

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO **FRASER PAPERS INC./PAPIERS FRASER INC.**, FPS CANADA INC., FRASER PAPERS HOLDINGS INC., FRASER TIMBER LIMITED, FRASER PAPERS LIMITED AND FRASER N.H. LLC (COLLECTIVELY, THE "APPLICANTS")

Applicants

FACTUM OF THE APPLICANTS
(Motion Returnable April 13, 2010)

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FACTUM OF THE APPLICANTS
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PART I – RELIEF REQUESTED BY THE APPLICANTS

1. The Applicants seek an Order, *inter alia*:
 - (i) an Order approving the terms of an asset purchase agreement between the Company and FPS Canada Inc. as vendors and Fortress Specialty Cellulose Inc., as purchaser ("Fortress"), dated March 18, 2010 (the "Purchase Agreement"); and
 - (b) an Order vesting title to the Purchased Assets (as defined in the Purchase Agreement) in Fortress upon completion.
2. All references to currency in this Affidavit are to Canadian dollars, and all capitalized terms used in this Affidavit and not otherwise defined are as defined in the Purchase Agreement.

PART II – THE FACTS

The Thurso Mill – Business and Operations

3. The Applicants own and operate a northern bleached hardwood kraft pulp manufacturing facility situated at Thurso, Quebec (the “**Thurso Mill**”). The Thurso Mill produces pulp for use in the manufacture of certain specialty and commodity fine paper applications. In 2008, the last year of full production, approximately 40% of the Thurso Mill’s pulp production was shipped to the Applicants’ paper mills in either Madawaska, Maine or Gorham, New Hampshire. The balance was sold to third parties.

*Affidavit of Glen McMillan, sworn April 9, 2010 (the “**McMillan Affidavit**), at para 4.*

4. When in production, the Applicants employ approximately 320 employees at the Thurso Mill. The Communications, Energy and Paperworkers Union of Canada (“**CEP**”) represents approximately 280 of these employees.

McMillan Affidavit, at para 5.

5. In 2008 and 2009, the Thurso Mill generated negative cash flows as a result of a number of changing factors, including a decrease in pulp prices, high oil prices and a strong Canadian dollar relative to the U.S. dollar. As a result, the Company made the decision to close the Thurso Mill on an indefinite basis commencing in June, 2009.

McMillan Affidavit, at para 6.

6. In May of 2009, the Applicants met with the Government of Quebec (the “**Province**”) to request financial assistance to keep the mill operating beyond the planned date of closure. During the meeting, it was explained that expected lower pulp prices were going to lead to ongoing

losses from the Thurso operations and that Fraser Papers did not have the financial resources to continue to fund operating losses.

M^cMillan Affidavit, at para 7.

7. On June 5, 2009, the Thurso Mill was indefinitely closed due to the prevailing market conditions that led to unsustainable cash losses. The Thurso Mill has remained closed during the Applicants' *Companies' Creditors Arrangement Act* ("CCAA") proceedings. Normal care and maintenance activities have continued in an effort to preserve the asset for possible re-start of operations.

M^cMillan Affidavit, at para 8.

8. On October 16, 2009, the Applicants submitted a proposal to Hydro Quebec in response to a tender for the purchase of electrical power to be generated from biomass fuel. The proposal was part of a \$70 million capital project involving the development and construction of a 22 megawatt biomass cogeneration facility at the Thurso Mill designed to lower the cost of steam for the pulping process and generate new revenues from the sale of electricity under a long term power purchase agreement (the "**Biomass Power Project**"). On December 16, 2009, the Applicants were informed that their proposal was accepted and they had been awarded, subject to certain conditions, an opportunity to secure a 15 year long term power purchase contract (the "**Hydro Quebec Contract**"). The terms of the Hydro Quebec Contract have been finalized although the agreement has not been executed.

M^cMillan Affidavit, at para 9.

Sale Process

9. In considering what options were available in respect of the Thurso Mill, the Applicants had to take the following factors into account:

- (i) the Thurso Mill's small size and fourth quartile cost position among global pulp mills;
- (ii) the highly cyclical market for the hardwood pulp produced at the Thurso Mill and declining demand for fine paper production in North America, together with relatively high freight costs incurred for shipments of pulp to European and Asian markets;
- (iii) the age of the Thurso Mill's fixed assets and the related costs associated with care and maintenance of these assets or capital required for any significant upgrade to them;
- (iv) the interest from potential investors as a result of the Biomass Power Project and the Hydro Quebec Contract;
- (v) the long term environmental obligations at the Thurso Mill and related sites owned by the Applicants;
- (vi) the pension deficits that exist under the two defined benefit pension plans administered by the Applicants and registered in the Province of Quebec (the “**Quebec Plans**”); and
- (vii) terms of the collective agreements with the CEP and the TNVR (an association of non-unionized Thurso Mill employees) that relate to the Thurso Mill.

