

CANADA

PROVINCE OF QUÉBEC  
DISTRICT OF MONTRÉAL

No.: 500-11-

**S U P E R I O R C O U R T**  
(Commercial Division)  
(Sitting as a court designated pursuant to the  
*Companies' Creditors Arrangement Act*,  
R.S.C. 1985, c. C-36)

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

**SHERMAG INC.**, a legal person constituted under the *Companies Act* (Québec), having its domicile at 2171 King Street West, in the City of Sherbrooke and District of Saint-François, Province of Québec, J1J 2G1

and

**JAYMAR FURNITURE CORP.**, a legal person constituted under the laws of Nova Scotia and continued under the laws of Canada, having its domicile at 75 Jaymar Street, in the City and District of Terrebonne, Province of Québec, J6W 1M5

and

**SCIERIE MONTAUBAN INC.**, a legal person constituted under the laws of Canada, having its domicile at 100 Route du Lac George, in the City of Notre-Dame-de-Montauban and District of Saint-Maurice, Province of Québec, G0X 1W0

and

**MÉGABOIS (1989) INC.**, a legal person constituted under the *Companies Act* (Québec), having its domicile at 2171 King Street West, in the City of Sherbrooke and District of Saint-François, Province of Québec, J1J 2G1

and

**SHERMAG CORPORATION**, a legal person constituted under the laws of the State of Delaware, having its chief executive office at Corporation Trust Center, 1209 Orange Street, in the City of Wilmington, State of Delaware, 19801, U.S.A.

and

**JAYMAR SALES CORPORATION**, a legal person constituted under the laws of the State of Nevada, having its chief executive office at Incorp Services, Inc., 3155 East Patrick Lane, Suite 1, in the City of Las Vegas, State of Nevada, 89120-3481, U.S.A.

Petitioners

and

**RSM RICHTER INC.**, a legal person duly constituted under the laws of Canada, having its principal place of business at 2 Place Alexis-Nihon, 21<sup>st</sup> Floor, in the City and District of Montréal, Province of Québec, H3Z 3C2

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**PETITION FOR AN INITIAL ORDER PURSUANT TO SECTIONS 4, 5 AND 11  
OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*  
(R.S.C. 1985, c. C-36)**

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**TO ONE OF THE HONOURABLE JUDGES OF THE SUPERIOR COURT, SITTING IN  
COMMERCIAL DIVISION, IN AND FOR THE JUDICIAL DISTRICT OF  
MONTRÉAL, PETITIONERS RESPECTFULLY SUBMIT THE FOLLOWING:**

**1. INTRODUCTION**

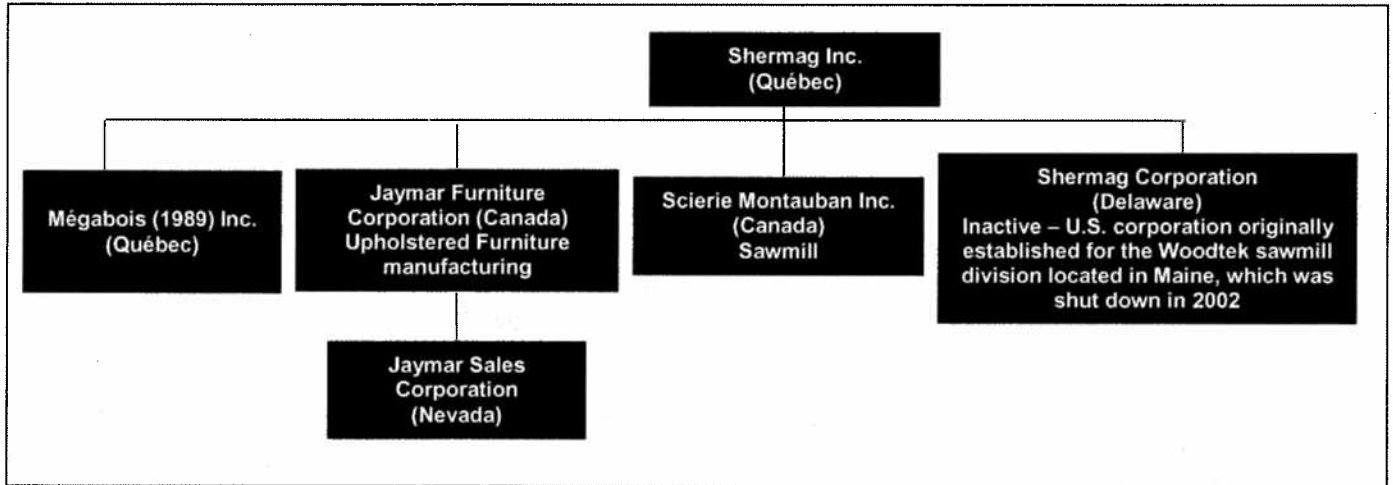
1. Petitioners seek protection under the *Companies' Creditors Arrangement Act* ("CCAA") to facilitate the reorganization of their business.
2. Petitioner Shermag Inc. ("**Shermag**") and Petitioner Mégaboïs (1989) Inc. ("**Mégaboïs**") are incorporated under Part IA of the *Companies Act* (Québec) and have their domicile at 2171 King Street West, in the City of Sherbrooke, Province of Québec, the whole as appears from excerpts of the corporate registry (CIDREQ) communicated herewith as **Exhibit R-1**.
3. Petitioner Jaymar Furniture Corp. ("**Jaymar**") was incorporated under the laws of Nova Scotia and has been continued under the *Canada Business Corporations Act* (the

“*CBCA*”) and has its domicile at 75 Jaymar Street, in the City of Terrebonne, Province of Québec, the whole as appears from an excerpt of the corporate registry (CIDREQ) communicated herewith as **Exhibit R-2**.

4. Petitioner Scierie Montauban Inc. (“**Scierie**”) is incorporated under the *CBCA* and has its domicile at 100 Route du Lac George, in the City of Notre-Dame-de-Montauban, Province of Québec, the whole as appears from an excerpt of the corporate registry (CIDREQ) communicated herewith as **Exhibit R-3**.
5. Petitioner Shermag Corporation (“**SherCorp**”) is incorporated under the laws of the State of Delaware and has its chief executive office at Corporation Trust Center, 1209 Orange Street, in the City of Wilmington, State of Delaware, U.S.A.
6. Petitioner Jaymar Sales Corporation (“**JaySales**”) is incorporated under the laws of the State of Nevada and has its chief executive office at Incorp Services, Inc., 3155 East Patrick Lane, Suite 1, in the City of Las Vegas, State of Nevada, U.S.A.
7. Petitioners’ center of main interests is in Sherbrooke where the administration of the business interests of Petitioners is conducted on a regular basis.
8. Petitioners submit and attorn to the jurisdiction of the Commercial Division of the Superior Court of the District of Montréal.
9. Petitioners are in the process of restructuring their operations and intend, in the context thereof, to file a plan of compromise and arrangement for all or part of their secured and unsecured debts, in accordance with their respective classes, and will request that this Court convene a meeting of their creditors so that they may vote on the plan of arrangement and compromise to be proposed.
10. As such, Petitioners are seeking the orders set forth herein from this Court in order to ensure the continuation of their operations and to prevent and stay any recourses and remedies of Petitioners’ creditors for an initial period of thirty (30) days.

**1.1. PETITIONERS' CORPORATE STRUCTURE**

11. Petitioners' corporate structure is illustrated in the diagram below. Jaymar, Scierie, Mégaboïs and SherCorp are wholly owned subsidiaries of Shermag. JaySales is a wholly owned subsidiary of Jaymar.



**1.2. PETITIONERS' HISTORY**

12. Founded in 1977 in the City of Sherbrooke by Mr. Serge Racine, Shermag originally produced glider rockers and gradually extended its product line through various acquisitions.

13. In 1986, Shermag proceeded to an initial public offering of shares for total proceeds of \$14 million which was used to enhance the distribution network and to finance several acquisitions.

14. Since then, Shermag's shares have been traded on the Toronto Stock Exchange ("TSX") under the symbol SMG. Based on a current price of \$0.35 per share (as of May 1<sup>st</sup>, 2008), Shermag has a market capitalization of approximately \$4.67 million. In 2003, Shermag's market capitalization exceeded \$200 million.

15. In 1991, Shermag took advantage of the newly ratified North American Free Trade Agreement and began marketing its products in the U.S. thereby providing a growth opportunity coupled with a more diversified revenue base.

16. In 1996, Shermag acquired Sofas International S.I. Inc. (“Sofas”), an upholstered furniture manufacturer. Later, Sofas’ operations have been transferred to Jaymar and Sofas has been combined into Shermag.
17. In 1997, Shermag proceeded to a second public offering of shares, which raised approximately \$25.6 million.
18. In 2001, Shermag created an import division to import certain finished furniture exhibiting designs and workmanship less profitably manufactured in Canada.
19. In May 2003, Shermag acquired Jaymar, one of Canada’s leading manufacturer of quality leather and fabric upholstered furniture, allowing Shermag to extend its product line and leverage its distribution channels.

### 1.3. **PETITIONERS’ BUSINESS**

20. Today, Petitioners are a leader in the design, production, sourcing and distribution of high-quality residential furniture with over \$85 million in net sales.
21. Petitioners offer what they qualify as “casual contemporary” product lines. They serve most of the residential furniture market with three categories of furniture, sold in the mid to mid-high-price points:
  - (i) casegoods: include products such as bedroom suites and dining room sets;
  - (ii) upholstered furniture: comprising chairs, sofas and loveseats made with either leather or fabric; and
  - (iii) glider rockers.
22. Petitioners enjoy a very enviable reputation in the North American market and figure prominently in the design of contemporary-style furniture.
23. Petitioners have three distinct channels of distribution in North America. These are (i) major department stores, (ii) independent retailers specializing in the distribution of

high-end furniture and (iii) national mass market chains. Petitioners' corporate mission is to be the home furnishing company of choice.

