

CANADA

PROVINCE OF QUÉBEC
DISTRICT OF
MONTREAL

No.: 500-11-036133-094

SUPERIOR COURT

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

**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

**FORTY-NINTH REPORT OF THE MONITOR
JULY 7, 2010**

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 and affiliates 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 the 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 subsequently extended to July 9, 2010 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 the “**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. BCHI, Bowater Canada Finance Corporation (“**BCFC**”), Bowater Canadian Limited, AbitibiBowater Canada Inc., BCFPI, Bowater LaHave Corporation and Bowater Maritimes Inc. have commenced both CCAA Proceedings and Chapter 11 Proceedings and are referred to herein collectively as the “**Cross-Border Petitioners**” and are also included in the definition of “**Petitioners**”.

5. The Petitioners are all subsidiaries of ABH (ABH, collectively with its subsidiaries, are referred to as the “**ABH Group**”).
6. 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.
7. 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.
8. On April 22, 2009, the Court amended the Initial Order to extend the stay of proceedings to the partnerships (the “**Partnerships**”) listed in Appendix “**D**” hereto.

BACKGROUND

9. 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.
10. 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 (“**ABUSH**”) (ABUSH and its respective subsidiaries are collectively referred to as the “**DCorp Group**”).
11. ACI is a direct and indirect wholly-owned subsidiary of ABH.
12. ABH wholly owns BI which in turn, wholly owns BCHI which, in turn, indirectly owns BCFPI which carries on the main Canadian operations of BI.

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

TERMS OF REFERENCE

14. In preparing this forty-ninth report of the Monitor (the “**Forty-Ninth Report**”) in these CCAA Proceedings, 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 (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 Forty-Ninth Report. Some of the information referred to in this Forty-Ninth 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 Forty-Ninth 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 Forty-Ninth Report are as defined in the previous reports of the Monitor and the Initial Order. All references to dollars are in U.S. currency and are translated at a rate of CDN\$1.00=US\$0.98 unless otherwise noted.
16. A glossary of the defined terms for the legal entities referred to in the Forty-Ninth Report is attached as Appendix “E”.
17. Copies of all of the Monitor's Reports, in both English and French, including a copy of this Forty-Ninth Report, and all motion records and Orders in the CCAA Proceedings will be available on the Monitor's website at www.ey.com/ca/abibowater. 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.

18. 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/abitibibowater>. The Monitor has included a link to Epiq's website from the Monitor's website.

PURPOSE

19. The purpose of this Forty-Ninth Report is to report to this Honourable Court with respect to the following:
 - (i) a summary of the transactions giving rise to issuance of the 7.95% unsecured notes issued October 31, 2001 (the "**7.95% Notes**") by BCFC;
 - (ii) a summary of BCFC's intercompany transactions for the three year period prior to the date of the Initial Order and the financial impact of these transactions on BCFC; and
 - (iii) the balance sheets of BCFC as at March 31, 2009 and December 31, 2008.
20. This Forty-Ninth Report represents the interim report of the Monitor in respect of the above-noted intercompany transactions. This report has been prepared on an expedited basis to accommodate the requests of certain of the holders of the 7.95% Notes. The transactions reviewed by the Monitor occurred as long as nine years ago. Consequently, documents have been difficult to locate and certain individuals involved in the transactions are no longer with the Petitioners. The Petitioners have been very cooperative with the Monitor in respect of the preparation of this Forty-Ninth Report but have not yet been able to locate certain relevant documents (as noted herein) and other documents have only very recently been provided to the Monitor for its review, including certain documents which have been provided immediately prior to the filing of this report and have not yet been reviewed in detail by the Monitor. The Monitor will continue to review the transactions noted herein and any additional documents provided to the Monitor subsequent to the filing of this report and shall prepare a supplemental report if

such information or further review materially effects or alters the information provided herein.

DOCUMENTS REVIEWED BY MONITOR IN PREPARING THE FORTY-NINTH REPORT

21. In preparing this Forty-Ninth Report the Monitor has reviewed the following documents with respect to certain legal entities (BCHI, BCFC, BCFLP, BCFPI, BPPCI and BCI) as more fully described in this Forty-Ninth Report including but not limited to: i) audited and unaudited financial statements, ii) minutes of board of director meetings, iii) tax opinions prepared by third parties, iv) the offering circular in respect of the 7.95% Notes, v) BCFC's bank statements vi) the purchase agreement and the indenture agreement in respect of the 7.95% Notes; vii) the 7.95% Notes prospectus dated December 10, 2001 (the "**Prospectus**"); and vii) certain promissory notes evidencing intercompany balances.

TRANSACTIONS GIVING RISE TO ISSUANCE OF 7.95% NOTES

22. The following section outlines the series of transactions which resulted from the acquisition of Alliance Forest Products, Inc. ("**Alliance**") by a subsidiary of BI on September 24, 2001. The purchase of Alliance was primarily financed through a Bridge Facility (as defined later herein) and the issuance of shares of BI. The Bridge Facility was repaid from the proceeds obtained by the issuance of the 7.95% Notes. Alliance subsequently changed its name to BCFPI and, on January 1, 2002, amalgamated with Bowater Pulp and Paper Canada Inc. ("**BPPCI**"). The amalgamated entity retained the name BCFPI.

Alliance Transaction

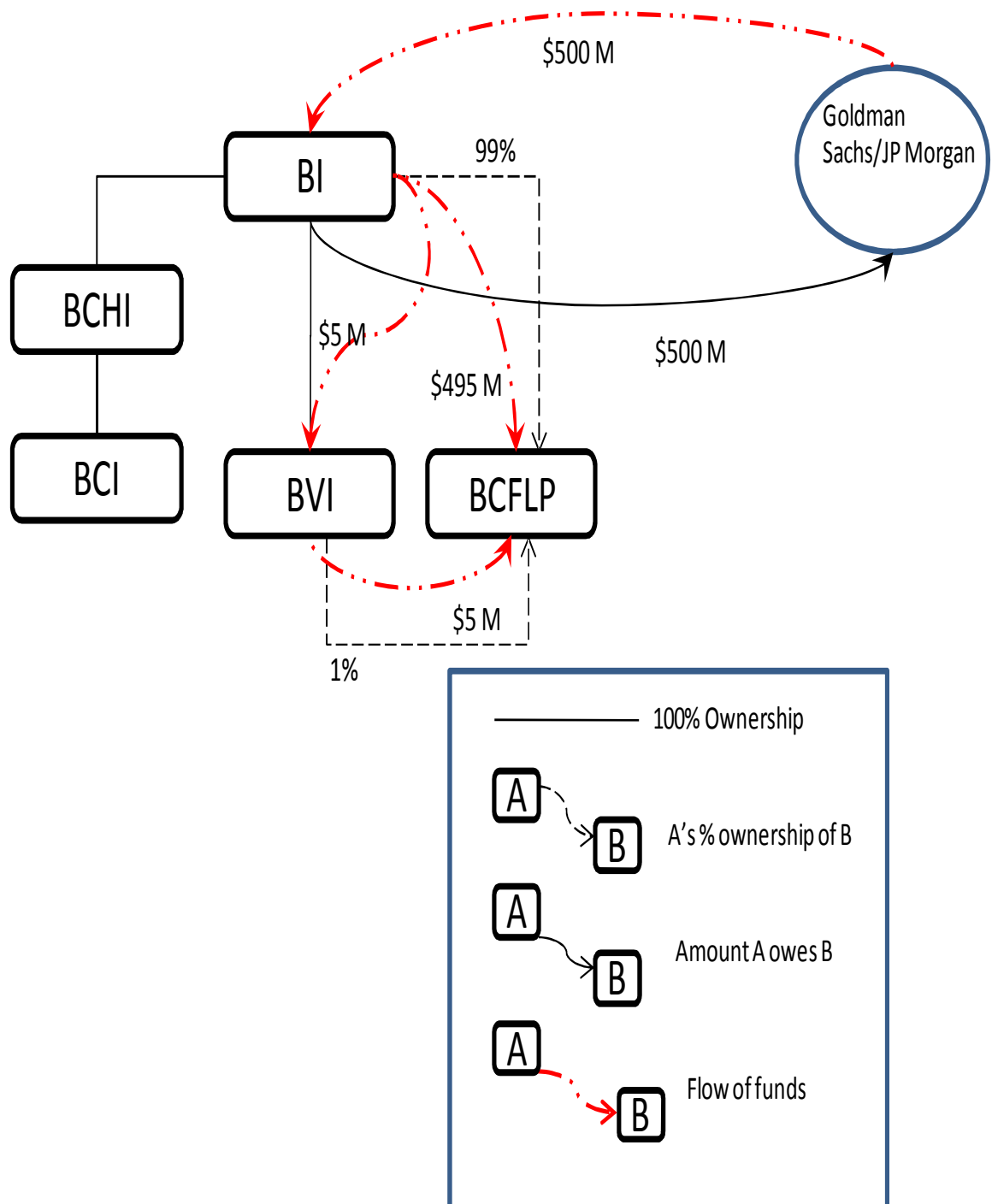
23. On April 1, 2001, BI entered into an arrangement agreement (the "**Alliance Agreement**") with Alliance, which at the time was a major Canadian forest products company, relating to a plan of arrangement pursuant to which Bowater Canada Inc. ("**BCI**"), a wholly-owned subsidiary of BCHI (which in turn is a wholly-owned subsidiary of BI), was to acquire all of the outstanding common shares of Alliance (the "**Alliance Acquisition**"). The Monitor has only recently been provided with a copy of the Alliance Agreement which has not yet been reviewed in detail by the Monitor however, the acquisition is described in detail in the Prospectus.

24. As further described in this Forty-Ninth Report, the Monitor has been advised that the Alliance Acquisition was completed on September 24, 2001 for a purchase price of approximately \$486 million (approximately \$251 million in cash and the balance in shares of BI). As part of the Alliance Acquisition, BI also loaned money to Alliance through BPPCI (a wholly-owned subsidiary of BCI) to repay approximately \$274.5 million of Alliance's outstanding third party debt (this part of the transaction is more fully described in paragraph 36). As a result, the total cash required by BI to fund the transaction was approximately \$525.5 million. The steps in respect of the purchase of Alliance are described in greater detail in the following paragraphs.

The Bridge Financing and the Flow of Funds

25. The cash component of the Alliance Acquisition and the debt repayment was principally financed by a bridge credit agreement between BI and Goldman, Sachs Credit Partners, L.P. and J.P. Morgan Securities Inc., as co-arrangers in the amount of \$500 million (the “**Bridge Facility**”). The Monitor has only recently been provided with a copy of the agreement evidencing the Bridge Facility which has not yet been reviewed in detail by the Monitor, however, the Offering Circular (as defined below) and the Prospectus makes reference to the details noted herein.
26. On September 24, 2001, the same day the Alliance acquisition closed, BI, using the proceeds from the Bridge Facility, purchased additional common shares from Bowater Ventures Inc. (“**BVI**”) for \$5 million. BVI subsequently used these funds to subscribe for general partnership units in Bowater Canada Finance Limited Partnership (“**BCFLP**”) at a cost of \$5 million, each pursuant to the subscription agreements dated September 24, 2001. BCFLP which was formed under the *Limited Partnership Act* (New Brunswick) with BVI (a wholly-owned subsidiary of BI) as the general partner and BI as the limited partner.
27. Pursuant to a subscription agreement dated September 24, 2001, BI, using the proceeds from the Bridge Facility, also subscribed for limited partnership units of BCFLP at a cost of \$495 million. As a result of these subscriptions, BCFLP had \$500 million in cash.

28. The corporate structure prior to the purchase of Alliance but as a result of the transactions described in paragraphs 25-27 in preparation for the closing of the Alliance Acquisition, was as summarized below:

