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C A N A D A
PROVINCE OF QUEBEC
DISTRICT OF QUEBEC
COURT No.: 500-11-057094-191
OFFICE No.: 0000438-2019-QC

S U P E R I O R C O U R T
Commercial Division

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

STORNOWAY DIAMOND CORPORATION

-&-

STORNOWAY DIAMONDS (CANADA) INC.

-&-

ASHTON MINING OF CANADA INC.

-&-

FCDC SALES AND MARKETING INC.

Petitioners

-&-

COMPUTERSHARE TRUST COMPANY OF CANADA

-&-

DIAQUEM INC.

-&-

INVESTISSEMENT QUÉBEC

-&-

FONDS DE SOLIDARITÉ DES TRAVAILLEURS DU QUÉBEC

-&-

FONDS RÉGIONAL DE SOLIDARITÉ F.T.Q. NORD-DU- QUÉBEC, SOCIÉTÉ EN COMMANDITE, acting through its general partner, **FONDS RÉGIONAUX DE SOLIDARITÉ FTQ**

-&-

CREE NATION OF MISTISSINI

-&-

GRAND COUNCIL OF THE CREE (EEYOU ISTCHEE)

-&-

CREE NATION GOVERNMENT

-&-

CATERPILLAR FINANCIAL SERVICES LIMITED

-&-

CHUBB LIFE INSURANCE COMPANY OF CANADA

-&-

THE BANK OF NOVA SCOTIA

-&-

XEROX CANADA LTD.

-&-

ATLAS COPCO CANADA INC.

-&-

CWB NATIONAL LEASING INC.

-&-

OSISKO GOLD ROYALTIES LTD.

-&-

CDPQ RESSOURCES INC.

-&-

TF R&S CANADA LTD.

-&-

ALBION EXPLORATION FUND LLC

-&-

WASHINGTON STATE INVESTMENT BOARD

-&-

TSX INC.

-&-

ATTORNEY GENERAL OF CANADA

-&-

QUEBEC REVENUE AGENCY

-&-

THE DIRECTOR APPOINTED PURSUANT TO THE CANADIAN BUSINESS CORPORATIONS ACT

-&-

THE REGISTRAR OF THE REGISTER OF PERSONAL AND MOVABLE REAL RIGHTS OF QUÉBEC, REPRESENTED BY THE QUEBEC MINISTRY OF JUSTICE

-&-

11641603 CANADA INC.

-&-

11641638 CANADA INC.

-&-

11641735 CANADA INC.

-&-

THE MINISTER OF ECONOMY, SCIENCE AND INNOVATION OF QUÉBEC

-&-

THE MINISTER OF FINANCE AND ECONOMY OF QUÉBEC

-&-

THE LAND REGISTRAR FOR THE REGISTRY OFFICE FOR THE REGISTRATION DIVISION OF SEPT-ILES

-&-

THE REGISTRAR OF PUBLIC REGISTER OF REAL AND IMMOVABLE MINING RIGHTS KEPT BY THE MINISTÈRE DE L'ÉNERGIE ET DES RESSOURCES NATUELLES (QUÉBEC)

Mises-en-cause

-&-

DELOITTE RESTRUCTURING INC.

Monitor

SECOND REPORT TO THE COURT
SUBMITTED BY DELOITTE RESTRUCTURING INC.
IN ITS CAPACITY AS MONITOR (THE "MONITOR")
(Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended)

CONTENTS

INTRODUCTION

1. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars. Capitalized terms not otherwise defined are as defined in the First Report, the *Motion Seeking (i) Extension of the Stay of Proceedings, (ii) Amendment and Restatement of the Initial Order; and (iii) Leave to Enter Into the Participating Streamers/Diaquem Transaction with Issuance of an Approval and Vesting Order and Ancillary Relief* (**"Motion"**) under the Companies' Creditors Arrangement Act (**"CCAA"**) and in the SPA.

2. On September 9, 2019, Stornoway Diamond Corporation (**"SWY"**), Stornoway Diamonds (Canada) Inc. (**"SDCI"**), Ashton Mining of Canada Inc. (**"Ashton"**) and FCDC Sales and Marketing Inc. (**"FCDC"**) (collectively the **"Petitioners"** or **"Stornoway"**) filed for and obtained protection from their creditors under Section 4, 5 and 11 of the CCAA pursuant to an Order rendered by this Honourable Court (the **"Initial Order"**). The Initial Order provides for, *inter alia*, (i) a stay of proceedings against the Petitioners until October 9, 2019 (the **"Stay Period"**) (ii) the appointment of Deloitte Restructuring Inc. as the monitor under the CCAA (**"Deloitte"** or the **"Monitor"**), (iii) the approval of the Interim Facility and the (iv) granting of an Interim Lenders' Charge, an Administration Charge, a D&O Charge and a SISP Managers Charge. The proceedings commenced under the CCAA by the Petitioners will be referred to herein as the **"CCAA Proceedings"**.

3. On September 8, 2019, the Monitor issued its First Report. The purpose of the First Report was to provide background information on Deloitte's qualification to act as Monitor, the business, affairs and financial results of the Petitioners, Stornoway's main creditors, the Petitioners' SISP process, on the contemplated transaction, the charges sought in the Initial Order and to cover specifically the Cash Flow Statement, in accordance with paragraph 23(1)(b) of the CCAA.

