

CANADA

SUPERIOR COURT

PROVINCE OF QUEBEC
DISTRICT OF MONTRÉAL

Commercial
Sitting as a court designated pursuant to the
Companies' Creditors Arrangement Act,
Division
R.S.C., c. C-36, as amended

No.: 500-11-036133-094

**IN THE MATTER OF THE PLAN OF COMPROMISE OR
ARRANGEMENT OF:**

ABITIBIBOWATER INC., a legal person incorporated under the laws of the State of Delaware, having its principal executive offices at 1155 Metcalfe Street, in the City and District of Montréal, Province of Quebec, H3B 5H2;

And

ABITIBI-CONSOLIDATED INC., a legal person incorporated under the laws of Canada, having its principal executive offices at 1155 Metcalfe Street, in the City and District of Montréal, Province of Quebec, H3B 5H2;

And

BOWATER CANADIAN HOLDINGS INC., a legal person incorporated under the laws of the Province of Nova Scotia, having its principal executive offices at 1155 Metcalfe Street, in the City and District of Montréal, Province of Quebec, H3B 5H2;

And

the other Petitioners listed on Appendices "A", "B" and "C";

Petitioners

And

ERNST & YOUNG INC., a legal person under the laws of Canada, having a place of business at 800 René-Lévesque Blvd. West, Suite 1900, in the City and District of Montréal, Province of Quebec, H3B 1X9;

Monitor

**TWENTY-SECOND REPORT OF THE MONITOR
NOVEMBER 19, 2009**

INTRODUCTION

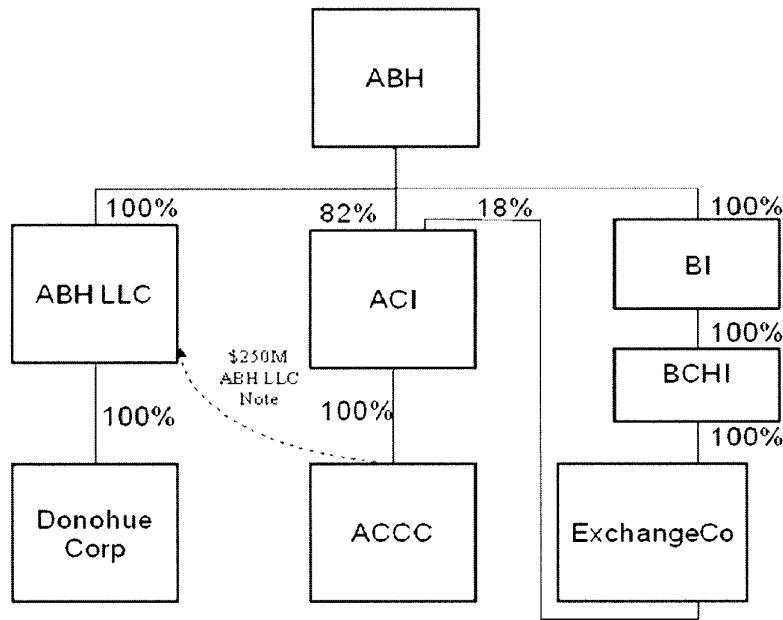
1. On April 17, 2009, Abitibi-Consolidated Inc. (“**ACI**”) and its subsidiaries listed in Appendix “**A**” hereto (collectively with ACI, the “**ACI Petitioners**”) and Bowater Canadian Holdings Incorporated (“**BCHI**”) and its subsidiaries listed in Appendix “**B**” hereto (collectively with BCHI, the “**Bowater Petitioners**”) (the ACI Petitioners and the Bowater Petitioners are collectively referred to herein as the “**Petitioners**”) filed for and obtained protection from their creditors under the *Companies’ Creditors Arrangement Act* (the “**CCAA**” and the “**CCAA Proceedings**”) pursuant to an Order of this Honourable Court, as amended on May 6, 2009 (the “**Initial Order**”). Pursuant to an Order of this Honourable Court dated November 10, 2009, Abitibi-Consolidated (U.K.) Inc., a subsidiary of ACI, was added to the list of ACI Petitioners.
2. Pursuant to the Initial Order, Ernst & Young Inc. (“**EYI**”) was appointed as monitor of the Petitioners (the “**Monitor**”) under the CCAA and a stay of proceedings in favour of the Petitioners was granted until May 14, 2009 (the “**Stay Period**”). The Stay Period has been extended until December 15, 2009 pursuant to further Orders of this Honourable Court.
3. On April 16, 2009, AbitibiBowater Inc. (“**ABH**”), Bowater Inc. (“**BI**”), and certain of their direct and indirect U.S. and Canadian subsidiaries, including BCHI and Bowater Canadian Forest Products Inc. (“**BCFPI**”) (collectively referred to herein as “**U.S. Debtors**”), filed voluntary petitions (collectively, the “**Chapter 11 Proceedings**”) for relief under Chapter 11 of the U.S. Bankruptcy Code, 11 U.S.C. §§ 101 et seq. (the “**U.S. Bankruptcy Code**”) in the United States Bankruptcy Court for the District of Delaware (the “**U.S. Bankruptcy Court**”).
4. The Petitioners are all subsidiaries of ABH (ABH, collectively with its subsidiaries, are referred to as the “**ABH Group**”).
5. On April 17, 2009, ABH and the petitioners listed on Appendix “**C**” hereto (collectively with ABH, the “**18.6 Petitioners**”) obtained Orders under Section 18.6 of the CCAA in