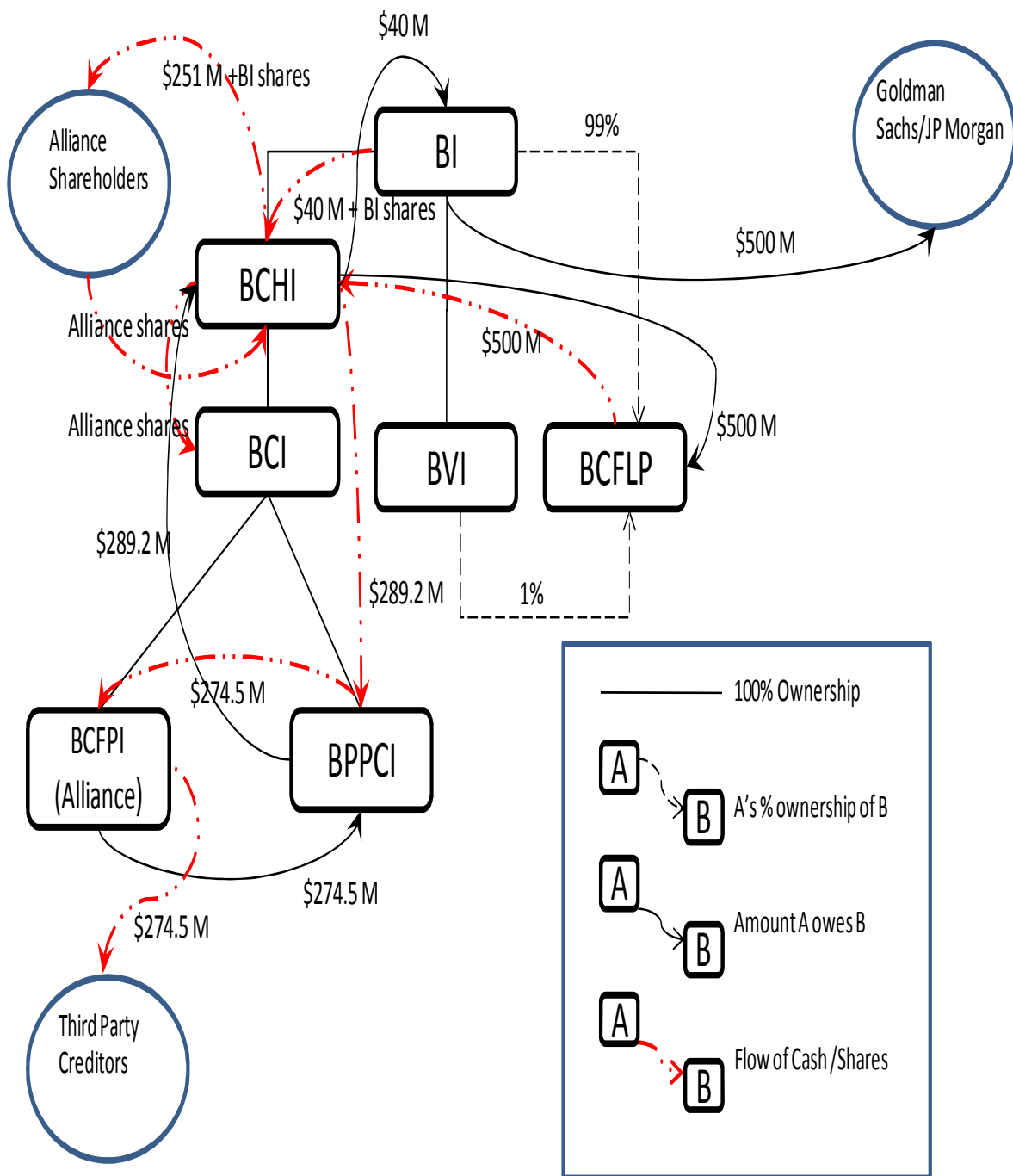


29. Alliance's name was changed to BCFPI on September 24, 2001.

Payment of Purchase Price to Alliance Stakeholders

30. The transactions in this section relate to the transfer of BI shares and the flow of funds from BCFLP to the owners of Alliance.
31. The Monitor was advised by Management that BI transferred approximately 4.2 million BI shares with a value of approximately \$173 million to BCHI in consideration for additional BCHI shares on September 21, 2001 in anticipation of the closing of the Alliance Acquisition, pursuant to a subscription agreement between BI and BCHI dated September 24, 2001.
32. As evidenced by a promissory note dated September 24, 2001, BCFLP advanced \$500 million to BCHI (the "**BCFLP/BCHI Note**"). BCHI is a non-operating subsidiary of BI. The BCFLP/BCHI Note had a maturity date of September 24, 2007 and an interest rate equal to the Floating Rate (as defined therein) plus 97.5 basis points.
33. As evidenced by a promissory note dated September 24, 2001, BCHI also borrowed approximately \$40.2 million from BI (the "**BI/BCHI Note**"). The BI/BCHI Note had a maturity date of September 24, 2007 and an interest rate equal to the Floating Rate (as defined therein) plus 97.5 basis points. The two advances (from BCFLP and BI) provided BCHI with approximately \$540 million of cash, sufficient to fund the cash payable on closing of the Alliance Acquisition.
34. The Monitor was advised by the Petitioners that on September 24, 2001, BCHI paid approximately \$251 million plus the BI shares (as noted in paragraph 31) to the Alliance shareholders through their depository agent. In return, BCHI received the shares of Alliance which were then contributed by BCHI to its wholly-owned subsidiary BCI in exchange for additional shares of BCI.
35. As evidenced by a promissory note dated September 24, 2001, BCHI also loaned approximately \$289.2 million to BPPCI (the "**BPPCI Note**"). The BPPCI Note has a stated maturity date of September 24, 2007 and an interest rate equal to the Floating Rate (as defined therein) plus 107.5 basis points.

36. As noted earlier in this Forty-Ninth Report, on September 24, 2001, BPPCI used the funds loaned from BCHI to loan approximately \$274.5 million to BCFPI (to repay certain of Alliance's outstanding debts) as evidenced by a promissory note dated September 24, 2001 (the "**BCFPI Note**"). The BCFPI Note has a stated maturity date of September 24, 2007 and an interest rate equal to the Floating Rate (as defined therein) plus 117.5 basis points.
37. The change in the corporate structure, as a result of the transactions described in paragraphs 31-36, was as summarized below:



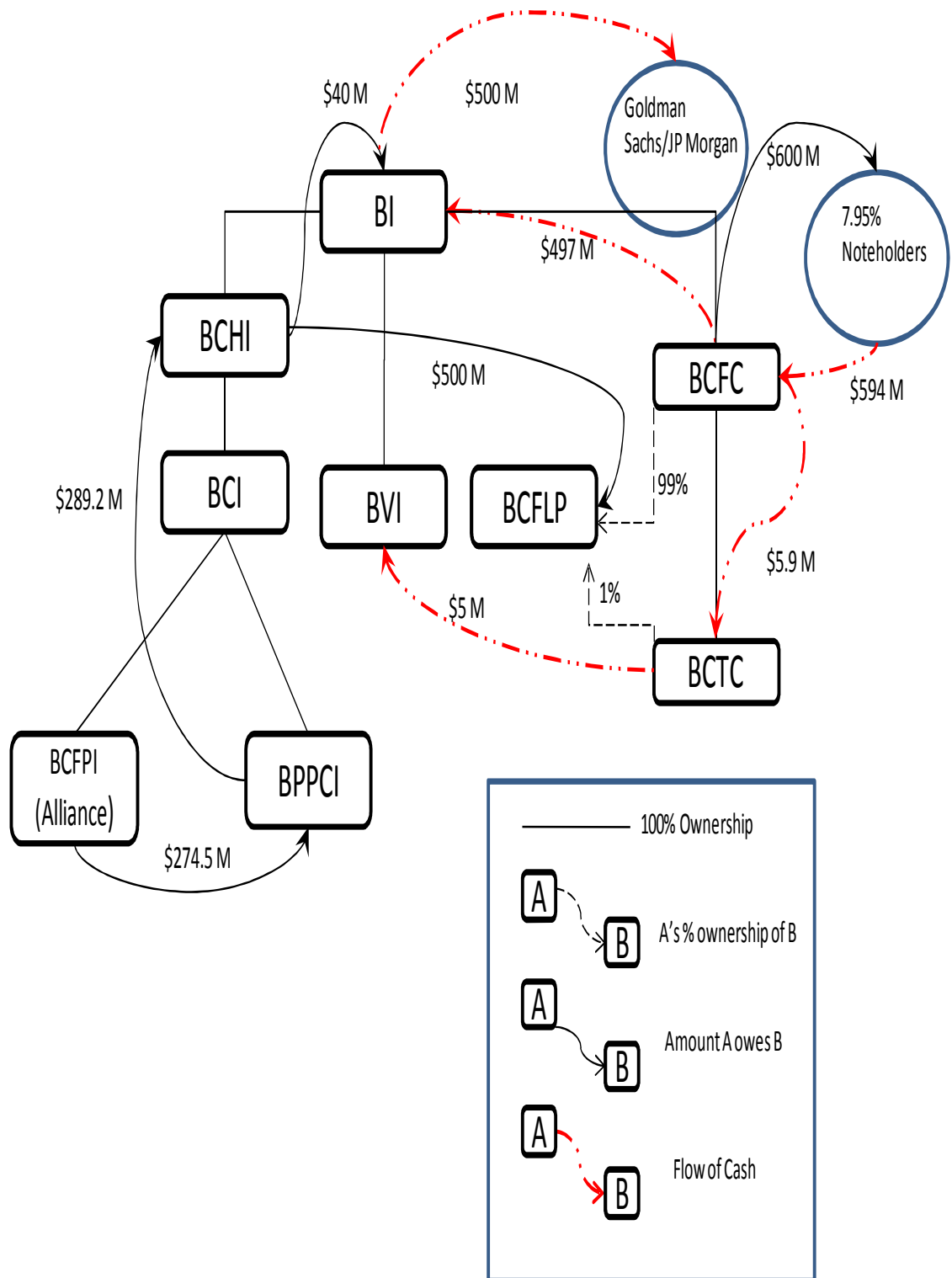
Creation of BCFC and Issuance of the 7.95% Notes

38. BCFC is an unlimited liability company organized under the laws of the Province of Nova Scotia and was incorporated on October 19, 2001. The Monitor was advised by the Petitioners that BCFC is non-operating company and a wholly-owned subsidiary of BI.
39. On October 31, 2001, pursuant to an indenture agreement and a purchase agreement, each dated October 31, 2001 (collectively, the “**7.95% Note Agreements**”), BCFC issued and sold the 7.95% Notes with a face value of \$600 million and with a maturity date of November 15, 2011. The Monitor was advised by the Petitioners that the 7.95% Notes, which yielded net proceeds of \$594.2 million (\$600 million less discounts and underwriters’ fees) are fully and unconditionally guaranteed by BI. The offering was structured, as described later herein, such that the proceeds would be used by BI to repay the Bridge Facility incurred in respect of the Alliance Acquisition.
40. Interest on the Notes was payable on May 15 and November 15 of each year commencing on May 15, 2002. As evidenced by the Minutes of the Board of Directors of BCFC for the years 2006 to 2009, BI funded the interest payments on the Notes until the date of the Petition through equity injections into BCFC. The BCFC bank statements for the period May 1, 2006 to April 30, 2009 show receipts from BI and payments to an account at the Bank of New York, both in the amount of approximately \$23.9 million on May 15th and November 15th prior to the CCAA filing.
41. BCFC, through its offering circular dated October 31, 2001 (the “**Offering Circular**”), advised potential investors that the 7.95% Notes would be BCFC’s senior obligations and would rank equally with other senior unsecured debt of BCFC, if any. The Offering Circular advised investors that BI’s guarantee of the 7.95% Notes would rank equally with BI’s other senior unsecured debt which totalled \$1.8 billion as at September 30, 2001.
42. The Offering Circular also advised potential investors that i) BCFC and its wholly-owned non-operating subsidiary Bowater Canada Treasury Corporation (“**BCTC**”) would use the proceeds from the 7.95% Notes to acquire BCFLP from BI and BVI, respectively; ii) BCFLP was formed to facilitate the financing of the Alliance Acquisition and to recapitalize BCHI and BCI; and iii) BI and BVI would use the proceeds from the sale of BCFLP to repay all

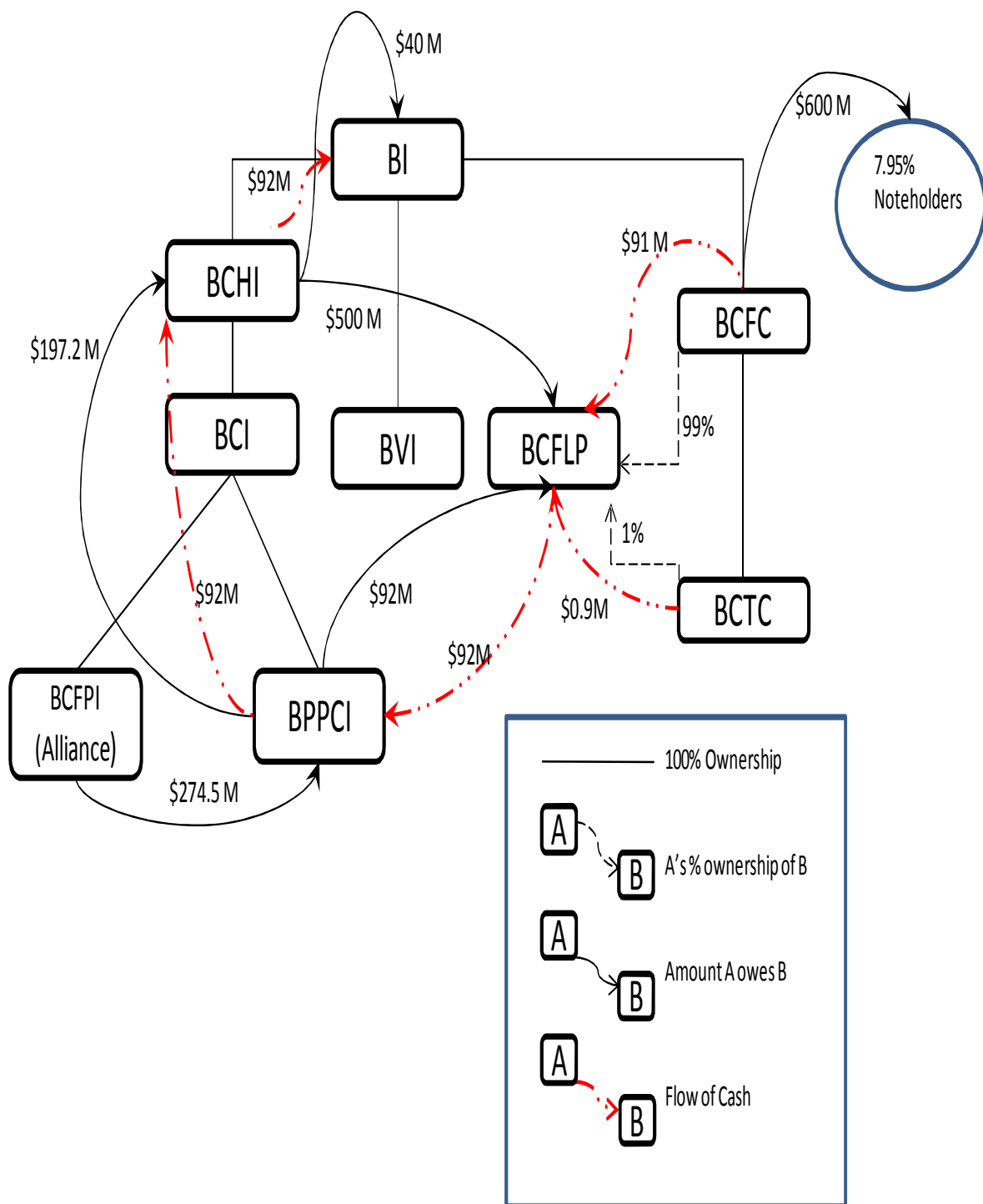
amounts outstanding under the Bridge Facility and to repay other short-term borrowings of BI.

