to 2008. This was partially offset by an increase of 16% in inter-segment revenues which impact occurred mainly in the latter five months of 2009 driven by the Oilfield services segment sales volume increase when compared to the prior year.

## **Operating Expenses**

Operating expenses represent the Company's product and service costs associated with the manufacture and sale of its hydrocarbon products and the provision of its transportation services. Operating expenses also include all costs directly related to the support and maintenance of plant and other operating equipment. Operating expenses in 2009 were \$8,841,000 lower than 2008, driven in large part by the lower average cost of crude feedstock and also by approximately \$600,000 savings in lab supplies and third party analysis costs, in insurance premiums, and in repairs and maintenance.

Operating expenses as a percent of revenues, after elimination of inter-segment transactions, was 94% for 2009, compared to 93% in 2008. The increase is the net result of a number of factors, including the high degree of volatility in crude oil prices in 2008 compared to 2009, management's strategy in the current year to increase market share, and thereby plant utilization through narrowing margins during the third quarter of 2009, the relatively higher charges in 2009 to cost of sales from high levels of inventory carried into the current year and the operating cost savings discussed above.

## **General and Administrative**

General and administrative expenses include salaries and other related expenses for the Company's administrative, finance, information technology and human resource functions. General and administrative expenditures increased by \$570,000, or 13%, to \$5,014,000 in 2009 from \$4,444,000 in 2008. Reductions in bank fees, interest and travel were more than offset by increased occupancy costs due in part to the move of head office in late 2008 to Calgary, in part to costs of work associated with the transition to International Financial Reporting Standards and in part due to legal and other services relating to recovery of direct costs and other losses for the direct fired heaters that were written off in 2008.

## **Depreciation**

Depreciation expense increased by \$91,000, or 4% to \$2,586,000 in 2009 compared to \$2,495,000 in 2008 driven by the capital invested during 2009.

## **Income Taxes**

The provision for income taxes in 2009 includes total current tax recovery of \$3,944,000 which includes \$1,561,000 resulting from carrying back losses in filing the corporate income tax returns for both Enerchem and Millard Trucking as well as expected income tax recoveries for 2009. Both impacts are based on accelerated charges for capital cost allowance generated from the reclassification of certain assets amongst tax classes. The impact of the reclassification is partially offset in the higher future tax provision for 2009 when compared to 2008.

The effective tax rate for each of the years is substantially different from the statutory rates of 29% and 29.5% for 2009 and 2008, respectively. In 2009, the most significant factor in creating the variance is the carry back of losses to prior years which generated a recovery of taxes at rates paid in the years to which the losses were applied. For 2008, the most significant reason for the variance relates to changes in the statutory rates announced by federal and provincial taxing authorities and the impact that had in determining the value of future tax liabilities.

## **Net Loss**

For the year ended December 31, 2009, the Company reported a net loss of \$30,000, or \$0.00 per common share diluted, compared to a net loss of \$1,901,000, or \$0.13 per common share diluted, for the year ended December 31, 2008. The reduced net loss in 2009 versus 2008 resulted from a combination of lower earnings from operations due to lower margins offset by lower non-cash charges to income in the current year. Margins were lower in 2009 due in part to high embedded costs in feedstock and HCF inventory carried into the year, as well as to competitive action taken by management during the third quarter. For the year 2009, the

Company did not take any one-time charges for restructuring, nor did it write down the value of capitalized equipment costs as was required in 2008.

EBITDA (refer to "Use of Non-GAAP Measures") for the year ended December 31, 2009 was \$1,242,000 compared to \$2,398,000 for 2008. The timing of the generation of EBITDA during the years was significantly different as the Company earned EBITDA of \$2,129,000 in the final quarter of 2009 compared to \$1,115,000 for the final quarter of 2008.

