

**HSE Integrated Ltd.**  
**Management Discussion and Analysis (“MD&A”)**  
**For the Quarter and Year To Date Ended September 30, 2009 and 2008**

The following management discussion and analysis is dated November 10, 2009, and is a review of the financial results of HSE Integrated Ltd. (“HSE”, “We”, “Our”, or the “Company”) for the quarter and year to date ended September 30, 2009 and 2008. This MD&A should be read in conjunction with HSE’s other documents filed on SEDAR at www.sedar.com. Unless otherwise disclosed, the financial information presented in this discussion has been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”) and takes into consideration information available to management up to November 10, 2009. Unless otherwise stated, dollar figures 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. We refer you to the end of the MD&A for the disclaimer on forward looking statements.

**Selected Financial Information**

	<b>Three Months Ended September 30, 2009</b>	Three Months Ended September 30, 2008	Quarter Over Quarter % Change	<b>Nine Months Ended September 30, 2009</b>	Nine Months Ended September 30, 2008	Year Over Year % Change
Revenue	<b>\$ 20,544</b>	\$ 28,202	(27.2%)	<b>\$ 62,511</b>	\$ 83,857	(25.5%)
Operating and materials	<b>17,456</b>	22,408	(22.1%)	<b>56,011</b>	68,400	(18.1%)
Operating margin	<b>3,088</b>	5,794	(46.7%)	<b>6,500</b>	15,457	(57.9%)
Operating margin %	<b>15.0%</b>	20.5%		<b>10.4%</b>	18.4%	
Selling, general & administrative	<b>2,072</b>	2,936	(29.4%)	<b>6,151</b>	7,780	(20.9%)
Net earnings (loss)	<b>(722)</b>	396	(282.3%)	<b>(4,456)</b>	(183)	2335.0%
- per share basic & diluted	<b>(0.02)</b>	0.01	(300.0%)	<b>(0.12)</b>	(0.00)	2335.0%
EBITDA <sup>(1)</sup>	<b>1,016</b>	2,858	(64.5%)	<b>349</b>	7,677	(95.5%)
EBITDA %	<b>4.9%</b>	10.1%		<b>0.6%</b>	9.2%	
Total assets				<b>\$59,706</b>	\$71,544	
Total long-term liabilities				<b>5,380</b>	20,004	

See Non-GAAP Measures for <sup>(1)</sup>

**Financial Review**

**Overview**

HSE operates in a single industry segment, the provision of industrial health and safety services. The Company provides a package of integrated asset, worker and community safety protection services including: on-site 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; on-site medical services; worker safety training; industrial hygiene services; and safety management and consulting services.

Total revenue for the quarter decreased 27.2% from \$28,202 in 2008 to \$20,544 in 2009. Operating margin of \$3,088 was 15.0% of revenues, down from \$5,794 or 20.5% of revenues in 2008. Selling, general and administrative expense (“SG&A”) decreased to \$2,072 from \$2,936 in the prior year. As a percentage of revenue SG&A decreased from 10.4% of revenue in fiscal 2008 to 10.1% in 2009. HSE reported a loss of \$722 or (\$0.02) per share compared to earnings of \$396 or \$0.01 per share in the prior year. EBITDA was \$1,016 or 4.9% of revenue in 2009, down 64.5% from \$2,858 or 10.1% of revenue in 2008.

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Total revenue for the nine month period declined 25.5% from \$83,857 in 2008 to \$62,511 in 2009. Operating margin of \$6,500 was 10.4% of revenue compared to \$15,457 or 18.4% of revenue in the prior year. SG&A was \$6,151 for the period, a 20.9% decline from \$7,780 in the prior year. However, as a percentage of revenue SG&A increased from 9.3% of revenue to 9.8%. The company reported a loss of \$4,456 or (\$0.12) per share compared to a loss of \$183 or (\$0.00) per share for the first nine months of the 2008 fiscal year. EBITDA for the period was \$349 (0.6% of revenue) compared to \$7,677 (9.2% of revenue) a year ago.

**Revenue**

The Company currently provides services to customers in two main business areas: Oilfield health and safety ("Oilfield") and Industrial health and safety ("Industrial"). Oilfield services are provided to customers who operate within the conventional upstream, or "wellhead", sector of the oil and gas industry. This includes oil and gas well exploration, drilling, completion and workover operations. Industrial services are provided to customers operating in a wide variety of other industries, including: non-conventional upstream oil development and production (including oilsands extraction); oil and gas processing and refining; petrochemicals; pulp and paper; utilities; power generation; and diverse manufacturing industries. It also includes worker safety training and safety management and consulting services. The Company tracks billings to customers by defined revenue groupings, but uses a common pool of equipment and manpower resources to provide these services. Management and administration services are provided from a common personnel pool.