Use of the Proceeds from the 7.95% Notes

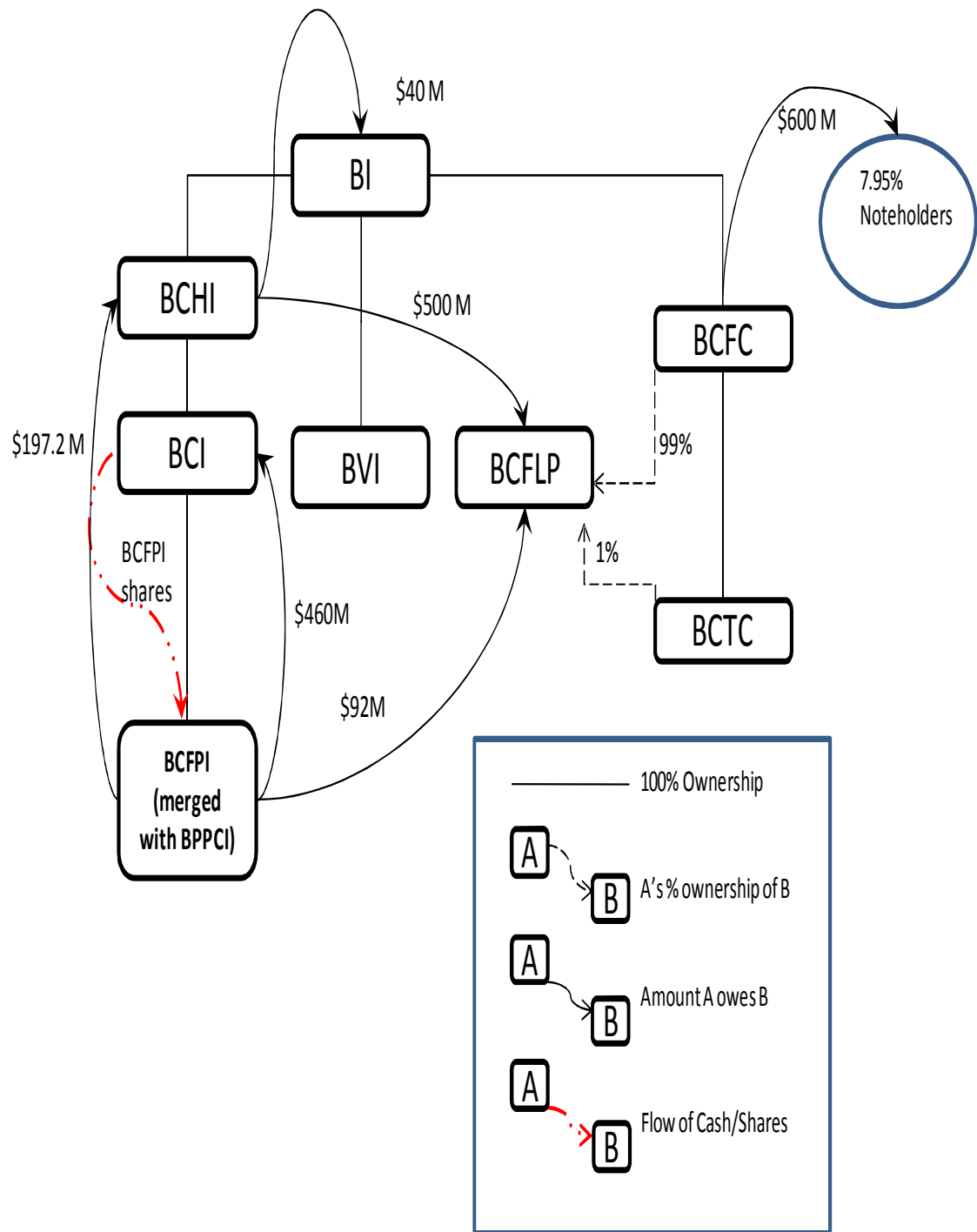
43. Pursuant to a subscription agreement dated November 6, 2001, BCFC used approximately \$5.9 million of the proceeds from the issuance of the 7.95% Notes to purchase shares of BCTC. Pursuant to a transfer agreement of the same date, BCTC used these funds to acquire 1% of BCFLP from BVI for approximately \$5 million.
44. On November 9, 2001, BCFC used certain of the proceeds from the 7.95% Notes to acquire 99% of BCFLP from BI for approximately \$497.2 million, pursuant to a transfer agreement. BI used these funds to repay the Bridge Facility in accordance with an extraordinary resolution of the shareholders dated November 6, 2001.
45. The change in the corporate structure, as a result of the transactions described in paragraphs 39, 43 and 44, was as summarized below:



46. On November 6, 2001, BCTC subscribed for additional units of BCFLP for \$0.9 million as evidenced by the subscription agreement between BCTC and BCFLP dated November 6, 2001.
47. On the same date, BCFC paid \$91 million to BCFLP to subscribe for additional units of BCFLP as evidenced by the subscription agreement between BCFC and BCFLP dated November 6, 2001.
48. On November 6, 2001, upon receipt of funds from BCFC and BCTC, BCFLP loaned approximately \$92 million to BPPCI as evidenced by a promissory note dated November 6, 2001 (the “**BCFLP/BPPCI Note**”). The BCFLP/BPPCI Note has a stated maturity date of November 15, 2011 and an interest rate of 8.05% per annum.
49. BPPCI used those funds to make a partial prepayment in the amount of approximately \$92 million in respect of its intercompany indebtedness to BCHI pursuant to the BPPCI Note. As a result of this partial prepayment, BPPCI issued to BCHI, an amended and restated promissory note in the amount of \$197.2 million with a stated maturity date of November 15, 2011 and an interest rate equal to 8.15% per annum.
50. BCHI loaned the funds received from BPPCI to BI in exchange for a promissory note issued by BI in the amount of approximately \$92 million dated November 6, 2001 (the “**BI/BCHI Note**”). The BI/BCHI Note has a stated maturity date of November 15, 2011 and an interest rate of 8.25% per annum. The BI/BCHI Note was subsequently distributed to BI as part of a reduction of paid-up capital.
51. The change in the corporate structure, as a result of the transactions described in paragraphs 46-50, was as summarized below:



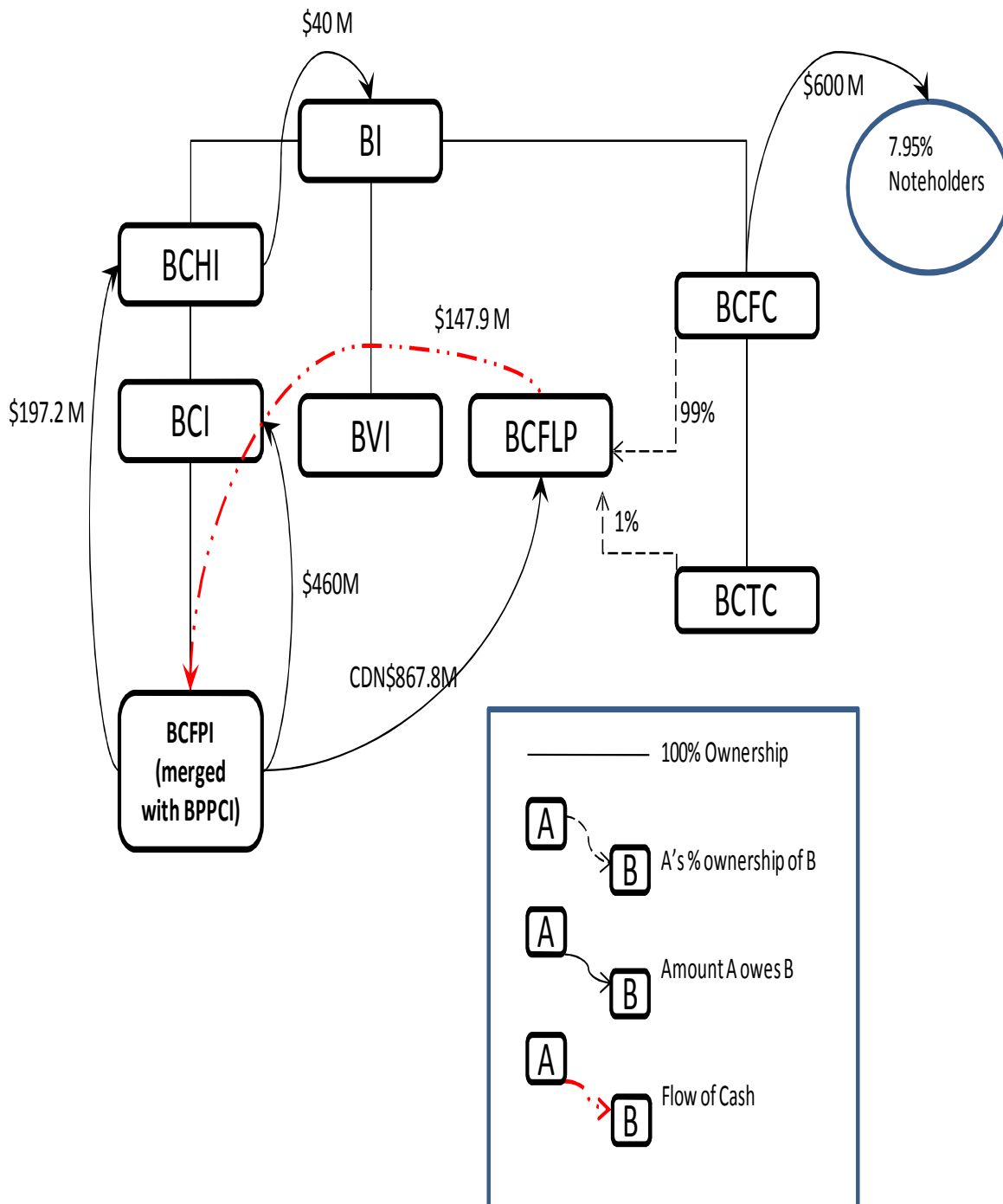
52. Pursuant to a share transfer agreement dated November 30, 2001, BPPCI purchased all of the issued and outstanding common shares of BCFPI from BCI in exchange for 100 common shares of BPPCI and notes in the principal amounts of \$81.5 million and \$343 million and a further note equal to the Alliance Amounts (as defined in the share transfer agreement), being \$35.5 million. In summary, the total consideration paid was 100 common shares of BPPCI and \$460 million in notes payable to BCI in exchange for the BCFPI shares.
53. Pursuant to an amalgamation agreement, BPPCI amalgamated with BCFPI effective as of January 1, 2002. The amalgamated entity retained the name BCFPI. As a result of the merger, the intercompany loan between BCFPI and BPPCI was eliminated but the debt owing by BPPCI to BCFLP (\$92 million) remained.
54. As a result of the transactions described in paragraphs 52 and 53 and after the amalgamation of BPPCI and BCFPI on January 1, 2002, the corporate structure as a result of these transactions was as described below:



55. The Monitor notes that Ernst & Young's U.S. affiliate ("EY LLP") was engaged by BI to provide tax consulting services. The Monitor has been advised by EY U.S. LLP that the services provided involved the issuance of opinions on January 16, 2002 with respect to the tax consequences relating to the cross-border structure utilized to finance the purchase of Alliance. The opinions rendered by EY U.S. LLP were delivered after the purchase of Alliance was completed.

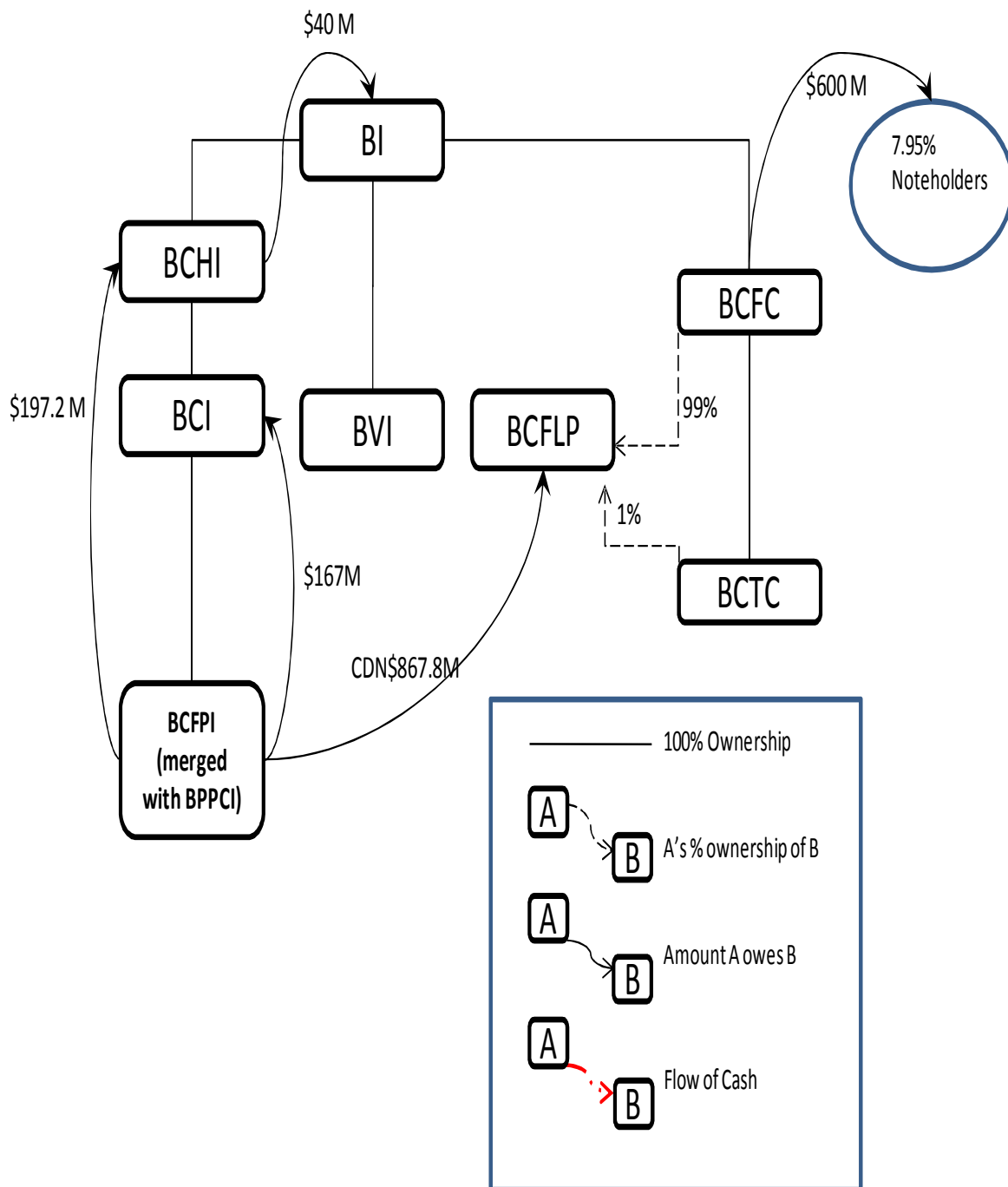
Funding of BCFPI

56. The BCFLP/BCHI Note was transferred to BCFPI with the approval of BCFLP, and, as such, BCFPI assumed responsibility for the \$500 million BCFLP/BCHI Note previously payable by BCHI.
57. The following transactions are documented in the resolution of the partners of BCFLP dated November 9, 2005. The Monitor has not been provided with any additional documents in respect of these advances and has not traced the original source of the funds so advanced.
58. On June 28, 2002, BCFLP advanced an additional \$33.2 million to BCFPI and a further \$33.3 million on December 17, 2002.
59. On June 30, 2003, BCFLP advanced an additional \$26.1 million to BCFPI and a further \$27.1 million on December 30, 2003. On June 30, 2004, BCFLP advanced an additional \$28.2 million to BCFPI.
60. In summary, while the Monitor has not yet traced the source of these advances, after these advances totalling \$147.9 million and the transfer of the BCFLP/BCHI Note, BCFPI was indebted to BCFLP in the approximate amount of \$739.9 million. On November 9, 2005, these amounts were converted to Canadian dollars on the books of BCFLP in the approximate amount of CDN\$867.8 million.
61. As a result of the transactions described in paragraphs 56 to 60, the corporate structure as a result of these transactions was as described below:



Sale of Accounts Receivable to BCI

62. On November 30, 2001, BCFPI sold approximately \$293 million of accounts receivable from Bowater Alabama to BCI in exchange for a note. This note was later used to offset the notes owing to BCI such that the remaining debt to BCI was approximately \$167 million.
63. The change in the corporate structure, as a result of the transactions described in paragraph 62, was as summarized below:

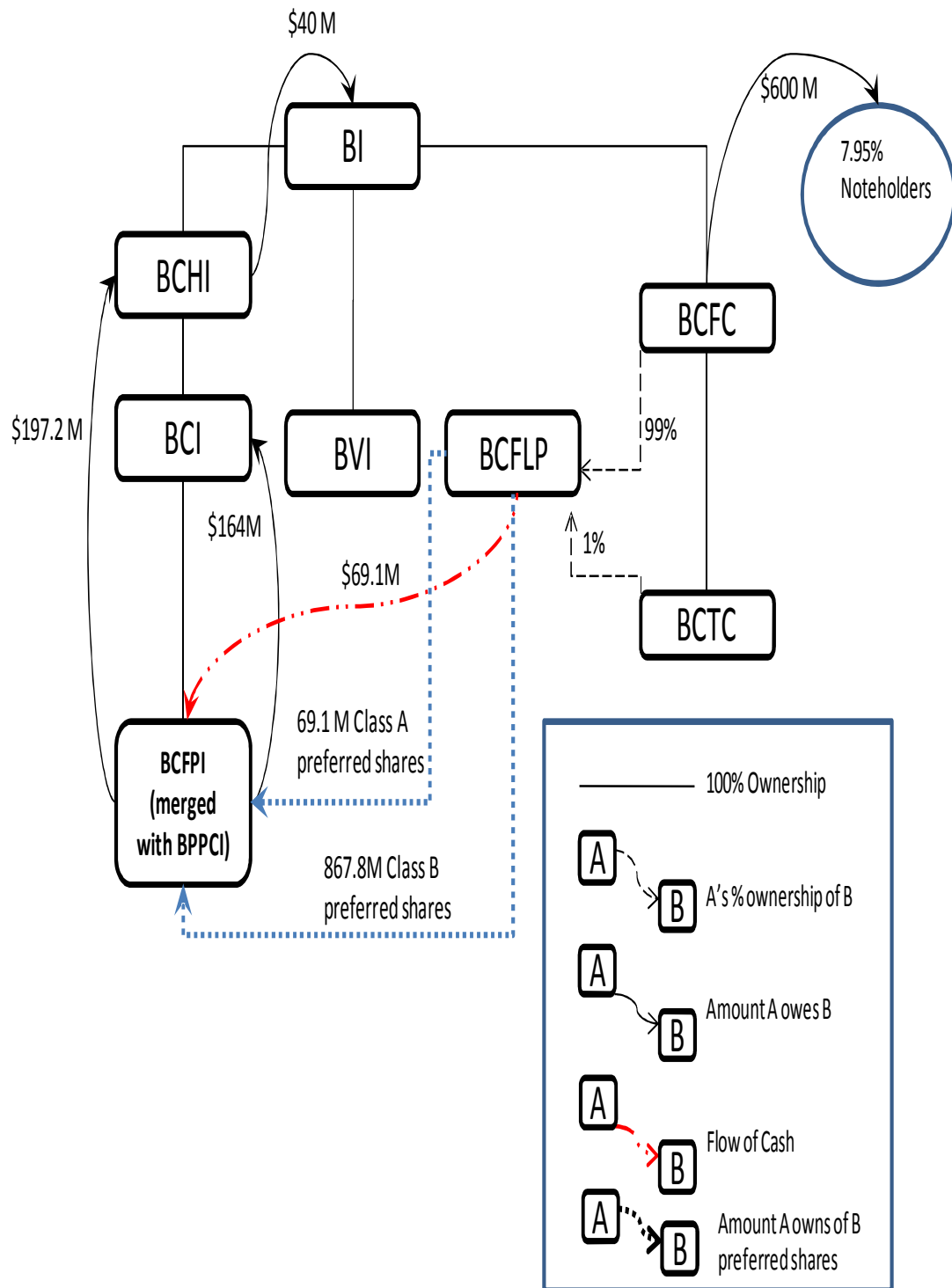


INTERCOMPANY TRANSACTIONS IN THE THREE YEAR PERIOD PRIOR TO INITIAL ORDER

64. The Monitor has reviewed the significant intercompany transactions involving BCFC during the three year period preceding the Petition. The Monitor has also reviewed other material non-trade intercompany transactions that have impacted BCFC.

BCFLP Equity Conversion

65. As evidenced by the Resolution of the Board of Directors of BCFPI, on June 30, 2005, BCFLP purchased 36.2 million Class A preferred shares of BCFPI. On December 23, 2005, \$731 million (Cdn\$867.8 million) of long-term advances (as described in paragraph 60 above) owed to BCFLP by BCFPI were cancelled in exchange for the issuance of 867.8 million Class B preferred shares of BCFPI.
66. As evidenced by the Resolution of the Board of Directors of BCFPI, on December 30, 2005, BCFLP purchased an additional \$32.87 million worth of Class A preferred shares of BCFPI. In total, BCFLP purchased \$69.1 million of Class A preferred shares of BCFPI. The Monitor has not yet traced the original source of the funds used to purchase these shares.
67. The change in the corporate structure, as a result of the transactions described in paragraphs 65-66, was as summarized below:



68. The audited financial statements for BCFPI for the year ended December 31, 2005 also show a liability of approximately CDN\$640 million owing to BI in respect of advances from BI to BCFPI. The Monitor understands these advances were under a grid note from BI that funded BCFPI's working capital and cash flow requirements. This amount is not included in the chart above.

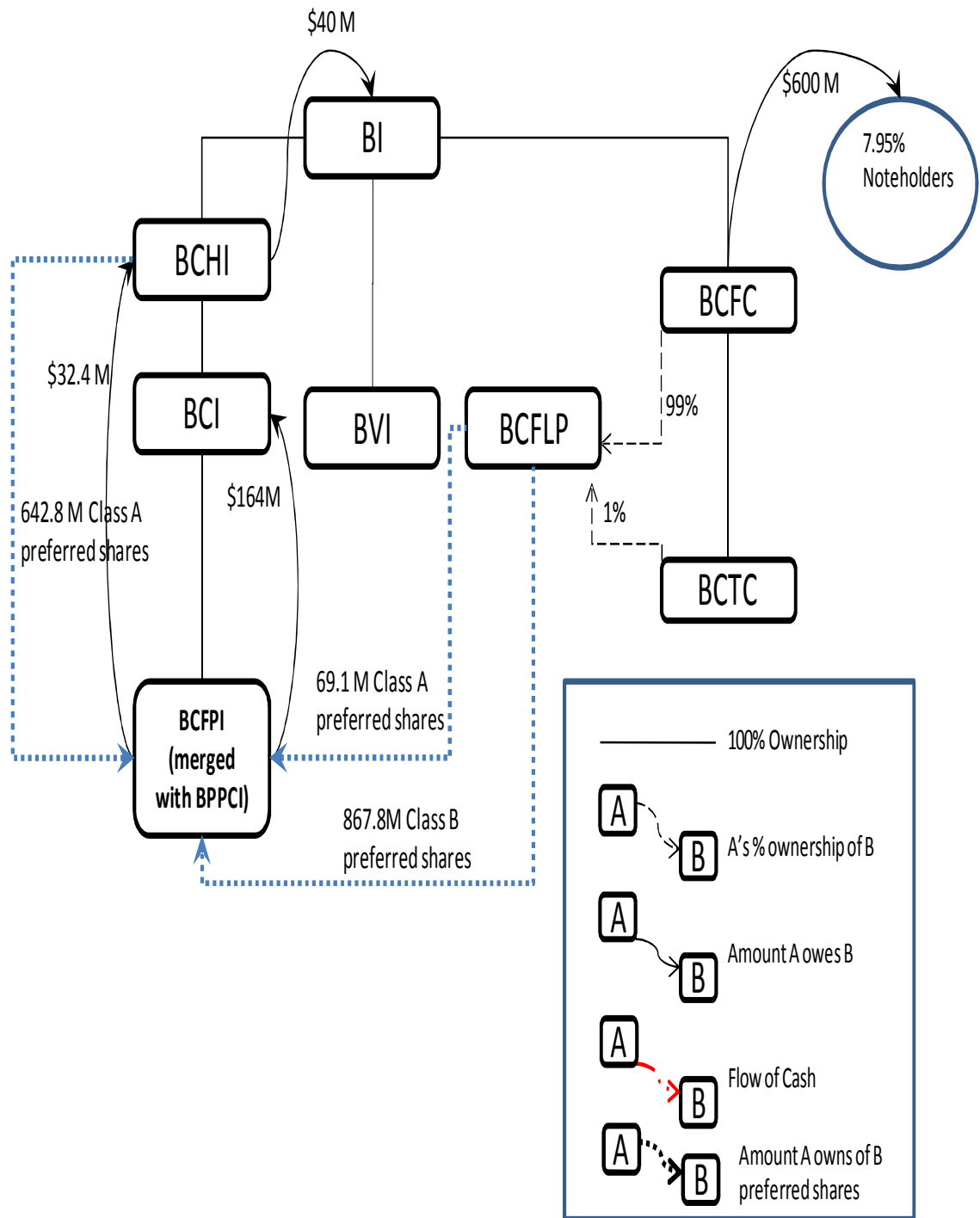
Impact of BCFLP Equity Conversion

69. BCFC's most significant asset, at the time of the transactions described in paragraphs 69 and 70, was its ownership of BCFLP. BCFLP was a creditor of BCFPI (operating entity) prior to the conversion of the obligations owed by BCFPI to BCFLP to preferred shares. Therefore, the Monitor examined the financial statements of BCFPI to determine the impact of the conversion of BCFPI debt to preferred shares of BCFPI. For reference, attached as Appendix "F" are the annual financial statements for BCFPI for the year ending December 31, 2005.
70. For the year ended December 31, 2004, the audited financial statements for BPPCI (which includes the consolidated results of BCFPI) indicated a net book value (assets less liabilities) of approximately CDN\$300 million. The publicly available audited financial statements for BCFPI, a reporting issuer, for the year ended December 31, 2005 indicate that BCFPI had losses for the year of approximately CDN\$352 million and a net book value (assets less liabilities) of approximately CDN\$882 million as at December 31, 2005, after the debt to preferred shares conversion.

BCHI/BCFPI Recapitalization

71. On February 28, 2006, BI transferred an intercompany receivable from BCFPI to BCHI in the amount of \$400 million (referred to in paragraph 68 but not included in the preceding chart) in exchange for common shares of BCHI. As a result, BCFPI owed approximately \$400 million to BCHI as opposed to BI. These advances were contemporaneously cancelled in exchange for the issuance of 455.2 million Class A preferred shares of BCFPI to BCHI.
72. In addition, notes totalling approximately \$164.8 million of the \$197.2 owing to BCHI by BCFPI were also cancelled by BCHI in exchange for approximately 187.6 million Class A preferred shares of BCFPI, leaving a net intercompany payable of \$32.4 million.

73. These transactions resulted in the conversion of notes and advances owed to affiliates by BCFPI totalling \$564.8 million to approximately 642.8 million Class A preferred shares of BCFPI.
74. The change in the corporate structure, as a result of the transactions described in paragraphs 71-73, was as summarized below:



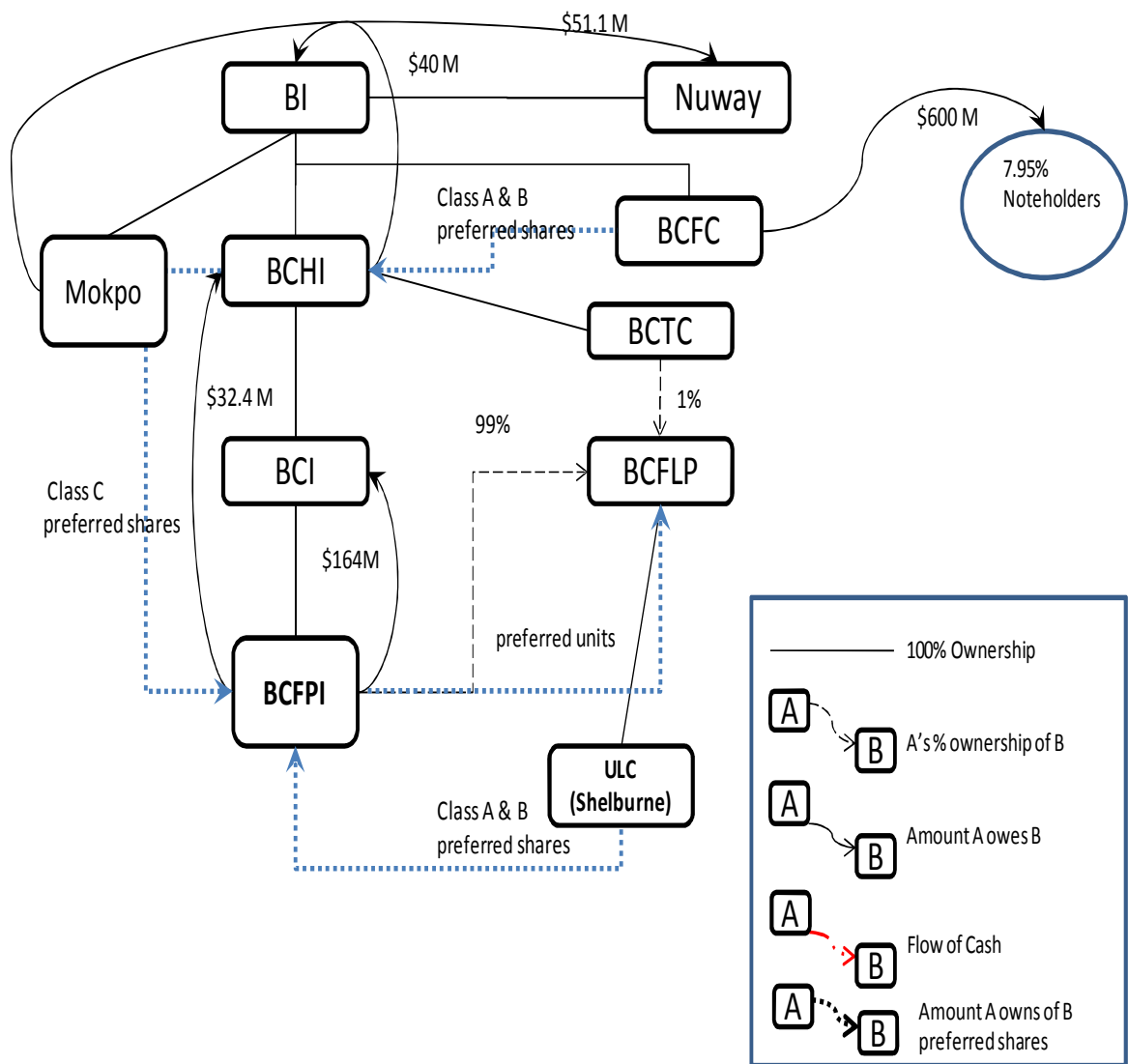
75. The effect of these transactions was to strengthen BCFPI's balance sheet. For the year ended December 31, 2006, BCFPI had a net loss of \$51 million (according to the audited financial statements) and a net book value (assets less liabilities) of approximately \$1,477 million which was primarily due to the conversion of the \$867.8 million owing to BCFLP and \$564.8 million owing to BCHI (total debt of \$1,432.6 million) into preferred shares as noted above.