24. Petitioners' clients include well-known retailers such as Sears and The Bay in Canada, Macy's, Hetcht's and Carson Pirie Scott in the United States of America.
25. Petitioners altogether employed up to one thousand fifty (1,050) people on or about December 28, 2007. However, Petitioners have reduced their number of employees for the reasons more fully explained below at Section 6.1.3. As of April 18, 2008, while Petitioners still have eight hundred and eleven (811) employees, only approximately three hundred and sixty (360) have an active status.

#### **1.4. PETITIONERS' FACILITIES**

26. Petitioners currently own or lease nineteen (19) facilities which are, *inter alia*, comprised of manufacturing plants, a distribution center, a development center, a sawmill, showrooms and the head office.

##### **1.4.1 Manufacturing Plants**

27. Shermag currently operates a total of three (3) manufacturing plants, all strategically located in Canada's eastern lumber region, with close proximity to hardwood supply, its main raw material. The non-operating plants have been temporarily shut down.
28. All operating plants are located in Québec and there are also two (2) non-operating plants located in New Brunswick.
29. All manufacturing plants are owned by Shermag.

##### **1.4.2 Distribution Center**

30. In June 2006, Shermag opened a new central warehouse in Montréal which is the principal distribution center for Petitioners.

#### **1.4.3 Development Center**

31. In April 2005, as an integral part of Shermag's focus on developing a regular flow of new products, as more fully explained below at Section 6.1.1, Shermag opened a Development Center.
32. This Development Center is no longer being used, although the activities are still being pursued in other Petitioners' Facilities.

#### **1.4.4 Sawmill**

33. Petitioners also own one sawmill in Notre-Dame-de-Montauban, Québec, with a production capacity of 10 million board feet per year.
34. In March 2006, a substantial part of the sawmill burnt down.
35. Since then, Petitioners have been subcontracting the sawing operations.
36. The sawmill has been the object of an offer to purchase which has been accepted. The sale should close later this month.

#### **1.4.5 Showrooms**

37. Shermag also leases three (3) showrooms located in Montréal, Mississauga (Ontario) and High Point (North Carolina).

#### **1.4.6 Head Office**

38. The 15,400 sq. ft. office building is located at 2171 King Street West, Sherbrooke, Québec, and is owned by Shermag.

#### **1.5. SHERMAG'S OWNERSHIP**

39. As mentioned above at paragraphs 13 and 14, Shermag has been a public corporation since 1986.

40. Its share structure consists of only one class of voting common shares and one class of non-voting preferred shares.
41. Clarke, Inc. ("**Clarke**"), a Nova Scotia based company, is currently Shermag's largest shareholder.
42. Clarke is a diversified holding company with interests in freight transportation services, international shipping warehousing, real estate and marketable securities.
43. Clarke is publicly traded on the TSX under the ticker symbol CKI.
44. It is in August 2006 that Clarke began acquiring large blocks of Shermag's common stock.
45. As of the day of the present Petition, Clarke has a 19.9999% stake in Shermag.
46. Caisse de dépôt et placement du Québec is the second largest shareholder of Shermag with a stake of approximately 11%.

## 2. **FINANCIAL SITUATION**

47. On February 8, 2008, Shermag reported its results for the third quarter and nine (9) month period ended December 28, 2007, the whole as appears from a copy of Shermag's Interim Report for the third quarter ended December 28, 2007, communicated herewith as **Exhibit R-4**.
48. As illustrated in Exhibit R-4, Shermag's financial results have been disappointing in comparison to the same period the year before.
49. Full comparative results for the third quarter and the nine (9) months ended December 28, 2007, are as follows:



<b>Comparative results -3<sup>rd</sup> Quarter (in thousands of dollars, except per share data)</b>	<b>3<sup>rd</sup> Quarter 2007-2008</b>	<b>3<sup>rd</sup> Quarter 2006-2007</b>
Gross revenue	\$25,317	\$40,562
Gross earnings	\$577	\$2,176
Unusual items – restructuring costs	\$16,729	\$3,474
<b>Loss before income taxes</b>	<b>(\$22,505)</b>	<b>(\$11,022)</b>
<b>Net loss</b>	<b>(\$22,282)</b>	<b>(\$7,708)</b>
Loss per common share – basic	(\$1.67)	(\$0.58)
Loss per common share – diluted	(\$1.67)	(\$0.58)
Exports	\$14,976	\$27,024

<b>Comparative results – Nine month period (in thousands of dollars, except per share data)</b>	<b>2007-2008</b>	<b>2006-2007</b>
Gross revenue	\$83,663	\$131,895
Gross earnings	\$7,606	\$12,459
Unusual items – restructuring costs	\$16,729	\$3,474
<b>Loss before income taxes</b>	<b>(\$33,239)</b>	<b>(\$19,211)</b>
<b>Net loss</b>	<b>(\$29,905)</b>	<b>(\$13,234)</b>
Loss per common share – basic	(\$2.24)	(\$0.99)
Loss per common share – diluted	(\$2.24)	(\$0.99)
Exports	\$48,672	\$89,237

50. As a matter of fact, Shermag’s financial situation has been considerably deteriorating since 2005.
51. Indeed, Shermag’s net sales decreased from approximately \$229 million in 2005 to \$155 million in 2007 to approximately \$93 million for the eleven (11) months ended February 29, 2008.
52. Furthermore, Shermag’s cumulative losses from 2005 to December 28, 2007 are approximately \$88 million.
53. The reasons behind those financial difficulties are more fully explained at Section 5 of the present Petition and the measures already undertaken to correct the financial situation are explained at Section 6 hereof.

3. **PETITIONERS' INDEBTEDNESS AND LIABILITIES**

54. The principal secured creditor of Petitioners is Wachovia Capital Finance of Canada (“**Wachovia**”).
55. According to Exhibit R-4, Petitioners’ debt towards Wachovia as of December 28, 2007 consisted of a \$13.8 million revolving loan and \$8.2 million in term debt.
56. Petitioners’ indebtedness towards Wachovia is secured on virtually all of the assets, movable or immovable, of Petitioners.
57. Under the credit facility currently in place with Wachovia (the “**Credit Facility**”), Shermag, Jaymar and Scierie are co-borrowers and are solidarily liable, the whole as appears from a copy of the Loan Agreement with Wachovia dated June 5, 2006 (the “**Loan Agreement**”) communicated herewith as **Exhibit R-5**.
58. Under the Credit Facility, the obligations of Shermag, Jaymar and Scierie are guaranteed by JaySales and SherCorp, the whole as appears from copies of the Guarantee Agreements dated June 5, 2006 communicated herewith as **Exhibit R-6**.
59. In addition to Petitioners’ debt toward Wachovia, Petitioners presently have an estimated \$10 million of payables and potential contingent liabilities which may exceed \$25 million.
60. According to Exhibit R-4, the unaudited liabilities of Petitioners as at December 28, 2007 can be summarized as follows:

<b>Liabilities</b> (in thousands of dollars)	
Current liabilities	
Accounts payable and accrued liabilities	11,671
Income taxes payable	5
Instalments on long-term debt	1,260
	<hr/>
	12,936
Long-term-term debt (Wachovia)	20,782
Deferred credits	2,657
Future income taxes	137
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	36,512
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61. Always according to Exhibit R-4, Petitioners' long-term debt of \$20.782 million as at December 28, 2007 is detailed as follows:

Revolving credit, lender's prime rate (6.25%)	13,809
Term loan, lender's prime rate (6.25%), payable in monthly capital instalments of \$104,167, maturing in June 2014	8,209
Loan, secured by rolling stock, 1.9%, payable in monthly blended instalments of \$894, maturing in March 2010	
Non-interest bearing loans from a government agency	
	<hr/>
	22,042
	<hr/>
Instalments due within one year	1,260
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	20,782

**4. APPLICATION OF THE CCAA**

62. As explained above at Section 3, Petitioners are indebted to its various creditors in an amount that well exceeds \$5 million.
63. Furthermore, Petitioners are not be able to meet their obligations as they become due since they face a liquidity crisis, given, amongst others, Wachovia's decision to reduce Petitioners' borrowing capacity on April 16, 2008 (as more fully explained at paragraph 92 below).
64. Moreover, given that Jaymar, Scierie, SherCorp and Mégaboïs are all subsidiaries of Shermag, they are "affiliated companies" for the purposes of the CCAA.
65. Thus, all Petitioners qualify as "debtor company" under the CCAA and meets the requirements of Section 3 of the CCAA.

**5. NEED FOR RESTRUCTURING**

66. As shown above in Section 2, Petitioners are facing serious financial difficulties.
67. The financial difficulties experienced by Petitioners may be explained, *inter alia*, by the following factors:
- (i) the sharp and sudden increase in value of the Canadian dollar as compared to the U.S. dollar;

- (ii) competition from cheaper importers; and
- (iii) weak retail furniture market.

**5.1. DECLINE IN THE U.S. DOLLAR AND U.S. ECONOMY**

68. Over the past five (5) years, the value of the Canadian dollar as compared to the U.S. dollar has increased from \$0.64 as of January 3, 2003 to \$0.9815 as of May 1<sup>st</sup>, 2008, as appears from two extracts of the proposed conversion measure available on the *Bank of Canada*'s web site, communicated herewith *en liasse* as **Exhibit R-7**.
69. This sharp and sudden increase in value has been very difficult to support for exporting Canadian enterprises for which an important part of their revenues were paid in U.S. dollars and for which the bulk of their expenses were paid in Canadian dollars.
70. An important part of Petitioners' sales and revenue is derived from the American market (approximately  $\frac{2}{3}$  of Petitioners' revenues) and is, as such, paid in American dollars, whereas the bulk of its operating expenses are paid in Canadian dollar.
71. As such, Petitioners' business, dependant on exports to the American market, has suffered greatly from the sharp and sudden increase in value of the Canadian dollar, having to support a sudden diminution in revenues for a similar volume of sales and similar operating costs.
72. The current weak U.S. economy has also hurt the financial results and the extent of this impact has yet to be fully determined.