The revenue for these business areas is shown below:

	Quarter ended September 30, 2009	Quarter ended September 30, 2008	Quarter over quarter % change	Quarter ended September 30, 2007	Quarter over quarter % change
Oilfield	\$ 6,169	\$ 12,039	(48.8%)	\$ 11,722	2.7%
Industrial	14,375	16,163	(11.1%)	11,856	36.3%
Total Revenue	\$20,544	\$28,202	(27.2%)	\$23,578	19.6%

As a % of Revenue:

Oilfield	30.0%	42.7%		49.7%	
Industrial	70.0%	57.3%		50.3%	
Total Revenue	100.0%	100.0%		100.0%	

	Nine months ended September 30, 2009	Nine months ended September 30, 2008	Year over year % change	Nine months ended September 30, 2007	Year over year % change
Oilfield	\$20,746	\$36,666	(43.4)%	\$38,007	(3.5)%
Industrial	41,765	47,191	(11.5)%	32,871	43.6%
Total Revenue	\$62,511	\$83,857	(25.5)%	\$70,878	18.3%

As a % of Revenue:

Oilfield	33.2%	43.7%		53.6%	
Industrial	66.8%	56.3%		46.4%	
Total Revenue	100.0%	100.0%		100.0%	

### Oilfield

Oilfield revenues in the third quarter decreased by 48.8% in 2009 compared to 2008 from \$12,039 to \$6,169. For the first nine months of the current fiscal year, Oilfield health and safety services revenue was \$20,746, 43.4% lower than the \$36,666 generated in the same period in the 2008 fiscal year. Services delivered to this group of clients comprised only 33.2% of revenue compared to 43.7% in the prior year. This significant year-over-year decline is due to lower overall activity levels in Western Canada in the conventional upstream, or “wellhead”, sector of the oil and gas industry: oil and natural gas well drilling, completion and workover (repair and maintenance) operations in the Western Canadian Sedimentary Basin. Compared to the same period in the prior year, this significant revenue decrease was caused by several negative external events including lower oil prices, lower natural gas prices, reduced access to debt and equity capital by Company clients, and the introduction of increased Crown royalties in Alberta, a major market for HSE.

Oilfield revenue tends to fluctuate between reporting periods in proportion to changes in conventional oilfield activity in the markets served including drilling, new well completions, and well workover activities. However, this change is not directly proportional, as not all conventional activity requires the use of our services. Services provided by HSE in the Oilfield sector are primarily oriented towards supporting the development of natural gas with a higher level of health and safety protection required for the development of sour gas – reserves of natural gas containing hydrogen sulphide – and crude oil containing sour gas. Some oil reservoirs tend to go “sour” over time due to the injection of water for secondary recovery, thus increasing the requirement for safety services.

The overall depressed economic environment for the conventional oil and gas industry has also put pressure on the prices HSE can charge its clients for services provided. To compensate for vastly reduced commodity prices, clients are seeking pricing relief for input services including health and safety. Therefore, in many cases HSE has been forced to adjust its pricing downward in order to maintain clients and market share. To compensate for lower prices, HSE has undertaken a series of internal cost reduction measures to maintain acceptable operating margins. These initiatives are discussed in detail under the discussion of Operating Materials Expense and Selling General and Administrative Expense below.

In the third quarter of 2009, the Company’s venture with Boots & Coots International Well Control, Inc. – Boots & Coots HSE Services LLC (“BCHSE”) – continued to generate modest revenues as BCHSE gained customer acceptance as a capable provider of worker and asset production services.

### Industrial

The Industrial health and safety services component of the Company’s total revenue also declined in the third quarter of 2009 due to the negative effects of the global recession which include reduced commodity prices, plant shutdowns, and project cancellations or delays. This general downward trend of industry spending on all goods and services took place to some degree in virtually every industry and geographical sector in which HSE operates.

Industrial revenue decreased \$1,788 (11.1%) to \$14,375 from \$16,163 in the same period in the prior year. Industrial health and safety services comprised 70.0% of total revenues, up from 57.3% in 2008. Without a significant recovery in Oilfield activity, Industrial revenues will continue to be significantly greater than Oilfield revenues for the foreseeable future.

The areas in which revenues were the strongest on a year-over-year basis were the oilsands region of northeast Alberta, as well as New Brunswick where HSE continues to work on major capital projects in the nuclear power and LNG sectors. Three new and significant clients were gained in the Fort McMurray area in the third quarter. The new location in Newfoundland-Labrador opened in the first quarter of 2009 continues to grow. Other industrial markets – particularly southern Ontario – continue to suffer from the general industry downturn in the mining, steel and automotive sectors. The non-oilsands industrial activity in western Canada is also depressed as clients work to conserve cash thus deferring some maintenance

and capital programs.