respect of voluntary proceedings initiated under Chapter 11 and EYI was appointed as the Information Officer in respect of the 18.6 Petitioners.

6. On April 16, 2009, ACI and ACCC filed petitions for recognition under Chapter 15 of the U.S. Bankruptcy Code. On April 21, 2009, the U.S. Bankruptcy Court granted the recognition orders under Chapter 15 of the U.S. Bankruptcy Code.
7. On April 22, 2009, the Court amended the Initial Order to extend the stay of proceedings to the partnerships listed in Appendix “D” hereto.

BACKGROUND

8. ABH is one of the world’s largest publicly traded pulp and paper manufacturers. It produces a wide range of newsprint and commercial printing papers, market pulp and wood products. The ABH Group owns interests in or operates pulp and paper facilities, wood products facilities and recycling facilities located in Canada, the United States, the United Kingdom and South Korea.
9. Incorporated in Delaware and headquartered in Montreal, Quebec, ABH functions as a holding company and its business is conducted principally through four direct subsidiaries: BI, Bowater Newsprint South LLC (“**Newsprint South**”) (BI, Newsprint South and their respective subsidiaries are collectively referred to as the “**BI Group**”), ACI (ACI and its subsidiaries are collectively referred to as the “**ACI Group**”) and AbitibiBowater US Holding LLC (“**ABH LLC**”) (ABH LLC and its respective subsidiaries are collectively referred to as the “**DCorp Group**”).
10. ACI is a direct and indirect wholly-owned subsidiary of ABH. ABH owns 82% of ACI and AbitibiBowater Canada Inc. (“**ExchangeCo**”) owns the remaining 18% of ACI. ABH wholly owns BI which, in turn, wholly owns BCHI which, in turn, owns ExchangeCo. BCHI also indirectly owns BCFPI which carries on the main Canadian operations of BI. In addition, ABH owns ABH LLC as noted in the chart below:



11. ACCC, a wholly-owned subsidiary of ACI, and BCFPI hold the majority of ABH's Canadian assets and operations.

PURPOSE

12. This is the twenty-second report of the Monitor (the “**Twenty-Second Report**”) in the CCAA Proceedings, the purpose of which is to report to this Honourable Court with respect to the Petitioners’ Motion seeking authorization or approval from this Honourable Court to:
 - (a) implement a series of intercompany transactions (the “**Repayment Steps**”) involving ACI, ACCC, ABH, ABH LLC, ExchangeCo and three limited liability companies (“**LLC Holdco**”, “**LLC 1**” and “**LLC 2**”, respectively, and collectively, the “**LLC Entities**”) to be created under the laws of Delaware, in order to settle, for tax purposes, the ABH LLC Note (as defined herein) and issue a new promissory note (the “**LLC 2 Note**”), the terms and conditions of which are to be substantially similar to that of the ABH LLC Note;
 - (b) execute a support agreement (the “**Support Agreement**”) among LLC Holdco, ABH LLC, LLC 1 and ACCC; and

- (c) to make certain proposed amendments to existing pre-filing financing arrangements in order to take into account the new guarantees and the new security to be issued under the Repayment Steps.
13. The implementation of the Repayment Steps, the execution of the Support Agreement and the proposed amendments to the pre-filing financing arrangements are collectively referred to herein as the “**Tax Restructuring Transaction**”.

TERMS OF REFERENCE

14. In preparing this Twenty-Second Report, the Monitor has been provided with and, in making comments herein, has relied upon unaudited financial information, the ABH Group’s books and records, financial information and projections prepared by the ABH Group and discussions with management of the ABH Group and its advisers (the “**Management**”). The Monitor has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of such information and, accordingly, the Monitor expresses no opinion or other form of assurance in respect of such information contained in this Twenty-Second Report. Some of the information referred to in this Twenty-Second Report consists of forecasts and projections. An examination or review of the financial forecast and projections, as outlined in the Canadian Institute of Chartered Accountants Handbook, has not been performed. Future-oriented financial information referred to in this Twenty-Second Report was prepared by the ABH Group based on Management’s estimates and assumptions. Readers are cautioned that, since these projections are based upon assumptions about future events and conditions, the actual results will vary from the projections, even if the assumptions materialize, and the variations could be significant.
15. Capitalized terms not defined in this Twenty-Second Report are as defined in the previous reports of the Monitor and the Initial Order. All references to dollars are in U.S. currency unless otherwise noted.
16. Copies of all of the Monitor’s Reports, in both English and French, including a copy of this Twenty-Second Report, and all motion records and Orders in the CCAA Proceedings

will be available on the Monitor's website at www.ey.com/ca/abitibowater. The Monitor has also established a bilingual toll-free telephone number that is referenced on the Monitor's website so that parties may contact the Monitor if they have questions with respect to the CCAA Proceedings.

17. Copies of all of the U.S. Bankruptcy Court's orders are posted on the website for Epiq Bankruptcy Solutions LCC ("**Epiq**") at <http://chapter11.epiqsystems.com/abitibowater>. The Monitor has included a link to Epiq's website from the Monitor's website.

THE TAX RESTRUCTURING TRANSACTION

The Background and Purpose of the Tax Restructuring Transaction

18. The Petitioners have advised the Monitor that:
 - (a) on April 1, 2008, ABH LLC issued a note (the "**ABH LLC Note**") whereby it promised to pay to ACCC the sum of \$201,614,222.50 with interest at a rate of 13.75% per annum;
 - (b) the ABH LLC Note was issued at the time of the merger of ACI and BI;
 - (c) as at the date of the Initial Order, approximately \$250 million was outstanding under the ABH LLC Note, including accrued interest;
 - (d) ABH LLC, a direct subsidiary of ABH, has no operations and has no known liabilities other than the ABH LLC Note and other intercompany payables; and
 - (e) ABH LLC has no assets other than its equity investment in the DCorp Group and receivables from other companies in the CCAA Proceedings and the Chapter 11 Proceedings.
19. The purpose of the Tax Restructuring Transaction is to repay the ABH LLC Note before year end in order to prevent a potential \$55.25 million Canadian withholding tax liability that would be payable by ACCC, which is explained in greater detail below.
20. As the Tax Restructuring Transaction requires the participation of a U.S. Debtor (namely ABH LLC) and putative U.S. Debtors to be created (namely LLC Holdco, LLC 1 and LLC 2), the Tax Restructuring Transaction will also require the approval of the U.S.

