

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

The following Management discussion and analysis is dated November 8, 2011 and is a review of the financial results of HSE Integrated Ltd. (“HSE”, “We”, “Our”, or the “Corporation”) for the three and nine month periods ended September 30, 2011 and 2010. This MD&A should be read in conjunction with HSE’s other documents filed on SEDAR at [www.sedar.com](http://www.sedar.com). Unless otherwise disclosed, the financial information presented in this discussion has been prepared in accordance with International Accounting Standard 34 *Interim Financial Reporting*. The consolidated interim financial information is for part of the period covered by the first International Financial Reporting Standards (IFRS) consolidated annual financial statements and IFRS 1 *First-time Adoption of International Financial Reporting Standards* has been applied. This MD&A takes into consideration information available to Management up to November 8, 2011. Unless otherwise stated, tabular amounts presented are expressed in thousands of Canadian dollars and per-share figures in dollars per weighted-average common share. The following MD&A contains forward-looking information and statements. Please refer to the end of the MD&A for the disclaimer on forward-looking statements.

### SELECTED FINANCIAL INFORMATION

	Three months ended Sept 30, 2011	Three months ended Sept 30, 2010 <sup>(2)</sup>	Year-over-year % change	Nine months ended Sept 30, 2011	Nine months ended Sept 30, 2010 <sup>(2)</sup>	Year-over-Year % change
Revenue	\$ 24,277	\$ 20,349	19.3%	\$ 73,663	\$ 59,606	23.6%
Direct operating expenses	17,747	16,366	8.4%	56,961	49,381	15.4%
Operating margin <sup>(1)</sup>	6,530	3,983	63.9%	16,702	10,225	63.3%
Operating margin %	26.9%	19.6%		22.7%	17.2%	
Selling, general and administrative	\$ 2,651	\$ 2,027	30.8%	7,089	5,891	20.3%
Net earnings (loss)	1,834	175	948%	2,882	(484)	696%
Per-share basic	0.05	0.00		0.07	(0.01)	
Per-share diluted	0.04	0.00		0.07	(0.01)	
EBITDA <sup>(1)</sup>	\$ 3,879	\$ 1,956	98.3%	\$ 9,613	\$ 4,334	121.8%
EBITDA %	16.0%	9.6%		13.0%	7.3%	
Total assets				\$ 55,376	\$ 48,070	15.2%
Total long-term liabilities				\$ 8,941	\$ 8,317	7.5%

(1) See “Non-GAAP Measures” (Page 16)

(2) IFRS transition date was January 1, 2010; 2010 financial results have been adjusted to conform to IFRS

### FINANCIAL REVIEW

#### Overview

HSE operates in two geographic segments – Canada and the United States – providing health and safety services to industry and the public sector. The Corporation offers a package of integrated asset, worker and community health and safety protection services including: onsite safety supervision; gas detection; fixed and mobile air quality monitoring; breathing equipment rentals and services; fixed and mobile firefighting and fire protection services and equipment; worker shower (decontamination) services; onsite medical services; first aid; emergency medical response; worker safety training; industrial hygiene services; and safety consulting and supervision.

Total revenue for the three months ended September 30, 2011 increased 19.3% to \$24,277 from \$20,349 in 2010. Operating margin (see “Non-GAAP Measures”) was \$6,530 or 26.9% of revenues, up 63.9% from \$3,983 or 19.6% of revenues in 2010. Selling, general and administrative expense (“SG&A”) increased to \$2,651 from \$2,027 in the prior year. As a percentage of revenue, SG&A increased from 10.0% of revenue in fiscal 2010 to 10.9% in 2011. The year-over-year SG&A increase related to costs associated with the Corporation’s Business Development group and the recognition of a liability for post-employment benefits related to the transition of CEOs in the quarter. HSE reported earnings of \$1,834 or \$0.05 per share for the third quarter of 2011 compared to earnings of \$175 or \$nil per share for the same period in 2010. EBITDA – Earnings before interest, taxes, depreciation and amortization (see “Non-GAAP Measures”), for the period was \$3,879 or 16.0% of revenue in 2011, a 98.3% increase from \$1,956 or 9.6% of revenue in 2010.

**HSE Integrated Ltd.**

## Management Discussion and Analysis

For the three-month and nine month periods ended September 30, 2011 and 2010

Total revenue for the nine month period increased 23.6% from \$59,606 in 2010 to \$73,663 in 2011. Operating margin was \$16,702 or 22.7% of revenue compared to \$10,225 or 17.2% of revenue in the prior year. SG&A was \$7,089 for the period, an increase of 20.3% from \$5,891 in the prior year. As a percentage of revenue SG&A decreased from 9.9% of revenue in 2010 to 9.6% in 2011. The company reported earnings of \$2,882 or \$0.07 per share compared to a loss of \$484 or (\$0.01) per share for the first nine months of the 2010 fiscal year. EBITDA for the period was \$9,613 or 13.0% of revenue, compared to \$4,334 or 7.3% of revenue a year ago.

**Revenue**

The Corporation provides health and safety services to customers in two distinct client classifications: Industrial and Oilfield. The differentiation takes place primarily because of the industries served and activity drivers that affect demand.

Industrial health and safety services are those provided to multiple industries and the public sector and include a wide range of clients including manufacturing, processing, refining and other facilities that operate continuously on a year-round basis. The customers operate in diverse industries and the public sector including: non-conventional upstream oil development and production (including oilsands extraction); oil and gas processing and refining; petrochemicals; pulp and paper; utilities; power generation; agriculture food and beverage; offshore operations; and manufacturing industries. Industrial revenue includes a mix of year-round contracts and “shutdowns” – scheduled major maintenance projects and repair activities on client facilities. Industrial also includes worker safety training and safety consulting services.

Oilfield operations are associated exclusively with conventional upstream oil and gas activity, which is often short-term, remote, mobile, and temporary because they are related to interruptible exploration, drilling, completion, and workover activities. Demand for Oilfield health and safety services is historically highly cyclical due to external factors such as commodity prices, currency exchange rates, capital markets, weather, and government policy. Even if other factors are stable, demand for Oilfield health and safety services is highly seasonal in Canada because field activity is greatly affected by weather and road access.

The Corporation tracks billings to customers by defined revenue groupings, but uses a common pool of equipment and manpower resources to provide these services. Management, operational support and administration services are provided from a common personnel pool.

The revenue for these business areas is shown below:

	Three months ended September 30		Year-over- year	Nine months ended September 30		Year-over- year
	2011	2010	% change	2011	2010	% change
Industrial	\$ 12,915	\$ 11,384	13.4%	\$ 42,171	\$ 35,234	19.7%
Oilfield	11,362	8,965	26.7%	31,492	24,372	29.2%
Total Revenue	\$ 24,277	\$ 20,349	19.3%	\$ 73,663	\$ 59,606	23.6%
As a percentage of revenue:						
Industrial	53.2%	55.9%		57.2%	59.1%	
Oilfield	46.8%	44.1%		42.8%	40.9%	
Total Revenue	100.0%	100.0%		100.0%	100.0%	

For the three months ended September 30, 2011, one customer provided more than 10% of the Corporation’s total revenue (2010 – one). Sales to this customer amounted to \$2,863 (2010 – \$2,802) during the period related to shutdown work and ongoing long-term energy related projects located entirely in Canada.

**Industrial**

The Industrial health and safety services component of the Corporation’s total revenue increased \$1,531 (13.4%) to \$12,915 in the third quarter of 2011 from \$11,384 in the third quarter of 2010, as the number and size of shutdown projects increased over that in the prior year. For the nine month period ended September 30, 2011, the Industrial health and safety services component of the Corporation’s total revenue increased \$6,937 (19.7%) to \$42,171 from \$35,234 for the same period in 2010. This was due to a large industrial project that ran from January through July, as well as an increase in plant shutdown work, particularly during May, June and September.

