

**Receiver's Second Report  
RE: CIC Pulp Ltd. operating as  
Meadow Lake Limited Partnership and  
Meadow Lake Pulp Ltd.**

**RSM Richter Inc.**  
Calgary, December 18, 2008

CANADA )  
PROVINCE OF SASKATCHEWAN )

IN THE QUEEN'S BENCH  
JUDICIAL CENTRE OF REGINA

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*  
R.S.C. 1985, C.C-36 AS AMENDED

AND IN THE MATTER OF A PROPOSED PLAN OF ARRANGEMENT FOR  
THE CREDITORS OF CIC PULP LTD. in its capacity as a general partner of  
MEADOW LAKE PULP LIMITED PARTNERSHIP and  
MEADOW LAKE PULP LTD. in its own capacity as agent and nominee for  
Meadow Lake Pulp Limited Partnership

BETWEEN:

CIC PULP LTD., operating as MEADOW LAKE PULP LIMITED PARTNERSHIP  
and MEADOW LAKE PULP LTD.

APPLICANTS

- and -

HSBC BANK CANADA, INVESTMENT SASKATCHEWAN INC.,  
101069101 SASKATCHEWAN INC., GUSCO HANDEL G. SCHARFELD & CO.,  
MILLAR WESTERN INVESTMENTS (SASKATCHEWAN) LTD.,  
MILLAR WESTERN HOLDINGS (MEADOW LAKE) LTD.  
and MILLAR WESTERN INDUSTRIES LTD.

RESPONDENTS

Receiver's Second Report  
December 18, 2008

1.0 INTRODUCTION

- 1.1 This report is filed by RSM Richter Inc. ("Richter") in its capacity as Receiver and Manager ("Receiver") of CIC Pulp Ltd. operating as Meadow Lake Pulp Limited Partnership and Meadow Lake Pulp Ltd. (collectively "MLPLP") pursuant to an Order of the Court of Queen's Bench of Saskatchewan ("Court") made on October 1, 2007 (the "Receivership Order").

- 1.2 Richter was previously appointed monitor (the "Monitor") of MLPLP pursuant to an Order of the Court made on December 28, 2005 granting MLPLP protection under the *Companies' Creditors Arrangement Act* (the "CCAA Order"). The Monitor was discharged on October 29, 2007.
- 1.3 On January 11, 2007, the Court approved the sale of MLPLP's pulp mill (the "Mill") to Meadow Lake Mechanical Pulp Inc. ("MLMP"). The sale closed on January 23, 2007 in accordance with the purchase and sale agreement ("PSA").
- 1.4 101069101 Saskatchewan Ltd. ("101"), MLMP, Elite Shine Investments Limited ("Elite"), which owns 80% of the common shares of MLMP, and MLPLP have entered into an agreement whereby Elite will purchase 101's interest in MLMP (comprising 101's 20% of MLMP's common shares and a promissory note) for a total of \$9,322,829; \$6,386,999 for 101's Class "A" common shares and \$2,935,830 for 101's Promissory Note.
- 1.5 The Receiver provided its first report to the Court (the "First Report") dated December 10, 2008.
- 1.6 The purpose of this report is to:
- Provide additional information to the Court in respect of certain repair and remediation costs associated with the Mill's water recovery pond (the "Recovery Pond"); and
  - Respectfully recommend the Court approve the payment of \$2.0 million to Elite in respect of the Recovery Pond's repair and remediation costs pursuant to a Release and Settlement Agreement to be made among 101, MLMP, Elite and MLPLP.

## 2.0 RECOVERY POND

- 2.1 The Receiver reported in its First Report that the Mill uses the Recovery Pond in connection with its pulp production process. The water held and circulated in the Recovery Pond has a significant elevated salt content compared to fresh ground water in the Meadow Lake area. Two settling water ponds are used in connection with the Recovery Pond and they also contain elevated salt content. The Recovery Pond (and the

settlement ponds) is an integral component of the Mill's production process. It was MLPLP's view that the Recovery Pond's liner was breached and it was leaking, perhaps contaminating MLPLP's property and nearby ground waters.

