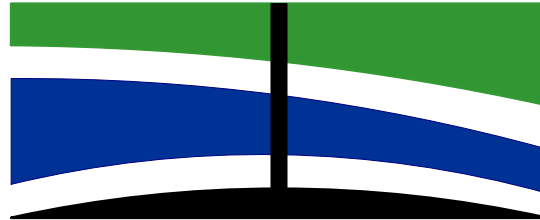


# Deepwell



## Energy Services

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### MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's Discussion and Analysis (MD&A) of Deepwell Energy Services Trust (the "Trust") has been prepared taking into consideration information available to August 13, 2008 and should be read in conjunction with the Trust's unaudited interim consolidated financial statements as at and for the three and six months ended June 30, 2008. This MD&A discusses operations and events for the three and six months ended June 30, 2008. Unless otherwise noted, references to the "quarter" or "Q2-08" refer to the three months ended June 30, 2008. References to "2008" or the "year" or "year-to-date" refer to the six months ended June 30, 2008. References to "Q2-07" refer to the three months ended June 30, 2007. References to "2007" or the "prior year" refer to the six months ended June 30, 2007.

The Trust is an unincorporated investment trust governed by the laws of the Province of Alberta. The business of the Trust is conducted through its direct and indirect wholly owned subsidiaries, Deepwell Energy Services Commercial Trust, Deepwell Energy Services Ltd., and Deepwell Energy Services LP ("Deepwell LP"). The Trust and its subsidiaries (collectively "Deepwell") are based in Calgary, Alberta and were established to acquire and operate businesses that engage in oilfield waste management services. The principal undertaking of Deepwell is to provide a variety of services to oil and natural gas exploration and production companies in western Canada.

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### Forward-looking statements

Certain statements in this MD&A constitute "forward-looking" statements that involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Trust or Deepwell LP, or industry results, 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 statements use such words as "may", "will", "intend", "should", "expect", "believe", "plan", "anticipate", "estimate", "predict", "potential", "continue" or the negative of these terms or other similar terminology. These statements reflect current expectations regarding future events and operating performance and speak only as of the date of this MD&A.

Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether 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.

Although the forward-looking statements contained in this MD&A are based upon what management believes are reasonable assumptions, the Trust cannot assure investors that actual results will be consistent with these forward-looking statements. These forward-looking statements are made as of the date of this MD&A. The Trust does not assume any obligation to update or revise them to reflect new events or circumstances, except as required by applicable securities legislation.

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## **Non-GAAP measures**

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The MD&A has been prepared in accordance with Canadian generally accepted accounting principles (GAAP). Certain supplementary information and measures not recognized under GAAP are also provided where management believes they assist the reader in understanding the Trust's results. These measures include:

- Earnings before interest, taxes, depreciation and amortization (EBITDA); and
- Funds from operations, which refers to cash flow from operating activities before changes in non-cash working capital.

These measures are identified and presented, where appropriate, together with reconciliations to the equivalent GAAP measure. Readers should be cautioned however, that these measures should not be construed as alternatives to measures determined in accordance with GAAP as an indicator of the Trust's performance. The Trust's method of calculating these measures may differ from that of other organizations and, accordingly may not be comparable with measures of other organizations.

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## **Strategy**

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Deepwell is committed to building value for its unitholders through disciplined management and the implementation of its long-term strategy. The core principles of Deepwell's strategy are summarized below.

- **Focus on oilfield waste management:** Deepwell currently operates exclusively in the oilfield waste management business, and intends to continue that focus. The oilfield waste management business in Alberta has significant barriers to entry, which support the long-term cash flow of current and future facilities.
- **Growth:** Deepwell is primarily focused on organic growth through adding new facilities and increasing capacity and services provided at existing facilities.
- **Operational efficiency:** A key objective is to attain and maintain efficient operations and a high standard of customer service within a safe working environment.

**Environmental stewardship:** Deepwell intends to meet or exceed regulatory requirements and industry standards. Deepwell's facilities are audited annually by regulatory bodies, and Deepwell has developed innovations to enhance environmental stewardship at new and existing facilities.