M^cMillan Affidavit, at para 10.

10. Beginning in late August, 2009, the Applicants also participated in discussions with a group of Thurso Mill employees (the “Employee Group”) who were interested in developing a business plan (the “Employee Business Plan”) to purchase the Thurso Mill.

M^cMillan Affidavit, at para 11.

11. Pursuant to the terms of an Employee Business Plan that was developed, the Employee Group proposed to purchase the Thurso Mill in exchange for \$1 and the assumption of all liabilities related to the Thurso Mill. The Employee Group also contemplated that the Applicants would retain a minority ownership interest in the Thurso Mill.

M^cMillan Affidavit, at para 12.

12. The Applicants and the Employee Group met with the Province to discuss the terms of the Employee Business Plan and to see if the Province would be willing to finance the start up and operation of the Thurso Mill by the Employee Group. The Applicants also advised the Province that they were unable to fund the costs of maintaining the Thurso Mill through the winter months and would have no choice but to permanently shut down the Thurso Mill.

M^cMillan Affidavit, at para 13.

13. The Province responded to the Employee Business Plan in early October 2009, and established a number of criteria that the Employee Group would have to meet in order to receive any start-up financing from the Province. Among the criteria required by the Province was that the Employee Group had to locate a business partner in the forestry industry (a “Strategic Partner”).

M^cMillan Affidavit, at para 14.

14. Importantly, from the point of view of the financial condition of the Applicants, the Province agreed to cover the cost of basic maintenance and heating of the Thurso Mill until January 31, 2010, in order to provide the Applicants and the Employee Group with the necessary time to locate a Strategic Partner. The Province has since extended its agreement to finance the basic maintenance and heating of the Thurso Mill until the transaction detailed below is completed.

M^cMillan Affidavit, at para 15.

15. In response to the Province's request that a Strategic Partner be found, the Applicants developed a list of seventeen potential parties. The Applicants contacted each of these potential parties to determine their interest in the Thurso Mill.

M^cMillan Affidavit, at para 16.

16. The Applicants also approached PricewaterhouseCoopers Inc., Court appointed Monitor of the Applicants (the "Monitor"), to request that the Monitor consider if there were additional parties that might be interested in purchasing the Thurso Mill.

M^cMillan Affidavit, at para 17.

17. The Monitor reviewed the Applicants' list of seventeen potential parties and added approximately nineteen additional potential purchasers to the list being considered. The Monitor contacted each of the additional nineteen potential purchasers and provided them with a description of the assets for sale. The Monitor requested that any interested party execute a

confidentiality agreement in order to obtain additional information, consistent with the protocol that was put in place by the Applicants.

M^cMillan Affidavit, at para 18.

18. Notwithstanding this marketing process, wherein numerous potential buyers were contacted, by the end of January 2010, Fortress was the only party to express interest with respect to the Thurso Mill. As a result, the Applicants agreed to negotiate with Fortress. Fortress is a publicly listed Company and is unrelated to Brookfield Asset Management Inc.

M^cMillan Affidavit, at para 20.

19. On February 1, 2010, the Applicants signed a letter of intent with Fortress setting out the terms and conditions upon which Fortress would be willing to purchase the Purchased Assets (the “**LOI**”). During this time, the Monitor was kept informed of discussions between Fortress and the Applicants and participated in certain discussions between the two parties.

M^cMillan Affidavit, at para 21.

20. Pursuant to the terms of the LOI, Fortress was granted the exclusive right to negotiate a definitive agreement of purchase and sale with respect to the Purchased Assets until March 31, 2010.

M^cMillan Affidavit, at para 22.

21. On March 18, 2010, the Applicants and Fortress entered into the Purchase Agreement and proceeded to execute same.

M^cMillan Affidavit, at para 23.

22. Pursuant to the Purchase Agreement the Applicants retain any and all liabilities with respect to the Quebec Plans and any other such pension plans for the benefit of active and inactive employees or retirees that are or were employed prior to Closing (as defined in the Purchase Agreement) in connection with the Business of the Applicants.