- 2.2 The PSA addressed this issue by providing for MLPLP to take steps to repair the Recovery Pond. MLMP obtained a cost estimate to repair the Recovery Pond (and clean the settlement ponds) a copy of which is attached as Exhibit "A". The cost to repair the Recovery Pond as estimated by MLMP is \$1.7 million. It would take several months to drain the Recovery Pond, assess the level of contamination, remove any contaminated soil and replace the liner. Repairing the Recovery Pond entails constructing a complicated bypass system so as not to interrupt the Mill's production process. Shutting down the Mill's operations for several months to effect repairs would be more costly than constructing a bypass system.
- 2.3 The Monitor engaged an environmental firm, SLR Consulting (Canada) Ltd., ("SLR"), to conduct a phase I and subsequently a phase II Environmental Site Assessment ("ESA") of the Mill's landfill sites (which were not purchased by MLMP). SLR was also engaged to conduct a series of soil samples around the Recovery Pond. It was not possible to obtain soil samples from directly underneath the Recovery Pond without draining it. Based on the soil samples that were obtained, SLR concluded that there does not appear to be significant leakage from the Recovery Pond, but there does appear to be contamination associated therewith.
- 2.4 The Receiver requested SLR review MLMP's cost estimate to repair the Recovery Pond for reasonability. A copy of the SLR internal memorandum dated October 2, 2008 in respect of their review is attached as Exhibit "B". SLR concluded that MLMP's overall approach to repair the Recovery Pond and the costs associated therewith appear to be sound. SLR noted in its memorandum that there may be alternative approaches to optimize MLMP's repair and remediation process, but that the cost savings associated with those options may be insignificant.

- 2.5 The cost to repair the Recovery Pond is an estimate based on available information. The extent of environmental contamination is unknown as soil samples from directly beneath the Recovery Pond cannot be obtained without draining it. There is a risk that the costs to complete the repairs may exceed \$1.7 million depending on the complexities encountered during the course of the remediation and repairs. MLPLP and MLMP have negotiated an agreement whereby MLPLP will pay MLMP \$2.0 million (from funds held by the Receiver) to settle this matter. In return, MLMP will covenant to repair and remediate the Recovery Pond (such repair was required by MLPLP pursuant to the PSA), and release MLPLP from any further responsibility in respect thereof. The Release and Settlement Agreement negotiated by MLPLP and MLMP is attached as Exhibit "C".
- 2.6 The Saskatchewan Ministry of Environment ("SMOE") has been regularly consulted with the proposed remediation of the landfill sites and environmental issues in respect of the Recovery Pond. The Receiver understands that SMOE does not oppose MLPLP's application nor the Release and Settlement Agreement, and will work directly with MLMP as it undertakes repairs and remediation work on the Recovery Pond. SMOE will provide a letter to this effect to MLPLP's legal counsel which will be made available to the Court once it is received.

### 3.0 OTHER

- 3.1 The Receiver holds and has invested \$42,583,386 payable to 101 and ISI (arising from the sale of inventory and the collection of accounts receivable). The funds can only be distributed in accordance with an Order or Orders of this Honourable Court. The \$2.0 million to be paid to MLMP is to be paid from the funds held by the Receiver.
- 3.2 The Receiver understands that 101 and ISI intend that the remaining funds will continue to be held by the Receiver until the costs associated with the capping of the landfill sites and long term monitoring program are known, at which time 101 and ISI envisage making a Court application for the distribution of the funds held by the Receiver.

3.3 Millar Western Forest Products Ltd. (MWF") provided marketing and other services to MLPLP pursuant to a Marketing Services Agreement ("MSA") and an Administrative Services Agreement ("ASA"). Both the MSA and ASA were terminated in 2007. Addressing the environmental matters as aforementioned in this report, in the Receiver's opinion, should be acceptable to MWF.

#### 4.0 CONCLUSION AND RECOMMENDATION

4.1 The PSA contemplated that MLPLP would repair the Recovery Pond including addressing environmental contamination associated with it. A cost estimate to effect repairs has been obtained, however, it is an estimate and actual costs may vary, perhaps materially. The negotiated Release and Settlement Agreement addresses rectification of the Recovery Pond, requires MLMP to assume the responsibility for repairs and SMOE does not oppose this application. The Receiver, therefore, respectfully recommends that the Court approve the payment of \$2.0 million to MLMP from the funds held by the Receiver.

