

MERCER INTERNATIONAL INC.  
Form PRE 14A  
March 01, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**SCHEDULE 14A**  
**PROXY STATEMENT PURSUANT TO SECTION 14(a) OF THE**  
**SECURITIES EXCHANGE ACT OF 1934**

(AMENDMENT NO.      )

Filed by the Registrant                       Filed by a party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

**Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Pursuant to §240.14a-12

**MERCER INTERNATIONAL INC.**

(Name of Registrant as Specified in its Charter)

Payment of Filing Fee (Check the appropriate box):

No fee required.

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(1) Title of each class of securities to which transaction applies:

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

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(1) Amount Previously Paid: \$10,236.11

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(2) Form, Schedule or Registration Statement No.: Form S-4

(3) Filing Party: Mercer International Inc.

(4) Date Filed: February 29, 2012

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**PRELIMINARY PROXY STATEMENT**

**MERCER INTERNATIONAL INC.**

Dear Shareholders of Mercer International Inc.:

You are cordially invited to attend a special meeting (the **Special Meeting**) of shareholders of Mercer International Inc. (the **Company** or **Mercer**) to approve the issuance of shares of Mercer's common stock (the **Mercer Shares**) in connection with an offer for all of the outstanding common shares (the **FibreK Shares**) of Fibrek Inc. ( **FibreK** ), a Canadian company whose common shares are listed on the Toronto Stock Exchange. The Company and MERC Acquisition Inc., its wholly-owned subsidiary, have made an offer (the **Offer**) to Fibrek's shareholders to acquire all of the issued and outstanding Fibrek Shares, in exchange for cash and/or Mercer Shares. Shareholders of Fibrek who accept and tender their shares in the Offer will have the option to receive either: C\$1.30 in cash per Fibrek Share; 0.1540 of a Mercer Share per Fibrek Share; or C\$0.54 in cash plus 0.0903 of a Mercer Share per Fibrek Share, subject to maximum cash consideration of C\$70.0 million and maximum share consideration of 11,741,496 Mercer Shares. Before we can complete the Offer, we must obtain the approval of the Company's shareholders for the Mercer Shares to be issued in the Offer, and we are sending you the accompanying proxy statement for this purpose.

The Special Meeting will be held at [ ], local time, on [ ], 2012, at [ ], unless postponed or adjourned to a later date. At the Company's special meeting, the Company will ask its shareholders to approve, among other proposals, the issuance of the Mercer Shares in connection with the Offer, as described in the accompanying proxy statement.

After careful consideration, the Company's board of directors has approved the Offer, including the issuance of Mercer Shares in connection with the Offer, and has determined that the Offer and such issuance of Mercer Shares is in the best interests of the Company and its shareholders. ***Accordingly, the Company's board of directors unanimously recommends that the Company's shareholders vote FOR each of the proposals put to the Company's shareholders at the Special Meeting.***

The Mercer Shares are listed on the NASDAQ Global Market under the symbol **MERC** and on the Toronto Stock Exchange under the symbol **MRI.U**. On [ ], 2012, the last practicable trading day before the date of this proxy statement, the closing sale price of Mercer Shares was \$[ ] per share as reported on the NASDAQ Global Market. The Fibrek Shares are traded on the Toronto Stock Exchange under the symbol **FBK**. On [ ], 2012, the last practicable trading day before the date of the accompanying proxy statement, the closing sale price of a Fibrek Share was C\$[ ] per share as reported on the Toronto Stock Exchange.

More information about the Company, Fibrek and the Offer is contained in the accompanying proxy statement. ***The Company urges you to read the accompanying proxy statement carefully and in its entirety. In particular, you should carefully consider the matters discussed in the section entitled Risk Factors, beginning on page 25 of the accompanying proxy statement.***

The Company's board of directors has set [ ], 2012 as the record date for determining holders of the Mercer Shares entitled to vote at the Special Meeting or any adjournment, postponement or rescheduling thereof. If you are a record holder of Mercer Shares on that date, you are urged to complete, date and sign the enclosed proxy card and promptly return it to us. **Your vote is very important, regardless of the number of Mercer Shares you own. Please read the accompanying proxy statement carefully and cast your proxy vote as promptly as possible.**

The Company is excited about the opportunities the proposed acquisition of Fibrek may bring to the Company's shareholders, and thanks you for your consideration and continued support.

Jimmy S.H. Lee

Chairman of the Board



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**ADDITIONAL INFORMATION**

This proxy statement incorporates important business and financial information about Mercer that is not included or delivered with this proxy statement. You can obtain this information by requesting it in writing or by telephone from Mercer at the following address:

Mercer International Inc.

Suite 1120, 700 West Pender Street

Vancouver, British Columbia, Canada V6C 1G8

Telephone: (604) 684-1099

Attention: Investor Relations

We will provide promptly without charge to you, upon request, a copy of any document incorporated by reference into this proxy statement, other than exhibits to these documents unless the exhibits are specifically incorporated by reference in these documents. **In order to ensure timely delivery of the documents in advance of the Special Meeting, any request should be made at least five (5) business days before the Special Meeting, or [ ], 2012. See the section entitled Where You Can Find More Information for additional details about where you can find information about Mercer.**

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**MERCER INTERNATIONAL INC.**

**NOTICE OF SPECIAL MEETING OF SHAREHOLDERS**

**To Be Held On [                      ], 2012**

To the Shareholders of Mercer International Inc.:

NOTICE IS HEREBY GIVEN that a special meeting of shareholders of Mercer International Inc. (the Company or Mercer ) will be held on [                      ], 2012 at [                      ] at [                      ] (Vancouver time) for the following purposes:

1. To consider and vote upon a proposal to approve the issuance of up to 15,000,000 additional shares of Mercer's common stock, par value \$1.00, in connection with the Company's offer to acquire all of the issued and outstanding shares of Fibrek Inc. by way of a take-over bid (the Offer ); and
2. To consider and vote upon a motion to adjourn or postpone the special meeting to a later date or dates, if necessary, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal described above.

The board of directors of the Company has fixed the close of business on [                      ], 2012 as the record date for the determination of shareholders entitled to vote at the meeting or any adjournment, postponement or rescheduling thereof.

The foregoing proposals and the Offer are more fully described in the proxy statement accompanying this Notice. A list of Mercer shareholders entitled to vote at the special meeting will be available for examination during regular business hours at our principal executive offices at 1120 700 West Pender Street, Vancouver, British Columbia, Canada, V6C 1G8 ten (10) calendar days prior to the special meeting.

By Order of the Board of Directors,

Jimmy S.H. Lee

Chairman of the Board

[                      ], 2012

YOUR VOTE IS VERY IMPORTANT. WHETHER OR NOT YOU PLAN TO ATTEND THE MEETING, WE URGE YOU TO COMPLETE, SIGN, DATE AND RETURN IN THE ENCLOSED ENVELOPE THE PROXY CARD THAT ACCOMPANIES THIS NOTICE OF SPECIAL MEETING OF SHAREHOLDERS, OR VOTE USING THE INTERNET OR TELEPHONE, AS PROMPTLY AS POSSIBLE, IN ORDER TO ENSURE THE PRESENCE OF A QUORUM. A PROXY MAY BE REVOKED IN THE MANNER DESCRIBED IN THE ACCOMPANYING PROXY STATEMENT.

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**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This proxy statement and the documents we have filed with the U.S. Securities and Exchange Commission (the "SEC") that are incorporated by reference herein contain forward-looking statements. Generally, forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. They often include words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," or similar meaning, or future or conditional verbs, such as "will," "should," "could," or "may," although not all forward-looking statements contain these identifying words. Forward-looking statements are based on expectations, forecasts and assumptions by our management and involve a number of risks, uncertainties and other factors, many of which are beyond our control that could cause actual conditions, events or results to differ significantly from those described in the forward-looking statements. These factors include, but are not limited to, the following:

we will incur additional indebtedness following completion of the Offer;

the Offer is conditional upon, among other things, the receipt of consents and approvals from governmental authorities that could delay completion of the Offer or impose conditions on us and Fibrek Inc. ("Fibrek") that could in turn result in an adverse effect on the business or financial condition of Mercer following our acquisition of Fibrek;

if the conditions under the Support Agreement are not met or waived, the Offer cannot be completed. The outcome of the appeal of the decision of the Bureau de décision may also have an impact on the completion of the Offer. Failure to complete the Offer could have a material adverse impact on the market price of the Fibrek Shares;

change-of-control provisions in Fibrek's agreements triggered in connection with the acquisition of Fibrek may lead to adverse consequences;

if less than  $66\frac{2}{3}\%$  of Fibrek's shareholders tender their shares in the Offer, Mercer will not be able to effect a subsequent acquisition transaction of the remaining Fibrek Shares and Fibrek will continue to have minority shareholders;

the date on which the Offer will close is uncertain;

our acquisition of Fibrek might not be successfully completed without the possibility of Fibrek shareholders exercising dissent rights in connection with a second step transaction;

there might be difficulties in integrating Fibrek's business and operations into our business and operations;

integrating Fibrek may divert Mercer's management's attention away from our operations;

failure to retain key employees could diminish the benefits of the Offer;

the market price of Mercer Shares could decline as a result of the large number of such shares that will become eligible for sale after the completion of the Offer;

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the issuance of Mercer Shares to Fibrek shareholders in connection with the Offer will reduce the percentage ownership of current Mercer shareholders;

Fibrek's current shareholders will own a large percentage of Mercer Shares after the completion of the Offer, and will have significant influence over the outcome of corporate actions requiring shareholder approval; such shareholders' priorities for Mercer's business may be different from Mercer's current shareholders;

our business is highly cyclical in nature;

our level of indebtedness could negatively impact our financial condition and results of operations;

a weakening of the global economy could adversely affect our business and financial results and have a material adverse effect on our liquidity and capital resources;

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cyclical fluctuations in the price and supply of our raw materials could adversely affect our business;

we operate in highly competitive markets;

we are exposed to currency exchange rate and interest rate fluctuations;

increases in our capital expenditures or maintenance costs could have a material adverse effect on our cash flow and our ability to satisfy our debt obligations;

we use derivatives to manage certain risk which has caused significant fluctuations in our operating results;

we are subject to extensive environmental regulation and we could have environmental liabilities at our facilities;

our business is subject to risks associated with climate change and social and government responses thereto;

Project Blue Mill may not generate the results or benefits we expect;

we are subject to risks related to our employees;

we rely on government grants and guarantees and participate in European statutory programs;

we are dependent on key personnel;

we may experience material disruptions to our production;

we may incur losses as a result of unforeseen or catastrophic events, including the emergence of a pandemic, terrorist attacks or natural disasters;

our insurance coverage may not be adequate;

we rely on third parties for transportation services; and

other risks to Fibrek Inc.'s business.

Given these uncertainties, you should not place undue reliance on our forward-looking statements. You should read this proxy statement and the documents incorporated by reference herein with the understanding that our actual future results may be materially different from what we expect. The foregoing review of important factors is not exhaustive or necessarily in order of importance and should be read in conjunction with the other cautionary statements that are included in or incorporated by reference into this proxy statement. These factors expressly qualify all

subsequent oral and written forward-looking statements attributable to us or persons acting on our behalf. New factors emerge from time to time, and it is not possible for us to predict all such factors. Except as required by law, we do not undertake any obligation to update or revise any forward-looking statements contained in or incorporated by reference in this proxy statement, whether as a result of new information, future events or otherwise.

#### **INFORMATION CONCERNING FIBREK**

Except as otherwise indicated herein, the information concerning Fibrek contained in this proxy statement has been taken from or is based upon Fibrek's and other publicly available documents and records. Although Mercer has no knowledge that would indicate that any statements contained herein concerning Fibrek taken from or based upon such documents and records are untrue or incomplete, neither Mercer nor any of its directors or officers assumes any responsibility for the accuracy or completeness of such information, including any of Fibrek's financial statements, or for any failure by Fibrek to disclose events or facts which may have occurred or which may affect the significance or accuracy of any such information and are unknown to Mercer. Mercer has limited means of verifying the accuracy or completeness of any of the information contained herein that is derived from Fibrek's publicly available documents or records or whether there has been any failure by Fibrek to disclose events that may have occurred or may affect the significance or accuracy of any information.

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Financial statements for Fibrek included in this proxy statement have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ( IFRS ), which differ from U.S. generally accepted accounting principles ( GAAP ) in certain material respects, and thus may not be comparable to financial statements of U.S. companies.

**EXCHANGE RATES**

Our reporting currency and financial statements included in this proxy statement are in Euros, as a significant majority of our business transactions are originally denominated in Euros. We translate non-Euro denominated assets and liabilities at the rate of exchange on the balance sheet date. Revenues and expenses are translated at the average rate of exchange prevailing during the period.

Additionally, since Fibrek is a Canadian public company, its reporting currency and financial statements included in this proxy statement are in Canadian dollars. Fibrek translates non-Canadian dollar denominated assets and liabilities at the rate of exchange on the balance sheet date. Revenues and expenses are translated at the average rate of exchange prevailing during the period.

The following table sets out exchange rates, based on the noon buying rates in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York (the Noon Buying Rate ) for the conversion of Euros and Canadian dollars to U.S. dollars in effect at the end of the following periods, the average exchange rates during these periods (based on daily Noon Buying Rates) and the range of high and low exchange rates for these periods:

	2011	Years Ended December 31,			2007
		2010	2009	2008	
		( / \$ )			
End of period	0.7708	0.7536	0.6977	0.7184	0.6848
High for period	0.6723	0.6879	0.6623	0.6246	0.6729
Low for period	0.7736	0.8362	0.7970	0.8035	0.7750
Average for period	0.7186	0.7541	0.7176	0.6826	0.7304
		(C/\$)			
End of period	1.0168	1.0009	1.0461	1.2240	0.9881
High for period	0.9448	0.9960	1.0289	0.9717	0.9168
Low for period	1.0605	1.0776	1.2995	1.2971	1.1852
Average for period	0.9887	1.0298	1.1412	1.0660	1.0740

On February 24, 2012, the date of the most recent weekly publication of the Noon Buying Rate before the filing of this proxy statement, the Noon Buying Rate for the conversion of Euros and Canadian dollars to U.S. dollars was 0.7428 per U.S. dollar and C\$0.9988 per U.S. dollar.

In addition, certain financial information relating to our Celgar mill included in this proxy statement is stated in Canadian dollars while we report our financial results in Euros. The following table sets out exchange rates, based on the noon rate provided by the Bank of Canada (the Daily Noon Rate ), for the conversion of Canadian dollars to Euros in effect at the end of the following periods, the average exchange rates during these periods (based on Daily Noon Rates) and the range of high and low exchange rates for these periods:

	2011	Years Ended December 31,			2007
		2010	2009	2008	
		(C\$/ )			
End of period	1.3193	1.3319	1.5000	1.7046	1.4428
High for period	1.2847	1.2478	1.4936	1.4489	1.3448
Low for period	1.4305	1.5067	1.6920	1.7316	1.5628
Average for period	1.3761	1.3671	1.5851	1.5603	1.4690

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On February 27, 2012, the Daily Noon Rate for the conversion of Canadian dollars to Euros was C\$1.3387 per Euro.

**NON-GAAP FINANCIAL MEASURES**

This proxy statement contains non-GAAP financial measures that is, financial measures that either exclude or include amounts that are not excluded or included in the most directly comparable measure calculated and presented in accordance with GAAP. Specifically, we make use of the non-GAAP measure Operating EBITDA .

Operating EBITDA is defined as operating income (loss) plus depreciation and amortization and non-recurring capital asset impairment charges. We use Operating EBITDA as a benchmark measurement of our own operating results and as a benchmark relative to our competitors. We consider it to be a meaningful supplement to operating income as a performance measure primarily because depreciation expense and non-recurring capital asset impairment charges are not an actual cash cost, and depreciation expense varies widely from company to company in a manner that we consider largely independent of the underlying cost efficiency of our operating facilities. In addition, we believe Operating EBITDA is commonly used by securities analysts, investors and other interested parties to evaluate our financial performance.

Operating EBITDA does not reflect the impact of a number of items that affect our net income (loss) attributable to common shareholders, including financing costs and the effect of derivative instruments. Operating EBITDA is not a measure of financial performance under GAAP, and should not be considered as an alternative to net income (loss) or income (loss) from operations as a measure of performance, nor as an alternative to net cash from operating activities as a measure of liquidity.

Operating EBITDA has significant limitations as an analytical tool, and should not be considered in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are that Operating EBITDA does not reflect: (i) our cash expenditures, or future requirements, for capital expenditures or contractual commitments; (ii) changes in, or cash requirements for, working capital needs; (iii) the significant interest expense, or the cash requirements necessary to service interest or principal payments, on our outstanding debt; (iv) noncontrolling interests on our Stendal mill operations; (v) the impact of realized or marked to market changes in our derivative positions, which can be substantial; and (vi) the impact of impairment charges against our investments or assets. Because of these limitations, Operating EBITDA should only be considered as a supplemental operational performance measure and should not be considered as a measure of liquidity or cash available to us to invest in the growth of our business. Because all companies do not calculate Operating EBITDA in the same manner, Operating EBITDA as calculated by us may differ from Operating EBITDA or EBITDA as calculated by other companies. We compensate for these limitations by using Operating EBITDA as a supplemental measure of our operational performance in addition to our GAAP financial statements incorporated by reference into this proxy statement.

**INDUSTRY AND MARKET DATA**

In this proxy statement, we rely on and refer to information and statistics regarding our market share and the markets in which we compete. We have obtained some of this market share information and industry data from internal surveys, market research, publicly available information and industry publications. Such reports generally state that the information contained therein has been obtained from sources believed to be reliable, but the accuracy or completeness of such information is not guaranteed. Although we believe this information is reliable, we have not independently verified, or cannot guarantee, the accuracy or completeness of that information and investors should use caution in placing reliance on such information.

Statements in this proxy statement or incorporated by reference into this proxy statement concerning the production capacity of our pulp mills are management estimates based primarily on historically achieved levels of production and assumptions regarding maintenance downtime. Statements concerning electrical generating

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capacity at our mills are also management estimates based primarily on our expected pulp production (which largely determines the amount of electricity we can generate) and assumptions regarding maintenance downtime, in each case within manufacturers' specifications of capacity.

In this proxy statement, please note the following:

references to we, our, us, the Company or Mercer mean Mercer International Inc. and its subsidiaries, unless the context clearly suggests otherwise, and references to Mercer Inc. mean Mercer International Inc., excluding its subsidiaries;

all references to monetary amounts are to Euros, the lawful currency adopted by most members of the European Union, unless otherwise stated;

€ refers to Euros; \$ refers to U.S. dollars; and C\$ refers to Canadian dollars;

References to MW mean megawatts and MWh mean megawatt hours; and

References to ADMT refers to air-dried metric tonnes.

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**QUESTIONS AND ANSWERS ABOUT THE OFFER AND THE MERCER SPECIAL MEETING**

*Pursuant to the terms of the support agreement between Mercer and Fibrek dated February 9, 2012 (the Support Agreement), Mercer and MERC Acquisition Ltd., its wholly owned subsidiary, have made an offer to Fibrek's shareholders to acquire all of the issued and outstanding common shares of Fibrek (Fibrek Shares) including any Fibrek Shares that become issued and outstanding upon the exercise of any options issued under Fibrek's stock option plan prior to the expiration of the offer, in exchange for cash and/or newly issued shares of Mercer's common stock (Mercer Shares). This proxy statement contains important information about the Support Agreement, the Offer and the special meeting of Mercer's shareholders (the Special Meeting). The following section provides answers to certain anticipated questions about the Offer, and the Special Meeting. Please note that this section may not address all issues that may be important to you as a Mercer shareholder. Accordingly, you should carefully read this entire proxy statement, including each of the annexes.*

**Q. Why am I receiving this proxy statement?**

A. Mercer has entered into the Support Agreement, pursuant to which Mercer has commenced the Offer for all outstanding Fibrek Shares. As a result of being listed for trading on the NASDAQ Global Market, issuances of Mercer Shares are subject to NASDAQ listing rules. We are currently permitted to issue just under 20% of the total outstanding Mercer Shares (being approximately 11,155,840 Mercer Shares) without shareholder approval. However, under NASDAQ Listing Rule 5635(a), we must seek shareholder approval with respect to issuances of our common stock when the shares to be issued are being issued in connection with the acquisition of the stock of another company and are equal to, or in excess of 20% of the number of Mercer Shares outstanding before the issuance. Because completion of the Offer contemplated by the Support Agreement would currently require us to issue 11,741,496 Mercer Shares, or approximately 21% of the currently outstanding Mercer Shares, we are asking you to approve the issuance of up to 15,000,000 Mercer Shares, as well as the other proposals described in this proxy statement. We are seeking approval to issue more Mercer Shares than currently contemplated by the Offer and Support Agreement to provide us with flexibility to address fluctuations in market prices and conditions and, if we elect to do so and if required, to match or compete with any alternative offer for Fibrek. We are holding the Special Meeting in order to obtain, among other things, shareholder approval of the issuance of Mercer Shares pursuant to the Support Agreement.

**Q. Who is soliciting my proxy?**

A. This proxy statement is being used by the board of directors of Mercer to solicit your proxy for use at the Special Meeting.

**Q. When and where is the Special Meeting of shareholders?**

A. The Special Meeting will be held on [ ], 2012 at [ ] at [ ] (Vancouver time).

**Q. Who can vote at the meeting?**

A. Registered shareholders of Mercer who own Mercer Shares on [ ], 2012 (the Record Date), may attend and vote at the Special Meeting. Each Mercer Share is entitled to one vote. There were [ ] Mercer Shares outstanding on the Record Date. If you own your Mercer Shares through a brokerage account or in another nominee form, you must provide instructions to the broker or nominee as to how your Mercer Shares should be voted. Your broker or nominee will generally provide you with appropriate forms at the time you receive this proxy statement. If you own your Mercer Shares through a brokerage account or nominee, you cannot vote in person at the Special Meeting unless you receive a proxy from the broker or the nominee.

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### **Q. What am I being asked to approve?**

A. You are being asked to approve the issuance of up to 15,000,000 new Mercer Shares in connection with the Offer. We currently anticipate using approximately 11,741,496 Mercer Shares as consideration under the Offer. We are seeking approval to issue more Mercer Shares than currently contemplated by the Support Agreement to provide us with flexibility to address fluctuations in market prices and conditions and, if we elect to do so and if required, to match or compete with any alternative offer for Fibrek.

### **Q. How do I vote?**

A: Registered shareholders of Mercer may vote in person at the Special Meeting, by mail, by phone or on the internet.

Voting by Mail. Complete, date, sign and mail the proxy in the enclosed postage pre-paid envelope. If you mark your voting instructions on the proxy, your Mercer Shares will be voted as you instruct. Please see the proxy for voting instructions.

Voting in Person. If you attend the Special Meeting, you may vote as instructed at the meeting. However, if you hold your Mercer Shares in street name (that is, through a broker/dealer or other nominee), you will need to bring to the meeting a proxy delivered to you by such nominee reflecting your ownership of Mercer Shares as of the Record Date.

Voting on the Internet. Go to [www.proxyvoting.com/merc](http://www.proxyvoting.com/merc) and follow the instructions. You should have your proxy in hand when you access the website.

Voting by Telephone. Call the toll-free number listed on the proxy from any touch-tone telephone and follow the instructions. You should have your proxy in hand when you call.

If you own your Mercer Shares through a brokerage account or in other nominee form, you should follow the instructions you receive from the record holder to see which voting methods are available.

### **Q: What does it mean if I receive more than one proxy?**

A: It means that you hold Mercer Shares in multiple accounts. Please complete and return all proxies to ensure that all your Mercer Shares are voted in accordance with your instructions.

### **Q: What if I change my mind after returning my proxy?**

A: If you are a registered shareholder of Mercer, you may revoke your proxy and change your vote at any time before it is voted at the Special Meeting. You may do this by:

sending a signed notice of revocation of proxy to our registrar and transfer agent at the address set out above stating that the proxy is revoked; or

submitting another proxy with a later date over the internet, by telephone or to our registrar and transfer agent at the following address: Computershare Shareowner Services P.O. Box 3550, South Hackensack, NJ 07606-9250 ; or

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voting at the Special Meeting.

Your proxy will not be revoked if you attend the Special Meeting but do not vote.

If you own your Mercer Shares through a broker or other nominee and wish to change your vote, you must send those instructions to your broker or nominee.

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**Q: Will my Mercer Shares be voted if I do not sign and return my proxy?**

A: If your Mercer Shares are registered in your name, they will not be voted unless you submit your proxy or vote in person at the Special Meeting. If your Mercer Shares are held in street name, your broker/dealer or other nominee will not have the authority to vote your Mercer Shares unless you provide instructions.

**Q: May I vote in person at the Special Meeting of shareholders?**

A: If your Mercer Shares are registered directly in your name with Mercer's transfer agent, then you are considered to be the shareholder of record with respect to those shares, and the proxy materials and proxy card are being sent directly to you by Mercer. If you are a Mercer shareholder of record, you may attend the Special Meeting and vote your Mercer Shares in person. However, even if you plan to attend the Special Meeting in person, Mercer requests that you sign and return the enclosed Mercer proxy card or vote your Mercer Shares by telephone or via the Internet to ensure that your Mercer Shares will be represented at the Special Meeting, if you are unable to attend.

If you own your Mercer Shares in street name, the proxy materials are being forwarded to you by your broker or other nominee together with a voting instruction card to return to your broker or other nominee to direct them to vote on your behalf. If you own your Mercer Shares in street name, you are not the shareholder of record, and you may not vote these shares in person at the Special Meeting unless you obtain a proxy from the broker, trustee or nominee that holds your Mercer Shares, giving you the right to vote the Mercer Shares at the meeting.

**Q: If my Mercer Shares are held in street name by my broker, will my broker vote my shares for me?**

A: Unless your broker has discretionary authority to vote on certain matters, your broker will not be able to vote your Mercer Shares without instructions from you. Brokers are not expected to have discretionary authority to vote for the Mercer proposals. Therefore, in order to make sure that your vote is counted, you should instruct your broker to vote your Mercer Shares following the procedures provided by your broker.

**Q: Who will count the votes?**

A: Agents of the Company will tabulate the proxies. Additionally, votes cast by registered shareholders of Mercer voting in person at the Special Meeting are tabulated by a person who is appointed by our management before the meeting.

**Q: How many Shares must be present to hold the Special Meeting?**

A: To hold the Special Meeting and conduct business, at least one-third of the outstanding Mercer Shares entitled to vote at the Special Meeting must be present at the meeting. This is called a quorum.

Votes are counted as present at the Special Meeting if a registered shareholder of Mercer either:

is present and votes in person at the Special Meeting; or

has properly submitted a proxy.

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Abstentions and broker non-votes (Mercer Shares held by a broker/dealer or other nominee that are not voted because the broker/dealer or other nominee does not have the authority to vote on a particular matter) will be counted for the purposes of a quorum.

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**About the Offer**

**Q. Why is Mercer proposing to acquire Fibrek?**

- A. The board of directors of Mercer has determined that the Offer is in the best interests of Mercer and its shareholders in part because it presents a compelling strategic opportunity for Mercer to expand both its pulp production capacity and its production and sale of renewable energy. The successful completion of the Offer will also allow Mercer to further diversify its business geographically. For a complete discussion of Mercer's reasons for making the Offer, see the section entitled "The Offer - Mercer's Reasons for Commencing the Offer" in this proxy statement.

**Q. What vote is required to consummate the Offer?**

- A. To consummate the Offer, Mercer shareholders must approve the issuance of Mercer Shares to be issued in exchange for Fibrek Shares tendered in the Offer. The approval of the issuance of Mercer Shares to be issued in connection with the Offer requires the affirmative vote of a majority of the Mercer Shares present in person or represented by proxy and entitled to vote at the Special Meeting at which a quorum is present, whether voting in person or represented by proxy at the Special Meeting.

In connection with this shareholder vote, Mercer has entered into voting support agreements with two institutional shareholders and its President and Chief Executive Officer who collectively hold, directly or indirectly, approximately 44% of the outstanding Mercer Shares. These shareholders have pledged, pursuant to the terms of their respective voting support agreements, to vote all of their Mercer Shares in favor of the motion to approve the issuance of the Mercer Shares at the Special Meeting. See the section entitled "Certain Agreements Related to the Offer - Voting Support Agreements" in this proxy statement. These voting support agreements are available on the SEC's web site at <http://www.sec.gov>.

**Q. Are there other conditions that need to be satisfied to consummate the Offer?**

- A. In addition to the requirement of obtaining Mercer shareholder approval, the number of Fibrek Shares validly deposited under the Offer, together with Special Warrants (defined herein), if any, held by Mercer at the expiry of the Offer must represent at least 50.1% of the outstanding Fibrek Shares on a fully diluted basis. The Offer is also conditional on the receipt of certain regulatory approvals and our Registration Statement on Form S-4 being declared effective by the SEC. For a summary of the conditions that need to be satisfied to consummate the Offer, see the section entitled "The Support Agreement" in this proxy statement.

**Q. What will Fibrek shareholders receive if they accept the Offer?**

- A. Shareholders of Fibrek who accept the Offer will have the option to receive either C\$1.30 in cash per Fibrek Share, 0.1540 of a Mercer Share, or C\$0.54 in cash plus 0.0903 of a Mercer Share per Fibrek Share, subject to proration. No fractional Mercer Shares will be issued in the Offer. Tendering shareholders of Fibrek will receive cash in lieu of fractional shares.

**Q. Will the number of Mercer Shares issuable to Fibrek shareholders in connection with the Offer be subject to any adjustment, for example if Mercer's stock price fluctuates?**

- A.

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No. The share exchange ratio is fixed at 0.1540 of a Mercer Share or 0.0903 of a Mercer Share plus C\$0.54 in cash for every Fibrek Share tendered in the Offer.

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**Q. Is there a maximum number of Mercer Shares that can be issued in the Offer?**

Under the Offer, the maximum aggregate share consideration will be 11,741,496 Mercer Shares and the maximum aggregate cash consideration is C\$70.0 million.

**Q. What will be the relative ownership of Mercer after the Offer?**

A. If all of the Fibrek Shares currently outstanding are tendered in the Offer, post-Offer the current shareholders of Mercer will hold approximately 83% of the outstanding Mercer Shares and the current shareholders of Fibrek will hold approximately 17% of the outstanding Mercer Shares.

**Q. Will Mercer Shares issued in connection with the Offer be registered and listed on an exchange?**

A. Yes. The Mercer Shares issued will be registered under the *Securities Act of 1933*, as amended (the *Securities Act*), and are expected to be listed on the NASDAQ Global Market under the symbol `MERC` and on the Toronto Stock Exchange under the symbol `MRI.U`.

**Q. Will there be any contractual transfer restrictions affecting the Mercer Shares issued in connection with the Offer?**

A. No, the Mercer Shares issued pursuant to the Offer will not be subject to any contractual transfer restrictions.

**Q. What will happen to the Fibrek options and other rights to acquire or receive Fibrek Shares?**

A. In accordance with the terms of the Support Agreement, we expect, prior to the expiry of the Offer, all unvested options to acquire Fibrek Shares to be accelerated and a cashless exercise of such options to be effected solely for the purpose of tendering the resulting Fibrek Shares under the Offer.

**Q. Will there be any change to the Mercer Shares held by Mercer shareholders?**

A. No. The Offer does not result in any changes to the existing Mercer Shares. The current shareholders of Mercer will continue to be shareholders of Mercer after the Offer.

**Q. Who will be the directors of Mercer following the Offer?**

A. The current composition of Mercer's board of directors will not change as a result of the Offer. See Annex H *Directors of Mercer* for a detailed biography of each current director of Mercer.

**Q. Do Mercer shareholders have appraisal or dissenters' rights in connection with the Offer?**

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A. No. Mercer shareholders do not have appraisal or dissenters' rights in connection with the issuance of the Mercer Shares to be issued in the Offer.

**Q. As a Mercer shareholder, how does the Mercer board of directors recommend that I vote?**

A. The Mercer board of directors has determined that the Support Agreement and the transactions contemplated thereby, including the Offer and the issuance of Mercer Shares in connection therewith, are advisable and in the best interests of Mercer and its shareholders. After careful consideration, the Mercer board of directors recommends that Mercer shareholders vote:

FOR Proposal No. 1 to approve the issuance of new Mercer Shares in connection with the Offer; and

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FOR Proposal No. 2 to approve any motion to adjourn or postpone the Special Meeting, if necessary, to solicit additional proxies if there are not sufficient votes at the time of the Special Meeting in favor of Proposal No. 1.

**Q. What risks should I consider in deciding how to vote?**

- A. You should carefully read this entire proxy statement, including each of the annexes, and pay specific attention to the section entitled Risk Factors , which sets forth certain risks and uncertainties related to the Offer and the business of Mercer.

**Q. When do you expect the Offer to close?**

- A. Mercer cannot predict the exact timing of the closing of the Offer and the related transactions. Mercer launched the Offer on February 29, 2012 in accordance with the terms of the Support Agreement and applicable securities laws. The Offer will be open for acceptance for at least 35 days and is set to expire on April 6, 2012, unless extended or withdrawn by Mercer. The closing of the Offer is also subject to the satisfaction of certain customary conditions, including, among other things, there being validly deposited under the Offer, and not withdrawn at the expiry date, that number of Fibrek Shares which, together with any Fibrek Shares and Special Warrants (defined herein) held by Mercer, represent at least 50.1% of the outstanding Fibrek Shares on a fully diluted basis, receipt of the requisite regulatory approvals and consents, a Registration Statement on Form S-4 to register the Mercer Shares to be issued in the Offer being declared effective by the SEC and the absence of a material change with respect to Fibrek. For more information regarding timing, see the section entitled The Support Agreement in this proxy statement.

**Q. What do Mercer shareholders need to do now?**

- A. Mercer urges its shareholders to read this proxy statement carefully and in its entirety, including its annexes, and to consider how the Offer affects them. If you are a shareholder of Mercer as of the Record Date, you are further urged to provide your proxy instructions by mailing your signed Mercer proxy card in the enclosed return envelope or by voting by telephone or via the internet following the instructions on your proxy card. Please provide your proxy instructions only once, unless you are revoking a previously delivered proxy instruction, and as soon as possible so that your Mercer Shares can be voted at the Special Meeting.

**Q. Who can help answer my questions?**

- A. If you are a Mercer shareholder and would like additional copies, without charge, of this proxy statement, or if you have questions about the Offer, including the procedures for voting your Mercer Shares, you should contact:  
Mercer International Inc.

Suite 1120, 700 West Pender Street

Vancouver, British Columbia, Canada V6C 1G8

Telephone: (604) 684-1099

Attention: Investor Relations

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**SUMMARY**

*This summary highlights selected information from this proxy statement. It does not contain all of the information that may be important to you. We encourage you to carefully read this entire proxy statement, including annexes, and the other documents to which this proxy statement refers, to fully understand the proposals to be considered at the Special Meeting.*

**Information About Mercer International Inc., MERC Acquisition Inc. and Fibrek Inc.**

***Mercer International Inc.***

Mercer International Inc.

700 West Pender Street

Suite 1120

Vancouver, British Columbia

V6C 1G8 Canada

Telephone: (604) 684-1099

Mercer Inc. is a Washington corporation and our shares of common stock are quoted and listed for trading on the NASDAQ Global Market (MERC) and listed in U.S. dollars on the Toronto Stock Exchange (MRI.U).

We are currently the largest publicly traded producer of market northern bleached softwood kraft, or NBSK, pulp in the world. Our operations are located in Eastern Germany and Western Canada. We operate three NBSK pulp mills with a consolidated annual production capacity of approximately 1.5 million ADMTs. We are the sole NBSK pulp producer, and the only significant producer of pulp for resale, known as market pulp, in Germany, which is the largest pulp import market in Europe.

Our principal executive offices are located at Suite 1120, 700 West Pender Street, Vancouver, British Columbia, Canada, V6C 1G8, and our telephone number is (604) 684-1099. Mercer's website is [www.mercerint.com](http://www.mercerint.com)

***MERC Acquisition Inc.***

MERC Acquisition Inc.

925 West Georgia Street

Suite 1000

Vancouver, British Columbia

V6C 3L2 Canada

Telephone: (604) 662-8808

MERC Acquisition Inc. (Mercer Acquisition) is a corporation incorporated under the *Canada Business Corporations Act* (the CBCA) and is a wholly owned subsidiary of Mercer. Mercer Acquisition was organized solely for the purpose of making the Offer and has not otherwise conducted any business activities to date.

***Fibrek Inc.***

Fibrek Inc.

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625 René-Lévesque Blvd. W., Suite 700

Montréal, Québec

H3B 1R2, Canada

Telephone: (514) 871-0550

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FibreK was incorporated on March 24, 2010 pursuant to the provisions of the CBCA for the purpose of participating in an arrangement under Section 192 of the CBCA pursuant to which SFK Pulp Fund completed its reorganization, on May 25, 2010, from an income trust structure to a corporation named Fibrek Inc.

FibreK is a leading producer and marketer of virgin and recycled kraft pulp operating three mills: the Saint-Félicien mill, the Fairmont mill, and the Menominee mill, with a combined annual production capacity of approximately 760,000 tonnes. The Saint-Félicien mill provides NBSK pulp to various sectors of the paper industry in Canada, the U.S. and Europe, for use in the production of specialized products. The Fairmont mill and the Menominee mill manufacture air-dried recycled bleached kraft pulp, or RBK pulp and primarily supply manufacturers of fine uncoated paper, tissue paper for commercial and industrial uses, and coated paper in the U.S.

FibreK's principal executive offices are located at 625 René-Lévesque Blvd. W., Suite 700, Montréal, Québec, H3B 1R2, Canada, and Fibrek's telephone number is (514) 871-0550. Fibrek's website is [www.fibreK.com](http://www.fibreK.com).

### **The Offer (see page 40)**

Pursuant to the Offer, we are offering to purchase all of the issued and outstanding Fibrek Shares for the following consideration per Fibrek Share tendered:

C\$1.30 in cash;

0.1540 of a Mercer Share; or

C\$0.54 in cash plus 0.0903 of a Mercer Share.

FibreK's shareholders tendering their Fibrek Shares will have the option of selecting one of the preceding options, subject to proration necessary to effect the maximum aggregate cash consideration of C\$70.0 million and the maximum aggregate share consideration of 11,741,496 Mercer Shares. Such proration will be based on the number of Fibrek Shares acquired in proportion to the number of issued and outstanding Fibrek Shares as of the applicable take-up date. No fractional Mercer Shares will be issued in the Offer.