**5.2. COMPETITION FROM CHEAPER IMPORTERS**

73. Petitioners are currently faced with considerable competition from cheaper importers, primarily from China, but also from Vietnam and Malaysia.
74. These Asian competitors did not enjoy competitive advantages when the U.S. dollar was much stronger. As a result of a "dollarized" currency, these competitors removed price elasticity and have hence created significant deflationary pressures on furniture product prices.

75. Petitioners have begun to produce and buy products in Asia, but this has to be further developed and implemented.

**5.3. WEAK RETAIL FURNITURE MARKET**

76. In the recent years, the Canadian furniture market has faced considerable challenges and can currently be considered as weak.

77. This slowdown in the furniture market can be mainly explained by (i) the housing crisis in the U.S., (ii) the credit crunch and (iii) the decline of the U.S. dollar.

**6. RESTRUCTURING EFFORTS**

78. As early as 2004, Petitioners have made considerable efforts to restructure their business and operations. They have, *inter alia*:

- (i) implemented a business transformation plan; and
- (ii) considered a proposal from Clarke to privatize Shermag.

**6.1. THE TRANSFORMATION PLAN**

79. Shermag's management began in approximately 2005 to execute a brand-based business transformation plan that is converting Petitioners into a customer-driven organization with a strong competitive position (the "**Transformation Plan**").

80. The Transformation Plan centered around two key attributes:

- (i) a reduction of domestic capacity and the transformation of the balance to a fast response, made-to-order ("**MTO**") manufacturing model; and
- (ii) outsourcing to Asia mass production of certain products no longer profitably produced in North America.

81. These two attributes, however, implied that Petitioners had to consolidate the domestic operating activities by, *inter alia*, closing some manufacturing plants and distributions centers and reducing the associated fixed costs.

82. The implementation of the Transformation Plan was a meaningful decision, however, and notwithstanding all efforts to date, Petitioners could not avoid the current liquidity crisis.

#### **6.1.1 The MTO Model**

83. The MTO model is applicable to both department stores and independent retailers because they can broaden the product offering without affecting inventory commitment or service. This model is particularly appealing for smaller independent retailers whose centralized organizations execute “special orders” better. Historically, large chains have had difficulty handling a “special order” business because of the added complexity on the selling floor and in the management of the supply chain. However, there is an increasing number of examples of larger scale retailers moving to incorporate “choice-based” products into their mix in order to differentiate themselves from purely priced and finance based competition.

#### **6.1.2 Outsourcing to Asia**

84. Pursuant to the Transformation Plan, Asia will be used in at least two different aspects of Petitioners’ operations:

- (i) components: Shermag has begun importing components and intends to increase Asian content in 2008 as Shermag integrates parts into its domestically made chairs and begins to locally complete unfinished beds made in Asia as part of its domestically made MTO collections like Wave, Yao and Bridgeport; and
- (ii) complete collections will be imported such as London, Contour and Bourbon Street. Production of glider rockers was also transferred to Asia (previously produced in Lennoxville).

#### **6.1.3 Consolidation of the Domestic Operating Activities**

85. So as to implement the Transformation Plan, Petitioners had to close various facilities:

- (i) On March 11, 2005, the plant in Scotstown, Québec, which manufactured bedroom and juvenile furniture, was permanently closed and this shutdown

affected a total of eighty-four (84) workers, the whole as appears from a press release dated March 11, 2005 communicated herewith as **Exhibit R-8**;

- (ii) On May 30, 2005, Shermag announced that it was to close its plant of Victoriaville and that such shutdown would affect 95 workers, the whole as appears from a press release dated May 30, 2005 communicated herewith as **Exhibit R-9**;
- (iii) On December 1, 2005, Shermag announced that it was to close its Saint-Léonard, Québec factory and consolidated its upholstery operations at the Jaymar facility in Terrebonne, Québec, thereby affecting approximately seventy (70) employees, the whole as appears from a press release dated December 1, 2005 communicated herewith as **Exhibit R-10**;
- (iv) On December 9, 2005, Shermag announced the consolidation of its sawmill operations at the Scierie's facility in Notre-Dame-de-Montauban, Québec. As a result of the consolidation of the sawmill operations, Petitioners ceased operations at the Lac-Mégantic sawmill, affecting forty-eight (48) workers, the whole as appears from a press release dated December 9, 2005 communicated herewith as **Exhibit R-11**;
- (v) On April 10, 2006, Shermag announced the opening of a new 350,000 sq.ft. distribution center in Montréal for the warehousing and distribution of its finished furniture products. As a result of such opening, the main distribution center in Sherbrooke, Québec closed as well as the secondary distribution center in Saint-Jean-sur-Richelieu and the distribution center in Victoriaville, Québec, reduced its activities, the whole as appears from a press release dated April 10, 2006 communicated herewith as **Exhibit R-12**;
- (vi) On February 12, 2007, Shermag announced that it would permanently shut down its plants located at Disraéli and Saint-Étienne-de-Lauzon, the whole as appears from a press release dated February 12, 2007 communicated herewith as **Exhibit R-13**; and

(vii) On December 10, 2007, Shermag announced the closure of four plants; those of Dudswell (Bishopton) and Placages Lennox, Cookshire-Eaton, in Québec and those of Edmundston and Saint-François-de-Madawaska in New Brunswick. These closures affected three hundred and twenty (320) employees and bring Shermag's total employees to approximately seven hundred and fifty (750), the whole as appears from a press release dated December 10, 2007 communicated herewith as **Exhibit R-14**.

86. Unfortunately, during this transition process, Petitioners have endured lower than desired financial results which include fixed asset charges related to the realignment of Petitioners' manufacturing facilities. Additionally, the significant weakening of the U.S. dollar has had a direct impact on Petitioners' ability to return to profitability.

#### **6.2. CLARKE'S PROPOSAL**

87. On February 7, 2008, Petitioners received a letter from Clarke, Shermag's largest shareholder, expressing an interest in privatizing Shermag at a price to be negotiated by Clarke and the independent members of Shermag's board of directors, the whole as appears from a copy of a press release dated February 7, 2008 communicated herewith as **Exhibit R-15**.

88. An independent committee reviewed Clarke's proposal and engaged an independent valuator (KPMG) as required by applicable securities legislation. The price indicated by Clarke was below the valuation range established by such independent valuator and, therefore, the independent committee was not in a position to recommend acceptance of the proposal.

89. On April 21, 2008, Shermag announced that the independent directors had informed Clarke of the foregoing and Clarke has indicated that it does not intend to proceed with an offer or amend its proposal at this time, the whole as appears from a press release dated April 21, 2008 communicated herewith as **Exhibit R-16**.



7. **FUTURE AND NEED FOR PROTECTION PURSUANT TO THE CCAA**

90. Petitioners are of the view that their overall business can be viable and, in fact, will be profitable over time.
91. Petitioners have previously attempted to improve process and restructure. However, Petitioners do face a liquidity crisis and also, further restructuring changes must be made in order to discontinue business operations that cannot be made profitable, and to streamline other business segments in order to increase profitability.
92. Although Petitioners strongly believe that they are a global leader in their field with significant competitive advantages and a strong customer base, it is recognized that in the absence of these proceedings, it will be extremely difficult, if not impossible, to maintain value for all stakeholders, given the current liquidity problems and the pressures being brought to bear upon Petitioners by creditors and other stakeholders.
93. For instance, on April 16, 2008, Wachovia, Petitioner's main creditor and banker, sent a letter to Petitioners in which Wachovia stated, *inter alia*, that (i) Petitioners breached financial covenants under the Loan Agreement, (ii) it would increase its interest rate from Prime to Prime plus 2%, retroactive to April 1, 2008, and (iii) it would reduce the maximum dollar amount available on the revolving loan from \$25 million to \$12.5 million, hence creating a liquidity crisis, the whole as appears from a copy of said letter communicated herewith as **Exhibit R-17**.
94. Furthermore, since the beginning of the year, at least eight (8) suppliers (including Maison Brison, Standish Communications Inc., H. Paulin & Co. Limitée, Clearview Strategic Partners Inc., International Home Furnishings Centers, Rollins Accounting & Inventory Services Inc. and Lanart Rug Inc.) have sent demand letters or instituted proceedings to obtain payment of outstanding invoices.
95. For instance, on April 22, 2008, Standish Communications Inc. sent a demand letter to Shermag in which it requested payment of outstanding invoices totalling \$125,929.80 before 4:00 p.m. on April 24, 2008, failing which it would file a petition for bankruptcy

against Shermag without further notice, the whole as appears from a copy of said demand letter communicated herewith as **Exhibit R-18**.

96. On May 1<sup>st</sup>, 2008, Wachovia served upon Shermag, Jaymar and Scierie Notices of Intention to Enforce Security pursuant to Section 244 of the *Bankruptcy and Insolvency Act* (the “**Notices**”), the whole as appears from a copy of said Notices communicated herewith *en liasse* as **Exhibit R-19**.
97. On May 2, 2008, Shermag, Jaymar and Scierie acknowledged receipt of the Notices and waived the ten (10) day delay under said Notices, the whole as appears from **Exhibit R-19**.
98. In addition, some employees or former employees have claimed substantial amounts (approximately \$2.5 millions) either through demand letter or proceedings.
99. Petitioners, together with their advisors, continue to review restructuring alternatives. At this stage a restructuring within a court supervised process is necessary to ensure fair and equitable treatment for all stakeholders. Once the business is stabilized, Petitioners will be able to update this Court on its restructuring efforts and alternatives, including the Petitioners’ proposed plan(s) of arrangement.
100. Petitioners need to obtain the Court’s protection in Canada to ensure that it can continue to operate in the normal course of business and preserve the value of its assets as a going concern, for the benefit of all stakeholders.
101. Petitioners file in support hereof as **Exhibit R-20**, its cash flow projection, which have been prepared together with the proposed monitor.