All of which is respectfully submitted this 18<sup>th</sup> day of December, 2008.

**RSM RICHTER INC.  
IN ITS CAPACITY AS RECEIVER AND MANAGER  
OF CIC PULP LTD. OPERATING AS  
MEADOW LAKE PULP LIMITED PARTNERSHIP  
AND MEADOW LAKE PULP LTD.**



Per: Robert J. Taylor, CA, CIRP



# MEADOW LAKE MECHANICAL PULP

A DIVISION OF SINARMAS GROUP

## MEMORANDUM

**DATE:** 2008 September 04  
**TO:** Ed Roste  
**FROM:** Doug Chisholm, Colin Schenk, Les Meyers, John Hayes  
**SUBJECT:** WRP Cleaning, Bypass, Relining.

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Ed – Please see attached the estimate for cleaning, Bypassing and relining the WRP.

### *Description of Work*

- **Cleaning out the 3 ponds – 2 settling ponds and WRP.**
  - Quotation from Everready
  - Cleaning can be done with the pond in Operation.
  - Duration is estimated at 80-90 days
  - Polymer usage is estimated from two samples in the ponds
  - Equipment supplied for round the clock work
    - Remote dredge
    - 2 dewatering units
    - Tanks, pumps and pipeline
    - Sludge conditioning tank and hopper

Estimated Cost – \$900,000

- **Mobilization / Demobilization costs**
  - Mobilization \$25,000
  - Demobilization \$25,000
  - Crane Costs \$25,000



- **Disposal of dredged Material**
  - Landfill - Trucking Cost required
  - Burn in Olivine - Loader will be used
  - Trucking Costs - \$75,000
  
- **Relining the pond with a liner similar to the DEP**
  - Estimate by Century Environmental
  - Estimated Time – 1month

Liner Costs - \$175,000  
 Bottom Preparation work - \$175,000

- **Bypass the pond while lining is being installed**

Description

- Inlet to settling ponds to remain the same (at the west end) both valves to the settling ponds would be open. V shaped weirs would be installed at the end of the outlets to split the flow equally to each pond.
- The overflows from the settling ponds to the WRP would be blocked off
- Pumping station will be set up to pump to the existing WRP pump suction c/w a recirculation line
- An equalization line would be installed between the two setting ponds.
- The set up is the designed to operate in the summer.

Estimated Costs -\$300,000

Total Estimated Costs - \$ 1,700,000

The best time to do this would be to start in the early spring and dewater for 2.5 months, empty the WRP for approx. 1 month and reline for 1 month and then put the WRP back into service in September.







that this degree of competence would then be applied to the operation of the centrifuge during the processing period, maintaining a low risk of reduced centrifuge efficiency.

The use of two centrifuges, as proposed should limit the impact of down time for maintenance and allow continued processing in the event of a more significant failure of either machine.

The initial dredging and processing period is estimated to be 2.5 months, with a total estimated volume of 48,000 m<sup>3</sup> being treated. Based on the 24hr per day 7 days per week processing indicated, this would require operation at a treatment rate of the order of 27 m<sup>3</sup>/hr. Since the proposal indicates the use of two centrifuges, each would be required to process approx 13.5 m<sup>3</sup>/hr, a size which is typical of many applications.

The capacity of the WRP is shown to be 24,000 m<sup>3</sup>. Since 48,000 m<sup>3</sup> is to be processed, it is therefore assumed that the centrate is being recycled to the WRP to assist in removal of heavy bottom sludge during the desludging period, or water from some other source is being added. The dredging unit is assumed to be capable of processing a slightly greater volume than the centrifuges, and would need a capacity of the order of 33 m<sup>3</sup>/hr to empty the WRP in the one month period indicated in the proposal, which would not be unreasonable. However, we could find no description of the disposal route for this water. This is a substantial volume and its disposal would incur significant costs.