PURPOSE OF THE SECOND REPORT

4. The purpose of this second report of the Monitor (the **"Second Report"**) is to provide information to the Court with respect to:

    (i) the activities of the Petitioners since the commencement of the CCAA Proceedings;

    (ii) the activities of the Monitor since the commencement of the CCAA Proceedings;

    (iii) the Petitioners' request for an Approval and Vesting Order and an Amended and Restated Initial Order:

        a. approving the Pre-Closing Reorganization Transactions;

        b. approving the Participating Streamers/Diaquem Transaction;

        c. vesting the Purchased Shares free and clear from Encumbrances (other than any Permitted Encumbrances) in favour of AcquisitionCo;

        d. vesting the Excluded Assets exclusively in NewCo 2;

        e. vesting the Excluded Liabilities exclusively in NewCo 2 and NewCo 3;

        f. releasing the Released Parties from any Released Claims;

        g. effective as at the Closing Date, adding NewCo 2 and NewCo 3 as Petitioners in these CCAA Proceedings;

h. effective as at the Closing Date, granting the Monitor with the additional power to assign SWY, NewCo 2 and NewCo 3 into bankruptcy, as the case may be;

i. effective as at the Closing date, releasing and discharging SDCI, FCDC and Ashton (as well as AmalCo) as Petitioners in these CCAA Proceedings; and

j. requesting an extension of the Stay Period until November 30, 2019

(iv) the Petitioners' original cash flow statement and a comparison to actual receipts and disbursements for the four-week period ended October 4, 2019;

(v) the Petitioners' updated cash flow forecast for the period from September 29, 2019 to November 30, 2019; and

(vi) the Monitor's conclusions and recommendations.

TERMS OF REFERENCE

5. In preparing this Second Report and making the comments herein, the Monitor has been provided with, and has relied upon, unaudited financial information, the Petitioners' books and records and financial information prepared by the Petitioners and discussions with management ("**Management**") of the Petitioners (collectively, the "**Information**"). The Monitor makes the following observations in connection with the Information, some of which has been provided to the Monitor in draft form:

   (i) the Monitor has reviewed the Information for reasonableness, internal consistency and use in the context in which it was provided. However, the Monitor has not audited or otherwise attempted to verify the accuracy or completeness of such information in a manner that would wholly or partially comply with Generally Accepted Assurance Standards ("**GAAS**") pursuant to the *Chartered Professional Accountants Canada Handbook* and, accordingly, the Proposed Monitor expresses no opinion or other form of assurance contemplated under GAAS in respect of the Information; and

   (ii) some of the information referred to in this Second Report consists of forecasts and projections. An examination or review of the financial forecast and projections, as outlined in *Chartered Professional Accountants Canada Handbook*, has not been performed.

6. Future oriented financial information referred to in this Second Report was prepared based on Management's estimates and assumptions. Readers are cautioned that since projections are based upon assumptions about future events and conditions that are not ascertainable, the actual results will vary from the projections, even if the assumptions materialize, and the variations could be significant.

7. Unless otherwise indicated, the Monitor's understanding of factual matters expressed in this Second Report concerning the Petitioners and their business are based on the Information, and not independent factual determinations made by the Monitor.

8. A copy of this Second Report and further reports of the Monitor, if any, will be made available on the Monitor's website at https://www.insolvencies.deloitte.ca/Stornoway. The Monitor has also provided a dedicated email address and phone number that are referenced on the Monitor's website so that parties may contact the Monitor if they have questions with respect to the Companies' restructuring or the CCAA process.

EXECUTIVE SUMMARY

9. With respect to the Petitioners' request for the approval of the Participating Streamers/Diaquem Transaction and the granting of the orders in relation thereto, the Monitor is of the view that:

    (i) the process that resulted in the execution of the SPA was fair and reasonable in the circumstances;

    (ii) the Participating Streamers/Diaquem Transaction is the highest and best transaction resulting from the marketing process;

    (iii) the Release (as defined below) sought by the Petitioners is a condition for closing and necessary for the completion of the Participating Streamers/Diaquem Transaction, and is fair and reasonable in the circumstances; and

    (iv) the approval by the Court of the Participating Streamers/Diaquem Transaction on the basis set forth in the proposed Approval and Vesting Order, is in the best interests of the Petitioners' stakeholders generally.

10. Accordingly, the Monitor supports the approval of the Participating Streamers/Diaquem Transaction and the granting of the orders sought by the Petitioners in relation thereto.

11. With respect to the Petitioners' request for the extension of the Stay Period, the Monitor is of the view that:

    (i) the Petitioners have acted, and are acting, in good faith and with due diligence;

    (ii) an extension of the Stay Period is necessary and appropriate in order to implement the Transactions contemplated under the SPA; and

    (iii) creditors would not be materially prejudiced by an extension of the Stay Period to November 30, 2019.

12. Accordingly, the Monitor respectfully recommends that the Petitioners' request for an extension of the Stay Period to November 30, 2019 be granted.

STATUS OF THE CCAA PROCEEDINGS

13. Since the granting of the Initial Order:

    (i) the Petitioners continued to operate as a going concern and to pay their current employees and their suppliers in the normal course of business, for both their pre- and post-filing claims, as permitted by the Initial Order;

    (ii) the Monitor, with the Petitioners' assistance, has been responding to questions of various stakeholders as to the status of these CCAA Proceedings;

    (iii) the Monitor has analyzed the receipts and disbursements transacted through the SWY and SDCI bank accounts on a weekly basis with the full co-operation of Management and was presented with all requests to pay for services rendered to the Petitioners' since the granting of the Initial Order;

    (iv) the Petitioners negotiated the terms of the SPA and all related documents including the structure of the Participating Streamers/Diaquem Transaction; and

(v) the Monitor was kept informed on the progress of the negotiations of the Participating Streamers/Diaquem Transaction and provided with a copy of drafts of the transaction documents, including the SPA, and was given the opportunity to provide its comments thereon.

14. Pursuant to the Initial Order:

(i) on September 9, 2019, the Monitor posted a copy of the CCAA application materials, the First Report and the Initial Order on the Monitor's website;

(ii) on September 9, 2019, the Monitor filed the first form (Form 1) with respect to the granting of the Initial Order and certain other information as required by the Office of the Superintendent of Bankruptcy (the "**OSB**");

(iii) on September 10, 2019, the Monitor sent a notice, by prepaid ordinary mail, which included information about the CCAA Proceedings, the telephone number and the Monitor's website (the "**Notice to Creditors**") to all the 260 known creditors (excluding former and current employees of the Petitioners) based on the contact information of such known creditors provided by Management. A copy of the Notice to Creditors was also posted on the Monitor's website;

(iv) on September 13, 2019, the Monitor posted a French translation of the First Report on the Monitor's website;

(v) on September 13, 2019, and September 20, 2019, respectively, the Monitor published a notice with respect to the Initial Order in *La Presse* and The *Globe and Mail*; and

(vi) on September 27, 2019, the Monitor filed the second form (Form 2) with respect to the financial information and certain other information as required by the OSB.