Industrial health and safety services generated 57.2% of total revenues year-to-date 2011 down from 59.1% in the same period of 2010.

### **Oilfield**

Oilfield revenues in the third quarter increased by \$2,397 (26.7%) compared to third quarter of 2010 as activity in the Western Canadian Sedimentary Basin (“WCSB”) and penetration into the Texas market increased. For the first nine months of the current fiscal year, Oilfield revenue was \$31,492, 29.2% higher than \$24,372 generated in the same period of 2010. Factors behind the recovery of activity in the WCSB include rising oil prices, improved development economics in Alberta, and continued success by Exploration and Production companies using horizontal drilling and multi-stage fracturing extraction technologies. As well there has been a trend towards higher number of drilling days per well, partly as a result of an increase in deeper zone targets and partly as a result of additional time for drilling horizontally at the target depth. Increased drilling days may increase the number of days medical services may be required, while deeper well depths increase the likelihood that sour gas may be encountered and the requirement for breathing air and gas detection services. As well, multi-stage fracturing requires the use of acid or hydrocarbon fluids, which increases demand for the Corporation’s shower and fire protection services.

In the United States, Boots & Coots HSE Services LLC (“BCHSE”), the Corporation’s venture with Boots & Coots Services contributed \$1,051 to revenue in the third quarter of 2011 compared to \$383 in the same period in 2010. For the nine months ended September 30, 2011 revenue was \$2,453, an increase of 153% over the \$969 generated in the nine months ended September 30, 2010. BCHSE’s customers are typically larger E&P companies whose corporate governance policies require more attention to the health and safety records of their company and their subcontractors. A portion of the work is ongoing work attached to a specific drilling rig where, as long as the rig is active, BCHSE has rental equipment and personnel on location.

### **Direct Operating Expense and Operating Margin**

Operating and materials expense consists of costs directly attributable to the delivery of health and safety services to customers. These include: wages and benefits for field employees and contractors; equipment rentals and leases; field service center property costs; transportation; fuel; consumables; equipment repairs and maintenance; and field office administration including field sales.

Operating margin for the third quarter increased to \$6,530 (26.9% of revenue) in 2011 from \$3,983 (19.6 % of revenue) in 2010. For the nine month period, operating margin increased from \$10,225 or 17.2% of revenue in 2010 to \$16,702 or 22.7% of revenue in the first nine months of 2011. Operating and materials expense for the third quarter increased to \$17,747 or 73.1% of revenue compared to \$16,366 or 80.4% of revenue in the third quarter of 2010. For the first nine months, operating and materials expense totaled \$56,961 or 77.3% of revenue compared to \$49,381 or 82.8% of revenue for the nine months ended September 30, 2010.

While operating margins will naturally increase as revenue increases since the fixed cost portion of the expense is spread over a higher revenue base, several initiatives started in the second quarter of 2011 contributed to this improvement, including more effective fleet and equipment management and more efficient manpower utilization.

The allowance for doubtful accounts receivable was \$425 or 1.8% of trade accounts receivable at the end of the third quarter compared to \$1,100 or 5.7% of trade accounts receivable at December 31, 2010. The major reason for the change in the allowance was the write-off in Q2 of two accounts totaling \$641 against amounts previously included in the allowance. Bad debt write-offs against the allowance for the quarter ended September 30, 2011 were \$142.

### **Selling, General and Administrative Expense**

Selling, general and administrative (“SG&A”) expense consists of costs not directly attributable to the delivery of services to customers. These include executive management; corporate head-office functions and support services; administrative personnel; corporate sales and marketing costs; liability insurance; professional fees; and public company costs.

SG&A for the quarter totaled \$2,651 (10.9% of revenue), up from \$2,027 (10.0% of revenue) in the prior year. For the first nine months, SG&A increased to \$7,089 from \$5,891 in the prior year. As a percentage of revenue SG&A decreased to 9.6% from 9.9% in the first nine months of 2010. The increase is related to the creation of the Corporation’s Business Development group, as well as higher bonus accruals as a result of improved profitability and the recognition of a liability of \$345 for post-employment benefits on the transition between CEOs in August.

## **EBITDA and Net Earnings**

EBITDA in the quarter increased 98.3% to \$3,879 from \$1,956 in the third quarter of 2010. The EBITDA margin was 16.0% for the quarter, up from an EBITDA margin of 9.6% in the third quarter of 2010. For the first nine months of 2011 EBITDA was \$9,613, up 121.8% from \$4,334 in the same period of 2010. This EBITDA increase was the result of the previously mentioned improvements in operating margin and control of expenses. Improved financial performance by BCHSE was also a contributing factor as BCHSE contributed \$291 in EBITDA (\$614 year-to-date) compared to \$88 in the third quarter of 2010 (\$101 year-to-date).

Property and equipment depreciation for the quarter was \$1,175, down from \$1,364 in the third quarter of 2010. Property and equipment depreciation for the nine months ended September 30, 2011 was \$3,653 down from \$4,359 in the same period of 2010. This is a result of HSE tightly controlling capital additions in 2009 and 2010. This reduction was partially offset by HSE undertaking a larger capital expansion program in 2011 than in the prior two years. Year-to-date capital additions (excluding light vehicles added through finance leases) totaled \$3,205 in 2011 compared to \$1,449 in 2010 and \$1,384 in 2009.

Intangible asset amortization for the quarter was \$123, up from \$103 in third quarter 2010. Intangible asset amortization for the nine months ended September 30, 2011 was \$368, up from \$309 in the same period of 2011. The increase in amortization is a result of the intangible assets acquired as part of the Taylored Safety acquisition that occurred on January 24, 2011.

Stock-based compensation for the third quarter was \$81 (2010 – \$26) consisting of equity settled awards of \$71 (2010 - \$47) and cash settled awards (“DSU”) of \$10 (2010 – (\$21)). Stock-based compensation for the nine months ended September 30, 2011 was \$190 (2010 - \$146) consisting of equity settled awards of \$162 (2010 - \$155) and cash settled awards of \$28 (2010 - \$(9)). The change in DSU expense is related to changes in the Corporation’s share price during the quarters and the resulting effect on the Black-Scholes valuation of the DSU. The increase in the expense for equity settled awards relates to year-over-year increases in strike prices as the Corporation’s share price improves.

Finance costs for the three months September 30, 2011 totaled \$157, up from \$137 for the same period in 2010. For the nine months ended September 30, 2011 finance costs totaled \$571, up from \$546 for the same period in 2010. Loans and borrowings declined in 2011 from the same period in 2010 as scheduled principal payments totaling \$327 on bank debt and \$636 on finance leases were made in the quarter resulting in a decrease to financing costs. Offsetting this was interest and accreted interest on the convertible debentures issued by the Corporation in December of 2010 and January of 2011.

The Corporation recognized a current tax provision of \$553 in the quarter (\$1,379 year-to-date) compared to a provision of \$502 in the third quarter of 2010 (\$187 year-to-date). The Corporation had a deferred tax recovery of \$44 in the quarter compared to a recovery of \$598 in the third quarter of 2010. For the nine months ended September 30, the deferred tax expense was \$569 in the current year compared to a recovery of \$531 in the prior year. The year-to-date differences relate to improved profitability as well as the receipt of tax assessments as described in the second quarter MD&A. These reassessments required the payment (and recognition as a current expense) of amounts previously recognized as a deferred tax asset.

Net earnings for the quarter were \$1,834 or \$0.05 per share compared to \$175 or \$nil per share in 2010. For the nine-month period, net earnings improved to \$2,882 or \$0.07 per share compared to a loss of \$484 in the prior year or (\$0.01) per share in 2010. The year-over-year increase was due to improvements in revenue, improved operating margins as cost reduction strategies were implemented, and reduced amortization charges.