### **Liquidity and Capital Resources**

In 2009, the Company's cash provided by operations before working capital changes was \$5,734,000 compared to \$2,895,000 in 2008. The Company's working capital has increased to \$17,780,000 at December 31, 2009 compared to \$13,915,000 at December 31, 2008. The increase in working capital is due to management's focus on aligning capital investment more closely to the organization's cash generating capability as well as to the recovery of income taxes paid in prior years. The Company's current ratio (defined as current assets divided by current liabilities) was 2.1 to 1 at December 31, 2009 compared to 2.4 to 1 at December 31, 2008, the difference being driven in large part by the variance in the amount carried in inventory. At the end of 2008, the carrying value of inventory was over two times the value at the end of 2009. Higher average costs and significantly higher volumes in the 2008 year end value negatively impacted the Company's margins in the first half of 2009. This impact is not expected for 2010 due to the just-in-time approach to inventory management employed at the fractionation plants since mid 2009.

During 2009, the Company maintained its bank operating line of credit at \$10,500,000, subject to margining requirements, to finance its working capital needs, and reduced its bank guarantee facility from \$17,000,000 to \$10,000,000 to better align feedstock purchase commitments to suppliers with guarantee facility costs. At December 31, 2009 the Company had outstanding bank guarantees of \$3,082,000 (December 31, 2008 - \$3,634,600).

In addition, the Company has a \$5,000,000 demand revolving credit facility (December 31, 2008 - \$8,000,000) that bears interest at the bank's prime rate plus 1.5%, to assist in financing projects undertaken at the Company's facilities and equipment purchases. At the end of 2009 and 2008 there were no amounts drawn on this facility.

As of December 31, 2009, the Company was in compliance with all debt covenants and obligations. The terms of the credit facility with the bank provide that retirement of the revolving credit facility loans, while repayable on demand by the bank, will not be requested by the bank unless the Company is in default of its obligations and covenants and if in the opinion of the bank there has been a change in the business, financial condition, operations or conduct of the Company. The Company believes that it has sufficient liquidity to operate its business and to execute its strategic plans.

In 2009, the Company financed its capital requirements, totaling \$1,205,000, from cash provided by operations and bank indebtedness. Investments in plants amounted to \$1,122,000 and the remaining \$83,000 was spent on computers, software, lab equipment and leasehold improvements. Enerchem also entered into capital lease arrangements for an amount of \$794,000 to finance the replacement of certain of its heavy equipment in the Transportation segment.

In 2008, items making up the \$4,134,000 capital expenditure included completion of the Slave Lake blend facility, the direct-fired heaters at Sundre (which were subsequently written down), increases to the Millard Trucking truck fleet and office interiors and furniture at the Calgary head office.

Enerchem repaid the full amount of bank indebtedness outstanding at December 31, 2008 during 2009 and has relied on internally generated cash flow and capital leases to finance ongoing capital requirements except for \$368,000 it had drawn on its operating line of credit at the end of the year. The capital lease arrangements have terms of four or five years and are repayable as follows:

Year	(\$ thousands)
2010	184
2011	184
2012	184
2013	181
2014	161

## Summary of Contractual Obligations and Off-Balance Sheet Arrangements

The following table summarizes the Company's contractual obligations including payments due for each of the next five years and thereafter.

Contractual obligations (\$ thousands)	Payments due by period				
	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
	\$	\$	\$	\$	\$
Operating leases <sup>(1)</sup>	1,600	659	780	161	-
Total contractual obligations	1,600	659	780	161	-

(1) Represents normal operating leases comprised of vehicles, trailers and office space.

In the normal course of business with vendors the Company may become liable for performance under letters of guarantee and credit. In this regard, the Company has arranged a \$10,000,000 bank guarantee facility available as security for its feedstock arrangements and purchase commitments. At December 31, 2009 the Company had outstanding \$3,082,000 in letters of guarantee, which terminated in February 2010, in favour of two suppliers for the purchase of petroleum feedstock.

For 2010 the Company expects cash flow from operations to be sufficient to meet its contractual obligations and off-balance sheet arrangements.

## Share Capital

At December 31, 2009 the Company had 15,007,173 common shares outstanding. In addition, as at December 31, 2009, the Company had reserved 565,000 common shares for issuance under outstanding stock options.