CONTEMPLATED PARTICIPATING STREAMERS/DIAQUEM TRANSACTION

<u>The Process Leading up to the proposed Transaction</u>

15. As described in the First Report, following an extensive review of its business and affairs, and in consultation with its senior secured creditors, the Petitioners determined that a comprehensive restructuring of their debt and equity structure was required. Accordingly, in April 2019, the Petitioners initiated a limited solicitation process focused on targeted potential strategic parties. That process did not yield positive results.

16. In consultation with its senior secured lenders and on the advice of the SISP Managers, the Petitioners then developed the SISP, which was launched on June 10, 2019.

17. In its capacity as advisor of SWY at that time, the Monitor was kept fully informed in connection with the SISP, and was advised of the following by the SISP Managers and the Petitioners:

(i) a teaser letter was sent to 51 identified parties;

(ii) 46 of those parties declined the opportunity; and

(iii) Three of those parties entered into a confidentiality agreement and were provided access to the virtual data room to conduct their due diligence process.

18. On July 15, 2019, a non-binding indication of interest to acquire certain assets of the Petitioners was submitted by an interested party (the "**Interested Party Bid**").

19. The Monitor was advised that the parties were unable to reach a consensus which would allow the transaction contemplated by the Interested Party Bid to proceed.

20. The SISP provided that the Streamers and Diaquem were deemed to be qualified bidders even if they did not submit a non-binding indication of interest, but only to the extent of the amount of their respective secured claims.

21. Following the end of the discussions regarding the Interested Party Bid, the Participating Streamers and Diaquem submitted a non-binding letter of intent to the Petitioners, which lead to the negotiation of the SPA.

Monitor's Approval of the Sale Process

22. The Petitioners' assets were made available for sale in the SISP and through various sale efforts prior to the SISP. Details of those sale efforts have been provided to the Court in the First Report.

23. In the Monitor's view, in the circumstances of this case and given the status of efforts to sell the Petitioners' assets and the limited level of interest expressed therein, the SISP was reasonable and appropriate and provided all interested parties with an adequate opportunity to perform due diligence and to formulate and submit an offer.

24. As indicated above, the Monitor was kept informed on an on-going basis of the status of the negotiations and provided with drafts of the SPA and its schedules for review and comment.

25. The Monitor is of the view that the process that resulted in the SPA was fair and reasonable in the circumstances.

Transaction Structure

26. As more fully detailed in the Motion, the Participating Streamers/Diaquem Transaction contemplates the acquisition, by the Participating Streamers and Diaquem through AcquisitionCo, of 100% of the equity interest in AmalCo, which will take place following the implementation of the Pre-Closing Reorganization and in particular the amalgamation of SDCI, FCDC, NewCo 1 and Ashton as AmalCo.

27. The consideration payable under the Participating Streamers/Diaquem Transaction is the undertaking of AcquisitionCo to assume, *inter alia*, the following Vendor Assumed Liabilities (and SWY shall have been fully released therefrom (to the extent permitted by law)):

    (i) all guarantee obligations of SWY in favour of the Streamers under the Streaming Agreements and in favour of Diaquem under the Diaquem Senior Credit Agreement;

    (ii) all obligations of SWY as solidary co-borrower under the Bridge Financing Agreement; and

    (iii) all Employee Obligations relating to certain Employees of SWY, as at the Closing Date.

28. In addition, pursuant to the SPA, AcquisitionCo will cause AmalCo to continue payment of the Target Companies Assumed Liabilities, including all amounts owing in respect thereof, up to the Closing Time, namely:

    (i) all Employee Obligations of Ashton, FCDC and SDCI as at the Closing Date;

(ii) all Employee Obligations of certain Employees of SWY;

(iii) all trade obligations incurred by SDCI towards its suppliers that are essential to its business and ongoing operations both prior to and following the commencement date of the CCAA Proceedings;

(iv) all obligations of Ashton, FCDC and SDCI under the Assumed Contracts, including any liabilities arising prior to the commencement of the CCAA Proceedings;

(v) all obligations of SDCI under the reclamation bond number M216451 issued by Chubb Insurance Company of Canada in favour of the Quebec Ministry of Energy and Natural Resources;

(vi) all obligations of SDCI under the Authority to Hold Funds on Deposit from SDCI to The Bank of Nova Scotia;

(vii) all obligations of SWY under the IT Assigned Agreements;

(viii) all obligations of Ashton, FCDC and SDCI under the Assigned Agreements;

(ix) all obligations of SDCI under the IBA Agreement, the Caterpillar Lease, the Diaquem Royalty Agreement and the Diaquem Loan Agreement; and

(x) all obligations of Ashton, FCDC and SDCI under the A&R CTIA, the Working Capital Facility, the Stream Agreement and the Bridge Financing Agreement.

29. The Participating Streamers/Diaquem Transaction also provides for the Pre-Closing Reorganization, the purpose of which is to preserve the tax attributes of the existing corporate structure while simplifying the structure going forward. As detailed in the Motion, the Pre-Closing Reorganization includes, *inter alia*, the following steps:

(i) the vesting and assignment by SWY of all intercompany claims owing by Ashton, FCDC and SDCI's, totalling approximately $620 million to NewCo 1;

(ii) the vesting of Excluded Assets in NewCo 2, for no consideration;

(iii) the assignment and vesting of the Excluded Liabilities in NewCo 2 and NewCo 3; and

(iv) as referred to above, the amalgamation of NewCo 1, SDCI, Ashton and FCDC, resulting in AmalCo;

30. The obligation of the parties to complete the Participating Streamers/Diaquem Transaction is subject to a number of conditions being fulfilled or waived, including:

(i) the Participating Secured Creditors shall have entered into, as amongst themselves, such agreements as further detailed in the SPA;

(ii) the receipt by AcquisitionCo of all material consents, approvals, exemptions, authorizations and waivers deemed necessary to implement the Transactions, including from any governmental or other regulatory bodies, or any other third parties, on terms acceptable to AcquisitionCo;

(iii) the amendment of the Caterpillar Lease, on terms satisfactory to its parties;

(iv) the issuance by the Court of the Approval and Vesting Order, which order shall not have been vacated, set aside or stayed;

(v) the payment of all fees payable in favor of the Secured Creditors by SDCI no later than on Closing;

(vi) the retention of certain key executives by SDCI or AcquisitionCo, as applicable and as further detailed in the SPA; and

(vii) the release of SWY from its obligations in connection with the Stream Agreement and the Diaquem Loan Agreement.