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## **Selected financial information**

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The following table below provides selected financial information that has been derived from, and should be read in conjunction with, the interim consolidated financial statements of the Trust.

	Three months ended June 30, 2008	Three months ended June 30, 2007	Six months ended June 30, 2008	Six months ended June 30, 2007
Revenue	\$4,738,690	\$2,532,151	\$9,866,380	\$6,959,661
Operating expenses	2,852,928	1,190,739	5,580,583	3,109,961
<b>Gross Margin</b>	1,885,762	1,341,412	4,285,797	3,849,700
General and administrative expenses	688,254	558,849	1,165,968	1,155,393
<b>EBITDA</b>	1,197,508	782,563	3,119,829	2,694,307
Depreciation, accretion and amortization	1,194,711	864,413	2,202,520	1,763,154
Financing fees	19,093	33,452	22,910	57,380
Unit-based compensation	121,509	359,600	241,939	534,737
Interest	133,536	229,450	239,634	435,011
Loss on sale or disposal of property and equipment	42	(17,500)	11,458	(10,239)
Loss on write-off of property and equipment	-	-	-	367,702
Fire-related expenses	-	-	-	162,119
Future income tax recovery	-	(62,651)	-	(87,201)
<b>Net income (loss)</b>	(271,383)	(624,201)	401,368	(528,356)
Non-cash items:				
Depreciation, amortization and accretion	1,194,711	864,413	2,202,520	1,763,154
Financing fees		33,452	-	57,380
Unit-based compensation	121,509	359,600	241,939	534,737
Loss on sale or disposal of property and equipment	42	(17,500)	11,458	(10,239)
Loss on write-off of property and equipment	-	-	-	746,332
Future income tax recovery	-	(62,651)	-	(87,201)
<b>Funds from operations</b>	\$1,044,879	\$553,113	\$2,857,285	\$2,475,807
Changes in non-cash working capital	351,968	1,404,547	(762,028)	(76,367)
<b>Cash flow from operating activities</b>	\$1,396,847	\$1,957,660	\$2,095,257	\$2,399,440
<b>Net income</b>	(\$271,383)	(\$624,201)	\$401,368	(\$528,356)
Per unit, basic and diluted	(0.04)	(0.14)	0.06	(0.12)
<b>EBITDA</b>	\$1,197,508	\$782,563	\$3,119,829	\$2,694,307
Per unit, basic and diluted	0.17	0.18	0.43	0.62
<b>Funds from operations</b>	\$1,044,879	\$553,113	\$2,857,285	\$2,475,807
Per unit, basic and diluted	0.15	0.13	0.40	0.57
<b>Distributions to Unitholders</b>	\$1,292,051	\$753,183	\$2,582,855	\$1,849,153
Per unit, basic and diluted	0.18	0.17	0.36	0.42
Gross margin as a percentage of revenue	40%	53%	43%	55%
General and administrative expenses as a percentage of revenue	15%	22%	12%	17%
Capital expenditures	\$858,390	\$1,613,245	\$3,770,183	\$2,451,930
Total assets, end of period	\$62,825,170	\$53,839,846	\$62,825,170	\$53,839,846
Long-term debt, end of period	\$10,000,000	\$13,500,000	\$10,000,000	\$13,500,000
Total long-term liabilities, end of period	\$10,776,341	\$13,869,652	\$10,776,341	\$13,869,652
Trust unit equity, end of period	\$56,314,060	\$40,443,363	\$56,314,060	\$40,443,363
Weighted average Trust units, basic	7,180,086	4,357,724	7,180,086	4,356,867
Weighted average Trust units, diluted	7,184,666	4,357,744	7,184,021	4,356,867

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## **Second quarter 2008 overview**

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Deepwell achieved significantly improved year-over-year results in what is traditionally the weakest quarter of the year for the industry. Deepwell generated revenue of \$4,738,690 for the second quarter of 2008, an increase of 87 percent from the same period in 2007. Second quarter EBITDA was \$1,197,508, an increase of 53 percent from the same period in 2007 and funds from operations for the quarter were 89 percent higher than Q2-07. Capacity growth, service additions and stronger commodity prices led to the improved results.