Bankruptcy Court. The Petitioners have advised the Monitor that the U.S. Debtors have filed a Motion for an Order authorizing the U.S. Debtors to implement the Tax Restructuring Transaction and such Motion is scheduled to be heard on November 24, 2009.

The Tax Issues

21. The Petitioners have advised, and the Monitor has confirmed with Ernst & Young LLP's tax group, that, under Canadian tax law, if cross-border intercompany indebtedness is incurred and not repaid by the end of the first taxation year of the lender (in this case, ACCC) following the taxation year in which the indebtedness arose (i.e. December 31, 2009), the intercompany indebtedness is recharacterized as a dividend as at the date it was incurred, which would result in a pre-filing Canadian withholding tax liability.
22. Accordingly, if the ABH LLC Note remains outstanding after December 31, 2009, ACCC may be liable for Canadian withholding tax on the deemed dividend in the amount of approximately \$55.25 million (the "**Withholding Tax**"), being 25% of the outstanding principal amount of the ABH LLC Note.
23. The Monitor has been advised by the Petitioners that the Withholding Tax would be payable by January 15, 2010. While the Withholding Tax would be pre-filing liability as it relates to the 2008 taxation year, the Monitor has been advised by the Petitioners that Canada Revenue Agency ("**CRA**") may try to collect the Withholding Tax by setting-off this amount against amounts owing to ACCC on account of post-filing GST refunds which are approximately \$3.5 million to \$7.0 million per month.
24. The Petitioners have advised the Monitor that ABH LLC does not have sufficient funds to repay ACCC the amounts outstanding under the ABH LLC Note prior to December 31, 2009.
25. In addition, the Petitioners have advised the Monitor that the failure to repay the ABH LLC Note before January 1, 2010 may also result in tax consequences in the U.S. for the U.S. Debtors as the ABH LLC Note could be deemed to be a taxable distribution under U.S. tax rules.

26. In order to avoid the potential consequences associated with the failure to repay the ABH LLC Note, the Petitioners propose to implement the Repayment Steps which would ultimately resolve the tax issues with respect to the ABH LLC Note while replacing ACCC's economic interests under and pursuant to the ABH LLC Note with an interest of equivalent value.

The Repayment Steps

27. The Repayment Steps are outlined in detail in the Petitioners' Motion and are summarized below:
- (a) ABH shall create LLC Holdco and LLC 1. ACCC shall create LLC 2. A limited liability company (an "LLC") is similar to a corporation in that it offers limited liability to its members. However, taxation for an LLC is passed to the individual owners of the LLC and corporate income tax is not paid. The LLC Entities will each have common units and preferred units, but not shares as they are not incorporated.
 - (b) The LLC Entities, which will each file petitions for relief under Chapter 11 of the U.S. Bankruptcy Code, will be created for the sole purpose of implementing the Repayment Steps and holding the ABH LLC Note, the LLC 1 Units (as defined herein), the LLC 2 Note and the LLC 2 Preferred Units (as defined herein).
 - (c) LLC 2 will acquire \$1,000 worth of units of a publicly listed Canadian partnership to ensure that LLC 2 will be a taxpayer under Canadian tax rules.
 - (d) ACCC will transfer the ABH LLC Note to LLC 2 in exchange for preferred units of LLC 2 ("**LLC 2 Preferred Units**"). The LLC 2 Preferred Units will be convertible into a \$250 million debt with terms and conditions similar to the ABH LLC Note. LLC 2 will be deemed under the Canadian tax rules to have acquired the ABH LLC Note at its principal amount.
 - (e) ACCC will reduce the stated capital maintained in respect of its class D preferred shares by \$250 million and distribute, subject to the security interest of the lenders