## **8. FILING OF A PLAN OF ARRANGEMENT**

102. Petitioners have, as already explained hereinabove, began a restructuring process both for their operations and their financial situation.
103. Given the present situation, Petitioners have to conclude that the measures already undertaken or implemented are not sufficient.

104. Therefore, Petitioners together with their advisors are in the process of preparing a business plan, which will allow Petitioners to be profitable overtime. Such plan will probably include the following:
- (i) Disposing of redundant assets;
  - (ii) Reducing indebtedness; and
  - (iii) Reducing financial costs.
105. In order to be profitable, Petitioners will have to sell some of their assets, further restructure their operations and file a plan of arrangement with their creditors.
106. Although, Petitioners are not yet in a position to provide the details of a plan of arrangement to be submitted to their creditors, they are confident that, together with their advisors, they will be able to do so for the benefit of all stakeholders.
107. It is Petitioners' intent to continue to carry their operations, in a restructured matter, which will allow for the maintaining of a very large number of jobs.

**9. RELIEF SOUGHT**

108. RSM Richter Inc. (“RSM”), in its capacity as proposed monitor, will file in support this Petition a report dealing with the following issues:
- (i) current liquidity crisis;
  - (ii) commencement of formal insolvency proceedings;
  - (iii) cash-flow projections of Petitioners;
  - (iv) D&O and Administration Charges, and financial thresholds contemplated in the proposed order;
  - (v) key employee retention
  - (vi) restructuring options; and
  - (vii) conclusions and recommendations.

A copy of said report is communicated herewith as **Exhibit R-21**.

**9.1. FINANCING**

109. As it appears from Exhibit R-21, Petitioners have an immediate need for financing to meet obligations as they fall due and to stabilize operations while Petitioners consider all their restructuring options.
110. As such, Petitioners and Wachovia have agreed to maintain in full force and effect the Credit Facility pursuant to the terms of a Forbearance Agreement dated May 5, 2008.
111. The entering into of this Forbearance Agreement will provide Petitioners with enough financing to carry their operations through the initial stay period.

**9.2. D&O CHARGE**

112. A successful restructuring of Petitioners will only be possible with the continued participation of Petitioners' board of directors and their officers. These personnel are essential to the ongoing viability of Petitioners' business, and the successful restructuring thereof.
113. Even though Petitioners intend to comply with all applicable laws and regulations, Petitioners' directors and officers may nevertheless be concerned about the potential for their personal liability in the context of the present restructuring.
114. Absent the protections sought in the conclusions of the present Petition, Petitioners are concerned that their directors or officers will be advised to resign their posts, which would jeopardize the continuation of Petitioners' business operations, and its successful restructuring.
115. Accordingly, Petitioners request that the initial order to be granted pursuant hereto include the protections sought in the conclusions of the present Petition, namely, the orders related to the indemnification and charge in favour of the directors and officers of Shermag.

116. For the reasons set out herein, Petitioners seek a \$1.5 million D&O Charge, which shall charge all Petitioners' assets, the whole as set forth more fully under paragraphs 23 and 24 of the conclusions of the present Petition. The amount of the D&O Charge takes into account hourly and salaried payroll, sales commissions, vacation pay and sales taxes.
117. Petitioners already subscribed to a D&O insurance with a threshold of \$10 million. However, there is still a need for a D&O Charge.

**9.3. APPOINTMENT OF MONITOR**

118. Petitioners request that this Court appoint RSM as Monitor, in accordance with the provisions of the *CCAA* and the initial order to be rendered by the Court (the “**Monitor**”).
119. RSM has agreed to act as Court appointed Monitor to Petitioners.
120. In addition to any powers or obligations provided for by the *CCAA*, Petitioners hereby request that this Court grant the Monitor the powers, rights, obligations and protections detailed in the conclusions of the present Petition, namely the orders related to the Administration Charge.

**9.4. ADMINISTRATION CHARGE**

121. For the reasons set out herein, Petitioners seek an Administration Charge in an amount of \$500,000, which shall charge all Petitioners' assets, the whole as set forth more fully under paragraph 32 of the conclusions of the present Petition.

**9.5. KEY EMPLOYEE RETENTION PROGRAM**

122. Shermag's board of directors has expressed concern that certain employees, including and especially the senior management, may not remain with Petitioners during their restructuring efforts because of the uncertainty of their continued long-term employment, and Petitioners' financial situation.

123. A number of key employees (“**Key Employees**”) have been identified who possess unique professional skills and knowledge of Petitioners’ business and operations and who are and will continue to be important contributors to Petitioners’ successful restructuring.
124. It is believed that in view of the specific skillset and experience of the Key Employees many of them have already or will likely receive competitive employment offers.
125. Petitioners require the continued service and assistance of the Key Employees in order to maintain its assets and business and to complete its restructuring process.
126. After discussions with the proposed Monitor, Petitioners formulated a Retention Bonus Plan (the “**Retention Bonus Plan**”) designed to address the necessity of the continued employment of Key Employees, a copy of which will be filed under seal at the hearing of the present Petition as **Exhibit R-22**.
127. The Retention Bonus Plan provides for a retention bonus payable to the Key Employees, payable in three (3) equal installments, the first payment being in May 2008, the second in September 2008 and the last in January 2009.
128. The Retention Bonus Plan is designed to provide the necessary incentive for the Key Employees to remain with Petitioners throughout the restructuring with a view to preserving value for the stakeholders through positive contributions to the restructuring while taking into account Petitioners’ financial constraints.
129. The benefits provided by the Retention Bonus Plan were established after taking into consideration, *inter alia*, the relevance of the Key Employees to a successful restructuring, the nature of their employment and functions, and the risk that they Key Employees would seek alternate employment in the absence of such incentive program.
130. Payments provided for under the Retention Bonus Plan will only be made to the Key Employees who have fulfilled their employment obligations to Petitioners throughout the restructuring process, who have not resigned or been terminated for cause when each of the three (3) installments becomes due.

131. It is believed the terms of the Retention Bonus Plan are reasonable and essential to ensure the retention of the Key Employees and the completion of the Petitioners' restructuring to the benefit of its stakeholders.
132. In view of the sensitive and confidential nature of the Retention Bonus Plan and the fact that disclosure of its specific terms may negatively affect and be detrimental to the outcome of Petitioners' restructuring, and thereby cause prejudice to Petitioners and to their stakeholders, Petitioners hereby request an order that Exhibit R-22 remain under seal.
133. In order to ensure that the Retention Bonus Plan will be paid, particularly in view of the Petitioners' current circumstances and financial situation, Petitioners hereby request:
  - (i) an order for the establishment of a trust pursuant to which Petitioners will deposit an amount equivalent to the Retention Bonus in trust with the proposed Monitor, acting as agent of the trust (the "**Trust Funds**"), which amount will be disbursed by the proposed Monitor to the Key Employees pursuant to the Retention Bonus Plan;
  - (ii) a declaration that the establishment of such a trust, the deposit by Petitioners of amounts therein and the disbursements made by the proposed Monitor in relation thereto or made by Petitioners in relation to the Retention Bonus Plan, shall be binding on any trustee in bankruptcy that may be appointed in respect of Petitioners and shall not be void or voidable and shall not be deemed to be a settlement, fraudulent preference, assignment, fraudulent conveyance or other reviewable transaction under the *Bankruptcy and Insolvency Act*, Section 1631 and following of the *Civil Code of Québec* or any other applicable federal or provincial legislation; and
  - (iii) a declaration that, to the extent that one or more Key Employees is no longer at the employ of Petitioners at the time where the payment of the Retention Bonus Plan has to be made, any Trust Funds not used for the payment of the Retention

Bonus Plan to the Key Employees shall be remitted to Petitioners and remain subject to the security held by Petitioners' secured lenders.

**9.6. POSTPONEMENT OF ANNUAL MEETING OF SHAREHOLDERS**

134. Shermag is a company incorporated under the *Companies Act* (Québec) and is required to call its next annual meeting of shareholders ("AMS") no later than July 31, 2008.
135. Shermag is presently devoting its efforts on stabilizing its business and returning it to a business as usual status with a view to preparing a business and financial plan for its business and eventually formulating one or more restructuring plans to maximize long term value for the benefit of all stakeholders.
136. Preparing and holding an AMS would divert the attention of senior management away from such tasks, would require significant resources and could impede Shermag's ability to achieve its restructuring under the *CCAA*.
137. Financial and other information will be available to the public through Petitioners' Court filings which are easily accessible on the Monitor's website, and other public records for the disclosure of documents of public companies.
138. Under these circumstances, it is impracticable for Shermag to prepare and hold an AMS during these proceedings and the Court has the authority to extend the time of calling of the AMS.

**9.7. CASH MANAGEMENT SYSTEM**

139. In order to ensure that Petitioners can continue to have access to the existing bank accounts and cash management system, Petitioners seek the relief set forth more fully at paragraphs 8(d) and 9 of the conclusions of the present Petition.



**10. CONCLUSIONS**

140. The initial order being sought by Petitioners is based on the standard form of *CCAA* Order of the Superior Court of Québec, Commercial Division, with changes that will be identified to this Court by counsel for Petitioners.
141. The filing and presentation of this Petition has been approved by the Directors of each of the Petitioners in accordance with the rules, regulations and by-laws governing each of such Petitioners.
142. For the reasons explained above, Petitioners believe it is both appropriate and necessary that the relief being sought be granted. With such relief, Petitioners will be able to restructure their business and affairs to maximize long term value for the benefit of all stakeholders.
143. Considering the urgency of the situation, Petitioners respectfully submit that the notices given of the presentation of the present Petition are proper and sufficient.
144. Petitioners respectfully submit that Petition should be granted in accordance with its conclusions.
145. The present Petition is well founded in fact and law.