MOKPO

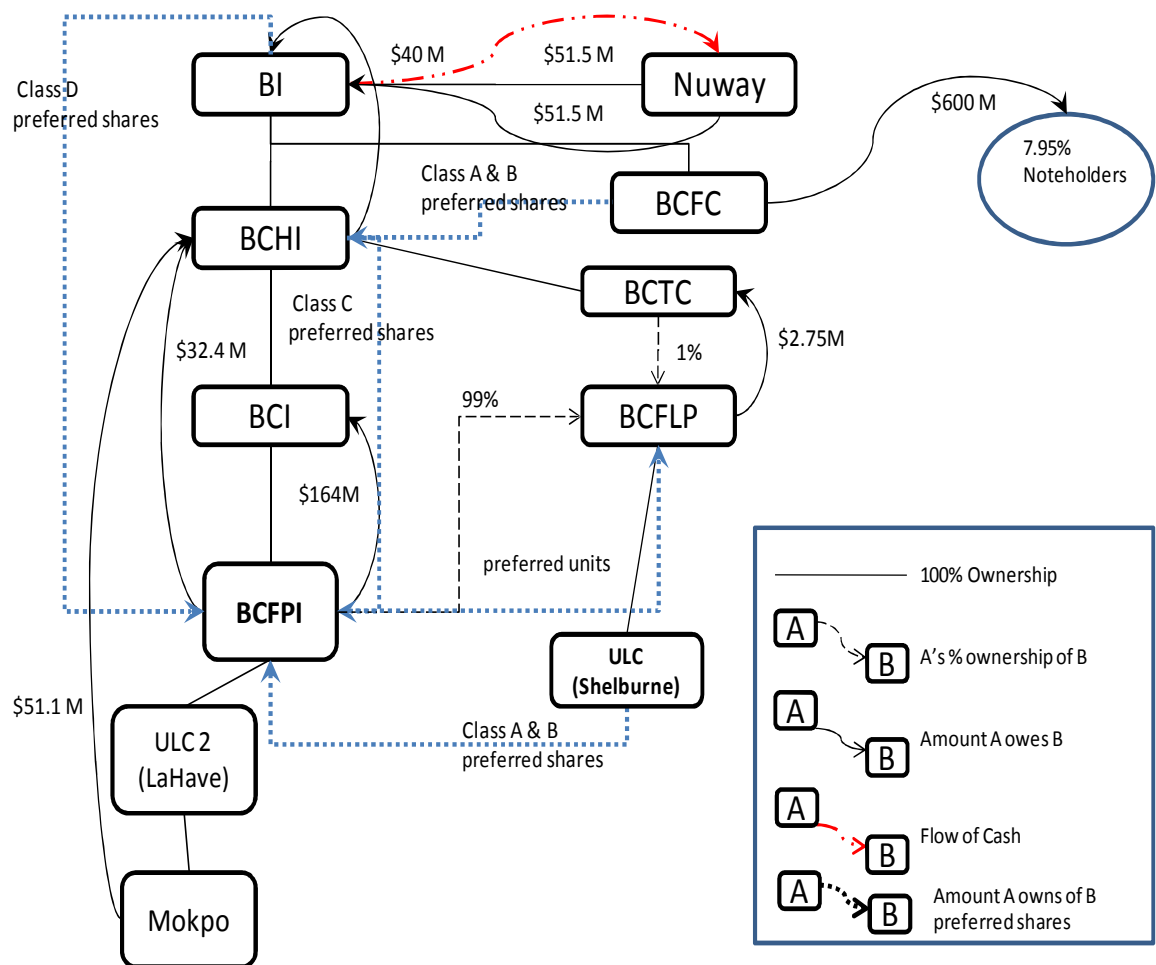
76. The effect of the following transactions was the transfer of Bowater-Korea Ltd. ("**Mokpo**") a wholly-owned subsidiary of BI (a U.S. company) to BCFPI (a Canadian company) in order to benefit from lower corporate tax rates in Canada for foreign subsidiaries.
77. Prior to 2007, Mokpo was a wholly-owned subsidiary of BI which operated a paper mill and recycling plant in Mokpo, South Korea. Mokpo was indebted to Bowater Nuway Inc. ("**Nuway**"), a wholly-owned subsidiary of BI, in respect of a bond in the amount of \$51.5 million. The Petitioners have not yet located a copy of the bond indenture for the Monitor's review, but reference was made to same in an early repayment agreement dated January 9, 2007.
78. In January 2007, ownership of Mokpo was transferred to BCFPI through a series of transactions (the "**Mokpo Transaction**").
79. Prior to the Mokpo Transaction, BCTC was a wholly-owned subsidiary of BCFC. BCFC and BCTC together owned 100% of the partnership units of BCFLP. According to BCFLP's financial statements for the year ended December 31, 2006, BCFLP listed as assets an interest receivable in the amount of \$290,000 and also Class A and Class B preferred shares of BCFPI.
80. While BCTC retained its 1% interest in the partnership units of BCFLP, BCFC contributed its limited partnership units of BCFLP to BCHI in exchange for Class A voting preferred shares of BCHI, pursuant to a transfer agreement dated January 19, 2007.
81. BCFLP created a Nova Scotia unlimited liability company named Bowater Shelburne Corporation ("**Shelburne**") and, pursuant to a transfer agreement dated January 19, 2007, transferred its Class A and Class B preferred shares in BCFPI to Shelburne in exchange for

member units of Shelburne. As a result, BCFLP no longer directly owned the preferred shares of BCFPI.

82. BCFPI was changed from a corporation incorporated under the *Canada Business Corporations Act* into a Nova Scotia corporation. Pursuant to a transfer agreement dated January 19, 2007, BCFPI then acquired the limited partnership units of BCFLP from BCHI (formerly owned by BCFC) in exchange for Class C preferred shares of BCFPI.
83. As evidenced by a transfer agreement dated January 19, 2007, BCFC contributed its holdings in BCTC to BCHI in return for a stated equivalent fair market value amount (\$10.5 million), as determined by BCFC and BCHI, of Class B preferred shares of BCHI. As a result, the primary asset retained by BCFC was the preferred shares of BCHI.
84. As evidenced by the Resolution of the General Partner of BCFLP, BCFLP (now a wholly-owned subsidiary of BCFPI) distributed \$375 million to BCFPI and BCTC (the “**Distribution**”) on a pro-rata basis by way of a return of a portion of their respective capital contributions. The Distribution owing to BCFPI was satisfied by the issuance of preferred return partnership units by BCFLP to BCFPI. The Distribution owing to BCTC (one percent (1%)) was satisfied by payment of \$1 million and a \$2.75 million note issued by BCFLP to BCTC (the “**BCFLP Note**”). The BCFLP Note had an interest rate of 7.5% and was payable within one year from the date of issuance.
85. The change in the corporate structure, as a result of the transactions described in paragraphs 80-84, was as summarized below:



86. BI loaned \$51.5 million to Nuway in exchange for a promissory note. Pursuant to a note subscription agreement dated January 19, 2007, Nuway agreed to loan those funds to Mokpo in exchange for a promissory note dated January 19, 2007 (the “**Mokpo Note**”). This loan was in addition to the existing \$51.5 million bond owed by Mokpo previously outstanding in favour of Nuway. Mokpo used these funds to retire the bond outstanding to Nuway. Nuway then used those funds to repay the loan initially granted by BI. As a result, the bond formerly payable by Mokpo to Nuway was replaced by the Mokpo Note.
87. BI incorporated a new Nova Scotia unlimited liability company named Bowater LaHave Corporation (“**LaHave**”) and transferred its shares in Mokpo to LaHave, pursuant to a transfer agreement dated January 19, 2007, in exchange for member units of LaHave. Pursuant to a transfer agreement dated January 19, 2007, BI then contributed its interest in LaHave to BCFPI in exchange for Class D preferred shares of BCFPI.
88. Nuway declared a dividend in the amount of \$51.1 million to BI as the holder of its common shares. The dividend was satisfied by Nuway’s contribution to BI of the receivable owing in respect of the Mokpo Note. Pursuant to a transfer agreement dated February 15, 2007, BI then contributed this receivable to BCHI in return for 1.9 million additional common shares of BCHI. As a result, BCHI obtained the Mokpo Note payable by Mokpo in the amount of \$51.5 million in return for the issuance of common shares of BCHI.
89. The change in the corporate structure, as a result of the all of the transactions described in paragraphs 80-88, was as summarized below:



90. BCFC's indirect interest in BCFPI was originally through the preferred shares of BCFPI held by BCFLP and now is through its preferred holdings in BCHI. In addition, the value of BCFPI was increased through this transaction by the addition of Mokpo. According to the BCFPI quarterly financial statements for the three months ending March 31, 2007, Mokpo had a net book value (assets less liabilities) of approximately \$200 million at that time.

BCFC BALANCE SHEETS

91. The Monitor was provided with the balance sheets for BCFC as at March 31, 2009 and for as at December 31, 2008 which are summarized in the table below:

(\$000's)	As at March 31, 2009	As at December 31, 2008
ASSETS		
Current assets:		
Cash	1	2
Deferred Financing Expense	1,246	1,364
Investment in Subsidiary - BCHI	818,916	818,916
Total Assets	820,163	820,282
LIABILITIES AND SHAREHOLDERS' EQUITY		
Accrued Interest	17,874	5,949
Accounts Payable Affiliate	121,626	121,638
Long Term Debt, Net of Current Installments	599,536	599,490
Long Term Tax Liability	8,315	8,477
Total Liabilities	747,351	735,554
Shareholders' equity:		
Capital Stock	214,650	214,650
Retained Earnings:		
Prior Year Retained Earnings	(129,922)	(99,483)
Prior Year Retained Earnings - Affiliates	-	
Current Year Retained Earnings	(11,916)	(30,439)
Total Retained Earnings	(141,838)	(129,922)
Total Equity	72,812	84,728
Total Liabilities and Shareholders' Equity	820,163	820,282

92. As can be seen in the table above, the primary asset of BCFC is its investment in BCHI. BCHI is the indirect owner of the common shares of BCFPI (through its ownership of BCI and through its ownership of Class A and C preferred shares of BCFPI) and is also the owner of the Mokpo Note. BCHI is also indebted to Bowater Pulp and Paper Canada Holdings Limited Partnership, a limited partnership under the laws of New Brunswick, with BVI as the general partner with a 1% interest and BI as the limited partner with a 99% interest, pursuant

to a promissory note dated December 31, 2001 in the principal amount of \$82 million which has been accruing interest at 8.05% per annum.

93. As noted herein, this Forty-Ninth Report is an interim report and prepared on an expedited basis by reviewing the information provided to the Monitor up to the time of writing. In the event that the Monitor is subsequently provided with additional information, it will provide a supplemental report if such information materially effects or alters the information provided herein.

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

John Barrett, CA, CIRP
Senior Vice President

Greg Adams, CA, CIRP
Senior 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 Québec 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. Canixel Hardboard Inc.
13. 9068-9050 Québec 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

APPENDIX “E”
GLOSSORY OF DEFINED LEGAL ENTITIES

ABH – AbitibiBowater Inc.

ABUSH – AbitibiBowater US Holding LLC

ACI - Abitibi-Consolidated Inc.

Alliance – Alliance Forest Products, Inc.

BCFC- Bowater Canada Finance Corporation

BCFLP – Bowater Canada Finance Limited Partnership

BCFPI – Bowater Canadian Forest Products Inc.

BCHI - Bowater Canadian Holdings Incorporated

BCI – Bowater Canada Inc.

BCTC – Bowater Canada Treasury Corporation

BI - Bowater Inc.

BPPCI – Bowater Pulp and Paper Canada Inc.

BVI – Bowater Ventures Inc.

Mokpo – Bowater-Korea Ltd.

Newsprint South – Bowater Newsprint South LLC

APPENDIX “F”
2004 & 2005 Financial Statements for BCFPI



Consolidated Financial Statements of

BOWATER CANADIAN FOREST PRODUCTS INC.

Years ended December 31, 2005 and 2004



KPMG LLP
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AUDITORS' REPORT

To the Shareholder of
Bowater Canadian Forest Products Inc.

We have audited the consolidated balance sheets of Bowater Canadian Forest Products Inc. as at December 31, 2005 and 2004 and the consolidated statements of operations, deficit and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Montréal, Canada

March 7, 2006, except for note 23 which is
dated April 21, 2006

BOWATER CANADIAN FOREST PRODUCTS INC.

Consolidated Financial Statements

Years ended December 31, 2005 and 2004

Financial Statements

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Consolidated Statements of Deficit	4
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BOWATER CANADIAN FOREST PRODUCTS INC.

Consolidated Balance Sheets

December 31, 2005 and 2004
(in millions of dollars)

	2005	2004
Assets		
Current assets:		
Accounts receivable:		
Trade	\$ 77.1	\$ 53.1
Other	60.2	56.3
Affiliates	220.2	219.0
Income and other taxes receivable	3.8	5.3
Inventories (note 7)	214.1	196.5
Assets held for sale (note 8)	4.6	—
Prepaid expenses	4.6	5.2
	584.6	535.4
Future income taxes (note 6)	—	40.8
Advances to affiliates (note 9)	350.3	437.2
Assets held for sale (note 8)	17.4	—
Capital assets (note 10)	1,369.8	1,567.0
Other assets (note 11)	145.3	113.7
Goodwill	5.9	6.4
	\$ 2,473.3	\$ 2,700.5

	2005	2004
Liabilities and Shareholder's Equity		
Current liabilities:		
Bank overdraft	\$ 17.1	\$ 13.5
Bank indebtedness (note 12)	—	1.5
Accounts payable and accrued charges	247.4	239.9
Current portion of long-term debt (note 14)	15.9	15.0
	280.4	269.9
Future income taxes (note 6)	7.5	26.1
Advances from affiliates (note 13)	857.8	1,616.5
Long-term debt, net of current portion (note 14)	389.8	416.9
Other liabilities	45.4	50.2
Non-controlling interest	10.1	22.4
	1,591.0	2,402.0
Shareholder's equity:		
Capital stock (note 15)	1,932.4	995.4
Paid-in surplus	565.5	565.5
Deficit	(1,615.6)	(1,262.4)
	882.3	298.5
Commitments and contingencies (note 18)		
Subsequent events (note 23)		
	\$ 2,473.3	\$ 2,700.5

See accompanying notes to consolidated financial statements.

On behalf of the Board of Directors,

/S/ William G. Harvey

BOWATER CANADIAN FOREST PRODUCTS INC.

Consolidated Statements of Operations

Years ended December 31, 2005 and 2004
(in millions of dollars)

	2005	2004
Sales (note 16)	\$ 1,764.9	\$ 1,770.6
Cost of sales	1,494.9	1,434.9
Amortization of capital assets	160.3	159.1
Distribution costs	208.8	214.8
Selling and administrative expenses (note 16)	64.3	62.7
Impairment of assets (note 2)	57.7	—
	1,986.0	1,871.5
Operating loss	(221.1)	(100.9)
Interest expense, net (note 4)	(150.6)	(147.3)
Other income (note 5)	19.2	68.3
Loss before income taxes and non-controlling interest	(352.5)	(179.9)
Provision for income tax expense (benefit) (note 6)	11.6	(76.8)
Loss before non-controlling interest	(364.1)	(103.1)
Non-controlling interest	12.3	7.1
Net loss	\$ (351.8)	\$ (96.0)

See accompanying notes to consolidated financial statements.