During the nine month period ended September 30, 2009, the Company had two customers representing more than 10% of revenue (2008 – none). The Company had sales of \$1.9 million to one customer during the quarter (\$6.6 million for the nine month period ended September 30, 2009). Sales to the second customer were \$2.6 million during the quarter (\$5.7 million for the nine-month period ended September 30, 2009). Sales to both customers relate to ongoing long-term industrial projects.

For the nine months ended September 30, 2009 HSE's Industrial revenue was \$41,765, a decline of 11.5% from the same period in fiscal 2008. Revenues from these clients accounted for 66.8% of total revenue compared to 56.3% a year ago. The growth in Industrial health and safety revenue in the period as a percentage of total revenue was caused by a greater decline in Oilfield health and safety revenue than Industrial.

### **Operating and Materials 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 and materials expense for the quarter ended September 30, 2009 totaled \$17,456 or 85.0% of revenue as compared to \$22,408 or 79.5% of revenue in 2008. Operating margin for the quarter declined from \$5,794 (20.5 % of revenue) in the third quarter of 2008 to \$3,088 (15.0 % of revenue) in 2009.

For the first nine months operating and materials totaled \$56,011 or 89.6% of revenue compared to \$68,400 or 81.6% of revenue for the period ended September 30, 2008. Operating margin for the first nine months declined from \$15,457 or 18.4% of revenue last year to \$6,500 or 10.4% of revenue in 2009.

The decrease in operating margins is due to several factors. First, the Company's fixed field service location operating costs were spread over a significantly lower revenue base. Second, the portion of revenue derived from equipment rentals as a percentage of total sales declined. This tends to reduce EBITDA margins, as a portion of the costs to be recovered does not affect EBITDA. Third, as discussed in more detail in the Outlook section, the Company experienced a certain amount of pricing pressure compared to 2008.

As discussed in the first and second quarter MD&A, the Company undertook a series of cost reductions including staff reductions, pay cuts and operating cost reductions. The Company incurred additional expenses totaling \$516 (\$282 in the first quarter and \$234 in the second quarter) to effect these cost reductions.

A new system of paying field service technicians came into effect June 1. Previously, most field service personnel in Western Canada were paid a base salary together with a job bonus. Effective June 1, this was changed to an hourly pay structure similar to the system already in place for the Company's Eastern operations. For Western operations, this change directly links field service personnel expense to revenue for the first time. Most of the reduction in operating expenses between the second quarter and the third quarter can be attributed to reductions in wage costs, as the third quarter was the first full quarter under which the Company's cost reductions were in place.

Management remains confident that, provided the Company's revenue mix follows historical patterns, it will be able to achieve break-even EBITDA (see "Non-GAAP measures") if monthly revenues average approximately \$6.0 to \$6.5 million per month.

Included in operating expenses is an addition to the provision for doubtful accounts of \$49 to reflect increased collection risks as a result of the deterioration in the general business environment. The

allowance for doubtful accounts receivable was \$1,256 (6.8% of trade accounts receivable) at the end of the quarter.

### **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 costs generally associated with the following: corporate head-office functions and services; administrative personnel; corporate sales and marketing costs; liability insurance; professional fees; and investor relations expenses.

SG&A for the quarter totaled \$2,072 (10.1% of revenue), down from \$2,936 (10.4% of revenue) in the prior year. Personnel costs declined as staff numbers declined year-over-year and the impact of salary reductions on March 1, 2009 came into effect. Travel and advertising costs declined as part of a company-wide initiative to reduce all costs in response to reduced operating levels.

In the quarter, the Company incurred expenses of approximately \$160 to defend against an unsolicited bid for the shares of HSE that commenced July 20. While the bid was ultimately subject to a cease-trade order by the Alberta Securities Commission and was therefore never legally constituted, the Company was nevertheless forced to spend significant funds on legal counsel, corporate secretarial services, transfer agents and teleconference services. The full costs of this event are included in the reported SG&A amounts to September 30, 2009.

For the first nine months SG&A declined to \$6,151 from \$7,780 in the prior year. However, as a percentage of revenue SG&A increased to 9.8% from 9.3% in 2008.

### **EBITDA and Net Loss**

EBITDA (see “Non-GAAP Measures”) in the quarter decreased from \$2,858 in the third quarter of 2008 to \$1,016 in the current quarter. The EBITDA decrease was primarily because of significant revenue declines on a year-over-year basis. For the first nine months EBITDA was \$349 compared to \$7,678 in the 2008 fiscal year.

EBITDA in the third quarter of 2009 was \$1,467 greater than the second quarter of the current fiscal year even though revenue only increased by \$978. This significant improvement in EBITDA reflects the full impact of the operating costs reductions described previously in this document which did not take full effect until June 1 of the current fiscal year.