On July 15, 2008, the Company commenced a normal course issuer bid to purchase up to 760,805 of its issued and outstanding common shares. Purchases under the normal course issuer bid terminated on July 14, 2009. All shares purchased under the issuer bid have been cancelled. During 2008, 225,600 common shares were purchased by the Company of which 43,100 common shares were acquired at purchase prices, including transaction fees, which exceeded the assigned value of the Company's issued and outstanding common shares, at \$1.94 per common share and 182,500 common shares were acquired at purchase prices, including transaction fees, which were less than the assigned value. The cost of common shares purchased which exceeded the assigned value of the Company's common shares, totaled \$89,000, or \$2.07 per common share, of which \$84,000 was recorded as a reduction of share capital at the average carrying value of the Company's common shares, with the balance of \$5,000 charged against retained earnings. The cost of common share purchases which were less

than the assigned value of the Company's common shares totaled \$281,000, or \$1.54 per common share, of which \$355,000 was recorded as a reduction of share capital at the average carrying value of the Company's common shares, with the offsetting balance of \$74,000 recorded as an increase in contributed surplus.

During 2009 prior to the expiry of the bid, the Company purchased 10,100 shares at prices ranging from \$0.58 to \$0.71 per share.

Enerchem commenced a normal course issuer bid (NCIB) on July 15, 2009, the intent of which is to purchase up to 500,000 of its issued and outstanding common shares. Purchases under the NCIB will terminate on July 14, 2010 or such earlier time as the full number of common shares are acquired or the NCIB is terminated by the Company. The Company has purchased and cancelled 10,200 shares under this bid as of March 11, 2010. The cost of these common share purchases, which were less than the assigned value of the Company's common shares, totaled \$9,000, or \$0.91 per common share, of which \$20,000 was recorded as a reduction of share capital at the average carrying value of the Company's common shares, with the offsetting balance of \$11,000 recorded as an increase in contributed surplus.

## Summary of Quarterly Results

The following tables provide selected unaudited financial information relating to the Company's quarterly activities in 2009 and 2008 and are prepared in accordance with Canadian GAAP with respect to the preparation of interim financial statements.

### 2009

(unaudited)	Three month period ended			
(\$ thousands except per share amounts)	December 31	September 30	June 30	March 31
Revenues	39,734	31,028	11,787	22,921
Net earnings (loss) for the period	1,401	345	(1,453)	(323)
Net earnings (loss) per share for the period				
Basic	\$0.10	\$ 0.02	\$ (0.10)	\$ (0.02)
Diluted	\$0.10	\$ 0.02	\$ (0.10)	\$ (0.02)

### 2008

(unaudited)	Three month period ended			
(\$ thousands except per share amounts)	December 31	September 30	June 30	March 31
Revenues	28,189	32,471	21,390	33,747
Net earnings (loss) for the period	81	(845)	(1,067)	(70)
Net earnings (loss) per share for the period				
Basic	\$ 0.00	\$ (0.06)	\$ (0.07)	\$ 0.00
Diluted	\$ 0.00	\$ (0.06)	\$ (0.07)	\$ 0.00

## Review of Fourth Quarter Results

Sales of HCF began to increase late in the third quarter of 2009 and continued at very high levels throughout the fourth quarter, resulting in a 25% increase in volumes sold when compared to the fourth quarter of 2008. Industry activity continued to build through the final quarter of 2009 and with the increased demand for products, management improved margins on all products to competitive levels. In addition to increased HCF sales, the increased level of industry activity drove revenue up in the Transportation services segment.

Consolidated revenues for the three months ended December 31, 2009 were \$11,545,000 or 41% higher than for the same period of the prior year. Margins before general and administrative and other costs were up 59%, the impact of the higher utilization of fractionation capacity in the fourth quarter of 2009. General and administrative costs were 17% or \$167,000 higher in the final quarter of 2009 compared to the same period in 2008, and income tax expense was lower. Net income was \$1,320,000 better in the fourth quarter of 2009 compared to the same period of 2008.

Contributions by business segment were as follows:

**Oilfield Services.** Segment revenues increased by \$5,076,000, or 25%, in the fourth quarter of 2009 when compared to the same period in the prior year. The increase reflects the net effect of improved volumes and lower prices. Volumes sold in the final quarter of the current year were up 45% from the final quarter of 2008 generating a \$9,736,000 increase in revenues while prices realized for the product were down, reducing the revenue gains by \$4,660,000. Prices realized were lower as a result of the lower average crude oil price in the final quarter of 2009 compared to the same period of 2008. This segment's contribution to the overall increase in margin before general and administrative and other costs was the most significant and was driven in the main by the higher sales volumes. Each additional cubic metre of HCF sold over a threshold established by the Company's fixed operating costs provides a significant contribution to operating margin and net income.