The net loss for the quarter was \$0.04 per unit basic and diluted (Q2-07 – net loss of \$0.14 per unit basic and diluted) and funds from operations for the quarter were \$0.15 per unit basic and diluted (Q2-07 – \$0.13 basic per unit and diluted).

The Trust's balance sheet remains strong with long term debt of \$10,000,000 and a funded debt to twelve month EBITDA of 1.99:1. At June 30, 2008 the Trust's available capacity on its credit facilities was approximately \$4,100,000. Distributions were maintained at 6 cents per unit. Total distributions paid to unitholders for the quarter, including distributions to participants under the Trust's Distribution Reinvestment Plan (DRIP), were \$1,292,051 or \$0.18 per unit (Q2-07 – \$0.18 per unit).

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## **Results of operations**

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### ***Revenue***

Revenues for the quarter were \$4,738,690 (year-to-date – \$9,866,380; prior year – \$6,959,661) an increase of 87 percent from the second quarter of 2007. In the quarter 60 percent of revenues were from processing and disposal fees and 40 percent were from the sale of recovered oil, compared to 66 percent and 34 percent, respectively, for the same period in 2007. Processing revenues of \$2,853,063 increased significantly (71 percent) from 2007 processing revenues of \$1,672,814. The addition of the Claesholm facility in 2008 contributed to the increased revenues, although revenue growth at the facility has been hampered by the timing of its start-up near the beginning of spring break-up. While the second quarter of 2008 included a longer than normal break-up, it was a slight improvement over the conditions in the second quarter of 2007. In addition to the revenue impact of the Claesholm facility and the reduced severity of spring break-up, overall industry conditions were improved over the second quarter of 2007.

Increased oil volumes received in the quarter were a result of the higher activity levels and due to product received from well fracturing and production oil classified as waste, which did not meet pipeline specification (off-spec production fluids). The increase in oil revenues was partially offset by additional oil repayments reflected directly in operating costs.

### ***Expenses***

#### ***Operating expenses***

Operating expenses were \$2,852,928 for the quarter (Q2-07 – \$1,190,436), yielding a gross margin of 40 percent for the quarter (Q2-07 – 53 percent). The decrease in operating margin is largely due to the start-up of the Claesholm facility. The facility began the quarter slowly and produced losses in the first two months of the quarter. The three original facilities produced a combined gross margin of 52 percent for the quarter, one percent lower than in Q2-07. Operating expenses include \$525,722 in oil credits repaid to customers compared to \$27,168 in Q2-07. The increase in oil credits is due largely to increased activity, and secondarily to an increased proportion of revenues coming from waste versus produced water for the quarter as well as to credits paid on off-spec production fluids in Q2-08. The increase in direct operating expenses was predominantly due to the addition of the Claesholm facility as well as trucking and landfill costs, which increased along with the higher oil and solid waste volumes.

#### ***General and administrative***

General and administrative expenses, which represent costs associated with the Trust's head office, senior management and public entity costs, were \$688,254 or 15 percent of revenue for the quarter and \$1,165,968 or 12 percent of revenue year-to-date (Q2-07 – \$558,849 or 22 percent of revenue; prior year – \$1,155,393 or 17 percent of revenue).

### **Depreciation, amortization and accretion**

Depreciation, amortization and accretion expense was \$1,194,711 for the quarter (Q2-07 – \$897,865) and consisted of depreciation of fixed assets of \$1,088,713 (Q2-07 – \$766,726), accretion of \$19,869 (Q2-07 – \$15,453). Amortization of intangible assets totalled \$86,129 (Q2-07 – \$82,234), and consisted of the amortization of completions and contracts, customer relationships, and non-competition agreements. The increase in depreciation expense is a result of the completion of the Claresholm facility in the first quarter of 2008.