Total amortization for the quarter was \$1,650, down from \$1,821 in 2008. Property and equipment amortization declined compared to the prior year at \$1,519 (down from \$1,647) as the Company controlled the pace of capital additions during 2008 and 2009. Intangible assets amortization declined to \$131 from \$174 in 2008 as certain amortization periods expired during 2008, particularly for non-competition agreements.

Stock-based compensation for the quarter was \$101 (2008 – \$23). The increase is primarily due to an increase in deferred share unit (“DSU”) expense. DSU expense for the quarter was \$64, primarily due to increases in the Company’s closing share price between June 30 and September 30. As well, more DSUs were granted during the quarter as the independent directors voted to take their fees in the form of DSUs rather than in cash.

Interest on long term debt and other interest and bank charges decreased from \$288 in 2008 to \$140 in 2009. Interest on the Company’s variable rate bank debt decreased as interest rates dropped. The Company’s average borrowing rate was approximately 3.0% lower in the third quarter of 2009 than in the equivalent quarter in 2008. This saved the company approximately \$80 in interest charges. As well, the Company had significantly lower levels of overall debt throughout the current quarter than it had in the third quarter of 2008.

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For the third quarter of 2009, the loss on disposal of property and equipment was \$35 with proceeds on sale of \$88. Partially offsetting the loss is the amortization of a deferred gain on sale / leaseback of assets as discussed in the 2008 annual MD&A. The remainder of asset divestitures consisted of retirement of vehicles replaced through the Company's fleet management program.

HSE had a \$185 income tax recovery for the quarter versus an income tax provision of \$197 for 2008. The change can be attributed primarily to a decrease in taxable income between quarters.

Net loss for the quarter was \$722 or \$(0.02) per share versus earnings of \$396 or \$0.01 per share in 2008. The year-over-year decline was primarily due to the decrease in EBITDA as described above.

**Current Quarter versus Q2 2009**

Revenue for the third quarter increased \$978 (5.0%) to \$20,544 from \$19,566 in the second quarter. Revenues from Oilfield health and safety services increased by \$1,852 as activity resumed after the removal of spring road bans which prohibit movement of heavy equipment during the spring thaw. Historically, oilfield activity is lowest in the second quarter. This was offset by a decrease in Industrial revenues of \$874 from \$15,249 in the second quarter to \$14,375 in the third quarter. The decline in Industrial revenue was caused because the second quarter is typically when most plant maintenance, repair and turnaround services are conducted. This activity historically declines in the summer months.

Operating expenses decreased by \$689 from \$18,145 million (92.7% of revenue) to \$17,456 million (85.0% of revenue). Operating cost decreases reflect the full impact of the field staff pay restructuring, total manpower reductions, and other cost containment activities.

SG&A increased from the first quarter by \$200. The primary cause was the cost incurred to defend the Company from an unsolicited takeover bid as described in greater detail earlier in this document.

**Liquidity and Capital Resources**

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

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

Years ended December 31,	2009	2010	2011	2012	2013	Total
Capital lease obligations	\$ 96	249	103	5	–	\$ 453
Vehicle operating leases	591	2,291	1,601	429	3	4,915
Property & other leases	704	2,559	1,797	1,163	844	7,067
Long-term debt	10	10,853	818	–	–	11,681
Total contractual obligations	\$1,401	15,952	4,319	1,597	847	\$24,116

**Liquidity**

On July 29, 2009, the Company amended its existing credit facilities with its current lender. The amended facility consists of a single \$15 million revolving operating facility. This facility, which matures July 27, 2010, is margined to property and equipment and accounts receivable. The facility bears interest at the bank's prime rate (or U.S. base rate) plus a fixed margin or at bankers' acceptance rates with a fixed stamping fee. An additional standby fee is also required on any unused portion of the credit facility. The facility is subject to certain covenants including a covenant with respect to the ratio of total liabilities to net worth (as defined in the agreement), a current ratio covenant, an interest coverage covenant and other positive and negative covenants. The credit facility is collateralized under a general security agreement. The Company complied with all covenants required under the credit facility.

At the end of the third quarter, the Company had \$15 million available under its revolving operating facility. Of this, \$10,829 has been drawn. On October 5, 2009, the Company paid down \$3,000 on the revolving operating facility, reducing the amount drawn to \$7,829.

At September 30 the Company had cash on hand of \$4,982.

### ***Cash Provided by (Used in) Operations***

Cash used in operations in the quarter was \$336 in 2009 compared to \$2,967 provided by operations for the equivalent quarter in 2008. Reduced revenue levels in the quarter resulted in lower operating cash flow excluding changes in working capital. Non-cash working capital decreased during the quarter primarily due to changes in receivables and prepaids. Prepaids changed as a result of the change in the renewal date of the Company's insurance policies. The increase in receivables during the quarter related to the billing of higher sales versus the second quarter. Days sales outstanding remained constant at 78 days during the third quarter of 2009. By comparison, days sales outstanding were 87 days for the comparable period in 2008. Operating cash flow in the third quarter of 2008 was improved by collections of accounts receivable as transition issues with the implementation of a new billing system effective January 1, 2008 were corrected.