### **Mercer's Reasons for commencing the Offer (see page 43)**

The Mercer board of directors has concluded that the acquisition of Fibrek through the Offer presents a compelling strategic opportunity to expand both its pulp production capacity and its production and sale of renewable energy and allow Mercer to further diversify its business geographically. In reaching its decision to approve the Offer, the Mercer board of directors considered a number of factors including, among other factors:

The acquisition of Fibrek fits within Mercer's strategy of focusing on world-class production assets that produce high quality pulp;

The ability of the Saint-Félicien mill to produce and sell surplus renewable energy is in line with Mercer's goal of increasing its revenues from energy sales;

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FibreK's mills are complementary to Mercer's existing operations and, through active management, we believe that the operations of Fibrek will generate increased value for Mercer's shareholders; and

Mercer's board of directors has received an opinion from Raymond James Ltd. (Raymond James), its financial advisor, to the effect that, as of the date of the opinion, the Offer is fair from a financial point of view to Mercer's shareholders.

### **Risk Factors (see page 25)**

Mercer and Fibrek are subject to numerous risks associated with their businesses and their industries. In addition, risks related to the Offer, including the possibility that the closing of the Offer may be delayed or not be completed at all, poses a number of unique risks to Mercer shareholders, including the following risks:

Mercer may not realize all of the anticipated benefits of the successful completion of the Offer;

we will incur additional indebtedness following the completion of the Offer;

there may be difficulties integrating Fibrek's business and operations into our business and operations;

after the consummation of the Offer, Fibrek's current shareholders could have significant influence over the outcome of corporate actions requiring shareholder approval and such shareholders' priorities for Mercer's business may be different from Mercer's current shareholders;

if less than  $66\frac{2}{3}\%$  of Fibrek's current shareholders tender their shares in the Offer, Mercer will not be able to effect a second step transaction of the remaining Fibrek Shares and Fibrek will likely continue to have minority shareholders;

Mercer and Fibrek both have incurred and will incur significant expenses as a result of the Offer, which will reduce the amount of capital available to fund Mercer's business after the successful completion of the Offer;

the market price of Mercer Shares could decline as a result of the large number of shares that will become eligible for sale after the Offer is completed; and

if the conditions to the completion of the Offer are not met or waived, the Offer will not occur.

These risks and other risks are discussed in greater detail in the section entitled "Risk Factors" and elsewhere in this proxy statement. Mercer encourages you to read and consider all of these risks carefully.

### **Market Price and Dividend Information (see page 23)**

The closing sale price per Mercer Share as reported on the NASDAQ Global Market on February 9, 2012, the last full trading day prior to the public announcement of entry into the Support Agreement, was \$8.25 and the closing sale price per Mercer Share on February 27, 2012 (the last practicable trading date before the filing of this proxy statement) as reported on the NASDAQ Global Market was \$8.43. Following the successful completion of the Offer, Mercer Shares, including the Mercer Shares issued in connection with the Offer, are expected to continue to trade on the NASDAQ Global Market under the symbol "MERC" and on the Toronto Stock Exchange under the symbol "MRI.U". Mercer has never declared or paid cash dividends on its capital stock.

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Mercer currently intends to retain earnings, if any, to finance the growth and development of its business and does not expect to pay any cash dividends to its shareholders in the foreseeable future. Payment of future dividends, if any, will be at the discretion of Mercer's board of directors and subject to the terms of the Company's senior indebtedness.

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The closing sale price per Fibrek Share as reported on the Toronto Stock Exchange on February 9, 2012, the last full trading day prior to the public announcement of entry into the Support Agreement, was C\$1.13, and the closing sale price per Fibrek Share on February 27, 2012 (the last practicable trading date before the filing of this proxy statement) as reported on the Toronto Stock Exchange was C\$1.18.

For more information, see the section entitled *Market Price and Dividend Information* .

### **Opinion of Raymond James to the Board of Directors of Mercer (see page 43)**

At the February 9, 2012 meeting of Mercer's board of directors, Raymond James rendered its oral opinion to the board of directors, subsequently confirmed in writing, to the effect that, as of February 9, 2012, and based upon and subject to certain matters stated therein, the Offer is fair, from a financial point of view, to Mercer's shareholders. See Annex F, *Opinion of Raymond James Ltd.* Holders of Mercer Shares are encouraged to read the opinion carefully in its entirety.

### **Overview of the Support Agreement (see page 55)**

The Support Agreement contains the principal terms and conditions of the proposed Offer.

### ***Non-Solicitation***

Until the earlier of either the closing of the Offer or the termination of the Support Agreement, Fibrek shall not, directly or indirectly, through any officer, director, employee, representative or agent, as the case may be, solicit, invite or encourage any person to consider the purchase of any Fibrek Shares or Fibrek's business or assets or take any action of any kind which might reasonably be expected to reduce the likelihood of success of the Offer.

Moreover, neither party to the Support Agreement nor any of its subsidiaries shall without the prior written consent of the other party initiate discussions with any third party regarding any transfer of rights or other transaction which could reasonably be expected to have a material adverse effect on the Offer .

For a more complete discussion of the exclusivity provisions, see the section entitled *The Support Agreement Non-Solicitation* in this Proxy Statement.

### ***Conditions to Closing of the Offer***

In order to consummate the Offer, among other conditions, Mercer shareholders must approve the issuance of Mercer Shares in connection with the Offer, the number of Fibrek Shares deposited under the Offer, together with any Fibrek Shares and Special Warrants held by Mercer at the expiry of the Offer must represent at least 50.1% of the outstanding Fibrek Shares on a fully diluted basis, requisite regulatory consents must be acquired and the Registration Statement on Form S-4 registering the Mercer Shares to be issued in the Offer must be declared effective by the SEC. For a summary of the conditions to the closing of the Offer, see the section entitled *The Support Agreement* in this proxy statement.

### ***Termination of the Support Agreement***

It is possible that the Offer and the transactions contemplated by the Support Agreement will not be completed. This might happen if, for example, either party is in default or has materially breached its covenants or obligations as specified in the Support Agreement and the non-breaching party provides written notice of such breach. For a more complete discussion of the manner in which the Support Agreement may terminate, see the section entitled *The Support Agreement Termination of the Support Agreement* in this proxy statement.

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### ***Termination Fee***

Upon the occurrence of certain events, Fibrek has agreed to pay Mercer an amount equal to C\$8,500,000. In certain other circumstances, Mercer may be entitled to an expense reimbursement of C\$2,000,000. For a more complete discussion of the termination fee, see the section entitled "The Support Agreement - Termination Fee" in this proxy statement.

### **Interests of Certain Persons in the Offer (see page 66)**

#### ***Mercer***

To the knowledge of Mercer, no director or executive officer of Mercer, nor any of their affiliates, have any interests in the Offer that differ from, or are in addition to, their interests as holders of Mercer Shares. As of February 27, 2012, the directors and executive officers of Mercer, together with their affiliates, beneficially owned in the aggregate approximately 2,735,022 Mercer Shares (including options held by them that are exercisable within 60 days), entitling them to exercise approximately 4.1% of the voting power of the Mercer Shares at the Special Meeting.

#### ***Fibrek***

As of February 27, 2012, the directors and executive officers of Fibrek, together with their affiliates, beneficially owned in the aggregate 3,860,982 Fibrek Shares, or approximately 2.9% of the outstanding Fibrek Shares on a fully diluted basis.

### **Voting Support Agreements (see page 60)**

Mercer has entered into voting support agreements with two institutional shareholders and its President and Chief Executive Officer who collectively hold, directly or indirectly, approximately 44% of the outstanding Mercer Shares. These shareholders have agreed, pursuant to the terms of their respective voting support agreements, to vote all of their Mercer Shares in favor of the motion to approve the issuance of the Mercer Shares at the Special Meeting. See the section entitled "Certain Agreements Related to the Offer - Voting Support Agreements" in this proxy statement.

### **Ownership of Mercer Following the Offer (see page 54)**

After the successful completion of the Offer, the percentage ownership of the outstanding shares of Mercer held by current Mercer shareholders and current Fibrek shareholders will depend on the percentage of Fibrek Shares that are tendered pursuant to the Offer. If all of the Fibrek Shares currently outstanding (which excludes any Fibrek Shares that may be issued or issuable after the date of this proxy statement) are tendered in the Offer, post-Offer the current shareholders of Mercer will hold approximately 83% of the outstanding Mercer Shares and the current shareholders of Fibrek will hold approximately 17% of the outstanding Mercer Shares.

### **Regulatory Approvals (see page 49)**

The Offer is subject to regulatory approvals under the *Hart-Scott-Rodino Antitrust Improvements Act of 1976* in the United States (the "HSR Act"), the *Competition Act* in Canada (the "Competition Act"), the *Investment Canada Act* (the "ICA") and the approval by the SEC of a Registration Statement on Form S-4 registering the Mercer Shares to be issued in connection with the Offer under the Securities Act.

### **NASDAQ and Toronto Stock Exchange Listing (see page 53)**

Pursuant to the terms of the Support Agreement, Mercer will use reasonable commercial efforts to cause all Mercer Shares to be issued in connection with the Offer to be approved for listing on the NASDAQ Global Market and the Toronto Stock Exchange at their time of issue.

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### **Anticipated Accounting Treatment (see page 53)**

Mercer will account for the potential acquisition of Fibrek as a purchase of the business, which means that the assets and liabilities of Fibrek will be recorded at their fair value and the results of operations of Fibrek will be included in Mercer's results from and after the effective time of such acquisition. The acquisition method of accounting is based on Accounting Standards Codification Topic 805, Business Combinations.

### **Appraisal Rights and Dissenters' Rights (see page 49)**

Mercer shareholders are not entitled to dissenters' rights or appraisal rights under the *Washington Business Corporations Act* (the "WBCA") in connection with the Offer.

### **Mercer Board and Management (see page 54)**

Following the closing of the Offer, the board of directors of Mercer will consist of seven directors, comprised of all of the current Mercer directors. See Annex H "Directors of Mercer" for a detailed biography of each current director of Mercer.

### **Comparison of Shareholder Rights**

The rights of holders of Fibrek Shares are governed by Fibrek's articles of incorporation and the CBCA. The rights of Mercer's shareholders are governed by Mercer's articles of incorporation, Mercer's by-laws and the WBCA. Accordingly, the rights associated with Fibrek Shares are different from the rights associated with Mercer Shares. After the successful completion of the Offer, Fibrek shareholders who have tendered their Fibrek Shares will become Mercer shareholders and will have rights that are different from those they have now as Fibrek shareholders. See Annex C to this proxy statement entitled "Comparison of Shareholders Rights and Corporate Governance Matters" for a discussion of certain aspects of Washington corporate law and Canadian corporate law, and the different rights associated with Mercer Shares and Fibrek Shares.

### **The Mercer Special Meeting of Shareholders (see page 36)**

The Special Meeting will be held at [ ], at [ ], Vancouver time, on [ ], 2012. Only holders of record of Mercer Shares at the close of business on the Record Date are entitled to notice of, attendance at and to vote at, the Special Meeting. As of the Record Date, there were [ ] Mercer Shares outstanding and entitled to vote at the Special Meeting, held by approximately [ ] holders of record. Each holder of Mercer Shares is entitled to one vote for each Mercer Share owned as of the Record Date.

There are two proposals at the Special Meeting. The first is a proposal to approve the issuance of new Mercer Shares in connection with the Offer. The second is a proposal to consider and vote upon a motion to adjourn or postpone the Special Meeting, if necessary, to solicit additional proxies if there are not sufficient votes in favor of the first proposal. If you are a Mercer shareholder, failure to return your proxy card or otherwise provide proxy instructions or vote your Mercer Shares in person will result in your Mercer Shares not being counted for purposes of determining whether a quorum is present at the Special Meeting. In the event that a quorum is not reached or the necessary votes are not received, the Special Meeting will have to be adjourned and recalled to obtain a quorum and the necessary votes.

**Table of Contents****SELECTED HISTORICAL AND PRO FORMA COMBINED FINANCIAL DATA**

The following tables present selected historical financial data for Mercer and Fibrek and comparative historical and unaudited pro forma per share data for Mercer and Fibrek.

**Selected Historical Financial Data of Mercer**

The following table sets forth selected historical financial and operating data as at and for the periods indicated. The following selected financial data is qualified in its entirety by, and should be read in conjunction with, our consolidated financial statements and related notes and management's discussion and analysis of financial condition and results of operations included in our Annual Report on Form 10-K for the year ended December 31, 2011, which is incorporated by reference in this proxy statement.

	Years Ended December 31,				
	2011	2010	2009	2008	2007 <sup>(1)</sup>
(Euro in thousands, other than per share and per ADMT amounts)					
<b>Statement of Operations Data</b>					
Revenues					
Pulp	831,396	856,311	577,298	689,320	704,391
Energy	57,972	44,225	42,501	30,971	22,904
	889,368	900,536	619,799	720,291	727,295
Costs and expenses	778,249	732,793	632,598	706,962	657,709
Operating income (loss)	111,119	167,743	(12,799)	13,329	69,586
Gain (loss) on derivative instruments	(1,418)	1,899	(5,760)	(25,228)	20,357
Interest expense	58,995	67,621	64,770	65,756	71,400
Investment income (loss)	1,501	468	(1,804)	(1,174)	4,453
Income (loss) from continuing operations after income taxes <sup>(2)</sup>	54,006	94,748	(72,125)	(85,540)	23,640
Net income (loss) per share attributable to common shareholders from continuing operations					
Basic	1.00	2.24	(1.71)	(2.00)	0.62
Diluted	0.89	1.56	(1.71)	(2.00)	0.58
Weighted average shares outstanding (in thousands)					
Basic	50,117	38,591	36,297	36,285	36,081
Diluted	56,986	56,963	36,297	36,285	45,303
<b>Balance Sheet Data</b>					
Current assets	373,226	356,880	200,934	258,901	290,259
Current liabilities	126,067	125,197	101,784	104,527	121,516
Working capital	247,159	231,683	99,150	154,374	168,743
Total assets	1,217,250	1,216,075	1,083,831	1,151,600	1,272,393
Long-term liabilities	807,641	877,315	896,074	914,970	895,262
Total equity	283,542	213,563	85,973	132,103	255,615
<b>Other Data</b>					
Pulp sales volume (ADMTs)	1,427,924	1,428,638	1,445,461	1,423,300	1,352,590
Pulp production (ADMTs)	1,453,677	1,426,286	1,397,441	1,424,987	1,404,673
Average pulp price realized (per ADMT) <sup>(3)</sup>	574	591	393	478	516

(1) The presentation for 2007 has been modified to conform to the presentation requirements as prescribed in the Accounting Standards Codification Topic 810, *Consolidations*.

(2) We do not report the effect of government grants relating to our assets in our income. These grants reduce the cost basis of the assets purchased.

(3) Our average realized pulp price reflects customer discounts and price movements between the order and shipment date.



**Table of Contents****Selected Historical Financial Data of Fibrek**

The following table sets forth selected historical financial and operating data of Fibrek, presented in accordance with IFRS as at and for the periods indicated. The following selected financial data is qualified in its entirety by, and should be read in conjunction with, Fibrek's consolidated financial statements and related notes attached as Annex A to this proxy statement and Management's Discussion and Analysis of Financial Condition and Results of Operations for Fibrek attached as Annex B to this proxy statement.

Financial statements for Fibrek attached as Annex A to this proxy statement have been prepared in accordance with IFRS, which differs from GAAP in certain material respects, and thus they may not be comparable to financial statements of U.S. companies.

	<b>Years Ended December 31,</b>	
	<b>2011<sup>(1)</sup></b>	<b>2010<sup>(1)</sup></b>
	<b>(Canadian Dollars in thousands, other than per share and per ADMT amounts)</b>	
<b>Statement of Operations Data</b>		
Total Sales	C\$ 537,690	C\$ 556,539
Profit (loss) from operations	C\$ 5,388	C\$ 35,022
Net income (loss)	C\$ (64,031)	C\$ 16,594
Net income (loss) per share		
Basic	C\$ (0.49)	C\$ 0.15
Diluted	C\$ (0.49)	C\$ 0.12
<b>Balance Sheet Data</b>		
Total assets	C\$ 481,792	C\$ 555,900
Long-term liabilities	C\$ 156,068	C\$ 112,918
<b>Other Data</b>		
Pulp sales volume (ADMTs)		
NBSK pulp	341,441	343,627
RBK pulp	346,481	368,538
Total pulp sales volume	687,922	712,165

(1) Selected financial data presented in accordance with IFRS.

**Table of Contents****Unaudited Pro Forma Consolidated Balance Sheet**

As at December 31, 2011

(In thousands of Euros)

	Mercer GAAP	Fibrex IFRS	Adjustments GAAP	Note	Fibrex GAAP	Acquisition Adjustments	Note	Pro Forma Consolidated
<b>ASSETS</b>								
Current assets								
Cash and cash equivalents	105,072	4,226			4,226			109,298
Marketable securities	12,216	24			24			12,240
Receivables	120,487	47,975			47,975			168,462
Inventories	120,539	75,698			75,698			196,237
Prepaid expenses and other	8,162	2,420			2,420			10,582
Deferred income tax	6,750							6,750
<b>Total current assets</b>	<b>373,226</b>	<b>130,343</b>			<b>130,343</b>			<b>503,569</b>
Long-term assets								
Property, plant and equipment	820,974	233,267	135,790	4(a)(b)(c)	369,057	(198,013)	4(k)	992,018
Deferred note issuance and other	10,763	1,577	1,358	4(g)	2,935	(1,604)	4(n)(k)	12,094
Deferred income tax	12,287							12,287
Note receivable								
	844,024	234,844	137,148		371,992	(199,617)		1,016,399
<b>Total assets</b>	<b>1,217,250</b>	<b>365,187</b>	<b>137,148</b>		<b>502,335</b>	<b>(199,617)</b>		<b>1,519,968</b>
<b>LIABILITIES</b>								
Current liabilities								
Accounts payable and other	99,640	50,490			50,490	7,262	4(h)(i)(j)(n)	157,392
Pension and other post-retirement benefit obligations	756							756
Debt	25,671	1,528	334	4(g)	1,862	3,790	4(n)	31,323
<b>Total current liabilities</b>	<b>126,067</b>	<b>52,018</b>	<b>334</b>		<b>52,352</b>	<b>11,052</b>		<b>189,471</b>
Long-term liabilities								
Debt	708,415	84,860	1,024	4(g)	85,884	48,552	4(n)(q)	842,851
Unrealized interest rate derivative losses	52,391							52,391
Pension and other post-retirement benefit obligations	31,197	28,924			28,924			60,121
Capital leases and other	13,053	4,512	(827)	4(d)	3,685			16,738
Deferred income tax	2,585							2,585
	807,641	118,296	197		118,493	48,552		974,686
<b>Total liabilities</b>	<b>933,708</b>	<b>170,314</b>	<b>531</b>		<b>170,845</b>	<b>59,604</b>		<b>1,164,157</b>
<b>EQUITY</b>								
Shareholders' equity								
Share capital	247,642	527,960			527,960	(452,162)	4(m)(p)	323,440
Paid-in capital	(4,857)					716	4(q)	(4,141)
Retained earnings (deficit)	37,985	(331,427)	148,171	4(a) to (f)	(183,256)	179,011	4(m)(i)	33,740
Accumulated other comprehensive income	21,346	(1,660)	(11,554)	4(e)(f)	(13,214)	13,214	4(m)	21,346

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Total shareholder equity	302,116	194,873	136,617	331,490	(259,221)	374,385
Noncontrolling deficit	(18,574)					(18,574)
Total equity	283,542	194,873	136,617	331,490	(259,221)	355,811
Total liabilities and equity	1,217,250	365,187	137,148	502,335	(199,617)	1,519,968

*The accompanying notes are an integral part of these financial statements.*

**Table of Contents****Unaudited Pro Forma Consolidated Statement of Operations**

For the year ended December 31, 2011

(In thousands of Euros, except per share data)

	Mercer GAAP	Fibrex IFRS	Adjustments GAAP	Note	Fibrex GAAP	Acquisition Adjustments	Note	Pro Forma Consolidated
<b>Revenues</b>								
Pulp	831,396	390,735			390,735			1,222,131
Energy	57,972							57,972
	889,368	390,735			390,735			1,280,103
<b>Costs and expenses</b>								
Operating costs	683,718	347,752	4,834	4(c)	352,586			1,036,304
Operating depreciation and amortization	55,760	26,067	528	4(b)(c)	26,595	(10,200)	4(l)	72,155
	149,890	16,916	(5,362)		11,554	10,200		171,644
Selling, general and administrative expenses	38,771	12,131			12,131			50,902
Operating income (loss)	111,119	4,785	(5,362)		(577)	10,200		120,742
<b>Other income (expense)</b>								
Impairment		(45,771)	45,771	4(a)				
Interest expense	(58,995)	(8,270)			(8,270)	(4,068)	4(o)	(71,333)
Investment income	1,501	140			140			1,641
Foreign exchange gain on debt	1,175							1,175
Gain (loss) on extinguishment of debt	(71)	2,000			2,000			1,929
Gain (loss) on derivative instruments	(1,418)	538			538			(880)
Total other income (expense)	(57,808)	(51,363)	45,771		(5,592)	(4,068)		(67,468)
Income (loss) before income taxes	53,311	(46,578)	40,409		(6,169)	6,132		53,274
Income tax benefit (provision)								
Current	(1,682)	49			49			(1,633)
Deferred	2,377							2,377
Net income (loss)	54,006	(46,529)	40,409		(6,120)	6,132		54,018
Less: net income attributable to noncontrolling interest	(3,931)							(3,931)
Net income (loss) attributable to common shareholders	50,075	(46,529)	40,409		(6,120)	6,132		50,087
<b>Net income per share attributable to common shareholders</b>								
Basic	1.00							0.81
Diluted	0.89							0.74

*The accompanying notes are an integral part of these financial statements.*



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**Notes To The Unaudited Pro Forma Consolidated Financial Statements**

**(In thousands of Euros, except shares and per share data)**

**Note 1. Basis of Presentation**

The unaudited pro forma consolidated balance sheet of Mercer International Inc. ( Mercer or the Company ) as at December 31, 2011, and the unaudited pro forma consolidated statement of operations for the year ended December 31, 2011 have been prepared by Mercer, after giving effect to the business combination between Mercer and Fibrek Inc. ( Fibrek ) as if it had occurred on December 31, 2011 for the unaudited pro forma consolidated balance sheet and on January 1, 2011 for the unaudited pro forma consolidated statement of operations. These unaudited pro forma consolidated financial statements have been compiled from, and include:

- (a) a pro forma consolidated balance sheet combining the audited consolidated balance sheet of Mercer as at December 31, 2011 and the audited consolidated statement of financial position of Fibrek as at December 31, 2011;
- (b) a pro forma consolidated statement of operations combining the audited consolidated statement of operations of Mercer for the year ended December 31, 2011 and the audited consolidated statement of earnings for Fibrek for the year ended December 31, 2011.

The financial statements of Mercer have been prepared in conformity with GAAP. The financial statements of Fibrek have been prepared in conformity with IFRS and have been reconciled with GAAP.

It is the Company's opinion that the pro forma consolidated balance sheet and pro forma consolidated statement of operations include all adjustments necessary for the fair presentation, in all material respects, of the pro forma financial statements as if the offer described in Note 3 to the pro forma consolidated financial statements had occurred as of the applicable dates. The adjustments and assumptions required to reflect the offer as of the applicable dates are described in Note 4 to the pro forma consolidated financial statements. The pro forma information is based on preliminary estimates; the final amounts recorded for the offer may differ materially from the information presented. These estimates are subject to change pending further review of the assets acquired and liabilities assumed.

The offer is reflected in the pro forma consolidated financial statements as being accounted for based on the acquisition method in accordance with the Accounting Standards Codification Topic 805, *Business Combinations*. Under the acquisition method, the total estimated purchase price is calculated as described in Note 3 to the pro forma consolidated financial statements. In accordance with the accounting guidance for business combinations, the assets acquired and liabilities assumed have been measured at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurements utilized estimates based on key assumptions of the offer, including historical and current market data. The pro forma adjustments included herein may be revised as additional information becomes available and as additional analysis is performed. The final fair value of assets acquired and liabilities assumed will be determined after the offer is complete, and may differ materially from the information presented.

The pro forma consolidated financial statements do not reflect cost savings (or associated costs to achieve such savings) from operating efficiencies, synergies or other restructuring that could result from the offer.

The unaudited pro forma consolidated financial statements should be read in conjunction with Mercer's audited consolidated financial statements for the year ended December 31, 2011 and Fibrek's audited consolidated financial statements for the year ended December 31, 2011.

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### **Note 2. Significant Accounting Policies**

The accounting policies used in the preparation of these pro forma consolidated financial statements are those set out in Mercer's audited consolidated financial statements of the year ended December 31, 2011. Fibrek follows IFRS, as outlined in Fibrek's consolidated financial statements as at December 31, 2011. As a result, in preparation of the pro forma financial statements, several adjustments were made to the Fibrek consolidated financial statements to conform to GAAP.

The pro forma consolidated financial statements are prepared in Euros (€), Mercer's reporting currency. Fibrek's audited consolidated financial statements are reported in Canadian dollars (C\$). Mercer translated Fibrek's consolidated statement of financial position to Euros using the exchange rate as at December 31, 2011 (C\$1.3193 to €1.00) and translated Fibrek's consolidated statement of earnings at the average rate of exchange for the year ended December 31, 2011 (C\$1.3761 to €1.00).

Certain amounts in Fibrek's consolidated financial statements have been reclassified to conform to Mercer's presentation.

Further accounting policy differences may be identified after completion and integration of the offer.

### **Note 3. Acquisition**

On February 9, 2012, Mercer entered into a Support Agreement with Fibrek for Mercer to acquire all of the Fibrek Shares by way of a take-over bid.

Pursuant to the offer, Fibrek shareholders will have the ability, on an individual basis, to elect to receive:

C\$1.30 in cash per Fibrek Share subject to proration;

0.1540 of a Mercer Share per Fibrek Share subject to proration; or

C\$0.54 in cash plus 0.0903 of a Mercer Share per Fibrek Share, subject to proration necessary to effect a maximum aggregate cash consideration of C\$70.0 million (€53,058) and a maximum aggregate share consideration of 11,741,496 Mercer Shares. Total consideration is C\$1.30 per Fibrek Share or approximately C\$170.0 million (€128,856). For the purpose of the pro forma consolidated financial statements we have assumed the maximum permitted amount of cash of C\$70.0 million, net of C\$5.6 million (€4,226) cash acquired from Fibrek and the cash given to Fibrek for the Warrants described in the following paragraph.

Concurrently with the execution of the Support Agreement, Mercer has agreed to purchase 32,320,000 special warrants (the Warrants) at a price of C\$1.00 per Warrant (the Warrant Placement) for total consideration of C\$32.3 million (€24,498). Each Warrant is convertible into a Fibrek Share on a one-for-one basis. Conversion is automatic in certain events and otherwise at the option of Mercer. The Warrants are also redeemable, including by Fibrek, at their subscription price in certain events. Completion of the Warrant Placement is subject to, among other things, obtaining Toronto Stock Exchange approval.

On February 23, 2012, the *Bureau de décision* dismissed Abitibi's request to cease trade the Offer and granted an order to cease trade the Warrant Placement. Subsequently, on February 24, 2012, Fibrek announced that it intended to appeal the decision to cease trade the Warrant Placement rendered by the *Bureau de décision*. For the purpose of the pro forma financial statements, we have assumed the Warrants will be issued.

**Table of Contents****Note 3. Acquisition (continued)**

Mercer is financing the cash portion of the offer by way of C\$70.0 million of new credit facilities established with Québec based capital providers and/or cash in hand and/or existing credit facilities. For the purpose of the pro forma financial statements, we have assumed the new credit facilities will finance the cash portion of the offer.

Mercer has completed a preliminary estimate of the fair value of all identifiable assets acquired and liabilities assumed. The fair value of all the assets acquired and liabilities assumed will ultimately be determined after the closing of the offer. Therefore, it is likely that the fair value of the assets acquired and liabilities assumed will vary from those shown below, and the differences may be material.

Purchase price:	
Cash issued for shares	48,832
Shares	75,798
	124,630
Fair value of assets acquired and liabilities assumed as at December 31, 2011:	
Current assets, net of cash acquired	126,117
Property, plant and equipment	171,044
Other long-term assets	581
Current liabilities, excluding current portion of long-term debt	(52,757)
Long-term debt	(87,746)
Employee future benefits	(28,924)
Other long-term liabilities	(3,685)
	124,630

**Note 4. Pro Forma Assumptions and Adjustments**

The pro forma consolidated financial statements include the following pro forma assumptions and adjustments.

**Adjustments from IFRS to GAAP:**

- (a) Reverse property, plant and equipment impairments of 151,557 recorded under IFRS. Under IFRS, a write-down of assets is required if the recoverable amount is less than its carrying amount. The recoverable amount is determined using discounted estimated future cash flows. Under GAAP, a write-down to estimate fair value is required only if the undiscounted future cash flows of the assets is less than the carrying amount. Using undiscounted cash flows Fibrek's assets are not impaired. Of the 151,557 impairment reversal, 45,771 was recorded in net income and 105,786 decreased the opening deficit.
- (b) Recognize accumulated depreciation expense in property, plant and equipment of 10,382 as a result of the impairment reversal noted in Note 4(a) above. Depreciation expense of 4,977 was recorded in net income and an adjustment of 5,405 increased the opening deficit.
- (c) Expense major maintenance costs of 5,385 capitalized in property, plant and equipment under IFRS as at December 31, 2011. Under IFRS, major inspections and overhauls are accounted for as a separate component of property, plant and equipment and amortized until the next major inspection or overhaul, and under GAAP these costs are directly expensed.

As part of this adjustment, 4,834 was recorded to

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**Note 4. Pro Forma Assumptions and Adjustments (continued)**

operating costs for the current year maintenance costs, 4,449 of depreciation expense was reversed and the remaining balance of 5,000 increased the opening deficit.

- (d) Reduce the landfill closure obligation by 827 for the change in discount rate used to calculate the obligation. Under IFRS, asset retirement obligations are calculated using a rate that reflects current market assessments of the time value of money and the risks specific to the liability. Under GAAP, the discount rate used is the risk-free interest rate adjusted for the effect of Fibrek's credit standing. The adjustment decreased the opening deficit by 827.
- (e) Upon the adoption of IFRS, Fibrek elected to apply the first time adoption exemption to recognize all unrecognized actuarial losses of 7,988 in deficit. Under GAAP, unrecognized actuarial losses are recorded in accumulated other comprehensive income, consequently these costs have been reclassified.
- (f) Upon the adoption of IFRS, Fibrek recognized the unrealized loss on translation of financial statements of foreign operations of 3,566 in deficit. Under GAAP, the unrealized loss is recorded in accumulated other comprehensive income, consequently these costs have been reclassified.
- (g) Under IFRS, a portion of Fibrek's deferred finance costs of 1,024 are included as an offset to the long-term portion of debt and 334 are included as an offset to the current portion of debt. Under GAAP these costs are recorded as an asset.

**Acquisition of Fibrek:**

- (h) Increase in accounts payable and other of 1,895 representing Fibrek's estimated costs associated with the offer.
- (i) Increase in accounts payable and other and deficit of 4,245 representing Mercer's estimated costs associated with the offer. These costs have been excluded from the pro forma consolidated statement of operations as they are non-recurring.
- (j) Increase in accounts payable and other of 372 associated with Fibrek's performance share program as a result of the assumed change in control.
- (k) Recognition of the property, plant and equipment preliminary estimated fair value adjustment of 198,013 and the write off of Fibrek's deferred financing costs of 2,354, based on the preliminary estimated purchase price allocation.
- (l) Preliminary estimated depreciation of 10,200 associated with the property, plant and equipment fair value adjustment calculated using a 20 year useful life.
- (m) Elimination of Fibrek's shareholders' equity.

**Financing for the Fibrek acquisition:**

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- (n) Recognition of credit facilities totalling C\$70.0 million ( 53,058) required to finance the offer. The long term portion of the credit facilities is 49,268 and the current portion of the credit facilities is 3,790. Finance costs related to the offer amounted to 750 and were included in accounts payable and other as at December 31, 2011.
- (o) Recognition of interest expense totalling 4,068 on the credit facilities using an interest rate of 8.5% for C\$40.0 million ( 30,318) of the debt and 6.5% for C\$30.0 million ( 22,740) of the debt.
- (p) Recognition of 11,741,496 shares issued, valued at 75,798 required to finance the offer.
- (q) Recognition of warrants issued as part of a credit facility agreement required to finance the offer valued at 716. The warrants are for 500,000 Mercer Shares at a subscription price equal to a 30% premium to the market price at the credit facility closing date.

**Table of Contents****Note 5. Pro Forma Earnings Per Share**

	<b>2011</b>
Pro forma net income attributable to common shareholders basic	50,087
Interest on convertible notes, net of tax	797
Pro forma net income attributable to common shareholders diluted	50,884
Pro forma net income per share attributable to common shareholders	
Basic	0.81
Diluted	0.74
Weighted average common shares, December 31, 2011	
Basic weighted average Mercer Shares outstanding	50,116,982
Mercer Shares issued on acquisition of Fibrek	11,741,496
Basic pro forma weighted average common shares outstanding	61,858,478
Effect of diluted shares	6,869,037
Diluted pro forma weighted average common shares outstanding	68,727,515
Outstanding common shares, December 31, 2011	
Mercer Shares outstanding	55,779,204
Mercer Shares issued on acquisition of Fibrek	11,741,496
Pro forma common shares outstanding	67,520,700

The 500,000 warrants issued to the lender of the C\$25.0 million credit facility are excluded from the calculation of diluted income per share attributable to common shareholders because they are anti-dilutive.

**Comparative Historical and Unaudited Pro Forma Per Share Data**

The following table sets forth certain historical, and pro forma combined financial information. The following tables set forth the Mercer historical net income (loss) per share for the year ended December 31, 2011, on an unaudited basis, and year ended December 31, 2010, and the historical book value per share as of December 31, 2011 and December 31, 2010, on an unaudited basis, and net income (loss) per share for Mercer on an unaudited pro forma combined basis, for the year ended December 31, 2011 and year ended December 31, 2010, and unaudited pro forma book value per share as of December 31, 2011. The following tables also set forth for Fibrek historical net income (loss) per share for the year ended December 31, 2011 and year ended December 31, 2010, on an unaudited basis, and the historical book value per share as of December 31, 2011 and December 31, 2010, on an unaudited basis. The information presented is based on the IFRS financial statements of Fibrek for the year ended December 31, 2011, which are included with this proxy statement.

The unaudited pro forma combined data were derived from and should be read together with the unaudited pro forma condensed combined financial statements and accompanying notes included in this proxy statement. This information is based on the historical balance sheets and related historical statements of operations of Mercer which have been incorporated by reference into this proxy statement and Fibrek which are included in this proxy statement. The pro forma combined data give effect to the transaction using the purchase method of accounting for business combinations.

**Table of Contents****Note 5. Pro Forma Earnings Per Share (continued)**

The unaudited pro forma combined per share data is presented for informational purposes only and is not intended to represent or be indicative of the per share data that would have been achieved if the Offer had been completed as of the dates indicated, and should not be taken as representative of future consolidated per share data of Mercer. The historical data of Mercer and Fibrek's historical data were derived from and should be read together with the consolidated financial statements and accompanying notes included elsewhere, or incorporated by reference into this proxy statement.

	<b>Years Ended December 31,</b>	
	<b>2011</b>	<b>2010</b>
<b>Mercer's Historical Data:</b>		
Net income per share <sup>(1)</sup> :		
Basic	1.00	2.24
Diluted	0.89	1.56
As of December 31, 2011 and 2010:		
Consolidated book value per share <sup>(2)</sup>	5.42	5.49
<b>Fibrek's Historical Data:</b>		
Net income (loss) per share:		
Basic <sup>(3)</sup>	C\$ (0.49)	C\$ 0.15
Diluted <sup>(3)</sup>	C\$ (0.49)	C\$ 0.12
As of December 31, 2011 and 2010:		
Consolidated book value per share <sup>(2)</sup>	C\$ 1.98	C\$ 2.58
<b>Pro Forma Combined Data:</b>		
	<b>(Unaudited)</b>	
Pro forma net income per share:		
Basic <sup>(4)</sup>	0.81	
Diluted <sup>(4)</sup>	0.74	
As of December 31, 2011:		
Pro forma book value per share <sup>(5)</sup>	5.54	

- (1) Historical net income per share was derived from Mercer's Annual Report on Form 10-K for the year ended December 31, 2011 as filed with the SEC and incorporated by reference into this proxy statement.
- (2) Consolidated book value per share was calculated by dividing total shareholders' equity by the common shares outstanding as of the respective dates.
- (3) Basic net income (loss) per share was calculated by dividing the estimated net income (loss) for IFRS purposes by the weighted average common shares outstanding. Diluted net income (loss) per share was calculated using diluted weighted average common shares outstanding.
- (4) Basic pro forma net income per share was calculated by dividing pro forma net income by the pro forma weighted average common shares outstanding as if the transaction had occurred on January 1, 2011. Diluted pro forma net income per share was calculated using pro forma diluted weighted average common shares outstanding.
- (5) Pro forma book value per share was calculated by dividing pro forma total shareholders' equity by the pro forma common shares outstanding as if the transaction had occurred on December 31, 2011.

**Table of Contents****MARKET PRICE AND DIVIDEND INFORMATION**

Mercer Shares are traded on the NASDAQ Global Market under the symbol **MERC** and on the Toronto Stock Exchange under the symbol **MRI.U**. Fibrek Shares are traded on the Toronto Stock Exchange under the symbol **FBK**. Following the consummation of the Offer, Mercer Shares, including the shares issued in connection with the Offer, are expected to continue to trade on the NASDAQ Global Market under the symbol **MERC** and on the Toronto Stock Exchange under the symbol **MRI.U**. The following table sets forth the respective high and low closing prices of Mercer Shares and Fibrek Shares for the periods indicated. The market prices set forth below may not be indicative of the future value of Mercer Shares.