### **Interest**

Total cash interest expense for the quarter was \$133,536 (Q2-07 – \$229,450), comprised of interest on long-term debt of \$123,303 (Q2-07 – \$216,309) and interest on the Trust's operating loan of \$10,233 (Q2-07 – \$13,141). Interest expense decreased from the second quarter of 2007 due to lower debt levels. Interest rates are floating, with a range from 0.125 percent to 1.400 percent over the lender's prime rate, depending on the Trust's ratio of consolidated funded debt to earnings before interest, taxes, depreciation, amortization, accretion, and unit-based compensation. Actual interest rates during the quarter ranged from 0.125 percent to 1.4 percent over the lender's prime rate.

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### **Distributions to unitholders**

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Distributions declared to unitholders for the quarter, including distributions to participants under the DRIP, were \$1,292,051 (Q2-07 – \$784,544). Actual cash distributions paid were \$1,259,739 (Q2-07 – \$753,183) excluding non-cash distributions to participants in the DRIP. Distributions were higher period-over-period due to the larger number of units outstanding in the current period, which was a result of Deepwell raising equity in support of its growth initiatives. The distribution rate per unit remained unchanged at \$0.06 per month in the second quarter, reflecting Deepwell's ongoing ability to generate cash from operating activities.

	Three months ended		Six months ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Cash flows from operating activities	\$ 1,396,847	\$ 1,957,660	\$ 2,095,257	\$ 2,399,441
Net income (loss)	(271,383)	(624,201)	401,368	(528,356)
Actual cash distributions paid during the period	1,259,739	753,183	2,498,423	1,849,153
Excess (shortfall) of cash flows from operating activities over cash distributions paid	137,108	1,204,477	(403,166)	550,288
Shortfall of net income (loss) over cash distributions paid	\$ (1,531,122)	\$ (1,377,384)	\$ (2,097,055)	\$ (2,377,509)

While the cash distributions to unitholders exceeded net income in the first six months of 2008, Deepwell's distributions have generally not been based upon net income, as net income includes a number of non-cash items such as depreciation, amortization, accretion, and unit-based compensation that do not affect the Trust's ability to make distributions to unitholders. While the Trust believes that the current operating assets have the ability to support the current level of distributions, the actual amounts of distributions paid by the Trust to the unitholders will depend upon numerous factors, including profitability of operations, debt covenants and obligations, the availability and cost of acquisitions, fluctuations in working capital, the timing and amount of capital expenditures, applicable law and other factors beyond the control of Deepwell.

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### **Investing activities**

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Net cash used in investing activities during the quarter was \$1,528,871 (Q2-07 – \$1,277,961).

### **Capital expenditures**

The Trust's capital expenditures for purchase of property and equipment for the quarter were \$858,390 (Q2-07 – \$1,613,245). During the period Deepwell invested \$410,808 in completing construction of the Claresholm facility. The remaining investment in property and equipment included investment in tank and containment upgrades, safety equipment, future sites, computing equipment, and other oilfield service equipment.

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### **Unitholders' equity**

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#### **Trust unit option plan**

As at June 30, 2008, a total of 511,971 options were issued and outstanding pursuant to the Trust's incentive unit option plan. The options carry a five-year term and, except for 73,800 options issued to executives during 2007 in lieu of a cash bonus for 2006 (vesting immediately), vest equally over a period of three years from the date of grant. The exercise price of each option is based upon the weighted average trading price for a period prior to the date of grant. The exercise price is adjusted downwards by 100 percent of the amount of distributions paid on outstanding Trust units. During the quarter, 29,000 options were granted at an exercise price of \$4.58.

<b>Options outstanding as at June 30, 2008</b>				<b>Options exercisable as at June 30, 2008</b>	
<u>Exercise price</u>	<u>Number of options</u>	<u>Weighted average contractual life</u>	<u>Weighted average exercise price</u>	<u>Number of options</u>	<u>Weighted average exercise price</u>
\$4.46	29,000	4.77	\$4.46	-	n/a
5.76	188,971	4.13	5.76	73,800	5.76
5.96	2,000	3.85	5.96	668	5.96
8.43	276,500	3.14	8.43	92,171	8.43
8.92	15,000	3.26	8.92	5,000	8.92
\$9.30	500	3.22	9.30	167	9.30
	511,971	3.61	\$7.22	171,806	\$7.29

The Trust recorded unit-based compensation expense and contributed surplus of \$121,509 during the period (Q2-07 – \$241,939).