M^cMillan Affidavit, at para 25.

23. Fortress has agreed to pay CDN \$3 million (the “**Purchase Price**”), subject to certain adjustments, for the Purchased Assets and also to assume the following liabilities:

- (a) all Environmental Liabilities (as defined in the Purchase Agreement) with respect to the Purchased Assets;
- (b) all liabilities relating to the ownership, operation and use of the Purchased Assets from and after the time of Closing (as defined in the Purchase Agreement); and
- (c) all obligations and liabilities under the Purchased Contracts (as defined in the Purchase Agreement), except those related to any default existing prior to the Time of Closing (as defined in the Purchase Agreement). Fortress has undertaken a review of the Purchased Contracts and has sent communications to all counterparties to agreements for which Fortress intends to assume the obligations thereunder. Located at Schedule “K” of the Purchase Agreement is a listing of the contracts Fortress intends to assume.

M^cMillan Affidavit, at para 27.

24. The Closing of the transaction contemplated by the Purchase Agreement is scheduled to take place on or about April 30, 2010.

McMillan Affidavit, at para 30.

Service

25. All parties with potential interests that are intended to be vested out pursuant to the requested Order have received service of the motion materials with respect to the approval of this transaction.

PART III – ISSUES AND THE LAW

Issue: What factors should the Court consider in determining whether to approve the transaction contemplated by the Purchase Agreement?

26. There is jurisdiction under the CCAA to approve asset sales in the absence of a Plan of Arrangement where a sale is in the best interests of a debtor company's various stakeholders, particularly where the sale is on a going concern basis.

Re Nortel Networks Corp., 2009 CarswellOnt 4467 at paras. 27-40 (Ont. S.C.J.) ("Nortel").

27. It is respectfully submitted that the sale of the Thurso Mill to Fortress is the type of sale contemplated by Justice Morawetz in *Nortel*. Fortress intends to restart and invest approximately \$150 million into the Thurso Mill. The intended investment may include the building of a biomass based cogeneration plant. Additionally, as a result of the start-up, approximately 320 people will have the opportunity to go back to work.

McMillan Affidavit, at paras 33 and 35.

28. The test uniformly applied by Ontario courts is from the Ontario Court of Appeal's decision in *Royal Bank v. Soundair Corp.* In *Soundair*, the court established four "duties" that a court must perform when deciding whether a receiver who has sold property acted properly.

Ontario courts have consistently recognized that the *Soundair* principles are “equally applicable *mutatis mutandis* in a CCAA sale situation”.

Royal Bank v. Soundair Corp., 1991 CarswellOnt 205 (Ont. C.A.) [“*Soundair*”].

Re Nortel Networks Corp. 2009 CarswellOnt 4838 at paras. 33-35 (Ont. S.C.J.) [“*Nortel*”].

29. In reviewing a proposed sale of assets, a court should consider:

- (i) whether the person selling has made a sufficient effort to get the best price and has not acted improvidently;
- (ii) the interests of all parties;
- (iii) the efficacy and integrity of the process by which offers are obtained; and
- (iv) whether there has been unfairness in the working out of the process.

Soundair, *supra* at para. 16.

(i) **Best Price**

30. The Applicants, with the assistance of the Monitor, made a significant and sufficient effort to obtain the best price for the Purchased Assets. The Applicants and the Monitor have worked together to market and sell the Thurso Mill in a broad process involving a total of 36 parties. The Applicants provided confidential information with respect to the Thurso Mill operations to 15 parties that requested additional information. The Applicants proceeded to negotiate a sale of the Thurso Mill to the only party that expressed interest in purchasing it.

McMillan Affidavit, at paras 17, 18, 20.

(ii) **Interest of All Parties**

31. The sale of the Thurso Mill on the terms of the Purchase Agreement is in the best interest of the Applicants’ stakeholders. The terms of the Purchase Agreement:

(a) provide a purchase price of \$3 million (the “**Purchase Price**”) to the Applicants. This offer is significantly greater than the informal business plan put forward by a group of Thurso Mill employees, whereby the Thurso Mill would have been purchased for \$1. The Purchase Price is also equal to or greater than the amount the Applicants would receive if they were forced to liquidate the Thurso Mill and related assets;

Monitor’s Eleventh Court Report, dated April 9, 2010 (the “Monitor’s Eleventh Report”), at para 23.