## **Current Quarter versus Q2 2011**

Revenue for the third quarter decreased 2.5% to \$24,277 from \$24,905 in the previous quarter. Oilfield health and safety revenue increased by \$3,156 as the Western Canadian Sedimentary Basin returned to work after spring breakup. Unusually wet weather, particularly in southern Saskatchewan, delayed some Oilfield work until late July. Normally industry activity would resume in mid May to mid June in these areas. Industrial revenue decreased by \$3,784 as safety work on a large construction project that had commenced in January was completed in late July. As well, a number of significant shutdown projects were completed in the prior quarter by HSE’s Industrial sector.

Operating expenses decreased by \$1,519 from \$19,266 (77.4% of revenue) to \$17,747 (73.1% of revenue). This is due to a number of factors, including improvements in personnel and equipment efficiencies and continued focus on cost reductions.

SG&A increased from \$2,391 in the previous quarter to \$2,651 in the current quarter primarily as a result of the recognition of post-employment benefits totaling \$345 on the transition between CEOs.

## Liquidity and Capital Resources

The Corporation's principal sources of capital are cash flows from operations, borrowings under an established credit facility with its senior lender, convertible debentures, finance leases and equity financing.

The Corporation, through the conduct of its operations, has undertaken certain contractual obligations as noted in the following table:

Years ended December 31	2011	2012	2013	2014	2015	Thereafter	Total
Finance lease obligations	\$ 615	\$ 1,515	\$ 567	\$ 234	\$ 65	–	\$ 2,996
Rental facilities & equipment	830	3,160	2,716	2,299	1,800	3,605	14,410
Convertible debentures				2,000			2,000
Term debt <sup>(1)</sup>	326	1,304	1,304	435	–	–	3,369
<b>Total contractual obligations</b>	<b>\$ 1,761</b>	<b>\$ 5,969</b>	<b>\$ 4,578</b>	<b>\$ 4,961</b>	<b>\$ 1,862</b>	<b>\$ 3,605</b>	<b>\$ 22,736</b>

(1) Principal portion only

### Liquidity

At September 30, 2011, the Corporation had cash on hand of \$1,291.

On April 27, 2010 the Corporation entered into a \$15,000 credit facility with a regional financial institution. The facility consists of a \$10,000 revolving operating loan facility for general operating purposes and a \$5,000 non-revolving reducing loan facility.

The \$5,000 non-revolving term facility is repayable in monthly payments of \$109 starting July 1, 2010. The facility is payable in full 48 months after initial drawdown. The operating facility is renewable annually and is margined to accounts receivable. Both facilities bear interest at prime plus a fixed percentage. A standby fee is also required on any unused portion of the operating facility. Both facilities are subject to certain covenants including a working-capital covenant, a debt-to-equity covenant, a fixed-charge-coverage ratio, and other positive and negative covenants. The facilities are collateralized under a general security agreement that includes accounts receivable and property and equipment.

On May 13, 2011, the Corporation signed a revised credit facility which reflected the effects of the conversion to IFRS. The Corporation complied with all covenants under the credit facility at September 30, 2011.

At September 30, 2011 the total outstanding on the term-loan facility was \$3,369, of which \$1,304 was current. During the quarter the Corporation made scheduled principal long-term debt payments of \$327 and finance lease payments of \$636.

On December 21, 2010 (\$1,925) and January 15, 2011 (\$75), the Corporation issued \$2,000 in Subordinated Secured Convertible Debentures. The Debentures mature on January 15, 2014 and bear interest at 10.0% per annum, payable quarterly in arrears on April 15, July 15, October 15 and January 15 in each year beginning April 15, 2011. The proceeds from the convertible debenture were used to fund part of the Corporation's 2011 capital program.

The Debentures consist of both debt and equity components that are presented separately in the Corporation's consolidated balance sheet. The debt component is measured by calculating the present value of both the quarterly interest obligation and the principal payment due at maturity, using the rate of interest that would have been applicable to a non-convertible debt instrument of the comparable term and risk at the date of issue. The residual portion of the Debenture proceeds is allocated to equity. As a result the debt component of the Debentures is less than the principal amount that would be paid at maturity, assuming no conversion occurs. The discount to face value of the debt component presented on the consolidated balance sheet will be accreted using the effective-interest method over the term of the Debenture. At September 30, 2011 the debt component of the convertible debenture was \$1,827 all of which is long-term.

The Corporation also has finance leases related to its light vehicles. The lease terms range from 3 to 5 years. The Corporation's obligations under finance leases are secured by the lessors' title to the leased assets. The terms and conditions of the finance lease contract do not specify any contingent rents, escalation clauses or any financial restrictions, conditions or covenants in respect of the Corporation's financial position or the related leased assets. At September 30, 2011 the total outstanding on the finance leases was \$2,824, of which \$1,741 was current.

### ***Cash Provided by Operations***

Cash provided by operations in the nine months ended September 30, 2011 was \$5,587 compared to \$3,678 for the same period in 2010. Improved revenue levels and operating margins during the period resulted in higher operating cash flow before considering changes in working capital. The reduction in non-cash working capital of \$3,236 was primarily due to higher trade receivables in the period which was as a result of increased revenues.

Days-sales-outstanding (“DSO”) was 87 days for the quarter compared to 74 days at December 31, 2010 and 75 days at the end of the same quarter in 2010. An unusually high proportion of the Corporation’s revenue was earned in September compared to prior years with the effect that a higher amount of the receivables balance is not yet due at September 30. As well, there were delays in receiving payments on a significant shutdown that completed in late July.

### ***Cash Provided Used in Financing and Investing***

During the quarter, the Corporation made scheduled payments totaling \$327 against its existing term debt facility and \$636 towards outstanding finance leases.

Purchases of property and equipment in the quarter amounted to \$1,118, virtually all of which was for revenue-generating health safety services rental equipment. Proceeds from the disposal of property and equipment were \$18.

### **Working Capital**

At September 30, 2011, the Corporation had working capital of \$14,342. This compares to \$12,016 at December 31, 2010 and \$9,217 at September 30, 2010.

### **Acquisition**

On January 24, 2011 the Corporation acquired all of the outstanding common shares of Taylored Safety Services Inc. (“Taylored”) with the issue of 1,137,532 shares at a price of \$0.54. Taylored provides safety consulting and industrial health services, and training to industry and is headquartered in Halifax, Nova Scotia.

### **Outlook**

The overall outlook for HSE for the remainder of 2011 and into 2012 is generally positive.

Risks to the Corporation include:

- Reductions in general economic growth levels. Estimates of Gross Domestic Product (“GDP”) growth in Canada and the United States for 2011 and 2012 have dropped by 0.7% since the first quarter of 2011. In the Bank of Canada’s Monetary Policy report issued October 25, 2011, the Bank’s targets were reduced to 2.1% for 2011 and 1.9% for 2012, with a rebound to 2.9% for 2013. These forecasts are approximately the same as those issued by private sector economists in September. The forecasts have reflected slowdowns in the European and US markets, with concerns about Canada’s export markets. These slowdowns may affect our Industrial work, particularly in Central Canada and the US.
- Depressed natural gas prices. Natural gas prices have dropped and look to remain low until supply imbalances are addressed. According to the US Energy Information Administration (“EIA”), the Henry Hub natural gas price averaged \$4.12 per thousand BTU in the quarter, down from \$4.28 a year ago and from highs in the \$10.00 range in the mid-2000’s. Because of increases in supply as a result of improvements in technology, which allowed the production of shale gas, there is an over-supply which has depressed prices. Until pipelines are constructed and liquefaction facilities are built to allow gas to be exported to areas outside North America, these depressed prices are likely to continue. Natural gas drilling and workover activity, and in particular “sour” gas work, has historically been the source of a large portion of the Corporation’s Oilfield safety work.
- Labor costs and availability. The Corporation tends to experience shortages of skilled workers at times. As well, the Corporation’s activity levels tend to vary, as the work is dependent on the customer’s schedule rather than an in-house production schedule. The Corporation had a number of large shutdowns that occurred at the same time in May through July, followed by a break from late July through early September. This was followed by the startup of a number of large shutdowns that all started within the same week in September. These events require that the Corporation vary its staff levels to meet shutdown requirements in addition to regular ongoing Industrial projects and Oilfield work.

