

THE QUEEN'S BENCH
Winnipeg Centre

BETWEEN:

THE MANITOBA SECURITIES COMMISSION,

Applicant,

-and-

CROCUS INVESTMENT FUND,

Respondent.

RECEIVER'S REPORT # 7
DATED: September 10, 2005

DELOITTE & TOUCHE INC.
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Telephone No. (204) 942 - 0051

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1. Deloitte & Touche Inc. (the "Receiver") was appointed Receiver of the Respondent's current and future assets, undertakings and properties of every nature and kind whatsoever, and wherever situate, including all proceeds thereof (the "Property") by an Order of this Court made on June 28, 2005 (the "Receiving Order").

2. Pursuant to the Receiving Order, the Receiver is empowered and authorized to sell, convey, transfer, lease or assign the Property or any part or parts thereof out of the ordinary course of business without the approval of the Court in respect of any transaction not exceeding \$100,000, provided that the aggregate consideration for all such transactions (the "Permitted Transactions") does not exceed \$100,000. If the Receiver wishes to sell, convey, transfer, lease or assign the Property or any part or parts thereof out of the ordinary course of

business other than in Permitted Transactions, it is required to make application to the Court.

3. The Receiver's review of the records of the Respondent disclosed that:

(a) by a Subscription Agreement made March 5, 2004, the Respondent and Sequoia Energy Inc. ("Sequoia") agreed, among other things, that:

- (i) the Respondent would subscribe for and acquire from treasury that number of Class A Convertible Preferred Shares (the "Shares") in the capital stock of Sequoia (which are convertible, at any time after issuance, at the instance of the holder, on a one for one basis, into Common Shares) as would provide the Respondent with a 25% interest in Sequoia on a fully diluted basis for aggregate subscription proceeds of \$550,000;
- (ii) Sequoia would pay the Respondent's costs incurred in connection with the Subscription Agreement, to a maximum of \$50,000;
- (iii) the shareholders of Sequoia would enter into a Shareholders Agreement; and

- (iv) Sequoia and the Respondent would enter into an Agreement to Provide Guarantee.

- (b) The transaction described in the Subscription Agreement closed, the Respondent paid \$550,000 to its solicitors on account of the subscription price, the solicitors paid \$500,000 to Sequoia and \$50,000 to the Respondent, Sequoia issued 1,340.67 Shares to the Respondent (which equated to the required 25% interest) and the parties thereto signed the Shareholders Agreement and the Agreement to Provide Guarantee.

- (c) The Shareholders Agreement granted the Respondent the right to convert the Shares into a \$550,000 debenture with a term of 5 years after the conversion date, which could be at anytime within 3 years after March 5, 2006 (under which the Respondent would not have been entitled to be paid the principal until March 5, 2011 at the earliest). The Shareholders Agreement also describes several events of default and remedies relating to the Shareholders. In particular, the Agreement states that it is an event of default "if a receiver ... is appointed to take charge of all or substantially all of the business or assets of a Shareholder or any of the Shares of a Shareholder and is not discharged within sixty (60) days thereafter or if that Shareholder consents to or acquiesces in such appointment." The Shareholder Agreement further provides that, if

an event of default has occurred and is continuing, Sequoia has an irrevocable option to purchase all of the shares owned by the defaulting Shareholder at an amount equal to the subscription price paid for such shares.

- (d) The Agreement to Provide Guarantee acknowledged that Sequoia might from time to time be indebted to commercial lenders, which might require, as a condition of advancing loans, that the Respondent provide such lenders with Guarantees of their loans, for which Sequoia would pay the Respondent certain fees.

4. As a result of the said review of the records of the Respondent and interviews conducted with certain employees or former employees of the Respondent, the Receiver determined that Sequoia was involved in the development and sale of a project to generate electricity from wind turbines located in the vicinity of St. Leon, Manitoba (the "St. Leon Project").