The costed proposal indicates there is some uncertainty over the dry solids content of the cake, and notes the impact of fibre content on the speed of processing. This is very important. 40% (as shown in the proposal) would seem to be a high dry solids content to anticipate (generally centrifuge cakes would be anticipated to be around 30% dry solids), but if this has been found during trials on samples and can be achieved in operation, then the costs of disposal of the dry cake will be minimized.

No details were available of the method proposed to reline the WRP, and thus it is not possible for us to comment on this aspect.

### **Proposed Program**

The initial dredging and processing period estimate of 2.5 months seems reasonable. Based on the 24hr per day 7 days per week processing indicated, this would require operation at a treatment rate of the order of 27 m<sup>3</sup>/hr. Since the proposal indicates the use of two centrifuges, each would be required to process approx 13.5 m<sup>3</sup>/hr, if operated in parallel, a size which is typical of many applications. These are relatively small units and should be reliable and easy to maintain, leading to the conclusion that this element of the programme should be relatively simple to achieve. It is possible that use of larger units could shorten the program if this is beneficial.

Without detail of the volume of solids currently retained in the WRP it is difficult to assess the quantity of solids, which will need to be transported to landfill. However, a conservative estimate would indicate a daily volume of less than 15 m<sup>3</sup>, which would only require the use of a single vehicle to transport. This should not therefore limit the speed of processing. It is assumed that the dewatered sludge would be directly discharged into containers using a movable conveyor.

The one month period proposed for emptying the WRP would appear to be consistent with the capacity of the equipment required for processing the sludge, and thus relatively easy to achieve. However, in order to meet the programme it will also be necessary to be able to transfer the water removed to wherever it is being stored or disposed of at the same rate of removal of approximately 30 m<sup>3</sup>/hr. We have no information as to whether the necessary

transport capacity exists, or whether arrangements have been made to store or dispose of this water. This would need further clarification to enable additional comment to be made.

The outline programme suggests relining of the WRP will take about one month. It is difficult to comment on this without knowledge of the method of repair which is being proposed. This would also need further clarification to enable additional comment to be made.

### **Proposed Costs**

The proposal indicates a daily standby rate of \$7,850 for the centrifuge operating crew. If this is extended to the programme duration, it would amount to a total cost of \$765,000 for personnel, leaving \$225,000 as the cost of hire of the processing equipment and consumables. Chemical costs are estimated to be of the order of \$25,000. Hire of the processing equipment would therefore be of the order of \$200,000 which equates to about \$2,000 per day. This would appear to be quite expensive. In our experience a system could be hired for the order of \$1000 - \$1200 per day and would be supervised by only one operator at any time. This is dependent on the availability of local contractors and local economic conditions.

With respect to the liner installation, the liner unit cost looks reasonable for supply and install. However, the base preparation costs are not itemized, but we would expect this would consist of re-contouring the base to provide a smooth surface for the new liner. In this case \$175,000 seems high. We would have anticipated this could be accomplished in a few days with a suitable piece of machinery which should be much less than \$175,000.

### **Impact On Mill Operations**

The proposal indicates that the WRP would be removed from the processing stream during the clean-up period and water would be recycled through the settling ponds only. Our interpretation of the process flow sheet information available suggests that only aeration takes place in the WRP rather than any other substantial processing. In addition, the reference to the proposed temporary arrangements for the settling pond being as designed for the summer suggests this approach might have been used before and has proved to be successful. If this is the case, it would be reasonable to assume it would be satisfactory again. If not, it may be that consideration could be given to operating the settling ponds in series rather than parallel as this could lower the risk of problems arising from excursions in the quality of feed to the ponds – local knowledge of the process will, however, be the best basis on which to make this assessment.

It is assumed from the documentation provided that the centrate from the sludge processing operation will not be recycled to the pulping process during this period but may be used to assist in loosening of sludge in the WRP. This is considered to be the preferred option as if the centrate were to be used, higher solids content in the centrate and in particular any residual polymer retained in the centrate could have an impact on the pulping process.

If the settling ponds were to be operated in series, it would be expected that the first would carry the higher sludge load. Whilst the centrifuges are on site, consideration might be given to intermediate pumping of this sludge and dewatering in one of the centrifuges which would improve overall sludge settling capacity and consequently generate the best possible water quality for recycling.