### ***Cash Provided by (Used in) Financing and Investing***

During the quarter the Company made scheduled debt reductions of \$204 towards capital lease and other long term debt obligations. Subsequent to the end of the quarter, the Company paid \$3,000 on its \$10,829 revolving operating line leaving \$7,171 available to be drawn.

Purchases of property and equipment for the third quarter amounted to \$483, the majority of which was revenue generating health safety services rental equipment. Proceeds from disposal of property and equipment were \$88.

### **Working Capital**

At September 30, 2009, the Company had working capital (not including current portions of long-term amounts totalling \$11,222) of \$18,567. This compares to \$20,514 on December 31, 2008 and \$22,735 at September 30, 2008. The change from December 31, 2008 relates to changes in non-cash working capital as collections of receivables during the period were partially offset by reductions in payables and accruals. The change from the balance at the end of the third quarter of 2008 related to improved cash position offset by reductions in non-cash working capital, particularly accounts receivable. The Company's cash position improved from \$1,991 on September 30, 2008 to \$4,982 at September 30, 2009.

### **Outlook**

There was an improvement in the business climate in most markets in which HSE operates in the third quarter of 2009 fiscal year. The price of oil rebounded sharply in the second quarter from its lows in the first quarter and remained at higher levels through Q3. Although the price of oil during the third quarter was less than half of its peak price in the third quarter of 2008, in July, August and September crude was more than double 52 week lows. Natural gas prices, predicted to be very weak because of surplus production and full storage facilities, were soft compared to the prior year but never reached the extreme lows suggested by some forecasters. Credit and equity markets began to thaw with financings resuming in all sectors of the economy.

Some plants in the auto and steel sector that were shut down were reactivated. Major capital projects in oilsands were announced or resumed. Plant maintenance work that was postponed in the second quarter to conserve cash proceeded once the owners became confident that economic conditions were

improving. While the economy may not have grown significantly in the third quarter, it stopped shrinking as was the case in the first half of the year. This in itself was a marked improvement.

It is against this backdrop of a general improvement in many sectors of the economy that HSE discusses the outlook for its Oilfield and Industrial sectors.

### *Oilfield*

The Oilfield component of HSE's business is direct worker, asset and community protection services provided to conventional oil and gas exploration, drilling, completion and production operations. The bulk of the business is in the Western Canadian Sedimentary Basin, and a small amount of activity takes place in the Permian Basin of West Texas.

Because of the major decline in crude oil and natural gas prices in the past year, the outlook for significantly improved activity for this industry sector is not promising. At the time of writing, crude oil prices are around \$US 80 per barrel and AECO spot natural gas prices are at about \$CDN 4.50 per thousand cubic feet. On an historical basis, these prices would appear encouraging for conventional oil and gas field activity.

However, along with the run-up in commodity prices that took place from 2002 to 2008 came a commensurate increase in operating costs. The inflationary element of equipment and labor cost increases during this period, combined with Alberta's New Royalty Framework, have created a situation where oil and gas development is not as attractive as when commodity prices were at these levels in previous years.

In an attempt to make reserve replacement more profitable, customers have requested pricing relief from all their suppliers including HSE. E&P companies are revisiting pricing with all their vendors in an attempt to reduce drilling and service costs sufficiently to make more prospects economic for development. Fortunately, the major adjustment to field service labor costs undertaken in the second quarter will help HSE maintain at least some of its operating margin in the face of price reductions. It may be possible that reduced drilling and development costs will increase total revenues because clients will be able to drill more wells than they would otherwise. Regardless, our Company must continue to be extremely diligent on costs and efficiencies if it is to achieve acceptable profit margins in the future.

History has proven this industry to be highly cyclical. Because of its diversified client base and relatively strong financial position, HSE was able to reduce costs without seriously reducing future delivery capability in terms of capacity or quality. The result has been the positive development of increased market share gained by servicing major clients that HSE has not worked for in the past. This opportunity occurred because competitors that formerly serviced these clients had to make staff and operational cuts to survive that ultimately impaired service quality.

There are several developments that indicate that the worst is over for the Oilfield component of HSE. Besides the firming of commodity prices, the Alberta government in late Q3 extended its drilling incentive program to March 31, 2011. This has made an increasing number of prospects economic to develop at current commodity prices. The Alberta government is working on a competitiveness review with the intention of determining whether or not Alberta is competitive with other jurisdictions for continued hydrocarbon development. Depending on the outcome, this, combined with the drilling incentives, could have a material impact on development economics in 2010 and beyond.