BOWATER CANADIAN FOREST PRODUCTS INC.

Consolidated Statements of Deficit

Years ended December 31, 2005 and 2004
(in millions of dollars)

	2005	2004
Deficit, beginning of year, as previously reported	\$ (1,262.4)	\$ (1,164.8)
Net loss	(351.8)	(96.0)
Dividends declared	(1.4)	(1.6)
Deficit, end of year	\$ (1,615.6)	\$ (1,262.4)

See accompanying notes to consolidated financial statements.

BOWATER CANADIAN FOREST PRODUCTS INC.

Consolidated Statements of Cash Flows

Years ended December 31, 2005 and 2004

(in millions of dollars)

	2005	2004
Cash flows from operating activities:		
Net loss	\$ (351.8)	\$ (96.0)
Adjustments for:		
Amortization of capital assets	160.3	159.1
Amortization of other assets	0.2	0.4
Future income taxes	6.1	(86.0)
Non-controlling interest	(12.3)	(7.1)
Gain on disposal of capital assets	(8.3)	(5.6)
Impairment of assets (note 2)	57.7	—
Unrealized exchange gain on long-term monetary items	(20.3)	(84.7)
Changes in net assets or liabilities of pension plans and other benefit plans	(34.9)	(13.4)
Share in income of a company subject to significant influence	(1.9)	(2.0)
Valuation allowance on investment tax credit carryforwards	26.3	—
Other	(3.3)	(1.2)
	(182.2)	(136.5)
Net change in non-cash operating working capital	(35.2)	92.0
	(217.4)	(44.5)
Cash flows from investing activities:		
Additions to capital assets	(52.3)	(53.4)
Advances to affiliates	75.1	(36.0)
Proceeds from sale of capital assets	9.7	7.3
	32.5	(82.1)
Cash flows from financing activities:		
Decrease in bank overdraft and bank indebtedness	2.1	(11.1)
Repayment of long-term debt	(16.6)	(17.9)
Advances from affiliates	131.6	121.3
Capital stock issued	69.2	36.3
Dividends paid	(1.4)	(2.0)
	184.9	126.6
Cash and cash equivalents, end of year	\$ —	\$ —
Other information related to cash flows:		
Cash paid during the year for:		
Interest	\$ 154.3	\$ 150.4
Income taxes	2.9	2.9
Non-cash activities (note 17)		

See accompanying notes to consolidated financial statements.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements

Years ended December 31, 2005 and 2004

(in millions of dollars)

1. Significant accounting policies:

(a) Basis of presentation:

The consolidated financial statements include the accounts of Bowater Canadian Forest Products Inc. (the "Company") and its subsidiaries.

These financial statements are expressed in Canadian dollars. All consolidated subsidiaries are wholly-owned, except for Bowater Maritimes Inc., which is owned at 67%. The Company also has a 30% interest in an unconsolidated entity, Chaleur Sawmills Associates, which is accounted for using the equity method.

All significant intercompany transactions and balances have been eliminated.

(b) Foreign currency translation:

Monetary assets and liabilities are translated from foreign currencies into Canadian dollars at rates of exchange prevailing at the date of the balance sheet. Revenues and expenses are translated at average rates in effect during the month in which the transaction took place. Translation gains and losses are included in other income.

(c) Inventories:

Inventories of finished products are valued at the lower of average cost and net realizable value. Inventories of raw materials, repair materials and other operating supplies are valued at average cost.

(d) Capital assets:

Capital assets are stated at cost after the deduction of investment tax credits and government grants. The Company amortizes its capital assets over their estimated useful lives using the straight-line method for buildings and equipment. The pulp and paper mills, which are the Company's principal capital assets, are amortized over a period of 20 years on a straight-line basis. The sawmills are amortized on the straight-line basis over a period of 10 to 20 years. Accumulated amortization includes write-downs of buildings and equipment.

During the construction period, interest is capitalized on major improvements and expansions. No amortization is charged on major improvements or expansions until construction is completed.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

1. Significant accounting policies (continued):

(e) Other assets:

Financing costs incurred in issuing long-term debt are deferred and amortized over the term of the related obligation.

Long-term investments, except the long-term investment in a sawmill partnership which is accounted for using the equity method, are accounted for at cost. When there is a permanent loss in value of a long-term investment, the amount recorded is written down to recognize this loss in value in the statement of operations.

(f) Goodwill and other intangible assets:

Goodwill is tested for impairment at least on an annual basis. The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting unit is compared with its fair value. When the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not to be impaired and the second step of the impairment test is unnecessary. The second step is carried out when the carrying amount of a reporting unit exceeds its fair value. The impairment value to be recognized is measured by the amount by which the carrying value of the assets of the reporting entity being measured exceeds their fair value, up to the total amount of such assets.

Fair value is determined with the assistance of an independent third party. In making its determination of fair value, the Company relies primarily on the discounted cash flow method. The discounted cash flow method uses projections of cash flows from each of the reporting units and includes, among other estimates, periods of operation, projections of future product pricing, production levels, product costs, market supply and demand, capital spending and an assumption of the weighted average cost of capital. Changes in any of these estimates could have a material effect on the fair value of these assets in future measurement periods. On an ongoing basis, the annual impairment tests are expected to be performed during the fourth quarter of each year.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

1. Significant accounting policies (continued):

(g) Impairment of long-lived assets:

Under CICA Handbook Section 3063, *Impairment of Long-Lived Assets*, long-lived assets are tested for impairment whenever events or changes in circumstances indicate that the assets might be impaired. When so indicated, the impairment test is carried out in two steps. In the first step, the carrying amount of the asset (or asset group) is compared with its recoverable amount. The carrying amount of a long-lived asset is not recoverable, if the carrying amount exceeds the sum of the undiscounted cash flows expected to result from its use and eventual disposal. The second step is carried out when the carrying amount of a long-lived asset is not recoverable, in which case, the fair value of the long-lived asset is compared with its carrying amount to measure the amount of the impairment loss, if any. When an impairment loss is recognized, it is presented in income from operations in the statement of operations. When quoted market prices are not available, the fair value of the long-lived assets is determined using the discounted estimated future cash flow method.

A long-lived asset classified as held for sale is initially measured and reported at the lower of its carrying amount or fair value less cost to sell. Long-lived assets to be disposed of, other than by sale, are classified as held and used until the long-lived asset is disposed of.

(h) Environmental expenditures:

The Company expenses environmental costs related to existing conditions resulting from past or current operations and from which no current or future benefit is discernible. Expenditures that extend the life of the related property are capitalized. The Company determines a liability on a site-by-site basis and records a liability at the time it is probable and can be reasonably estimated.

(i) Income taxes:

The Company accounts for income taxes using the asset and liability method. Under this method, future income tax assets and liabilities are determined based on the temporary differences between the accounting basis and the tax basis of assets and liabilities. These temporary differences are measured using the enacted or substantively enacted tax rates and laws expected to apply when these differences reverse. Future tax benefits are recognized to the extent that realization of such benefits is considered more likely than not. The effect on future tax assets and liabilities of a change in income tax rates is recognized in operations in the period that includes the substantive enactment date.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

1. Significant accounting policies (continued):

(j) Employee future benefits:

The Company maintains defined benefit plans providing pension, other retirement, and post-employment benefits to most of its employees. Pension plan assets are valued at fair value for purposes of calculating the expected return on plan assets. The cost of pension and other post-employment benefits (including medical benefits, dental care, life insurance, and certain compensated absences) related to the employees' current service is charged to income annually. The cost is computed on an actuarial basis using the projected benefit method estimating the usage frequency and cost of services covered and management's best estimates of investment yields, salary escalation, and other factors. The Company has elected to use the corridor method to amortize actuarial gains or losses (such as changes in actuarial assumptions and experience gains or losses) over the average remaining service life of active employees. Under the corridor method, amortization is recorded only if the accumulated net actuarial gains or losses exceed 10% of the greater of the accrued pension benefit obligation and the value of the plan assets.

(k) Cash and cash equivalents:

Cash and cash equivalents are restricted to investments that are readily convertible into a known amount of cash, that are subject to minimal risk of changes in value and which have an original maturity of three months or less. As well, changes in short-term borrowings are treated as financing activities.

(l) Use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management estimates relate to the determination and evaluation of reserves for environmental matters and the useful life of assets for depreciation and evaluation of net recoverable amount. Actual results could differ from those estimates.

(m) Revenue recognition:

Revenue is recognized when persuasive evidence of an arrangement exists, the earnings process is completed, collection is considered reasonably assured and the risks and rewards of ownership have been transferred to the customer.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

1. Significant accounting policies (continued):

(n) Asset retirement obligations:

The Company records the fair value of a liability for an asset retirement obligation in the period in which it is incurred and in which a reasonable estimate of a fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset. Subsequently, the asset retirement cost is allocated to expense using a systematic and rational method and the liability is accreted to its face amount.

The Company has certain asset retirement obligations that have indeterminate useful lives and, therefore, have an indeterminate settlement date for the related asset retirement obligation. As a result, no asset retirement obligation was recorded for these assets. These assets include, for example, wastewater and effluent ponds that will have to be drained once the related operating facility is closed, and storage sites or owned facilities for which removal of chemicals and other related materials will be required once the related operating facility is closed. Once the life of these assets becomes determinable and an estimate of fair value can be made, an asset retirement obligation will be recorded.

(o) Guarantees:

Certain disclosures must be made by a guarantor about his obligations under guarantees in his consolidated financial statements. A guarantee is a contract or an indemnification agreement that contingently requires the Company to make payments to the other party based on changes in an underlying that is related to an asset, a liability or an equity security of the other party, or based on a third party's failure to perform under an obligating agreement. A liability will be recorded when the Company deems it probable that a payment relating to a guarantee will have to be made to the other party of the contract or agreement, considering recourse against any third party.

2. Impairment of assets:

During January 2006, the ultimate parent company, Bowater Incorporated, announced its plan to permanently close the Thunder Bay "A" kraft pulp mill in the second quarter of 2006. Accordingly, the Company recorded an asset impairment charge of \$57.7 million during the fourth quarter of 2005. Fair value of the "A" kraft pulp mill was nominal and was determined based on the estimated sale and salvage value plus any projected cash generated from its operations through April 2006. In connection with this decision, the Company will incur a 20% staffing reduction at this site. See note 3 "Severance related liabilities" for a discussion of the severance costs associated with this staffing reduction. For segment reporting purposes, the impairment charge is included in the Coated and Specialty Papers Division.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

3. Severance related liabilities:

In the fourth quarter of 2005, the Company recorded severance charges of approximately \$13.3 million for employee termination costs including severance and other benefits related to the permanent closure of the "A" kraft pulp mill at the Thunder Bay facility and the elimination of approximately 260 positions. These severance charges are classified as cost of sales. The remaining severance related accrual of \$13.3 million at December 31, 2005 is expected to be paid out in 2006, and is included in "Accounts payable and accrued charges" in the Consolidated Balance Sheet. Additionally, the Company expects to record pension related charges of approximately \$5.9 million in 2006, related to the permanent closure of the Thunder Bay "A" kraft pulp mill. These severance charges are included in the segment results of the Coated and Specialty Papers Division.

In 2004, the Company recorded severance charges of approximately \$2.8 million for employee termination costs including severance, medical, pension and other benefits, primarily from the voluntary termination of 35 employees related to the indefinite closure of the groundwood pulp mill at the Thunder Bay facility. Approximately \$1.6 million of the \$2.8 million employee termination costs were pension-related costs. During 2005, the accrual was reduced to nil by payments of \$1.2 million. These severance charges are included in the segment results of the Coated and Specialty Papers Division.

In connection with a multifaceted cost reduction initiative announced in the fourth quarter of 2002, the Company reduced its salaried and hourly workforce at certain locations and recorded approximately \$29.6 million for employee termination costs (\$1.6 million in 2004, \$27.5 million in 2003 and \$0.5 million in 2002), including severance, pension and other benefits. The majority of the terminations were part of either a voluntary or involuntary workforce reduction that was finalized in 2003 or 2002. Included in the 2004 termination charges are pension related costs of \$1.2 million. Approximately \$0.4 million and \$1.2 million is included in the Coated and Specialty Papers Division and in the Canadian Forest Products Division, respectively.

Severance and termination charges are classified as either cost of sales (manufacturing personnel) or selling and administrative expenses (administrative personnel) in the Company's consolidated statement of operations.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

4. Interest expense, net:

	2005	2004
Interest on long-term debt ⁽¹⁾	\$ 152.1	\$ 148.0
Interest on short-term debt	1.6	1.7
Amortization of deferred financing costs	0.2	0.4
	153.9	150.1
Interest income ⁽²⁾	(3.3)	(2.8)
	\$ 150.6	\$ 147.3

⁽¹⁾ The Company is charged interest on advances from the ultimate parent company. In 2005, such interest amounted to \$108.2 million (\$99.9 million in 2004).

⁽²⁾ The Company earns interest on some advances to its affiliates. In 2005, such interest amounted to \$2.8 million (\$2.5 million in 2004).

