



District of British Columbia  
Division No. 3 – Vancouver  
Court No. S088488

## Material Adverse Change Report

Section 11.7 of the *Companies' Creditors Arrangement Act*

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

AND

**IN THE MATTER OF THE CANADA BUSINESS CORPORATIONS ACT**  
**R.S.C., 1985 c. C-44**

AND

**IN THE MATTER OF HYDROXYL SYSTEMS INC.**

Pursuant to the Order (the "Initial Order") pronounced December 5, 2008, the Supreme Court of British Columbia granted Hydroxyl Systems Inc. (the "Company") protection from its creditors under the *Companies' Creditors Arrangement Act* (the "CCAA") and appointed Campbell, Saunders Ltd. (the "Monitor") as CCAA Monitor.

Section 11.7(3)(b(i) of the CCAA requires the Monitor to file a report with the Court on the state of the Company's business and financial affairs forthwith after ascertaining any material adverse change in the Company's projected cash-flow or financial circumstances. The Canadian Association of Insolvency and Restructuring Professionals defines "Material Adverse Change" in its Standard Professional Practice No. 99-6 to mean a change, in the Monitor's opinion, which:

- has a significant adverse effect on the projected cash-flow; or
- impairs the ability of the insolvent person to carry on operations; or
- impairs the likelihood of success of a proposal; or
- significantly prejudices the rights or interests of one or more classes of creditors

### MATERIAL ADVERSE CHANGE

The Company filed a revised cash-flow dated April 30, 2009, projecting revenues as follows:

1. in the aggregate amount of \$487,950 for the period April 27, 2009, to June 19, 2008;

2. in the aggregate amount of \$1,556,565 for the period April 27, 2009 to December 31, 2009;

Depending on the time frame analyzed, projected receivables from Aker/STX comprise 65% to 75% of the Company's total projected receivables for the remainder of 2009.

In 2007, the Company commenced legal proceedings in Finland against KrügerKaldnes AS seeking to have certain patents registered to KrügerKaldnes AS declared invalid. The Company was unsuccessful in these legal proceedings, and on or about March 13, 2009, the Finnish Court awarded costs to KrügerKaldnes AS in the amount of EUR\$277,486.01, being approximately CDN\$430,103 (the "Costs Award").

On or about May 18, 2009, KrügerKaldnes AS commenced proceedings to enforce the Costs Award by issuing an attachment order to Aker/STX. As a result, until the attachment order is vacated or varied or some other arrangement is made, Aker/STX cannot pay any further amounts to the Company.

The Monitor has been advised by management of the Company that the Company is working diligently to address this issue.

### CONCLUSION

The Monitor has determined that the above information results in a Material Adverse Change in the cash-flow projections and financial circumstances of the Company.

This conclusion has been discussed with management of the Company.

Dated this 25<sup>th</sup> day of May 2009

Campbell, Saunders Ltd.  
In its capacity as Monitor of Hydroxyl Systems Inc.  
Per:



Steve Lum, CIRP