Secondly, the overall cost of drilling a well has declined sharply due to lower drilling, service and steel prices. This will help stimulate overall activity, however the impact on profit margins will only be positive to those companies with highly efficient operations and cost control.

Thirdly, the price of natural gas is likely to continue to increase in 2010. High decline rates from existing production – particularly shale gas plays – combined with reduced drilling, will cause the supply demand curves to cross after an extended period of gas surpluses. Improved industrial activity will increase the

demand for natural gas, further assisting prices. While gas prices are unlikely to return to historical peaks, more analysts are predicting gas will sell in a higher range that will encourage more drilling activity. This will benefit HSE.

While drilling activity in the fourth quarter of 2009 and even 2010 is not likely to return to the high levels of 2008 and prior years, the Company is confident that Oilfield revenues will be greater next year than in 2009, although growth in activity in the first half of 2010 remains uncertain. In the fourth quarter, HSE will open a field service location in Fort Nelson, B.C., to participate in the active Horn River shale gas development scheduled for that area.

### *Industrial*

Industrial health and safety services remains a bright spot for the Company as we continue to demonstrate successful expansion by introducing new products, moving into new markets, and gaining clients that we have never worked for before.

Although for the first nine month of the current fiscal year to September 30 Industrial revenues are down 11.5% to \$41,765 from \$47,191 last year, they are still \$8,894 or 27.1% higher than the first nine months of the 2007 fiscal year. The contraction in total Industrial revenue in 2009 compared to 2008 has been discussed above. What is remarkable about this increasingly important element of HSE's go-forward growth strategy is the growth that continues despite the severity of the worst global recession in decades.

The oilsands region of northeast Alberta continues to show promise. HSE gained three significant new clients in this period. One is an existing bitumen producer, the second is a new oilsands construction project, and the third is an entirely new product for multiple clients that involves advanced worker wellness and health services in remote areas. This demonstrates that HSE's business model, reputation and delivery capabilities are valuable to our clients in all market conditions. Further, HSE continues to develop innovative solutions to the challenges facing industrial operators.

In the U.S., a major new contract for plant maintenance services signed in the second quarter with a global supplier of industrial gases began to make a meaningful contribution to revenues. The client wanted a single-source supplier for industrial safety services in order to ensure a uniform level of service and quality across its operations. In Q3, work was done in several new markets. Going forward, this contract will serve as a marketing building block and a model for similar relationships with other clients.

Atlantic Canada continues to be a growth area for HSE. In the third quarter the Company generated record revenues from operations in New Brunswick, Nova Scotia and Newfoundland-Labrador. While revenues from some capital projects will decline, growth in new clients, contracts and opportunities continues. The growth in providing offshore safety specialists for oil and gas and other operations adds a new dimension to HSE. Success on the east coast could lead to future opportunities on the west coast.

HSE believes that the contraction in total Industrial revenues that occurred in 2009 is a one-time event caused primarily by the severity and breadth of the recession. Looking forward, the Company sees a growing order book of plant turnarounds in all markets, resumption of capital projects in the oilsands by current HSE clients, the opportunity to expand the Company's new worker wellness product to other remote locations, and the ability to continue to move into new markets and establish profitable operations in a relatively short time with modest capital investment.

### **Cost Control and Short-Term Outlook**

Much of the focus of senior management in the first half of 2009 was on cost control. In the third quarter the Company was able to harvest some of its cost adjustments by developing an improved operating margin on significantly lower revenues than in the past. Based on the stabilization of business - albeit at reduced levels - HSE believes that the worst is over. While higher revenues will be required to reach historic levels of profitability, at current levels of business HSE can strengthen the balance sheet and undertake carefully selected growth opportunities.

The wild card in 2010 remains the highly cyclical Oilfield side of the company. Based on macro-economic cash flow models that incorporate commodity prices, capital costs and historic reinvestment ratios, analysts are predicting an increase in drilling activity in Canada next year. At the time of writing, however, this has not been verified by HSE's clients through the normal budget announcement and services procurement processes. Budgeting is currently underway. But with the high volatility in commodity prices, E&P company spending plans are often quite dynamic. If prices go down they will cut back spending. If they rise, spending will increase.

Based on futures prices for crude oil and natural gas, there exists more upside opportunity than downside risk. Producers can lock in their future production through hedging at higher prices than those that exist today. Based on historical cash flow and reinvestment models, there is reasonable likelihood that there will be an increase in drilling activity in Canada next year, although the improved levels will still be low by recent historical standards.

In this business there also exists the opportunity for sharply increased drilling in 2010 should natural gas prices rise higher than currently predicted. Although shale gas discoveries across North America have forever changed the continental gas market, these reservoirs are characterized by high rates of decline. Their long-term deliverability is as yet not fully understood.