- Stock market constraints. A portion of our customer base, junior oil and gas producers, raise funds for drilling activity through stock issues rather than operating cash flow. The constraints in the stock markets, particularly over the last three months may have an impact on their ability to raise these funds for the 2011 – 2012 winter drilling season. While the Corporation tends to be less exposed to these companies, it does present a possible risk to the Oilfield activity for the winter.

However, a number of factors point to improvements in revenues and profitability. These include:

- Oil prices. In spite of shocks to the economy and warnings about reductions in GDP, oil prices have traded higher over the last year. According to the EIA, West Texas Intermediate (“WTI”) averaged just under \$90 per barrel during the third quarter of 2011 compared to \$76 per barrel for Q3 of 2010. These prices are expected to continue into 2012. For example, CIBC World Markets October Commodities update forecasts that WTI will average \$92 per barrel throughout 2012. At this price, it is likely that our customers will continue oil-directed drilling and workover activity, as well as oilsands activity, at a pace at least equivalent to existing activity. On November 3, 2011 the Petroleum Services Association of Canada (“PSAC”) released its 2012 drilling forecast which predicted a 10% increase in wells drilled in 2012 to 15,100 from an upwardly revised 2011 total of 13,700 wells. These estimates were predicated on an average price for WTI of \$85 per barrel throughout 2012 and an average AECO spot price for natural gas of \$3.50 / mcf.
- Strategic Framework Initiatives. The Corporation prepared a Strategic Framework in the first quarter that included geographic areas where the Corporation could increase market share. The Framework also proposed initiatives to improve profitability through better cost control. Cost reduction initiatives that the Corporation undertook starting in the second quarter are now showing a positive impact. We expect that these cost control initiatives will continue.

On balance, Management expects activity in existing markets to remain steady or increase slightly.

### ***Industrial***

Industrial revenue is derived from a combination of long-term safety work, shutdowns and other project work. Long-term contracts include provision of safety, medical or fire and shower protection for construction projects and operating facilities. Revenue from these sources tends to be fairly stable. With major oilsands projects being contemplated over the next several years, northeast Alberta will be a significant driver of growth. Shutdowns and project work can vary from one person for one or two days to fifty or more staff and associated equipment for periods of two to three months. These projects are associated with plant shutdowns, and tend to recur, but may not occur every year. Each project is bid and Industrial revenue for a given year will be partially dependent on the number of contracts awarded for shutdowns in that year. The bidding process for the 2012 shutdown season is under way, and results look promising.

In the first quarter of 2011, HSE expanded into the business area of safety supervision and consulting services with the establishment of a Consulting Services Division, which will provide expert safety supervisors to projects on a contract basis. HSE’s consulting group has secured a number of contracts that will be executed in the fourth quarter. HSE believes that Consulting Services will provide a strong vertical integration with the other services the Corporation offers.

### ***Oilfield***

HSE’s Oilfield business continues to increase from its low point in 2009. One reason for this recovery is the overall increase in drilling activity, particularly in Alberta. While the Corporation’s Oilfield revenue is not directly proportional to wells drilled or rig operating days, it is correlated to drilling activity.

In addition to increased drilling activity, there has also been a shift from drilling targeted at natural gas formations, particularly shallow gas, toward drilling targeted at oil, often in deeper formations. As a result although well counts have dropped significantly since peaking in 2007, operating days for drilling rigs have not been impacted to the same extent. While it is not a certainty, deeper wells could encounter sour gas (and thus require breathing air services) as they drill to target depth, and are more likely to require on-site medical services.

As well, the Corporation’s fire / shower business has increased significantly as a result of changes in drilling technology. In particular multi-stage fracturing is commonly performed using flammable hydrocarbons. Fracturing of this type requires that fire protection be available on site.

In a press release dated June 1, 2011, the Canadian Association of Oilwell Drilling Contractors (“CAODC”) released a forecast update for 2011. The revision predicted an increase in the number of rigs operating, in the average well depth and in the number of operating days over the balance of the year. While the actual increase for the third quarter was less than predicted (primarily because of rain and flooding affecting large portions of southeast Saskatchewan and southern Manitoba), rig activity is heading toward predicted levels. To the end of September, there have been 10,107 wells completed in the WCSB, an increase of 32% over 2010.

In November, a number of petroleum producers released guidance on their expectations for 2012 drilling. These showed increases of between 5% and 15%, but contained caveats that the budgets may be adjusted depending on cash flow. Presenters to the 2012 PSAC Drilling Activity Forecast predicted that the mix of drilling in 2012 would be heavily weighted to oil formation targets, particularly deeper targets, with an increase in average days per well to 10.3 for 2012 from 9.0 in 2011.

This shift to drilling fewer, deeper wells with oil as the target instead of gas has changed demand for HSE's Oilfield health and safety services. A rise in the number of rig-operating days is good for HSE's medical services business. This level and type of activity also increases the demand for HSE's mobile fire and shower services because many of these oilwells are completed using large volumes of flammable hydrocarbon fracturing fluids or abrasive hydrochloric acid.

As mentioned, the outlook for natural gas remains challenged. Of the wells completed to the end of September, 3,443 or 34% were gas wells compared to 3,736 or 49% in 2010. Activity has tended to be aimed toward formations that are rich in natural gas liquids. Presenters at the 2012 PSAC Drilling Activity Forecast on November 3 estimated that only about 20% of the wells drilled in the 2012 would be for gas targets. These wells tend to be drilled to maintain drilling licenses or to target liquids-rich formations.

### **United States**

HSE has reported segmented financial information for its two U.S. operations: CRS Technologies Inc. ("CRS"), which operates from Taylor, Michigan (a suburb of Detroit), and Boots & Coots HSE Services LLC, which operates from a head office in Houston, Texas with a stand-alone regional BCHSE service location in Midland, Texas, as well as through other Boots & Coots Services service locations in the region.

BCHSE contributed \$1,051 to revenue for the three months ended September 30, 2011, almost tripling its revenue of \$383 for the same period in 2010. The Corporation's 2011 capital budget included \$830 for rental equipment expansion for BCHSE. In July, an additional \$250 was approved to respond to demands for more equipment. Customers have responded to the quality of work and equipment with requests for more work. During the third quarter BCHSE signed an MSA with the US subsidiary of a Canadian intermediate oil and gas company. As well, it began to receive multiple requests for fire / shower services. Since mid August the fire / shower unit has been active on multi-stage fracturing jobs.

CRS contributed \$548 to revenue for the three months ended September 30, 2011, compared to \$535 for the same period in 2010. Growth has been steady but because the market is more mature, competition is stiff. HSE believes that in the future, further penetration of the large U.S. industrial health and safety services market is possible from this location.

While long-term growth for HSE will be focused on US expansion, for 2012 the plan is to focus on gaining market recognition and growing organically in both Canada and the US.