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### **Liquidity**

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Net cash provided by financing activities for the quarter was \$440,261 (Q2-07 – \$590,739). The Trust paid distributions to unitholders of \$1,292,051 (Q2-07 – \$753,183) during the quarter, of which \$32,312 was realized in proceeds from its distribution reinvestment plan (Q2-07 – \$31,060).

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### **Credit facilities**

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The Trust renewed its existing credit facilities on June 30, 2008 with a Canadian chartered bank (the "credit facilities"), which consisted of the following:

#### **Demand loan**

Under the credit facilities, the Trust has a \$2,000,000 demand revolving operating loan. During the quarter interest ranged from the lender's prime rate plus 0.125 percent to 1.4 percent and this rate is dependent on the funded debt to EBITDA ratio. As at June 30, 2008 the borrowing base for the demand loan was \$1,300,000 and the amount drawn was \$700,000.

**Long-term debt**

Under the credit facilities, the Trust has a \$25,000,000, 364-day extendible revolving term loan committed to May 29, 2009. No set principal repayment has been established and the Trust has the ability to repay, borrow and repay again until the 364-day term expires. Interest ranges from the lender's prime rate plus 0.125 percent to 1.4 percent per annum. Interest is calculated monthly and paid in arrears. As at June 30, 2008 an aggregate of \$10,000,000 is outstanding of which \$277,778 is current. The revolving period extends to May 29, 2009, at which time the credit facility is eligible for renewal.

As security for the credit facilities, Deepwell LP granted lenders a security interest over all of its assets. In addition, the Trust and its subsidiaries guaranteed the indebtedness of Deepwell LP under the credit facilities with such guarantee being secured by all of the assets of each such guarantor. In respect of any proceeds resulting from the enforcement of the credit facilities or the aforementioned guarantees, the lenders, as creditors, will have a prior-ranking claim relative to the unitholders.

**Interest rate risk**

The operating loan and the extendible revolving term loan bear interest at a floating interest rate. Therefore, to the extent that the Trust borrows under these facilities the Trust is at risk to rising interest rates.

**Contractual obligations, commitments and contingencies**

The following table shows future contractual obligations by period:

Payments by period	Total	2008	2009-2010	2011-2012	Thereafter
Long-term debt	\$10,000,000	\$ -	\$ 6,666,667	\$ 3,333,333	\$ -
Commitments	477,387	82,697	163,024	139,962	91,704
<b>Total contractual obligations</b>	<b>\$10,477,387</b>	<b>\$ 82,697</b>	<b>\$ 6,829,691</b>	<b>\$ 3,473,296</b>	<b>\$ 91,704</b>

**Financial instruments**

All of the Trust's financial instruments as at June 30, 2008 relate to standard working capital and credit facility items. There are no significant differences between the carrying value of these financial instruments and their estimated fair values. There are no unusual off-balance sheet arrangements and the Trust does not use any financial instruments such as derivatives. Of the Trust's financial instruments, only accounts receivable represent credit risk, and management views the credit risk related to accounts receivable as minimal. The operating loan and the extendible revolving term loan bear interest at a floating interest rate. Therefore, to the extent that the Trust borrows under these facilities, the Trust is at risk to rising interest rates.