**Energy Marketing.** Revenues for this segment were \$6,758,000 higher for the final quarter of 2009 when compared to the same quarter of 2008, a 127% increase due to the higher volumes of by-products available for sale from the increased sales volumes by the Oilfield services segment. Energy marketing's contribution to margin for the fourth quarter of 2009 was much improved over the comparative prior year period because in 2009 crude oil prices fell during the quarter while in 2009 they rose over the quarter.

**Transportation Services.** Revenues for this segment were up \$251,000 or 5% to \$5,144,000 for the final quarter of 2009 when compared to the same period of 2008. The fourth quarter of 2009 opened with lower activity levels than in the prior year, but ramped up very quickly over the last two months of the quarter. In addition, rates had been lowered in the third quarter of 2009 as part of management's focus on customer relationships and these rates were held through the fourth quarter.

At 92%, operating expenses as a percentage of revenues were lower for the fourth quarter of 2009 when compared to 93% for the fourth quarter of 2008. The Oilfield services segment contributed 65% of the improvement as a result of the increased sales volumes, each unit of which provided a cash contribution to the fixed levels of costs. The Energy marketing segment contributed a further 25% of the improvement due mainly to the different crude oil price environments the Company faced in the respective quarters. In 2009, crude oil prices were less volatile and rising over the period from feedstock purchase to by-product sale, while in 2008, with the precipitous drop in crude oil prices in the last month of the year, segment margins were negatively impacted.

General and administrative expenses for the fourth quarter of 2009 were up \$167,000 or 17% over the comparable period in 2008 due to general increases in operating costs at the Company's office locations, to increased professional fees for the transition to International Financial Reporting Standards and to litigation costs which were discussed earlier in this MD&A.

Depreciation expenses were higher in the fourth quarter of 2009 compared to the same period in the prior year as a result of the capital spent in late 2008 and through 2009.

Earnings before tax for the fourth quarter of 2009 at \$1,470,000 were \$1,027,000 higher than for the fourth quarter of 2008 reflecting the improved business climate, the resulting higher volumes and the impact of the operational changes made by management to increase efficiency and inventory management.

For the three months ended December 31, 2009 the Company reported net earnings of \$1,401,000 compared to net earnings of \$81,000 in the same period of the prior year. Variations in the impacts of future income tax provisions in the quarters augmented the improvement in earnings before tax for the fourth quarter of 2009 compared to the same quarter of the prior year.

EBITDA (refer to "Use of Non-GAAP Measures") for the three months ended December 31, 2009 increased 91%, to \$2,130,000 compared to \$1,115,000 for the same quarter in the prior year. The increase in EBITDA is the combined result of higher volumes produced and sold by the Company and the positive effects of cost control in the business.

Cash provided by operations for the three months ended December 31, 2009 totaled \$3,394,000 compared to \$786,000 for the three months ended December 31, 2008. Capital expenditures in the fourth quarter of 2009 totaled \$365,000 compared to \$581,000 in the same period of the prior year. In the fourth quarter of 2009 the capital was invested in the tie in to the Slave Lake Plant of a new battery constructed in the area by one of the Company's crude oil suppliers. Capital expenditures in the fourth quarter of 2008 were directed to the winterization of the blend facility in Slave Lake, office leasehold improvements and furniture at the Calgary offices, and fleet additions in Millard.

## **Trends and Outlook**

Industry analysts commenting on activity levels in the WCSB for the upcoming year continue to predict drilling activity at levels well below historic highs, although certain areas in the WCSB, in locations very near the Company's producing facilities, have recently become desirable areas for producers drilling and completing crude oil wells using new horizontal drilling technology.

Enerchem is poised to deliver significantly improved financial results in 2010 as increased market and market share, customer relationship management and operating efficiencies contribute to the Company's ability to deliver record HCF sales volumes through the first quarter of 2010. In addition, tight management of raw material and finished goods inventory will reduce volatility risk in crude oil prices, allowing a better matching of costs in the production process.