### **Quarterly Results**

	2011			2010 <sup>(2)</sup>			2009 <sup>(2)</sup>	
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Revenue	\$ 24,277	\$ 24,905	\$ 24,481	\$ 22,422	\$ 20,349	\$ 18,350	\$ 20,907	\$ 19,090
Net earnings (loss)	1,834	541	507	923	175	(783)	124	(2,178)
Per share								
Basic	\$ 0.05	\$ 0.01	\$ 0.01	0.02	0.00	(0.02)	0.00	(0.06)
Diluted	\$ 0.04	\$ 0.01	\$ 0.01	0.02	0.00	(0.02)	0.00	(0.06)
EBITDA <sup>(1)</sup>	3,879	3,248	2,486	2,459	1,956	411	1,966	496

(1) See "Non-GAAP Measures" (Page 16)

(2) IFRS transition date was January 1, 2010; 2010 financial results have been adjusted to conform to IFRS; 2009 financial results have not been restated and are presented in previous Canadian GAAP

HSE's business has two seasonal components. Revenue for Oilfield health and safety services is historically highest in the first and fourth quarters and lowest in the second quarter because this sector uses equipment that can only access well locations during certain times of the year, and because of the effects of weather on field activity. Industrial revenue includes a mix of year-round contracts and shutdowns. These shutdowns tend to be scheduled during the second and third quarters to avoid the possibility of adverse effects from freezing weather. As a result, Industrial revenue tends to be highest in the second and third quarters.

**HSE Integrated Ltd.**

Management Discussion and Analysis

For the three-month and nine month periods ended September 30, 2011 and 2010

Revenue by quarter for the last eight quarters is as follows:

	2011			2010 <sup>(1)</sup>			2009 <sup>(1)</sup>	
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Industrial	\$ 12,915	\$ 16,699	\$ 12,557	\$ 12,040	\$ 11,384	\$ 11,926	\$ 11,924	\$ 12,533
Oilfield	11,362	8,206	11,924	10,382	8,965	6,424	8,983	6,557
Total revenue	\$ 24,277	\$ 24,905	\$ 24,481	\$ 22,422	\$ 20,349	\$ 18,350	\$ 20,907	\$ 19,090

(1) IFRS transition date was January 1, 2010; 2010 financial results have been adjusted to conform to IFRS; 2009 financial results have not been restated and are presented in previous Canadian GAAP

**Related-Party Transactions****Key Management Personnel and Director Transactions**

Members of key management personnel, officers, or director, or their related parties, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of these entities. A number of these entities transacted with the Corporation in the reporting period. The aggregate value of transactions and outstanding balances relating to key management personnel and entities over which they have control or significant influence are as follows:

Director / key management personnel	Transaction	Note	Transaction value				Accounts Payable Balances outstanding as at	
			Three months ended September 30		Nine months ended September 30		Sept 30 2011	Dec 31 2010
			2011	2010	2011	2010		
Director	Office rent and property taxes	(i)	58	57	212	222	–	–
Director	Supplies and sub-license fees (per agreement)	(ii)	240	88	863	173	40	55
Key Manager	Office rent and Property taxes	(iii)	85	74	272	230	–	–
Directors / Officers	Convertible debentures	(iv)	–	–	40	–	40	–
Director	Post-Employment Benefit	(v)	345	–	345	–	330	–

- (i) The Corporation paid rent and property taxes for one of its regional offices to a corporation which is controlled by a member of the Board of Directors. The term of the lease is 15 years and expires on January 31, 2019.
- (ii) The Corporation purchased various safety supplies and performed maintenance on safety equipment under a sub-license agreement with a corporation which is controlled by a member of the Board of Directors.
- (iii) The Corporation paid rent and property taxes for one of its regional offices to a corporation controlled by a Senior Manager for a subsidiary in the United States. The term of the lease is 5 years and expires on December 31, 2015.
- (iv) A placement of convertible debentures to related parties occurred in December 2010 and January 2011. The related parties were directors, family of directors, and officers of HSE.
- (v) The Corporation recognized a liability for post-employment benefits of \$345 on the transition between CEOs in August 2011. The benefit is payable monthly over a 2 year term and expires August 31, 2013.

Significant subsidiaries	Country of incorporation	Ownership Interest	
		September 30, 2011	December 31, 2010
HSE Integrated Inc. ("INC")	USA	100%	100%
Boots & Coots HSE Services, LLC ("BCHSE")	USA	90%	90%
CRS Technologies Inc. ("CRU")	USA	100%	100%

## Critical Accounting Policies and Estimates

This MD&A summarizes HSE's financial condition and results of operations based upon its Interim Financial Statements, which were prepared in accordance with IFRS. The unaudited interim consolidated financial statements require management to select significant accounting policies which are contained within the notes to statements. These significant accounting policies involve critical accounting estimates due to complex judgments and assumptions required to be made by management. These estimates, judgments and assumptions are based on the circumstances that exist at the reporting date and may affect the reporting amounts of earnings and expenses during the reporting periods and the carrying amounts of assets, liabilities, accruals, provisions, contingent liabilities, and other financial obligations as well as the determination of fair values.

### ***Allowance for Doubtful Accounts Receivable***

The Corporation assesses any impairment of trade receivables through a continuous process of reviewing its receivables both on an individual-customer basis and on an overall basis. The review includes an assessment, performed at least monthly, of the aging status of customers, historical collection experience, financial condition of customers, industry economic trends, and other factors. Based on the review, allowances for specific customers are determined. The process involves a high degree of judgment and can frequently involve significant dollar amounts. Accordingly, the Corporation's financial position, results of operations, and cash flows can be affected by adjustments to the allowance when actual losses differ from estimates.

### ***Impairment Tests***

The Corporation assesses, at the end of each reporting period, whether there is an indication that an asset group may be impaired. Goodwill is reviewed for impairment annually or more frequently if there are indications that impairment may have occurred. If any indication of impairment exists, HSE estimates the recoverable amount of the asset group. External triggering events include, for example, changes in customer or industry dynamics, commodity prices, drilling levels and economic declines. Internal triggering events for impairment include lower profitability or obsolescence.

The Corporation's impairment tests compare the carrying amount of the asset or cash generating unit ("CGU") to its recoverable amount. The recoverable amount is the higher of fair value less costs to sell and value in use. The determination of value in use requires the estimation and discounting of cash flows which involves key assumptions that consider all information available on the respective testing date. Management uses its judgment, considering past and actual performance as well as expected developments in the respective markets and in the overall macro-economic environment and economic trends to model and discount future cash flows.

### ***Property, Plant and Equipment and Intangible Assets***

Property, plant and equipment and intangible assets are recorded at cost less accumulated amortization and accumulated impairment losses. The depreciation methods used and estimates of useful lives and residual values of assets are established by management based on industry norms, historical experience and other information. If these estimates are incorrect, asset values, depreciation expense and gain / loss on disposal of assets could be affected.

### ***Acquisitions***

The assets and liabilities acquired through business combinations are recognized at fair value on the date HSE effectively obtains control. The measurement of business combinations is based on the information available at the acquisition date. The determination of fair value of the acquired intangible assets (including goodwill), property, plant and equipment and other assets and the liabilities assumed at the date of acquisition, as well as the useful lives of the acquired intangible assets and property, plant and equipment, is based on projected cash flows and market conditions at the date of acquisition. These amounts are based on various assumptions and could be materially affected if these assumptions are inaccurate.

### **Lease Classification**

The Classification of a lease as operating or financing depends upon whether substantially all the risks and rewards of the asset are transferred. The Corporation has determined that its facility leases are operating leases since the rent paid to the landlords is increased to market rates at regular intervals and the Corporation does not participate in the residual value of any of the buildings. The Corporation has determined that its light duty vehicles are finance leases since the lease payments cover effectively 100% of the value of the leased asset.

### **Income Taxes**

Tax interpretations, regulations and legislation in the various jurisdictions in which the Corporation and its subsidiaries operate are subject to change. In addition, the Corporation's tax liabilities may be affected by complexities introduced as a result of business acquisitions. As such, income taxes are subject to measurement uncertainty and the interpretations can impact net earnings through the income tax expense arising from the change in current and deferred income tax assets or liabilities.