5. Other income, net:

	2005	2004
Unrealized exchange gain on long-term monetary items	\$ 20.5	\$ 84.7
Other foreign exchange loss	(6.6)	(18.5)
Gain on disposal of capital assets	8.3	5.6
Share in income of a company subject to significant influence	1.9	2.0
Other	(4.9)	(5.5)
	\$ 19.2	\$ 68.3

6. Income taxes:

The provision for income tax expense (benefit) attributable to loss before income taxes and non-controlling interest consists of:

	Current	Future	Total
Year ended December 31, 2005	\$ 5.5	\$ 6.1	\$ 11.6
Year ended December 31, 2004	9.2	(86.0)	(76.8)

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

6. Income taxes (continued):

The provision for income tax expense (benefit) attributable to loss before income taxes and non-controlling interest differs from the amounts computed by applying the combined federal and provincial income tax rate of 34.08% (32.48% in 2004) to loss before non-controlling interest as a result of the following:

	2005	2004
Loss before income taxes and non-controlling interest	\$ (352.5)	\$ (179.9)
Computed "expected" income taxes	(120.1)	(58.4)
Increase (decrease) in income taxes resulting from:		
Valuation allowance	138.2	(1.8)
Adjustment to future tax assets and liabilities for substantively enacted changes in tax laws and rates	(11.6)	(0.1)
Large corporation's tax	3.9	4.5
Non-taxable portion of foreign exchange gain	(3.1)	(13.4)
Other	4.3	(7.6)
	\$ 11.6	\$ (76.8)

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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6. Income taxes (continued):

The tax effects of temporary differences that give rise to significant portions of the future tax assets and future tax liabilities at December 31, 2005 and 2004 are presented below:

	2005	2004
Future tax assets:		
Non-capital loss carryforwards and pool of deductible research and development expenditures	\$ 155.4	\$ 155.5
Investment tax credit carryforwards	36.6	33.3
Liabilities	33.5	28.0
Unrealized exchange loss on long-term monetary items in foreign currency	3.2	—
Other	5.8	2.2
	234.5	219.0
Less valuation allowance	183.0	20.6
Total future tax assets	51.5	198.4
Future tax liabilities:		
Buildings and equipment - differences in net book value and undepreciated capital cost	8.0	106.2
Unrealized exchange gain on long-term monetary items in foreign currency	—	36.4
Net pension plan asset	30.7	15.7
Other	20.3	25.4
Total future tax liabilities	59.0	183.7
Net future tax (liabilities) assets	\$ (7.5)	\$ 14.7
	2005	2004
As reported in the consolidated balance sheet:		
Non-current future tax asset	\$ —	\$ 40.8
Non-current future tax liability	(7.5)	(26.1)
Net future tax (liabilities) assets	\$ (7.5)	\$ 14.7

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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6. Income taxes (continued):

During 2005, the valuation allowance of the Company increased by \$162.4 million. During 2005, based on operating losses and current evaluation of available tax planning strategies, it was determined, in accordance with CICA Handbook Section 3465, that the Company should record a tax charge to establish a valuation allowance against the remaining net deferred tax assets, which are primarily for loss carryforwards and tax credits. In connection with this requirement, the Company recorded a tax charge of \$138.2 million in order to establish this valuation allowance. The remaining increase of \$24.2 million in the valuation allowance is related to an amount of \$36.3 million of research and development tax credits from the Federal and Quebec governments (see note 20), net of expired investment tax credits of \$12.1 million. This charge is reflected in cost of sales in the Consolidated Statement of Operations.

The non-capital losses and investment tax credit carryforwards expire at various dates between 2006 and 2014.

7. Inventories:

	2005	2004
Raw materials	\$ 74.3	\$ 69.0
Work in process	28.8	21.2
Repair materials and other operating supplies	51.8	53.0
Finished products	59.2	53.3
	\$ 214.1	\$ 196.5

8. Assets held for sale:

The Company is currently marketing for the sale of approximately 373,000 acres of timberland in Canada. The Company expects the sales to be completed in 2006. The total amount of \$22.0 million includes the carrying value of the timberland (approximately \$17.4 million) of one of its woodland operations and certain assets of its Degelis sawmill (approximately \$4.6 million). The Company expects the proceeds of the timberland sales to exceed the carrying value. All of the assets held for sale are included in the Canadian Forest Products Division segment.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

9. Advances to affiliates:

	2005	2004
Notes receivable from an affiliated company, Bowater Mersey Paper Company Ltd., in the amount of US\$7.0 million (US\$68.6 million in 2004), bearing interest at prevailing market rates, without repayment terms ⁽¹⁾	\$ 8.1	\$ 82.8
Note receivable from the parent company, Bowater Canada Inc., in the amount of US\$293.8 million (US\$293.8 million in 2004), without interest and with no repayment terms	342.2	354.4
	\$ 350.3	\$ 437.2

⁽¹⁾ The prevailing market rate is established as the prime rate plus 1%.

10. Capital assets:

			2005
	Cost	Accumulated amortization	Net book value
Land	\$ 40.6	\$ —	\$ 40.6
Buildings and equipment	3,334.2	2,083.5	1,250.7
Timberland	47.3	22.3	25.0
Construction in progress	53.5	—	53.5
	\$ 3,475.6	\$ 2,105.8	\$ 1,369.8

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

10. Capital assets (continued):

	2004		
	Cost	Accumulated amortization	Net book value
Land	\$ 40.4	\$ —	\$ 40.4
Buildings and equipment	3,500.6	2,056.4	1,444.2
Timberland	71.8	28.8	43.0
Construction in progress	39.4	—	39.4
	\$ 3,652.2	\$ 2,085.2	\$ 1,567.0

The Company and its subsidiaries have timber harvesting licensing arrangements in the provinces of New Brunswick, Québec and Ontario.

11. Other assets:

	2005	2004
Pension assets	\$ 129.0	\$ 99.7
Deferred financing costs, net of accumulated amortization	1.1	1.3
Long-term investments ⁽¹⁾	12.9	12.4
Other	2.3	0.3
	\$ 145.3	\$ 113.7

⁽¹⁾ The major part of long-term investments consists of a \$11.8 million (\$11.1 million in 2004) investment, representing a 30% ownership interest in a sawmill partnership.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

12. Bank indebtedness:

	Commitment 2005	Outstanding		Commitment available
		2005	2004	
Revolving credit facility ⁽¹⁾	\$ 40.8	\$ —	\$ —	\$ 6.5
Uncommitted lines of credit ⁽²⁾	—	—	1.5	—

⁽¹⁾ Commitment available at December 31, 2005. The commitment available under the revolving credit facility is subject to covenant restrictions and is reduced by outstanding letters of credit amounting to \$34.3 million (\$23.0 million related to certain employee benefit plans and \$11.3 million for certain energy contracts).

⁽²⁾ The Company has available other various lines of credit totalling \$30 million, of which \$1.1 million was reserved for letters of credit as of December 31, 2005. The Company had no amounts drawn on these lines of credit as of December 31, 2005. Amounts drawn under these demand credit facilities bear interest at a prime rate.

The Company and the ultimate parent company, Bowater Incorporated, has available for the Company a three-year, US\$35 million revolving credit facility due April 2007. Borrowings under this facility incur interest based, at the option of the Company, on specified market interest rates plus a margin tied to the credit rating of the ultimate parent company's long-term debt. The facility contains various covenants which are calculated based on Bowater Incorporated's consolidated financial statements.

These covenants include requirements to maintain:

- i. a minimum consolidated net worth (generally defined as common shareholder s' equity, plus any outstanding preferred stock, plus minimum pension liability amounts) of US\$1.3 billion (as amended in December 2005). If Bowater Incorporated generates net income, the minimum net worth requirement increases by half of its consolidated net income for each fiscal quarter, excluding gains from cash flow hedges in place as of December 31, 2004.
- ii. a maximum of 65.0% ratio of total debt to total capital (defined as total debt less revaluation of debt assumed through acquisitions, plus net worth including minority interest, plus minimum pension liability amounts); and
- iii. an annual minimum EBITDA (generally defined as net earnings, excluding extraordinary, non-recurring or non-cash items, plus income taxes plus depreciation plus net interest expense) of US\$250.0 million measured quarterly, beginning March 31, 2005 through December 31, 2005, and US\$400.0 million at the end of each quarter thereafter.

At December 31, 2005, the ultimate parent Company, Bowater Incorporated, was in compliance with all of its financial covenants.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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13. Advances from affiliates:

	2005	2004
Advances from affiliates, composed of several notes of individual amounts varying from US\$0.3 million to US\$157.2 million, totalling US\$189.1 million (from US\$0.3 million to US\$343.1 million, totalling US\$912.5 million in 2004), bearing interest at various rates between 8.0% and 8.15% (between 8.0% and 8.15% in 2004), without repayment terms	\$ 220.2	\$ 1,100.7
Advances from the ultimate parent company, in an amount of US\$547.5 million (US\$427.7 million in 2004), bearing interest at prevailing market rates, without repayment terms ⁽¹⁾	637.6	515.8
	\$ 857.8	\$ 1,616.5

⁽¹⁾ The prevailing market rate is established as the mid-grade 30-day commercial paper index.

14. Long-term debt:

	2005	2004
Debentures:		
10.85% due in 2014	\$ 125.0	\$ 125.0
Senior Notes:		
10.625% Series A due in 2010 (US\$98.0 million)	114.1	118.2
10.50% Series B (2005: US\$51.0 million; 2004: US\$61.2 million) ⁽ⁱ⁾	59.4	73.8
10.60% Series C due in 2011 (US\$70.0 million)	81.5	84.4
10.26% Series D (2005: US\$13.2 million; 2004: US\$15.4 million) ⁽ⁱ⁾	15.4	18.6
Non-interest bearing loan with the government of Quebec due in 2008, with earlier possible payments if certain criteria are met	10.3	11.9
	405.7	431.9
Less current portion of long-term debt	15.9	15.0
	\$ 389.8	\$ 416.9

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

14. Long-term debt (continued):

- (i) The Series B Senior Notes are payable by capital payments of US\$10.2 million per year with the final payment due in 2010. The Series D Senior Notes are payable by capital payments of US\$2.2 million per year with the final payment due in 2011.

As of December 31, 2005, the Company was in compliance with all its debt indentures.

All of the Company's long-term debt is unsecured.

Based on exchange rates as of December 31, 2005, repayments required on long-term debt over the next five years and thereafter are as follows:

2006	\$	15.9
2007		15.9
2008		21.8
2009		14.4
2010		128.6
2011 and thereafter		209.1
	\$	405.7

15. Capital stock:

Authorized:

As at December 31, 2005, the Company's authorized share capital consists of an unlimited number of common shares, an unlimited number of Class A preferred shares and an unlimited number of Class B preferred shares. The Class A preferred shares are entitled to non-cumulative cash dividends at the rate of 8% per annum, redeemable at the option of the Company at a redemption price of \$1,000 per share plus declared and unpaid dividends. The Class B preferred shares are entitled to cash dividends at the rate of 8.5% per annum, redeemable at the option of the Company at a redemption price of \$1 per share plus declared and unpaid dividends.

	2005	2004
Issued and paid:		
68,060,541 common shares	\$ 959.0	\$ 959.0
105,430.522 (36,342.276 in 2004) Class A preferred shares	105.6	36.4
867,768,765 Class B preferred shares	867.8	—
	\$ 1,932.4	\$ 995.4

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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15. Capital stock (continued):

On June 30, 2005, the Company issued to Bowater Canada Finance Limited Partnership ("BCFLP"), 36,215.791 Class A preferred shares for a total consideration of \$36.2 million paid in cash. On December 30, 2005, the Company issued to BCFLP 32,872.455 Class A preferred shares for a total consideration of \$33.0 million paid in cash. On December 23, 2005, \$867.8 million of long-term advances owed to BCFLP were cancelled in consideration for the issuance of 867,768,765 Class B preferred shares to BCFLP.

On December 16, 2004, the Company issued to Bowater Canada Inc., the parent company, 36,342.276 Class A preferred shares for a total consideration of \$36.3 million paid in cash.

16. Related party transactions:

The Company, in the normal course of business, has sold to a company under common control \$975.7 million (\$1,015.4 million in 2004) of its manufactured products at a price established and agreed to by the related parties. Selling and administrative expenses include \$26.5 million (\$28.2 million in 2004) of commissions paid to a company under common control, Bowater America, Inc. Also, Bowater Incorporated, the ultimate parent company, reallocated administrative expenses to the Company. In 2005, the Company was charged \$5.2 million from this reallocation (\$5.6 million in 2004).

17. Statement of cash flows:

Non-cash investing and financing activity items:

	2005	2004
Investing activities:		
Additions to capital assets which were in accounts payable and accrued charges at the end of the year	\$ 2.3	\$ 6.0
Financing activities:		
Reduction in advances from affiliates which were converted to Class B preferred shares	(867.8)	—
Increase in capital stock from the conversion of advances from affiliates to Class B preferred stock	867.8	—

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

18. Commitments and contingencies:

(a) Commitments:

Minimum payments required under operating leases are as follows:

2006	\$	3.1
2007		3.0
2008		2.9
2009		2.8
2010		2.5
Subsequent years		16.8
	\$	31.1

The Company assumed various long-term purchase contracts, the more significant including a steam purchase contract at its Dolbeau, Québec, operation. The Dolbeau operation's steam purchase contract expires in 2023 and has total commitments of approximately \$232.4 million (\$11.6 to \$12.5 million in years 2006 to 2010 and \$172.3 million thereafter).

The Company has a service contract with Boralex Dolbeau Inc. ("Boralex") to provide all services needed to operate the Dolbeau wood-fired cogeneration facility in exchange for a fixed fee adjusted for inflation.

Dolbeau also guarantees minimum electricity revenue to Boralex and will reimburse Boralex for any penalty paid to Hydro-Québec for undelivered kilowatt-hour under the minimum quantity.

(b) Contingencies:

The Company is involved in various legal proceedings relating to contracts, commercial disputes, taxes, environmental issues, employment and workers' compensation claims and other matters. The Company periodically reviews the status of these proceedings with both inside and outside counsel. Management believes that the ultimate disposition of these matters will not have a material adverse effect on the financial condition, but it could have a material adverse effect on the results of operations in a given quarter or year.

Countervailing and antidumping duties:

In response to the expiration of the Softwood Lumber Agreement, a number of industry groups in the United States filed petitions with the U.S. Department of Commerce ("USDOC") and the U.S. International Trade Commission ("USITC") alleging unfair trade practices by the Canadian softwood lumber industry. These petitions proposed that certain softwood lumber exports from Canada to the United States be charged countervailing and antidumping duties.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

18. Commitments and contingencies (continued):

(b) Contingencies (continued):

Lumber duties imposed by the USDOC became effective for lumber shipments from Canada to the U.S. beginning May 22, 2002. The USDOC imposed antidumping duties (ADD) of 8.43% on all the Company's Canadian softwood lumber imports and countervailing duties (CVD) of 18.79% on softwood lumber imported from all provinces except New Brunswick and Nova Scotia. Since May 22, 2002, the Company has been posting cash deposits to cover the duties based upon the duty rates then in effect. These rates have been adjusted several times. On January 24, 2005, the ADD rate was amended to 3.78%. On February 24, 2005, the CVD rate was amended to 16.37%. Most recently, the CVD rate was changed to 8.7% and the ADD rate was changed to 2.11% on December 12, 2005. Lumber duties are included as a component of distribution costs on the consolidated statement of operations. CVD charges of \$27.2 million (2004 - \$31.4 million) and ADD charges of \$6.9 million (2004 - \$15.3 million) were incurred during fiscal year 2005.

The Canadian government has appealed the duties to the World Trade Organization ("WTO") and the U.S. courts and under the terms of the North American Free Trade Agreement (NAFTA) and requested that the duties be refunded. The final amount of CVD and ADD that may be assessed on Canadian softwood lumber imports into the U.S. will depend upon negotiations among the governments involved in the dispute or upon determinations made by the NAFTA, WTO or other adjudicatory panels to which the duties may be appealed. Until the dispute about the duties is resolved, the Company will continue to pay the duties as required by the USDOC. To date, CVD and ADD of approximately US\$93.3 million have been paid. Should these duty rates be eliminated or decreased, a portion or all of the US\$93.3 million could be reversed into operating income in future periods.