**WHEREFORE MAY IT PLEASE THIS HONOURABLE COURT TO:**

1. GRANT the Petition.
2. ISSUE an order pursuant to Sections 4, 5 and 11 of the *CCAA* (the “**Order**”), divided under the following headings:
  - Service
  - Application of the *CCAA*
  - Effective Time
  - Plan of Arrangement
  - Stay of Proceedings against the Petitioners, the Property, the Directors or others

- Possession of Property and Carrying on Business
- Restructuring
- Directors Indemnification and Charge
- Powers of the Monitor
- Priorities and General Provisions Relating to *CCAA* Charges
- Retention Bonus Plan
- Postponement of Annual Meeting of Shareholders
- General

### **Service**

3. EXEMPT Shermag Inc., Jaymar Furniture Corp., Scierie Montauban Inc., Mégaboïs (1989) Inc., Shermag Corporation and Jaymar Sales Corporation (the “**Petitioners**”) from having to serve the Petition and from any notice of presentation.

### **Application of the *CCAA***

4. DECLARE that Petitioners are a debtor company to which the *CCAA* applies.

### **Effective time**

5. DECLARE that from immediately after midnight (Montréal time) on the day prior to the Order (the “**Effective Time**”) to the time of the granting of the Order, any act or action taken or notice given by any Person in respect of Petitioners, the Directors or the Property (as those terms are defined hereinafter), are deemed not to have been taken or given, as the case may be, to the extent such act, action or notice would otherwise be stayed after the granting of the Order.

### **Plan of Arrangement**

6. ORDER that Petitioners file with this Court and submit to its creditors one or more plans of compromise or arrangement under the *CCAA* (collectively, the “**Plan**”) between, among others, Petitioners and one or more classes of its creditors as Petitioners may

deem appropriate, on or before the Stay Termination Date (as defined hereinafter) or such other time or times as may be allowed by this Court.

**Stay of Proceedings against the Petitioners, the Property, the Directors or others**

7. ORDER that, until and including June 4, 2008, or such later date as the Court may order (the “**Stay Termination Date**”, the period from the date of the Order to the Stay Termination Date being referred to as the “**Stay Period**”), no right, legal or conventional, may be exercised and no proceeding, at law or under a contract, by reason of this Order or otherwise, however and wherever taken (collectively the “**Proceedings**”) may be commenced or proceeded with by anyone, whether a person, firm, partnership, corporation, stock exchange, government, administration or entity exercising executive, legislative, judicial, regulatory or administrative functions (collectively, “**Persons**” and, individually, a “**Person**”) against or in respect of Petitioners, or any of the present or future property, assets, rights and undertakings of Petitioners, of any nature and in any location, whether held directly or indirectly by Petitioners, in any capacity whatsoever, or held by others for Petitioners (collectively, the “**Property**”), and all Proceedings already commenced against Petitioners or any of the Property, are stayed and suspended until the Court authorizes the continuation thereof, the whole subject to the provisions of the *CCAA*.
8. ORDER that, without limiting the generality of the foregoing, during the Stay Period, all Persons having agreements, contracts or arrangements with Petitioners or in connection with any of the Property, whether written or oral, for any subject or purpose:
  - (a) are restrained from accelerating, terminating, cancelling, suspending, refusing to modify or extend on reasonable terms such agreements, contracts or arrangements or the rights of Petitioners or any other Person thereunder;
  - (b) are restrained from modifying, suspending or otherwise interfering with the supply of any goods, services, or other benefits by or to such Person thereunder (including, without limitation, any directors’ and officers’ insurance, any

telephone numbers, any form of telecommunications service, any oil, gas, electricity or other utility supply);

- (c) are restrained from interfering or retaining in any manner the delivery of any goods by or to the Petitioners, so long as Petitioners pay the prices or charges for the services rendered by such Persons for the services received after the date of the Order as such prices or charges become due in accordance with the law or as may be hereafter negotiated;
- (d) shall continue to perform and observe the terms and conditions contained in such agreements, contracts or arrangements, so long as Petitioners pay the prices or charges for such goods and services received after the date of the Order as such prices or charges become due in accordance with the law or as may be hereafter negotiated (other than deposits whether by way of cash, letter of credit or guarantee, stand-by fees or similar items which Petitioners shall not be required to pay or grant), unless the prior written consent of Petitioners and the Monitor is obtained or the leave of this Court is granted; and
- (e) shall, subject to the rights of Wachovia Capital Finance Corporation (Canada) (the “**Lender**”), continue to operate bank services and accounts currently in place and available to Petitioners at the Bank of Montreal (“**BMO**”) (the “**Accounts**”) in accordance with existing banking services agreements, are restrained from stopping, withholding, redirecting or otherwise interfering with any amount in the Accounts or setting off (subject to paragraph 9 hereof) or applying amounts in the Accounts against any indebtedness owing to it by any of Petitioners, or from discontinuing, failing to renew on terms no more onerous than those existing prior to these proceedings, altering, interfering with or terminating existing related banking arrangements, and shall continue to honour debits and cheques (including those already in circulation at the date of the Order) drawn on the Accounts, unless otherwise directed by Petitioners and the Monitor, in each case provided that there are sufficient funds in the relevant

Account for such debit items or cheques, or other reasonable assurances of payments are provided to BMO.

9. ORDER that, without limiting the generality of the foregoing and subject to the rights of the Lender and Section 18.1 of the *CCAA*, if applicable, cash or cash equivalents placed on deposit by Petitioners with any Person during the Stay Period, whether in an operating account or otherwise for itself or for another entity, shall not be applied by such Person in reduction or repayment of amounts owing to such Person as of the date of the Order or due on or before the expiry of the Stay Period or in satisfaction of any interest or charges accruing in respect thereof; however, this provision shall not prevent any financial institution from: (i) reimbursing itself for the amount of any cheques drawn by Petitioners and properly honoured by such institution, or (ii) holding the amount of any cheques or other instruments deposited into Petitioners' account until those cheques or other instruments have been honoured by the financial institution on which they have been drawn.
10. ORDER that, notwithstanding the foregoing, any Person who provided any kind of letter of credit, bond or guarantee (the "**Issuing Party**") at the request of Petitioners shall be required to continue honouring any and all such letters, bonds and guarantees, issued on or before the date of the Order; however, the Issuing Party shall be entitled, where applicable, to retain the bills of lading or shipping or other documents relating thereto until paid therefore.
11. DECLARE that, to the extent any rights, obligations, or time or limitation periods, including, without limitation, to file grievances, relating to Petitioners or any of the Property may expire, other than the term of any lease of real property, the term of such rights or obligations, or time or limitation periods shall hereby be deemed to be extended by a period equal to the Stay Period. Without limitation to the foregoing, in the event that Petitioners becomes bankrupt or a receiver within the meaning of paragraph 243(2) of the *Bankruptcy and Insolvency Act (Canada)* (the "**BIA**") is appointed in respect of Petitioners, the period between the date of the Order and the day on which the Stay

Period ends shall not be calculated in respect of Petitioners in determining the 30-day periods referred to in Sections 81.1 and 81.2 of the *BIA*.

12. ORDER that no Person may commence, proceed with or enforce any Proceedings against any former, present or future director or officer of Petitioners or any person that, by applicable legislation, is treated as a director of Petitioners or that will manage in the future the business and affairs of Petitioners (each, a “**Director**”, and collectively the “**Directors**”) in respect of any claim against such Director that arose before this Order was issued and that relates to obligations of Petitioners for which such Director is or is alleged to be liable (as provided under Section 5.1 of the *CCAA*) until further order of this Court or until the Plan, if one is filed, is sanctioned by the Court or is refused by the creditors or is not sanctioned by the Court.
13. ORDER that no Person shall commence, proceed with or enforce any Proceedings against any of the Directors, officers, employees, legal counsel or financial advisers of Petitioners or the Monitor, for or in respect of the Restructuring (as defined hereinafter) or the formulation and implementation of the Plan without first obtaining leave of this Court, upon seven days written notice to Petitioner’s *ad litem* counsel and to all those referred to in this paragraph whom it is proposed be named in such Proceedings.
14. ORDER that notwithstanding anything herein contained to the contrary:
  - (a) the Lender will not be subject to, or affected by, any stay of proceedings, including, without limitation, those provided for under paragraphs 7, 8 and 9 of the Order, in favour of the Petitioners under the Order, the *CCAA*, the filing of any notice of intention to file a proposal under the *BIA* or a proposal under the *BIA*;
  - (b) any and all claims and rights of the Lender shall not be compromised or arranged pursuant to any Plan or under any proposal to be filed by the Petitioners pursuant to the *BIA*;
  - (c) the Lender shall be treated as an unaffected creditor in any *CCAA* proceedings or Plan, or any proposal filed by the Petitioners pursuant to the *BIA*; and

- (d) the Monitor is authorized to disclose directly to the Lender upon reasonable request any and all information obtained by the Monitor in relation to the Petitioners' restructuring process, to answer all reasonable questions and perform any reasonable verification requested from time to time by the Lender and will provide to the Lender a copy of all Monitor's reports to be filed in Court, the whole without the requirement of any further authorization by the Petitioners and at the Petitioners' expense. Petitioners shall be informed by the Monitor, acting reasonably, of any and all information provided to the Lender.
15. ORDER that, notwithstanding any other provision of the Order, the Petitioners be and are hereby authorized to borrow, repay and reborrow from the Lender such amounts from time to time in accordance with the terms and conditions set forth in the Forbearance Agreement agreed to and accepted by the Petitioners on May 5, 2008, under such security as already exists or may hereinafter be created in favour of the Lender and which will not be affected hereby. All such security will secure all obligations to date or hereafter created in the same manner as if the Order had never been granted.