31. The Participating Streamers/Diaquem Transaction is not conditional upon further financing or due diligence.

32. The SPA may be terminated on or before the Closing Date as set out in Section 8.1 of the SPA:

(i) by mutual agreement, with the consent of the Monitor or approval of the Court;

(ii) by written notice from AcquisitionCo, if any material portion of the Retained Assets is destroyed, damaged, appropriated or expropriated;

(iii) if the Approval and Vesting Order has not been obtained by November 16, 2019, or if the Court declines to grant it;

(iv) if there has been a material breach by SWY of any representation, warranty or covenant contained in the SPA which is not curable and has rendered the satisfaction of a closing condition to the benefit of AcquisitionCo impossible, or has not been cured within the applicable cure period;

(v) if there has been a material breach by AcquisitionCo of any representation, warranty or covenant contained in the SPA which is not curable and has rendered the satisfaction of a closing condition to the benefit of SWY impossible, or has not been cured within the applicable cure period;

(vi) by written notice from AcquisitionCo, if the closing has not occurred by November 16, 2019, unless due to AcquisitionCo's breach of the SPA; and

(vii) by written notice from SWY, if the closing has not occurred by November 16, 2019, unless due to SWY's breach of the SPA.

<u>The Effect of the Transaction on Creditors and Other Interested Parties</u>

33. As indicated in the First Report, the SISP resulted in only one non-binding indication of interest, the Interested Party Bid, for a proposed consideration which was significantly inferior to the face value of the aggregate secured obligations of the Petitioners to the Streamers and Diaquem and which provided for no consideration to unsecured creditors (other than in respect of any statutory obligations to any retained employees).

34. The Participating Streamers/Diaquem Transaction provides for the following:

(i) the uninterrupted operation of the Renard Mine and the continued employment of approximately 540 employees;

(ii) the continued undertaking to pay of all amounts owing in respect of Assumed Liabilities;

(iii) the continuation of existing agreements and related obligations required for the operation of the Renard Mine including the payment in full of all mine-level supplier claims (both pre-and post-filing) resulting in the uninterrupted supply of goods and services; and

(iv) the ongoing monitoring of the environmental impact of the Renard Mine.

35. The Participating Streamers/Diaquem Transaction also contemplates the vesting out, or transfer and assignment, of all Excluded Liabilities of SDCI, Ashton and FCDC, to NewCo 3. The Monitor understands that the most material known claims that are included in the Excluded Liabilities are the unsecured obligations of SDCI towards the Ministre des Finances et de l'Économie du Québec (the **"Ministre"**) under the Loan Agreement dated December 6, 2012 (referred to in previous materials provided to the Court as the "Road Loan") and the subordinated secured royalty obligations of SDCI towards Fonds de Solidarité des Travailleurs du Québec, Fonds Régional de Solidarité F.T.Q. Nord-du-Québec, S.E.C. and Diaquem Inc. under the Royalty Agreement dated May 3, 2012.

36. The Monitor has considered whether the impact of the Transactions on, or the treatment of, the creditors of the Target Companies (Ashton, FCDC and SDCI) would have been materially different if the structure of the transaction would have taken the form of an asset purchase (substantially all of which are located in SDCI and Ashton). In the Monitor's view, all Excluded Liabilities including both of the aforementioned claims would have been subordinated to the payment in full of the claims of the Streamers and Diaquem under their respective senior secured loan agreements. Given the outcome of the SISP and the consideration proposed in the Interested Party Bid, the Monitor believes that the proposed treatment of these claims would have been no different.

37. As far as the creditors of SWY are concerned, it is the Monitor's view that the consideration payable for the Purchased Shares is fair and reasonable given the circumstances. The only material assets owned by SWY consist of (i) the shares of the Target Companies (Ashton, FCDC and SDCI), which are pledged in favour of the Streamers and Diaquem to secure the payment in full of amounts owing to such creditors, and (ii) unsecured intercompany claims of approximately $620 million, which claims have also been pledged in favor of the Streamers and Diaquem to secure the payment in full of amounts owing to such creditors.

<u>Comparison with a Liquidation in Bankruptcy</u>

38. The Monitor has considered whether the Participating Streamers/Diaquem Transaction would be more beneficial to the Petitioners' stakeholders generally than a sale or disposition of assets under a bankruptcy.

39. Given the SISP and considering the value of the Petitioners' assets, the Monitor is of the view that the only other option, namely a sale in bankruptcy, is unlikely to result in a better outcome for the Petitioners' creditors. Notably, the Monitor is of the view that creditors who will suffer a shortfall following Participating Streamers/Diaquem Transaction would not obtain any greater recovery in a sale in bankruptcy.

40. Furthermore, bankruptcy proceedings would:

(i) Cause additional delays and uncertainty in the sale of the Petitioners' assets;

(ii) Jeopardize the going concern operations of the Renard Mine;

(iii) Potentially lead to unremedied environmental damage; and

(iv) Likely result in employees, trade creditors and suppliers to be unemployed and unpaid.

41. Accordingly, it is the Monitor's view that a sale or disposition of the Petitioners' assets in a bankruptcy would not be more beneficial than proceeding with the implementation and closing of the Participating Streamers/Diaquem Transaction.

<u>Consultation with creditors</u>

42. Considering the results of the SISP, the Petitioners consulted with their senior secured creditors namely, the Streamers and Diaquem as well as certain creditors who's obligations constitute Assumed Liabilities.