(b) ensure that the following stakeholders receive the following payments:

- (i) all real property taxes owing prior to the Closing (as defined in the Purchase Agreement) will be paid in full;
- (ii) all vacation pay owing to employees prior to Closing will be paid;
- (iii) all outstanding Civil Code Liens (as defined in the Purchase Agreement) will be paid in full; and
- (iv) the Applicants will receive the balance of the proceeds of the Purchase Price, available to the creditors in accordance with the priority of their claims.

McMillan Affidavit, at paras 24, 27, 28.

(c) provide for the resumption in employment for approximately 320 employees of the Thurso Mill and direct benefits to suppliers and indirect economic benefit to the region surrounding the Thurso Mill; and

McMillan Affidavit, at para 35.

Monitor’s Eleventh Report, at para 26.

(d) provide for the assumption by Fortress of the Environmental Liabilities associated with the Thurso Mill, thereby relieving the Applicants from those liabilities and reducing the total number of claims to be made against the Applicants.

Monitor's Eleventh Report, at para 26.

(iii)(iv) Integrity of Sale Process and Fairness

32. The process to market and sell the Thurso Mill has been conducted in a fair and open manner whereby all potentially interested parties were contacted and provided with the opportunity to purchase the Thurso Mill and related business. In establishing a fair and even handed process the Applicants and the Monitor worked together to market and sell the Thurso Mill. The Monitor provided input on the negotiations related to the Purchase Agreement. The Court appointed Monitor supports the sale of the Thurso Mill in accordance with the terms of the Purchase Agreement.

McMillan Affidavit, at para 37.

Monitor's Eleventh Report, at paras 20, 21 and 33.

33. The record before this Honourable Court establishes, and the Applicants respectfully submit, that the Soundair principles have been satisfied.

34. The recent amendments to the CCAA address the disposition of a debtor company's business assets. Section 36(1) of the CCAA provides as follows:

A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 36(1) [“CCAA”].

35. According to the Industry Canada Briefing Book, section 36 “is intended to provide the debtor company with greater flexibility in dealing with its property while limiting the possibility of abuse”.

Industry Canada, “Bill C-55: Clause by Clause Analysis – Bill Clause No. 131 – CCAA Section 36” [“Industry Canada”].

Re Canwest Global Communications Corp., 2009 CarswellOnt 7169 at para. 32 (Ont. S.C.J.) [“Canwest”].

36. A debtor company must give notice to those secured creditors who are likely to be affected by its application to the court for authorization to dispose of assets outside of the ordinary course of business.

CCAA, supra at s. 36(2).

37. The separate service list for this motion includes, among others, those parties with registered security interests pursuant to the *Quebec Register of Personal and Movable Real Rights* and those parties with statutory and registered liens on all real property that is to be purchased under the Purchase Agreement.

Affidavit of Service of Jean H. Turner sworn April 9, 2010.

Proofs of Service of Denis Beaulieu dated April 9, 2010.

Proofs of Service of Patrice Paradis dated April 9, 2010.

38. In deciding whether to grant authorization to the debtor company to dispose of its assets, the court is to consider, among other things:

- (i) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;
- (ii) whether the Monitor approved the process leading to the proposed sale or disposition;

- (iii) whether the Monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;
- (iv) the extent to which the creditors were consulted;
- (v) the effects of the proposed sale or disposition on the creditors and other interested parties; and
- (vi) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

CCAA, supra at s. 36(3).

(i) Reasonable Sales Process in the Circumstances

39. It is respectfully submitted that the process leading to the sale of the Thurso Mill is reasonable in the circumstances. The Applicants and the Monitor developed and implemented an exhaustive sales strategy on an aging pulp mill that requires substantial capital improvement and that has significant environmental and employee liabilities.

McMillan Affidavit, at para 37.

Monitor's Eleventh Report, at paras 20 and 21.

(ii) (iii) Monitor Approval and Court Report in Support

40. The Monitor supports the sale contemplated by the terms of the Purchase Agreement.

Monitor's Eleventh Report, at para 33.

(iv) Consultation of Creditors

41. The Applicants' principled secured creditors, namely CIT Business Credit Canada Inc., Brookfield Asset Management and the Minister of Business New Brunswick, are aware of and have consented to the sale of the Thurso Mill.

Monitor's Eleventh Report, at para 23.