### **Summary**

The review undertaken by SLR has shown that the overall approach proposed to enable the repair of the WRP base appears to be sound, based on interpretation of the data made available to SLR. One or two issues have been raised by the review which may be worthy of consideration as possible means by which risk could be reduced or the process optimized. It is recognized, however, that these may be rendered insignificant with greater understanding of the detail of the proposal.

Further information on the method of disposal of the water from the WRP and the method of repair of then lining would enable a more comprehensive response to be made. A more detailed breakdown of the costs would be helpful to allow further comment on these to be made.

Stuart

*DRAFT*  
*December 1, 2008*

**RELEASE AND SETTLEMENT AGREEMENT**

This Release and Settlement Agreement (the "Agreement"), dated as of [◆, 2008], is made and entered into between 101069101 SASKATCHEWAN LTD. ("101"), MEADOW LAKE MECHANICAL PULP INC. ("MLMP"), MEADOW LAKE PULP LIMITED PARTNERSHIP, by its receiver and manager RSM RICHTER INC. (the "Partnership"), MEADOW LAKE PULP LTD., by its receiver and manager RSM RICHTER INC. ("MLP"), and ELITE SHINE INVESTMENTS LIMITED ("ELITE") (collectively, the "Parties").

**WHEREAS**, MLMP and King Paper Source International Trading (Shanghai) Co., Ltd. ("KPS") are parties to a pulp purchase agreement dated as of January 23, 2007 (the "Off-Take Agreement");

**WHEREAS**, MLMP and KPS wish to make certain amendments to the Off-Take Agreement as more particularly described in the first amending agreement dated January 31, 2007 and the second amending agreement dated February 5, 2008 (the "Amending Agreements");

**WHEREAS**, Pursuant to the unanimous shareholders agreement dated January 23, 2007 made between 101, Elite and MLMP, MLMP is not permitted to agree to or permit any amendment of the terms of the Off-Take Agreement without the prior written consent of 101;

**WHEREAS**, 101 has agreed to consent to the amendments contemplated by the Amending Agreements on a conditional basis, subject to the terms and conditions set out in a conditional delivery agreement dated as of July 21, 2008 (the "Conditional Delivery Agreement");

**WHEREAS**, one of the conditions set out in the Conditional Delivery Agreement is that 101 and MLMP agree on a final resolution satisfactory to both of them with regards to the remediation of the water recovery pond as required by the 101 Agreement dated January 23, 2007 made between 101, MLMP, Investment Saskatchewan Inc. ("ISI") and Meadow Lake Pulp Ltd. (the "101 Agreement");

**WHEREAS**, the Parties desire to terminate the 101 Agreement as well as the securities pledge and assignment agreement (the "Securities Pledge and Assignment Agreement") and the landfill lands use agreement (the "Landfill Lands Use Agreement") both entered into in connection with the 101 Agreement and both dated as of January 23, 2007 and release each other from all obligations, past and future, owing to one another thereunder;

**NOW, THEREFORE, IN CONSIDERATION OF** the mutual covenants and agreements set forth herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Parties agree as follows:

**1. Definitions:** All capitalized terms not otherwise defined herein have the means ascribed to them in the 101 Agreement.

2. **Payment:** The Partnership shall pay no later than the close of business, Central Standard Time, on ♦, 2008 (the "Stipulated Payment Time"), to MLMP, the amount of \$2,000,000 CDN (the "Payment"). MLMP agrees to use the Payment for the sole and express purposes of the fulfillment of its obligations pursuant to section 6 below.

3. **Condition Precedent:** This Release and Settlement Agreement is subject to the condition precedent that the Partnership obtain an Order of the Saskatchewan Court of Queen's Bench authorizing the Payment. If for any reason, the Partnership has not obtained the Order described in the preceding sentence or MLMP has not received the Payment within 5 days of the Stipulated Payment Time, the Parties agree that the condition precedent shall not have been satisfied and this Agreement shall be null and void and of no force or effect.