	Mercer (NASDAQ)			Fibrek (TSX)		
	High (US\$)	Low (US\$)	Aggregate Avg. Daily Volume (#)	High (C\$)	Low (C\$)	Aggregate Avg. Daily Volume (#)
<b>Annual Information for the past 5 years</b>						
2007	13.68	7.04	238,875	5.56	1.89	293,873
2008	8.99	1.60	200,913	2.31	0.41	136,235
2009	3.73	0.27	204,464	1.00	0.20	164,965
2010	7.95	2.68	335,413	1.88	0.77	178,584
2011	14.88	5.34	400,027	1.65	0.69	150,010
<b>Quarterly Information for the past 3 years</b>						
<b>2009</b>						
First Quarter	2.14	0.27	123,442	0.84	0.35	72,599
Second Quarter	1.23	0.57	190,324	0.40	0.20	196,770
Third Quarter	3.73	0.50	409,883	0.75	0.20	233,324
Fourth Quarter	3.50	1.90	90,189	1.00	0.59	155,699
<b>2010</b>						
First Quarter	5.87	2.68	328,256	1.45	0.77	154,753
Second Quarter	6.08	3.98	461,473	1.88	1.04	228,003
Third Quarter	5.58	3.97	223,854	1.07	0.90	157,274
Fourth Quarter	7.95	4.93	329,703	1.25	0.98	173,928
<b>2011</b>						
First Quarter	14.05	7.66	564,013	1.65	1.15	208,755
Second Quarter	14.88	10.08	446,888	1.64	1.27	104,117
Third Quarter	11.25	6.80	332,906	1.37	0.75	57,481
Fourth Quarter	7.46	5.34	259,968	1.02	0.69	247,673
<b>Monthly Information for the past 12 months</b>						
February 2011	13.91	8.42	920,626	1.59	1.34	252,428
March 2011	14.05	12.36	492,850	1.65	1.36	202,775
April 2011	14.88	12.17	473,678	1.64	1.54	177,356
May 2011	13.73	11.55	485,289	1.64	1.45	105,056
June 2011	12.89	10.08	385,878	1.46	1.27	36,638
July 2011	11.25	9.17	334,039	1.37	1.10	67,629
August 2011	9.53	7.22	466,611	1.13	0.94	50,187
September 2011	8.76	6.80	185,388	0.99	0.75	55,458
October 2011	7.46	6.56	268,867	1.00	0.70	47,072
November 2011	6.85	5.34	313,617	0.97	0.69	326,232
December 2011	6.53	5.74	197,422	1.02	0.97	476,046
January 2012	8.18	6.23	267,921	1.12	1.00	255,166
February 2012 (through February 27, 2012)	8.68	7.60	235,718	1.34	1.01	1,845,341

**Table of Contents****Mercer International Inc.**

On February 9, 2012, the last full trading day prior to the public announcement of entry into the Support Agreement, the closing price per Mercer Share as reported on the NASDAQ Global Market was \$8.25 per share. On February 27, 2012, the last practicable date before the filing of this proxy statement, the closing price per Mercer Share as reported on the NASDAQ Global Market was \$8.43. Because the market price of Mercer Shares is subject to fluctuation, the market value of the Mercer Shares that holders of Fibrek Shares will receive pursuant to the Offer may increase or decrease. As of February 27, 2012, Mercer had approximately 329 shareholders of record.

Mercer has never declared or paid cash dividends on its capital stock. Mercer currently intends to retain earnings, if any, to finance the growth and development of its business, and does not expect to pay any cash dividends to its shareholders in the foreseeable future. Payment of future dividends, if any, will be at the discretion of Mercer's board of directors and subject to the terms of the Company's senior indebtedness.

**Fibrek Inc.**

On February 9, 2012, the last full trading day prior to the public announcement of entry into the Support Agreement, the closing price per Fibrek Share as reported on the Toronto Stock Exchange was C\$1.13 per share. On February 27, 2012, the last practicable date before the filing of this proxy statement, the closing price per Fibrek Share as reported on the Toronto Stock Exchange was C\$1.18.

Fibrek has not declared or paid cash dividends on its capital stock since converting to a corporation from an income trust in March 2010.

**Comparative Per Share Market Price Data**

The following table sets forth the high, low and closing prices for Mercer Shares on the NASDAQ Global Market and Fibrek Shares as reported on the Toronto Stock Exchange on February 9, 2012, the last trading day before Mercer and Fibrek announced the Offer, and February 27, 2012. The table also includes the value of a Fibrek Share on an equivalent price per share basis, as determined by reference to the share exchange ratio to be applied in respect of each Fibrek Share tendered in the Offer. These equivalent prices per share reflect the fluctuating value of Mercer Shares that Fibrek shareholders would receive in exchange for each Fibrek Share tendered if the Offer was closed on either of these dates, applying the share exchange ratio of 0.1540 of a Mercer Share in exchange for each Fibrek Share tendered, if the tendering shareholders elected to receive only Mercer Shares.

	Mercer Shares			Fibrek Shares			Equivalent share price of Fibrek Shares with Exchange Ratio of 0.1540:1		
	High	Low	Close	High	Low	Close	High	Low	Close
February 9, 2012	\$ 8.50	\$ 8.23	\$ 8.25	C\$ 1.14	C\$ 1.11	C\$ 1.13	\$ 1.31	\$ 1.27	\$ 1.27
February 27, 2012	\$ 8.80	\$ 8.36	\$ 8.43	C\$ 1.22	C\$ 1.17	C\$ 1.18	\$ 1.35	\$ 1.29	\$ 1.30

The table above shows only historical comparisons. These comparisons may not provide meaningful information to Mercer shareholders in determining whether to approve the issuance of Mercer Shares in connection with the Offer. Mercer and Fibrek shareholders are urged to obtain current market quotations for Mercer Shares and Fibrek Shares and to review carefully the other information contained in this proxy statement. See "Where You Can Find Additional Information" in this proxy statement. Based on the volume weighted average price of the Mercer Shares for the five trading days preceding the announcement of our intention to make the Offer, being C\$8.44, the value of the consideration offered by Mercer under the Offer that a Fibrek shareholder having elected any of the consideration options thereunder would have received under the Offer is C\$1.30.

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**RISK FACTORS**

*The information below sets forth the risks and uncertainties relating to the Offer and the proposals disclosed in this proxy statement could materially adversely affect Mercer's business, financial condition and/or operating results. This information should be read in conjunction with Mercer's annual report on Form 10-K for the year ended December 31, 2011, which is incorporated by reference into this proxy statement. You should fully consider these risks in determining whether to vote in favor of the proposals described herein.*

**Cautionary Statement Concerning Forward-Looking Statements and Risk Factors**

This proxy statement and the documents incorporated by reference herein contain forward-looking statements that involve risks and uncertainties, as well as assumptions, that could cause the results of Mercer or Fibrek to differ materially from those expressed or implied by such forward-looking statements. Forward-looking statements generally are identified by the words may, will, project, might, expects, anticipates, believes, intends, estimates, should, could, would, strategy, plan, continue, pursue, or the negative of these words and expressions of similar meaning. All statements, other than statements of historical fact, are statements that could be deemed forward-looking statements. For example, forward-looking statements include any statements of the plans, strategies and objectives of management for future operations, including the execution of integration and restructuring plans and the anticipated timing of filings; any statements concerning proposed new products, services or developments; any statements regarding future economic conditions or performance; statements of belief and any statement of assumptions underlying any of the foregoing. Forward-looking statements may also include any statements of the plans, strategies and objectives of management with respect to the approval and closing of the Offer, Mercer's ability to solicit a sufficient number of proxies to approve the issuance of Mercer Shares in connection with the Offer, and other matters related to the consummation of the Offer.

Additional factors that could cause actual results to differ materially from those expressed in the forward-looking statements are discussed in reports filed with the SEC by Mercer. See the section entitled [Where You Can Find More Information](#).

If any of these risks or uncertainties materializes or any of these assumptions proves incorrect, the results of Mercer, Fibrek and the combined companies could differ materially from the forward-looking statements. All forward-looking statements in this proxy statement are current only as of the date on which the statements were made. Mercer and Fibrek do not undertake any obligation to publicly update any forward-looking statement to reflect events or circumstances after the date on which any statement is made or to reflect the occurrence of unanticipated events.

**Risk Factors relating to the Offer**

*We will incur additional indebtedness following completion of the Offer.*

We will incur indebtedness in connection with the completion of the Offer as a result of entering into new loan facilities. Such additional indebtedness will be incremental to current indebtedness. See [Risk Factors](#) Our level of indebtedness could negatively impact our financial condition and results of operations. Our ability to make payments of the principal and interest on such additional indebtedness or any other indebtedness depends upon our ability to generate cash from operations. If the cash generated from our activities is insufficient to meet the obligations to pay interest and principal when due under any additional loan facility or such other indebtedness, or if we fail to comply with any terms or conditions thereof, the lenders thereto may exercise their rights under such indebtedness (including any security arrangements in respect thereto), which could result in a material adverse effect on us. A breach of loan covenants and undertakings could result in a significant loss to us.

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*The Offer is conditional upon, among other things, the receipt of consents and approvals from governmental authorities that could delay completion of the Offer or impose conditions on us and Fibrek that could in turn result in an adverse effect on the business or financial condition of Mercer following our acquisition of Fibrek.*

The Offer is conditional upon, among other things, our having obtained all approvals, consents and clearances from every governmental authority that we reasonably determine are necessary or advisable in connection with the Offer, including the expiration or earlier termination of the waiting periods under the HSR Act and the receipt of approvals under the Competition Act and the ICA. While we expect to obtain the required regulatory approvals, we cannot be certain that all the required approvals will be obtained or, if obtained, on what terms such approvals will be obtained. A substantial delay in obtaining satisfactory approvals or the imposition of unfavorable terms or conditions in connection with obtaining the approvals could delay completion of the Offer or have an adverse effect on the business, financial condition or results of operations of Mercer following the acquisition of Fibrek.

*If the conditions under the Support Agreement are not met or waived, the Offer cannot be completed.*

Even if the issuance of the Mercer Shares to be issued in the Offer is approved by the shareholders of Mercer, specified conditions must be satisfied or waived to complete the Offer. These conditions are described in the Support Agreement. Mercer cannot assure you that all of the conditions will be satisfied. If the conditions are not satisfied or waived, the Offer cannot be completed or will be delayed, which would result in the loss of some or all of the expected benefits of the potential acquisition of Fibrek.

*Change-of-control provisions in Fibrek's agreements triggered in connection with the acquisition of Fibrek may lead to adverse consequences.*

Fibrek may be a party to agreements that contain change-of-control or similar provisions that may be triggered in connection with the Offer, as a result of our acquisition of at least a majority of Fibrek Shares. The operation of these change-of-control or similar provisions, if triggered, could result in unanticipated expenses in connection with the consummation of the Offer.

Certain Fibrek employee benefit plans or agreements contain change-of-control clauses providing for compensation to be granted to certain senior officers of Fibrek if, following a change of control, Fibrek terminated the employment relationship between Fibrek and these employees, or if these employees suffer a substantial change in their working conditions within specified periods following a change of control. If successful, we expect that the Offer would constitute a change of control of Fibrek, thereby giving rise to potential change-of-control payments.

*The date on which the Offer will close is uncertain.*

The date on which the Offer will close depends on the satisfaction of the conditions set forth in the Support Agreement, or the waiver of certain of those conditions by Mercer or Fibrek. While Mercer currently expects to complete the Offer in the second quarter of 2012, the completion date of the transaction might be later than expected because of unforeseen events.

### **Additional Risks related to Mercer upon the Successful Completion of the Offer**

*Our acquisition of Fibrek might not be successfully completed without the possibility of Fibrek shareholders exercising dissent rights in connection with a second step transaction.*

In order for us to acquire all of the issued and outstanding Fibrek Shares, it might be necessary, following the completion of the Offer, to effect a second step transaction. A second step transaction under the CBCA might result in Fibrek shareholders having the right to dissent and demand payment of the fair value of their Fibrek Shares. If the statutory procedures governing dissent rights are available, this right could lead to judicial determination of the fair value required to be paid to dissenting Fibrek shareholders.

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### ***There might be difficulties in integrating Fibrek's business and operations into our business and operations.***

The Offer has been made with the expectation that its successful completion will result in increased earnings and cost savings for us following the integration of Fibrek. This expectation is based on presumed synergies from consolidation and enhanced growth opportunities. These anticipated benefits will depend in part on whether Fibrek's operations can be integrated in an efficient and effective manner into our operations, and whether the expected bases or sources of synergies in fact do produce the benefits anticipated. Most operational and strategic decisions, and certain staffing decisions, with respect to Fibrek following its acquisition by us have not yet been made and may not have been fully identified. These decisions and such integration may present significant challenges to management, including the integration of systems and personnel of the two companies, and special risks, including possible unanticipated liabilities, significant one-time write-offs or restructuring charges, unanticipated costs, and the loss of key employees.

While we believe that our expectations regarding the achievement of synergies and other benefits of the Offer are reasonable, there can be no assurance that the integration of Fibrek's operations, management and culture into ours will be timely or effectively accomplished, or ultimately will be successful in increasing earnings and reducing costs.

### ***Integrating Fibrek may divert Mercer's management's attention away from our operations.***

Successful integration of Mercer's and Fibrek's operations and personnel will place an additional burden on our management and our internal resources. This additional burden could lead to a significant diversion of management attention, which could lead to a decrease in Mercer's future operating results and thereby negatively impact its share price.

### ***Failure to retain key employees could diminish the benefits of the Offer.***

The successful combination of Mercer and Fibrek will depend in part on the retention of key personnel of Fibrek, including senior management. There can be no assurances Mercer will be able to retain Fibrek's key personnel. Upon completion of the Offer, certain members of Fibrek's management with change of control employment agreements could trigger such agreements requiring Mercer to pay severance costs in the future.

## **Risks related to Mercer Shares**

### ***The market price of Mercer Shares could decline as a result of the large number of such shares that will become eligible for sale after the completion of the Offer.***

If the Offer is successfully concluded, the new Mercer Shares issued will become saleable immediately following the closing of the Offer. Consequently, a large number of additional Mercer Shares will be eligible for resale in the public market. Current shareholders of Mercer and former shareholders of Fibrek may not wish to continue to invest in the operations of the combined companies after the consummation of the Offer or, for other reasons, may wish to dispose of some or all of their interests in Mercer after the Offer is completed. Sales of a large number of new Mercer Shares in the public market following the completion of the Offer could adversely affect the market price of all Mercer Shares.

### ***The issuance of Mercer Shares to Fibrek shareholders in connection with the Offer will reduce the percentage ownership of current Mercer shareholders.***

If the Offer is completed and assuming that the maximum share consideration under the Support Agreement is required to be issued, Mercer will issue approximately 11,741,496 Mercer Shares as consideration for the outstanding Fibrek Shares. Mercer shareholders will continue to own their existing Mercer Shares, which will not be affected, except that the issuance of Mercer Shares described above will cause a significant reduction in the relative percentage interests of current Mercer shareholders in earnings and voting, as well as liquidation, book and market value.

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*FibreK's current shareholders will own a large percentage of Mercer Shares after the completion of the Offer, and will have significant influence over the outcome of corporate actions requiring shareholder approval; such shareholders' priorities for Mercer's business may be different from Mercer's current shareholders.*

If all of the Fibrek Shares currently outstanding are tendered in the Offer, post-Offer the current shareholders of Mercer will hold approximately 83% of the outstanding shares of Mercer shares and the current shareholders of Fibrek will hold approximately 17% of the outstanding Mercer Shares. Accordingly, such former Fibrek shareholders may be able to influence the outcome of any corporate transaction or other matter submitted to the Mercer shareholders for approval, including the election of directors, any merger, consolidation or sale of all or substantially all of Mercer's assets or any other significant corporate transaction, such that such former shareholders of Fibrek could delay or prevent a change of control of Mercer, even if such a change of control would benefit Mercer's other shareholders. The interests of such former Fibrek shareholders may differ from the interests of other Mercer shareholders.

### **Risk Factors relating to Mercer's Business**

*Our business is highly cyclical in nature.*

The pulp business is highly cyclical in nature and markets for our principal products are characterized by periods of supply and demand imbalance, which in turn affects product prices. Pulp markets are highly competitive and are sensitive to cyclical changes in the global economy, industry capacity and foreign exchange rates, all of which can have a significant influence on selling prices and our operating results. The length and magnitude of industry cycles have varied over time but generally reflect changes in macro-economic conditions and levels of industry capacity.

Industry capacity can fluctuate as changing industry conditions can influence producers to idle production capacity or permanently close mills. In addition, to avoid substantial cash costs in idling or closing a mill, some producers will choose to operate at a loss, sometimes even a cash loss, which can prolong weak pricing environments due to oversupply. Oversupply of our products can also result from producers introducing new capacity in response to favorable pricing trends.

Demand for pulp has historically been determined primarily by the level of economic growth and has been closely tied to overall business activity. From 2006 to mid-2008, pulp prices steadily improved. However, the global economic crisis in the latter half of 2008 resulted in a sharp decline of pulp prices from a high of \$900 per ADMT to \$635 per ADMT at the end of 2008. Pulp prices began to increase in the second half of 2009 and continued to increase to record levels through June of 2010, before declining slightly in the fourth quarter of 2010. Pulp prices again rebounded to record levels in the first half of 2011 but declined sharply in the latter part of the year, primarily due to economic uncertainty in Europe and credit tightening in China. We cannot predict the impact of sustained economic weakness on the demand and prices for our products.

Prices for pulp are driven by many factors outside our control, and we have little influence over the timing and extent of price changes, which are often volatile. Because market conditions beyond our control determine the price for pulp, prices may fall below our cash production costs, requiring us to either incur short-term losses on product sales or cease production at one or more of our mills. Therefore, our profitability depends on managing our cost structure, particularly raw materials which represent a significant component of our operating costs and can fluctuate based upon factors beyond our control. If the prices of our products decline, or if prices for our raw materials increase, or both, our results of operations and cash flows could be materially adversely affected.

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### ***Our level of indebtedness could negatively impact our financial condition and results of operations.***

As of December 31, 2011, we had approximately 734.1 million of indebtedness outstanding, of which 477.5 million relates to the 828.0 million project finance facility at our Stendal mill (the Stendal Loan Facility ). We may also incur additional indebtedness in the future. Our high debt levels may have important consequences for us, including, but not limited to the following:

our ability to obtain additional financing for working capital, capital expenditures, general corporate and other purposes or to fund future operations may not be available on terms favorable to us or at all;

a significant amount of our operating cash flow is dedicated to the payment of interest and principal on our indebtedness, thereby diminishing funds that would otherwise be available for our operations and for other purposes;

increasing our vulnerability to current and future adverse economic and industry conditions;

a substantial decrease in net operating cash flows or increase in our expenses could make it more difficult for us to meet our debt service requirements, which could force us to modify our operations;

our leveraged capital structure may place us at a competitive disadvantage by hindering our ability to adjust rapidly to changing market conditions or by making us vulnerable to a downturn in our business or the economy in general;

causing us to offer debt or equity securities on terms that may not be favorable to us or our shareholders;

limiting our flexibility in planning for, or reacting to, changes and opportunities in our business and our industry; and

our level of indebtedness increases the possibility that we may be unable to generate cash sufficient to pay the principal or interest due in respect of our indebtedness.

The indenture governing our 9.5% senior notes due 2017 (the Senior Notes ) and our bank credit facilities contain restrictive covenants which impose operating and other restrictions on us and our subsidiaries. These restrictions will affect, and in many respects will limit or prohibit, our ability to, among other things, incur or guarantee additional indebtedness or enter into sale/leaseback transactions, pay dividends or make distributions on capital stock or redeem or repurchase capital stock, make investments or acquisitions, create liens and enter into mergers, consolidations or transactions with affiliates. The terms of our indebtedness also restrict our ability to sell certain assets, apply the proceeds of such sales and reinvest in our business.

Failure to comply with the covenants in the indenture relating to our Senior Notes or in our bank credit facilities could result in events of default and could have a material adverse effect on our liquidity, results of operations and financial condition.

Our ability to repay or refinance our indebtedness will depend on our future financial and operating performance. Our performance, in turn, will be subject to prevailing economic and competitive conditions, as well as financial, business, legislative, regulatory, industry and other factors, many of which are beyond our control. Our ability to meet our future debt service and other obligations, in particular the Stendal Loan Facility, may depend in significant part on the extent to which we can implement successfully our business strategy. We cannot assure you that we will be able to implement our strategy fully or that the anticipated results of our strategy will be realized.

***A weakening of the global economy could adversely affect our business and financial results and have a material adverse effect on our liquidity and capital resources.***

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Global financial markets experienced extreme and unprecedented disruption in the second half of 2008, including, among other things, extreme volatility in security prices, severely diminished liquidity and credit availability, rating downgrades of certain investments and declining valuations of others. Although financial

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markets have stabilized and the modest global economic recovery which emerged in the second half of 2009 largely continued through 2011, the overall state of the global economy remains generally weak and we remain subject to a number of risks associated with these adverse economic conditions. Price appreciation in 2010 and the first half of 2011 has been due in significant part to demand from China and other Asian countries, and any reduction in demand in these locations could exacerbate the impact of economic weakness elsewhere.

Principally, as pulp demand has historically been determined by the level of economic growth and business activity, demand and prices for our product have historically decreased substantially during economic slowdowns. Additionally, restricted credit availability restrains our customers ability or willingness to purchase our products resulting in lower revenues. Depending on their severity and duration, the effects and consequences of a global economic downturn could have a material adverse effect on our liquidity and capital resources, including our ability to raise capital, if needed, and otherwise negatively impact our business and financial results.

### ***Cyclical fluctuations in the price and supply of our raw materials could adversely affect our business.***

Our main raw material is fiber in the form of wood chips and pulp logs. Such fiber is cyclical in terms of both price and supply. The cost of wood chips and pulp logs is primarily affected by the supply and demand for lumber. Demand for these raw materials is generally determined by the volume of pulp and paper products produced globally and regionally. Since 2006, generally higher energy prices, a focus on, and governmental initiatives related to, green or renewable energy have led to an increase in renewable energy projects in Europe, including Germany. Demand for wood residuals from such energy producers, combined with lower harvesting rates, has generally put upward pressure on prices for wood residuals such as wood chips in Germany and its neighboring countries. This has resulted in higher fiber costs for our German mills and such trend could continue to put further upward pressure on wood chip prices.

Similarly, North American sawmill activity declined significantly during the recession, reducing the supply of chips and availability of pulp logs to our Celgar mill. Additionally, North American energy producers are exploring the viability of renewable energy initiatives and governmental initiatives in this field are increasing, all of which could lead to higher demand for sawmill residual fiber, including chips. The cyclical nature of pricing for these raw materials represents a potential risk to our profit margins if pulp producers are unable to pass along price increases to their customers or we cannot offset such costs through higher prices for our surplus energy.

We do not own any timberlands or have any long-term governmental timber concessions and we currently have few long-term fiber contracts at our German operations. Raw materials are available from a number of suppliers and we have not historically experienced material supply interruptions or substantial sustained price increases, however our requirements have increased and may continue to increase as we increase capacity through capital projects or other efficiency measures at our mills. As a result, we may not be able to purchase sufficient quantities of these raw materials to meet our production requirements at prices acceptable to us during times of tight supply. In addition, the quantity, quality and price of fiber we receive could be affected as a result of industrial disputes, material curtailments or shut-down of operations by suppliers, government orders and legislation (including new taxes or tariffs), weather conditions, acts of god and other events beyond our control. An insufficient supply of fiber or reduction in the quality of fiber we receive would materially adversely affect our business, financial condition, results of operations and cash flow. In addition to the supply of wood fiber, we are dependent on the supply of certain chemicals and other inputs used in our production facilities. Any disruption in the supply of these chemicals or other inputs could affect our ability to meet customer demand in a timely manner and could harm our reputation. Any material increase in the cost of these chemicals or other inputs could have a material adverse effect on our business, results of operations, financial condition and cash flows.

### ***We operate in highly competitive markets.***

We sell our pulp globally, with a large percentage sold in Europe, North America and Asia. The markets for pulp are highly competitive. A number of other global companies compete in each of these markets and no company holds a dominant position. Our pulp is considered a commodity because many companies produce similar and largely standardized products. As a result, the primary basis for competition in our markets has been

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price. Many of our competitors have greater resources and lower leverage than we do and may be able to adapt more quickly to industry or market changes or devote greater resources to the sale of products than we can. There can be no assurance that we will continue to be competitive in the future. The global pulp market has historically been characterized by considerable swings in prices which have and will result in variability in our earnings. Prices are typically denominated in U.S. dollars.

### ***We are exposed to currency exchange rate and interest rate fluctuations.***

The majority of our sales are in products quoted in U.S. dollars while most of our operating costs and expenses, other than those of the Celgar mill, are incurred in Euros. In addition, all of the products sold by the Celgar mill are quoted in U.S. dollars and the Celgar mill costs are primarily incurred in Canadian dollars. Our results of operations and financial condition are reported in Euros. As a result, our revenues are adversely affected by a decrease in the value of the U.S. dollar relative to the Euro and to the Canadian dollar. Such shifts in currencies relative to the Euro and the Canadian dollar reduce our operating margins and the cash flow available to fund our operations and to service our debt. This could have a material adverse effect on our business, financial condition, results of operations and cash flows.

In 2002, our 74.9% owned subsidiary, Stendal, entered into variable-to-fixed interest rate swaps to fix interest payments under the Stendal mill financing facility, which has kept Stendal from benefiting from the general decline in interest rates that ensued. These derivatives are marked to market at the end of each reporting period and all unrealized gains and losses are recognized as earnings or losses for the relevant reporting periods.

### ***Increases in our capital expenditures or maintenance costs could have a material adverse effect on our cash flow and our ability to satisfy our debt obligations.***

Our business is capital intensive and requires that we regularly incur capital expenditures to maintain our equipment, improve efficiencies and comply with environmental laws. Our annual capital expenditures may vary due to fluctuations in requirements for maintenance, business capital, expansion and as a result of changes to environmental regulations that require capital expenditures to bring our operations into compliance with such regulations. In addition, our senior management and board of directors may approve projects in the future that will require significant capital expenditures. Increased capital expenditures could have a material adverse effect on our cash flow and our ability to satisfy our debt obligations. Further, while we regularly perform maintenance on our manufacturing equipment, key pieces of equipment in our various production processes may still need to be repaired or replaced. If we do not have sufficient funds or such repairs or replacements are delayed, the costs of repairing or replacing such equipment and the associated downtime of the affected production line could have a material adverse effect on our business, financial condition, results of operations and cash flows.

### ***We use derivatives to manage certain risk which has caused significant fluctuations in our operating results.***

We use derivative instruments to limit our exposure to interest rate fluctuations. Concurrently with entering into the Stendal financing, Stendal entered into variable-to-fixed rate interest swaps for the full term of our Stendal Loan Facility to manage its interest rate risk exposure with respect to the full principal amount of this facility. Because we effectively fixed the rate on our Stendal Loan Facility, the value of our derivative position moves inversely to interest rates.

We record unrealized gains or losses on our derivative instruments when they are marked to market at the end of each reporting period and realized gains or losses on them when they are settled. These unrealized and realized gains and losses can materially impact our operating results for any reporting period. For example, our operating results for 2011 included an unrealized net loss of 1.4 million on our interest rate derivative, while our operating results for 2010 included an unrealized net gain of 1.9 million. For 2009, our operating results included an unrealized net loss of 5.8 million on our interest rate derivative.

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If any of the variety of instruments and strategies we utilize are not effective, we may incur losses which may have a materially adverse effect on our business, financial condition, results of operations and cash flow. Further, we may in the future use derivative instruments to manage pulp price risks. The purpose of our derivative activity may also be considered speculative in nature; we do not use these instruments with respect to any pre-set percentage of revenues or other formula, but either to augment our potential gains or reduce our potential losses depending on our perception of future economic events and developments.

### ***We are subject to extensive environmental regulation and we could have environmental liabilities at our facilities.***

Our operations are subject to numerous environmental laws as well as permits, guidelines and policies. These laws, permits, guidelines and policies govern, among other things:

unlawful discharges to land, air, water and sewers;

waste collection, storage, transportation and disposal;

hazardous waste;

dangerous goods and hazardous materials and the collection, storage, transportation and disposal of such substances;

the clean-up of unlawful discharges;

land use planning;

municipal zoning; and

employee health and safety.

In addition, as a result of our operations, we may be subject to remediation, clean up or other administrative orders or amendments to our operating permits, and we may be involved from time to time in administrative and judicial proceedings or inquiries. Future orders, proceedings or inquiries could have a material adverse effect on our business, financial condition and results of operations. Environmental laws and land use laws and regulations are constantly changing. New regulations or the increased enforcement of existing laws could have a material adverse effect on our business and financial condition. In addition, compliance with regulatory requirements is expensive, at times requiring the replacement, enhancement or modification of equipment, facilities or operations. There can be no assurance that we will be able to maintain our profitability by offsetting any increased costs of complying with future regulatory requirements.

We are subject to liability for environmental damage at the facilities that we own or operate, including damage to neighboring landowners, residents or employees, particularly as a result of the contamination of soil, groundwater or surface water and especially drinking water. The costs of such liabilities can be substantial. Our potential liability may include damages resulting from conditions existing before we purchased or operated these facilities. We may also be subject to liability for any offsite environmental contamination caused by pollutants or hazardous substances that we or our predecessors arranged to transport, treat or dispose of at other locations. In addition, we may be held legally responsible for liabilities as a successor owner of businesses that we acquire or have acquired. Except for Stendal, our facilities have been operating for decades and we have not done invasive testing to determine whether or to what extent environmental contamination exists. As a result, these businesses may have liabilities for conditions that we discover or that become apparent, including liabilities arising from non-compliance with environmental laws by prior owners. Because of the limited availability of insurance coverage for environmental liability, any substantial liability for environmental damage could materially adversely affect our results of operations and financial condition.

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Enactment of new environmental laws or regulations or changes in existing laws or regulations might require significant capital expenditures. We may be unable to generate sufficient funds or access other sources of capital to fund unforeseen environmental liabilities or expenditures.

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### ***Our business is subject to risks associated with climate change and social and government responses thereto.***

Currently, there are differing scientific studies and opinions relating to the severity, extent and speed at which climate change is or may be occurring around the world. As a result, we are currently unable to identify and predict all of the specific consequences of climate change on our business and operations.

To date, the potential and/or perceived effects of climate change and social and government responses to it have created both opportunities, such as enhanced sales of surplus green energy, and risks for our business.

While all of the specific consequences from climate change are not yet predictable, we are subject to risks that government and social focus on and demand for carbon neutral or green energy will create greater demand for the wood residuals or fiber that is consumed by our pulp mills as part of their production process. In addition, governmental initiatives or legislation may also increase both the demand and prices for wood residuals. As governments pursue green energy initiatives, they may implement financial, tax, pricing or other legislated incentives for renewable energy producers that cannibalize or materially adversely affect fiber supplies for existing traditional users, such as lumber and pulp and paper producers.

Such additional demand for wood residuals and/or governmental initiatives may materially increase the competition and prices for wood residuals over time. This could increase our fiber costs and/or restrict our ability to acquire fiber at competitive prices or at all during times of shortages. If our fiber costs increase and we cannot pass on these costs to our customers or offset them through higher prices for our sales of surplus energy, it will negatively affect our operating margins, results of operations and financial position. If we cannot obtain the fiber required to operate our mills, we may have to curtail and/or shut down production. This could have a material adverse effect on operations, financial results and financial position.

Other potential risks to our business from climate change include:

a greater susceptibility of northern softwood forest to disease, fire and insect infestation, which could diminish fiber availability;

the disruption of transportation systems and power supply lines due to more severe storms;

the loss of water transportation for logs and our finished goods inventories due to lower water levels;

decreases in quantity and quality of processed water for our mill operations;

the loss of northern softwood boreal forests in areas in sufficient proximity to our mills to competitively acquire fiber; and

lower harvest levels decreasing the supply of harvestable timber and, as a consequence, wood residuals.

The occurrence of some or all of these events could have a material adverse effect on our operations and/or financial results.

### ***Project Blue Mill may not generate the results or benefits we expect.***

In January 2012, we announced a project ( Project Blue Mill ) at our Stendal mill to increase production and efficiency through debottlenecking initiatives, including the installation of a new 40 MW steam turbine at the mill. Project Blue Mill is subject to customary risks and uncertainties inherent for large capital projects which could result in the project not completing on schedule or as budgeted. The Stendal mill could experience operating difficulties or delays during the start-up period when the new 40 MW turbine is being ramped up. Project Blue Mill may not increase the Stendal mill's pulp production and energy generating capacity to the levels we had planned. Cost overruns, equipment breakdowns or failures to perform to design specifications could have a material adverse effect on our Stendal mill's results of operations and financial performance.

*We are subject to risks related to our employees.*

The majority of our employees are unionized and we have collective agreements in place with our employees at all of our mills. In September 2008, we negotiated a four-year collective agreement, effective

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May 1, 2008, with the hourly workers at our Celgar mill and, in December 2010, we entered into our current collective agreement with our Rosenthal employees. In July 2011, we entered into a collective agreement with our pulp workers at the Stendal mill. Although we have not experienced any work stoppages in the past, there can be no assurance that we will be able to negotiate acceptable collective agreements or other satisfactory arrangements with our employees upon the expiration of our collective agreements. This could result in a strike or work stoppage by the affected workers. The registration or renewal of the collective agreements or the outcome of our wage negotiations could result in higher wages or benefits paid to union members. Accordingly, we could experience a significant disruption of our operations or higher on-going labor costs, which could have a material adverse effect on our business, financial condition, results of operations and cash flow.

### ***We rely on government grants and guarantees and participate in European statutory programs.***

We currently benefit from a subsidized capital expenditure program and lower cost of financing as a result of German federal and state government grants and guarantees at our Stendal mill. Should either the German federal or state governments be prohibited from honoring legislative grants and guarantees at Stendal, or should we be required to repay any such legislative grants, this may have a material adverse effect on our business, financial condition, results of operations and cash flow.

Since 2005, our German mills have benefitted from sales of emission allowances under the EU Emissions Trading Scheme. As a result of our Rosenthal and Stendal mills' eligibility for special tariffs under the Renewable Energy Act, the amount of emissions allowances granted to our German mills under the EU ETS has been reduced. Additionally, all such German legislation is subject to amendment or change which could adversely affect the eligibility of our Rosenthal and Stendal mills to participate in this statutory program and/or the tariffs paid thereunder. As a result we cannot predict with any certainty the amount of future sales of surplus energy we may be able to generate.

### ***We are dependent on key personnel.***

Our future success depends, to a large extent, on the efforts and abilities of our executive and senior mill operating officers. Such officers are industry professionals many of whom have operated through multiple business cycles. Our officers play an integral role in, among other things:

sales and marketing;

reducing operating costs;

identifying capital projects which provide a high rate of return; and

prioritizing expenditures and maintaining employee relations.

The loss of one or more of our officers could make us less competitive in these areas which could materially adversely affect our business, financial condition, results of operations and cash flows. We do not maintain any key person life insurance for any of our executive or senior mill operating officers.

### ***We may experience material disruptions to our production.***

A material disruption at one of our manufacturing facilities could prevent us from meeting customer demand, reduce our pulp and energy sales and/or negatively impact our results of operations. Any of our mills could cease operations unexpectedly due to a number of events, including:

unscheduled maintenance outages;

prolonged power failures;

equipment failure;

design error or employee or contractor error;

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chemical spill or release;

explosion of a boiler;

disruptions in the transportation infrastructure, including roads, bridges, railway tracks, tunnels, canals and ports;

fires, floods, earthquakes or other natural catastrophes;

prolonged supply disruption of major inputs;

labor difficulties; and

other operational problems.

Any such downtime or facility damage could prevent us from meeting customer demand for our products and/or require us to make unplanned capital expenditures. If any of our facilities were to incur significant downtime, our ability to meet our production capacity targets and satisfy customer requirements would be impaired and could have a material adverse effect on our business, financial condition, results of operations and cash flows.

***We may incur losses as a result of unforeseen or catastrophic events, including the emergence of a pandemic, terrorist attacks or natural disasters.***

The occurrence of unforeseen or catastrophic events, including the emergence of a pandemic or other widespread health emergency (or concerns over the possibility of such an emergency), terrorist attacks or natural disasters, could create economic and financial disruptions, could lead to operational difficulties (including travel limitations) that could impair our ability to manage or operate our business and adversely affect our results of operations.

***Our insurance coverage may not be adequate.***

We have obtained insurance coverage that we believe would ordinarily be maintained by an operator of facilities similar to our mills. Our insurance is subject to various limits and exclusions. Damage or destruction to our facilities could result in claims that are excluded by, or exceed the limits of, our insurance coverage. Additionally, the weak global and financial markets have also reduced the availability and extent of credit insurance for our customers. If we cannot obtain adequate credit insurance for our customers, we may be forced to amend or curtail our planned operations which could negatively impact our sales revenues, results of operations and financial position.

***We rely on third parties for transportation services.***

Our business primarily relies upon third parties for the transportation of pulp to our customers, as well as for the delivery of our raw materials to our mills. Our pulp and raw materials are principally transported by truck, barge, rail and sea-going vessels, all of which are highly regulated. Increases in transportation rates can also materially adversely affect our results of operations.

Further, if our transportation providers fail to deliver our pulp in a timely manner, it could negatively impact our customer relationships and we may be unable to sell it at full value. If our transportation providers fail to deliver our raw materials in a timely fashion, we may be unable to manufacture pulp in response to customer orders. Also, if any of our transportation providers were to cease operations, we may be unable to replace them at a reasonable cost. The occurrence of any of the foregoing events could materially adversely affect our results of operations.

***Other risks to Fibrek's business.***

Fibrex operates largely in the same business as us and is subject to substantially similar industry and business risks as we are.



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**THE SPECIAL MEETING**

**General**

Mercer is sending you this proxy statement as part of the solicitation of proxies by Mercer's board of directors for use at the Special Meeting any adjournments or postponements of such meeting. Mercer is first mailing this proxy statement, including a notice of the Special Meeting of shareholders and a form of proxy on or about [                      ].

**Date, Time and Place of the Mercer Special Meeting**

The Special Meeting is scheduled to be held on:

[                      ], 2012 at [                      ] (Vancouver time)  
at [                      ]

**Purpose of the Mercer Special Meeting**

At the Special Meeting Mercer shareholders will be asked to:

1. consider and vote upon a proposal to approve the issuance of up to 15,000,000 additional Mercer Shares in connection with the Offer proposed under the Support Agreement; and
2. consider and vote upon any motion to adjourn or postpone the Special Meeting to a later date or dates, if necessary, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal described immediately above.

**MERCER'S BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR EACH OF PROPOSALS NO. 1 AND 2.**

**Proposals to be Voted on at the Mercer Special Meeting**

***Proposal No. 1: Approval of Additional Mercer Shares***

To consider and vote upon a proposal to approve the issuance of up to 15,000,000 Mercer Shares in connection with the Offer which has been made substantially as provided for pursuant to the Support Agreement, which is included as Annex G to this proxy statement. We currently expect to utilize approximately 11,741,496 Mercer Shares as consideration to Fibrek's shareholders who tender their Fibrek shares in the Offer. We are seeking approval to issue more Mercer Shares than currently contemplated by the Support Agreement to provide us with flexibility to address fluctuations in market prices and conditions and, if we elect to do so and if required, to match or compete with any alternative offer for Fibrek.