**Possession of Property and Carrying on Business**

16. ORDER that, subject to the terms of the Order, Petitioners shall remain in possession of the Property until further order in these proceedings.
17. ORDER that Petitioners shall continue to carry on its business and financial affairs in a manner consistent with the commercially reasonable preservation thereof.

**Restructuring**

18. DECLARE that, to facilitate the orderly restructuring of its business and financial affairs (the "**Restructuring**"), Petitioners shall have the right, subject to approval of the Monitor or further order of the Court, to:
- (a) permanently or temporarily cease, downsize or shut down any of its operations or locations as it deems appropriate and make provision for the consequences thereof in the Plan;

- (b) pursue all avenues to market and sell, subject to subparagraph (c), the Property, in whole or part;
- (c) convey, transfer, assign, lease, or in any other manner dispose of the Property, in whole or in part, provided that the price in each case does not exceed \$900,000 or \$5,000,000 in the aggregate with the specific exclusion of (i) the liquidation of the inventory located in the Montreal distribution center and (ii) the sale of the sawmill located in Notre-Dame-de-Montauban which shall not require any authorization;
- (d) terminate the employment of such of its employees or temporarily or permanently lay off such of its employees already laid-off employees as it deems appropriate and, to the extent any amounts in lieu of notice, termination or severance pay or other amounts in respect thereof are not paid in the ordinary course, make provision for any consequences thereof in the Plan, as Petitioners may determine;
- (e) subject to paragraphs 20 and 21 hereof, vacate or abandon any leased real property or repudiate any lease and ancillary agreements related to any leased premises as it deems appropriate, provided that Petitioners gives the relevant landlord at least seven days prior written notice, on such terms as may be agreed between Petitioners and such landlord, or failing such agreement, to make provision for any consequences thereof in the Plan; and
- (f) repudiate such of its agreements, contracts or arrangements of any nature whatsoever, whether oral or written, as it deems appropriate, on such terms as may be agreed between Petitioners and the relevant party, or failing such agreement, to make provision for the consequences thereof in the Plan and to negotiate any amended or new agreements or arrangements.

19. DECLARE that, in order to facilitate the Restructuring, Petitioners may, subject to approval of the Monitor:

- (a) settle claims of customers and suppliers that are in dispute; and



- (b) establish a plan for the retention of key employees and the making of retention payments or bonuses in connection therewith.
20. DECLARE that, if leased premises are vacated or abandoned by Petitioners pursuant to subparagraph 18(e), the landlord may take possession of any such leased premises without waiver of, or prejudice to, any claims or rights of the landlord against Petitioners, provided the landlord mitigates its damages, if any, and re-leases any such leased premises to third parties on such terms as any such landlord may determine.
21. ORDER that Petitioners shall provide to any relevant landlord notice of Petitioner's intention to remove any fixtures or leasehold improvements at least seven days in advance. If Petitioners has already vacated the leased premises, it shall not be considered to be in occupation of such location pending the resolution of any dispute.
22. DECLARE that, pursuant to sub-paragraph 7(3)(c) of the *Personal Information Protection and Electronic Documents Act*, S.C. 2000, c.5, Petitioners are permitted, in the course of these proceedings, to disclose personal information of identifiable individuals in its possession or control to stakeholders or prospective investors, financiers, buyers or strategic partners and to its advisers (individually, a "**Third Party**"), but only to the extent desirable or required to negotiate and complete the Restructuring or the preparation and implementation of the Plan or a transaction for that purpose, provided that the Persons to whom such personal information is disclosed enter into confidentiality agreements with Petitioners binding them to maintain and protect the privacy of such information and to limit the use of such information to the extent necessary to complete the transaction or Restructuring then under negotiation. Upon the completion of the use of personal information for the limited purpose set out herein, the personal information shall be returned to Petitioners or destroyed. In the event that a Third Party acquires personal information as part of the Restructuring or the preparation and implementation of the Plan or a transaction in furtherance thereof, such Third Party may continue to use the personal information in a manner which is in all respects identical to the prior use thereof by Petitioners.

### **Directors Indemnification and Charge**

23. ORDER that, in addition to any existing indemnities, Petitioners shall indemnify each of the Directors from and against the following (collectively, “**D&O Claims**”):

- (a) all costs (including, without limitation, full defence costs), charges, expenses, claims, liabilities and obligations, of any nature whatsoever, which may arise on or after the date of the Order relating to acts, omissions or circumstance which occurred after the Effective Time (including, without limitation, an amount paid to settle an action or a judgment in a civil, criminal, administrative or investigative action or proceeding to which a Director may be made a party), provided that any such liability relates to such Director in that capacity, and, provided that such Director (i) acted honestly and in good faith in the best interests of Petitioners and (ii) in the case of a criminal or administrative action or proceeding in which such Director would be liable to a monetary penalty, such Director had reasonable grounds for believing his or her conduct was lawful, except if such Director has actively breached any fiduciary duties or has been grossly negligent or guilty of wilful misconduct; and
- (b) all costs, charges, expenses, claims, liabilities and obligations relating to the failure of Petitioners to make any payments or to pay amounts in respect of employee or former employee entitlements to wages, vacation pay, termination pay, severance pay, pension or other benefits, in each case accruing and falling due after, or any other amount for services performed on or after the date of the Order and that such Directors sustain, by reason of their association with Petitioners as a Director, except to the extent that they have actively breached any fiduciary duties or have been grossly negligent or guilty of wilful misconduct.

The foregoing shall not constitute a contract of insurance or other valid and collectible insurance, as such term may be used in any existing policy of insurance issued in favour of Petitioners or any of the Directors.

24. DECLARE that, as security for the obligation of Petitioners to indemnify the Directors pursuant to paragraph 23 hereof, the Directors are hereby granted a hypothec on, mortgage of, lien on and security interest in the Property to the extent of the aggregate amount of \$1,500,000 (the “**D&O Charge**”), having the priority established by paragraphs 33 and 34 hereof. Such D&O Charge shall not constitute or form a trust. Such D&O Charge, notwithstanding any language in any applicable policy of insurance to the contrary, shall only apply to the extent that the Directors do not have coverage under any directors’ and officers’ insurance, which shall not be excess insurance to the D&O Charge. In respect of any D&O Claim against any of the Directors (collectively, the “**Respondent Directors**”), if such Respondent Directors do not receive confirmation from the applicable insurer within 21 days of delivery of notice of the D&O Claim to the applicable insurer, confirming that the applicable insurer will provide coverage for and indemnify the Respondent Directors, then, without prejudice to the subrogation rights hereinafter referred to, Petitioners shall pay the amount of the D&O Claim upon expiry. Failing such payment, the Respondent Directors may enforce the D&O Charge provided that the Respondent Directors shall reimburse Petitioners to the extent that they subsequently receive insurance benefits for the D&O Claim paid by Petitioners, and provided further that Petitioners shall, upon payment, be subrogated to the rights of the Respondent Directors to recover payment from the applicable insurer as if no such payment had been made.

#### **Powers of the Monitor**

25. ORDER that RSM Richter Inc. is hereby appointed to monitor the business and financial affairs of Petitioners as an officer of this Court (the “**Monitor**”) and that the Monitor shall, in addition to the duties and functions referred to in Section 11.7 of the *CCAA*:
- (a) send notice of the Order, within 10 days, to every known creditor of Petitioners having a claim of more than \$250 against it, advising that such creditor may obtain a copy of the Order on the internet at the website of the Monitor (the “**Website**”) or, failing that, from the Monitor and the Monitor shall so provide

it. Such notice shall be sufficient in accordance with Subsection 11(5) of the *CCAA*;

- (b) assist Petitioners, to the extent required by Petitioners, in dealing with its creditors and other interested Persons during the Stay Period;
- (c) assist Petitioners, to the extent required by Petitioners, with the preparation of its cash flow projections and any other projections or reports and the development, negotiation and implementation of the Plan;
- (d) advise and assist Petitioners, to the extent required by Petitioners, to review Petitioner's business and assess opportunities for cost reduction, revenue enhancement and operating efficiencies;
- (e) assist Petitioners, to the extent required by Petitioners, with the Restructuring and in its negotiations with its creditors and other interested Persons and with the holding and administering of any meetings held to consider the Plan;
- (f) report to the Court on the state of the business and financial affairs of Petitioners or developments in these proceedings or any related proceedings within the time limits set forth in the *CCAA* and at such time as considered appropriate by the Monitor or as the Court may order;
- (g) report to this Court and interested parties, including but not limited to creditors affected by the Plan, with respect to the Monitor's assessment of, and recommendations with respect to, the Plan;
- (h) retain and employ such agents, advisers and other assistants as are reasonably necessary for the purpose of carrying out the terms of the Order, including, without limitation, one or more entities related to or affiliated with the Monitor;
- (i) engage legal counsel to the extent the Monitor considers necessary in connection with the exercise of its powers or the discharge of its obligations in these proceedings and any related proceeding, under the Order or under the *CCAA*;

- (j) may act as a “foreign representative” of Petitioners in any proceedings outside of Canada;
- (k) may give any consent or approval as are contemplated by the Order; and
- (l) perform such other duties as are required by the Order, the *CCAA* or this Court from time to time.

The Monitor shall not otherwise interfere with the business and financial affairs carried on by Petitioners, and the Monitor is not empowered to take possession of the Property nor to manage any of the business and financial affairs of Petitioners.