### **Future Accounting Pronouncements**

In October, 2010 the IASB published amendments to IFRS 9 "Financial Instruments", which is the result of the first phase of the International Accounting Standards Board's (IASB) project to replace IAS 39 "Financial Instruments: Recognition and Measurement". The amendments are effective January 1, 2013, with early adoption permitted. The Corporation intends to adopt the changes in its financial statements commencing January 1, 2013. The new standard replaces the current multiple classification and measurement models of financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. As well, it requires various changes to the treatment of gains and losses on financial assets and liabilities measured at fair value. The adoption of this standard is not expected to have a material impact on the Corporation's Consolidated Financial Statements.

In October, 2010 the IASB also issued amendments to IFRS 7 "Financial Instruments: Disclosures", effective for fiscal years beginning on or after January 1, 2012. The Corporation intends to adopt the amendments effective January 1, 2012. The changes provide for additional disclosures with respect to transferred financial assets where the assets are not derecognized in the financial statements. The changes are not expected to have a material impact on the Corporation's financial statements.

In May, 2011 the IASB issued the new standards IFRS 10 "Consolidated Financial Statements", IFRS 11 "Joint Arrangements" and IFRS 12 "Disclosure of Interests in Other Entities". As a consequence, the IASB reissued IAS 27 "Consolidated and Separate Financial Statements" as IAS 27 (2011) "Separate Financial Statements" and reissued IAS 28 "Investments in Associates" as IAS 28 (2011) "Investments in Associates and Joint Ventures". These standards are all required to be adopted for fiscal years beginning on or after January 1, 2013, with early adoption permitted. IFRS 12 may be early adopted without the adoption of the other standards, but if any other provisions are adopted, all standards must be adopted concurrently.

IFRS 10 provides a single model, based on a revised definition of control, for purposes of determining when an entity is considered to be a subsidiary, with the consequent requirement to consolidate the entity's assets and liabilities and results of operations. IFRS 11 provides revised guidance for the classification of entities subject to joint control, and more restrictive treatment as to the acceptable methods of accounting for entities subject to joint control. IFRS 12 contains the disclosure requirements with respect to investments in subsidiaries, joint arrangements, associates and unconsolidated structured entities. These disclosures are intended to provide additional information about the nature of the Corporation's interests in other entities, the consequent risks to the Corporation and the effects of these interests on the Corporation's financial position, financial performance and cash flows.

As a consequence of the issue of IFRS 10, IAS 27 has been amended to remove any prior guidance with respect to consolidated financial statements. It carries forward the existing guidance with respect to preparation of separate financial statements. As well, IAS 28 was amended to clarify the accounting in specific cases related to discontinued operations and to changes in interests held in associates and joint ventures.

The Corporation intends to adopt these changes effective January 1, 2013. The Corporation does not expect the adoption of these amendments to have a material effect on the financial statements.

In May, 2011 the IASB issued IFRS 13 "Fair Value Measurement", to be applied prospectively effective January 1, 2013. IFRS 13 replaces the fair value measurement guidance provided in individual standards with a single definition of fair value. It does not change the circumstances where fair value is permitted or required, but instead provides guidance as to how to measure fair

value in circumstances where fair value is appropriate. The Corporation intends to adopt IFRS 13 prospectively effective January 1, 2013. The Corporation does not expect IFRS 13 to have a material impact on the financial statements.

## **Financial and Other Instruments**

The Corporation's financial instruments include cash and cash equivalents, accounts receivable, other long-term receivables, bank indebtedness, accounts payable and accrued liabilities, and loans and borrowing. The carrying value of these instruments approximates their fair value, either because of their short maturities or because the interest rates to which they are subject approximate market rates.

The Corporation is exposed to the following risks from its financial instruments:

- Credit risk
- Liquidity risk
- Market risk

These risks, and the Corporation's method of mitigating the risks, are described following:

### ***Credit Risk***

Credit risk is the risk of financial loss to the Corporation if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Corporation's receivables from customers. The maximum credit exposure associated with trade accounts receivable is the carrying value.

The Corporation's trade receivables are due from customers in a variety of industries including a significant proportion with customers operating in the energy and manufacturing industries. The ability of customers within the energy industry to pay the Corporation is partially affected by fluctuations in the price they receive for various hydrocarbon products.

The Corporation follows a credit policy under which the Corporation reviews each new customer individually for credit worthiness before the Corporation's standard payment and delivery terms and conditions are offered. The Corporation's review includes external ratings, where available, and trade references. Customers that fail to meet the Corporation's credit worthiness criteria may transact with the Corporation only on a prepayment basis. On an ongoing basis, the Corporation also reviews the payment patterns of its existing customers and the customers' continued credit worthiness.

Trade receivables are recorded at the invoiced amount and do not bear interest. Standard payment terms are net 30. However, these may be varied by agreements with particular customers. As well, industry practices, particularly within the upstream oil and gas industry, result in payment terms of up to 60 days.

The allowance for doubtful accounts is the Corporation's best estimate of the amount of probable credit losses in the Corporation's existing trade receivables. The Corporation determines the allowance by reviewing individual accounts past due for collectability, assessing historical write-off experience adjusted for changes in both general and industry-specific economic conditions, and overall account aging. The Corporation reviews its allowance for doubtful accounts on an ongoing basis, but at least monthly.

### ***Liquidity Risk***

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they fall due. The Corporation requires liquidity to meet financial obligations as they come due and to fund its operating and investing activities. The Corporation's contractual financial liabilities include interest payments, trade and other payables, income taxes payable, a revolving operating line of credit, a non-revolving term-debt facility, a convertible debenture and finance leases for equipment and vehicles.

HSE manages its liquidity risk by ensuring, to the extent possible, that it has access to funding sources at competitive rates to meet its liabilities when due, under both normal and distressed conditions without unacceptable losses or risking damage to the Corporation's reputation. The Corporation generally uses operating cash flow to provide liquidity to meet its financial obligations. As a result, the Corporation is exposed to a loss of liquidity if its customers delay their payments beyond the levels that they have in the past. To mitigate this, the Corporation has projected its operating cash flows under different scenarios with respect to receivables aging to determine the effect on operating cash inflows. The Corporation monitors its receivables collections to ensure that, if collections are delayed, there are sufficient operating funds available to meet its financial obligations. As well, the Corporation has access to undrawn operating lines of credit of \$10,000 to fund operations.

These credit lines are renewable annually and are margined to accounts receivable. HSE believes it has sufficient funding through these sources to meet its obligations as they come due.

### ***Market Risk***

Market risk is the risk that changes in market prices of financial assets and liabilities, including foreign exchange rates, interest rates, and equity prices, will affect the Corporation's financial position, results of operations, and cash flows.

HSE is exposed to currency risk on U.S.-dollar denominated financial assets and liabilities. The Corporation adjusts the reported amounts of foreign-currency denominated financial assets and liabilities to their Canadian-dollar equivalent at each balance sheet date. For amounts held directly by the Corporation, any related foreign exchange gains and/or losses are recognized in the consolidated statement of earnings. For amounts held by the Corporation's foreign operations, the amount is included in other comprehensive earnings. At September 30, 2011 the extent of this exposure was not material.

HSE is exposed to interest-rate risk on its prime-based revolving operating facility and its non-revolving reducing loan facility. Based on amounts outstanding at September 30, 2011 a 1% increase in the average prime interest rate for the year would cost the Corporation \$34 in additional interest expense.