We are currently permitted to issue up to approximately 11,155,840 Mercer Shares, or just under 20% of the total outstanding Mercer Shares, without holding a shareholder vote. However, under NASDAQ Listing Rule 5635(a), a company listed on the NASDAQ Global Market is required to obtain shareholder approval prior to the issuance of common stock, among other things, in connection with the acquisition of another company's stock, if the number of shares of common stock to be issued is equal to or in excess of 20% of the number of shares of common stock then outstanding. The additional Mercer Shares to be issued in the Offer are currently expected to exceed the 20% threshold under the NASDAQ Listing Rules by approximately 156,000 Mercer Shares. Accordingly, in order to ensure compliance with NASDAQ Listing Rule 5635(a), Mercer must obtain the approval of Mercer shareholders for the issuance of these securities in the transaction.

**MERCER'S BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR PROPOSAL NO. 1.**



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### ***Proposal No. 2: Adjournment***

To consider and vote upon a motion to adjourn or postpone the Special Meeting to a later date or dates, if necessary, to solicit additional proxies if there are insufficient votes at the time of the Special Meeting to approve Proposal No. 1.

**MERCER S BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR PROPOSAL NO. 2.**

### **Required Vote for Approval of Proposal 1 and Proposal 2**

Approving Proposal 1 and Proposal 2 requires the affirmative vote of a majority of the Mercer Shares present in person or represented by proxy and entitled to vote at the special meeting at which a quorum is present. Each shareholder of record on the Record Date will be entitled to one vote per Mercer Share held on the Record Date on all matters submitted for consideration of, and to be voted upon by, the shareholders at the Special Meeting.

### **Record Date; Mercer Shareholders Entitled to Vote**

Mercer s board of directors has fixed [ ] 2012 as the Record Date for the Special Meeting. Only shareholders of record at the close of business on that date will receive notice of and be able to vote at the Special Meeting. At the close of business on the Record Date, there were [ ] Mercer Shares outstanding held by approximately [ ] record holders.

As of the record date, the directors and executive officers of Mercer beneficially owned approximately [ ] Mercer Shares, entitling them to exercise approximately [ ]% of the voting power of Mercer Shares.

### **Quorum**

The required quorum for the approval of Proposal 1 and Proposal 2 is one-third ( $\frac{1}{3}$ ) of the Mercer Shares issued and outstanding as of the Record Date. Mercer Shares voted FOR, AGAINST or WITHHELD from a matter voted upon by the shareholders at the Special Meeting will be treated as being present at the special meeting for purposes of establishing a quorum for the transaction of business, and will also be treated as shares represented and voting at the special meeting (the Votes Cast ) with respect to any such matter.

### **Proxies; Abstentions and Broker Non-Votes**

You should complete and return the accompanying proxy card or vote your proxy by telephone or the Internet, whether or not you plan to attend the Special Meeting in person. All properly executed proxies received by Mercer before the Special Meeting that are not revoked will be voted at the Special Meeting in accordance with the instructions indicated on the proxies or, if no direction is indicated, FOR approval of the Proposals. Properly executed proxies, other than proxies voting against Proposal 2, also will be voted for any adjournment or postponement of the Special Meeting for the purpose of soliciting additional votes to approve Proposal 1, if necessary.

Properly executed proxies marked Abstain will not be voted at the Special Meeting. Abstentions will be counted for purposes of determining both: (i) the presence and absence of the quorum for the approval of the Proposals, and (ii) the total number of Votes Cast with respect to a proposal. Accordingly, abstentions will have the same effect as a vote against a proposal submitted for consideration of the shareholders.

If your Mercer Shares are held in street name by your broker, you must follow the directions your broker provides to you regarding how to instruct your broker to vote your Mercer Shares. You cannot vote Mercer Shares held in street name by returning a proxy card to Mercer. In addition, a broker cannot vote Mercer

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Shares it holds in street name for the beneficial owners without specific instructions from the beneficial owner. Broker non-votes will be counted for purposes of determining the presence or absence of a quorum for the approval of the Proposals, but will not be counted for purposes of determining the number of Votes Cast with respect to a proposal. Broker non-votes include shares for which a bank, broker or other nominee holder has not received voting instructions from the beneficial owner and for which the nominee holder does not have discretionary power to vote on a particular matter.

Mercer's board of directors is not currently aware of any business to be brought before the special meeting other than the Proposals. However, if any other matters are properly brought before the special meeting, the proxies named in the proxy card will have discretion to vote the shares represented by duly executed proxies in their sole discretion.

Mercer's board of directors urges you to complete, date and sign the accompanying proxy card and return it promptly in the enclosed, pre-paid envelope or to alternatively vote your proxy via the telephone or Internet voting instructions on your card. If your Mercer Shares are held in street name by your broker, you must follow the directions your broker provides to you regarding how to instruct your broker to vote your Mercer Shares. You cannot vote Mercer Shares held in street name by returning a proxy card to Mercer.

### **Voting and Revocation of Proxies**

#### ***Voting by Mail***

Complete, date, sign and mail the proxy in the enclosed postage pre-paid envelope. If you mark your voting instructions on the proxy, your Mercer Shares will be voted as you instruct. Please see the proxy for voting instructions.

#### ***Voting by Telephone***

Call the toll-free number listed on the proxy from any touch-tone telephone and follow the instructions. You should have your proxy in hand when you call.

#### ***Voting over the Internet***

Go to [www.proxyvoting.com/merc](http://www.proxyvoting.com/merc) and follow the instructions. You should have your proxy in hand when you access the website.

#### ***Voting in Person***

If you attend the Special Meeting, you may vote as instructed at the meeting. However, if you hold your Mercer Shares in street name (that is, through a broker/dealer or other nominee), you will need to bring to the meeting a proxy delivered to you by such nominee reflecting your ownership of Mercer Shares as of the Record Date.

Your grant of a proxy on the enclosed proxy card does not prevent you from voting in person or otherwise revoking your proxy at any time before it is voted at the Special Meeting. To revoke your proxy, either:

Deliver a signed notice of revocation or a properly executed new proxy card bearing a later date to:  
Mercer International Inc.

Suite 1120, 700 West Pender Street

Vancouver, British Columbia, Canada V6C 1G8

Attend the Special Meeting and vote your Mercer Shares in person.  
Attendance at the Special Meeting will not, in and of itself, have the effect of revoking your proxy.



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**Solicitation of Proxies and Expenses**

The cost of soliciting proxies will be borne by Mercer. Mercer may reimburse brokerage firms, banks and other persons representing the beneficial owners of shares for their expenses in forwarding solicitation materials to such beneficial owners. Solicitation of proxies by mail may be supplemented by telephone, telegram, facsimile or personal solicitation by Mercer directors, officers or regular employees without additional compensation.

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### **THE OFFER**

*This section and the section entitled **The Support Agreement** is a summary of the material terms of the Offer and the Support Agreement. Because it is a summary, it may not contain all of the information that is important to you. You should read carefully this entire proxy statement, including the Support Agreement, which is included as Annex G to this proxy statement, and the other documents to which Mercer has referred.*

#### **Background to the Offer**

The management and board of directors of Mercer continually review Mercer's position in light of the changing competitive environment in its industry, with the objective of identifying strategic alternatives and other opportunities, including business combination transactions, joint ventures and other commercial transactions that may be available from time to time to complement Mercer's business, support its strategy and enhance shareholder value. As part of this ongoing review process, Mercer identified the strategic opportunity presented by an acquisition of Fibrek.

Mercer had initially preliminarily evaluated a transaction with Fibrek dating back several years. In the fourth quarter of 2011, Mercer learned from an independent Canadian investment bank that Fibrek's largest shareholder, Fairfax Financial Holdings Limited (Fairfax), may possibly be interested in selling its Fibrek Shares. In November 2011, Mercer's chief executive officer and chief financial officer arranged and had a preliminary meeting with representatives of Fairfax to discuss the concept of a combination between Mercer and Fibrek. No understanding was reached and there was no further dialogue between Mercer and Fairfax in respect of Fibrek.

On November 28, 2011, AbitibiBowater Inc. doing business as Resolute Forest Products (Abitibi) announced that it intended to make a hostile take-over bid of Fibrek (the Abitibi Bid). On the next day, Fibrek's board of directors announced that it had begun a process of reviewing and evaluating Abitibi's announcement with its financial and legal advisors, and recommended that shareholders defer making any decision until Fibrek's board of directors had the opportunity to review the full details of the Abitibi Bid and to make a formal recommendation on its merits.

On December 15, 2011, Abitibi launched the Abitibi Bid for all of the issued and outstanding Fibrek Shares.

Following the launching of the Abitibi Bid, Mercer's management accelerated its review of a potential combination of Fibrek and Mercer with a view to delivering enhanced growth and value to shareholders. On December 22, 2011, a meeting of the representatives of Mercer and TD Securities Inc. was held at which Mercer's interest was discussed. On the following day, Fibrek and Mercer signed a confidentiality and standstill agreement regarding a potential strategic acquisition of Fibrek by Mercer. Thereafter, Mercer and its advisors commenced their initial due diligence and held preliminary discussions with Fibrek's management and advisors regarding a potential take-over.

On December 30, 2011, Fibrek's board of directors delivered its directors' circular, which included a recommendation to shareholders of Fibrek not to tender their Fibrek Shares. Attached to the directors' circular was an opinion of TD Securities Inc., which concluded that the Abitibi Bid was inadequate from a financial point of view to the Fibrek shareholders (other than those Fibrek shareholders who had entered into lock-up agreements with Abitibi).

On January 2, 2012, representatives of Mercer visited Fibrek's Saint-Félicien mill and the Fairmont mill. On January 3, 2012, a meeting of the representatives of Mercer and Fibrek took place, at which Mercer received a management presentation.

On January 13, 2012, the board of directors of Mercer met and was updated on the status of Mercer's evaluation of a potential transaction with Fibrek. After receiving the input and recommendations of Mercer

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management and reviewing advice received from Mercer's legal and financial advisors, the board of directors supported the continued evaluation by management and Mercer's legal and financial advisors of a potential transaction involving Fibrek, including the development of various financing models and proposals relating thereto.

In late January 2012, Mercer representatives and its financial and legal advisors travelled to Montréal and Québec City where meetings were held with Québec capital providers and representatives of the provincial government of Québec with respect to a potential offer by Mercer, potential funding for the same and to confirm Fibrek's eligibility to participate in Québec's publicly announced co-generation plants based forest biomass power purchase program. Subsequently, the chief executive officer and the chief financial officer of Mercer had discussions with two of Mercer's largest shareholders and met with one of them with respect to obtaining support for the issuance of the Mercer Shares that would be required in the Offer.

On January 30, 2012, Mercer formalized its retention of Raymond James Ltd. ( Raymond James ) to act as financial adviser.

On February 2, 2012, the board of directors of Mercer met and were advised that both the Québec financing meetings and discussions with Mercer's shareholders were proceeding favorably. Mercer's legal and financial advisors were also present at this meeting. The board of directors and its financial and legal advisors reviewed the merits, risks and opportunities associated with an acquisition of Fibrek and the potential value to be created for Mercer shareholders, as well as a recommendation from management in favor of the making of such a take-over bid offer. The board of directors authorized Mercer's management to offer to acquire all of the outstanding Fibrek Shares for consideration of C\$1.30 per Fibrek Share (or its share equivalent) and to negotiate and settle the terms of definitive documentation.

On February 3, 2012, Mercer made a non-binding offer to acquire all of the issued Fibrek Shares. The offer included the entering into of the Support Agreement and the Special Warrant Agreement (defined herein). The Special Warrant Agreement provided for the issuance of 32,320,000 Special Warrants at a price of C\$1.00 per Special Warrant and would allow Mercer to become a Shareholder of Fibrek regardless of whether the Offer was successful.

Following further discussions and negotiations regarding the terms of the proposal on February 4, 5 and 6, 2012, the parties entered into a letter of intent on February 6, 2012, which, among other things, set forth the material proposed terms of the Offer and the Special Warrant financing, granted Mercer a limited period of exclusivity expiring on February 10, 2012, limited Fibrek's ability to pursue alternative transactions and permitted the parties to negotiate definitive transaction documentation.

Between February 6, 2012 and February 9, 2012, Mercer and Fibrek, together with their legal and financial advisors, negotiated the Support Agreement that set out the terms of the proposed transaction, including representations, warranties, conditions and transaction protection measures in the Support Agreement, and the terms of the Special Warrant Agreement, including terms relating to when the Special Warrants would be exercisable by us, what would constitute a deemed conversion event and a redemption event and pricing.

On February 9, 2012, Mercer was informed by Fibrek's representatives that Fibrek's board of directors met to consider the Offer, a draft Support Agreement and Special Warrant Agreement and to receive the advice of its financial and legal advisors and to consider other factors relevant to the proposed transaction. Mercer understands that TD Securities Inc. delivered to Fibrek's board of directors a fairness opinion to the effect that, as of that date and subject to the scope of review, assumptions, qualifications and limitations discussed therein, the consideration offered to Fibrek shareholders (other than those who entered into lock-up agreements with Abitibi) pursuant to the Offer is fair, from a financial point of view, to such shareholders. Mercer was informed that, at the meeting, Fibrek's board of directors unanimously resolved and determined that: (i) the Offer is in the best interests of Fibrek and its shareholders; (ii) it recommend that shareholders accept the Offer and deposit their Fibrek Shares under the Offer; and (iii) Fibrek enter into the Support Agreement and the Special Warrant Agreement and perform its obligations thereunder.

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The Mercer board of directors also met on February 9, 2012. At the meeting, Mercer's legal counsel reviewed a summary of the proposed transaction and material agreements. Raymond James also rendered its oral opinion to the board of directors that the consideration to be paid by Mercer in the Offer was fair, from a financial point of view, to Mercer's shareholders. The Mercer board, after consultations with its legal and financial advisors, and such other factors it considered relevant to the proposed transactions, approved the Offer, the Support Agreement and the Special Warrant Agreement, subject to such modifications that were considered necessary or advisable in order to execute the transaction documents.

Following respective board of directors' approval, Mercer and Fibrek continued to negotiate the terms of the Support Agreement, which, together with the Special Warrant Agreement and lock-up agreements with all of Fibrek's directors and officers holding Fibrek Shares or options to acquire Fibrek, other than Hubert T. Lacoix, who holds his Fibrek Shares in a blind trust, were signed, in final form, late in the evening on February 9, 2012. Prior to the opening of the financial markets on February 10, 2012, Mercer and Fibrek each issued a news release announcing the Support Agreement, the Special Warrant agreement and Mercer's intention to make the Offer.

On February 9, 2012, Mercer also entered into voting support agreements (the "Voting Support Agreements") with its two largest institutional shareholders, IAT Reinsurance Ltd. and Platinum Investment Management Limited, as well as its Chairman and Chief Executive Officer, Jimmy S.H. Lee (collectively, the "Supporting Shareholders") who collectively own approximately 44% of the outstanding Mercer Shares at the announcement of Mercer's intention to make the Offer. Pursuant to the terms of the Voting Support Agreements, each Supporting Shareholder agreed to vote (or cause to be voted) all of their Mercer Shares in favor of the approval of the Mercer Shares to be issued in connection with the Offer. The Supporting Shareholders are also prohibited from selling, assigning or otherwise transferring any of the Mercer Shares they hold until the termination of their respective Voting Support Agreements.

The Voting Support Agreements each terminate upon the earlier of: (i) the date of termination of the respective Voting Support Agreement in accordance with its terms; (ii) the completion of the meeting of holders of Mercer Shares held in connection with the Mercer Shareholder Approval; (iii) the completion of the Offer; (iv) the date Mercer advises that it will not be proceeding with the Offer; and (v) 120 days from the date of each respective Voting Support Agreement. In the case of termination of any Voting Support Agreement, such agreement shall terminate and be of no further force of effect, and the parties thereto will have no further obligation or liability to each other.

On February 13, 2012, Abitibi announced that it had applied to the *Bureau de décision et de révision* (Québec) (the "*Bureau de décision*"), the administrative tribunal with statutory jurisdiction in securities law and regulatory matters in Québec, for an order to cease trade the Offer and the Special Warrant Financing. Abitibi also announced that it had extended the expiry date of the Abitibi Bid to February 23, 2012 (the Abitibi Bid had previously been extended to February 13, 2012, from January 20, 2012). A hearing was held to consider Abitibi's application commencing on February 17, 2012. At the hearing, both Fibrek and Mercer made submissions to the effect that the requested relief should not be granted because the Offer, the Support Agreement, the Special Warrant Agreement and the issuance of the Special Warrants were in compliance with applicable laws, and it would be contrary to the public interest to cease trade a superior offer.

On the same day, Fairfax, Pabrai Investment Funds, Oakmont Capital Inc. and Steelhead Partners, LLC filed, through counsel, a submission before the Toronto Stock Exchange seeking to stop the issuance of the Special Warrants. Fibrek filed, through counsel, a response letter in opposition to such submission on February 17, 2012.

Also on February 17, 2012, Mercer and Fibrek obtained a waiver from IQ Rexfor Inc., wherein IQ Rexfor Inc. agreed to waive the application of the change of control restrictions in Fibrek's C\$78 million term loan with IQ Rexfor Inc. in respect of the Offer.

On February 23, 2012, the *Bureau de décision* dismissed Abitibi's request to cease trade the Offer but granted an order to cease trade the Special Warrant financing, and Abitibi extended its unsolicited offer until 5:00 p.m. (Eastern time) on March 9, 2012.

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On February 24, 2012, Fibrek announced that it intended to appeal the decision to cease trade the Special Warrant financing rendered by the *Bureau de décision*. On February 25, 2012, Mercer also determined to appeal the aforesaid decision.

Fibrek filed an inscription in appeal on February 27, 2012.

On February 28, 2012, the Mercer board of directors met and received an update from its management and external legal and financial advisors regarding the Offer. At the meeting, Raymond James also confirmed to the board of directors its previous oral fairness opinion to the effect that the consideration to be paid by Mercer in the Offer was fair, from a financial point of view, to Mercer's shareholders and thereafter delivered its written fairness opinion. The Mercer board of directors then approved the making of the Offer and the mailing of the Offer and related documentation to Fibrek shareholders and related matters.

On February 29, 2012, Mercer mailed its take-over bid circular to Fibrek shareholders.

### **Mercer's Reasons for Commencing the Offer**

The Mercer board of directors has concluded that the acquisition of Fibrek through the Offer presents a compelling strategic opportunity to expand both its pulp production capacity and its production and sale of renewable energy and allow Mercer to further diversify its business geographically. In reaching its decision to approve the Offer, the Mercer board of directors considered a number of factors including, among other factors:

The acquisition of Fibrek fits within Mercer's strategy of focusing on world-class production assets that produce high quality pulp;

The ability of the Saint-Félicien mill to produce and sell surplus renewable energy is in line with Mercer's goal of increasing its revenues from energy sales; and

Fibrek's mills are complementary to Mercer's existing operations and, through active management, we believe that the operations of Fibrek will generate increased value for Mercer's shareholders.

### **Opinion of Raymond James to the Board of Directors of Mercer**

On January 30, 2012 Mercer formalized the retention of Raymond James to act as its financial advisor in connection with the Offer and to prepare an opinion as to whether the Offer is fair from a financial point of view to Mercer's shareholders. At the February 9, 2012 meeting of Mercer's board of directors, Raymond James rendered its oral opinion to the board of directors, subsequently confirmed in writing, to the effect that, as of February 9, 2012, and based upon and subject to certain matters stated therein, the Offer is fair, from a financial point of view, to Mercer's shareholders. See Annex F, Opinion of Raymond James Ltd.

### **General**

Mercer retained Raymond James to provide a fairness opinion in connection with the potential Offer based on Raymond James' qualifications, expertise, reputation, and extensive knowledge of the pulp sector. Raymond James is a full service investment dealer, which has prepared numerous valuations and fairness opinions and has participated in a significant number of transactions involving private and publicly traded companies. In its selection process, Mercer management had looked into a range of investment banks which specialized in transactions for corporations. In particular, due to Raymond James' extensive knowledge of the industry sector, the Mercer board of directors unanimously decided to engage Raymond James.

Other than the engagement between Mercer and Raymond James with respect to rendering the fairness opinion in connection with the Offer as described herein and Mercer's engagement of Raymond James as financial advisor in connection with the Offer, there is no material relationship that existed during the past two

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years or is mutually understood to be contemplated in which any compensation was received or is intended to be received by Raymond James as a result of the relationship between Raymond James, Mercer or Fibrek, or any of their respective associates, affiliates or insiders.

In consideration for providing a fairness opinion and other financial advisory services in connection with the Offer, Raymond James is to be paid a fee, a portion of which is payable upon consummation of the Offer, and is to be reimbursed for its reasonable out-of-pocket expenses. Furthermore, Mercer has agreed to indemnify Raymond James, in certain circumstances, against certain expenses, losses, claims, actions, suits, proceedings, damages and liabilities which may arise directly or indirectly from services performed by Raymond James.

The full text of Raymond James' written opinion, dated February 9, 2012, which sets forth, among other things, the assumptions made, procedures followed, matters considered, and qualifications and limitations on the review undertaken by Raymond James in connection with its opinion is attached with the consent of Raymond James, to this proxy statement as Annex F and is incorporated into this proxy statement. This summary of Raymond James' opinion set forth in this proxy statement is qualified in its entirety by reference to the full text of Raymond James' written opinion attached as Annex F. You are encouraged to read Raymond James' written opinion and this section carefully and in their entirety.

Mercer's board of directors, and not Raymond James, determined the amount of consideration to be paid by Mercer in the Offer and Raymond James' written opinion does not constitute a recommendation to the Mercer shareholders or any other shareholders as to how such shareholders or any other shareholder should vote with respect to the transaction. The written opinion addresses only the fairness, from a financial point of view, of the Offer to Mercer's shareholders. It does not address the relative merits of the transaction as compared to alternative transactions or strategies that may be available to Mercer, nor does it address Mercer's underlying decision to engage in the Offer. Further, Raymond James was not engaged by Mercer to prepare, and Raymond James has not prepared, a formal valuation or appraisal of the shares or any of the assets or other securities of either Mercer or Fibrek and its fairness opinion should not be construed as such.

Raymond James' written opinion and its related presentation were among the many factors that the Mercer board of directors took into consideration in making its determination to approve, and to recommend that Mercer's shareholders approve the Offer.

The following is a summary of Raymond James' opinion. We encourage you to read Raymond James' written opinion carefully in its entirety, which is attached as Annex F hereto.

### ***Scope of Review***

In connection with its written opinion, Raymond James reviewed and relied upon, or carried out, among other things, the following:

1. the Support Agreement;
2. the letter of intent entered into between Mercer and Fibrek dated February 3, 2012;
3. annual reports and forms 10-K of Mercer, including audited consolidated financial statements and management's discussion and analysis for the fiscal years ended December 31, 2010 and 2009;
4. unaudited consolidated interim financial statements of Mercer and management's discussion and analysis for the three month periods ended September 30, 2011, June 30, 2011 and March 31, 2011;
5. proxy statements of Mercer for the years ended December 31, 2010 and 2009;
6. public filings submitted by Mercer to securities commissions or similar regulatory authorities and stock exchanges in Canada and the United States;



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7. discussions with senior management of Mercer;
8. discussions with legal counsel to Mercer;
9. the press release by Mercer announcing the Offer;
10. certain other internal information (including financial models, forecast, projections, estimates and related confidential information) prepared and provided to us by Mercer management concerning the business, operations and prospects of Mercer;
11. industry reports in respect of Mercer and for the pulp industry in general;
12. annual reports of Fibrek, including audited consolidated financial statements for the fiscal years ended December 31, 2010 and 2009;
13. unaudited consolidated interim financial statements of Fibrek and management's discussion and analysis for the three month periods ended September 30, 2011, June 30, 2011 and March 31, 2011;
14. annual information forms of Fibrek for the years ended December 31, 2010 and 2009;
15. public filings submitted by Fibrek to securities commissions or similar regulatory authorities and stock exchanges;
16. discussions with senior management of Fibrek;
17. discussions with the financial advisors of Fibrek;
18. certain other internal information prepared and provided to us by Fibrek management concerning the business, operations and prospects of Fibrek;
19. public information relating to the business, operations, financial performance and stock trading history of Mercer, Fibrek and other selected public companies considered by Raymond James to be relevant;
20. representations contained in certificates delivered or to be delivered in conjunction with its fairness opinion addressed to us from senior officers of Mercer and Fibrek as to the completeness and accuracy of the information upon which such fairness opinion is based and such matters specified therein; and
21. such other corporate, industry and financial market information, investigations and analyses as Raymond James considered necessary or appropriate in the circumstances.

Raymond James has not, to the best of its knowledge, been denied access by Mercer or Fibrek to any information requested by Raymond James. Raymond James has assumed the accuracy and fair presentation of, and relied upon the audited financial statements of Mercer and Fibrek and

the reports of the auditors thereon.

While this summary describes the analysis and factors that Raymond James deemed material in rendering its opinion, it is not a comprehensive description of all analyses and factors considered by Raymond James. The preparation of a fairness opinion is a complex process that involves various determinations as to the most appropriate and relevant methods of financial analysis and the application of these methods to the particular circumstances. Therefore, a fairness opinion is not readily susceptible to partial analysis or a summary description. In arriving at its written opinion, Raymond James did not attribute any particular weight to any analysis or factor considered by it, but rather made qualitative judgments as to the significance and relevance of each analysis and factor. Accordingly, Raymond James believes that its analyses must be considered as a whole and that selecting portions of its analyses and of the factors considered by it, without considering all analyses and factors, could create a misleading or incomplete view of the evaluation process underlying its written opinion. Several analytical methodologies were employed and no one method of analysis should be regarded as critical to the overall conclusion reached by Raymond James. Each analytical technique has inherent strengths and weaknesses, and the nature of the available information may further affect the value of particular techniques. The conclusion reached by Raymond James is based on all analyses and factors taken, as a whole, and also on application of Raymond James' own experience and judgment. This conclusion may involve significant elements of subjective judgment and qualitative analysis.

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### ***Assumptions and Limitations***

In rendering its fairness opinion, Raymond James relied upon and assumed the completeness, accuracy and fair presentation of all financial and other information, data, valuations, appraisals, advice, opinions and representations pertaining to Mercer, Fibrek and their respective subsidiaries obtained by Raymond James from public sources, contained in the Support Agreement, provided to it by senior management of Mercer and Fibrek and their respective consultants or advisors, or as otherwise provided to it pursuant to its engagement. Raymond James' fairness opinion is conditional upon such completeness, accuracy and fair presentation. Subject to the exercise of its professional judgment and except as expressly described herein, Raymond James has not attempted to verify independently the accuracy or completeness of any such information, data, valuations, appraisals, advice, opinions, representations, budgets, estimates or forecasts.

The Offer is subject to a number of conditions outside the control of Mercer and Raymond James has assumed all conditions precedent to the completion of the Offer can be satisfied in due course and all consents, permissions, exemptions or orders of relevant regulatory authorities will be obtained, without adverse conditions or qualification. In rendering its fairness opinion, Raymond James expresses no view as to the likelihood that the conditions with respect to the Offer will be satisfied or waived or that the Offer will be implemented within the time frame indicated in the Support Agreement. Raymond James' fairness opinion does not constitute a recommendation as to how any Mercer shareholder should vote with respect to the proposed Offer or any other related matter.

In arriving at its fairness opinion, in addition to the facts and conclusions contained in the materials, information, documents, reports, representations and opinions provided from Fibrek and Mercer, Raymond James has assumed, among other things, that the representations and warranties provided in representation certificates from senior management of both Mercer and Fibrek are current and accurate in all material respects.

Raymond James is not a legal, tax or accounting expert and therefore expresses no opinion concerning any legal, tax or accounting matters concerning the Offer.

Raymond James' fairness opinion is rendered on the basis of securities markets, economic, financial and general business conditions prevailing as at the date of the opinion and the condition and prospects, financial and otherwise, of Mercer and Fibrek as reflected in the information and documents reviewed by Raymond James and as represented to Raymond James in its discussions with management of Mercer and Fibrek and pursuant to the representation certificates discussed above. In its analyses and in preparing its fairness opinion, Raymond James made numerous assumptions with respect to industry performance, general business and economic conditions and other matters, all of which are beyond the control of Raymond James or any party to the Offer and while reasonable under current circumstances, may prove to be incorrect. Raymond James' fairness opinion is given as of February 9, 2012 and Raymond James disclaims any undertaking or obligation to advise any person of any change in any fact or matter affecting such fairness opinion which may come or be brought to Raymond James' attention after that date. Without limiting the foregoing, in the event that there is any material change in any fact or matter affecting its fairness opinion after February 9, 2012, Raymond James reserves the right to change, modify or withdraw such fairness opinion.

### ***Summary of Financial Analyses***

The following represents a summary of the material financial analyses performed by Raymond James in connection with providing its written opinion to Mercer's board of directors. Some of the summaries of financial analyses performed by Raymond James include information presented in tabular format. In order to fully understand the financial analyses performed by Raymond James, you should read the tables together with the text of each summary. The tables alone do not constitute a complete description of the financial analyses. Considering the data set forth in the tables without considering the full narrative description of the financial analyses, including the methodologies and assumptions underlying the analyses, could create a misleading or incomplete view of the financial analyses performed by Raymond James.

**Table of Contents***Comparable Company Analysis*

Based on public and other available information, Raymond James calculated the multiples of enterprise value ( EV ) (which Raymond James defined as equity value, plus debt and minority interest, less cash and cash equivalents) to the estimated calendar year 2012 and 2013 earnings before interest, taxes, depreciation and amortization ( EBITDA ) for comparable companies in the pulp industry. Raymond James believes that Canfor Pulp Products Inc. and Mercer are the most relevant comparable companies for Fibrek as both companies operate NBSK pulp mills in Canada. The multiples for the selected companies were based on consensus estimates and other publicly available information.

Company	2012E EV/EBITDA Multiple	2013E EV/EBITDA Multiple
Canfor Pulp Products Inc.	5.7x	4.3x
Mercer	5.9x	4.7x

Raymond James compared the EV/EBITDA multiples of these select comparable companies to the multiple that results from Mercer's Offer for Fibrek and management's EBITDA forecast for Fibrek. This analysis indicates that the multiple associated with the Offer for Fibrek was lower than these select comparable companies. Raymond James also performed sensitivity analysis on the key variables of forecast EBITDA and EV/EBITDA multiple.

*Precedent Transactions Analysis*

In the precedent transactions approach Raymond James reviewed the publicly available information with respect to pulp mill transactions in the industry. Raymond James calculated the multiples of enterprise value (which Raymond James defined as equity value plus debt less cash and cash equivalents) net of working capital to thousands of tonnes of capacity per year ( mtpy ). The derived average mtpy multiple range of US\$285 to US\$345 was applied to the current capacity of Fibrek's Saint Félicien NBSK mill in Raymond James' net asset value ( NAV ) analysis.

Date	Name of Acquirer	Name of Target	Price/Tonne (US\$/mtpy)
Oct 2010	International Grand Investment Corp.	Woodland Pulp LLP	\$ 152
Apr 2010	Paper Excellence B.V.	Saint-Gaudens/Tarascon	\$ 238
Apr 2010	Paper Excellence B.V.	Mackenzie <sup>(1)</sup>	\$ 85
Dec 2006	Asia Pulp & Paper Co. Ltd.	Meadow Lake Mechanical Pulp	\$ 100
Nov 2006	SFK Pulp Fund	Fairmont/Menominee	\$ 388
Nov 2004	Mercer International Inc.	Celgar <sup>(1)</sup>	\$ 488
Mar 2001	Pope & Talbot Inc.	Mackenzie <sup>(1)</sup>	\$ 431
Nov 2000	LaPointe Partners, Inc.	Samoa Pacific Cellulose, LLC	\$ 359
Sep 2000	Tembec Inc.	Cellurhone/Pyrenecell	\$ 234
Dec 1999	Tembec Inc./Kruger Inc.	Marathon <sup>(1)</sup>	\$ 374
<b>Average</b>			<b>\$ 285</b>
<b>Median</b>			<b>\$ 299</b>
<b>NBSK Average<sup>(1)</sup></b>			<b>\$ 345</b>

(1) Pure NBSK pulp mill transaction.

*Net Asset Value Analysis*

Under the NAV approach Raymond James separately considered the assets and liabilities of Fibrek using assumptions and methodologies which were considered appropriate in the circumstances. Raymond James considered the following three components of Fibrek's business: (i) Fibrek's Saint Félicien NBSK mill; (ii) Fibrek's two recycled bleached kraft mills; and (iii) Fibrek's power assets.



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A summary of the NAV approach for Fibrek is as follows:

C\$	Low	High
<b>Saint Félicien NBSK Mill</b>		
Mill Capacity (000 tonnes)	375	375
Value Per Tonne <sup>(1)</sup>	\$ 285	\$ 345
Implied Value Range (millions)	\$ 107	\$ 129
<b>Recycled Bleached Kraft Mills</b>		
Implied Value Range <sup>(2)</sup> (millions)	\$ 30	\$ 40
<b>Power Assets</b>		
Annual EBITDA (millions)	\$ 22	\$ 22
EBITDA Multiple <sup>(3)</sup>	6.0x	8.0x
	\$ 132	\$ 176
Add: Net Working Capital <sup>(4)</sup>	\$ 101	\$ 101
Total	\$ 370	\$ 446
Less: Net Debt	\$ 114	\$ 114
Implied Equity Value	\$ 256	\$ 332
Shares Outstanding (millions)	130	130
Implied Share Price	\$ 1.97	\$ 2.55

(1) Based on Precedent Transactions Analysis and assuming US\$/C\$ foreign exchange rate of 1.00. Value per tonne excludes working capital.

(2) Based on 3.0x-4.0x management 2012 forecast.

(3) EBITDA multiple range of between 6.0x to 8.0x selected for Fibrek's power assets. Average EBITDA multiple of comparable power companies is 8.4x (2012E) and 7.2x (2013E). Comparable power companies include: Algonquin Power & Utilities Corp., Atlantic Power Corporation, Boralex Inc., Capstone Infrastructure Corporation and Northland Power Inc.

(4) Net working capital estimated as at December 31, 2011. Net working capital added back as it is excluded from value per tonne calculated in Precedent Transactions Analysis.

*Discounted Cash Flow Analysis*

Raymond James performed a discounted cash flow analysis for Fibrek which involved taking projected unlevered free cash flows over the given period and adding a terminal value all discounted by the weighted average cost of capital in order to obtain a net present value per share.

Raymond James based its discounted cash flow analysis on management estimates for financial performance of the business over the analyzed period (through fiscal year 2016).

In its analysis, Raymond James applied discount rates ranging from 12% to 14% to reflect the overall risk associated with Fibrek's operations and projected financial performance. Raymond James calculated a terminal value at the end of 2016 using an EBITDA multiple ranging from between 4.0x to 6.0x. The discounted cash flow analysis resulted in a range of values from C\$2.45 to C\$3.64 per share.

*Pro Forma Transaction Analysis*

Raymond James performed a summary merger analysis of Mercer and Fibrek based on the transaction structure as outlined in the Offer. The analysis was based on management's forecast for the combined business. Based on these assumptions, the transaction is estimated to be accretive to Mercer's EPS in both 2012 and 2013.



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### ***Summary Analysis***

Raymond James is of the opinion that, as of February 9, 2012, the Offer is fair from a financial point of view to Mercer's shareholders.

The material analyses performed by Raymond James have been summarized above. Nonetheless, the summary set forth above does not purport to be a complete description of the analyses performed by Raymond James. Raymond James did not form a conclusion as to whether any individual analysis, considered in isolation, supported or failed to support an opinion as to fairness. Rather, in reaching its conclusion, Raymond James considered the results of the analyses in light of each other and ultimately reached its opinion based on the results of all analyses taken as a whole.

### **Offer Consideration**

The shareholders of Fibrek who accept the terms of the Offer and tender their Fibrek Shares in connection with the Offer will receive either: C\$1.30 in cash; C\$0.54 in cash plus 0.0903 of a Mercer Share; or 0.1540 of a Mercer Share for each Fibrek Share tendered. The Offer consideration will be prorated as necessary to ensure that the aggregate Offer consideration does not exceed C\$70.0 million or 11,741,496 Mercer Shares. Such proration will be based on the number of Fibrek Shares acquired in proportion to the number outstanding at the applicable take-up date. The share exchange ratio of 0.1540 Mercer Shares for each Fibrek Share tendered was negotiated between Fibrek and Mercer, and no adjustment of the share exchange ratio will be made. Moreover, no fractional Mercer Shares will be issued. In lieu of fractional shares, shareholders of Fibrek who have tendered Fibrek Shares will receive a cash payment for such fractional shares.

### **No Appraisal Rights**

Neither Mercer nor Fibrek shareholders will be entitled to dissenters' rights or appraisal rights under the WBCA, the CBCA or Canadian corporate law, in connection with the Offer. However, under the CBCA, Fibrek shareholders whose Fibrek Shares have not been taken up in the Offer have certain rights to dissent and receive payment in cash of the fair market value of their Fibrek Shares in the event of a subsequent acquisition transaction.

### **Regulatory Matters**

The Offer is not subject to any federal, state or foreign regulatory approvals, other than the approval by the SEC of the Registration Statement on Form S-4, of which this proxy statement is a part, and the approval for the listing of the new Mercer Shares on the NASDAQ Global Market and the Toronto Stock Exchange.

Additionally, the proposed acquisition of Fibrek will be subject, among other things, to review by the Canadian and U.S. competition and antitrust regulators and by the Minister of Industry Canada (the "Minister") under the ICA. We are committed to working closely with these regulatory authorities to provide information and data necessary for their review of the transaction and to resolving regulatory concerns, if any, as promptly as possible.

### ***HSR Act***

Under the HSR Act and the rules promulgated thereunder by the U.S. Federal Trade Commission (the "FTC"), certain transactions, including the completion of the Offer, may not be consummated unless notification has been given and certain information has been furnished to the FTC and the Antitrust Division of the U.S. Department of Justice (the "Antitrust Division") and certain waiting period requirements have been satisfied. We intend to file any required Premerger Notification and Report Form with the FTC and the Antitrust Division for review in connection with the Offer as soon as practicable.

Under the HSR Act, our purchase of Fibrek Shares in the Offer may not be completed until the expiration of a 30 calendar day waiting period following the filing by Mercer, as the ultimate parent entity of Mercer

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Acquisition, of a Premerger Notification and Report Form concerning the Offer with the FTC and the Antitrust Division, unless the waiting period is earlier terminated by the FTC and the Antitrust Division. Accordingly, the required waiting period with respect to the Offer will expire at 11:59 p.m., Eastern Time, 30 days following such filing, unless such 30th day is a Saturday, Sunday, or other legal public holiday, in which case the waiting period will expire at 11:59 p.m., Eastern Time, on the next regular business day, unless earlier terminated by the FTC and the Antitrust Division or unless the FTC or the Antitrust Division issues a request for additional information and documentary material (a Second Request ) prior to that time. If within the 30 calendar day waiting period either the FTC or the Antitrust Division issues a Second Request, the waiting period with respect to the Offer would be extended until 30 calendar days following the date of substantial compliance by Mercer with that request, unless the FTC or the Antitrust Division terminates the additional waiting period before its expiration. After the expiration of the 30 calendar day waiting period, the waiting period could be extended only by court order or with Mercer's consent. In practice, complying with a Second Request can take a significant period of time. Although Fibrek is required to file certain information and documentary material with the FTC and the Antitrust Division in connection with the Offer, neither Fibrek's failure to make those filings nor a request for additional documents and information issued to Fibrek by the FTC or the Antitrust Division will extend the waiting period with respect to the purchase of Fibrek Shares in the Offer.