26. ORDER that Petitioners and its directors, officers, employees and agents, accountants, auditors and all other Persons having notice of the Order shall forthwith provide the Monitor with unrestricted access to all of the Property, including, without limitation, the premises, books, records, data, including data in electronic form, and all other documents of Petitioners in connection with the Monitor’s duties and responsibilities hereunder.
27. DECLARE that the Monitor may provide creditors and other relevant stakeholders of Petitioners with information in response to requests made by them in writing addressed to the Monitor and copied to Petitioner’s counsel. The Monitor shall not have any duties or liabilities in respect of such information disseminated by it pursuant to the provisions of the Order or the *CCAA*, other than as provided in paragraph 29 hereof. In the case of information that the Monitor has been advised by Petitioners or the Lender is confidential, proprietary or competitive, the Monitor shall not provide such information to any Person without the consent of Petitioners or the Lender, as the case may be, unless otherwise directed by this Court.
28. DECLARE that the Monitor shall not be, nor be deemed to be, an employer or a successor employer of the employees of Petitioners or a related employer in respect of Petitioners within the meaning of any federal, provincial or municipal legislation governing employment, labour relations, pay equity, employment equity, human rights, health and safety or pensions or any other statute, regulation or rule of law or equity for any similar purpose and, further, that the Monitor shall not be, nor be deemed to be, in

occupation, possession, charge, management or control of the Property or business and financial affairs of Petitioners pursuant to any federal, provincial or municipal legislation, statute, regulation or rule of law or equity which imposes liability on the basis of such status, including, without limitation, the *Environment Quality Act* (Québec), the *Canadian Environmental Protection Act, 1999* or the *Act Respecting Occupational Health and Safety* (Québec) or similar other federal or provincial legislation.

29. DECLARE that, in addition to the rights and protections afforded to the Monitor by the CCAA, the Order or its status as an officer of the Court, the Monitor shall not incur any liability or obligation as a result of its appointment and the fulfilment of its duties or the provisions of the Order, save and except any liability or obligation arising from the gross negligence or wilful misconduct, and no action or other proceedings shall be commenced against the Monitor relating to its appointment, its conduct as Monitor or the carrying out the provisions of any order of this Court, except with prior leave of this Court, on at least seven days notice to the Monitor and its counsel. The entities related to or affiliated with the Monitor referred to in subparagraph 25(h) hereof shall also be entitled to the protection, benefits and privileges afforded to the Monitor pursuant to this paragraph.
30. ORDER that Petitioners shall pay the fees and disbursements of the Monitor, the Monitor's legal counsel, Petitioner's legal counsel and other advisers, incurred in connection with or with respect to the Restructuring, whether incurred before or after the Order, and shall provide each with a reasonable retainer in advance on account of such fees and disbursements, if so requested.
31. ORDER that the Petitioners will make the necessary arrangements for the receipt of the invoices of the above-mentioned professionals on a weekly basis, but no later than every second week, and ORDER Petitioners to pay such invoices within three (3) business days of their receipt.
32. DECLARE that the Monitor, the Monitor's legal counsel, the Petitioner's legal counsel and other advisers, as security for the professional fees and disbursements incurred both before and after the making of the Order in respect of these proceedings, the Plan and the Restructuring, in addition to the retainers referred to paragraph 30 hereof, be entitled to

the benefit of and are hereby granted a hypothec on, mortgage of, lien on, and security interest in the Property to the extent of the aggregate amount of \$500,000 (the “**Administration Charge**”), having the priority established by paragraphs 33 and 34 hereof.

**Priorities and General Provisions Relating to CCAA Charges**

33. DECLARE that the priorities of the Administration Charge and D&O Charge (collectively, the “**CCAA Charges**”), as between them with respect to any Property to which they apply, shall be as follows:
  - (a) first, the Administration Charge; and
  - (b) second, the D&O Charge;
34. DECLARE that each of the CCAA Charges shall rank in priority to any and all other hypothecs, mortgages, liens, security interests, priorities, conditional sale agreements, financial leases, charges, encumbrances or security of whatever nature or kind (collectively, “**Encumbrances**”) affecting any of the Property.
35. ORDER that, except as otherwise expressly provided for herein, Petitioners shall not grant any Encumbrances in or against any Property that rank in priority to, or *pari passu* with, any of the CCAA Charges unless Petitioners obtain the prior written consent of the Monitor and the prior approval of the Court.
36. DECLARE that each of the CCAA Charges shall attach, as of the Effective Time of the Order, to all present and future Property of Petitioners, notwithstanding any requirement for the consent of any party to any such charge or to comply with any condition precedent.
37. DECLARE that the CCAA Charges and the rights and remedies of the beneficiaries of such Charges, as applicable, shall be valid and enforceable and shall not otherwise be limited or impaired in any way by: (i) these proceedings and the declaration of insolvency made herein; (ii) any petition for a receiving order filed pursuant to the BIA in respect of Petitioners or any receiving order made pursuant to any such petition or any assignment

in bankruptcy made or deemed to be made in respect of Petitioners; or (iii) any negative covenants, prohibitions or other similar provisions with respect to borrowings, incurring debt or the creation of Encumbrances, contained in any agreement, lease, sub-lease, offer to lease or other arrangement which binds Petitioners(a “**Third Party Agreement**”), and notwithstanding any provision to the contrary in any Third Party Agreement:

- (a) the creation of any of the *CCAA* Charges shall not create or be deemed to constitute a breach by Petitioners of any Third Party Agreement to which it is a party; and
- (b) any of the beneficiaries of the *CCAA* Charges shall not have liability to any Person whatsoever as a result of any breach of any Third Party Agreement caused by or resulting from the creation of the *CCAA* Charges.

38. DECLARE that notwithstanding: (i) these proceedings and any declaration of insolvency made herein, (ii) any petition for a receiving order filed pursuant to the *BIA* in respect of Petitioners and any receiving order allowing such petition or any assignment in bankruptcy made or deemed to be made in respect of Petitioners, and (iii) the provisions of any federal or provincial statute, the payments or disposition of Property made by Petitioners pursuant to the Order and the granting of the *CCAA* Charges, do not and will not constitute settlements, fraudulent preferences, fraudulent conveyances or other challengeable or reviewable transactions or conduct meriting an oppression remedy under any applicable law.
39. DECLARE that the *CCAA* Charges shall be valid and enforceable as against all Property of Petitioners and against all Persons, including, without limitation, any trustee in bankruptcy, receiver, receiver and manager or interim receiver of Petitioners, for all purposes.

#### **Retention Bonus Plan**

40. APPROVE the Retention Bonus Plan, Exhibit R-22;



41. AUTHORIZE Petitioners to perform their obligations thereunder, including the making of any and all payments provided therein in accordance with the terms thereof;
42. AUTHORIZE Petitioners to execute and deliver any such additional or ancillary documents as may be necessary to give effect to the Retention Bonus Plan;
43. ESTABLISH a trust pursuant to which Petitioners will deposit an amount equivalent to the Retention Bonus Plan in trust with the Monitor , acting as trustee of the trust (the “**Trust Funds**”), which amount will be disbursed by the Monitor to the Key Employees pursuant to the Retention Bonus Plan;
44. DECLARE that the establishment of such a trust, the deposit by Petitioners of amounts therein and the disbursements made by the Monitor in relation thereto or made by Petitioners in relation to the Retention Bonus Plan, shall be binding on any trustee in bankruptcy that may be appointed in respect of Petitioners and shall not be void or voidable and shall not be deemed to be a settlement fraudulent preference, assignment, fraudulent conveyance or other reviewable transaction under the *Bankruptcy and Insolvency Act*, Section 1631 and following of the *Civil Code of Québec* or any other applicable federal or provincial legislation;
45. DECLARE that, to the extent that one or more Key Employees is no longer at the employ of Petitioners when the payments become due pursuant to the Retention Bonus Plan, any Trust Funds not used for the payment of the Retention Bonus to the Key Employees shall be remitted to Petitioners and remain subject to the security held by Petitioners’ secured lenders;
46. ORDER the sealing of the Retention Bonus Plan, Exhibit R-22;

**Postponement of Annual Meeting of Shareholders**

47. ORDER that Shermag be relieved of any obligation (i) to call and hold an annual meeting of shareholders on or before July 31, 2008, and (ii) to prepare any related documents, including the year-end financial statements, the Management’s Information Circular and

the Annual Information Form, which would otherwise be given or communicated in the context of said annual meeting of shareholders;

48. ORDER that Shermag be directed to hold its annual meeting of shareholders within three (3) months following the Stay Termination Date, as can be extended from time to time by orders of the Court;

### **General**

49. DECLARE that the Order and any proceeding or affidavit leading to the Order, shall not, in and of themselves, constitute a default or failure to comply by Petitioners under any statute, regulation, licence, permit, contract, permission, covenant, agreement, undertaking or other written document or requirement.
50. DECLARE that, except as otherwise specified herein, Petitioners are at liberty to serve any notice, proof of claim form, proxy, circular or other document in connection with these proceedings by forwarding copies by prepaid ordinary mail, courier, personal delivery or electronic transmission to Persons or other appropriate parties at their respective given addresses as last shown on the records of Petitioners and that any such service shall be deemed to be received on the date of delivery if by personal delivery or electronic transmission, on the following business day if delivered by courier, or three business days after mailing if by ordinary mail.
51. DECLARE that Petitioners and the Lender may serve any court materials in these proceedings on all represented parties electronically, by emailing a PDF or other electronic copy of such materials to counsels' email addresses, provided that Petitioners shall deliver "hard copies" of such materials upon request to any party as soon as practicable thereafter.
52. DECLARE that any party in these proceedings, other than Petitioners, may serve any court materials electronically, by emailing a PDF or other electronic copy of all materials to counsels' email addresses, provided that such party shall deliver both PDF or other electronic copies and "hard copies" of all materials to counsel to Petitioners (Davies

Ward Phillips & Vineberg LLP, c/o Denis Ferland and Christian Lachance) and the Monitor and to any other party requesting same.