The Company continues to maintain a healthy balance sheet and is looking for opportunities to utilize its capacity to make accretive business acquisitions.

While it is difficult to predict the long term view for the industry, management has a very positive outlook for 2010 and has altered plans for both the timing and length of its annual fractionation plant shut down for turnaround. Normally starting in early April and continuing for most of the month, the shut down is anticipated to occur much later in the second quarter and be restricted to a seven to ten day time frame.

The Company's 2010 capital program is expected to be approximately \$1,500,000 for projects related to cooling, vapor recovery and other safety and reliability related expenditures. Capital expenditures may increase as investment opportunities are developed.

## **Critical Accounting Policies**

The Company's financial statements have been prepared in accordance with Canadian GAAP and include estimates that reflect management's estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses for the period reported. Estimates are based upon historical experience and various other assumptions that reflect management's best judgments. These estimates are evaluated periodically and form the basis for making judgments regarding the carrying values of assets and liabilities and the reported amount of revenue and expenses. Actual results could differ from these estimates.

The following discussion outlines the accounting policies and practices and management's estimates that are critical to determining Enerchem's financial results.

### **Property, Plant and Equipment**

Property, plant and equipment ("PP&E") are recorded at cost and are depreciated over their estimated useful lives on a straight line basis. Judgment is involved in determining the useful life of the PP&E. The Company's investment in PP&E results in depreciation expense being a significant component of operating expenses and any misjudgment in determining the useful lives could result in a misstatement of depreciation expense.

### **Income Taxes**

The provision for income taxes is calculated based on the expected tax treatment of transactions recorded in the Company's financial statements. Income tax assets and liabilities, both current and future, are measured according to the income tax legislation that is expected to apply when the asset is realized or when the liability settled. If the Company's interpretations differ from those of tax authorities or judgments with respect to tax losses change, the income tax provision could increase or decrease, potentially significantly, in future periods.

### **Inventories**

Inventories are carried at the lower of average cost and estimated net realizable value. Finished goods inventories include an allocation of direct labour and overhead attributable to production. High volatility in crude oil feedstock prices and attainable prices can significantly affect the potential net realizable value of inventories, therefore management assesses the values of inventories on a regular basis and records adjustments as necessary.

### **Accounts Receivable**

Accounts receivable are recorded net of allowance for doubtful accounts. Management takes appropriate action in providing credit to new customers and closely monitors longer outstanding accounts on an ongoing basis to minimize the negative impacts that could arise out of the ability to not collect these amounts.

## **Changes in Accounting Policies and Practices**

- (a) Effective January 1, 2009 the Company adopted CICA Handbook Section 3064, "Goodwill and Intangible Assets" which replaced the existing standard for goodwill and other intangible assets in Section 3062 and research and development costs in Section 3450. The Section establishes standards for the recognition, measurement, presentation

and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Adoption of this standard did not materially impact the Company's financial statements.

- (b) Effective January 1, 2009, the Company changed the basis on which it depreciates certain assets from a declining balance basis to a straight-line basis. As of 2009, all assets are depreciated on a straight-line basis. The accounting change is treated as a change in estimate and is applied prospectively. The benefit of the change is improved consistency of process, particularly in connection with periodic reassessments of remaining asset lives. The estimated useful lives under the straight-line method were computed as necessary in order to maintain the depreciation expense at essentially the same level as under the declining balance method immediately preceding the change. The effect of these changes on depreciation expense is nil in the current year.
- (c) On January 20, 2009 the Emerging Issues Committee of the CICA issued EIC-173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities." The EIC concluded that the credit risk of an entity and applicable counterparties should be taken into account when determining the fair values of financial assets or liabilities, including derivative instruments. The recommendations of EIC-173 are effective for interim and annual reporting periods in 2009 and were applied retrospectively, without restatement of prior periods. The application of the EIC recommendations did not have a material effect on the Company's financial statements.
- (d) The CICA amended CICA Handbook Section 3862, "Financial Instruments – Disclosures" that requires additional disclosures about the fair value measurements of financial instruments and enhances liquidity risk disclosures. The application of this amendment is for all periods ending after September 30, 2009. The adoption did not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

## **Recent Accounting Pronouncements Not Yet Adopted**

- (a) CICA Handbook Section 1582, "Business Combinations" will be applicable to business combinations for which the acquisition date is on or after the Company's interim and fiscal year beginning January 1, 2011. Early adoption is permitted. The section improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements regarding a business combination and its effects.
- (b) CICA Handbook Section 1601, "Consolidated Financial Statements" will be applicable to financial statements relating to the Company's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for the preparation of consolidated financial statements. The Company has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.
- (c) CICA Handbook Section 1602, "Non-controlling Interests" will be applicable to financial statements relating to the Company's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination.