5. The Receiver's review of the records of the Respondent also disclosed that, pursuant to the Agreement to Provide Guarantee, the Respondent guaranteed the obligations of Sequoia to Assiniboine Credit Union Limited ("Assiniboine") to the extent of \$1,250,000 (the "Sequoia Guarantee"). The Sequoia Guarantee was given to enable Sequoia to establish a credit facility with Assiniboine to provide working capital for its business, including with respect to the St. Leon Project.

6. The Receiver learned that, as of the date the Receiving Order was made, the St. Leon Project had been completed and sold and Sequoia held certain funds on deposit with Assiniboine. While no other projects were presently underway, the Receiver was advised that Sequoia intended to continue in business as a developer of projects similar to the St. Leon Project.

7. After the Receiving Order was made, counsel for Sequoia advised the Receiver that Assiniboine had taken the position that, given the current circumstances of the Respondent, it was no longer prepared to rely on the Sequoia Guarantee unless the Respondent provided adequate security for its obligations thereunder. Counsel for Sequoia took the position that:

- (a) the failure of the Respondent to provide such security and the fact that an unsecured Guarantee from the Respondent was now unacceptable to a commercial lender put it in breach of the Agreement to Provide Guarantee and that Sequoia had suffered damages as a result of now being required to find an alternate means of raising working capital;
- (b) in the circumstances, Sequoia was entitled to redeem the Shares on payment to the Respondent of the sum of \$500,000 (being the amount actually paid to it out of the funds advanced by the Respondent);

- (c) in the circumstances, Sequoia was entitled to a credit of \$100,000 against the amount payable to redeem the Shares on account of the alleged damages that it had sustained.

8. As stated above, at or about the time of the closing to the Subscription Agreement transactions, the Respondent's solicitors (who also acted for Sequoia) had returned the sum of \$50,000 (out of the \$550,000 that had been advanced as the subscription price for the Shares) to the Respondent, presumably on account of costs incurred by the Respondent. However, the Receiver's review also disclosed that the Respondent had never submitted an accounting of or invoice for its costs to Sequoia.

9. In these circumstances, the Receiver had to decide whether it would contest the positions being advanced on behalf of Sequoia or attempt to reach a settlement. One of the factors taken into consideration by the Receiver in this regard was whether, even if Sequoia was incorrect in its positions, it was in the best interests of the Respondent to continue to hold the Shares. The Receiver concluded that, as Sequoia had no projects presently underway and there was no current exposure to the Respondent under the Sequoia Guarantee, it was preferable to negotiate a settlement.

10. With the assistance of counsel, and without admitting the validity of the positions advanced on behalf of Sequoia, the Receiver negotiated a settlement with Sequoia pursuant to which it was agreed that, subject to the approval of the Court, Sequoia would pay \$500,000 to redeem the Shares and

would obtain a release of the Sequoia Guarantee from Assiniboine (the "Sequoia Settlement"). In arriving at the Sequoia Settlement, the Receiver took into consideration the amount of the funds on deposit with Assiniboine and concluded that, as the Respondent had no direct or immediate right to a share thereof, it was preferable to sell the Shares at the present time for the said sum of \$500,000, which has been paid to the solicitors for the Receiver and is being held by them in trust pending approval of the Sequoia Settlement by the Court.

11. The Receiver makes this Report in support of its recommendation that the Court approve the Sequoia Settlement. In particular, the Receiver is of the view that it is in the best interests of the Respondent to:

- (a) liquidate the Shares immediately rather than continue to hold them as an investment, thereby making their value subject to the ongoing risks to be encountered by Sequoia in conducting its business; and
- (b) avoid the possibility of time consuming and expensive litigation with Sequoia over issues on which the rights of the parties are not clear.

RESPECTFULLY SUBMITTED BY:

Deloitte & Touche Inc., in its capacity as
Receiver of the Property of Crocus
Investment Fund

Per:


A.R. Holmes, Senior Vice-President