43. The Monitor also understands that the Petitioners have provided prior notice of the Motion and Participating Streamers/Diaquem Transaction to three creditors, namely the Ministre, PSP Investment and FTQ, and has had several exchanges with the latter two's representatives in connection therewith.

44. The Monitor is of the view that the degree of creditor consultation and notification was appropriate in the circumstances. The Monitor does not consider that any material change in the outcome of the SISP would have resulted from additional creditor consultation. In addition, the Monitor notes that the public disclosure requirements, incumbent on SWY as a reporting issuer, provided public notice of SWY's financial situation, the SISP and these CCAA Proceedings, including through its various press-releases.

<u>Releases and Discharges</u>

45. The proposed Approval and Vesting Order includes a comprehensive release and discharge in favour of (i) the present and former directors, officers, employees, legal counsel and advisors of the Petitioners (including for purpose of clarity Newco 1, Newco 3 and AmalCo), (ii) the Monitor and its legal counsel, and (iii) the Streamers under the Stream Agreement, Diaquem Inc. and Investissement Quebec, including in each case their respective directors, officers, employees, legal counsel and advisors (the persons listed in (i), (ii) and (iii) being collectively the "**Released Parties**") from all Released Claims, that becomes effective upon the filing of the Certificate by the Monitor in connection with the closing of the Participating Streamers/Diaquem Transaction (the **"Release"**). The Release does not release any claim against the directors and officers of the Petitioner that is not permitted to be released pursuant to Section 5.1(2) of the CCAA.

46. The Release is an integral part of the Participating Streamers/Diaquem Transaction and is a condition to the closing thereof.

47. The Monitor understands that the purpose of the Release is to achieve certainty and finality for the Released Parties in the most efficient and appropriate manner given the current circumstances.

48. In addition, the Monitor believes that the Release is fair and justified in the circumstances as a result of the significant contributions of the Released Parties' to the restructuring efforts of the Petitioners and to achieving a positive outcome of these CCAA Proceedings including in particular through the completion of the Participating Streamers/Diaquem Transaction which will result in the assumption of the Vendor Assumed Liabilities, the continued payment of the Target Company Liabilities, as well as contributions relating to the provision of financing (Bridge Financing and Working Cap Facility) during the pendency of the CCAA proceedings and the continued support of the Streamers and Diaquem following closing of the Transactions.

49. Without the Release and the continued support of the Streamers and Diaquem, the Participating Streamers/Diaquem Transaction could not be completed.

50. The Monitor understands that the Motion will be served on the service list maintained in these CCAA Proceedings and on all mis-en-cause identified on the Motion. A copy of this Second Report will also be served by the Monitor (or the Petitioners) on such Parties.

51. In light of the foregoing, in the Monitor's opinion, the Release contained in the SPA and the proposed Approval and Vesting Order, including those relating to Section 36.1 of the CCAA and Sections 38 and 95 to 101 of the BIA and any other federal or provincial law relating to preferences, fraudulent conveyances or transfers at undervalue, are fair and reasonable in the circumstances and will allow for the completion of the Participating Streamers/Diaquem Transaction.

52. In addition, consistent with the Pre-Closing Reorganization, the Excluded Liabilities shall be assigned to and shall vest absolutely and exclusively with NewCo 2 and NewCo 3, as applicable, and shall be forever discharged and released as against SDCI, Ashton, FCDC and NewCo 1 (as well as AmalCo, following the amalgamation). The Monitor is of the view that the vesting and assignment of these Excluded Liabilities and the corresponding releases and discharges are fair and reasonable in the circumstances.

INDEPENDENT REVIEW OF SECURITY

53. Counsel to the Monitor conducted a review of the security of the Streamers, Diaquem and Caterpillar Financial Services Limited (**"CFSL"**) over the Petitioners' assets and delivered its opinions to the Monitor (together, the "**Security Opinion**"). Subject to the customary qualifications, assumptions and limitations set out therein, the Security Opinion indicates that the security of the Streamers, Diaquem and CFSL over the Petitioners' assets that are subject to such security is valid and has been rendered opposable against third persons or perfected in accordance with applicable laws.

ACTUAL RECEIPTS AND DISBURSEMENTS

54. The highlights of the Petitioners' financial performance for the period commencing on September 9, 2019, and ending on September 29, 2019, are presented in the Actual Cash Flow annexed hereto as Table A. Our comments on the financial performance of the Petitioners during such period are as follows:

    (i) compared with the initial statement of projected cash flow presented by the Petitioners to the Court (the "**Initial Cash Flow Statement**"), the Petitioners experienced an unfavourable variance of approximately $275K in respect of cash inflows. The variance is primarily attributable to lower total net sales from September's sale, which is related to a lower quantity of carats sold, a weaker diamond price and partly offset by an appreciation of the US dollar relatively to the Canadian dollar.

    (ii) compared with the Initial Cash Flow Statement, the Petitioners experienced a favourable variance of approximately $7,518K in respect to the cash outflows. The variance is primarily attributable to the following:

        i. favourable variance of $317K related to lower payroll payments, as this expense has been lower than anticipated;
        ii. favourable variance of $3,389K related to lower than projected payments to suppliers. This variance is mainly due to timing as the Petitioners have been managing their supplier payments on a conservative basis, as most pre-filing invoices have been paid in the

normal course of business. Based on the revised cash flow statement, these disbursements will be made in the near future;

iii. favourable variance of $1,176K related to lower than projected payment to Gaz Metro. This lower payment is mainly due to timing. Based on the revised cash flow statement, this disbursement will be made in the coming weeks;

iv. unfavourable variance of $227K related to consultant fees as higher payments than projected have been made. This difference is permanent;

v. favourable variance of $1,000K related to bridge lenders professional fees, as those expenses have not been paid as of September 29. This variance is mainly due to timing as these disbursements will be made in the near future;

vi. favourable variance of $750K related to TD financial advisor fees, as those expenses have not been paid as of September 29. This variance is mainly due to timing as these disbursements will be made in the near future;

vii. favourable variance of $194K related to hedging agreements termination. This favourable variance results from the termination of all hedging agreements following the commencement of these CCAA Proceedings. No payments were required to be made. The variance is permanent;

viii. favourable variance of $741K related to the contingency for unexpected fees and expenses, as those expenses have been lower than anticipated; and

ix. favourable timing variance of $178K related to the other expenses initially budgeted. Based on the revised cash flow statement, these costs will have to be disbursed in the near future.