## **Financial Instruments and Other**

### **Fair Values**

The carrying values of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate their fair value due to the relatively short periods to maturity on these instruments. The fair value of the Company's bank indebtedness is estimated based on market prices for same or similar instruments and approximates carrying value. The fair value of capital lease obligations approximates the carrying value because the interest rates approximate the rates for similar borrowing arrangements.

### **Credit Risk**

The Company's Oilfield services segment's revenues are predominantly from fluids sold to large crude oil and natural gas exploration and producing companies which may result in a significant exposure to one customer or on a combined basis to several individual customers. The Company's Energy marketing segment's revenues are attributable to several large crude oil and natural gas producers and oilfield services companies which account for all of this segment's revenues. Concentration of credit risk on the Company's trade accounts receivable exists in the crude oil and natural gas industry. Management regularly reviews outstanding accounts receivable and follows up with customers when settlement has not occurred on a timely basis. Management believes that the Company is exposed to minimal credit risk since the majority of its business is conducted with companies that have a large market presence in the industry and/or are large publicly held companies.

### **Petroleum Prices**

The Company is exposed to changes in crude oil and natural gas prices as a result of its use of crude oil for feedstock and natural gas for processing at its Sundre and Slave Lake fractionation plants. The potential fluctuations in these commodities' prices could have a significant impact on the cost of producing the Company's products and its profitability. To mitigate the effects on profitability of upward changes in petroleum prices, the Company is able to increase product prices to reflect their underlying values. This ability, however, is sensitive to competitive product pressures. In addition, this risk is reduced in part, from time to time, through the use of crude oil and natural gas forward purchase contracts. The contracts are not used for speculative trading purposes. Realized gains or losses on these contracts are reported as adjustments to feedstock and natural gas costs in the related production period.

As at December 31, 2009 and 2008 the Company did not have any outstanding crude oil and natural gas forward purchase contracts.

### **Interest Rate Risk**

The Company manages its interest rate risk on borrowings by utilizing a combination of short term fixed rates through the use of 30 to 90 day Bankers' Acceptance rates and floating rates on debt.

## **Health, Safety and Environmental (HSE)**

The Company has achieved and maintained a Certificate of Recognition which is given to employers who develop health and safety programs which meet standards established by the ENFORM, an organization which provides training, certification and safety services to the Canadian petroleum industry, and Alberta Human Resources and Employment. The Company's Oilfield services segment has received a Work Safe Alberta 2006 Best Safety Performer Award for exceptional performance in workplace health and safety. This award is presented to only 300 employers of a possible 140,000. The Company has safety and environmental personnel who report directly to the President and Chief Executive Officer of the Company and are responsible for maintaining and developing the Company's HSE policies and monitoring its operations to ensure compliance with established policies. However, there can be no assurances that the

Company's procedures will prevent environmental damage occurring from spills of materials handled by the Company.

## **Competition and Industry Conditions**

The capital expenditure programs of E&P companies have a significant effect on the sales of HCF produced by Enerchem and the provision of related services. .. The primary catalysts to high expenditures and activity levels by E&P companies are crude oil and natural gas prices which, in turn, are influenced strongly by supply and demand expectations. Forecasting the price of crude oil or natural gas is extremely difficult as many global factors affecting commodity prices are beyond the control of the Company.

There is a strong correlation between drilling activity and demand for the Company's hydrocarbon fracturing and drilling fluids and especially between deep-well drilling and applications common to the foothills region and northern Alberta and British Columbia. Crude oil and natural gas activity in these geographic regions is normally strong during winter months or other times when climatic conditions are favorable. In addition, as the fluids and services are sold in highly competitive markets, the Company's revenues and earnings can be affected by changes in competitive prices and new technologies and methods.