## **Business Risks**

The activities the Corporation undertakes involve a number of risks and uncertainties, some of which are: economic and market events including disruptions in international credit markets and reductions in macroeconomic activity; business cyclicality within the industries in which HSE's customers operate; competitive conditions including pricing pressures; risks of customer credit default; deterioration in the financial condition of financial institutions and insurance companies with which HSE deals; availability of financing at competitive rates; changes in foreign exchange rates and interest rates; and litigation and contingencies. Additional risks and uncertainties that the Corporation may be unaware of, or that were determined to be immaterial, may also become important factors that affect the Corporation. Further details regarding specific risks that may affect the Corporation are provided below:

### ***Business Cyclicality***

The demand for HSE's Oilfield services is highly dependent upon the level of expenditures made by oil and gas companies on exploration, development and production activities. These expenditures are in turn affected by a number of factors:

- The price received by HSE's customers for crude oil and natural gas directly impacts their cash flow available to purchase the Corporation's services. Fluctuations in crude oil and natural gas prices can produce periods of high and low demand for the Corporation's services. Alternatively, a number of factors that are beyond the control of HSE's customers, including weather, geopolitical conditions, and the strength of the global economy, may reduce demand for their products, which in turn will reduce the price they receive.
- Since crude oil and natural gas prices are normally denominated in U.S. currency, fluctuations in the Canadian-dollar exchange rate relative to the U.S. dollar can also affect the cash flow available to the Corporation's customers to purchase its services.
- Exploration, development and production activity levels within particular markets are influenced by factors including royalties, regulatory and taxation changes, weather, and access to pipeline capacity.
- Changes in equity and debt-financing markets independent of any individual company's circumstances may reduce access to capital that is used to fund exploration, development, and production activities.

These fluctuations in activity can cause cyclical demand swings in the Corporation's activity levels and operating results.

The demand for HSE's Industrial services is exposed to business cycles and contraction risks in the oil and gas industry and other industrial sectors such as forestry, pulp and paper, automotive, manufacturing, mineral extraction, and other segments of the economy that could experience reduced demand or significant fluctuations of the market value of their finished goods. As well, a significant portion of the Corporation's Industrial services are provided to customers in the non-conventional upstream oil and gas industry, including oilsands extraction. These customers are exposed to similar risks with respect to crude oil pricing as customers for whom HSE provides Oilfield services.

### ***Availability of Qualified Staff***

The Corporation's ability to provide reliable service is dependent upon attracting and retaining skilled employees. The demand for workers with particular skills used by the Corporation is high and the supply remains limited.

### ***Competitive Conditions***

The Corporation's main competitor is its own customer base. There is a risk, typically under distressed economic conditions, that customers may elect to use their own personnel to perform services that HSE currently provides. The Corporation attempts to mitigate this risk by providing staff with more training and safety service experience than the customer is able to provide on its own.

While no one competitor in Canada provides the full suite of services that the Corporation provides, HSE has competitors in each market it serves. These competitors are typically privately owned, regionally based companies that provide a specialized set of services. These competitors may provide pricing pressure that may affect our margins and market position within particular lines of business. The Corporation attempts to mitigate this risk by providing an integrated suite of services that our competitors cannot provide, and by distinguishing ourselves through higher levels of service and expertise.

Recently, a larger private-equity-financed U.S. safety services provider commenced operations in Canada. While this provider is currently restricting its activities to providing Industrial safety services within a small portion of the industries and geographic locations in which the Corporation provides services, there is a risk that this competitor may begin to market its services to a wider array of customers and locations. Management is of the view that this may provide an opportunity for additional business for the Corporation as customers may be more likely to outsource safety services work when there is more than one provider available.

### ***Customer Credit***

HSE generally invoices its customers in arrears for its services. Because of this, the Corporation is subject to the risk that its customers may delay payment of its invoices through a variety of means, or fail to pay the invoice at all. Changes in economic conditions, either in general or within a particular industry, may increase this risk.

### ***Customer Dependence***

The Corporation has ongoing contracts or master service agreements with a variety of customers. For certain customers the volume of revenue generated approaches or exceeds 10% of the Corporation's total revenue on a quarterly or annual basis. While there is no indication that any of these customers are likely to change safety service providers, if a contract were cancelled and the Corporation were unable to replace the business with other existing or new customers, the Corporation's revenue, operating results and cash flows would be adversely affected. The Corporation attempts to mitigate this risk by providing an integrated suite of services that are not available from a single competitor, by providing access to our services on a country-wide basis, and by distinguishing itself through higher levels of service and expertise.

### ***Customer and Government Safety Requirements***

All companies are required to track and publish safety statistics. Certain customers require that their vendors maintain specific minimum standards with respect to safety in order to provide services as an accredited vendor. There is a risk that, if the Corporation's safety statistics fall below an acceptable level, it would not be allowed to provide services to these customers. If this occurred, the Corporation's revenues and profit levels would be adversely affected.

As well there is a risk that customer safety requirements and government regulations or legislation may change either as part of an ongoing review process, or in reaction to specific events such as the Macondo blowout in the Gulf of Mexico. While changes in these requirements may provide opportunities to provide health and safety personnel and equipment to the Corporation's customers in order to address new requirements, these changes may also pose the following risks to the Corporation. First, there is a risk that additional expenses may need to be incurred to refit equipment or provide additional training to staff. There is no guarantee that these costs could be passed on to customers and, as a result, the Corporation's profits may suffer if unanticipated changes are made. Second, there is a risk that additional regulations could make an activity or line of business unprofitable for our customers. This could cause them to exit the activity causing a reduction in the Corporation's revenues as customer activity decreases.

The Corporation mitigates these risks by ensuring that its field personnel are trained to levels that meet or exceed "best-practices" levels and that its equipment meets any requirements specified by the equipment manufacturer. The Corporation's

industry technical specialists monitor industry sources to keep the Corporation apprised of potential changes to regulations. As well, the Corporation maintains a comprehensive internal safety program including regular senior management and Board of Directors review of safety results, the use of standardized “best-practices” procedures for all work performed, and specific procedures that require that all incidents be investigated to determine root causes of the incident and to recommend what, if any, changes to the Corporation’s procedures are necessary to prevent recurrence.

### ***Availability of Financing***

Historically, the Corporation has funded the growth of its operations and its acquisitions from bank debt, share issues, and convertible debentures, in addition to cash generated from operations. Continued access to bank debt at competitive rates requires that the Corporation meet various financial and non-financial covenants. There is no certainty HSE will continue to be able to obtain sufficient financing at competitive rates. The Corporation’s ability to grow as planned may be limited if sources of competitively priced financing are unavailable.

### ***Income Taxes***

The Corporation uses various estimates and judgments when preparing corporate tax returns. These returns are subject to audit and reassessment by various tax authorities. These reassessments could have a material effect on reported amounts for income tax assets and liabilities as well as current tax expense.

### ***Foreign-Exchange Exposure***

HSE’s consolidated financial statements are presented in Canadian dollars, but include the results of its U.S. subsidiaries for which the functional currency is the U.S. dollar. Changes in the U.S.-dollar exchange rate versus the Canadian-dollar rate may have material effects on net income and other comprehensive income reported by the Corporation’s U.S. subsidiaries.

### ***Litigation and Contingencies***

In the ordinary course of business activities, the Corporation may be contingently liable for litigation and claims with customers, suppliers, former employees and third parties. Management believes that adequate provisions have been recorded in the accounts where required. Although it may not be possible to accurately estimate the extent of potential costs and losses, if any, Management believes that the ultimate resolution of such contingencies would not have a material adverse effect on the financial position of the Corporation.