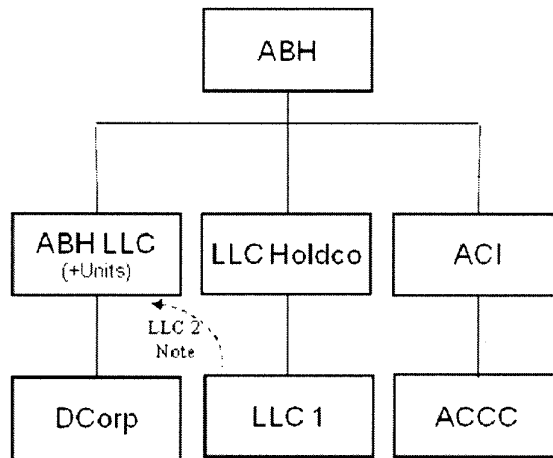
under the ACCC Term Loan (the “**ACCC Term Lenders**”), to ACI the LLC 2 Preferred Units and the common units of LLC 2. This distribution will not give rise to any tax consequences.

- (f) ACI will reduce the stated capital maintained in respect of its common shares by \$305 million and distribute, subject to the security interest of the ACCC Term Lenders, to ABH the LLC 2 Preferred Units and the common units of LLC 2. Concurrently, ExchangeCo will renounce its share of the distribution (being \$55 million or 18% of \$305 million) such that all of the LLC 2 Preferred Units and the common units of LLC 2 will be transferred to ABH. This reduction of ACI’s stated capital will allow ACI to distribute the LLC 2 Preferred Units and the common units of ABH LLC to ABH without giving rise to any withholding taxes.
- (g) ABH will transfer, subject to the security interest of the ACCC Term Lenders, the LLC 2 Preferred Units to LLC 1 in exchange for common units of LLC 1 (the “**LLC 1 Units**”). However, ABH will retain the common units of LLC 2. This step and the following step are designed to put in place the structure required to obtain the desired result prior to the merger of LLC 2 and ABH LLC, as described below.
- (h) ABH will transfer the LLC 1 Units to LLC Holdco in exchange for common units of LLC Holdco.
- (i) The LLC 2 Preferred Units will be converted into the LLC 2 Note (with substantially similar terms, conditions and pledges as those of the ABH LLC Note).
- (j) LLC 1 will grant a first priority security interest in all of its assets, including the LLC 2 Note, in favour of the ACCC Term Lenders.
- (k) LLC Holdco will grant a first priority security interest in the LLC 1 Units in favour of the ACCC Term Lenders.

- (l) LLC 2 and ABH LLC will merge, with ABH LLC being the resulting entity and therefore liable to LLC 1 under the LLC 2 Note. The ABH LLC Note will be extinguished on the merger.
 - (m) LLC Holdco, ABH LLC, LLC 1 and ACCC will enter into the Support Agreement under which LLC Holdco and LLC 1 will be required, unless otherwise provided in the CCAA and Chapter 11 plans, to transfer to ACCC, either the LLC 2 Note, the LLC 1 Units or other assets of equivalent value, in the event of certain triggering events. The Petitioners have advised the Monitor that they believe this will result in the creditors of ACCC being placed in the same economic condition as prior to the Tax Restructuring Transaction.
 - (n) If approved by the U.S. Bankruptcy Court, such Court will grant a security interest in the LLC 2 Note and the LLC 1 Units in favour of ACCC to secure the performance of the obligations under the Support Agreement, subject only to the first priority security interest in favour of the ACCC Term Lenders.
 - (o) LLC 1 will become a guarantor under the ACCC Term Loan, the 13.75% Senior Secured Notes due April 1, 2011 (the “**Senior Secured Notes**”) and the 15.5% senior unsecured notes issued by ACCC (the “**15.5% Senior Unsecured Notes**”).
 - (p) The LLC 2 Note will be pledged by LLC 1 in favour of the ACCC Term Lenders.
28. The Petitioners have advised the Monitor, and the Monitor has confirmed with the Ernst & Young LLP tax group, that, as a result of the merger between LLC 2 and ABH LLC, the ABH LLC Note will be deemed, for the purposes of the *Income Tax Act* (Canada), to have been settled by a payment made by ABH LLC to LLC 2 equal to LLC 2’s cost amount of the ABH LLC Note, being equal to the principal amount outstanding under the ABH LLC Note.
29. The LLC 2 Note (which has terms substantially similar to the ABH LLC Note) will be a loan between ABH LLC and LLC 1, an indirect wholly-owned subsidiary of ABH, both of which are U.S. entities. In effect, the Tax Restructuring Transaction transfers the ABH LLC Note from ACCC to a U.S. entity and, in return, ACCC receives an interest in the