In 2005, the Province of Québec mandated that annual harvests of softwood timber on Crown-owned land be reduced 20% below 2004 levels. The 20% reduction is required to be achieved, on average, for the three-year period beginning April 1, 2005 and ending March 31, 2008. These requirements did not have a material impact on the results of operations or financial condition of the Company in 2005 and are not expected to have a material impact in 2006.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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19. Employee future benefits:

The Company's pension plans are principally defined benefit pension plans and cover substantially all employees. Benefits from these plans are based on years of service and either career earnings or final average earnings.

The Company also provides post-retirement benefits to eligible employees. The costs of these benefits, which are principally health care, are accounted for during the employees' active service period.

The unrecognized net transition amount is being amortized over the average expected future service periods of employees.

The Company measures its accrued benefit obligation and the fair value of plan assets for accounting purposes as at September 30 of each year. Actuarial valuations for funding purposes are conducted on a triennial basis, unless required earlier by pension legislation. The latest actuarial valuations were conducted for two plans on December 31, 2003, for one plan on December 30, 2004 and for five plans on December 31, 2004.

The following table provides a reconciliation of the changes in the plans' benefit obligations and fair value of plan assets for the fiscal years ended December 31, 2005 and 2004, and a statement of the funded status as of December 31, 2005 and 2004:

	2005		2004	
	Pension plans	Other benefit plans	Pension plans	Other benefit plans
Change in benefit obligation:				
Benefit obligation, beginning of year	\$ 1,319.9	\$ 94.2	\$ 1,284.4	\$ 89.8
Service cost	18.0	2.5	17.9	2.9
Interest cost	79.1	5.3	76.3	5.3
Plan participants' contribution	10.7	—	9.8	—
Plan amendments	40.3	(1.6)	—	—
Benefits paid	(80.7)	(5.5)	(79.5)	(6.3)
Curtailment gain	—	(18.1)	—	—
Special termination benefits	—	—	2.8	—
Actuarial (gain) loss	139.9	(4.9)	8.2	2.5
Benefit obligation, end of year	\$ 1,527.2	\$ 71.9	\$ 1,319.9	\$ 94.2

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

19. Employee future benefits (continued):

	2005	2004
	Pension plans	Pension plans
Change in plan assets:		
Fair value of plan assets, beginning of year	\$ 1,049.7	\$ 958.3
Actual return on plan assets	150.0	111.1
Employer contributions	63.7	50.0
Plan participants' contributions	10.7	9.8
Benefits paid	(80.7)	(79.5)
Fair value of plan, end of year	\$ 1,193.4	\$ 1,049.7

	2005			2004	
	Pension plans	Other benefit plans	Pension plans	Other benefit plans	
Reconciliation of funded status:					
Funded status	\$ (333.8)	\$ (71.9)	\$ (270.2)	\$ (94.2)	
Employer contributions after measurement date	27.2	—	14.1	—	
Unamortized actuarial loss (gain)	318.6	(3.8)	259.9	9.4	
Unamortized net transition obligation	35.4	23.1	42.3	35.2	
Unamortized prior service cost	41.3	(0.5)	2.1	2.1	
Net asset (liability) recognized	\$ 88.7	\$ (53.1)	\$ 48.2	\$ (47.5)	

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

19. Employee future benefits (continued):

The following table provides the amounts recognized in the consolidated balance sheets:

	2005		2004	
	Pension plans	Other benefit plans	Pension plans	Other benefit plans
Accrued benefit liability	\$ (40.3)	\$ (53.1)	\$ (51.5)	\$ (47.5)
Pension asset	129.0	—	99.7	—
Net asset (liability) recognized	\$ 88.7	\$ (53.1)	\$ 48.2	\$ (47.5)

The following table presents the total of these plans that are not fully funded; these amounts are included in the current benefit obligation and fair value of plan assets at year-end as presented above:

	2005	2004
	Pension plans	Pension plans
Accrued benefit obligation	\$ 1,499.2	\$ 1,294.0
Fair value of plan assets	1,164.2	1,023.2
Funded status	\$ (335.0)	\$ (270.8)

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

19. Employee future benefits (continued):

The following table provides the components of net periodic benefit cost:

	2005		2004	
	Pension plans	Other benefit plans	Pension plans	Other benefit plans
Service cost	\$ 18.0	\$ 2.5	\$ 17.9	\$ 2.9
Interest cost	79.1	5.3	76.3	5.3
Actual return on plan assets	(150.0)	—	(111.1)	—
Actuarial loss (gain)	139.9	(4.9)	8.2	2.5
Plan amendments	40.3	(1.6)	—	—
Curtailment gain	—	(1.3)	—	—
Special termination benefits	—	—	2.8	—
Net expense (income) before adjustments to recognize the long-term nature of the plans	127.3	—	(5.9)	10.7
Difference between expected and actual return on plan assets	70.2	—	34.2	—
Difference between net actuarial loss (gain) and actuarial loss (gain)	(128.9)	5.5	0.3	(1.8)
Difference between amortization of prior service cost for year and actual plan amendments for year	(39.2)	1.9	0.3	0.4
Amortization of transitional obligation	6.9	3.7	6.6	4.3
Net periodic benefit cost	\$ 36.3	\$ 11.1	\$ 35.5	\$ 13.6

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

19. Employee future benefits (continued):

The weighted average assumptions used in the measurement of the Company's benefit obligation and net periodic benefit cost are as follows:

	2005		2004	
	Pension plans	Other benefit plans	Pension plans	Other benefit plans
Discount rate	5.0%	5.0%	6.0%	6.0%
Expected return on plan assets	7.5%	—	7.5%	—
Rate of compensation increase	3.5%	—	3.75%	—

The assumed health care cost trend rate used in measuring the accumulated other benefit plans' obligation was between 6.14% and 8.54% at the end of 2005 and is expected to decrease gradually to between 3.20% and 3.74% in 2011 and remain at that level thereafter. A one percentage point change in assumed health care costs would have the following effects:

	2005		2004	
	Other benefit plans		Other benefit plans	
Sensitivity analysis	1% increase	1% decrease	1% increase	1% decrease
Effect on service and interest costs	\$ 0.8	\$ (0.7)	\$ 0.9	\$ (0.7)
Effect on benefit obligation	5.7	(4.7)	11.0	(9.0)

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

19. Employee future benefits (continued):

The percentage of fair value of total plan assets held by the pension plans as of the measurement date was as follows:

Asset category	Weighted average target allocation	2005	2004
Equity securities	59%	59%	58%
Debt securities	39%	39%	40%
Real estate	2%	2%	2%
	100%	100%	100%

The Company's investment strategy for pension plans is to maximize the long-term rate of return on plan assets within an acceptable level of risk in order to secure the Company's obligation to pay pension benefits to qualifying employees while minimizing and stabilizing pension expense and contributions. The asset allocation for each plan is reviewed periodically and rebalancing toward target asset mix is made when asset classes fall outside of a predetermined range. Risk is managed for each plan through diversification of asset classes, specific constraints imposed within asset classes, annual review of the investment policies to assess the need for changes, and monitoring of fund managers for compliance with mandates as well as performance measurement. A series of permitted and prohibited investments are listed in the Company's respective investment policies. Prohibited investments include investments in the equity securities of the ultimate parent company, Bowater Incorporated, or its affiliates as well as investments in the ultimate Company's debt securities.

In addition to the above, the Company's contributions for defined contribution plans amount to \$1.5 million (\$1.4 million in 2004).

20. Government assistance:

The Company is eligible to receive grants in the form of tax credits from the Federal and Quebec governments related to research and development activities and certain eligible road construction expenditures. In 2005, a charge of \$24.1 million, net of \$7.2 million of tax credits recognized for the current year, was recorded in cost of sales and an amount of \$5.0 million increased capital assets following the increase in the valuation allowance for an amount of \$36.3 million related to tax credit carryforwards previously recognized (see note 6). In 2004, \$12.8 million was recognized and applied to reduce the cost of sales.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

21. Financial instruments:

Fair value:

The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies. However, considerable judgment is necessary to develop these estimates. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different assumptions or methodologies may have a material effect on the estimated fair value amounts.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

- (i) Short-term financial assets are valued at their carrying amounts as presented in the balance sheet, which are reasonable estimates of fair value due to the relatively short period to maturity of the instruments.
- (ii) Rates currently available to the Company for long-term debt with similar terms and remaining maturities have been used to estimate the fair value of the long-term debt.
- (iii) The carrying amounts of the advance to/from affiliates have not been determined due to the relationship between the Company and the demonstrated ability to change the terms of the advances.

The estimated fair values of the Company's financial instruments which differ from their carrying values are as follows:

	2005	2004
Long-term debt carrying amount	\$ 405.7	\$ 431.9
Long-term debt fair value	435.0	511.3

Credit risk:

The Company's financial assets that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. Cash and cash equivalents are held in major financial institutions. Concentrations of credit risk with respect to receivables are limited due to the large number of customers and their dispersion across geographic areas.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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21. Financial instruments (continued)

Interest rate risk:

The majority of the Company's long-term debt is at fixed interest rates, thus limiting the interest rate risk.

22. Segment information:

Factors management used to identify the Company's reportable segments:

The Company's reportable segments are business units responsible for the marketing, sale or manufacturing of different products and the operations of certain manufacturing and timber harvesting sites. They are managed separately because of the different products and sites for which they are responsible.

Description of the types of products and services from which each reportable segment derives its revenues:

Effective January 1, 2005, the Company has two reportable segments: the Canadian Forest Products Division and the Coated and Specialty Papers Division. A paper and market pulp manufacturing site previously included in the Newsprint Division was merged into Bowater Incorporated's Coated and Specialty Papers Division. As a result, the Coated and Specialty Papers Division became a new division of the Company. Additionally, the Forest Products Division was merged into the Canadian Forest Products Division and the Coated and Specialty Papers Division. These changes were made to reflect segment reporting changes made by the Company's ultimate parent company, Bowater Incorporated. Prior year results have been restated to facilitate comparison to the 2005 presentation.

Canadian Forest Products Division:

The Canadian Forest Products Division operates four paper manufacturing sites in the provinces of Quebec and New Brunswick. The division manages 0.4 million acres of owned or leased timberland and over 21.2 million acres of Crown-owned land in Quebec and New Brunswick, on which the Company has cutting rights. In addition, the division operates nine sawmills and supplies wood to four paper mills and seven sawmills, and is responsible for the marketing and sales of the Company's timber and lumber production. In January 2005, the Company sold its treated wood facility located in Dégelis, Québec for proceeds of \$0.7 million.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

22. Segment information (continued):

Description of the types of products and services from which each reportable segment derives its revenues (continued):

Coated and Specialty Papers Division:

The Coated and Specialty Papers Division (formerly the Newsprint Division) operates one paper and market pulp manufacturing site in the province of Ontario. The division also manages 8.4 million acres of Crown-owned land in Ontario. The financial results from market pulp sales are included in the Coated and Specialty Papers Division results; however, the Pulp Division, a division of Bowater Incorporated, has the marketing and sales responsibility for the market pulp products.

The following tables summarize information about segment operating profit and loss and segment assets for the years ended December 31, 2005 and 2004:

	2005			
	Coated and Specialty Papers Division	Canadian Forest Products Division	Corporate/ Other Eliminations	Total
Sales - including internal sales	\$ 820.3	\$ 1,188.9	\$ —	\$ 2,009.2
Eliminations of internal sales	(244.3)	—	—	(244.3)
Sales - external customers ⁽¹⁾	576.0	1,188.9	—	1,764.9
Amortization of capital assets	61.5	98.3	0.5	160.3
Segment operating loss	(142.4)	(67.3)	(11.4)	(221.1)
Total assets	582.2	1,377.8	513.3	2,473.3
Capital expenditures	15.8	36.5	—	52.3
Goodwill	—	5.9	—	5.9

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

22. Segment information (continued):

Description of the types of products and services from which each reportable segment derives its revenues (continued):

Coated and Specialty Papers Division (continued):

	2004			
	Coated and Specialty Papers Division	Canadian Forest Products Division	Corporate/ Other Eliminations	Total
Sales - including internal sales	\$ 870.2	\$ 1,143.1	\$ —	\$ 2,013.3
Eliminations of internal sales	(242.7)	—	—	(242.7)
Sales - external customers ⁽¹⁾	627.5	1,143.1	—	1,770.6
Amortization of capital assets	61.5	97.6	—	159.1
Segment operating loss	(50.2)	(46.3)	(4.4)	(100.9)
Total assets	660.1	1,421.3	619.1	2,700.5
Capital expenditures	24.3	29.1	—	53.4
Goodwill	—	6.4	—	6.4

	Sales by product	
	2005	2004
Newsprint	\$ 679.2	\$ 673.4
Uncoated specialty papers	403.4	375.7
Market pulp	318.8	349.2
Lumber and other wood products	363.5	372.3
	\$ 1,764.9	\$ 1,770.6

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
(in millions of dollars)

22. Segment information (continued):

Description of the types of products and services from which each reportable segment derives its revenues (continued):

Coated and Specialty Papers Division (continued):

	Sales by country (2)	
	2005	2004
Canada	\$ 250.6	\$ 253.3
United States	1,236.0	1,271.0
United Kingdom	90.9	71.3
Japan	8.7	20.6
Other countries	178.7	154.4
	\$ 1,764.9	\$ 1,770.6

(1) Including sales to the ultimate parent company.

(2) Sales are allocated to countries based on the location of the customer. No unaffiliated customer represented 10% or more of consolidated sales.

23. Subsequent events:

On March 27, 2006, the Company completed the sale of its Degelis sawmill assets for proceeds of approximately \$7.1 million. The gain of \$0.9 million from this sale will be recognized during the first quarter of 2006.

On April 21, 2006, the Company completed the sale of its Baker Brook sawmill and approximately 225,000 acres of timberland in Canada for combined proceeds of approximately \$79.4 million. A gain of approximately \$52.0 million from this sale will be recognized during the second quarter of 2006.

The carrying value of the Degelis sawmill and timberland assets are classified as assets held for sale in the consolidated balance sheet at December 31, 2005 (see note 8).

The following transactions occurred on February 28, 2006, in the order presented:

- (a) Advances of approximately US\$400.0 million owed by the Company to the ultimate parent company, Bowater Incorporated, were transferred by Bowater Incorporated to BCHI in exchange for common shares of BCHI. Immediately following this transaction, the Company owed US\$400 million to BCHI.

BOWATER CANADIAN FOREST PRODUCTS INC.

Notes to Consolidated Financial Statements, Continued

Years ended December 31, 2005 and 2004
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23. Subsequent event (continued):

- (b) Advances of approximately US\$400 million (described above) owed by the Company to BCHI were cancelled in exchange for the issuance of 455,200 Class A preferred shares to BCHI. Notes of approximately US\$164.8 million due to BCHI were cancelled in exchange for the issuance of 187,558.536 Class A preferred shares to BCHI.

These transactions, which will be recorded in the first quarter of 2006, resulted in the conversion of notes and advances from affiliates totaling US\$564.8 million to 642,758.536 Class A preferred shares and had no impact on the Company's cash flows.

24. Reclassification:

Certain prior years' numbers have been reclassified to conform with the presentation adopted for 2005.