At any time before or after Mercer's acceptance for payment of Fibrek Shares pursuant to the Offer, if the Antitrust Division or the FTC believes that the Offer may substantially lessen competition in any line of commerce affecting U.S. consumers, the FTC and the Antitrust Division have the authority to challenge the transaction by seeking a federal court order enjoining the transaction or, if Fibrek Shares have already been acquired, requiring disposition of such Fibrek Shares or, as a condition to clearance, the divestiture of substantial assets of Mercer, Fibrek or any of their respective subsidiaries or affiliates or requiring other conduct relief. U.S. state attorneys general and private persons may also bring legal action under the antitrust laws seeking similar relief or seeking conditions of Mercer's obligation to accept for payment Fibrek Shares tendered in the Offer.

### ***Competition Act***

Part IX of the Competition Act requires pre-merger notification to the Commissioner of Competition under the *Competition Act* (the Commissioner ) for transactions that exceed certain financial thresholds and, in the case of share acquisitions, exceed an additional voting interest threshold. If a transaction is subject to pre-merger notification, a pre-merger notification filing containing certain prescribed information must be submitted to the Commissioner and the applicable waiting period must expire or be waived by the Commissioner before the transaction may be completed. The initial statutory waiting period is 30 days from the date of a complete filing but can be extended if the Commissioner issues a supplementary information request (which is a demand for more detailed information), after which time closing can only occur 30 days following the submission of the requested supplementary information. In the context of an unsolicited bid, where the Commissioner receives the prescribed information from the bidder prior to receiving information from the corporation whose shares are being acquired, the Competition Act requires the Commissioner to immediately notify the target corporation, and the target must then supply the Commissioner with its prescribed information within ten days after being so notified. Although Fibrek will thus be required to file its information and documentary materials with the Competition Bureau in connection with the Offer within ten days after being so notified, neither Fibrek's failure to make its filing nor a request for additional documents and information issued to Fibrek by the Competition Bureau will extend the statutory waiting period applicable to the Offer, which will be determined only in reference to our filing and submissions.

The Commissioner's review of a transaction, and communication of the Commissioner's intention as to whether or not to oppose a transaction, may however take longer than the statutory waiting period, particularly for mergers that raise some competition law issues. The Competition Bureau has adopted service standards to indicate the expected time for the completion of its substantive review, which depends on the complexity of the transaction as determined by the Competition Bureau. The two potential designations are non-complex and

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complex , with respective service standards of 14 days and 45 days. In cases where a supplementary information request is issued, the service standard will be similar to the statutory waiting period and will end 30 days after the submission of the supplementary information.

As an alternative to a pre-merger notification filing, for transactions which are unlikely to raise any significant competition issues, the parties may request an advanced ruling certificate ( ARC ) from the Commissioner. The issuance of an ARC is at the discretion of the Commissioner and a request for an ARC will only be granted by the Commissioner where a transaction clearly does not raise competition Law issues.

Regardless of whether a pre-merger notification filing is required, the Commissioner may apply to the Competition Tribunal, a specialized tribunal empowered to deal with certain matters under the Competition Act, with respect to a merger (as defined in the Competition Act). If the Competition Tribunal finds that a merger or proposed merger prevents or lessens or is likely to prevent or lessen competition substantially, it may order that all or part of the merger or proposed merger not proceed or impose other conditions on its completion or, in the event that the merger has been completed, order its dissolution or the disposition of some or all of the assets or shares involved. In certain circumstances, the Competition Tribunal may also issue an interim order under the Competition Act prohibiting the completion of the merger for a period of up to 30 days (which may be extended up to a maximum total of 60 days) to allow the Commissioner to complete the review.

If the Commissioner determines that she does not, at the time of the review, have sufficient grounds to apply to the Competition Tribunal for an order regarding a proposed merger under the merger provisions of the Competition Act, the Commissioner may issue an advisory opinion (known as a no-action letter) stating that the Commissioner does not intend to commence proceedings before the Competition Tribunal. However, the Commissioner retains the ability to initiate such proceedings at any time during the year following the completion of the merger.

The purchase of Fibrek Shares pursuant to the Offer is a notifiable transaction for the purposes of Part IX of the Competition Act and requires a pre-merger notification filing to the Commissioner as it exceeds the prescribed thresholds. Mercer and Fibrek have jointly requested that the Commissioner issue an advance-ruling certificate under Section 102 of the Competition Act or, alternatively, to waive the requirement to file a notice and supply information under Section 114 of the Competition Act and provide a no action letter in respect of the proposed acquisition of Fibrek Shares.

## *ICA*

Generally, any acquisition by a non-Canadian of control of a Canadian business is either notifiable or reviewable under the ICA, a Canadian statute that governs such acquisitions. Whether an acquisition is notifiable or reviewable depends on the structure of the transaction and the value and nature of the assets of the Canadian business being acquired. If an acquisition is reviewable, the acquiror must submit an application for review with prescribed information to the Minister and, before the acquisition may be completed, the Minister must determine whether the proposed transaction is likely to be of net benefit to Canada .

A transaction will be reviewable when there is a direct acquisition of control of a Canadian business by a World Trade Organization ( WTO ) investor (a corporation or other entity being a WTO investor if it is ultimately controlled by individuals who are nationals of a country that is a member of the WTO) and the value of the assets of that entity, and of all other entities in Canada the control of which is acquired, is equal to or greater than C\$330,000,000 (2012 threshold). A direct acquisition of control of a Canadian business can occur by means of a purchase of assets or voting interests. For the purposes of the ICA, an acquisition of control is deemed to occur when a non-Canadian directly acquires more than a 50% voting interest in a Canadian corporation and is presumed to occur where there is an acquisition of between 33% and 50% of the voting shares.

The Minister has an initial 45-day period to determine whether the investment is likely to be of net benefit to Canada. The Minister may extend the period for a further 30 days by giving notice to the prospective acquiror prior

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to the expiration of the initial 45-day period. Further extensions may be permitted but only with the consent of the prospective acquiror. If the Minister is not satisfied that the investment is likely to be of net benefit to Canada, the Minister must send a notice to that effect to the prospective acquiror. The acquiror then has 30 days to make additional representations and undertakings to the Minister demonstrating the net benefit of the investment.

The purchase of Fibrek Shares pursuant to the Offer is a reviewable acquisition under the ICA. We therefore intend to file the required application for review with the Minister in connection with the Offer as soon as practicable.

### ***Canadian Securities Regulatory Matters***

The issuance and distribution of Mercer Shares under the Offer is being made pursuant to general exemptions from the prospectus and dealer registration requirements under applicable Canadian securities laws. Although the resale of Mercer Shares issued under the Offer is subject to restrictions under the securities laws of certain Canadian jurisdictions, shareholders in such jurisdictions will, in general, be able to rely on exemptions from such resale restrictions.

Under Canadian securities laws, once issued, Mercer Shares will, except for control distributions described below, be generally freely tradeable in Canada without the need for the holder of such Mercer Shares to prepare and file a prospectus or rely on an exemption from the prospectus requirements, provided: (i) the issuer, being Mercer, is and has been a reporting issuer in a jurisdiction of Canada for the four months immediately preceding the trade; (ii) no unusual effort is made to prepare the market or to create a demand for the security that is the subject of the trade; (iii) no extraordinary commission or consideration is paid to a person or company in respect of the trade; and (iv) if the selling security holder is an insider or officer of the issuer, the selling security holder has no reasonable grounds to believe that Mercer is in default of securities legislation.

If, however, the resale or trade of Mercer Shares constitutes a control distribution, then any resale or trade of Mercer Shares would require either: (i) the preparation and filing of a prospectus in the relevant Canadian jurisdiction(s) in order to qualify such resale or trade for public distribution in Canada and render the subject Mercer Shares freely tradeable in such Canadian jurisdiction(s); (ii) in the absence of a Canadian prospectus, the reliance on a separate statutory or discretionary exemption from the applicable prospectus requirements for the resale or trade of Mercer Shares; or (iii) the giving of notice and filing of a prescribed form with the Canadian securities regulatory authorities at least seven days before the first resale or trade that is part of the control distribution indicating the selling security holder's intention to distribute securities and particulars of the proposed trade, including the number and class of securities proposed to be sold and whether the sale will occur privately or on an exchange or market.

In general terms, a control distribution is a distribution effected by a control person, being (i) a person or company who holds a sufficient number of the voting rights attached to all outstanding voting securities of an issuer to affect materially the control of the issuer and, if a person or company holds more than 20% of the voting rights attached to all outstanding voting securities of an issuer, the person or company is deemed, in the absence of evidence to the contrary, to hold a sufficient number of the voting rights to affect materially the control of the issuer, or (ii) each person or company in a combination of persons or companies, acting in concert by virtue of an agreement, arrangement, commitment or understanding, which holds in total a sufficient number of the voting rights attached to all outstanding voting securities of an issuer to affect materially the control of the issuer, and, if a combination of persons or companies holds more than 20% of the voting rights attached to all outstanding voting securities of an issuer, the combination of persons or companies is deemed, in the absence of evidence to the contrary, to hold a sufficient number of the voting rights to affect materially the control of the issuer.

Given the complex and subjective nature of the question of whether a particular holder may be a control person under Canadian securities laws, we make no representation concerning the right of any Fibrek shareholder who may receive Mercer Shares in the Offer to trade in such securities in Canada. We recommend that recipients of Mercer Shares consult their own counsel concerning whether they may freely trade Mercer Shares in Canada in compliance with applicable Canadian securities laws.

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The Offer is being made in compliance with applicable Canadian securities laws and regulations governing takeover bids.

### **NASDAQ Global Market and Toronto Stock Exchange Listing of Mercer Shares**

Pursuant to the terms of the Support Agreement, Mercer will use reasonable commercial efforts to cause all Mercer Shares to be issued in connection with the Offer to be approved for listing on the NASDAQ Global Market and the Toronto Stock Exchange at their time of issue.

### **Anticipated Accounting Treatment**

Mercer will account for the Offer as a purchase of the business, which means that the assets and liabilities of Fibrek will be recorded at their fair value and the results of operations of Fibrek will be included in Mercer's results of operations from and after the effective time of the Offer. The acquisition method of accounting is based on the Accounting Standards Codification Topic 805, Business Combinations.

### **Federal Securities Laws Consequences**

The Mercer Shares to be issued in the Offer will be registered under the Securities Act. These shares will be freely transferable under the Securities Act, except for Mercer Shares issued to any person who is deemed to be an affiliate of Mercer. Persons who may be deemed to be affiliates include individuals or entities that control, are controlled by, or are under common control with Mercer and includes Mercer's respective executive officers and directors, as well as principal shareholders. Affiliates may not sell their Mercer Shares acquired in the Offer, except pursuant to an effective registration statement under the Securities Act, covering the resale of those shares; or an applicable exemption under the Securities Act.

### **Consummation of the Offer**

Mercer launched the Offer on February 29, 2012 in accordance with applicable U.S. and Canadian law and the regulations of NASDAQ and the Toronto Stock Exchange. Pursuant to the terms of Canadian take-over bid regulations, the Offer period will last at least 35 and is set to expire on April 6, 2012 although the Offer period may be extended. Following the expiration of the Offer period and satisfaction or, to the extent permissible under the terms of the Support Agreement and by applicable law, waiver of all conditions to the obligations of the parties set forth in the Support Agreement, the closing of the Offer is expected to occur.

### **Compulsory Acquisition and Subsequent Acquisition Transaction**

If, within 120 days after the date of the Offer, the Offer is accepted by Fibrek shareholders holding not less than 90% of the issued and outstanding Fibrek Shares (calculated on a fully-diluted basis), other than Fibrek Shares held at the date of the Offer by or on behalf of us or our affiliates or associates (as defined in the CBCA), and we acquire such deposited Fibrek Shares, then we will acquire the Fibrek Shares not deposited under the Offer on the same terms as the Fibrek Shares acquired under the Offer pursuant to either the provisions of Section 206 of the CBCA (a Compulsory Acquisition) or pursuant to a subsequent acquisition transaction.

If we take up and pay for Fibrek Shares validly deposited under the Offer and a Compulsory Acquisition is not available or if we elect not to pursue a Compulsory Acquisition, we currently intend, depending upon the number of Fibrek Shares taken up and paid for under the Offer, to take such action as is necessary or advisable, including causing one or more special meetings of Fibrek shareholders to be called to consider a proposed arrangement, amalgamation, merger, reorganization, consolidation, recapitalization or similar transaction involving Fibrek and/or its subsidiaries and us or one of our wholly-owned subsidiaries which, if successfully completed, will result in us owning, directly or indirectly, all of the Fibrek Shares and/or all of the assets of Fibrek and will provide for consideration per Fibrek Share that is at least equal in value to and is in the same form as the consideration per Fibrek Share offered under the Offer.

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Provided that we own at least 66<sup>2</sup>/<sub>3</sub>% of the issued and outstanding Fibrek Shares (calculated on a fully-diluted basis) and, if required by Québec Regulation 61-101, sufficient votes are cast by minority holders to constitute a majority of the minority on a fully-diluted basis pursuant to Québec Regulation 61-101, we should own a sufficient number of Fibrek Shares to effect a subsequent acquisition transaction.

### **Mercer Board of Directors**

Following the closing of the Offer, the board of directors of Mercer will consist of seven directors, comprised of Mercer's current seven directors, being: Jimmy S.H. Lee, William D. McCartney, Graeme A. Witts, Eric Lauritzen, Guy Adams, James Shepherd and Bernard Picchi. See Annex H Directors of Mercer for a detailed biography of each current director of Mercer.

### **Ownership of Mercer Following the Offer**

Based on the number of Fibrek Shares currently outstanding and the maximum aggregate share consideration outlined in the Support Agreement, Mercer expects to issue an aggregate of approximately 11,741,496 Mercer Shares in connection with the Offer. The completion of the Offer will not change the number of Mercer Shares currently owned by Mercer shareholders. However, since Mercer expects to issue a number of new Mercer Shares in connection with the Offer, each outstanding Mercer Share immediately prior to the closing of the Offer will represent a smaller percentage of the total number of Mercer Shares outstanding following the closing of the Offer.

After the Offer, the percentage ownership of the outstanding shares of Mercer held by current Mercer shareholders and current Fibrek shareholders will depend on the percentage of outstanding Fibrek Shares that are tendered pursuant to the Offer. If all of the Fibrek Shares currently outstanding (which excludes any Fibrek Shares that may be issued or issuable after the date of this proxy statement) are tendered in the Offer, post-Offer the current shareholders of Mercer will hold approximately 83% of the outstanding Mercer Shares and the current shareholders of Fibrek will hold approximately 17% of the outstanding Mercer Shares.

For more information regarding the current and anticipated beneficial ownership of officers, directors and certain key shareholders of the combined companies prior to and after consummation of the Offer, see the section entitled "Principal Shareholders of Mercer", and the annexes entitled "Principal Shareholders of Fibrek" and "Mercer Directors" to this proxy statement.

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**THE SUPPORT AGREEMENT**

*This section contains a summary of the material provisions of the Support Agreement. Because it is a summary, it does not include all the information that may be important to you and is qualified by reference to the text of the Support Agreement. Before you decide how to vote, we encourage you to read carefully the entire copy of the Support Agreement which was filed with our Annual Report on Form 10-K for the fiscal year ended December 31, 2011 and which is incorporated by reference into this proxy statement as Annex G.*

**The Offer**

Mercer and Fibrek entered into the Support Agreement pursuant to which Mercer agreed to make the Offer.

The Offer is conditional upon, among other things, there being properly and validly deposited under the Offer and not withdrawn at the expiration of the Offer (the Expiry Time ) that number of Fibrek Shares which, together with the Fibrek Shares and any Special Warrants held by Mercer and its affiliates, represent at least 50.1% of the Fibrek Shares outstanding on a fully diluted basis. Unless all of the conditions of the Offer are satisfied or waived by Mercer at or prior to the Expiry Time, Mercer has the right to withdraw the Offer and shall not be required to take up and pay for or extend the period of time during which the Offer is open and postpone taking up and paying for, any Fibrek Shares deposited thereunder.

**Approval by Fibrek s board of directors**

Pursuant to the Support Agreement, Fibrek has agreed to support the Offer. Fibrek has confirmed to Mercer that Fibrek s board of directors, upon consultation with its outside legal and financial advisors, and upon receipt of a fairness opinion from TD Securities Inc., determined that the Offer is in the best interests of Fibrek and Fibrek s shareholders, approved the Offer and the Support Agreement and has resolved to recommend that shareholders accept the Offer.

**Representations and Warranties**

The Support Agreement contains a number of customary representations and warranties of Fibrek and Mercer relating to, among other things, the corporate status of Fibrek and the corporate authorization and enforceability of, and board approval of, the Support Agreement.

**Non-Solicitation**

Except as may be expressly permitted by the Support Agreement, Fibrek has agreed not to directly or indirectly, through any of its representatives or otherwise:

- (i) make, solicit, assist, initiate, encourage, promote or otherwise facilitate (including by way of furnishing information, permitting any visit to any facilities or properties of Fibrek or entering into any form of written or oral agreement, arrangement or understanding) any inquiries, offers or proposals regarding an Acquisition Proposal (as defined in the Support Agreement) or otherwise co-operate in any way with, or assist with or participate in any way in any effort or attempt by any person to make an Acquisition Proposal;
- (ii) enter into or participate in any discussions or negotiations regarding an Acquisition Proposal;
- (iii) withdraw, modify or qualify (or propose to do so) in a manner adverse to Mercer, the approval or recommendation of Fibrek s board of directors or any committee thereof of the Offer or the Support Agreement;
- (iv) approve, recommend or remain neutral or propose publicly to approve, recommend or remain neutral to any Acquisition Proposal, or

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- (v) accept, recommend (or remain neutral), approve or enter into (or propose to do so) any letter of intent, agreement in principle, agreement, understanding or arrangement in respect of an Acquisition Proposal or providing for the payment of any break, termination or other fees or expenses to any person in the event that Fibrek completes the transactions contemplated in the Support Agreement or any other transaction with Mercer or any of its affiliates agreed to prior to any termination of the Support Agreement, whether formal or informal.

Additionally, Fibrek has agreed that it will cease, and will cause its representatives to, immediately terminate any existing solicitation, assistance, discussions, negotiations or process with any persons (other than Mercer, its affiliates or its representatives) with respect to any proposal that constitutes, or which could reasonably be expected to lead to, an Acquisition Proposal, whether or not initiated by Fibrek, and to request the return or destruction of all such confidential information provided in connection therewith. Fibrek has also agreed not to amend, modify or waive, but to enforce any of the enforceable standstill, confidentiality and non-solicitation provisions of the confidentiality agreements entered into by Fibrek with other persons relating to a potential Acquisition Proposal.

**Right to Match**

Pursuant to the Support Agreement, Fibrek has agreed that it will not accept, approve, recommend or enter into any agreement, understanding or arrangement in respect of an Acquisition Proposal (other than a confidentiality and standstill agreement permitted by the Support Agreement). It has also agreed not to withdraw, modify or qualify its approval or recommendation of the Offer in any manner adverse to Mercer and to recommend or approve an Acquisition Proposal unless:

- (i) Fibrek's board of directors determines that the Acquisition Proposal constitutes a superior proposal;
- (ii) Fibrek has complied with certain covenants, including providing Mercer with a full and complete copy of the Acquisition Proposal;
- (iii) a period (the Response Period) of five (5) business days shall have elapsed from the later of (A) the date on which Mercer received written notice from Fibrek's board of directors that it has determined, subject only to compliance with the relevant provisions of the Support Agreement to accept, approve, recommend or enter into a binding agreement to proceed with the Superior Proposal (as defined in the Support Agreement) and (B) the date Mercer received a full and complete copy of such Acquisition Proposal;
- (iv) after the Response Period, Fibrek's board of directors determines in good faith, after consultation with its financial and legal advisors, that such Acquisition Proposal, after due consideration of any amendments to the Offer proposed by Mercer constitutes a superior proposal; and
- (v) Fibrek concurrently terminates the Support Agreement and has paid or concurrently pays to Mercer the Termination Fee (as defined below).

During the Response Period, Mercer has the right, but not the obligation, to offer to amend in writing the terms of the Support Agreement and the Offer. Under the terms of the Support Agreement, Fibrek agrees that, if requested by Mercer, it will negotiate with Mercer in good faith to amend the terms of the Support Agreement and the Offer. Fibrek's board of directors will review any such written amendment to determine, in good faith in the exercise of its fiduciary duties whether the Acquisition Proposal to which Mercer is responding would be a superior proposal when assessed against the Offer as it is proposed by Mercer to be amended. If Fibrek's board of directors does not so determine, it will cause Fibrek to enter into an amendment to the Support Agreement reflecting the proposal by Mercer to amend the terms of the Offer and upon the execution by the parties of such amendment will reaffirm its recommendation of the Offer, as so amended.

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### **Waiver of Conditions**

The Support Agreement provides that the conditions contained therein are for the exclusive benefit of Mercer and that they may be asserted by Mercer regardless of the circumstances giving rise to any such assertion, including any action or inaction by Mercer. Subject to the terms of the Support Agreement, Mercer may waive any of the conditions found therein in whole or in part at any time without prejudice to any other rights which Mercer may have.

### **Termination Fee**

Upon the occurrence of a Termination Fee Event (as such term is defined in the Support Agreement), Fibrek has agreed to pay to Mercer an amount equal to C\$8,500,000 (the Termination Fee ). In certain other circumstances, Mercer is entitled to an expense reimbursement of C\$2,000,000 (the Expense Reimbursement ). If Fibrek has made an Expense Reimbursement payment to Mercer and a Termination Fee subsequently becomes payable, the Termination Fee shall be reduced by the amount of such Expense Reimbursement.

### **Termination of the Support Agreement**

The Support Agreement may be terminated by notice in writing:

- (a) by mutual written consent of Fibrek and Mercer;
  
- (b) by Mercer, by written notice to Fibrek at any time if:
  - (i) Fibrek is in default or has materially breached its covenants or obligations as specified under the Support Agreement; or
  
  - (ii) any representation or warranty of Fibrek:
    - (A) that is qualified by reference to a Material Adverse Effect (as such term is defined in the Support Agreement) shall be untrue or incorrect in any respect;
  
    - (B) that is qualified by reference to materiality shall be untrue or incorrect in any respect; or
  
    - (C) that is not qualified by reference to a Material Adverse Effect or materiality shall be untrue or incorrect in any material respect,
  
- (c) by Fibrek, by written notice to Mercer, at any time if:
  - (i) Mercer is in default or has materially breached its covenants or obligations as specified under the Support Agreement; or
  
  - (ii) any representation or warranty of Mercer shall be untrue or incorrect in any material respect,

provided that in each case the applicable cure period has lapsed;

- (d) by Mercer, by written notice to Fibrek, if Fibrek's board of directors or any committee thereof (i) withdraws, amends or modifies in any manner adverse to Mercer its recommendation in favor of the Offer, or fails to recommend in favor of the Offer; (ii) approves or recommends in favor of any Acquisition Proposal; or (iii) Fibrek's board of directors fails to publicly recommend or reaffirm its approval of the Offer and recommendation that securityholders deposit all of their Fibrek Shares under the Offer within three (3) business days of the written request by Mercer that Fibrek's board of directors make such a recommendation or reaffirmation;
  
- (e) by Fibrek, by written notice to Mercer in order to accept, recommend or enter into a binding written agreement with respect to a superior proposal, the whole in accordance with and without any breach of its obligations under the Support Agreement;

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- (f) by either Fibrek or Mercer by written notice to the other if the Expiry Time does not occur on or prior to the Outside Date (as such term is defined in the Support Agreement), provided that the failure of the Expiry Time to occur is not the result of the breach of a representation, warranty or covenant by the party terminating the Support Agreement and provided further that Fibrek may only terminate the Support Agreement if Mercer has not waived the unsatisfied conditions and publicly announced its intention to take up and pay for Fibrek Shares that have been deposited pursuant to the Offer;
  - (g) by either Fibrek or Mercer, by written notice to the other if the Offer terminates, expires or is withdrawn at the Expiry Time without Mercer taking up and paying for any of the Fibrek Shares as a result of the failure of any of the conditions of the Offer being satisfied or waived, unless the failure of such condition shall be due to the failure of the party seeking to terminate the Support Agreement to perform the obligations required to be performed by it under the Support Agreement;
  - (h) by Fibrek or Mercer, if any court of competent jurisdiction or other governmental entity having authority over the parties shall have issued any order, decree or ruling enjoining or otherwise prohibiting the contemplated transactions, which order, decree or ruling is final and non-appealable (unless such order, decree or ruling has been withdrawn, reversed or otherwise made inapplicable); or
  - (i) by Mercer, by written notice to Fibrek at any time if:
    - (i) Fibrek has materially breached any covenant or obligation under the Special Warrant Agreement; or
    - (ii) any representation or warranty of Fibrek under the Special Warrant Agreement:
      - (A) that is qualified by reference to a Material Adverse Effect shall be untrue or incorrect in any respect;
      - (B) that is qualified by reference to materiality shall be untrue or incorrect in any respect; or
      - (C) that is not qualified by reference to a Material Adverse Effect or materiality shall be untrue or incorrect in any material respect,
- provided that in each case the applicable cure period has lapsed.

## **Conduct of Business by Fibrek**

Pursuant to the terms of the Support Agreement, Fibrek has agreed that, during the period from the execution of the Support Agreement until the transaction date, except as otherwise expressly contemplated or permitted by the Support Agreement or expressly consented to by Mercer in writing (which consent shall not be unreasonably withheld or delayed), Fibrek shall, and shall cause each of its subsidiaries to, conduct its business in the ordinary course of business consistent with past practice, and to use commercially reasonable efforts to maintain and preserve their business organization, assets, employees, goodwill and business relationships, as further specified in the Support Agreement.

## **Indemnities**

From and after the Effective Time, Mercer shall cause Fibrek and its subsidiaries (or any successors thereof) jointly and severally to indemnify the directors and officers of Fibrek and its subsidiaries, to the fullest extent to which Mercer and Fibrek are permitted to indemnify them under their respective constating documents and the currently existing indemnification agreements between Fibrek and its directors and officers and applicable law, from all claims in connection with any transactions or matters contemplated under the Support Agreement or otherwise in connection with Fibrek, its subsidiaries and their respective businesses and property.

## **Governing Law and Jurisdiction**

The Support Agreement is governed by the laws of the Province of Québec and the federal laws of Canada applicable therein.

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**Table of Contents****CERTAIN AGREEMENTS RELATED TO THE OFFER**

*The following summary describes the material provisions of certain agreements that it is expected will be entered into or have been entered into in connection with, or otherwise relate to, the Offer. The rights and obligations of the parties to these agreements are governed by the express terms and conditions of such agreements, respectively, and not by this summary. This summary may not contain all of the information about these agreements that may be important to you, and is qualified in its entirety by reference to the complete text of these agreements. We encourage you to read these agreements carefully and in their entirety for a more complete understanding of these agreements. See the section entitled *Where You Can Find More Information*.*

**Confidentiality Agreement**

On December 23, 2011, Mercer and Fibrek entered into a confidentiality agreement (the Confidentiality Agreement). Pursuant to the terms of the Confidentiality Agreement, we agreed, among other things, to keep confidential and not disclose without Fibrek's prior written consent the proprietary information of Fibrek furnished to Mercer. Except for information deemed highly confidential under the Confidentiality Agreement, the restrictions of the Confidentiality Agreement do not apply to disclosures made for the purposes of obtaining regulatory compliance in connection with the Offer. Mercer also agreed that, for a period of 12 months from the date of the Confidentiality Agreement or until the time they enter into a support agreement related to the Offer, whichever is earlier, it would not purchase any securities of Fibrek.

**Special Warrant Agreement**

On February 9, 2012, Mercer and Fibrek entered into a Special Warrant Agreement (the Special Warrant Agreement). Pursuant to the terms of the Special Warrant Agreement, Mercer agreed to purchase 32,320,000 special warrants of Fibrek (the Special Warrants) on a private placement basis, at a price of C\$1.00 per Special Warrant for total subscription proceeds of approximately C\$32,320,000. The Special Warrants are convertible into Fibrek Shares on a one-for-one basis. Conversion is automatic in certain events and otherwise at the option of Mercer. The Special Warrants are also redeemable by Mercer or Fibrek at their subscription price in certain stipulated events.

On February 24, 2012, Fibrek announced that it intended to appeal the decision to cease trade the Special Warrant financing rendered by the *Bureau de décision*. On February 25, 2012, Mercer also determined to appeal the aforesaid decision. Fibrek filed an inscription on appeal on February 27, 2012.

The proceeds from the private placement of Special Warrants will be deposited in trust on closing of the private placement and will be releasable either to Fibrek on conversion of the Special Warrants to Fibrek Shares, or to Mercer on redemption. The Special Warrants will be automatically converted into Fibrek Shares in the event of a Deemed Conversion Event (as such term is defined in the Special Warrant Agreement), including if following the close of business on the third business day following the date on which the Expiry Time occurs if at the Expiry Time the Minimum Tender Condition has not been satisfied, provided a Redemption Event (as such term is defined in the Special Warrant Agreement) has not occurred and Fibrek is otherwise in compliance with all of the terms of the Special Warrant Agreement and the Support Agreement. In addition, Mercer shall be entitled at any time and from time to time, immediately upon the earlier of: (i) the later of (a) seven business days after the date the Offer is made; (b) twenty-one days from the date of the Special Warrant Agreement; or (iii) on the date upon which Abitibi takes up or acquires legal or beneficial ownership or control of any of the Fibrek Shares subject to the existing lock-up agreements between Abitibi and certain of the shareholders of Fibrek, Mercer is entitled to convert all or any portion of the Special Warrants into Fibrek Shares without payment of any additional consideration. Upon the conversion of the Special Warrants into Fibrek Shares, Fibrek will receive the pro rata portion of the trust funds along with all earned interest on such funds corresponding to the number of Special Warrants converted.

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Mercer has the right to require Fibrek to redeem all or any portion of the Special Warrants at any time following the occurrence of a Redemption Event (as such term is defined in the Special Warrant Agreement).

In the event of a Redemption Event Mercer is entitled, at any time after the occurrence of the Redemption Event, at its option, to exercise its right to redeem all or any part of the Special Warrants then outstanding by delivering to Fibrek a redemption notice specifying the number of Special Warrants to be redeemed and indicating the Redemption Event giving rise to its ability to redeem the Special Warrants. Notwithstanding the foregoing, in the event of a delivery of a superior proposal pursuant to the Support Agreement, Mercer is prohibited from delivering a redemption notice to Fibrek prior to the expiration of the two business day period provided under Section 3.1(i) of the Special Warrant Agreement, provided that Fibrek has paid to Mercer the termination fee in accordance with Section 5.3(b)(ii) of the Support Agreement.

If at any time, the Special Warrants are converted into Fibrek Shares and a termination fee becomes payable under the Support Agreement, Mercer covenants and agrees to pay to Fibrek an amount in cash equal to either (x) the termination fee paid to Mercer pursuant to the terms and conditions of the Support Agreement in the event that the Special Warrant Profit (as such term is defined in the Special Warrant Agreement) actually received by Mercer is equal to or exceeds such termination fee or (y) the Special Warrant Profit actually received by Mercer in the event that the Special Warrant Profit actually received by Mercer is less than such termination fee.

In addition, the Special Warrant Agreement provides that in the event that Fibrek receives a superior proposal and as a result the termination fee becomes payable, Mercer will be required to tender or vote its Fibrek Shares received upon conversion of the Special Warrants in favor of such superior proposal, if shareholders (other than Mercer) holding in excess of 50.1% of the Fibrek Shares tender or vote their shares, or cast their votes as the case may be, in favor of such superior proposal.

On February 13, 2012, Fairfax, Pabrai Investment Funds, Oakmont Capital Inc. and Steelhead Partners, LLC filed a submission before the TSX seeking to stop the issuance of the Special Warrants, for which Fibrek filed a response letter on February 17, 2012. On February 23, 2012, the *Bureau de décision* granted an order to cease trade the Special Warrant financing. Both Mercer and Fibrek are appealing the decision to cease trade the Special Warrant financing rendered by the *Bureau de décision*.

As a result of the foregoing, and as the matter is before the Court of Québec, at this time, we cannot predict whether Fibrek will be permitted to issue the Special Warrants to us pursuant to the terms of the Special Warrant Agreement or at all.

## **Voting Support Agreements**

On February 9, 2012, Mercer entered into the Voting Support Agreements with the Supporting Shareholders who collectively own approximately 44% of the outstanding Mercer Shares at the announcement of Mercer's intention to commence the Offer. Pursuant to the terms of the Voting Support Agreements, each Supporting Shareholder agreed to vote (or cause to be voted) all of their Mercer Shares in favor of our shareholder proposal to issue additional Mercer Shares in connection with the Offer. The Supporting Shareholders are also prohibited from selling, assigning or otherwise transferring any of the Mercer Shares they hold as of the date of each respective Voting Support Agreement until the termination of such agreement.

The Voting Support Agreements each terminate upon the earlier of: (i) the date of termination of the respective Voting Support Agreement in accordance with its terms; (ii) the completion of the Special Meeting; (iii) the completion of the Offer; (iv) the date Mercer advises that it will not be proceeding with the Offer; and (v) 120 days from the date of each respective Voting Support Agreement. In the case of termination of any Voting Support Agreement, such agreement shall terminate and be of no further force of effect, and the parties thereto will have no further obligation or liability to each other.

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The Voting Support Agreements are each governed by the laws of the State of Washington and any federal laws applicable to agreements made and to be performed in the United States.

Copies of the voting support agreements are available on the SEC's web site at <http://www.sec.gov>.

## **Lock-up Agreements**

On February 9, 2012, in connection with the Support Agreement, we entered into lock-up agreements with Fibrek's directors and senior managers holding an aggregate of approximately 2.9% of the outstanding Fibrek Shares on a fully diluted basis (the Locked-up Shares) on that date. Under the terms of the applicable lock-up agreement, each of the holders of Locked-up Shares has agreed, among other things: (i) to exercise any eligible options in accordance with instructions received from Fibrek; (ii) to within thirty (30) days after commencement of the Offer in accordance with the Support Agreement, to (A) deposit or cause to be deposited all of the Locked-up Shares (other than the Locked-up Shares issuable upon the exercise of eligible options which shall be deposited as described in clause (B) hereof); and (B) deposit or cause to be deposited any Locked-Up Shares issued upon the exercise of all eligible options held by the holders of Locked-up Shares in accordance with the Support Agreement; (iii) not to sell, assign, transfer or encumber the Locked-Up Shares or agree to do any of the foregoing and not to permit any of its affiliates to sell, assign, transfer or encumber the Locked-Up Shares or agree to do any of the foregoing; (iv) to take all such steps as are required to ensure that at the time at which the Locked-Up Shares are taken up and paid for under the Offer the Locked-up Shares will be owned beneficially by the holders of Locked-up Shares with a good and valid title free of any encumbrances; (v) except in order to tender to a superior proposal, not to exercise, and to cause any of its affiliates to exercise, any statutory or other rights of withdrawal with respect to any of the Locked-Up Shares once deposited pursuant to the Offer (or otherwise disposed of) unless the lock-up agreement is terminated prior to Mercer taking up the Fibrek Shares under the Offer; and (vi) to not take any action, directly, or indirectly, which may in any way adversely affect the success of the Offer or the purchase of any Fibrek Shares under the Offer.

Each of the lock-up agreements may be terminated: (i) upon mutual consent of the parties to such lock-up agreements; (ii) by the applicable holders of Locked-up Shares, if we have not taken up and paid for the Fibrek Shares deposited pursuant to the applicable lock-up agreement on or prior to the outside date, as such term is defined in the Support Agreement; (iii) by the applicable holder of Locked-up Shares at any time the Offer is modified to reflect any change contemplated in the stipulated sections of the Support Agreement.

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**INFORMATION ABOUT MERCER INTERNATIONAL INC.**

Mercer Inc. is a Washington corporation and our shares of common stock are quoted and listed for trading on the NASDAQ Global Market (MERC) and listed in U.S. dollars on the Toronto Stock Exchange (MRI.U).

We acquired our initial pulp and paper operations in 1993. Subsequently, we disposed of our paper operations to focus our business on our core pulp operations. We are currently the largest publicly traded producer of market northern bleached softwood kraft, or NBSK, pulp in the world. Our operations are located in Eastern Germany and Western Canada. We operate three NBSK pulp mills with a consolidated annual production capacity of approximately 1.5 million air-dried metric tonnes, or ADMTs. We are the sole kraft pulp producer, and the only significant producer of pulp for resale, known as market pulp, in Germany, which is the largest pulp import market in Europe. Our three mills are:

**Rosenthal mill.** Our wholly-owned subsidiary, Rosenthal, owns and operates a modern, efficient ISO 9001 and 14001 certified NBSK pulp mill that has a current annual pulp production capacity of approximately 345,000 ADMTs. Additionally, the Rosenthal mill is a significant producer of green energy and exported 161,286 MWh of electricity in 2011, resulting in approximately 14.9 million in annual revenues. The Rosenthal mill is located near the town of Blankenstein, Germany approximately 300 kilometers south of Berlin.

**Celgar mill.** Our wholly-owned subsidiary, Celgar, owns and operates the Celgar mill, a modern, efficient ISO 9001 and 14001 certified NBSK pulp mill with an annual pulp production capacity of approximately 520,000 ADMTs. The Celgar mill also produces green energy and exported 140,069 MWh of electricity in 2011, resulting in approximately C\$14.5 million in annual revenues. The Celgar mill is located near the city of Castlegar, British Columbia, Canada, approximately 600 kilometers east of Vancouver, British Columbia, Canada.

**Stendal mill.** Our 74.9% owned subsidiary, Stendal, owns and operates a state-of-the-art, single-line, ISO 9001 and 14001 certified NBSK pulp mill that has an annual pulp production capacity of approximately 645,000 ADMTs. Additionally, the Stendal mill is a significant producer of green energy and exported 350,758 MWh of electricity in 2011, resulting in approximately 32.5 million in annual revenues. The Stendal mill is located near the town of Stendal, Germany, approximately 130 kilometers west of Berlin.