## **Operating Risk and Insurance**

Enerchem has an insurance and risk management program in place to protect its assets, operations and employees. The Company's operations are, however, subject to risks inherent in the crude oil and natural gas industry such as malfunction and failures and natural disasters with resultant fluid spills, explosions and fires. These risks could expose the Company to substantial liability for personal injury, loss of life, business interruption, property damage or destruction, pollution and other environmental damages. Although the Company has obtained insurance against certain of the risks to which it is exposed, such insurance is subject to coverage limits and no assurance can be given that such insurance will be adequate to cover the Company's liabilities or will be generally available in the future or, if available, that premiums will be commercially justifiable. If the Company were to incur substantial liability and such damages were not covered by insurance or were in excess of policy limits, its business, results of operations and financial condition could be materially adversely affected.

## **Disclosure Controls and Internal Control Over Financial Reporting**

National Instrument 52-109 - *Certification of Disclosure in Issuers' Annual and Interim Filings*, issued by the Canadian Securities Administrators requires that the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") for an issuer certify that they are responsible for establishing and maintaining disclosure controls and procedures ("DC&P") for the issuer, that DC&P have been designed to provide reasonable assurance that material information relating to the issuer is made known to them, that they have evaluated the effectiveness of the issuer's DC&P, and that their conclusions about the effectiveness of those DC&P at the end of the period covered by the relevant annual filings by the issuer have been disclosed.

Enerchem's CEO and CFO have evaluated the effectiveness of the Company's DC&P as at December 31, 2009 and have concluded that they were effective.

In addition, an evaluation of the design and operating effectiveness of internal control over financial reporting ("ICFR") was conducted as of December 31, 2009 by and under the supervision of management, including the CEO and CFO. The control framework used to design

the Company's ICFR was *Internal Control – Integrated Framework* (COSO Framework) published by the Committee of Sponsoring Organizations of the Treadway Commission.

Based on this evaluation, the CEO and CFO have concluded and certified the following:

- ICFR as defined by National Instrument 52-109 is effective as of December 31, 2009
- there were no changes in the Company's ICFR during the period beginning October 1, 2009 and ended on December 31, 2009 that have materially affected, or are reasonably likely to materially affect the Company's ICFR
- there has been no fraud involving management or other employees who have a significant role in the Company's ICFR

## **International Financial Reporting Standards (“IFRS”)**

In February 2008, the CICA's Accounting Standards Board confirmed transition timing for publicly accountable enterprises in Canada to adopt IFRS. Accordingly, the Company will be required to adopt IFRS on January 1, 2011, including reporting for interim periods in fiscal 2011. The company has developed a changeover plan to complete transition to IFRS by January 1, 2011, including the preparation of required comparative information relating to 2010.

The key elements of Enerchem's changeover plan include:

- Determination of appropriate changes to accounting policies and required disclosures;
- Identification and implementation of changes in supporting processes and information systems;
- Compliance with internal control over financial reporting requirements;
- Communication with internal and external stakeholders regarding expected outcomes; and
- Training of internal staff and education of relevant external stakeholder to support the changes.

Enerchem has engaged the services of experts who have previously guided organizations through the transition in other countries. The Company has determined which mandatory and optional exemptions apply to its consolidated financial statements and has created accounting policy documents which support the elections it has taken. The Company has also defined its cash generating units and expects to complete the componentization of the Company's assets by the end of the first quarter of 2010.

With respect to changes in supporting processes and information systems, the Company has identified options to approach the consolidation of information for purposes of reporting under IFRS requirements. One of the system options under investigation includes utilization of software recently put into use in the Company to streamline the process of consolidation under Canadian GAAP. Additionally, management has identified other areas where existing systems are expected to be inadequate for purposes of supporting the information needs of the business as it grows and is assessing financial system options. The assessment and decision with respect to the appropriate systems will be completed by the end of the second quarter of 2010.

Management expects that the transition to IFRS will not have a material impact on the Company's consolidated financial statements due to the limited complexity of its business.

Training of internal staff and education of relevant external stakeholders to support the changes is a deliverable for management during the first and second quarters of 2010.