55. As of the date of this Second Report, all post-filing expenses incurred by the Petitioners have been or will be paid in the normal course out of the existing working capital of the Petitioners or through a draw of additional funds from the initial amount of $20 million made available as part of the Interim Financing as described in the Monitor's First Report. Consequently, at this time, the Petitioners do not require additional Interim Financing as appears from the revised cash flow statement annexed hereto as Table B.

OVERVIEW OF THE 9 WEEK CASH FLOW PROJECTIONS

56. The Petitioners, with the assistance of the Monitor, have prepared the statement of projected cash flow (the "**Cash Flow Statement**") for the 9-week period from September 30 to December 1, 2019 (the "**Cash Flow Period**") for the purpose of projecting the Petitioners' estimated liquidity needs during the Cash Flow Period. A copy of the Cash Flow Statement is attached as Appendix B to this Second Report.

57. The Cash Flow Statement has been prepared by the Petitioners using probable and hypothetical assumptions set out in the notes to the Cash Flow Statement.

58. The Monitor's review of the Cash Flow Statement consisted of inquiries, analytical procedures and discussions related to Information supplied to it by Management. Since the hypothetical assumptions need not be supported, the Monitor's procedures with respect to them were limited to evaluating whether they were consistent with the purpose of the Cash Flow Statement. The Monitor also reviewed the support provided by Management for the probable assumptions, and the preparation and presentation of the Cash Flow Statement.

59. Based on the Monitor's review and the foregoing qualifications and limitations, nothing has come to its attention that causes it to believe that, in all material respects:

(i) The hypothetical assumptions are not consistent with the purpose of the Cash Flow Statement;

(ii) As at the date of this Second Report, the probable assumptions developed by Management are not suitably supported and consistent with the plans of the Petitioners or do not provide a reasonable basis for the Cash Flow Statement, given the hypothetical assumptions; or

(iii) The Cash Flow Statement does not reflect the probable and hypothetical assumptions.

60. Since the Cash Flow Statement is based on assumptions regarding future events, actual results will vary from the information presented even if the hypothetical assumptions occur, and the variations may be material. Accordingly, the Monitor expresses no opinion as to whether the projections in the Cash Flow Statement will be achieved. The Monitor expresses no opinion or other form of assurance with respect to the accuracy of any financial information presented in this report, or relied upon in preparing this report. Neither does the Monitor express any opinion as to the performance of the Petitioners' statutory obligations with regard to projected payments to be made in accordance with the Cash Flow Statement, *inter alia* the payment of wages, the government remittances and the payroll deductions to be made by the Petitioners.

61. The Cash Flow Statement has been prepared solely for the purpose described in the Notes to the Cash Flow Statement, and readers are cautioned that the Cash Flow Statement may not be appropriate for other purposes.

62. Based on the projections for the period ending on December 1, 2019, the Petitioners should need to draw $2 million of additional funds from the Interim Financing. As of September 29, 2019, $7 million have already been drawn from the Interim Financing.

63. Management has advised the Monitor that it believes that the forecast reflected in the Cash Flow Statement is reasonable.

REQUEST FOR AMENDMENTS TO THE INITIAL ORDER

64. The Petitioners seek the issuance of the Amended and Restated Initial Order, which provides for, *inter alia*, the following:

(i) the addition of NewCo 2, and NewCo 3 as Petitioners in these CCAA Proceedings;

(ii) upon the Effective Date of the Participating Streamers/Diaquem Transaction:

    i. AmalCo will no longer be a Petitioner under these CCAA Proceedings; and

    ii. NewCo 2, NewCo 3 and SWY will remain Petitioners under these CCAA Proceedings;

(iii) effective as at the Closing Date, granting the Monitor with the additional power to assign SWY, NewCo 2 and NewCo 3 into bankruptcy, as the case may be.

REQUEST FOR EXTENSION OF THE STAY OF PROCEEDINGS

65. The Petitioners are seeking an extension of the Stay Period until November 30, 2019, in order to complete the Participating Streamers/Diaquem Transaction. The Monitor has been

advised that, in parallel, Stornoway intends to continue its mining operations in the ordinary course of business.

66. As described earlier in this Second Report, the Cash Flow Statement indicates that the Petitioners should have sufficient liquidity to continue to meet their obligations during the proposed extension of the Stay Period.

THE MONITOR'S CONCLUSIONS AND RECOMMENDATIONS

Participating Streamers/Diaquem Transaction

67. The Monitor is of the view that the Petitioners have canvased the market since April 2019, including through the SISP, and that the Participating Streamers/Diaquem Transaction is the best option available in the circumstances. The Monitor is further of the view that:

    (i) The aggregate consideration provided for under the Participating Streamers/Diaquem Transaction is fair and reasonable in the circumstances; and

    (ii) there is no evidence to suggest that any viable alternative exists that would deliver a better recovery for the Petitioners' creditors.

68. Accordingly, and based on the foregoing, the Monitor is of the view that the approval of the Participating Streamers/Diaquem Transaction is in the best interests of the stakeholders generally and the Monitor supports the Petitioners' request for approval of the Streamers/Diaquem Transaction and the granting of the orders sought in the Motion.

Release

69. For the reasons stated above, the Monitor supports the Petitioners' request for the Release.

Amendments to Initial Order and Extension of the Stay

70. As noted above, the current Stay Period expires on October 9, 2019. The Monitor understands that the extension of the Stay Period sought by the Petitioners is required to complete the Participating Streamers/Diaquem Transaction.

71. Based in the information presently available, the Monitor believes that creditors of the Petitioners will not be materially prejudiced by the proposed extension of the Stay Period.