## Quarterly information

	Quarter Ended							
	June 2008	March 2008	December 2007	September 2007	June 2007	March 2007	December 2006	September 2006
Revenue	\$4,738,690	\$5,127,690	\$3,650,736	\$3,513,654	\$2,532,151	\$4,427,510	\$4,059,296	\$3,808,795
Operating expenses	2,852,928	2,727,653	1,941,216	1,584,126	1,190,437	1,919,222	1,605,492	2,040,285
<b>Gross Margin</b>	1,885,762	2,400,037	1,709,520	1,929,528	1,341,714	2,508,288	2,453,804	1,768,510
General and administrative	688,254	477,714	842,448	520,373	558,848	596,544	730,354	448,788
<b>EBITDA</b>	1,197,508	1,922,323	867,072	1,409,155	782,866	1,911,744	1,723,450	1,319,722
Depreciation, amortization and accretion	1,213,804	1,011,626	838,528	915,875	897,865	922,669	993,621	697,052
Financing fees	-	-	114,043	-	-	-	-	15,588
Unit-based compensation	121,509	120,430	138,706	141,372	359,902	175,137	197,812	53,620
Interest	133,536	106,098	44,639	110,841	229,450	205,561	149,325	102,469
Loss (gain) on sale of property and equipment	42	11,416	1,466	-	(17,500)	7,261	34,295	-
Loss on write-off of property and equipment	-	-	-	-	-	367,702	162,119	-
Fire-related expenses	-	-	-	-	-	162,119	-	-
Future income tax recovery	-	-	-	-	(62,651)	(24,550)	(47,799)	-
<b>Net income (loss)</b>	<b>\$ (271,383)</b>	<b>\$ 672,753</b>	<b>\$ (270,310)</b>	<b>\$ 241,067</b>	<b>\$ (624,200)</b>	<b>\$ 95,845</b>	<b>\$ 234,077</b>	<b>\$ 450,993</b>
<b>Net income (loss) per Trust unit:</b>								
Basic	(\$0.04)	\$0.09	\$(0.04)	\$0.04	\$(0.14)	\$0.02	\$0.05	\$0.10
Diluted	(\$0.04)	\$0.09	\$(0.04)	\$0.04	\$(0.14)	\$0.02	\$0.05	\$0.10
<b>Weighted average number of Trust units outstanding</b>								
Basic	7,180,086	7,173,770	7,154,344	6,324,139	4,357,724	4,356,000	4,356,000	4,356,000
Diluted	7,184,666	7,173,770	7,154,344	6,327,260	4,357,744	4,356,000	4,357,187	4,477,793

The Trust's business is seasonal with the first and fourth quarters traditionally being the two strongest quarters for the industry and the second quarter being the weakest. The underlying causes of the seasonality are variations in prevailing weather conditions, which in turn have effects on the ability to carry out field operations. While Deepwell's facilities remain open and accessible throughout the year, its customers are, at times, restricted from moving waste due to spring break-up or periods of rainfall. In the Grande Cache region restrictions also occur at certain times of the year in designated wildlife areas.

## Outlook

Deepwell anticipates that, based upon current industry activity levels, its quarterly performance during the remainder of 2008 will continue to surpass levels in comparable quarters of previous years. Stronger year-over-year industry activity, coupled with the addition of the Claresholm facility, should be the primary contributors to anticipated growth. Commodity prices remain at levels higher than in previous years, although they have softened recently. Expectations are that commodity prices will remain higher than 2007 levels, leading to year-over-year increases in industry activity and oil revenue.

The Petroleum Services Association of Canada recently reiterated an earlier forecast for drilling activity to be somewhat stronger than initially forecast for 2008, while the Canadian Association of Oilwell Drilling Contractors recently increased its drilling forecast for 2008. These forecast levels remain considerably lower than the record activity levels experienced in 2005 and 2006, but are stronger than initial forecasts of a

serious downturn for 2008. Activity levels at oilfield waste processing facilities are driven by a combination of new well tie-ins and existing production within their service areas. With the total number of producing wellbores in Alberta continuing to increase (even if at somewhat lower annual rates), demand for third-party waste management services is also expected to grow. The medium to longer-term effects on industry activity levels of Alberta's new royalty regime, with higher royalty rates commencing in January 2009, remain uncertain.

Deepwell continues to pursue opportunities for increasing services and capacity at existing facilities and anticipates the construction of a facility in a new market territory in 2009.