HSE's strategy in 2009 has been to cut costs enough to establish a positive cash flow at sharply reduced levels of revenue without permanently impairing delivery capability, abandoning major markets, or shrinking the scope of products and services. Should we be rewarded with some pleasant surprises on natural gas prices after more than a year of bad news, the potential for the Company to do much better in 2010 than it appears today is quite real.

## Quarterly Results

	2009				2008			2007
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Revenue	\$ 20,544	\$ 19,566	\$ 22,401	\$ 29,905	\$ 28,202	\$ 28,087	\$ 27,569	\$ 26,464
Net earnings (loss)	(722)	(1,928)	(1,806)	431	396	(568)	(11)	(9,173)
EBITDA <sup>(1)</sup>	1,016	(451)	(216)	2,713	2,858	2,187	2,633	2,601
Income (loss) per share – basic and diluted	(0.02)	(0.05)	(0.05)	\$ 0.01	\$ 0.01	\$(0.02)	\$ 0.00	\$(0.25)

See Non-GAAP Measures for <sup>(1)</sup>

HSE's business has two offsetting seasonal components. Revenue for Oilfield health and safety services is historically highest in 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 "turnarounds" – scheduled major maintenance projects and repair activities on client facilities. These turnarounds 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.

Revenue by quarter for the last eight quarters is as follows

	2009				2008			2007
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Oilfield	\$ 6,169	\$ 4,317	\$ 10,260	\$ 14,597	\$ 12,039	\$ 8,667	\$ 15,961	\$ 15,879
Industrial	14,375	15,249	12,141	15,308	16,163	19,420	11,608	10,585
Total revenue	\$ 20,544	\$ 19,566	\$ 22,401	\$ 29,905	\$ 28,202	\$ 28,087	\$ 27,569	\$ 26,464

## **Related Party Transactions**

During the quarter, the Company had the following transactions with related parties all of which are measured at exchange amounts:

- During the third quarter of 2009, the Company paid rent for a regional office to a corporation related to a Director of the Company in the amount of \$57 (2008 – \$61). For the nine-month period ended September 30, the amount paid was \$218 (2008 – \$223).
- During the third quarter of 2009, the Company also paid rent of \$74 (2008 – \$79) for a regional office to a corporation controlled by a Senior Manager of the Company. For the nine-month period ended September 30, the amount paid was \$222 (2008 – \$231).

## **Critical Accounting Policies and Estimates**

HSE prepares its consolidated financial statements in accordance with Canadian generally accepted accounting principles. In doing so, management is required to make various estimates and judgments in determining the reported amounts of assets, liabilities, revenues and expenses, as well as the disclosure of commitments and contingencies. Management bases its estimates and judgments on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Estimates and assumptions are reviewed periodically, and actual results may differ from those estimates under different assumptions or conditions. Management must use its judgment related to uncertainties in order to make these estimates and assumptions.

The accounting policies and estimates believed to require the most difficult, subjective or complex judgments and which are material to the Company's financial reporting results include: allowance for doubtful accounts, impairment of long-lived assets, amortization of property and equipment, and future income tax liabilities. A full description of the methods for determining these accounting policies and estimates, as well as the risks related to the possible effects of changes in these policies and estimates, can be found in HSE's 2008 Annual Report.

## **Accounting Pronouncements**

Effective July 1, 2009 the Accounting Standards Board issued new guidance with respect to the assessment of embedded derivatives upon reclassification of a financial asset out of the "held-for-trading" category. This change had no effect on the Company.

Effective for annual financial statements related to years ending after September 30, 2009, the Accounting Standards Board adopted changes with respect to the disclosure of fair value measurements of financial instruments and with respect to the liquidity risk associated with financial instruments. These changes will be incorporated into the Company's year-end disclosures.

## **International Financial Reporting Standards**

On February 13, 2008, the Canadian Accounting Standards Board ("AcSB") confirmed the requirement for all publicly accountable enterprises to adopt International Financial Reporting Standards ("IFRS") for fiscal years beginning on or after January 1, 2011. Effective January 1, 2011 HSE will be required to report its interim and annual financial statements in accordance with IFRS including comparative information for the 2010 period.

HSE has developed a project plan that consists of three major phases: initial assessment, detailed assessment and design, and implementation.

We have completed the following related to the initial assessment:

- Developed a project plan including conversion timelines

**HSE Integrated Ltd.**

Management Discussion and Analysis

For the Quarter and Year to Date Ended September 30, 2009 and 2008

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- Assessed resources and training needs
- Identified at a high level differences between Canadian GAAP and IFRS that have the greatest potential impact to HSE. Areas identified to date, include property plant and equipment, lease accounting, impairment testing, and financial statement disclosures.
- Conducted a high level review of the first time adoption exemptions detailed in IFRS 1

During the balance of 2009, we expect to complete the detailed scoping of Canadian GAAP / IFRS differences and identify the impact to HSE's IT systems.