residual value of the LLC 2 Note through the Support Agreement and related security. The Tax Restructuring Transaction results in the resolution of the Withholding Tax issue and eliminates the potential U.S. and Canadian tax consequences.

30. The Tax Restructuring Transaction will result in the following final structure:



The Support Agreement

31. The Support Agreement provides that, unless otherwise provided in the CCAA plan or the Chapter 11 plan, LLC Holdco and LLC 1 are required to transfer to ACCC, the LLC 2 Note, the LLC 1 Units or other assets of equivalent value in the event of certain triggering events. Such triggering events include (i) any liquidation event by any of ABH, ACI or the DCorp Group, (ii) the effective date of one or more plans of compromise or arrangement under the CCAA and of a plan of reorganization under the U.S. Bankruptcy Code, (iii) any event of default under the LLC 2 Note, (iv) in respect of ABH LLC or the DCorp Group, the dismissal or conversion of their respective Chapter 11 cases and, in respect of ACI, the lifting or expiry of the stay of proceedings, and (v) any default under the Support Agreement. In addition, ABH LLC and LLC 1 are prohibited from making any payment or otherwise reducing any amount owing under the LLC 2 Note without further order from this Honourable Court and the U.S. Bankruptcy Court.

32. As noted herein, ABH LLC's assets consist primarily of its equity interest in the DCorp Group, an insolvent entity, and receivables from related companies in the CCAA Proceedings and the Chapter 11 Proceedings. The Monitor has been advised by the Petitioners that the Support Agreement is intended to protect ACCC's interest in the residual value of the LLC 2 Note.

THE MONITOR'S COMMENTS ON THE TAX RESTRUCTURING TRANSACTION

33. Ernst & Young LLP's tax group has reviewed the Repayment Steps and is satisfied that they are reasonable and, once implemented, should have the tax consequences intended by the Petitioners.
34. The Monitor is of the view that a requirement to pay the Withholding Tax and the potential ability of CRA to effect collection by setting off post-filing GST refunds otherwise payable to ACCC, could adversely impact ACCC's liquidity and may negatively impact its creditors and other stakeholders.
35. The Monitor is of the view that the Repayment Steps and the Support Agreement permit the satisfaction, for tax purposes, of the ABH LLC Note in a manner that should prevent the payment of the Withholding Tax by ACCC, while replacing the Petitioners' interest in the ABH LLC Note with a residual interest in the LLC 2 Note through the Support Agreement. In the Monitor's view, the Support Agreement preserves the economic benefit currently attributable to the ABH LLC Note for the benefit of ACCC and its stakeholders. The Monitor is of the view that the Repayment Steps and the Support Agreement are reasonable in the circumstances.
36. The Monitor notes that the Repayment Steps contemplate that both ACCC and ACI will reduce their stated capital notwithstanding that both corporations are insolvent. ACI is incorporated under the *Canada Business Corporation Act* (the "CBCA") and ACCC is incorporated under the *Quebec Companies Act* (the "QCA").
37. The Petitioners have advised that the reduction of stated capital by ACI and ACCC will be pursuant to sections 191 of the CBCA and 123.62 of the QCA, respectively. The Petitioners have also advised that the necessity to implement the Repayment Steps

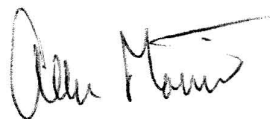
without delay justifies the Petitioners to reduce the stated capital of ACCC and ACI notwithstanding the provisions of section 123.63 of the QCA and section 38(3) of the CBCA.