Our principal executive offices are located at Suite 1120, 700 West Pender Street, Vancouver, British Columbia, Canada, V6C 1G8, and our telephone number is (604) 684-1099. Mercer's website is [www.mercerint.com](http://www.mercerint.com)

For a description of Mercer's capital stock, please see Annex D, Description of Mercer's Capital Stock, to this proxy statement.

**INFORMATION ABOUT MERCER ACQUISITION**

Mercer Acquisition is a corporation incorporated under the CBCA, and a wholly-owned subsidiary of Mercer. Mercer Acquisition was organized solely for the purpose of making the Offer and has not otherwise conducted any business activities to date. Mercer Acquisition's registered office is located at Suite 1000, 925 West Georgia Street, Vancouver, British Columbia, Canada V6C 3L2.

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**INFORMATION ABOUT FIBREK**

FibreK was incorporated on March 24, 2010 pursuant to the provisions of the CBCA for the purpose of participating in an arrangement under Section 192 of the CBCA pursuant to which SFK Pulp Fund completed its reorganization from an income trust structure to a corporation named Fibrek Inc. on May 25, 2010.

FibreK is a leading producer and marketer of virgin and recycled kraft pulp operating three mills: the Saint-Félicien mill, the Fairmont mill, and the Menominee mill, with a combined annual production capacity of approximately 760,000 tonnes. The Saint-Félicien mill provides NBSK pulp to various sectors of the paper industry in Canada, the U.S. and Europe, for use in the production of specialized products. The Fairmont mill and the Menominee mill manufacture RBK pulp and primarily supply manufacturers of fine uncoated paper, household paper for commercial and industrial uses, and coated paper in the U.S.

**NBSK Pulp Operations**

The Saint-Félicien mill is located in Saint-Félicien, Québec, approximately 450 kilometres north of Montréal in the Lac-Saint-Jean region. The Saint-Félicien mill commenced production in 1978 with an initial annual capacity of approximately 230,000 tonnes. Improvements to the Saint-Félicien mill over the years have allowed for an increase in its capacity to approximately 375,000 tonnes per year. The Saint-Félicien mill supplies NBSK pulp to various sectors of the paper industry, for use in products such as lightweight coated papers, groundwood specialties, tissue grades, food packaging grades, supercalendered grades, high-quality woodfree coated grades and uncoated papers.

**RBK Pulp Operations**

The Fairmont mill is located in Fairmont, West Virginia, while the Menominee mill is located in Menominee, Michigan. The Fairmont and Menominee mills both commenced operations in the mid-1990s. With a total combined production of approximately 385,000 tonnes, both mills hold a share position of 48% of the approximately 800,000 tonne North American RBK market pulp segment.

FibreK's principal executive offices are located at 625 René-Lévesque Blvd. W., Suite 700, Montréal, Quebec, H3B 1R2, Canada, and Fibrek's telephone number is (514) 871-0550. Fibrek's website is [www.fibreK.com](http://www.fibreK.com).

For more information about Fibrek see Annex A Consolidated Financial Statements of Fibrek for the Years Ended December 31, 2011 and 2010, Annex B Management's Discussion and Analysis of Financial Information and Results of Operations of Fibrek and Annex E Principal Shareholders of Fibrek.

**Table of Contents****PRINCIPAL SHAREHOLDERS OF MERCER INTERNATIONAL INC.**

The following table and the related notes present information as of February 27, 2012 with respect to the beneficial ownership of Mercer Shares prior to the Offer and the expected beneficial ownership of Mercer Shares following the Offer by (i) each current director and named executive officer of Mercer, (ii) each person or group who is known to the management of Mercer to be the beneficial owner of more than 5% of all shares of Mercer voting securities outstanding as of February 27, 2011 and (iii) all current directors and current executive officers of Mercer, as a group. Unless otherwise indicated in the footnotes to the table below and subject to applicable community property laws, Mercer believes that each of the shareholders named in the table below has sole voting and investment power with respect to the shares indicated as beneficially owned.

**Share Ownership of Certain Beneficial Owners**

The following table sets forth information regarding the beneficial ownership of Mercer Shares as of February 27, 2012 by each shareholder known by us to own more than five percent (5%) of Mercer Shares other than as set forth under "Share Ownership of Directors and Executive Officers" below. Such information is based solely upon the Voting Support Agreements, as well as statements made in filings with the SEC or other information we believe to be reliable.

<b>Name and Address of Owner</b>	<b>Number of Mercer Shares Owned</b>	<b>Percent of Outstanding Mercer Shares</b>	<b>Percent of Outstanding Mercer Shares after Completion of the Offer<sup>(3)</sup></b>
Peter R. Kellogg <sup>(1)</sup> 48 Wall Street, 30 <sup>th</sup> Floor New York, NY 10005	15,156,223	27.2% <sup>(4)</sup>	22.4%
Platinum Investment Management Ltd. <sup>(2)</sup> Level 4, 55 Harrington Street Sydney, NSW 2000, Australia	7,449,356	13.4% <sup>(4)</sup>	11.0%

(1) Based on the Voting Support Agreement dated February 8, 2012 entered into between IAT Reinsurance Company Ltd. and the Company.

(2) Based on the Voting Support Agreement dated February 9, 2012 entered into between Platinum Investment Management Ltd. and the Company.

(3) Assumes that the maximum share consideration of 11,741,496 Mercer Shares is issued and taken up in connection with the Offer

(4) The percentage of outstanding Mercer Shares is calculated out of a total of 55,779,204 Mercer Shares issued and outstanding on February 27, 2012.

**Table of Contents****Share Ownership of Directors and Executive Officers**

The following table sets forth information regarding the ownership of Mercer Shares as of February 27, 2012 by (i) each of Mercer's current directors; (ii) our Chief Executive Officer, Chief Financial Officer and three other most highly compensated executive; and (iii) all of our directors and executive officers as a group. Unless otherwise indicated, each person has sole voting and dispositive power with respect to the Mercer Shares set forth opposite his name. Each person has indicated that he will vote all Mercer Shares owned by him in favor of each of the proposals to be considered at the Special Meeting.

Name of Owner	Number of Mercer Shares Owned	Percent of Outstanding Mercer Shares <sup>(9)</sup>	Percent of Outstanding Mercer Shares after Completion of the Offer <sup>(10)</sup>
Jimmy S.H. Lee <sup>(1)</sup>	1,986,434	3.6%	2.9%
Guy W. Adams <sup>(2)</sup>	21,000	*	*
William D. McCartney <sup>(2)</sup>	32,000	*	*
Graeme A. Witts <sup>(2)</sup>	88,685	*	*
Eric Lauritzen <sup>(2)</sup>	53,500	*	*
Bernard Picchi <sup>(3)</sup>	25,000	*	*
James Shepherd <sup>(3)</sup>	5,000	*	*
David M. Gandossi <sup>(4)</sup>	275,421	*	*
Wolfram Ridder <sup>(5)</sup>	40,000	*	*
Leonhard Nossol <sup>(6)</sup>	41,600	*	*
Claes-Inge Isacson <sup>(7)</sup>	16,466	*	*
Directors and Executive Officers as a Group (16 persons) <sup>(8)</sup>	2,735,022	4.9%	4.1%

\* Less than one percent (1%) of our issued and outstanding Shares on February 27, 2012.

- (1) Includes 200,000 shares of restricted stock, which vest and become non-forfeitable in equal amounts between 2012 and 2016. Does not include 198,008 performance share units granted under our 2010 Stock Incentive Plan (as defined below) that are subject to forfeiture and represent Mercer Shares that could not be acquired within 60 days of the date of this table.
- (2) In June 2011, 5,000 restricted shares were granted to each non-employee director (other than our Lead Director) in connection with his role as a non-employee director of Mercer. These Mercer Shares vest and become non-forfeitable in June 2012 unless a change in control of the Company occurs prior thereto.
- (3) Includes 5,000 restricted shares granted in June 2011 in connection with being elected an independent director of Mercer. These Mercer Shares vest and become non-forfeitable on June 2, 2012 unless a change of control of Mercer occurs prior thereto.
- (4) Includes 175,421 Mercer Shares and presently exercisable options to acquire up to 100,000 Shares. Does not include 92,883 performance share units granted under the 2010 Stock Incentive Plan.
- (5) Includes 20,000 Mercer Shares and presently exercisable options to acquire up to 20,000 Shares. Does not include 57,339 performance share units granted under the 2010 Stock Incentive Plan.
- (6) Includes 16,600 Mercer Shares and presently exercisable options to acquire up to 25,000 Shares. Does not include 51,565 performance share units granted under the 2010 Stock Incentive Plan.
- (7) Does not include 29,180 performance share units granted under the 2010 Stock Incentive Plan.
- (8) Includes presently exercisable options to acquire up to 175,000 Mercer Shares.
- (9) Based on 55,779,204 Mercer Shares outstanding on February 27, 2012.
- (10) Assumes the maximum share consideration is issued and taken up in the Offer.

As of February 27, 2012, there were 55,779,204 Mercer Shares issued and outstanding. Following the Offer, assuming that Mercer acquires 100% of the currently issued and outstanding Fibrek Shares (including Fibrek Shares to be issued pursuant to currently unexercised options to acquire Fibrek Shares), assuming the maximum share consideration of 11,741,496 Fibrek Shares is issued and taken up in the Offer, there are expected to be 67,520,700 Mercer Shares issued and outstanding.

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**INTERESTS OF CERTAIN PERSONS IN THE OFFER**

Except as set forth in this proxy statement, no other securities of Fibrek are beneficially owned, nor is control or direction exercised over any of such securities, by: (i) us or our directors or officers; or (ii) to our knowledge, after reasonable inquiry, any associate or affiliate of one of our insiders, any of our associates or affiliates, any of our insiders or any person acting jointly or in concert with us.

Except as set forth in this proxy statement: (i) neither we nor any of our directors or officers purchased, sold or effected any transaction in securities of Fibrek during the six-month period preceding the date of the Offer; and (ii) to our knowledge, after reasonable inquiry, no associate or affiliate of one of our insiders, none of our insiders and no person acting jointly or in concert with us, purchased, sold or effected any transaction in securities of Fibrek during the six-month period preceding the date of the Offer.

Except as set forth in this proxy statement: (i) neither we nor any of our directors or officers entered into any agreements, commitments or understandings to acquire any securities of Fibrek; and (ii) to our knowledge, after reasonable inquiry, no associate or affiliate of one of our insiders, none of our associates or affiliates, none of our insiders and no person acting jointly or in concert with us, entered into any agreements, commitments or understandings to acquire any securities of Fibrek.

To our knowledge, there are no direct or indirect benefits of accepting or refusing to accept the Offer, or in connection with any second step transaction, that will accrue to any director or officer of Mercer or Mercer Acquisition, to any associate or affiliate of a director or officer of Mercer or Mercer Acquisition, to any associate or affiliate of Mercer or Mercer Acquisition, to any other insider of Mercer or Mercer Acquisition or to such insider's associates or affiliates or to any person or company acting jointly or in concert with Mercer or Mercer Acquisition, other than those benefits that will accrue to Fibrek shareholders generally.

**Interests of Mercer Directors and Executive Officers in the Offer**

To the knowledge of Mercer, no director or executive officer of Mercer, nor any of their affiliates, have any interests in the Offer that differ from, or are in addition to, their interests as other holders of Mercer Shares. As of the record date for the Special Meeting, the directors and executive officers of Mercer, together with their affiliates, beneficially owned or had the right to vote, directly or indirectly, in the aggregate approximately [ ] Mercer Shares, entitling them to exercise approximately [ ]% of the voting power of the Mercer Shares at the Special Meeting. Mercer cannot complete the Offer unless the issuance of the Mercer Shares to be issued in connection with the Offer is approved by the affirmative vote of the holders of a majority of the Mercer Shares voting at the Special Meeting.

**Interests of Fibrek's Directors and Executive Officers in the Offer**

As of February 9, 2012, the directors and executive officers of Fibrek, together with their affiliates, beneficially owned in aggregate 3,860,982 Fibrek Shares or approximately 2.9% of the outstanding Fibrek Shares on a fully diluted basis. All of these Fibrek Shares are eligible to be tendered in the Offer under the same terms and conditions as the Fibrek Shares not held by Fibrek's directors or officers. Additionally, in connection with the Offer, Mercer entered into lock-up agreements with most of Fibrek's directors and officers pursuant to which such persons agreed to support the Offer by, among other things, tendering the Locked-up Shares in the Offer.

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**EXPERTS**

The consolidated financial statements of Mercer as of and for the years ended December 31, 2011, December 31, 2010 and December 31, 2009 and management's report on the effectiveness of internal control over financial reporting as of December 31, 2011, included in our Annual Report on Form 10-K for the year ended December 31, 2011, which is incorporated by reference in this proxy statement, have been audited by PricewaterhouseCoopers LLP, independent registered chartered accountants, as set forth in their report which is incorporated by reference herein, and have been so incorporated in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

The consolidated financial statements of Fibrek as at and for the years ended December 31, 2011 and 2010 included in this proxy statement have been audited by Samson Belair / Deloitte & Touche s.e.n.c.r.l, independent auditors, as stated in their report, which is included elsewhere in this proxy statement, and have been so included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

The consolidated financial statements of Fibrek as of and for the years ended December 31, 2011 and 2010 included in this proxy statement, have been prepared in accordance with IFRS.

**WHERE YOU CAN FIND MORE INFORMATION**

We are subject to the informational requirements of the *Securities Exchange Act of 1934*, as amended (the Exchange Act) and are required to file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any document we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for more information about the operation of the public reference room. The SEC maintains a web site that contains reports, proxy and information statements, and other information regarding issuers, including Mercer International Inc., that file electronically with the SEC. You may access the SEC's web site at <http://www.sec.gov>.

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**AVAILABLE INFORMATION AND INCORPORATION BY REFERENCE**

The SEC allows us to incorporate by reference information that we file with it into this proxy statement, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is an important part of this proxy statement. The information incorporated by reference into this proxy statement is deemed to be part of this proxy statement, and any information filed with the SEC after the date of this proxy statement will automatically be deemed to update and supersede information contained in this proxy statement.

The following document previously filed with the SEC is incorporated by reference in this proxy statement:

Our annual report on Form 10-K for the fiscal year ended December 31, 2011;

our Proxy Statement on Schedule 14A filed with the SEC on April 20, 2011 in respect of our annual meeting of shareholders held on June 1, 2011;

Current Reports on Form 8-K filed with the SEC on January 26, January 31 and February 13, 2012; and

Our Registration Statement on Form 8-A12G (with respect to the description of Mercer's shares of common stock) (File No.: 001-51826) filed with the SEC on March 1, 2006.

We incorporate by reference all documents filed pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act (other than any information furnished pursuant to Item 2.02 or 7.01 of any Current Report on Form 8-K) after the date of this proxy statement and prior to the conclusion of the Special Meeting.

You should rely only on the information contained or incorporated by reference in this proxy statement. We have not authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. You should assume that the information appearing in this offering memorandum is accurate only as of the date of this proxy statement. Our business, financial condition, results of operations and prospects may have changed since that date.

Any statement contained in a document incorporated or deemed to be incorporated by reference into this proxy statement will be deemed to be modified or superseded for the purposes of this proxy statement to the extent that a statement contained herein, or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein, modifies or supersedes that statement. The modifying or superseding statement need not state it has modified or superseded a prior statement or include any other information set forth in the document that it modifies or supersedes. The making of a modifying or superseding statement is not an admission for any purposes that the modified or superseded statement, when made, constituted a misrepresentation, an untrue statement of a material fact or an omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in light of the circumstances in which it was made. Any statement so modified or superseded will not be deemed, except as so modified or superseded, to constitute a part of this proxy statement.

We will provide promptly without charge to you, upon oral or written request, a copy of any document incorporated by reference in this proxy statement, other than exhibits to these documents unless the exhibits are specifically incorporated by reference in these documents. Requests should be directed as follows:

Mercer International Inc.

700 West Pender Street

Suite 1120

Vancouver, British Columbia

V6C 1G8 Canada

Telephone: (604) 684-1099

Attention: Investor Relations

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*Consolidated financial statements*

**FIBREK INC.**

*December 31, 2011 and 2010*

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**FIBREK INC.**

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**Independent Auditor's Report**

To the Board of Directors of

Fibrex Inc.

We have audited the accompanying consolidated financial statement of Fibrex Inc. (the Company) which comprise the consolidated statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010, and the consolidated statements of earnings, consolidated statements of comprehensive income, consolidated statements of changes in equity, and consolidated statements of cash flows for the years ended December 31, 2011 and December 31, 2010, and a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the Consolidated Financial Statements.**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the auditing standards generally accepted in the United States of America. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

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**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Fibrek Inc. as at December 31, 2011, December 31, 2010 and January 1, 2010 and its financial performance and its cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Montréal, Canada

February 22, 2012

<sup>1</sup> Chartered accountant auditor permit No. 13201

**Table of Contents****FIBREK INC.****Consolidated statements of earnings**

years ended December 31, 2011 and 2010

(in thousands of Canadian dollars, except per share amounts)

	2011 \$	2010 \$
<b>Sales</b>	<b>537,690</b>	556,539
Cost of products sold, including depreciation (Notes 6)	<b>472,248</b>	466,259
Delivery costs	<b>42,165</b>	41,494
Selling and administrative expenses	<b>17,889</b>	13,764
<b>Profit from operations</b>	<b>5,388</b>	35,022
Financial expenses (Note 20)	<b>11,380</b>	17,336
Financial income	<b>(192)</b>	(30)
(Gain) loss on financial instruments (Note 20)	<b>(3,492)</b>	3,216
Loss on disposal of property, plant and equipment	<b>390</b>	74
Gain on settlement of claim (Note 24)	<b>(55)</b>	(5,544)
(Gain) loss on foreign currency translation (Note 20)	<b>(1,530)</b>	3,381
Impairment (Note 7)	<b>62,985</b>	
<b>(Loss) earnings before income taxes</b>	<b>(64,098)</b>	16,589
Recovery of income taxes (Note 14)	<b>(67)</b>	(5)
<b>Net (loss) earnings</b>	<b>(64,031)</b>	16,594

**Per share information (Note 13)**

	(Loss) earnings per share	
	2011 \$	2010 \$
Basic	<b>(0.49)</b>	0.15
Diluted	<b>(0.49)</b>	0.12

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****FIBREK INC.****Consolidated statements of comprehensive income**

years ended December 31, 2011 and 2010

(in thousands of Canadian dollars)

	2011 \$	2010 \$
<b>Net (loss) earnings</b>	<b>(64,031)</b>	16,594
Other comprehensive (loss) income:		
Actuarial loss on retirement benefits, net of tax effects of \$nil, (2010 \$nil) (Note 10)	<b>(12,616)</b>	(4,997)
Unrealized gain (loss) on translation of financial statements of foreign operations, net of tax effects of \$nil, (2010 \$nil)	<b>1,928</b>	(5,124)
<b>Other comprehensive loss</b>	<b>(10,688)</b>	(10,121)
<b>Comprehensive (loss) income</b>	<b>(74,719)</b>	6,473

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****FIBREK INC.****Consolidated statements of financial position**

as at December 31, 2011 and 2010

(in thousands of Canadian dollars)

	December 31, 2011 \$	December 31, 2010 \$	January 1, 2010 \$
<b>Assets</b>			
Current assets			
Cash and cash equivalents (Notes 9 and 16)	5,576	16,421	19,174
Trade and other receivables (Note 5)	63,294	68,424	53,424
Inventories (Note 6)	99,868	77,187	78,255
Prepaid expenses	3,193	3,097	4,036
Investment at fair value through profit or loss (Note 24)	32	5,544	
	<b>171,963</b>	170,673	154,889
Deferred financing fees (Note 11)	1,315	1,716	421
Property, plant and equipment (Note 7)	307,553	382,609	407,442
Intangible assets (Note 8)	196	239	309
Other assets	765	663	856
	<b>481,792</b>	555,900	563,917
<b>Liabilities</b>			
Current liabilities			
Trade and other payables	66,488	56,064	45,213
Landfill closure liability (Note 9)	125	160	445
Derivative instruments			113
Current portion of long-term debt (Note 11)	2,016	1,876	36,682
Convertible unsecured subordinated debentures (Note 12)		49,609	
	<b>68,629</b>	107,709	82,453
Debt derivative at fair value through profit or loss			859
Landfill closure liability (Note 9)	2,256	1,731	3,166
Employee benefits (Note 10)	38,159	28,389	24,560
Convertible unsecured subordinated debentures (Note 12)			47,696
Long-term debt (Note 11)	115,653	82,798	118,776
	<b>224,697</b>	220,627	277,510
<b>Equity</b>			
Shareholders' capital (Note 13)	696,537	696,537	
Unitholders' capital (Note 13)			658,609
Equity Component of Debentures (Note 12)		4,188	
Reserves	(2,190)	(4,847)	
Deficit	(437,252)	(360,605)	(372,202)
	<b>257,095</b>	335,273	286,407

481,792

555,900

563,917

Contingent liabilities and guarantees (Note 19)

Commitments (Note 18)

The accompanying notes are an integral part of these consolidated financial statements.

**Approved by the Board and authorized for issue on February 22, 2012.**

(Signed) Hubert T. Lacroix, Director

(Signed) François R. Roy, Director

**Table of Contents****FIBREK INC.****Consolidated statements of changes in equity**

years ended December 31, 2011 and 2010

(in thousands of Canadian dollars)

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	2011						Total \$
	Shareholders capital (Note 13) \$	Reserves Unrealized loss on translation \$	Employee benefits reserve \$	Equity component of Debentures \$	Deficit \$		
Balance, December 31, 2010 (Note 26)	696,537	(5,124)	277	4,188	(360,605)	335,273	
Total comprehensive gain (loss) for the year		1,928			(12,616)	(10,688)	
Share-based payment (Note 15)			729			729	
Redemption of debentures (Note 12)				(4,188)		(4,188)	
Net loss					(64,031)	(64,031)	
<b>Balance, December 31, 2011</b>	<b>696,537</b>	<b>(3,196)</b>	<b>1,006</b>		<b>(437,252)</b>	<b>257,095</b>	

  

	2010						Total \$
	Unitholders capital (Note 13) \$	Shareholders capital (Note 13) \$	Reserves Unrealized loss on translation \$	Employee benefits reserve \$	Equity component of Debentures \$	Deficit \$	
Balance, January 1, 2010 (Note 26)	658,609					(372,202)	286,407
Total comprehensive loss for the year			(5,124)			(4,997)	(10,121)
Share-based payment (Note 15)				277			277
Conversion into a corporation	(658,609)	658,609			4,188		4,188
Issuance of shares		37,928					37,928
Net earnings						16,594	16,594
<b>Balance, December 31, 2010 (Note 26)</b>		<b>696,537</b>	<b>(5,124)</b>	<b>277</b>	<b>4,188</b>	<b>(360,605)</b>	<b>335,273</b>

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****FIBREK INC.****Consolidated statements of cash flows**

years ended December 31, 2011 and 2010

(in thousands of Canadian dollars)

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	2011 \$	2010 \$
<b>Operating activities</b>		
Net (loss) earnings	(64,031)	16,594
Adjustments for:		
Income tax recovery included in net (loss) earnings	(67)	(5)
Depreciation of property, plant and equipment	35,827	34,415
Amortization of intangible assets	44	70
Financial expenses	11,380	17,336
Unrealized (gain) loss on translation of monetary items denominated in foreign currency	(235)	564
Gain on settlement of claim	(55)	(5,544)
Employee benefits	(2,971)	(1,196)
Share-based payment	729	277
Changes in landfill closure liability (Note 9)	342	(1,374)
Loss on disposal of property, plant and equipment	390	74
Impairment	62,985	
(Gain) loss on financial instruments	(3,492)	3,216
Changes in non-cash operating working capital items (Note 16)	(6,872)	2,194
Income tax (paid) received	(14)	5
	<b>33,960</b>	<b>66,626</b>
<b>Financing activities</b>		
Borrowings under the term loan plan, net of financing fees		75,646
Borrowings under ABL Credit Facility	72,805	10,427
Borrowings under the Investissement Quebec Plan		978
Refinancing fees		(2,062)
Share issuance costs		37,928
Reimbursement of long-term debt (including the ABL Credit Facility)	(41,474)	(160,132)
Redemption of debentures	(51,749)	
Interest paid	(9,247)	(12,501)
	<b>(29,665)</b>	<b>(49,716)</b>
<b>Investing activities</b>		
Acquisitions of property, plant and equipment	(31,458)	(20,013)
Grants received to fund capital expenditures	10,043	364
Proceeds from disposal of property, plant and equipment	20	16
(Increase) decrease in other assets	(100)	290
Proceeds from disposal of investment at FVTPL, net of transaction fees (Note 24)	6,307	
	<b>(15,188)</b>	<b>(19,343)</b>

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Effect of foreign exchange rate changes on cash and cash equivalents held in foreign currency	48	(320)
Cash and cash equivalents outflow	<b>(10,845)</b>	<b>(2,753)</b>
Cash and cash equivalents, beginning of year	<b>16,421</b>	19,174
<b>Cash and cash equivalents, end of year (Note 16)</b>	<b>5,576</b>	16,421

Supplemental disclosure of cash flow information (Note 16).

The accompanying notes are an integral part of these consolidated financial statements.

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### **FIBREK INC.**

#### **Notes to the consolidated financial statements**

**years ended December 31, 2011 and 2010**

**(in thousands of Canadian dollars, except per share amounts)**

#### **1. Description of the Company**

FibreK Inc. is the successor to SFK Pulp Fund (the Fund) following the completion of the conversion of the Fund from an income trust structure to a corporate structure by way of the transfer of units held by unitholders of the Fund to Fibrek Inc., on the basis of one common share for each unit so transferred (the Arrangement). As a result of the Arrangement, the holders of units became the shareholders of Fibrek.

FibreK Inc. was incorporated on March 24, 2010 under the *Canadian Business Corporations Act* and did not carry on any active business prior to the Arrangement, other than executing the arrangement agreement pursuant to which the Arrangement was implemented on May 25, 2010. The registered office of Fibrek is located at 625 René-Lévesque Blvd. West, Suite 700, Montréal, Québec, H3B 1R2.

FibreK Inc. obtained the final order from the Québec Superior Court with respect to the plan of arrangement on May 25, 2010. Comparative figures presented in the consolidated financial statements of the Company include all amounts previously reported by the Fund. Reference to Company, share, dividends and shareholders means Fund, unit, distributions and unitholders for transactions that occurred before the conversion of the Fund into a corporation.

FibreK Inc., together with its subsidiaries (collectively the Company), is a producer and marketer of premium virgin and recycled kraft pulp. The Saint-Félicien (Québec) mill supplies northern bleached softwood kraft (NBSK) pulp to various sectors of the paper industry primarily in Canada, the United States and Europe for use in specialty products. The Fairmont (West Virginia) and Menominee (Michigan) mills manufacture air-dried market recycled bleached kraft (RBK) pulp and primarily supply manufacturers of uncoated freesheet, coated papers, commercial and away-from-home tissue mainly in the United States.

#### **2. Summary of significant accounting policies**

##### *Statement of compliance*

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standard Board (IFRS) that are issued and effective as at December 31, 2011, the Company's first annual IFRS reporting date. Prior to January 1, 2011, the Company prepared its interim and annual consolidated financial statements in accordance with Canadian generally accepted accounting principles (GAAP).

The adoption of IFRS resulted in changes to the accounting policies as compared with the most recent annual financial statements prepared under Canadian GAAP. The accounting policies set out below have been applied consistently to all periods presented. They also have been applied in the preparation of an opening IFRS statement of financial position as at January 1, 2010 (the Transition Date), as required by IFRS 1, *First Time Adoption of International Financial Reporting Standards* (IFRS 1). The impact of the transition from Canadian GAAP to IFRS is explained in Note 26.

##### *Basis of presentation*

These consolidated financial statements have been prepared on a historical cost basis, with the exception of financial instruments classified as fair value through profit or loss. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

The principal accounting policies effective are set out below.



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### **FIBREK INC.**

#### **Notes to the consolidated financial statements**

**years ended December 31, 2011 and 2010**

**(in thousands of Canadian dollars, except per share amounts)**

#### **2. Summary of significant accounting policies (continued)**

##### *Basis of consolidation*

These consolidated financial statements include the accounts of the Company and its subsidiaries. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. All intercompany transactions, balances, income and expenses are eliminated in full on consolidation.

##### *Revenue recognition*

The Company's sales consist of NBSK and RBK pulp to various sectors of the paper industry primarily in Canada, the United States, and Europe. Sales are recognized after the Company has transferred the risks and rewards of ownership to the buyer and retains neither a continuing right to dispose of the goods, nor effective control of those goods; usually, this means that sales are recorded upon shipment of goods to customers in accordance with agreed terms of delivery.

Sales are measured at the fair value of the consideration received or receivable and are reduced for estimated customers rebates and other similar allowances.

##### *Related party transactions*

Related party transactions are recorded on terms equivalent to those that prevail in arm's length transactions.

##### *Cash and cash equivalents*

Cash and cash equivalents in the consolidated statement of financial position comprise cash in financial institutions and on hand, and short-term deposits with a maturity of three months or less, which are readily convertible into a known amount of cash. The Company's cash and cash equivalents are invested with major financial institutions in business accounts and bankers' acceptances that are available on demand by the Company.

##### *Inventories*

Pulp is measured at the lower of cost and net realizable value, with cost being determined using the weighted average cost method. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and any applicable variable selling costs.

Raw materials (wood fibre and wastepaper), production and maintenance supplies and other raw materials are measured at the lower of cost determined using the weighted average cost method and replacement cost. Raw materials are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost.

The cost of inventories comprises all costs of purchase, costs of conversion, and other costs incurred in bringing the inventories to their present location and condition. The costs of purchase comprise the purchase price, import duties and non-recoverable taxes, transportation, handling and other costs directly attributable to the acquisition of finished goods, materials or services. The costs of conversion include direct material and labour costs, and a systematic allocation of fixed and variable overheads incurred in converting materials into finished goods.



**Table of Contents****FIBREK INC.****Notes to the consolidated financial statements**

years ended December 31, 2011 and 2010

(in thousands of Canadian dollars, except per share amounts)

**2. Summary of significant accounting policies (continued)***Property, plant and equipment*

Property, plant and equipment are recorded at cost, less accumulated depreciation and accumulated undepreciated impairment losses.

The cost of property, plant and equipment consists of the purchase price net of grants, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Depreciation is based on cost less residual value and provided for using the following methods and rates over the estimated useful lives of the assets:

Land	Not amortized	indefinite life
Buildings and related components	Straight-line	10 to 40 years
Warehouse under finance lease	Straight-line	over the lease term
Equipment:		
Processing equipment	Straight-line	5 to 20 years
Mobile equipment	Declining balance	30%
Furniture and fixtures	Straight-line	20 years
Computers	Straight-line	3 to 10 years
Roads, lots and other	Straight-line	20 years
Major maintenance	Straight-line	1 to 4 years
Construction in progress	Not amortized	

Additions to property, plant and equipment are amortized from the date they are available for use. Expenditures incurred to replace a component of an item of property, plant and equipment, including those associated with major inspections, are capitalized.

Assets subject to finance leases are recorded in the financial statements under the same category as if they were directly owned by the Company and amortized over the shorter of their estimated useful life or the lease term.

The depreciation method, residual values, and useful lives of property, plant and equipment are reviewed annually and any change in estimate is applied prospectively.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in the statement of earnings.

*Borrowing costs*

The Company capitalizes borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, until the qualifying assets are ready for their intended use. All other borrowing costs are expensed as incurred.

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Qualifying assets are major assets that necessarily take a substantial period of time to get ready for use or sale. Borrowing costs include the costs related to specific or general borrowed funds. These funds which relate to borrowings that could have been avoided had the asset not been acquired, constructed or produced.

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### **FIBREK INC.**

#### **Notes to the consolidated financial statements**

**years ended December 31, 2011 and 2010**

**(in thousands of Canadian dollars, except per share amounts)**

## **2. Summary of significant accounting policies (continued)**

### *Intangible assets*

Intangible assets represent application software and are recorded at cost. These assets are recognized at cost less accumulated depreciation and accumulated impairment losses. Depreciation is recognized on a straight-line basis over their useful life of 3 to 10 years. Additions to intangible assets are amortized from the date they are available for use.

The depreciation method and useful life is reviewed annually and any change in estimate is applied prospectively.

### *Leases*

Leases are classified as either finance or operating leases. Finance leases are those that substantially transfer the benefits and risks of ownership of an asset to the lessee. All leases other than finance leases are operating leases.

Assets held under finance leases are recognized as assets of the Company at the lower of the fair value at the inception of the lease or the present value of the minimum lease payments. The corresponding liability is recognized as a finance lease obligation. Lease payments are apportioned between financial expenses and reduction of the lease obligation to achieve a constant rate of interest on the remaining liability. Financial expenses are charged to the statement of earnings, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the Company policy on borrowing costs.

Total payments under operating leases are expensed on a straight-line basis over the term of the relevant lease. Incentives received upon entry into an operating lease are recognized as a liability and as reduction of rental expense on a straight-line over the lease term.

### *Impairment of assets*

At each financial position reporting date, the Company determine whether there is any indication that its assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated to determine the extent of the impairment, if any.

The recoverable amount is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted at a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in the consolidated statement of earnings.

For an asset that does not generate independent cash inflows, the review of the recoverable amount is performed at the cash generating unit level to which the asset belongs. A cash generating unit is the smallest identifiable group of assets that generates independent cash inflows.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, to the extent the increased carrying amount does not exceed what the carrying amount would be, had no impairment loss been previously recognized. A reversal of an impairment loss is recognized immediately in the consolidated statement of earnings.

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**FIBREK INC.**

**Notes to the consolidated financial statements**

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**2. Summary of significant accounting policies (continued)**

*Financial instruments*

The Company recognizes financial assets and financial liabilities when the Company becomes a party to a contract. Financial assets and financial liabilities, with the exception of financial assets and financial liabilities classified at fair value through profit or loss, are measured at fair value plus transaction costs on initial recognition.

Measurement in subsequent periods depends on the classification of the financial instrument.

*i) Financial assets at fair value through profit or loss (FVTPL)*

Financial assets are classified as FVTPL when acquired principally for the purpose of trading or so designated by management (fair value option), or if they are derivative assets that are not part of an effective and designated hedging relationship. Financial assets classified as FVTPL are measured at fair value on initial recognition, with subsequent changes recognized in the statement of earnings, and transaction costs are expensed when incurred.

The Company's financial assets classified as FVTPL include investment at FVTPL and derivative instruments that are not part of an effective and designated hedging relationship. The Company does not currently apply hedge accounting.

*ii) Financial liabilities at FVTPL*

Financial liabilities are classified as FVTPL if they are designated as such by management, or they are derivative liabilities that are not part of an effective and designated hedging relationship.

Financial liabilities classified as FVTPL are measured at fair value on initial recognition, with subsequent changes recognized in the statement of earnings, and transaction costs are expensed when incurred.

The Company's financial liabilities classified as FVTPL include derivative instruments that are not part of an effective and designated hedging relationship. The Company does not currently apply hedge accounting.

*iii) Loans and receivables*

Loans and receivables are non-derivative financial assets that have fixed or determinable payments and are not quoted in an active market. Subsequent to initial recognition, loans and receivables are carried at amortized cost using the effective interest method.

Trade and other receivables and cash and cash equivalents are classified as loans and receivables.

*iv) Other financial liabilities*

Other financial liabilities are financial liabilities that are not classified as FVTPL. Subsequent to initial recognition, other financial liabilities that are not subject to hedge accounting are measured at amortized cost using the effective interest method.

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The Company's other financial liabilities include trade and other payables and long-term debt.

The effective interest method is a method of calculating the amortized cost of an instrument and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash flows (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument to the net carrying amount on initial recognition.

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**FIBREK INC.**

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**2. Summary of significant accounting policies (continued)**

*v) Impairment of financial assets*

At each financial position reporting date, the financial assets, other than those at FVTPL, are assessed to determine if those financial assets are impaired. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

The amount of the impairment loss is recognized in profit or loss and is measured by the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been if the impairment had not been recognized.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account.

*vi) Classification as debt or equity*

Debt and equity instruments issued by a group entity are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

*vii) Compound instruments*

The components parts of compound instruments issued by the Company are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument. A conversion option that would be settled by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is an equity instrument.

At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for similar non-convertible instruments. The conversion option classified as equity is determined by deducting the amount of the liability component from the fair value of the compound instrument as a whole. This is recognized and included in equity, net of income tax effects, and is not subsequently remeasured.

*viii) Derecognition of financial assets*

The Company derecognize financial assets only when the contractual rights to the cash flows from the assets expire, or when it transfers substantially all the risks and rewards of ownership of the asset to another entity. On derecognition of financial assets, the gain or loss is recognized in profit or loss.

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### **FIBREK INC.**

#### **Notes to the consolidated financial statements**

**years ended December 31, 2011 and 2010**

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#### **2. Summary of significant accounting policies (continued)**

##### *Comprehensive income*

Comprehensive income is the change in the Company's net assets during the period that results from transactions and other events and circumstances except those resulting from investments by shareholders and dividends to shareholders. The Company's other comprehensive income includes only the unrealized gain or loss on the translation of financial statements of foreign operations with a different functional currency than the Company and the unrealized actuarial gain or loss under defined benefit plans.

##### *Foreign currency translation*

The Canadian dollar is the functional and presentation currency of the Company. Functional currency is also determined for each of the Company's subsidiaries, and items included in the financial statements of the subsidiaries are measured using their functional currency.

Transactions in currencies other than the functional currency are translated into the functional currency using the exchange rates prevailing at the dates of the transaction. Monetary assets and liabilities not denominated in the functional currency are translated at the period-end rates of exchange. Foreign exchange gains and losses are recognized in the consolidated statement of earnings.

Assets and liabilities of entities with functional currencies other than Canadian dollar are translated at the period-end rates of exchange, and the results of their operations are translated at average rates of exchange for the year. The resulting translation adjustments are included in other comprehensive income in equity.

Intercompany amounts with foreign operations for which settlement is neither planned nor likely to occur in the foreseeable future are part of the Company's net investment in the foreign operations. Foreign exchange gains and losses related to these intercompany amounts are included in other comprehensive income.

##### *Income taxes*

Income taxes are determined using the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Deferred income tax assets are recognized to the extent that realization is considered probable.

Current and deferred taxes are recognized in profit or loss, except when they relate to items that are recognized in other comprehensive income or directly in equity, in which case, the current and deferred taxes are also recognized in other comprehensive income or directly in equity respectively.

##### *Landfill closure liability*

The Company owns a landfill in Menominee, Michigan. The Company provides for estimated closure and post-closure monitoring costs over the operating life of its landfill as air-space is consumed. Such costs are estimated based on the technical requirements of regulations of the U.S. Environmental Protection Agency or the applicable state requirements, and include such items as a final cap and cover on the site, methane gas and leachate management, and groundwater monitoring. The landfill closure liability is measured based on the best estimate of the obligation, discounted at a risk free rate.