The detailed assessment and design phase will include a comprehensive analysis of the impact of the IFRS differences identified in the initial assessment phase.

During the implementation phase, we will execute the required changes to business processes, financial systems, accounting policies and controls over financial reporting. Implementation will include parallel runs.

At this time, the impact of the transition to IFRS on HSE's financial statements is not reasonably determinable.

**Financial and Other Instruments**

The Company's financial instruments include cash and cash equivalents, accounts receivable, bank indebtedness, accounts payable and accrued liabilities, income taxes payable, obligations under capital leases and long-term debt. 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 Company is exposed to the following risks as a result of its use of financial instruments:

- credit risk
- liquidity risk
- market risk

These risks, and the Company's method of mitigating the risks, are described in the Management Discussion and Analysis included in the Company's 2008 Annual Report.

**Business Risks**

The activities the Company 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 cyclicalities 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 that HSE deals with; availability of financing at competitive rates; changes in foreign exchange rates and interest rates and litigation and contingencies. Additional risks and uncertainties that the Company may be unaware of, or that were determined to be immaterial may also become important factors that affect the Company. A discussion of the business risks faced by the Company are included in the Management Discussion and Analysis included in the Company's 2008 Annual Report.

**Internal Control Over Financial Reporting**

There have been no changes in the Company's internal control over financial reporting during the quarter ended September 30, 2009 that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting.

## Common Shares Outstanding

At November 10, 2009 and December 31, 2008 there were 37,575,675 common shares of HSE outstanding. At September 30, 2009, the Company had options outstanding to issue 2,426,832 shares at a weighted average exercise price of \$1.55 per share. Of these options, 1,386,979 were exercisable. At November 10, 2009, the Company had options outstanding to issue 2,426,165 shares at a weighted average exercise price of \$1.55 per share. Of these options, 1,386,979 were exercisable.

## Non-GAAP Measures

This report makes reference to EBITDA, a measure that is not recognized under generally accepted accounting principles. 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 EBITDA should not be construed as an alternative to net earnings determined by GAAP as an indication of the Company's performance. HSE's method of calculating EBITDA may differ from that of other companies and, accordingly, may not be comparable to measures used by other companies.

## EBITDA Calculation

For the Nine Months Ended September 30	2009	2008
Net loss	<b>\$(4,456)</b>	\$ (183)
Add (deduct):		
Amortization	<b>5,081</b>	5,966
Stock-based compensation	<b>250</b>	313
Interest and bank charges	<b>409</b>	916
Foreign exchange loss	<b>8</b>	4
Loss on disposal of property and equipment	<b>254</b>	454
Income tax	<b>(1,197)</b>	207
<b>EBITDA</b>	<b>\$ 349</b>	\$7,677

## Quarterly EBITDA Calculation

	2009				2008			2007
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Net earnings (loss)	<b>\$(722)</b>	\$(1,928)	\$(1,806)	\$ 431	\$ 396	\$(568)	\$(11)	\$(9,173)
Add (deduct):								
Amortization	<b>\$1,650</b>	\$1,692	1,739	1,399	1,821	1,920	2,125	2,243
Impairment of goodwill and intangible assets	–	–	–	–	–	100	–	10,505
Stock-based compensation	<b>101</b>	99	50	95	23	155	135	255
Interest and bank charges	<b>140</b>	120	149	200	288	331	297	311
Foreign exchange loss (gain)	<b>(3)</b>	12	(1)	(35)	4	2	(2)	12
Loss on disposal of property and equipment	<b>35</b>	126	93	193	129	326	–	103
Income taxes	<b>(185)</b>	(572)	(440)	430	197	(79)	89	(1,655)
<b>EBITDA</b>	<b>\$ 1,016</b>	\$(451)	\$(216)	\$2,713	\$2,858	\$2,187	\$2,633	\$2,601

## **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 Company'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 which may cause actual results, performance or achievements of the Company 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. This forward-looking information reflects the Company's current expectations regarding future events and operating performance based on assumptions and analyses made by the Company based on its experience and an assessment of current conditions, known trends, expected future developments and other factors which management believe to be appropriate under the circumstances.

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 Company's services by customers in various industries and geographic locations; pricing levels for the Company's services; commodity prices; foreign currency exchange rates; interest rates; access to financing; the Company'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 Company'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 Company's profile at [www.sedar.com](http://www.sedar.com).

The Company 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 Company 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 our profile on the SEDAR website at [www.sedar.com](http://www.sedar.com) and at [www.hseintegrated.com](http://www.hseintegrated.com).