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### **Critical accounting estimates**

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Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods. The most significant estimates relate to depreciation, amortization, asset retirement obligations, accretion, income taxes, unit-based compensation and recoverability of goodwill and intangibles. Actual results could differ from those estimates. The consolidated financial statements have, in management's opinion, been properly prepared using careful judgment within reasonable limits of materiality and within the framework of the Trust's accounting policies as disclosed in the Trust's consolidated financial statements.

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### **Risks and uncertainties**

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#### ***Cyclicality of the oil and natural gas industry***

The demand for oilfield services is largely dependent on the activity levels of oil and natural gas exploration and development companies. Industry conditions are influenced by numerous factors over which the Trust has no control, including: the level of oil and natural gas prices and production; expectations about future oil and natural gas prices; the cost of exploring for, producing and delivering oil and natural gas; the expected rates of declining production from maturing basins; the discovery of new oil and natural gas reserves; available pipeline and other oil and natural gas transportation capacity; weather conditions; global political stability, military actions, regulatory and economic conditions; the ability of oil and natural gas companies to raise capital; fuel conservation measures, alternative fuel requirements, and increasing consumer demand for alternatives to oil and natural gas; and technological advances in fuel economy and energy generation devices.

#### ***Oil and natural gas prices***

The revenue, cash flow and earnings of the Trust are substantially dependent upon and affected by the level of activity associated with oil and natural gas exploration and production. Both short-term and long-term trends in oil and natural gas prices affect the level of such activity. Worldwide military, political and economic events, including initiatives by the Organization of Petroleum Exporting Countries, may affect both the demand for and the supply of oil and natural gas. Weather conditions, governmental regulation, levels of consumer demand, the availability of pipeline capacity and other factors beyond Deepwell's control may also affect the supply of and demand for oil and natural gas, leading to future price volatility.

#### ***Seasonal weather***

In Canada, the level of activity in the oil and natural gas industry is influenced by seasonal weather patterns. Spring break-up during the second quarter of each year leaves many secondary roads temporarily incapable of supporting the weight of heavy equipment, which results in severe restrictions on the provision of energy services. The timing and duration of spring break-up are dependent on weather patterns and the duration of this period will have an impact on the level of business of the Trust.

***Dependence on key personnel***

The success of the Trust will likely continue to be dependent on the skills and expertise of the officers of the Trust. Deepwell does not currently carry “key man” insurance that would compensate the Trust for the loss of any senior executives.

***Competition for human resources***

During periods of high activity related to oil and natural gas exploration and development, demand for experienced and skilled employees increases. The success of the Trust is dependent upon the ability to retain the services of experienced and skilled employees and the ability to recruit and retain other key employees.

***Reliance on major customers***

It is estimated that the top 10 customers of Deepwell accounted for approximately 50 percent of revenue for the six months ended June 30, 2008, the largest customer accounting for 22 percent. Deepwell does not generally enter into long-term contracts with its customers and there can be no assurance that the current customers will continue their relationships with Deepwell.

***Competition***

Deepwell faces competition from a variety of competitors. Many of these competitors have strong financial, marketing and other resources. There can be no assurance that such competitors will not substantially increase the resources devoted to the development and marketing of oilfield services that compete with those of Deepwell or that new competitors will not enter the various markets in which Deepwell is active.

***Operating risks and insurance***

The business of Deepwell will be subject to hazards inherent in the oil and natural gas industry, such as equipment defects, malfunction and failures; accidental release; natural disasters which result in fires; vehicle accidents and explosions that can cause personal injury; loss of life; suspension of operations; damage to formations; damage to facilities; business interruption; and damage to or destruction of property, equipment and the environment. These risks could expose Deepwell LP to substantial liability for personal injury, wrongful death, property damage, pollution, and other environmental damages. The frequency and severity of such incidents are likely to affect operating costs, insurability and relationships with customers, employees and regulators.

Management will monitor the activities of Deepwell LP for quality control and safety. However, there are no assurances that Deepwell LP’s safety procedures will always prevent such damages. Although Deepwell maintains insurance coverage that management believes to be adequate and customary in the industry, there can be no assurance that such insurance will be adequate to cover such liabilities.