42. The Applicants' creditors were not generally consulted on the sale of the Thurso Mill to Fortress. However, the Monitor provided regular updates on the sale of the Thurso Mill in its court reports. The Monitor provided updates on the sale of the Thurso Mill in its 8th, 9th and 10th Court Reports dated February 2, 2010, February 22, 2010 and April 1, 2010, respectively. In addition to the Monitor's court reports, the Affidavit of Peter Gordon, sworn March 30, 2010, provides an update with respect to the sale of the Thurso Mill.

Monitor's Eighth Court Report, dated February 2, 2010 at paras. 24-32.

Monitor's Ninth Court Report, dated February 22, 2010 at paras. 43-48.

Monitor's Tenth Court Report, dated April 1, 2010 at paras. 91-94.

Affidavit of Peter Gordon, sworn March 30, 2010, at paras 18-21.

(v) Effect of Sale on Stakeholders

43. It is respectfully submitted that if approved, the sale of the Thurso Mill to Fortress on the terms and conditions of the Purchase Agreement presents the best possible outcome for the Applicant's stakeholders. As stated in paragraph 31 above (in greater detail), the purchase price will satisfy various claims made by employees, lien holders and municipalities. The transaction will also transfer potential environmental liabilities out of the estate, thereby reducing the total number of claims against the Applicants' estate.

McMillan Affidavit, at paras 34 and 37.

Monitor's Eleventh Report, at para 26.

(vi) Fair Consideration When Considering Market Value

44. It is respectfully submitted that the value received in exchange for the Thurso Mill is fair and reasonable, taking into account its market value. Of the 36 potential purchasers contacted by the Applicants and the Monitor, only Fortress expressed interest in proceeding with a purchase of

the Thurso Mill. The lack of interest reflects the risk associated with the industry as well as the age of the Thurso Mill and the significant liabilities to be assumed by any purchaser.

McMillan Affidavit, at para 20.

Monitors' Eleventh Report, at para 27.

45. The Applicants respectfully submit that the record before this Honourable Court not only establishes that the Soundair principles have been satisfied, but also establishes that the transaction contemplated by the Purchase Agreement satisfies the factors enumerated in recently amended Section 36 of the CCAA.

PART IV – ORDER REQUESTED

46. The Applicants request an Order granting the relief set out in the Notice of Motion dated April 9th, 2010.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 12TH DAY OF
APRIL, 2010.**



Larry C. Ellis, of counsel to the Applicants

SCHEDULE A – AUTHORITIES CITED

Tab	Document
1.	<i>Re Nortel Networks Corp.</i> , 2009 CarswellOnt 4467 (Ont. S.C.J.).
2.	<i>Royal Bank v. Soundair Corp.</i> , 1991 CarswellOnt 205 (Ont. C.A.).
3.	<i>Re Nortel Networks Corp.</i> , 2009 CarswellOnt 4838 (Ont. S.C.J.).
4.	Industry Canada, “Bill C-55: Clause by Clause Analysis – Bill Clause No. 131 – CCAA Section 36”.
5.	<i>Re Canwest Global Communications Corp.</i> , 2009 CarswellOnt 7169 (Ont. S.C.J.).

SCHEDULE B – RELEVANT STATUTES

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36.

36(1) Restriction on disposition of business assets - A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.

(2) Notice to creditors - A company that applies to the court for an authorization is to give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.

(3) Factors to be considered – In deciding whether to grant the authorization, the court is to consider, among other things,

- (a) Whether the process leading to the proposed sale or disposition was reasonable in the circumstances;
- (b) Whether the monitor approved the process leading to the proposed sale or disposition;
- (c) Whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;
- (d) The extent to which the creditors were consulted;
- (e) The effects of the proposed sale or disposition on the creditors and other interested parties; and
- (f) Whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

(5) Related persons – For the purpose of subsection (4), a person who is related to the company includes

- (a) a director or officer of the company;
- (b) a person who has or has had, directly or indirectly, control in fact of the company; and
- (c) a person who is related to a person described in paragraph (a) or (b).

(6) Assets may be disposed of free and clear – The court may authorize a sale or disposition free and clear of any security, charge or other restriction and, if it does, it shall also order that other assets of the company or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.

(7) Restriction – employers – The court may grant the authorization only if the court is satisfied that the company can and will make the payments that would have been required under paragraphs 6(4)(a) and 5(a) if the court had sanctioned the compromise or arrangement.

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