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### **FIBREK INC.**

#### **Notes to the consolidated financial statements**

**years ended December 31, 2011 and 2010**

**(in thousands of Canadian dollars, except per share amounts)**

#### **2. Summary of significant accounting policies (continued)**

##### *Landfill closure liability (continued)*

The liability is re-measured at each reporting date to reflect current estimates and changes in the discount rate. Changes in the liability that result from the passage of time (accretion) are recorded as borrowing costs, which are presented as financial expense in the consolidated statement of earnings. The estimated costs and estimated total available air-space is reviewed and updated by management on a periodic basis and changes in such estimated amounts are reflected on a prospective basis unless they indicate there is an impairment of the carrying value of the corresponding asset.

##### *Environmental expenditures*

Environmental expenditures that will benefit the Company in future years are capitalized as part of property, plant and equipment. Amortization is charged to earnings over the estimated useful life of the asset. Environmental expenditures that are not expected to provide a benefit to the Company in future periods are accrued and recorded in earnings when a requirement to remedy an environmental exposure is identified.

##### *Employee benefits*

The Company sponsors contributory defined benefit plans that provide for pension and post-employment benefits for certain employees. Beginning January 1, 2010, all Canadian non-unionized employees have stopped accruing benefits under the accruing defined benefits pension plans and started with a new defined contribution plan. The Company maintains defined contribution 401(K) plans for all US employees that meet service eligibility requirements. The Company also maintains non-funded non-contributory supplementary defined benefit plans for executives and a former executive as well as a non-funded non-contributory supplementary defined contribution pension plan for executives.

The cost of benefits earned, under defined benefit plans, is actuarially determined using the projected benefit method, with actuarial valuations being carried out at the end of each annual reporting period. The expected return on plan assets is based on the fair value of pension assets, which are measured at fair value. The net actuarial gains or losses are recognized in other comprehensive income in the period they arise which is directly recognized in the deficit. As such, the benefit expense is not impacted by those gains or losses.

Contributions to defined contribution plans are expensed as incurred.

##### *Share-based payment plans*

The Company has share-based payment plans under which it receives services from employees against consideration for equity instruments of the Company or cash payments.

For plans that are settled with shares of the Company, the expense is determined based on the fair value of the award granted and recognized over the period during which services are received, which is usually the vesting period. For awards with graded vesting, the fair value of each tranche is recognized over its respective vesting period.

For cash-settled plans and plans where the employee can choose to settle in equity or cash, the expense is determined based on the fair value of the liability at the end of the reporting period until the award is settled. The fair value of the liability is determined with reference to the market price of the Company's shares at the reporting date or through the use of an option pricing model depending on the nature of awards under the plan.

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At the end of each reporting period, the Company re-assesses its estimates of the number of awards that are expected to vest and recognizes the impact of the revisions in the statement of earnings.

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### **FIBREK INC.**

#### **Notes to the consolidated financial statements**

**years ended December 31, 2011 and 2010**

**(in thousands of Canadian dollars, except per share amounts)**

#### **2. Summary of significant accounting policies (continued)**

##### *Government grants*

Government grants are recognized when there is reasonable assurance that the Company will comply with the conditions and that the grants will be received.

Government grants related to expenditures for property, plant and equipment are recognized as a reduction in the cost of those assets. Government grants related to expenses are recognized as a reduction of those expenses.

The benefit of a government loan at a below-market rate of interest is treated as a government grant, measured as the difference between proceeds received and the fair value of the loan based on prevailing market interest rates.

#### **3. Accounting standards issued but not yet effective**

The following new accounting standards or amendments to existing accounting standards have been published and are required, except for International Accounting Standards ( IAS ) 1 *Presentation of Financial Statements*, to be applied for accounting periods beginning on or after January 1, 2013, with early adoption permitted. The amendments to IAS 1, *Presentation of Financial Statements*, are to be applied for accounting periods beginning on and after July 1, 2012.

##### *IFRS 9 Financial Instruments ( IFRS 9 )*

IFRS 9 was issued in November 2009 and was amended in October 2011, provides guidance on the classification and measurement of financial assets and financial liabilities, and requirements for the derecognition of financial assets and financial liabilities. This standard will replace IAS 39, *Financial Instruments - Recognition and Measurement ( IAS 39 )*.

The Company has not yet assessed the impact of this new standard on its consolidated financial statements or determined whether it will early adopt the standard.

##### *IFRS 10 Consolidated Financial Statements ( IFRS 10 )*

IFRS 10 was issued in May 2011 and will replace the consolidation requirements in Standing Interpretations Committee ( SIC ) 12, *Consolidation - Special Purpose Entities*, and IAS 27, *Consolidated and Separate Financial Statements*. The standard provides a single consolidation model that identifies control as the basis for consolidation for all types of entities. The revised definition of control indicates that control over an investee exists when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

##### *IFRS 11 Joint Arrangements ( IFRS 11 )*

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IFRS 11 was issued in May 2011 and will supersede IAS 31, *Interests in Joint Ventures*, and SIC-13, *Jointly Controlled Entities Non-Monetary Contributions by Venturers*. This standard reduces the types of joint arrangements to two: joint operations and joint ventures. It requires a single method of accounting for joint ventures, the equity method, eliminating the proportionate consolidation method.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

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**FIBREK INC.**

**Notes to the consolidated financial statements**

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**3. Accounting standards issued but not yet effective (continued)**

*IFRS 12 Disclosure of Interests in Other Entities ( IFRS 12 )*

IFRS 12, issued in May 2011, addresses disclosure requirements of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

*IAS 28 Investments in Associates and Joint Ventures ( IAS 28 )*

As a consequence of the issuance of IFRS 10, IFRS 11 and IFRS 12, IAS 28 was retitled and amended in May 2011 to include the requirements for the application of the equity method when accounting for joint ventures.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

*IFRS 13 Fair Value Measurement ( IFRS 13 )*

IFRS 13, issued in May 2011, defines fair value, sets out a framework for measuring fair value and provides disclosure requirements about fair value measurement. This standard will apply when other IFRS require or permit fair value measurement.

The Company has not yet assessed the impact of this new standard on its consolidated financial statements or determined whether it will early adopt the standard.

*IAS 19 Employee Benefits ( IAS 19 )*

In June 2011, IAS 19 was amended to remove the corridor approach, which was an option to defer some gains and losses that arise from defined benefit plans. The options for presenting gains and losses are also removed. It requires companies to include service cost and finance cost in profit or loss and remeasurements in other comprehensive income. The amendments also improve disclosure requirements relating to the characteristics of defined benefit plans, the amounts recognized in the financial statements and the risks arising from defined benefit plans.

The Company has not yet assessed the impact of this new standard on its consolidated financial statements or determined whether it will early adopt the standard.

*IAS 1 Presentation of Financial Statements ( IAS 1 )*

Issued in June 2011, the amendments to IAS 1 will require the grouping of items within other comprehensive income into items that might be reclassified to profit or loss and items that will not be reclassified to profit or loss in subsequent accounting periods.

The Company has not yet assessed the impact of this new standard on its consolidated financial statements or determined whether it will early adopt the standard.



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### **FIBREK INC.**

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#### **4. Critical accounting estimates and judgements**

The preparation of the consolidated financial statements using accounting policies consistent with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. The preparation of the consolidated financial statements also requires management to exercise judgement in the process of applying the accounting policies.

##### *a) Critical accounting estimates*

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized prospectively from the period in which the estimates are revised.

The following are the key assumptions about the future and other key sources of estimation uncertainty that have a significant risk of resulting in a material adjustment within the next financial year.

##### *i) Impairment of assets*

When there is indication that an asset may be impaired, the Company is required to estimate the asset's recoverable amount. Recoverable amount is the greater of the value in use and the fair value less costs to sell. Determining the value in use requires the Company to estimate expected future cash flows associated with the assets and a suitable discount rate in order to calculate present value.

On adoption of IFRS, the Company recognized an impairment loss of \$136,964. Details of the impairment loss calculation are included in Note 26.

##### *ii) Useful lives of property, plant and equipment and intangible assets*

Property, plant and equipment and intangible assets are amortized over the estimated useful life of the assets. Changes in the estimated useful lives could significantly increase or decrease the amount of depreciation recorded during the year.

Total depreciation recorded for the year ended December 31, 2011 was \$35,871 (2010 \$34,485).

##### *iii) Employee benefits*

The Company sponsors defined benefit plans providing pension and other post-employment benefits to eligible employees. The determination of expense and obligations associated with employee benefits requires the use of assumptions such as the expected return on assets available to fund pension obligations, the discount rate to measure obligations, the expected mortality, the expected rate of future compensation and the expected healthcare cost trend rate. Because the determination of the cost and obligations associated with employee benefits requires the use of various assumptions, there is measurement uncertainty inherent in the actuarial valuation process. Actual results will differ from results that are estimated based on assumptions.

##### *iv) Landfill closure liability*

The Company has obligations associated with closure and post-closure activities over the operating life of a landfill in Menominee, Michigan. The Company is required to make estimates regarding these future costs to establish the current measurement of the landfill closure liability.

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Total liability associated with the landfill closure recorded as at December 31, 2011 was \$2,381 (2010 \$1,891).

Further details are included in Note 9.

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years ended December 31, 2011 and 2010

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**4. Critical accounting estimates and judgements (continued)***b) Critical judgements used in applying accounting policies**i) Income taxes*

The measurement of income taxes payable and deferred income tax assets and liabilities requires management to make judgements in the interpretation and application of the relevant tax laws. The actual amount of income taxes only becomes final upon filing and acceptance of the tax return by the relevant authorities, which occurs subsequent to the issuance of the financial statements.

*ii) Classification of leases*

The Company is a lessee under a number of lease contracts, the accounting of which is dependent on whether the leases are classified as finance or operating leases. In determining the appropriate classification, the Company applies judgement as to whether the benefits and risks of ownership of associated assets have been substantially transferred to the Company.

Further details on the accounting treatment of finance and operating leases are included in Note 2.

*iii) Functional currency of foreign operations*

The Company has foreign subsidiaries and therefore needs to determine the functional currency to be used for the translation of their operations. Management used its judgement to determine the functional currency that most faithfully represents the economic effects of the underlying transactions, events and conditions of the Company's foreign operations. As part of this approach, management gives priority to the primary indicators and also considers additional factors, which are designed to provide additional supporting evidence to determine a subsidiary's functional currency.

**5. Trade and other receivables**

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Trades receivable	45,750	57,527	49,559
Grants receivable	9,761	6,794	168
Sales taxes receivable	7,125	2,725	3,078
Tax credits receivable	84		
Others	574	1,378	619
	<b>63,294</b>	68,424	53,424

All trades receivable and other receivables disclosed above are pledged as security for the credit facilities.



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**6. Inventories**

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Wastepaper	8,385	10,241	7,802
Wood fibre	6,730	7,698	8,302
Pulp	58,243	34,501	36,987
Production and maintenance supplies, and other raw materials	26,510	24,747	25,164
	<b>99,868</b>	77,187	78,255

Inventories are pledged as security for the credit facilities.

In addition, inventory expense and depreciation were recognized in cost of products sold during the following years:

	2011	2010
	\$	\$
Raw materials and consumables used	363,425	339,046
Parts, energy, labour costs and other costs	94,424	90,575
Change in pulp inventory	(26,038)	2,229
Write-downs of pulp inventory to net realizable value	4,566	
Reversal of previous inventories write-down		(76)
Depreciation	35,871	34,485
Total	<b>472,248</b>	466,259

**7. Property, plant and equipment**

	December 31, 2011	Carrying amounts December 31, 2010	January 1, 2010
	\$	\$	\$
Land	4,937	5,006	4,912
Buildings and related components	24,931	32,763	34,472
Warehouse under finance lease	334	1,802	2,182
Equipment, roads, lots and other	262,018	329,422	357,859
Construction in progress	8,228	7,028	3,335

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Major maintenance	7,105	6,588	4,682
	<b>307,553</b>	382,609	407,442

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**7. Property, plant and equipment (continued)**

Property, plant and equipment are pledged as security for the credit facilities.

	Land \$	Buildings and related components \$	Warehouse under finance lease \$	Cost Equipment, roads, lots and other \$	Construction in progress \$	Major maintenance \$	Total \$
January 1, 2010	6,058	58,401	4,924	718,936	3,335	7,864	799,518
Additions	142	402		3,724	3,833	6,594	14,695
Disposals		(6)		(643)		(4,332)	(4,981)
Adjustments		(21)		(410) <sup>(2)</sup>	(56)		(487)
Effect of foreign currency translation	(51)	(1,170)	(264)	(7,780)	(84)		(9,349)
December 31, 2010	6,149	57,606	4,660	713,827	7,028	10,126	799,396
Additions	58	1,864		12,098	1,195	6,652	21,867
Disposals		(69)		(785)		(3,532)	(4,386)
Effect of foreign currency translation	25	494	105	3,209	5		3,838
<b>December 31, 2011</b>	<b>6,232</b>	<b>59,895</b>	<b>4,765</b>	<b>728,349</b>	<b>8,228</b>	<b>13,246</b>	<b>820,715</b>

	Land \$	Buildings and related components \$	Warehouse under finance lease \$	Equipment, roads, lots and other \$	Major maintenance \$	Total \$
January 1, 2010 <sup>(1)</sup>	1,146	23,929	2,742	361,077	3,182	392,076
Depreciation expense		1,509	272	27,946	4,688	34,415
Elimination on disposals of assets		(1)		(555)	(4,332)	(4,888)
Adjustments		(1)		(157) <sup>(2)</sup>		(158)
Effect of foreign currency translation	(3)	(593)	(156)	(3,906)		(4,658)
December 31, 2010	1,143	24,843	2,858	384,405	3,538	416,787
Depreciation expense		1,488	260	27,957	6,122	35,827
Impairment losses recognized in profit or loss	150	8,441	1,249	53,145		62,985
Elimination on disposals of assets		(11)		(422)	(3,519)	(3,952)
Adjustments				(107) <sup>(2)</sup>		(107)
Effect of foreign currency translation	2	203	64	1,353		1,622

<b>December 31, 2011</b>	<b>1,295</b>	<b>34,964</b>	<b>4,431</b>	<b>466,331</b>	<b>6,141</b>	<b>513,162</b>
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- (1) Includes \$136,964 of impairment applied on all assets categories, including land, recognized at Transition Date (Note 26).
- (2) These adjustments include those resulting from the revision of the estimated cash flows relating to the landfill closure liability (Note 9).

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**7. Property, plant and equipment (continued)***Impairment charge*

At each financial position reporting date, the Company determine whether there is any indication that its assets are impaired. The unsolicited Insider Bid from Abitibi filed on December 15, 2011, as detailed in Note 27, was identified as an indication for the Company to perform an impairment test. Consequently, the Company has reviewed its assumptions to estimate future cash flows for both cash generating units ( CGU ), the NBSK and RBK segments. As a result of these tests, an impairment loss of \$62,985 included in the consolidated statement of earnings and an effect of foreign currency translation of \$418 included in other comprehensive income was recognized on property, plant and equipment of the RBK segment.

The estimation of the recoverable amount was based on assumptions regarding the future development of several factors, including pulp prices, sales volumes, input prices (woodchips, wastepaper, energy, chemicals, etc.), capital expenditures and currency rates. The value in use was calculated through discounting the expected cash flows using a weighted average cost of capital ( WAAC ) appropriate for the CGUs . The WACC is essentially composed of an estimated return on equity and market interest rates on debt for similar companies adjusted for a risk relevant to the Company. When calculating value in use at the end of 2011, the discount rate was 12.0% for both CGUs .

**8. Intangible assets***Application software*

	Cost	Accumulated amortization	Total
	\$	\$	\$
January 1, 2010	1,107	798	309
Additions		70	(70)
Disposals			
Effect of foreign currency translation	(30)	(30)	
December 31, 2010	1,077	838	239
Additions		44	(44)
Disposals	(80)	(80)	
Effect of foreign currency translation	10	9	1
<b>December 31, 2011</b>	<b>1,007</b>	<b>811</b>	<b>196</b>

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**9. Landfill closure liability**

The following table presents the carrying amount of the obligations associated with the closure and post-closure activities over the operating life of the landfill:

	2011	2010
	\$	\$
Balance, beginning of year	1,891	3,611
Liability incurred	(42)	(59)
Accretion and effect of change in discount rate	477	437
Changes in estimates		(1,958)
Foreign currency translation	55	(140)
Balance, end of year	2,381	1,891
Current portion (2011 US\$123; 2010 US\$161)	125	160
Long-term portion (2011 US\$2,218; 2010 US\$1,741)	2,256	1,731
	2,381	1,891

The total undiscounted amount of estimated cash flows required to settle the obligations is \$3,415 US\$3,358 (\$3,252 US\$3,270 and \$6,528 US\$6,211 as at December 31 and January 1, 2010, respectively), which has been discounted using a risk free rate of 2.5% (3.9% and 4.4% as at December 31 and January 1, 2010, respectively). The majority of these obligations is expected to be settled over the next 32 years, and will be funded using cash flows from operations at the time of retirement. In 2010, the Company revised the estimated cash flows required to settle the obligations resulting in a reduction of the liability; the offset was applied against property, plant and equipment (Note 7) and the remaining amount was recorded in earnings.

Anticipated undiscounted cash flows required to settle the obligations are estimated as at December 31, 2011, as follows:

	\$
Within one year	125
Between one and five years	667
Later than five years	2,623

As at December 31, 2011, the Company held restricted cash in the amount of \$110 US\$108 (2010: \$106 US\$106) to provide for payment of the costs of landfill closure monitoring and maintenance or response activities of the landfill to protect health, safety, and the environment. In addition, as at December 31, 2011, the Company had outstanding letters of credit in the aggregate amount of \$386 US\$380 (2010: \$378 US\$380) and a deposit of \$99 US\$98 (2010: \$97 US\$98) to secure a portion of such activities related to closure of the landfill pursuant to a requirement by the Department of Environmental Quality of Michigan.

**10. Employee benefits**

The Company maintains contributory defined benefit pension plans covering certain groups of employees. The Company also maintains non-funded, non-contributory supplementary defined benefit pension plans for one of its executives and a former executive. Pursuant to the terms of employment with this executive, the Company has an obligation to ensure that his plan is secured, which is currently achieved through a letter of

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**10. Employee benefits (continued)**

credit. These plans provide pensions based on length of service and average employee earnings. The Company provides other benefit plans consisting of group health care and life insurance benefits to eligible retired employees and their dependents. These post-employment plans are unfunded.

The Company's funding policy is to contribute annually the amount required to provide for benefits earned in the year and to fund past service obligations over periods not exceeding those permitted by the applicable regulatory authorities. In 2012, the Company expects to contribute approximately \$6,250 to all its plans in accordance with normal funding policy. Past service obligations arise from improvements to plan benefits. They are recognized immediately in the benefit expense in the period that they occur, to the extent they are vested.

The Company measures its accrued benefit obligation and the fair value of plan assets for accounting purposes as at December 31 of each year. Actuarial valuations for funding purposes are conducted on an annual basis.

Beginning January 1, 2010, all Canadian non-unionized employees have stopped accruing defined benefits under the defined pension plan and started participating in a new defined contribution plan.

The following table presents the difference between the fair value of the defined benefit pension assets and the actuarially determined accrued benefit obligation as at December 31, 2011, December 31, 2010 and January 1, 2010. These differences are also referred to as either the deficit or surplus, as the case may be, or the funded status of the plans.

	December 31, 2011		December 31, 2010		January 1, 2010	
	Pension plans \$	Other post-employment benefits \$	Pension plans \$	Other post-employment benefits \$	Pension plans \$	Other post-employment benefits \$
Present value of funded benefit obligations	127,699	2,990	119,395	2,778	111,985	2,766
Fair value of plan assets	93,988		94,692		90,746	
	(33,711)	(2,990)	(24,703)	(2,778)	(21,239)	(2,766)
Present value of unfunded benefit obligations	1,306		881		555	
<b>Plan deficit</b>	<b>(35,017)</b>	<b>(2,990)</b>	<b>(25,584)</b>	<b>(2,778)</b>	<b>(21,794)</b>	<b>(2,766)</b>
Experience adjustments on plan liabilities	(6,712)	(142)	(7,136)	80		
Experience adjustments on plan assets	(5,762)		2,059			

The Company has elected to recognize future gains (losses) in other comprehensive income and, as such, the obligation reported on the Company's statement of financial position is equal to the status of the plans (since there are no unvested past service costs) and the benefit expense is not affected by those gains (losses).



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**10. Employee benefits (continued)**

	2011		2010	
	Pension plans \$	Other post-employment benefits \$	Pension plans \$	Other post-employment benefits \$
<b>Present value of defined benefit obligation:</b>				
Defined benefit obligation, beginning of year	120,276	2,778	112,540	2,766
Employer's current service cost	1,217	61	1,217	61
Interest cost	6,543	152	6,632	165
Benefits paid	(6,647)	(143)	(8,230)	(134)
Plan participants' contributions	904		981	
Actuarial loss (gain)	6,712	142	7,136	(80)
Defined benefit obligation, end of year	129,005	2,990	120,276	2,778
<b>Fair value of plan assets:</b>				
Fair value of plan assets, beginning of year	94,692		90,746	
Expected return on plan assets	6,348		5,958	
Actuarial (loss) gain	(5,762)		2,059	
Employer's contributions	4,453	143	3,178	134
Plan participants' contributions	904		981	
Benefits paid	(6,647)	(143)	(8,230)	(134)
Fair value of plan assets, end of year	93,988		94,692	

The actual return on plan asset was \$586 and \$8,017 for the years ended December 31, 2011 and 2010, respectively.

The assets of the pension plans are held by an independent trustee and are accounted for separately in the Company's pension funds. The expected rate of return on assets is based on the expected rate of return on each asset classes using a stochastic projection tool that generates multiple expected-return scenarios over long periods of time for different asset classes. Expected fees payable by the plan are deducted from this expected rate of return. As at December 31, 2011 and 2010, the assets do not include the Company's own financial instruments or any property occupied by, or other assets used by, the Company.

	2011 Fair Value of Plan assets %	2010 Fair Value of Plan assets %
Cash and short-term investments		0.9

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Bond	44.1	41.5
Canadian, U.S. and foreign equities	55.9	57.6
	100.0	100.0

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**10. Employee benefits (continued)**

Amounts recognized in profit or loss in respect of these defined benefit plans are as follows:

	2011		2010	
	Pension plans	Other post-employment benefits	Pension plans	Other post-employment benefits
	\$	\$	\$	\$
Employer's current service cost	1,217	61	1,217	61
Interest cost	6,543	152	6,632	165
Expected return on plan assets	(6,348)		(5,958)	
<b>Total benefit expense</b>	<b>1,412</b>	<b>213</b>	<b>1,891</b>	<b>226</b>

Actuarial losses and gains recognized in other comprehensive income are reconciled as follows:

	2011		2010	
	Pension plans	Other post-employment benefits	Pension plans	Other post-employment benefits
	\$	\$	\$	\$
<b>Other comprehensive income:</b>				
Balance of actuarial (losses) gains recognized in other comprehensive income, beginning of year	(5,077)	80		
Actuarial (loss) gain recognized in the year before tax	(12,474)	(142)	(5,077)	80
<b>Balance of actuarial (losses) gains recognized in other comprehensive income, end of year</b>	<b>(17,551)</b>	<b>(62)</b>	<b>(5,077)</b>	<b>80</b>

The principal assumptions used for the purposes of the actuarial valuations were as follows:

<i>Pension plans</i>	2011	2010
	%	%
Discount rate	5.0	5.5
Expected long-term return on assets	6.75	6.75

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Rate of compensation increase	<b>2.75</b>	2.75
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*Other post-employment benefits*

	<b>2011</b>	<b>2010</b>
	<i>%</i>	<i>%</i>
Discount rate	<b>5.0</b>	5.5
Rate of compensation increase	<b>2.75</b>	2.75
<b>Assumed health care cost trend rate at end of year:</b>		
Initial health care cost trend	<b>7.0</b>	7.0
Annual rate of decline in trend rate	<b>0.25</b>	0.25
Ultimate health care cost trend rate	<b>3</b>	3

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**10. Employee benefits (continued)**

In determining the long-term rate of return on assets assumption, the Company considers the weighted average of historical returns, input from investment advisors and its actuary's simulation model of expected long-term rates of return on assets assuming the Company's targeted investment portfolio mix as outlined above.

A variation of 100 point basis in the health care cost trend rate would result as follows:

	2011 \$	2010 \$
Effect of change in health care cost trend rate	<b>increase</b>	increase
Total of service cost and interest cost	<b>4</b>	4
Accrued benefit obligation	<b>31</b>	28
Effect of change in health care cost trend rate	<b>decrease</b>	decrease
Total of service cost and interest cost	<b>(3)</b>	(3)
Accrued benefit obligation	<b>(33)</b>	(32)

The Company also maintains defined contribution 401(K) plans for all US employees and a defined contribution plan for all Canadian non-unionized employees. In addition, the Company maintains a non-funded, non-contributory supplementary defined contribution pension plan for executives, for which a deficit of \$152 was included in the financial position as at December 31, 2011 (\$27 as at December, 2010). All the defined contribution plans are expensed as incurred and the total expense recognized in profit or loss relating to the defined contribution plans amounted to \$1,058 and \$932 for 2011 and 2010, respectively.

**11. Long-term debt**

	December 31, 2011 \$	December 31, 2010 \$	January 1, 2010 \$
Term Loan	<b>76,898</b>	77,648	
Previous Term Facility (US\$106,812)			112,259
ABL Credit Facility denominated in Canadian dollars	<b>17,500</b>		
ABL Credit Facility denominated in US dollars (US\$17,000)	<b>17,289</b>		
Previous Revolving Credit Facility denominated in Canadian dollars			19,381
Previous Revolving Credit Facility denominated in US dollars (US\$15,000)			15,765
Obligation under finance lease at a rate of 14.9%	<b>3,697</b>	3,917	4,400
PSIF Investissement Québec	<b>4,076</b>	5,324	4,321
Deferred financing fees	<b>(1,791)</b>	(2,215)	(668)

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	<b>117,669</b>	84,674	155,458
Less: current portion of long-term debt	<b>2,016</b>	1,876	36,682
	<b>115,653</b>	82,798	118,776

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**11. Long-term debt (continued)**

*Refinancing*

On July 16, 2010, the Company completed its refinancing transactions (the Refinancing Transactions ) comprised of:

a term loan for an amount of \$78 million (the Term Loan );

a \$75 million asset-based secured revolving credit facility (the ABL Credit Facility ); and

a \$40 million (gross proceeds) rights offering (the Rights Offering ).

As a result of the Refinancing Transactions, the Company repaid its previous revolving credit facility scheduled to mature on October 30, 2010 and its previous term loan scheduled to mature on October 30, 2012. Therefore, the repayment of the previous credit facilities was accounted as an extinguishment of the credit facilities.

*Term Loan*

The Term Loan provides for a five-year secured term loan in a principal amount of \$78 million, bearing interest at a rate of 8.25% and to be repaid in quarterly instalments at a rate of approximately 1% per annum of the original principal amount thereof, with the balance due and payable at maturity on July 15, 2015. All obligations in respect of the Term Loan are secured by a first-ranking hypothec on all present and future assets, movable and immovable, of the Company and its subsidiaries and a second ranking hypothec on all of the existing and subsequently acquired accounts receivable, inventory and assets relating to the Company and its subsidiaries, with exception of the assets securing the ABL Credit Facility. The Term Loan contains certain covenants and events of default customary to borrowings of this nature, including a requirement for the Company to maintain at all times certain minimum levels of wood fibre and wastepaper supply under contract.

The Term Loan also requires the Company to maintain certain customary financial ratios, namely an interest coverage ratio of not less than 2.0x at all times and a total debt (including Debentures) to capitalization ratio of not more than 40% until December 31, 2011, 37.5% in 2012 and 35% thereafter.

As at December 31, 2011 and 2010, the Company was in compliance with all terms and conditions of the Term Loan.

*ABL Credit Facility*

The ABL Credit Facility provides for borrowings of up to \$75 million and had an initial term of three years ending July 16, 2013. On August 3, 2011, as provided under the ABL Credit Facility, the term was extended for an additional year, bringing the maturity to July 16, 2014. The amount available to be drawn under the ABL Credit Facility will vary from time to time, based upon the Company's trade receivables and inventory levels, and can be drawn in Canadian or in US dollars. The obligations under the ABL Credit Facility are secured by, among other things, a first-ranking hypothec on all of the existing and after acquired trade and other receivables and inventories of the Company and its subsidiaries and a second-ranking hypothec on all present and future assets, movable and immovable, of the Company and its subsidiaries, with

exception of the assets securing the Term Loan. The ABL Credit Facility contains certain covenants and events of default

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#### **11. Long-term debt (continued)**

##### *ABL Credit Facility (continued)*

customary to borrowings of this nature. The ABL Credit Facility also provides for certain springing financial covenants depending on the net amount available to draw. Should these covenants be triggered, the ABL Credit Facility would require the Company to maintain a fixed charge coverage ratio of not less than 1.2x and put some limitations on capital expenditures.

At the Company's option, all Canadian dollar denominated loans under the ABL Credit Facility bear interest at a rate based either on a Canadian Prime Rate or the applicable bankers' acceptance rate, plus a margin in each case. All US dollar denominated loans under the ABL Credit Facility bear interest at a rate based either on LIBOR or the US Base Rate, plus a margin in each case.

As at December 31, 2011 and 2010, the Company was in compliance with all terms and conditions of the ABL Credit Facility.

##### *Previous credit facilities*

The previous credit facilities were established on October 31, 2006 and consisted of the following: (i) a six-year, US\$178,760 senior secured term facility (or the Canadian equivalent) and (ii) a four-year, \$55,000 senior secured revolving credit facility subject to a borrowing base calculation. The term facility was amortized at a rate of 1% per annum of the original amount of the term facility in quarterly instalments.

As at January 1st, 2010, an amount of \$112,259 US\$106,812 was drawn under the term facility bearing interest at LIBOR (base rate floor of 2%) plus a margin of 6%.

##### *PSIF Investissement Québec*

On February 23, 2007, the Company obtained a \$6,000 interest-free loan granted by Investissement Québec through the Soutien à l'industrie forestière program (PSIF) to support investments made in the forest industry. On April 22, 2009, Investissement Québec modified the agreement to be payable in monthly instalments over a maximum of four years starting December 31, 2010, whereas previously the instalments were due over five years starting November 27, 2009.

The drawings under the loan were recognized at their discounted value which was computed at a weighted average interest rate of 6% (2010 6%). The differences between the discounted values and the principal amounts at initial recognition were recorded against property, plant and equipment since they were considered as grants from the government. Theoretical interest is being expensed over the term of the loan using the effective interest rate method. As at December 31, 2011, the outstanding principal amounts were \$4,375 (2010 \$5,875). Under the loan agreement, the Company must comply with certain restrictive covenants, including the requirement to meet certain financial ratios. As at December 31, 2011 and 2010, the Company was in compliance with all terms and conditions of the PSIF loan.

##### *Obligation under finance lease*

The Company leases a warehouse under finance lease which can be renewed for 20 years at the Company's option. Minimal payments are determined by an escalatory price clause.



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**11. Long-term debt (continued)***Deferred financing fees*

Deferred financing fees of \$1,315 (2010 \$1,716) are not netted against the related financial liabilities as the ABL Credit facilities are not used on a permanent basis by the Company.

*Future payments*

Future principal repayments and minimum finance lease payments as at December 31, 2011, are as follows:

	Long-term debt \$	Deferred financing fees \$	Finance lease \$
Within one year	2,250	(440)	902
Between one and five years	113,812	(1,351)	3,771
Later than five years			985
Total principal repayments, interest capitalized repayments and future minimum lease payments	116,062	(1,791)	5,658
Less: Theoretical interest on PSIF	(299)		
Imputed interest			(1,961)
	115,763	(1,791)	3,697

**12. Convertible unsecured subordinated debentures**

On September 7, 2006, the Company issued convertible extendible unsecured subordinated debentures (the Debentures) for a principal amount of \$51,750 (including the over-allotment option). The Debentures, which bore interest at 7% payable semi-annually and matured on December 31, 2011, were completely redeemed on June 28, 2011.

Under certain conditions, Debentures may have been converted into shares at the holder's option. Furthermore, the Debentures were redeemable at the Company's option. The Company may, at its option and subject to certain conditions, have elected to satisfy the redemption price of the Debentures by issuing Company shares.

Financing fees of \$2,838 were incurred in conjunction with the issuance of Debentures of which \$2,480 were deferred and were being amortized over the term of the Debentures, using the effective interest rate method. The initial liability portion of the Debentures was being accreted such that the liability at maturity would have equalled the face value of the then outstanding Debentures. On the Transition Date and until the effective date of the Arrangement (Note 1), the conversion option was recognized as a financial liability and measured at fair value through profit or loss. Further details are included in Note 26.

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For the year ended December 31, 2011, the Company redeemed Debentures in an aggregate amount of \$51,749. Redemption was made in two stages, namely on February 28 and June 28, 2011. On the redemption dates, the Company paid to the holders of redeemed Debentures a redemption price equal to the

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**12. Convertible unsecured subordinated debentures (continued)**

principal amount of the Debentures, plus accrued and unpaid interest up to the date prior to the redemption date. Redemption prices on February 28 and June 28, 2011 were respectively of \$1,011.12 and 1,034.14 per \$1,000.00 principal amount of Debentures. As a result of these redemptions, a total gain on redemption of \$2,752 was recognized in the consolidated statement of earnings for the year ended December 31, 2011 (Note 20).

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Initial amortized amount		45,149	45,149
Accretion		5,042	3,651
Deferred financing costs		(582)	(1,104)
		49,609	47,696
Current portion		49,609	
			47,696

**13. Shareholders capital/Unitholders capital***Authorized and issued common shares*

An unlimited number of common shares are issuable. Each share is freely transferable and represents a shareholder's proportionate undivided interest in the Company. Each share confers to its holder the right to one vote at any meeting of shareholders and to participate equally and ratably in any dividends of the Company, if any, and, in the event of any required distribution of all of the property of the Company, in the net assets of the Company remaining after satisfaction of all liabilities. Shares have no conversion or pre-emptive right.

*Fund units*

An unlimited number of units were issuable pursuant to the trust agreement. Each unit was freely transferable and represented a unitholder's proportionate undivided interest in the Fund. Each unit conferred to its holder the right to one vote at any meeting of unitholders and to participate equally and ratably in any distributions of the Fund, if any, and, in the event of any required distribution of all of the property of the Fund, in the net assets of the Fund remaining after satisfaction of all liabilities. Units had no conversion or pre-emptive right.

*Shares/Units issued and outstanding*

\$000,000,000      \$000,000,000      \$000,000,000

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	2011		
	Number of	Amount	
	units	shares	\$
Balance, January 1 and December 31, 2011		<b>130,075,556</b>	<b>696,537</b>

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**13. Shareholders capital/Unitholders capital (continued)***Shares/Units issued and outstanding (continued)*

	\$000,000,000	\$000,000,000 2010	\$000,000,000
	units	Number of shares	Amount
			\$
Balance, January 1, 2010	90,472,708		658,609
Conversion of units into shares (Note 1)	(90,472,708)	90,472,708	
Issuance of shares		39,602,848	37,928
<b>Balance, December 31, 2010</b>		<b>130,075,556</b>	<b>696,537</b>

On May 25, 2010, all the outstanding units of the Fund were exchanged for common shares of the Company on a one-for-one basis.

*Rights Offering*

On July 16, 2010, the Company issued an aggregate of 39,602,848 common shares of the Company pursuant to a rights offering at a price of \$1.01 per common share for net proceeds of \$37,928 after deducting standby fees of \$400 and expenses of \$1,671.

*Per share/unit information*

The following tables reconcile the net earnings to net earnings adjusted for dilutive effect and the weighted average number of shares outstanding used in computing basic earnings per share to weighted average number of shares outstanding used in computing diluted earnings per share:

	<b>2011</b>	2010
	<b>\$</b>	<b>\$</b>
Net earnings	<b>(64,031)</b>	16,594
Impact of assumed conversion of Debentures		5,535
<b>Net earnings adjusted for dilutive effect</b>	<b>(64,031)</b>	22,129
	<b>2011</b>	2010
Average number of shares outstanding used in computing basic earnings per share	<b>130,075,556</b>	108,809,369

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Dilutive effect of Debentures*		70,743,677
Dilutive effect of rights offering		3,038,027
Average number of shares outstanding used in computing diluted earnings per share	<b>130,075,556</b>	182,591,073

\* Assuming a conversion price of \$0.77 for the year ended December 31, 2010 (being the trading price of the shares at the beginning of the year).

For the year ended December 31, 2011, the share option plan and the potential conversion of the Debentures were anti-dilutive. For the diluted earnings per share computation purpose, the number of 16,970,633 shares

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**13. Shareholders capital/Unitholders capital (continued)***Per share/unit information (continued)*

was excluded from the denominator and the amount of \$1,875 was excluded from the numerator. For the year ended December 31, 2010, 1,746,538 antidilutive share options were excluded from the computation of diluted earnings per share.

**14. Income taxes**

Immediately prior to converting into a corporation on May 25, 2010, the Company, as a publicly traded income trust, was to be taxed on income earned starting in 2011, similarly to rules applying to corporations. Accordingly, deferred income tax assets and liabilities of the Company on Canadian operations were determined with respect to estimated temporary differences between the carrying values of existing assets and liabilities and their respective tax bases that were expected to reverse starting in 2011 at the then combined enacted or substantively enacted tax rate. The Company was not subject to, and did not recognize, any deferred income tax assets or liabilities on temporary differences expected to reverse prior to 2011.

Effective May 25, 2010, upon conversion into a corporate structure, the income of the Company became subject to income taxes applicable to corporations.

The components of tax expense (recovery) are as follows:

	2011	2010
	\$	\$
Current tax expense (recovery):		
Current tax expense (recovery) in respect of the current year	14	(5)
Adjustment recognized in the current year in relation to the current tax of prior years	(81)	
<b>Total income tax recovery recognized in the current year</b>	<b>(67)</b>	<b>(5)</b>

A reconciliation of income taxes at the combined Canadian statutory income tax rate with reported income taxes is as follows:

	2011	2010
	\$	\$
(Loss) earnings before income taxes	(64,098)	16,589
Combined Canadian statutory income tax rate	28.40%	29.90%
	<b>(18,204)</b>	4,960

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Computed income tax (recovery) expense at combined Canadian statutory income tax rate		
Variance resulting from:		
(Utilization of) unrecognized tax attributes, net of permanent differences	27,553	(4,423)
Effect of difference between combined Canadian statutory income tax rate and those rates applicable to foreign subsidiaries	(9,335)	(542)
	14	(5)
Adjustment recognized in the current year in relation to the current tax of prior years	(81)	
Income tax recovery recognized in the current year	(67)	(5)

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**14. Income taxes (continued)**

The combined Canadian statutory income tax rate has decreased by 1.5% resulting from the reduction of the Canadian federal statutory tax rate.