***Environmental risks***

The Canadian oil and natural gas industry is regulated by a number of federal and provincial governmental bodies and agencies under a variety of complex federal and provincial legislation that sets forth numerous prohibitions and requirements with respect to planning and approval processes related to land use, sustainable resource management, waste management, responsibility for the release of presumed hazardous materials, protection of wildlife and the environment, and the health and safety of workers. Legislation provides for restrictions and prohibitions on the transport of dangerous goods and the release or emission of various substances, including substances used and produced in association with certain oil and natural gas industry operations. The legislation addresses various permits required for drilling, access road construction, camp construction, well completion, installation of surface equipment, air monitoring, surface and ground water monitoring in connection with these activities, waste management and access to remote or environmentally sensitive areas.

Deepwell is subject to a complex and increasingly stringent array of legal requirements and potential liabilities, including with respect to the ownership and management of property, the need to obtain and comply with permits and approvals, the health and safety of employees, and the handling, use, storage, disposal, intentional or accidental release, and transportation of certain substances, including hazardous materials and dangerous goods. Failure to comply with these requirements could expose Deepwell to substantial potential penalties. There can be no assurance that Deepwell will not be required, at some future date, to incur significant costs to comply with environmental laws, or that its operations, business, assets or

cash flow will not be materially adversely affected by existing conditions or by the requirements or potential liability under current or future environmental laws.

***Credit risk***

All of the accounts receivable of Deepwell is with customers involved in the oil and natural gas industry whose revenues may be impacted by fluctuations in commodity prices. Collection of these receivables could be negatively influenced by any prolonged substantial reduction in oil and/or natural gas prices, which could have a material adverse effect on the financial results and cash flows of Deepwell.

***Access to additional financing***

Deepwell may find it necessary in the future to obtain additional debt or equity financing to support ongoing operations of Deepwell, to undertake capital expenditures or to undertake acquisitions or other business combination transactions. There can be no assurance that additional financing will be available to Deepwell when needed or on terms acceptable to Deepwell. The inability to raise financing to support ongoing operations or to fund capital expenditures or acquisitions could limit Deepwell's growth and may have a material adverse effect on the financial results and cash flows of Deepwell.

***Capital expenditures***

The timing and amount of capital expenditures by Deepwell will directly affect the amount of cash generated from operating activities. The cost of labour and equipment has escalated over the past several years.

***Leverage and restrictive covenants***

Deepwell has credit facilities which contain a number of financial covenants that require Deepwell to meet certain financial ratios and financial condition tests. Failure to comply with the obligations in the credit facilities could result in a default which, if not cured or waived, could result in a termination of distributions by Deepwell and would permit acceleration of the relevant indebtedness. If the indebtedness under the credit facilities were to be accelerated, there can be no assurance that the assets of Deepwell would be able to repay in full that indebtedness, which could result in the lenders realizing on the assets of Deepwell. There is no assurance that Deepwell will be able to refinance any or all of the credit facilities at their maturity dates on acceptable terms, or on any basis.

***Uncertainty of cash distributions***

The actual amounts of distributions paid by the Trust to the unitholders will depend upon numerous factors, including profitability of operations, debt covenants and obligations, the availability and cost of acquisitions, fluctuations in working capital, the timing and amount of capital expenditures, applicable law and other factors beyond the control of Deepwell.

***Government regulations***

The Trust's operations are subject to a variety of Canadian federal, provincial and local laws, regulations and guidelines, including laws and regulations relating to health and safety, the protection of the environment, and taxation.

The planned changes in the structure of oil and natural gas royalties payable to the Province of Alberta, intended to commence in 2009, could impact the exploration and development activities of exploration and production companies and lower the demand for Deepwell's services.

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***Related-party transactions***

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There were no related-party transactions in the three months ended June 30, 2008.

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***Internal controls***

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During the quarter, no changes were made that materially affected, or are reasonably likely to materially affect, internal controls over financial reporting.