## **Disclosure and Internal Controls**

### ***Disclosure Controls and Internal Controls over Financial Reporting***

The Chief Executive Officer (“CEO”) and the Chief Financial Officer (“CFO”) are responsible for designing disclosure controls and procedures (“DC&P”) and internal controls over financial reporting (“ICFR”) as defined in National Instrument 52-109 Certification of Disclosure in Issuer’s Annual and Interim Filings (“52-109”), or causing them to be designed under their supervision, in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

HSE’s DC&P have been designed to provide reasonable assurance that material information relating to HSE is made known to the CEO and the CFO by others and that information required to be disclosed by HSE in its annual filings, interim filings or other reports filed or submitted by HSE under securities legislation is recorded, processed, summarized and reported within the time periods specified in applicable securities legislation. There have been no changes in ICFR during the three month period ended September 30, 2011. Our ICFR have been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. As of September 30, 2011, the CEO and the CFO together with HSE’s management have evaluated the design and effectiveness of the Corporation’s DC&P and have concluded that they are effective.

Because of their inherent limitations, DC&P and ICFR may not prevent or detect all misstatements, errors or fraud. Control systems, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control systems are met.

## Common Shares and Convertible Debentures Outstanding

At September 30, 2011 and November 8, 2011, 38,713,207 common shares of HSE were outstanding (December 31, 2010 – 37,575,675). At September 30, 2011, the Corporation had options outstanding to issue 2,233,666 shares (December 31, 2010 – 2,279,165) at a weighted-average exercise price of \$0.73 per share (December 31, 2010 – \$1.24). Of these options, 1,252,384 were exercisable (December 31, 2010 – 1,154,479). At November 8, 2011 there were 2,251,036 options outstanding at a weighted average price of 0.76 per share. Of these options, 1,292,550 were exercisable.

At September 30, 2011 and November 8, 2011 the Corporation had \$2,000 of convertible debentures outstanding that were convertible to 4.0 million shares based on the applicable conversion price.

## Non-GAAP Measures

Certain measures in this document do not have any standardized meaning as prescribed by IFRS and, therefore, are considered non-GAAP measures.

This report makes reference to Operating Margin, a measure that is not recognized under IFRS. Management believes that, in addition to net earnings, operating margin is a useful supplementary measure. Operating margin is defined as revenue less all direct operating expenses incurred by field operations and support functions such as fleet management. This report also makes reference to EBITDA, a measure that is not recognized under IFRS. Management believes that, in addition to net earnings, EBITDA is a useful supplementary measure. EBITDA provides investors with an indication of earnings before provisions for interest and bank charges, taxes, amortization, foreign exchange gains or losses, gains or losses on the disposal of property and equipment, and the non-cash effect of stock-based compensation expense.

Investors should be cautioned that Operating Margin and EBITDA should not be construed as an alternative to net earnings determined by IFRS as an indication of the Corporation's performance. HSE's method of calculating Operating Margin and EBITDA may differ from that of other companies' and, accordingly, may not be comparable to measures used by other companies.

## EBITDA Calculation

Nine month periods ended September 30	2011	2010 <sup>(1)</sup>	2009 <sup>(1)</sup>
Net earnings (loss)	\$ 2,882	\$ (484)	\$ (4,456)
Add (deduct):			
Depreciation and amortization	4,021	4,668	5,081
Stock-based compensation	190	146	250
Finance costs	571	546	417
(Gain) loss on disposal of property and equipment	1	(198)	254
Income tax expense (recovery)	1,948	(344)	(1,197)
EBITDA	\$ 9,613	\$ 4,334	\$ 349

(1) HSE's IFRS transition date was January 1, 2010; 2010 financial results have been adjusted to conform to IFRS; 2009 financial results have not been restated and are presented in previous Canadian GAAP

## Quarterly EBITDA Calculation

	2011				2010 <sup>(1)</sup>				2009 <sup>(1)</sup>
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4	
Net earnings (loss)	\$ 1,834	\$ 541	\$ 507	\$ 923	\$ 176	\$ (783)	\$ 124	\$ (2,178)	
Add (deduct):									
Depreciation and amortization	1,298	1,382	1,341	1,465	1,466	1,508	1,692	1,618	
Impairment of property and equipment	-	-	-	-	-	-	-	1,641	
Stock-based compensation	81	38	71	39	25	64	57	43	
Finance costs	157	197	217	209	139	212	195	127	
(Gain) loss on disposal of property and equipment		(35)	36	314	247	(132)	(313)	57	
Expiry of contingent consideration liability		-	-	(810)	-	-	-	-	
Income tax expense (recovery)	509	1,125	314	319	(97)	(458)	211	(812)	
<b>EBITDA</b>	<b>\$ 3,879</b>	<b>\$ 3,248</b>	<b>\$ 2,486</b>	<b>\$ 2,459</b>	<b>\$ 1,956</b>	<b>\$ 411</b>	<b>\$ 1,966</b>	<b>\$ 496</b>	

(1) HSE's IFRS transition date was January 1, 2010; 2010 financial results have been adjusted to conform to IFRS; 2009 financial results have not been restated and are presented in previous Canadian GAAP

## Forward-Looking Statements

Certain statements in this MD&A constitute forward-looking information and statements (collectively "forward-looking statements") within the meaning of applicable securities laws. These forward-looking statements concern, among other things, the Corporation's prospects, expected revenues, expenses, profits, financial position, strategic direction and growth initiatives, all of which involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of the Corporation to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. When used in this MD&A, such forward-looking statements use such words as *expect, anticipate, estimate, believe, may, will, would, could, might, intend, plan, continue, ongoing, project, objective, should*, and other similar terms and phrases. These forward-looking statements reflect the Corporation's current expectations regarding future events and operating performance based on assumptions and analyses made by the Corporation based on its experience and an assessment of current conditions, known trends, expected future developments and other factors that Management believe to be appropriate under the circumstances.

These forward-looking statements include among others:

- Expectations as to the effects of increases in drilling activity on the use of the Corporation's services
- Effects of the type of contracts entered into by BCHSE on its prospects for future work
- Expectations as to the outlook for the Corporation
- Expectations as to general economic activity levels and their effect on the Corporation's prospects
- Expectations as to prices for commodities, particularly oil and natural gas, and the effect of changes in those prices on activity levels for the Corporation
- Expectations as to general stock market price levels and the effect of these on portions of the Corporation's customer base
- Predictions as to the timing, duration and quantum of cost control initiatives undertaken by the Corporation
- Expectations as to activity levels in the Corporation's existing markets
- Expectations as to the number and value of shutdown projects to be undertaken by the Corporation in 2012
- Expectations as to the revenue prospects, both direct and ancillary, for the Corporation's Consulting Services Division
- Expectations as to availability and cost for employees

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- Expectations as to the effect of horizontal drilling technology on the Corporation's Oilfield activity levels
- Expectations about drilling activity in the WCSB in 2012
- Expectations with respect to penetration into US Oilfield and Industrial markets

The forward-looking statements contained in this MD&A reflect several material factors, expectations and assumptions including, without limitation: economic conditions within Canada and the United States, both in general and within specific industries; demand for the Corporation's services by customers in various industries and geographic locations; pricing levels for the Corporation's services; commodity prices; foreign currency exchange rates; interest rates; access to financing; the Corporation's future operating results and financial condition; and competition within particular markets or for particular services.

Forward-looking statements involve significant risks and uncertainties and should not be read as a guarantee of future performance or results, and will not necessarily be an accurate indication of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements including, but not limited to, the factors discussed above and other risk factors discussed herein and listed from time to time in the Corporation's reports and public disclosure documents including its annual report, annual information form and other filings with securities commissions in Canada as reported under the Corporation's profile at [www.sedar.com](http://www.sedar.com).

The Corporation cautions that the foregoing list of assumptions, risks and uncertainties is not exhaustive. The forward-looking statements contained in this MD&A speak only as of the date of this MD&A, and the Corporation assumes no obligation to publicly update or revise them to reflect new events or circumstances, except as may be required pursuant to applicable laws.

**Additional Information**

Additional information relating to HSE is available under the Corporation's profile on the SEDAR website at [www.sedar.com](http://www.sedar.com) and [www.hseintegrated.com](http://www.hseintegrated.com).