53. DECLARE that, unless otherwise provided herein or ordered by this Court, no document, order or other material need be served on any Person in respect of these proceedings, unless such Person has served a Notice of Appearance on the solicitors for Petitioners (Davies Ward Phillips & Vineberg LLP, c/o Denis Ferland and Christian Lachance), the Monitor and the Lender (McMillan Binch Mendelsohn LLP, c/o Max Mendelsohn and Marc-André Morin) and has filed such notice with this Court.
54. DECLARE that Petitioners or the Monitor may, from time to time, apply to this Court for directions concerning the exercise of their respective powers, duties and rights hereunder or in respect of the proper execution of the Order on notice only to each other.
55. DECLARE that any interested Person may apply to this Court to vary or rescind the Order or seek other relief upon seven days notice to Petitioners (Davies Ward Phillips & Vineberg LLP, c/o Denis Ferland and Christian Lachance), the Monitor, the Lender (McMillan Binch Mendelsohn LLP, c/o Max Mendelsohn and Marc-André Morin) and to any other party likely to be affected by the order sought or upon such other notice, if any, as this Court may order.
56. DECLARE that the Order and all other orders in these proceedings shall have full force and effect in all provinces and territories in Canada.
57. DECLARE that the Monitor, with the prior consent of Petitioners, shall be authorized to apply as it may consider necessary or desirable, with or without notice, to any other court or administrative body, whether in Canada, the United States of America or elsewhere, for orders which aid and complement the Order and any subsequent orders of this Court and, without limitation to the foregoing, an order under section 304 of the *U.S. Bankruptcy Code*, for which the Monitor shall be the foreign representative of Petitioners. All courts and administrative bodies of all such jurisdictions are hereby respectively requested to make such orders and to provide such assistance to the Monitor as may be deemed necessary or appropriate for that purpose.

58. REQUEST the aid and recognition of any Court or administrative body in any Province of Canada and any Canadian federal court or administrative body and any federal or state court or administrative body in the United States of America and any court or administrative body elsewhere, to act in aid of and to be complementary to this Court in carrying out the terms of the Order.
59. ORDER the provisional execution of the Order notwithstanding any appeal and without the necessity of furnishing any security.
60. THE WHOLE without costs.

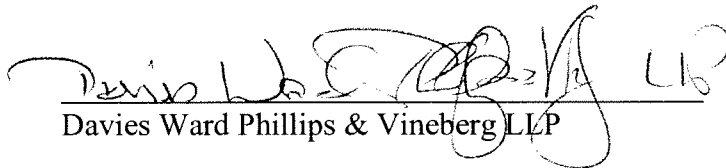
MONTREAL, May 5, 2008

(s) Davies Ward Phillips & Vineberg

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**DAVIES WARD PHILLIPS & VINEBERG LLP**  
Attorneys for Petitioners Shermag Inc., Jaymar  
Furniture Corp., Scierie Montauban Inc., Mégabois  
(1989) Inc., Shermag Corporation and Jaymar Sales  
Corporation

TRUE COPY

  
\_\_\_\_\_  
Davies Ward Phillips & Vineberg LLP

CANADA  
PROVINCE OF QUÉBEC  
DISTRICT OF MONTRÉAL

No.: 500-11-

**S U P E R I O R C O U R T**  
(Commercial Division)  
(Sitting as a court designated pursuant to the  
*Companies' Creditors Arrangement Act*,  
R.S.C. 1985, c. C-36)

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

**SHERMAG INC.**

and

**JAYMAR FURNITURE CORP.**

and

**SCIERIE MONTAUBAN INC.**

and

**MÉGABOIS (1989) INC.**

and

**SHERMAG CORPORATION**

and

**JAYMAR SALES CORPORATION**

Petitioners

and

**RSM RICHTER INC.**

Monitor

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**ATTESTATION OF AUTHENTICITY**

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I, the undersigned, Christian Lachance, attorney, practising my profession with the law firm of Davies Ward Phillips & Vineberg LLP, having its principal place of business at 1501 McGill College Avenue, 26<sup>th</sup> Floor, in the City and District of Montréal, Province of Québec, solemnly affirm that:

1. On May 5, 2008, at 10:51 a.m., Davies Ward Phillips & Vineberg LLP received by fax an Affidavit signed by Josée Girard dated May 5, 2008, a copy of such Affidavit is attached to this Attestation of Authenticity.

2. All the facts alleged herein are true.

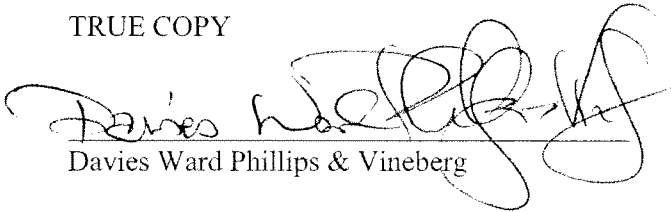
**AND I HAVE SIGNED:**

(s) Christian Lachance  
\_\_\_\_\_  
CHRISTIAN LACHANCE

**SOLEMNLY AFFIRMED BEFORE ME,** at  
Montréal, on this 5<sup>th</sup> day of May, 2008.

(s) Lyne Levasseur (#102,612)  
\_\_\_\_\_  
Commissioner for Oaths for all  
judicial districts of Québec

TRUE COPY

  
\_\_\_\_\_  
Davies Ward Phillips & Vineberg

**AFFIDAVIT**

I, the undersigned, JOSÉE GIRARD, Vice-President Finance of Shermag Inc., having my place of business at 2171 King Street West, in the City of Sherbrooke, Province of Québec, solemnly declare as follows:

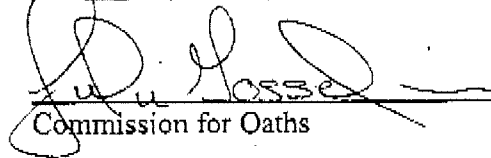
1. I am the duly authorized representative of the Petitioners;
2. All the facts contained in the present Petition for an Initial Order Pursuant to Sections 4, 5 and 11 of the *Companies' Creditors Arrangement Act* are true;
3. All the facts contained in this Affidavit are true.

AND I HAVE SIGNED:

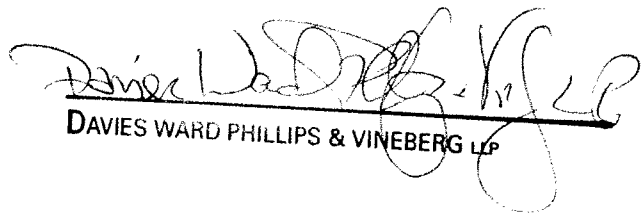


\_\_\_\_\_  
JOSÉE GIRARD

Solemnly affirmed before me, in the City of Sherbrooke, Province of Québec, this 5 day of May, 2008

  
\_\_\_\_\_  
Commission for Oaths

**TRUE COPY**

  
\_\_\_\_\_  
DAVIES WARD PHILLIPS & VINEBERG LLP

**NOTICE OF PRESENTATION**

TO: Me Max Mendelsohn  
Me Marc-André Morin  
Me Nicholas Scheib  
**McMillan Binch Mendelsohn LLP**  
1000 Sherbrooke Ouest/West, Suite 2700  
Montréal (Québec) Canada H3A 3G4

Attorneys for Wachovia Capital Finance of Canada

AND TO: Mr. Phil Manel, CA  
**RSM Richter Inc.**  
2 Place Alexis Nihon, Suite 2200  
Montreal, Quebec, H3Z 3C2

Proposed Monitor

**TAKE NOTICE** that the present Petition for an Initial Order Pursuant to Sections 4, 5 and 11 of the *Companies' Creditors Arrangement Act* will be presented for adjudication before one of the judges of the Superior Court, sitting in the Commercial Division, in and for the judicial district of Montréal, on May 5, 2008, at 2:00 p.m., in room 12.61 of the Montréal Courthouse, located at 1 Notre-Dame Street East, in the City of Montréal, Province of Québec, or so soon thereafter as counsel may be heard.

**DO GOVERN YOURSELVES ACCORDING.**

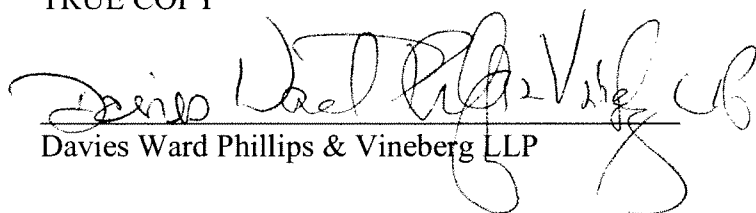
MONTRÉAL, May 5, 2008

(s) Davies Ward Phillips & Vineberg LLP

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**DAVIES WARD PHILLIPS & VINEBERG LLP**  
Attorneys for Petitioners Shermag Inc., Jaymar Furniture Corp., Scierie Montauban Inc., Mégaboïs (1989) Inc., Shermag Corporation and Jaymar Sales Corporation

TRUE COPY

  
Davies Ward Phillips & Vineberg LLP



No. 1301-09-0001  
**S U P E R I O R C O U R T**  
(Commercial Division)  
(Sitting as a court designated pursuant to the  
*Companies' Creditors Arrangement Act*)

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(District of Montréal)

**IN THE MATTER OF THE PLAN OF  
COMPROMISE OR ARRANGEMENT OF  
SHERMAG INC. ET ALS.**

Petitioners

and

**RSM RICHTER INC.**

Monitor

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**PETITION FOR AN INITIAL ORDER  
PURSUANT TO SECTIONS 4, 5 AND 11 OF THE  
COMPANIES' CREDITORS ARRANGEMENT  
ACT (R.S.C. 1985, C. c-36), NOTICE OF  
PRESENTATION AND AFFIDAVIT**

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**COPY FOR:**

Mr. Phil Manel, CA, CPA  
RSM Richter Inc.  
2 Place Alexis Nihon, Suite 2200  
Montreal, Quebec, H3Z 3C2

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Attorneys for Petitioners  
Per: Me Denis Ferland  
Me Christian Lachance  
Dir 514 841 6423  
O/F 223966



**DAVIES**

**DAVIES WARD PHILLIPS & VINEBERG LLP**

1501 McGill College Avenue     Tel 514 841 6400  
26<sup>e</sup> Floor     Fax 514 841 6499  
Montreal Canada H3A 3N9     BP-0181