72. The Monitor also believes that the Petitioners have acted, and are acting, in good faith and with due diligence and that the sought extension of the Stay Period is appropriate.

73. The Monitor respectfully submits to the Court this, its Second Report.

DATED AT MONTREAL, this 2nd day of October 2019.

DELOITTE RESTRUCTURING INC.
In its capacity as Court-Appointed Monitor of the Petitioners

Jean-François Nadon, CPA, CA, CIRP, LIT
President

Benoît Clouâtre, CPA, CA, CIRP, LIT
Senior Vice President

Appendix A

Stornoway Diamond Corporation
Cash Flow Projection - Budget to Actual
(in $000 CAD)

For the cumulative period of 4 weeks, from September 9, 2019 till September 29, 2019

	Budget	Actual	Var. ($)	Var. (%)	Comments
Receipts					
Gross Sales	20,910	20,520	(390)		The $390k cumulative and negative variance is related to September's sale. It is due to a lower quantity of carats sold (impacted negatively by $48k), a weaker diamond price (impacted negatively by $437k) and partly offset by an appreciation of the US dollar relatively to the Canadian dollar (impacted positevly by $95k).
Payment to Streamers	(2,509)	(2,394)	115		The cumulative positive variance is due to September's sale being lower than budgeted.
Sales Tax Receivable	-	-	-		
Cree Subvention	-	-	-		
Other Receipts	7,000	7,000	-		
Fuel Tax	-	-	-		
	25,401	25,126	(275)	-1.1%	
Disbursements					
Payroll	4,754	4,437	317		The $317k cumulative and positive variance is mainly due to timing. It should be offset in the upcoming weeks.
Severance	-	4	(4)		
Retention Incentives	200	100	100		
Rent	60	53	7		
Pension	360	328	32		
Group Insurance	235	227	8		
AP Payment	12,129	8,740	3,389		The $3,389k cumulative and positive variance is mainly due to timing and should be offset in the upcoming weeks.
Gaz Metro Payment	1,176	-	1,176		The $1,176k cumulative positive variance is mainly due to timing. It should be offset in the upcoming weeks.
Bond Renewal Fees	-	-	-		
Royalty to IQ	-	-	-		
Mining Duty	-	-	-		
Consultant Fees	1,000	1,227	(227)		The $227k cumulative and negative variance is permanent.
Bridge Lenders Professional Fees	1,000	-	1,000		The $1,000k cumulative and positive variance is mainly due to timing, as payments that were budgeted in the current and previous week should be made in the upcoming weeks.
TD Financial Advisor Fees	750	-	750		The $750k cumulative and positive variance is mainly due to timing, as payments that were budgeted in the previous week should be made in the upcoming weeks.
Hedging	108	(86)	194		The $194k cumuative and positive variance is permanent and is due to the fact that following the Company's CCAA filling, all hedging agreements were terminated, therefore no payments had to be made.
Insurance Tail	323	323	-		
Interest Payments on Bridge	-	-	-		
Debt Repayment - FTQ	-	-	-		
Debt Repayment - IBA	-	-	-		
Debt Repayment - Road Loan	-	-	-		
Debt Repayment - IQ	-	-	-		
Debt Repayment - Caterpillar	4,336	4,301	35		
Debt Repayment - Bondholders	-	-	-		
Contingencies and Others	720	(21)	741		Throughout the entire cash flow forecast, this contingency will cover unforeseen negative variances to the cashflow forecast.
	27,151	19,633	7,518	27.7%	
Other Transactions					
Bridge Lenders Redirection of Payments	2,509	2,393	(116)		The cumulative negative variance for bridge lenders redirection of payments is in line with the payment to streamers variance.
Bridge Lenders Funding	5,700	5,700	-		
Net Cash Flow	6,459	13,586	7,127	110.3%	
Beginning Cash	4,839	5,025	185		
Ending Cash	**11,298**	**18,610**	**7,312**	**65%**	

Appendix B
Cash flow Statement

SDC
Cash Flow Projection
(in $000 CAD)

Week beginning:	30-Sep-19	7-Oct-19	14-Oct-19	21-Oct-19	28-Oct-19	4-Nov-19	11-Nov-19	18-Nov-19	25-Nov-19	30-Sep-19
Week ending:	6-Oct-19	13-Oct-19	20-Oct-19	27-Oct-19	3-Nov-19	10-Nov-19	17-Nov-19	24-Nov-19	1-Dec-19	1-Dec-19
Receipts										
Gross Sales	-	-	-	-	22,398	-	-	-	-	22,398
Payment to Streamers	-	-	-	-	(2,688)	-	-	-	-	(2,688)
Sales Tax Receivable	-	-	-	-	-	-	-	-	-	-
Cree Grant	-	-	-	372	-	-	-	-	-	372
Working Cap Facility ("WCF")	-	-	-	2,000	-	-	-	-	-	2,000
Fuel Tax	-	-	-	-	385	-	-	-	-	385
	-	-	-	2,372	20,095	-	-	-	-	22,467
Disbursements										
Payroll	1,408	824	1,501	917	1,408	1,207	1,213	1,220	1,227	10,925
Severance	-	-	285	-	-	-	-	-	-	285
Retention Incentives	100	-	-	-	-	-	-	-	-	100
Rent	60	-	-	-	60	-	-	-	-	120
Pension	113	67	113	67	113	97	97	98	98	862
Group Insurance	235	-	-	-	235	-	-	-	-	470
AP Payment	1,777	2,677	3,154	2,584	1,408	2,273	2,273	2,273	1,051	19,471
Gaz Metro Payment	1,176	-	-	-	1,045	-	-	-	1,222	3,443
Bond Renewal Fees	-	-	-	-	-	-	-	-	-	-
Royalty to IQ	-	-	-	-	-	-	-	-	-	-
Mining Duty	-	-	-	-	-	-	-	-	-	-
CCAA Consultant Fees	200	200	-	150	150	-	-	-	-	700
Bridge Lenders Professional Fees	-	-	-	-	1,350	-	-	-	-	1,350
TD Financial Advisor Fees	-	-	-	-	750	-	-	-	-	750
Hedging	-	-	-	-	-	-	-	-	-	-
Insurance Tail	-	-	-	-	-	-	-	-	-	-
Interest Payments on WCF	-	-	-	-	-	-	-	-	-	-
Debt Repayment - FTQ	-	-	-	-	-	-	-	-	-	-
Debt Repayment - IBA	393	-	-	-	-	-	-	-	-	393
Debt Repayment - Road Loan	-	-	-	-	-	-	-	-	-	-
Debt Repayment - IQ	-	-	-	-	-	-	-	-	-	-
Debt Repayment - Caterpillar	-	-	-	-	-	-	-	-	-	-
Debt Repayment - Bondholders	-	-	-	-	-	-	-	-	-	-
	5,462	3,768	5,053	3,718	6,519	3,577	3,584	3,591	3,598	38,869
Contingencies	(180)	(180)	(180)	(180)	(180)	(180)	(180)	(180)	(180)	(1,620)
WCF Lenders Redirection of Payments	-	-	-	-	-	2,688	-	-	-	2,688
Bridge Lenders Funding	-	-	-	-	-	-	-	-	-	-
Net Cash Flow	(5,642)	(3,948)	(5,233)	(1,526)	13,396	(1,069)	(3,764)	(3,771)	(3,778)	(15,334)
Beginning Cash	18,610	12,968	9,020	3,787	2,261	15,658	14,589	10,825	7,054	18,610
Ending Cash	**12,968**	**9,020**	**3,787**	**2,261**	**15,658**	**14,589**	**10,825**	**7,054**	**3,276**	**3,276**