	2011	2010
	\$	\$
Deferred tax (liabilities)/assets in relation to :		
Non-capital and capital losses carryforward		5,764
Property, plant and equipment	(4,102)	(9,359)
Trade and other receivables		16
Inventories		890
Deferred financing fees		902
Landfill closure liability		750
Trade and other payables		329
Employee benefits	4,102	
Other		708

**Net deferred tax asset/(liability)**

All variations in the deferred tax assets and liabilities have been recognized in the consolidated statement of earnings for the years ended December 31, 2011 and 2010.

As at December 31, 2011, the Company has not recognized deferred income tax assets with respect to Canadian operating losses of \$73,324 expiring from 2026 to 2031, foreign operating losses of \$95,014 US\$93,426 which expire from 2026 to 2031, Canadian capital losses of \$751 which can be utilized indefinitely, and deductible temporary differences of \$355,028.

*Tax reassessment*

In January 2009, the Company received notices of assessment for the 2002 and 2003 taxation years from the Canada Revenue Agency ( CRA ) and the Ministère du Revenu du Québec ( MRQ ) reassessing the tax value allocated to the assets of the Saint-Félicien Mill at the time such assets were purchased by the Company from Abitibi-Consolidated Inc. in August 2002. These assessments do not involve any taxes payable. In October 2009, the Company requested statements of revised losses from CRA and MRQ. In September 2010, the Company received from the CRA a statement of revised losses. In December 2010, the Company filed a notice of objection. The CRA has acknowledged receipt of Fibrek s notice of objection. An introductory meeting between Fibrek representatives and CRA took place in October 2011.

On February 21, 2012 CRA presented a verbal proposition to the Company. Management expects a settlement in the first quarter of 2012. The amount of the tax attributes not recognized in the deferred income tax assets detailed above was adjusted based on that proposition.

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**15. Share-based payment**

Liabilities recorded for share-based payment plans included in trade and other payables are as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Long-term incentive plan	359	285	101
Share option plan	50	41	
	<b>409</b>	326	101

Contributed surplus recorded for share-based payment plans are as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Employee benefits reserve	1,006	277	

Compensation expense recognized for share-based payment plans are as follows:

	00000 2011	00000 2010
	\$	\$
Long-term incentive plan	74	184
Share option plan	738	318
	<b>812</b>	502

*i) Long-term incentive plan*

Effective January 1, 2006, the Company implemented a Performance Share Plan under which Performance Shares ( PS ) were awarded by the Board of Directors to certain key executives. The PS were awarded as of January 1<sup>st</sup> of each year based on an incentive amount determined by the Board. To determine the awarded amount of PS, the incentive amount was divided by the average trading price of the Company's shares for the 20 trading days immediately preceding the day on which the award was made. The PS vested after three years and were payable in cash once the Board had determined the achievement of the specified performance targets. The amount of cash to be received by the participants was determined by multiplying the number of vested PS by the value of the Company's shares as at the end of the performance cycle (three years), based on the average trading price of the Company's shares for the 20 trading days immediately preceding the vesting date. The participants were also entitled to an amount equivalent to the dividends declared on the Company's shares during the vesting period for all the PS that vested. PS that had not achieved the vesting condition were automatically cancelled.

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As at December 31, 2011, an amount of \$359 was payable in accordance with a modification to the plan approved by the Board only for the cycle starting in 2009. This amount represents 20% of the PS awarded on January 1, 2009 for which the executive member is still in his position, even if the performance targets were not achieved. Those PS vested on December 31, 2011.

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**15. Share-based payment (continued)***i) Long-term incentive plan (continued)*

In addition, if a change of control occurs within six months from December 31, 2011, the payout for the PS which have vested on December 31, 2011 will be recalculated pursuant to the formula set above using the price paid by the Offeror for the Common Shares if this price is higher than the market price of the Common Shares on the vesting date.

The table below summarizes the changes in the number of outstanding PS:

	2011	2010
Balance, beginning of year	1,693,750	1,943,517
Cancelled		(195,745)
Exercised	(1,693,750)	
Expired*		(54,022)
Balance, end of year		1,693,750

\*: No incentive was paid as targets were not met.

As a result of the implementation of the share option plan on May 19, 2010, no additional PS were awarded and the plan terminated at the end of the 2009-2011 cycle.

*ii) Share option plan*

Effective May 19, 2010, the Company implemented a share option plan under which options may be awarded by the Board of Directors to executives and key employees. The options normally vest over a four-year period, one third of the options vesting on each anniversary of their date of award, commencing on the second anniversary. The options may also be subject to performance vesting conditions and the Board may accelerate the date upon which any option becomes exercisable. The option holders are entitled to exercise their vested options at a predetermined exercise price.

Effective on February 9, 2012, the Board authorized the Company to amend the terms of the unvested outstanding share options to provide that the vesting period be accelerated. This amendment would be effective solely for the purpose of tendering under the Mercer Offer (Note 27) all common shares issuable upon exercise of the outstanding in-the-money share options. The amendment would terminate upon expiry of the Mercer Offer. As at December 31, 2011, the Company had not exercised the Stock Option Plan acceleration amendment and none of the options outstanding were exercisable. As at December 31, 2010 none of the options outstanding were exercisable.

With the consent of the Board, the option holders are entitled to either (i) elect to exercise their options through a cashless exercise pursuant to which they would receive such number of common shares equal to their in-the-money value of the options, or (ii) elect to surrender their options in exchange for a cash payment equal to the in-the-money value of the options. Notwithstanding the manner in which the option holders elect to exercise their options, the number of common shares reserved for allotment pursuant to the share option plan, which include all regular and special awards, shall not exceed 4,523,635.



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**15. Share-based payment (continued)***ii) Share option plan (continued)*

The options which may be awarded under the share option plan shall not exceed ten years. The exercise price of any options awarded under the share option plan shall be the volume weighted average closing price of the common shares on the Toronto Stock Exchange ( TSX ) for the five trading day period following the black-out period relating to the filing of the Company's annual financial statements, provided that the exercise price shall not be less than the volume weighted average trading price per common share on the TSX over the five trading days preceding the day the option is awarded.

*a) Regular grants*

The table below summarizes the changes in the number of outstanding options under the regular grants:

	2011		2010	
	Number of options	Weighted average exercise price \$	Number of options	Weighted average exercise price \$
Outstanding, beginning of year	1,135,269	1.35		
Granted	939,814	1.56	1,135,269	1.35
Outstanding, end of year	2,075,083	1.45	1,135,269	1.35

The Company recognizes share-based payment cost based on the best available estimates of the performance condition, if any, using the Black-Scholes option pricing model. The effect of a change in estimate is recognized over the related vesting period.

For the year ended December 31, 2011, a share-based payment expense of \$574 was recorded in the consolidated statement of earnings in relation to this regular grant (2010 \$204). As at December 31, 2011, an amount of \$37 (2010 \$27) was included in trade and other payables.

*b) Special one-time grant*

On May 25, 2010, the Board awarded 1,086,009 options under the special one-time grant to executives having an exercise price of \$1.35 per common share and a term of six years from the date of award. The vesting of these options is subject to the achievement of the following minimum performance conditions:

50% of the options will vest on the third anniversary of the date of award, provided the Company's weighted average closing share price over the previous 20 trading days is \$3.50 per common share or greater, (the First Performance Criteria ), and;

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the other 50% of the share options will vest on the fifth anniversary of their date of award, provided the Company's weighted average closing share price over the previous 20 trading days is \$5.00 per common share or greater (the Second Performance Criteria). If the First Performance Criteria has not been met on the third anniversary of the date of award but the Second Performance Criteria is met, then the first 50% will also vest on the fifth anniversary of the award date.

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**15. Share-based payment (continued)***ii) Share option plan (continued)**b) Special one-time grant (continued)*

The Company recognizes share-based payment costs based on the best available estimates of the performance condition using the binomial option pricing model. The effect of a change in estimate is recognized over the related vesting period.

For the year ended December 31, 2011 share-based payment expense of \$164 was recorded in the consolidated statement of earnings in relation to this special one-time grant (2010 \$114). As at December 31, 2011, an amount of \$13 (2010 \$ 14) was included in trade and other payables.

The following assumptions were used to estimate the fair value, at the date of award, of each option issued to executives and key employees:

	<b>2011</b>		<b>2010</b>
	<b>Regular grant</b>	Regular grant	Special one-time grant
Share price on date of grant	\$ <b>1.55</b>	\$ 1.30	\$ 1.30
Risk-free interest rate	<b>2.57%</b>	2.18%	2.32%
Expected dividend yield	<b>NIL</b>	NIL	NIL
Expected life of options	<b>4.5 years</b>	4.5 years	5.0 years
Expected volatility	<b>76.07%</b>	69.42%	65.41%
Weighted average fair value of issued options	\$ <b>0.93</b>	\$ 0.72	\$ 0.57

Expected volatility is based on peer companies' historical share price volatility over the past 5 years.

*iii) Deferred share unit plan*

Effective December 9, 2010, the Company implemented a deferred share unit plan for directors of the Company. Under the plan, eligible directors have the right to elect, for the following fiscal year, to receive all or part of their fees and/or annual retainer in share units. The number of share units to be granted is based on the weighted average trading price of the common shares on the TSX for the five (5) business days immediately preceding a given date or in such manner as is required or allowed by the rules and policies of the TSX (the Market Price). A participant is entitled to receive, upon such participant's Termination of Board Service (as such expression is defined in the plan), the payment in cash of the share units that are credited to the participant's account on such given date based, for each vested share unit, on the value of a common share at the Market Price on the date of such participant's Termination of Board Service.

For the years ended December 31, 2011 and 2010, no director had elected to receive his/her annual retainer and/or fees for the following year in share units, election which can only be done once a year.



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**16. Supplemental disclosure of cash flow information**

Changes in non-cash operating working capital items:

	2011	2010
	\$	\$
Trade and other receivables	8,900	(9,648)
Inventories	(21,366)	(1,344)
Prepaid expenses	(10)	810
Trade and other payables	5,604	12,376
	<b>(6,872)</b>	2,194

Supplemental information:

	2011	2010
	\$	\$
Additions to property, plant and equipment included in trade and other payables	6,127	2,398

Cash and cash equivalents consist of:

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Cash	5,466	16,315	19,064
Restricted cash	110	106	110
	<b>5,576</b>	16,421	19,174

**17. Contractual obligations***Fibre supply agreement*

The Company is party to a three-year renewable fibre supply agreement with Abitibi Consolidated Company of Canada ( ACCC ) at market price, effective September 1, 2009.

*Waste paper supply agreements*

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The Menominee and Fairmont Mills have entered into supply agreements for waste paper which cover the majority of the mills' expected consumption mainly at market prices, terminating between one and three years.

### *Gas supply agreement*

The Menominee Mill was a party to a gas supply agreement, namely the Master Retail Gas Sales Agreement, pursuant to which it agreed to purchase approximately 100% of its expected consumption of gas, at market rates, through October 2010 which includes a fixed price for transportation.

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**17. Contractual obligations (continued)***Gas supply agreement (continued)*

In October 2010, the Company signed new three-year gas supply agreements for the Menominee Mill expiring in October 2013. Under these agreements, the Menominee Mill's contracted volumes are 2,167,174 decatherm and the purchase prices are at quoted market rates. If the mill's consumption is less than expected, it has the option to sell the excess quantity at the then prevailing quoted market rates.

Based on the terms of these agreements, as at December 31, 2011, the purchase commitment over the remaining term of the agreements which represents the fixed portion for transportation is as follows:

	\$
<b>2012</b>	<b>305</b>
<b>2013</b>	<b>248</b>

**18. Commitments**

The Company has commitments under various operating leases of mobile equipment, warehouses and office space and services. The operating lease contract related to office space rental contains a five-year renewal option. There is no contingent rent or purchase option in any of the operating leases. Future minimum lease payments are due as follows:

	\$
Within one year	<b>1,946</b>
Between one and five years	<b>2,377</b>
Later than five years	

As at December 31, 2011, the Company had commitments related to capital expenditures totaling approximately \$6,419 and letters of credit of \$3,877.

**19. Contingent liabilities and guarantees***Environmental matters*

The Company's operations are subject to numerous environmental laws, regulations and guidelines. It is the opinion of management that under existing legislation and regulatory practices, expenditures required for environmental compliance should not have a material adverse effect on the Company's financial position. However, future discovery of previously unknown environmental issues, including contamination of property underlying or in the vicinity of the Mills, could require the Company to incur material unforeseen expenses.

*Legal matters*

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The Company is subject to various claims and proceedings which have been instituted against it during the normal course of business. Management currently believes that the matters pending or asserted are not expected to have any material adverse effect on the financial position, results of operations or cash flows of the Company.

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**19. Contingent liabilities and guarantees (continued)**

*Indemnification of third parties*

In the normal course of business, the Company could enter into agreements which contain features meeting the definition of a constructive obligation as defined by IFRS. These are customary in the industry.

The Company has entered into agreements which provide for indemnification provisions for its directors, trustees and officers against expenses including legal fees, judgements, fines and any amount actually and reasonably incurred by them in connection with any action, suit or proceeding in which they are sued as a result of their service, subject to certain provisions. The Company purchases directors' and officers' liability insurance.

In connection with the Rights Offering, the Company entered into a dealer manager agreement and a standby purchase agreement, whereby the Company may have to indemnify the parties to these agreements with respect to the representations and warranties made.

Under the terms of the ABL Credit Facility, the Company agreed to indemnify, hold harmless and defend the lender, as agent for the lenders, from and against any and all losses, liabilities, claims, damages and expenses arising out of, in connection with or as a result of, among others, (i) the ABL Credit Facility and related loan documents, including the use of the proceeds and compliance with or enforcement by the lender of its rights thereunder, (ii) any contractual obligations entered into by the Company, (iii) the role of the lender in any actual or prospective investigation, litigation or other proceeding relating to the ABL Credit Facility, and (iv) the breach of any environmental legislation.

Under the terms of the Term Loan, the Company agreed to indemnify the lender for any costs resulting from (i) any change of law impacting the lender's costs or revenues with respect to the Term Loan, (ii) an event of default, and (iii) a breach of any applicable law, including any environmental legislation.

The Support Agreement entered into by Fibrek and Mercer contains, among other things, a termination fee of \$8,500 payable by Fibrek in certain circumstances, including the acceptance of an unsolicited superior proposal from a third party. Furthermore, unless such termination fee is paid and provided that Mercer has not materially breached any covenant or other obligation under the Support Agreement, Mercer shall be entitled to an expense reimbursement payment of \$2,000.

In connection with the Special Warrant Agreement entered into by Fibrek and Mercer, Fibrek may have to indemnify Mercer with respect to its representations and warranties made.

The nature of these guarantees prevents the Company from making reasonable estimates of the maximum potential amount it could be required to pay to counterparties, if any. Historically, the Company has never made any indemnification payments and as at December 31, 2011, the Company had not recorded a liability in respect of these indemnifications.

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**20. Financial instruments**

This section provides disclosures relating to the nature and extent of the Company's exposure to risk arising from financial instruments, including credit risk, liquidity risk, foreign currency risk and interest rate risk, and how the Company manages those risks.

*Credit risk*

Credit risk arises from cash and cash equivalents and restricted cash held with banks and financial institutions, and primarily from the Company's trade receivables. The maximum exposure to credit risk is equal to the carrying value of the financial assets.

	December 31, 2011	December 31, 2010	January 1, 2010
	\$	\$	\$
Cash and cash equivalents	5,576	16,421	19,174
Trade and other receivables	56,085	65,699	50,346
<b>Financial assets</b>	<b>61,661</b>	<b>82,120</b>	<b>69,520</b>

To mitigate this credit risk, the Company tries to maintain strict controls on receivables and is putting even greater emphasis on analyzing and reviewing the financial positions of its customers; rigorous evaluation procedures are generally applied to all new customers. A specific credit limit is generally established for each customer and reviewed periodically by the Company. The Company does not hold any collateral or other credit enhancements over these balances nor does it have a legal right of offset against any amounts owed by the Company to the counterparty.

Pursuant to their respective terms, trade receivables are aged as follows as at December 31, 2011 and 2010:

	2011	2010
	\$	\$
Not past due	37,410	48,934
Past due 1-30 days	8,556	9,213
Past due 31-60 days	268	
Past due more than 61 days	340	1,659
<b>Trade receivables</b>	<b>46,574</b>	<b>59,806</b>
Less: allowance for doubtful accounts	(824)	(2,279)
<b>Trade receivables, net</b>	<b>45,750</b>	<b>57,527</b>

Management considers that substantially all receivables should be fully collectible as most of the Company's customers are large corporations with good credit standing and no history of default. As at December 31, 2011, one customer (two as at December 31, 2010) represented more than 10% of the Company's total trade receivables. Allowance for doubtful accounts is based on management's assessment



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**20. Financial instruments (continued)***Credit risk (continued)*

of risk relating to past due trade receivables and information relating to industry. Movement in the allowance for doubtful accounts is presented as follows:

	2011	2010
	\$	\$
Balance, beginning of year	2,279	3,196
Amounts written off	(1,639)	
Impairment losses reversed		(775)
Effect of foreign exchange rate changes on allowance for doubtful accounts	184	(142)
Balance, end of year	824	2,279

No impairment loss for credit deterioration was recognized for the years ended December 31, 2011 and 2010.

*Liquidity risk*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company manages liquidity risk through the management of its capital structure and financial leverage, and by continuously monitoring forecasts and actual cash flows, as outlined in Note 21 to the consolidated financial statements ( Capital Disclosure ).

The Term Loan is made available at a fixed interest rate, however, the ABL Credit Facility is available at floating interest rates. In the event of an increase in the base reference interest rates or discount rates, the Company's financial expenses will increase.

The following are the contractual maturities of the financial liabilities, principal and interest (assuming current interest rates), at December 31, 2011 and 2010:

	2011				2017 and thereafter
	Total	2012	2013 - 2014	2015 - 2016	2017 and thereafter
	\$	\$	\$	\$	\$
Trade and other payables	66,488	66,488			
Current portion of landfill closure liability	125	125			
Term Loan	98,993	7,088	13,956	77,949	

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ABL Credit Facility	34,789		34,789		
PSIF Investissement Québec	4,375	1,500	2,875		
Obligation under finance lease	5,660	902	1,852	1,920	986
Total	210,430	76,103	53,472	79,868	986

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**20. Financial instruments (continued)***Liquidity risk (continued)*

		2010			2016 and thereafter
	Total	2011	2012 - 2013	2014 - 2015	
	\$	\$	\$	\$	\$
Trade and other payables	56,064	56,064			
Current portion of landfill closure liability	160	160			
Convertible unsecured subordinated debentures	55,372	55,372			
Term Facility	106,126	7,133	14,097	84,896	
PSIF Investissement Québec	5,875	1,500	3,000	1,375	
Obligation under finance lease	6,401	866	1,779	1,845	1,911
<b>Total</b>	<b>229,998</b>	<b>121,095</b>	<b>18,876</b>	<b>88,116</b>	<b>1,911</b>

Landfill closure liability represents contribution for the following year only. Other years are not presented as the amount could fluctuate significantly due to the variation of future performance and change in assumptions. ABL Credit Facility represents principal amounts only, since interests fluctuate significantly due to the variation of the outstanding balance on which they are calculated

*Foreign currency risk*

Exchange rate fluctuations between the Canadian dollar and its US counterpart have a significant impact on the Company's sales, as pulp prices are denominated in US dollars; these fluctuations also impact sales made in Canada which are dependent on the price of pulp in North America. The Company's operating results and cash flows may be adversely affected by changes in the Canadian dollar exchange rate with its US counterpart.

In accordance with its policy, the Company may use derivative financial instruments to protect itself against exchange rate fluctuations for specific minimal spot pulp sales. As at December 31, 2011 and 2010, the Company held no derivative financial instruments relating to foreign exchange. All foreign currency gains or losses, excluding those related to foreign operations which have been included in other comprehensive income, have been recorded in the consolidated statements of earnings for the years ended December 31, 2011 and 2010. Furthermore, as part of the objective in managing its foreign currency risk, the Company uses natural hedging positions by having US operations and a portion of its ABL Credit Facility denominated in US currency.

Assuming no change in commodity prices and interest rates, an increase of CAN\$0.01 of the Canadian dollar in relation to the US dollar for the years ended December 31, 2011 and 2010 would have had the following favourable impact on each of the financial instrument classes below (those for which the offsetting impact is recorded in earnings):

2011 2010

	\$	\$
Other financial instruments	157	247

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**20. Financial instruments(continued)***Foreign currency risk (continued)*

The Company would have had an equal but opposite effect for a decrease of CAN\$0.01 of the Canadian dollar in relation to the US dollar at December 31, 2011 and 2010. Financial instruments at FVTPL consist of an investment at FVTPL. Other financial instruments are cash and cash equivalents, trade and other receivables, trade and other payables, and the ABL Credit Facility.

*Interest rate risk*

The Company's interest rate risk is primarily related to the ABL Credit Facility and short-term investments. The ABL Credit Facility bears interest, at the Company's option, at bankers' acceptance rate or Canadian Prime Rate plus a margin in each case for Canadian borrowings and at LIBOR or the US Base Rate plus a margin in each case for US borrowings; short-term investments' rate is based on Canadian bankers' acceptance rate. Amounts outstanding under ABL Credit Facility, on which the Company is exposed to interest rate, are detailed in Note 11 to the consolidated financial statements ( Long-term debt ).

For the year ended December 31, 2011, a 100 basis points variation in interest rates, assuming all other variables are constant, would have resulted in a decrease/increase of \$131 (2010 \$28) in the Company's net earnings.

*Fair value**i) Establishing fair value*

The carrying amount of cash and cash equivalents, restricted cash, trade and other receivables, trade and other payables approximate their fair value due to their short-term maturity. Investment at FVTPL is carried at its fair value based on quoted market prices.

The fair values of other financial instruments are estimated as follows:

	<b>December 31, 2011</b>	December 31, 2010	January 1, 2010
	\$	\$	\$
Convertible unsecured subordinated debentures		51,852	39,588
Term Loan	<b>76,569</b>	77,302	
Term facility denominated in US dollars			88,958
ABL Credit Facility	<b>34,783</b>		
Revolving Credit Facility			27,278
PSIF Investissement Québec	<b>4,106</b>	5,465	4,270
	<b>115,458</b>	134,619	160,094

The fair value of the Debentures is estimated based on a valuation model established using quoted market inputs. The fair value of the Term Loan and the Term Facility are estimated using present value techniques based on market rates and are calculated considering the same terms

and conditions except for interest rates used for discounting purposes. The fair value of the PSIF -Investissement Québec loan is estimated using a present value technique based on market rates.

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**20. Financial instruments (continued)***Fair value (continued)**ii) Hierarchy of financial assets and liabilities measured at fair value*

Financial instruments recorded on the consolidated statement of financial position are classified using a fair value hierarchy that reflect the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);

Level 3 valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs)

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The following table presents the financial instruments recorded at fair value in the consolidated statements of financial position, classified using the fair value hierarchy described above:

	Level 1	2011 Level 2	Level 3
	\$	\$	\$
Investment at FVTPL	32		
Total	32		
	Level 1	2010 Level 2	Level 3
	\$	\$	\$
Investment at FVTPL	5,544		
Total	5,544		

During the year, there has been no significant transfer of amounts between Level 1 and Level 2.

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**20. Financial instruments (continued)***Fair value (continued)**iii) Other information*

	2011	2010
	\$	\$
<b>Financial expenses</b>		
Interest on long-term debt and Debentures	8,855	11,431
Amortization of interest capitalized on Term Facility and interest accretion on Debentures	513	2,898
Interest on PSIF Investissement Québec	252	275
Amortization of deferred financing fees	1,203	1,396
Loss on extinguishment of credit facilities		678
Other financial expenses	557	658
	<b>11,380</b>	17,336
<b>(Gain) loss on financial instruments</b>		
Gain on financial instrument (Note 24)	(740)	
Gain on redemption of debentures (Note 12)	(2,752)	
Loss on Debenture derivative		3,329
Master Retail Gas Sales Agreement		(113)
	<b>(3,492)</b>	3,216
<b>(Gain) loss on foreign currency translation</b>		
Cash and cash equivalents denominated in foreign currency	(101)	1,153
Loans and receivables	(1,669)	2,531
Other	240	(303)
	<b>(1,530)</b>	3,381

**21. Capital disclosure**

The Company defines its capital as follows: shareholders' equity, long-term debt including the current portion and convertible unsecured subordinated debentures, net of cash and cash equivalents. The Company's objectives when managing capital are:

Ensure the Company will continue as a going concern and meet its financial obligations

Maintain cash and short-term borrowing availability sufficient to fund operations in a volatile market

Invest capital improvements in order to maintain and improve the Company's cost position

Preserve its financial flexibility in order to benefit from potential opportunities as they arise

The Company monitors capital considering several measures including liquidity and leverage. The Company manages the capital structure and makes adjustments in light of changes in economic conditions

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**21. Capital disclosure (continued)**

and the risk characteristics of the underlying assets. It is expected that fluctuations in working capital will be funded from cash on hand or the ABL Credit Facility.

The following table illustrates the financial ratios calculated as at December 31,

	2011	2010
	\$	\$
Long-term debt including current portion	<b>119,460</b>	86,889
Convertible unsecured subordinated debentures		50,191
Less: cash	<b>(5,466)</b>	(16,315)
Net debt	<b>113,994</b>	120,765
Shareholders' equity	<b>257,095</b>	335,273
Net debt to equity, calculated according to the Company's capital management objective	<b>0.44</b>	0.36
Debt to total capitalization, calculated according to financial covenants under the Term Loan	<b>0.23</b>	0.15

The Company is subject to financial covenants under its Term Loan, ABL Credit Facility, and its PSIF Investissement Québec loan, which are measured using different guidelines. As at December 31, 2011 and 2010, the Company was in full compliance with its financial covenants under the respective agreements.

At December 31, 2011 the Company had cash and cash equivalents of \$5,576 and \$22,367 available under its ABL Credit Facility. At December 31, 2010 the Company had cash and cash equivalents of \$16,421 and \$54,187 available under its Revolving Credit Facility.

**22. Segmented information**

Management has determined that the Company operates in two reportable segments, namely the manufacturing of premium NBSK pulp at the Saint-Félicien mill and the manufacturing of premium RBK pulp at the Fairmont and Menominee mills.

Segmented information is summarized as follows:

	2011	
	NBSK	RBK
		Total

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	\$	\$	\$
Sales	274,688	263,002	537,690
Cost of product sold	200,636	235,741	436,377
Delivery costs	21,829	20,336	42,165
Selling and administrative expenses	8,382	9,507	17,889
Depreciation	30,315	5,556	35,871
Profit (loss) from operations	13,526	(8,138)	5,388

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**22. Segmented information (continued)**

	NBSK \$	2010 RBK \$	Total \$
Sales	284,815	271,724	556,539
Cost of product sold	200,934	230,840	431,774
Delivery costs	21,958	19,536	41,494
Selling and administrative expenses	5,608	8,156	13,764
Depreciation	28,670	5,815	34,485
Profit from operations	27,645	7,377	35,022

	NBSK \$	2011 RBK \$	Total \$	NBSK \$	2010 RBK \$	Total \$
Acquisition of property, plant and equipment	17,777	4,090	21,867	10,456	4,239	14,695
Property, plant and equipment	288,005	19,548	307,553	300,514	82,095	382,609
Total assets	375,699	106,093	481,792	396,100	159,800	555,900

Geographic information related to sales is as follows:

	2011 \$	2010 \$
Canada	32,074	39,316
United States	415,292	395,419
Europe	66,813	88,716
Others	23,511	33,088
	537,690	556,539

Sales have been allocated to geographic regions based on the region in which the customer is domiciled. All property, plant and equipment of the NBSK segment are located in Canada and all property, plant and equipment of the RBK segment are located in the United States.

For the year ended December 31, 2011, sales to two customers representing 10% or more of the Company's total sales reached \$125,591 (\$58,648 and \$66,943) allocated among NBSK and RBK segments. For the year ended December 31, 2010, only one major customer contributed for \$75,380 of the Company's total sales, also allocated among NBSK and RBK segments.



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**23. Special termination benefits**

On December 1, 2009, the Company announced a reorganization of its activities in its NBSK and RBK mills which took effect in the last quarter of 2009 and in the beginning of 2010. As a result, expenses of nil and \$879 were recognized in the years ended December 31, 2011 and 2010 respectively relating to separation payments for terminated employees; the expenses are included in Cost of products sold and Selling and administrative expenses .

	2011	2010
	\$	\$
<b>Special termination benefit liability</b>		
Balance, beginning of year	68	1,237
Benefits incurred		879
Benefits paid	(5)	(2,048)
Balance, end of year	63	68

**24. Gain on settlement of claim**

In December 2010, the Company was allocated an initial 236,226 common shares of AbitibiBowater Inc. as partial settlement for a claim filed pursuant to the procedures undertaken by AbitibiBowater Inc. under the *Companies Creditors Arrangement Act*, resulting in a gain on settlement of claim totalling \$5,544. A minimal amount of common shares of AbitibiBowater Inc. have been reserved for the benefit of holders of disputed claims and could be distributed subsequently to unsecured creditors in accordance with the terms of the plan of reorganization. On February 3, 2011, the Company sold the 236,226 common shares at a market price of \$26.75 per share resulting in a gain of \$763 net of transaction fees. In April 2011, the Company was allocated an additional 2,122 common shares of AbitibiBowater Inc. from the reserved common shares resulting in a gain on settlement of claim totalling \$55. As at December 31, 2011, the investment was recorded at its closing market price of \$14.84 per share and an unrealized loss of \$23 was recognized in relation to the mark to market of the financial instrument.

**25. Related party transactions and balances**

Related party transactions conducted in the normal course of operations are measured at the fair value (the amount established and agreed to by the related parties), unless specific requirements within IFRS require different treatment.

Compensation of executive officers and key management:

	2011	2010
	\$	\$
Short-term benefits	3,003	3,534

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Post-employment benefits	<b>210</b>	116
Termination benefits		639
Share-based payment	<b>812</b>	502
	<b>4,025</b>	4,791

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#### **25. Related party transactions and balances (continued)**

- i) During the year, executive officers and key management were awarded share options as described in Note 15. As at December 31, 2011, executive officers and key management owned 2,025,823 share options awarded under the regular grants and 1,086,009 share options awarded under the special one-time grant. No share options were owned by the Directors.
- ii) As part of the Rights Offering described in Note 13, the Company paid underwriters fees of \$400 to Fairfax Financial Holdings Limited which, as a shareholder, exercises a significant influence on the Company. No amount is outstanding as at December 31, 2011 and 2010.

#### **26. Conversion to IFRS**

##### *i) Overview*

The Canadian Accounting Standards Board determined that IFRS replaces Canadian GAAP for publicly accountable enterprises, including the Company, for interim financial report and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

These consolidated financial statements represent the first annual financial statements of the Company prepared in accordance with IFRS. Prior to January 1, 2011, the Company prepared its interim and annual consolidated financial statements in accordance with Canadian GAAP.

The accounting policies described in Note 2 have been selected to be consistent with IFRS.

##### *ii) First-time adoption of IFRS*

The adoption of IFRS requires the application of IFRS 1, which provides guidance for an entity's initial adoption of IFRS. IFRS 1 generally requires retrospective application of IFRS effective at the end of its first annual IFRS reporting period. However, IFRS 1 also provides optional exemptions and mandatory exceptions to this retrospective treatment.

The Company has elected to apply the following optional exemptions in its preparation of an opening IFRS statement of financial position as at January 1, 2010, the Company's Transition Date:

To elect to recognize in opening equity all cumulative actuarial gains and losses related to its defined benefit pension plans at the Transition Date.

To elect not to apply retrospectively IAS 21, *The Effect of Changes in Foreign Exchange Rates*, and deem the cumulative translation differences for all foreign operations to be zero at the Transition Date.

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To elect not to comply with the requirements in IFRIC 1 for *Changes in Existing Decommissioning, Restoration and Similar Liabilities* that occurred before the Transition Date to IFRS. The Company followed the measurement guidance under this exception to remeasure the exiting obligation (landfill closure liability) and the related asset at Transition Date.

To apply IAS 23, *Borrowing Costs* prospectively from the Transition Date. IAS 23 requires the capitalization of borrowing costs directly attributable to the acquisition, production or construction of certain assets.

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#### **26. Conversion to IFRS (continued)**

##### *ii) First-time adoption of IFRS (continued)*

To apply IFRS 2, *Share-based Payments* retrospectively only to equity awards that were issued after November 7, 2002 and had not vested by the Transition Date and outstanding liability awards.

To apply IFRS 3, *Business Combinations* prospectively from the Transition Date, therefore not restating business combinations that took place prior to the Transition Date.

To apply the transition provisions of IFRIC 4, *Determining whether an Arrangement Contains a Lease*, therefore determining if arrangements existing at the Transition Date contain a lease based on the circumstances existing at that date.

IFRS 1 does not permit changes to estimates that have been made previously. Accordingly, estimates used in the preparation of the Company's opening IFRS statement of financial position as at the Transition Date are consistent with those made under Canadian GAAP.

The Company's IFRS consolidated statement of financial position as at the Transition Date is included as comparative information in *iv)* below.

##### *iii) Changes to accounting policies*

The following summarizes the significant changes to the Company's accounting policies to be consistent with IFRS on adoption date.

#### **Property, plant and equipment**

IAS 16, *Property, Plant and Equipment* ( IAS 16 ) requires the Company to choose, for each class of capital assets, between the cost model and the revaluation model. The Company has selected the cost model in accounting for all of its capital assets.

The Company has changed its accounting policies to reflect the requirement under IAS 16 that, when an item of property, plant and equipment comprises major components with different useful lives, the components are amortized separately over their respective useful lives.

#### **Impairment of assets**

IAS 36, *Impairment of Assets* ( IAS 36 ) requires a write-down of assets if the recoverable amount (defined as the greater of the fair value less costs to sell and the value in use of an asset or a cash generating unit) is less than its carrying amount. Value in use is determined using discounted estimated future cash flows. Under Canadian GAAP, a write-down to estimated fair value was required only if the undiscounted estimated future cash flows of a group of assets were less than its carrying amount. The Company has changed its accounting policies related to impairment of assets to be consistent with the requirements under IFRS.

IAS 36 also requires the reversal of any previous impairment losses, with the exception of goodwill, where circumstances have changed such that the level of impairment in the value of the assets has been reduced. Canadian GAAP prohibited the reversal of impairment losses.



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**26. Conversion to IFRS (continued)***iii) Changes to accounting policies (continued)*

Under IFRS, the determination of an impairment is calculated on a different basis compared to Canadian GAAP. As a result of the transition, the Company carried out a review of the recoverable amount of plant and related equipment in its business units. This review led to the recognition of an impairment loss of \$136,964, which has been recognized directly in opening deficit and accumulated other comprehensive income as a component of the transition to IFRS.

The distribution of impairment loss recognized against assets is as follows:

	\$
Land	1,146
Buildings and related components	6,130
Equipment, roads, lots and other	129,602
Intangible assets	86

The recoverable amount of the relevant assets has been determined on the basis of their value in use. The discount rate used in measuring value in use was 12% per annum. There was no impairment recognized under Canadian GAAP.

**Provisions**

IFRS requires the recognition of a decommissioning liability for legal or constructive obligations, while Canadian GAAP required the recognition of such liabilities only for legal obligations. A constructive obligation exists when an entity has created reasonable expectations that it will take certain actions.

The Company has changed its accounting policies to reflect these requirements, however this change has not result in the recognition of additional provisions. Therefore, under IFRS, no constructive obligation is recognized.

**Financial instruments**

IFRS requires that the liability portion of compound instruments be evaluated first and the residual allocated to equity, which is the case for the Debentures. Under Canadian GAAP, there was no specific requirements.

The Company has changed its valuation method for compound instruments to be consistent with the requirements under IFRS.

**Employee benefits**

IFRS requires that the past service cost element of defined benefit plans be expensed on an accelerated basis, with vested past service costs expensed immediately and unvested past service costs recognized on a straight-line basis over the vesting period. Under Canadian GAAP, past service costs were generally amortized on a straight-line basis over the expected average remaining service period of active employees under the plan.

The Company's accounting policies related to employee benefits have been changed to reflect these requirements under IFRS.

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**26. Conversion to IFRS (continued)***iv) Reconciliations of Canadian GAAP to IFRS*

The following provides reconciliations from Canadian GAAP to IFRS on the Transition Date.

	\$0000000	\$0000000 December 31, 2009 (Canadian GAAP) \$	\$0000000 Transition Adjustments \$	\$0000000 January 1, 2010 (IFRS) \$
<b>Assets</b>				
Current assets				
Cash and cash equivalents		19,174		19,174
Trade and other receivables		53,424		53,424
Inventories	c	79,003	(748)	78,255
Prepaid expenses		4,036		4,036
		155,637	(748)	154,889
Deferred financing fees		421		421
Property, plant and equipment	a,b	542,360	(134,918)	407,442
Intangible assets	a	395	(86)	309
Other assets		856		856
		699,669	(135,752)	563,917
<b>Liabilities</b>				
Current liabilities				
Trade and other payables		45,213		45,213
Landfill closure liability		445		445
Derivative instruments		113		113
Current portion of long-term debt		36,682		36,682
		82,453		82,453
Debt derivative at fair value through profit or loss	d		859	859
Landfill closure liability	e	2,075	1,091	3,166
Employee benefits	f	14,022	10,538	24,560
Convertible unsecured subordinated debentures		47,696		47,696
Long-term debt		118,776		118,776

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		265,022	12,488	277,510
<b>Equity</b>				
Unitholders' capital		658,609		658,609
Equity component of Debentures	d	6,242	(6,242)	
Deficit		(225,500)	(146,702)	(372,202)
Accumulated other comprehensive income	g	(4,704)	4,704	
		434,647	(148,240)	286,407
		699,669	(135,752)	563,917

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**26. Conversion to IFRS (continued)***iv) Reconciliations of Canadian GAAP to IFRS (continued)*

Reconciliation of equity:

	\$00000000	\$00000000	\$00000000
	Note	December 31, 2010 \$	January 1, 2010 \$
Equity under Canadian GAAP		472,508	434,647
Reconciling items:			
Property, plant and equipment and intangible assets	a, b	(120,933)	(135,004)
Employee benefits	f	(15,185)	(10,538)
Inventories	c	(578)	(748)
Landfill closure liability	e	(539)	(1,091)
Debenture derivative	d		(859)
Equity under IFRS		335,273	286,407