38. As part of the Tax Restructuring Transaction, the Petitioners have advised the Monitor that they intend to make certain proposed amendments to existing pre-filing financing arrangements in order to take into account the new guarantees and the new security to be issued under the Repayment Steps.

All of which is respectfully submitted.

ERNST & YOUNG INC.
in its capacity as the Court Appointed Monitor
of the Petitioners

Per:



Alex Morrison, CA, CIRP
Senior Vice President

Ken Brooks
Senior Vice President

John Barrett, CA, CIRP
Vice President

APPENDIX "A"

ABITIBI PETITIONERS

1. Abitibi-Consolidated Company of Canada
2. Abitibi-Consolidated Inc.
3. 3224112 Nova Scotia Limited
4. Marketing Donohue Inc.
5. Abitibi-Consolidated Canadian Office Products Holding Inc.
6. 3834328 Canada Inc.
7. 6169678 Canada Inc.
8. 4042140 Canada Inc.
9. Donohue Recycling Inc.
10. 1508756 Ontario Inc.
11. 3217925 Nova Scotia Company
12. La Tuque Forest Products Inc.
13. Abitibi-Consolidated Nova Scotia Incorporated
14. Saguenay Forest Products Inc.
15. Terra Nova Explorations Ltd.
16. The Jonquière Pulp Company
17. The International Bridge and Terminal Company
18. Scramble Mining Ltd.
19. 9150-3383 Quebec Inc.
20. Abitibi-Consolidated (U.K.) Inc.

APPENDIX "B"

BOWATER PETITIONERS

1. Bowater Canada Finance Corporation
2. Bowater Canadian Limited
3. Bowater Canadian Holdings. Inc.
4. 3231378 Nova Scotia Company
5. AbitibiBowater Canada Inc.
6. Bowater Canada Treasury Corporation
7. Bowater Canadian Forest Products Inc.
8. Bowater Shelburne Corporation
9. Bowater LaHave Corporation
10. St-Maurice River Drive Company Limited
11. Bowater Treated Wood Inc.
12. Canoxel Hardboard Inc.
13. 9068-9050 Quebec Inc.
14. Alliance Forest Products Inc. (2001)
15. Bowater Belledune Sawmill Inc.
16. Bowater Maritimes Inc.
17. Bowater Mitis Inc.
18. Bowater Guérette Inc.
19. Bowater Couturier Inc.

APPENDIX "C"

18.6 PETITIONERS

1. AbitibiBowater US Holding 1 Corp.
2. AbitibiBowater Inc.
3. Bowater Ventures Inc.
4. Bowater Incorporated
5. Bowater Nuway Inc.
6. Bowater Nuway Mid-States Inc.
7. Catawba Property Holdings LLC
8. Bowater Finance Company Inc.
9. Bowater South American Holdings Incorporated
10. Bowater America Inc.
11. Lake Superior Forest Products Inc.
12. Bowater Newsprint South LLC
13. Bowater Newsprint South Operations LLC
14. Bowater Finance II, LLC
15. Bowater Alabama LLC
16. Coosa Pines Golf Club Holdings, LLC

APPENDIX "D"
PARTNERSHIPS

1. Bowater Canada Finance Limited Partnership
2. Bowater Pulp and Paper Canada Holdings Limited Partnership
3. Abitibi-Consolidated Finance LP