NOTES TO THE CASH-FLOW STATEMENT

NOTE A – PURPOSE

The purpose of these cash-flow projections is to determine the liquidity requirements of the Company during the CCAA proceedings.

NOTE B

The Cash Flow Statement has been prepared by the Company using probable and hypothetical assumptions set out in the notes to the Cash Flow Statement.

The Proposed Monitor's review of the Cash Flow Statement consisted of inquiries, analytical procedures and discussions related to Information supplied to it by Management. Since the hypothetical assumptions need not be supported, the Proposed Monitor's procedures with respect to them were limited to evaluating whether they were consistent with the purpose of the Cash Flow Statement. The Proposed Monitor also reviewed the support provided by Management for the probable assumptions, and the preparation and presentation of the Cash Flow Statement.

NOTE C - DEFINITIONS

(1) CASH-FLOW STATEMENT

In respect of a Company, means a statement indicating, on a weekly basis (or such other basis as is appropriate in the circumstances), the projected cash-flow of the Company as defined in section 2(1) of the Act based on Probable and Hypothetical Assumptions that reflect the Company's planned course of action for the period covered.

(2) HYPOTHETICAL ASSUMPTIONS:

Means assumptions with respect to a set of economic conditions or courses of action that are not necessarily the most probable in the Company's judgment, but are consistent with the purpose of the Cash-Flow Statement.

(3) PROBABLE ASSUMPTIONS:

Means assumptions that:

(i) The Company believes reflect the most probable set of economic conditions and planned courses of action, **Suitably Supported** that are consistent with the plans of the Company; and
(ii) Provide a reasonable basis for the Cash-Flow Statement.

(4) SUITABLY SUPPORTED:

Means that the Assumptions are based on either one or more of the following factors:

(i) The past performance of the Company;
(ii) The performance of other industry/market participants engaged in similar activities as the Company;
(iii) Feasibility studies;
(iv) Marketing studies; or
(v) Any other reliable source of information that provides objective corroboration of the reasonableness of the Assumptions.

The extent of detailed information supporting each Assumption, and an assessment as to the reasonableness of each Assumption, will vary according to circumstances and will be influenced by factors such as the significance of the Assumption and the availability and quality of the supporting information.

NOTE C - ASSUMPTIONS

Assumptions	Source	Probable Assumption	Hypothetical Assumption
Opening cash balance	Based on current bank balances	x	
Exchange rate	Exchange rates used by management are the following: • US $ / Cnd $ = 1.32 / 1.00		x
Forecast cash receipts:			
Gross sales	Amounts related to the 19-07 diamonds sales (USD$66.23 / ct, 256,200 ct)	x	x
Payment to Streamers	Amount due to the streamers related to the 19-07 sale – to be re-advanced as per Amended Bridge Loan Agreement	x	x
Cree grant	Based on the Company's calculation and historical receipts	x	
Working cap facility ("WCF")	Interim financing during CCAA	x	
Fuel tax	Fuel tax receivable from the Government	x	
Forecast cash disbursements:			
Payroll	Based on the Company's historical payroll reports	x	
Retention incentives	Based on the Company's plan already in place to retain key employees an amount of $300K is currently held in NRF trust account – the total amount of $400k will be released to employees at the end of September 2019	x	
Rent	Based on lease agreements	x	
Pension	Employer portion of pension costs for employees based on contracts	x	
Group insurance	Insurance costs for employees insurance based on insurance contracts	x	
AP payment	Weekly estimate of disbursements required based on historical costs	x	

Gaz Metro payment	Monthly estimate of disbursements required based on historical costs	x	
Consultant fees	Management estimate of professional fees to be incurred in the following weeks for monitor and legal services		x
WCF lenders professional fees	Management estimate of professional fees to be incurred in the following weeks for secured lenders legal services		x
TD financial advisor fees	Based on contract with the Company financial advisors regarding SISP	x	
Hedging	All hedging agreements have been terminated by mutual agreement		x
Insurance tail	Based on insurance contract	x	
Debt repayment - IBA	Based on loan contracts with the Cree nation	x	
Debt Repayment - Caterpillar	Based on loan contracts with Caterpillar	x	
Contingencies	General provision		x
Bridge lenders redirection of payments	Amount reimbursed by the streamers related to the 19-07 sale	x	
Interim Facility advance	As per WCF and budget needs	x	
Amended Bridge Loan advance	As per Amended Bridge Loan Agreement	x	