4. **Release:** Upon the fulfillment of Article 2 and Article 3 of this Release and Settlement Agreement by the relevant Party, the Parties agree that the 101 Agreement, the Securities Pledge and Assignment Agreement and the Landfill Lands Use Agreement shall be terminated and the Parties shall unconditionally release, acquit, and discharge each other, as well as their respective successors, assigns, shareholders, direct or indirect parents, subsidiaries and affiliates, and each of their respective officers, directors, employees, representatives, subcontractors, agents, insurers and attorneys from and against any and all claims, suits, causes of action (whether in law or equity), rights, obligations, indemnities, undertakings, debts, agreements, liabilities, or damages whatsoever that either of the Parties, their respective successors, assigns, shareholders, direct or indirect parents, subsidiaries and affiliates, their respective officers, directors, employees, representatives, subcontractors, agents and attorneys once had, now have or could assert in the future against each other or any other party in connection with the 101 Agreement or a breach thereof.

5. **Return of Security:** Upon the fulfillment of Article 2 and Article 3 of this Release and Settlement Agreement by the relevant Party, Elite shall return to 101 the Pledged Notes and the certificate representing the Pledged Shares delivered to Elite pursuant to the 101 Agreement and the Securities Pledge and Assignment Agreement.

6. **Use of Payment:** MLMP agrees to use the Payment solely for the purposes of remediating the MLPLP Pond Environmental Contamination and, to that end, agrees as follows:

- (a) MLMP shall as soon as reasonably practicable following its receipt of the payment commence with the development of a plan for the remediation of the MLPLP Pond Environmental Contamination;
- (b) MLMP shall consult with 101 in the development of its remediation plan and shall keep 101 apprised as to the finalization and implementation of such plan;
- (c) MLMP shall exercise its best commercial efforts to complete the remediation of the MLPLP Pond Environmental Contamination within two years of the date of this Agreement.

7. **All Claims Are Barred:** Except for such actions as may be necessary or appropriate to enforce the terms of this Agreement, the Parties irrevocably covenant to refrain from making any claim or demand, or causing to be commenced, any suit, action or proceeding of any kind or character whatsoever against each other arising out of, resulting from or in any way related to the 101 Agreement, the Securities Pledge and Assignment Agreement or the Landfill Lands Use Agreement.

8. **Entire Agreement:** This Agreement constitutes the complete understanding between and among the Parties. No modification of this Agreement shall be binding, unless evidenced in writing and signed by an authorized representative of each of the Parties.

9. **Enurement:** This Agreement shall be binding on and inure to the benefit of each of the Parties, their successors, representatives, agents, officers, directors, employees and assigns.

10. **Proper Authority:** The persons executing this Agreement on behalf of the Parties each represent and warrant that they have full and complete authority to do so, and to make and give the promises, releases, and covenants set forth in this Agreement. The Parties each represent and warrant that the claims released by each of them pursuant to this Agreement have not been assigned.

11. **Governing Law:** The terms of this Agreement shall be governed, construed and enforced in accordance with the internal laws of the Province of Saskatchewan, without regard to Saskatchewan conflict of laws provisions.

12. **Counterparts and Facsimile Execution:** This Agreement may be executed in identical counterparts and by fax signature, and each such counterpart shall be deemed an original but such counterparts shall nevertheless together constitute one and the same instrument.

*(The next page is the signature page)*

IN WITNESS HEREOF, the undersigned certify their assent to the terms of this Agreement.

**101069101 SASKATCHEWAN LTD.**

By: \_\_\_\_\_  
Name:  
Title:

By: \_\_\_\_\_  
Name:  
Title:

**MEADOW LAKE PULP LIMITED PARTNERSHIP, by its receiver and manager RSM RICHTER INC.**

By: \_\_\_\_\_  
Name:  
Title:

**ELITE SHINE INVESTMENTS LIMITED**

By: \_\_\_\_\_  
Name:  
Title:

By: \_\_\_\_\_  
Name:  
Title:

**MEADOW LAKE MECHANICAL PULP INC.**

By: \_\_\_\_\_  
Name:  
Title:

By: \_\_\_\_\_  
Name:  
Title:

**MEADOW LAKE PULP LTD., by its receiver and manager RSM RICHTER INC.**

By: \_\_\_\_\_  
Name:  
Title:

*(Signature page to Release and Settlement Agreement)*