# Responsibility of Management

The management of West Fraser Timber Co. Ltd. is responsible for the preparation, integrity and objectivity of the consolidated financial statements. The consolidated financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada and necessarily include amounts that represent the best estimates and judgments of management.

Management maintains a system of internal controls over financial reporting that encompasses policies, procedures and controls to provide reasonable assurance that assets are safeguarded against loss or unauthorized use, transactions are executed and recorded in accordance with management's authorization and financial records are accurate and reliable.

The Company's independent auditors, who are appointed by the shareholders upon the recommendation of the Audit Committee and the Board of Directors, have completed their audit of the financial statements in accordance with Canadian generally accepted auditing standards and their report follows.

The Board of Directors provides oversight to the financial reporting process through its Audit Committee, comprised of three Directors, none of whom is an officer or employee of the Company. The Audit Committee meets regularly with management and the Company's auditors to review the statements and matters relating to the audit. The Company's auditors have full and free access to the Audit Committee. The Audit Committee reports its findings to the Board of Directors for consideration in approving the consolidated financial statements for issuance to the shareholders.

Henry Ketcham

**Henry H. Ketcham**
Chairman, President and
Chief Executive Officer

**Gerry Miller**
Executive Vice-President, Finance
and Chief Financial Officer

February 17, 2011

## Auditors' Report



**To the Shareholders of West Fraser Timber Co. Ltd.**

We have audited the accompanying consolidated financial statements of West Fraser Timber Co. Ltd., which comprise the consolidated balance sheets as at December 31, 2010 and 2009 and the consolidated statements of earnings, comprehensive earnings, changes in equity and cash flows for the years then ended, and the related notes including a summary of significant accounting policies.

**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 Canadian generally accepted accounting principles, 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. 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, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. 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.

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of West Fraser Timber Co. Ltd. as at December 31, 2010 and 2009 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

**Chartered Accountants**

Vancouver, British Columbia

February 17, 2011

## Consolidated Balance Sheets

As at December 31, 2010 and 2009

| (In millions of Canadian dollars) | **2010** | 2009 |
|---|---|---|
| **ASSETS** | | |
| **Current assets** | | |
| Cash and short-term investments | **$ 163.1** | $ 12.0 |
| Accounts receivable (note 18) | **246.0** | 200.6 |
| Income taxes receivable | **—** | 67.6 |
| Inventories (note 4) | **372.4** | 407.7 |
| Prepaid expenses | **18.4** | 15.8 |
| | **799.9** | 703.7 |
| **Property, plant, equipment and timber** (note 5) | **1,501.8** | 1,624.1 |
| **Deferred pension costs** (note 12) | **168.0** | 132.7 |
| **Goodwill** | **263.7** | 263.7 |
| **Other assets** (note 6) | **81.6** | 88.9 |
| | **$ 2,815.0** | $ 2,813.1 |
| **LIABILITIES** | | |
| **Current liabilities** | | |
| Cheques issued in excess of funds on deposit | **$ 2.4** | $ 21.8 |
| Operating loans (note 8) | **8.8** | 78.7 |
| Accounts payable and accrued liabilities | **258.0** | 252.6 |
| Current portion of asset retirement obligations (note 9) | **47.6** | 41.5 |
| Income taxes payable | **58.3** | — |
| Current portion of long-term debt (note 8) | **0.3** | 100.3 |
| | **375.4** | 494.9 |
| **Long-term debt** (note 8) | **299.5** | 315.9 |
| **Other liabilities** (note 9) | **160.6** | 166.9 |
| **Future income taxes** (note 15) | **214.3** | 217.2 |
| | **1,049.8** | 1,194.9 |
| **SHAREHOLDERS' EQUITY** | | |
| **Share capital** (note 10) | **600.5** | 599.7 |
| **Accumulated other comprehensive earnings** | **(72.1)** | (59.8) |
| **Retained earnings** | **1,236.8** | 1,078.3 |
| | **1,765.2** | 1,618.2 |
| | **$ 2,815.0** | $ 2,813.1 |

Contingency (note 21)

**Approved by the Board of Directors**

**Janice G. Rennie**
Director

**J. Duncan Gibson**
Director

## Consolidated Statements of Earnings and Comprehensive Earnings

For the years ended December 31, 2010 and 2009

| (In millions of Canadian dollars, except earnings per share) | | 2010 | | 2009 |
|---|---|---|---|---|
| **Sales** | $ | 2,885.9 | $ | 2,352.5 |
| **Costs and expenses** | | | | |
| Cost of products sold | | 1,806.7 | | 1,724.6 |
| Freight and other distribution costs | | 441.2 | | 396.3 |
| Export taxes | | 59.7 | | 47.3 |
| Amortization | | 181.2 | | 244.7 |
| Selling, general and administration | | 140.4 | | 98.8 |
| Asset impairments (note 11) | | – | | 16.9 |
| Restructuring charges (note 11) | | – | | 5.2 |
| | | 2,629.2 | | 2,533.8 |
| **Operating earnings** | | 256.7 | | (181.3) |
| **Other** | | | | |
| Interest expense – net (note 13) | | (26.6) | | (26.5) |
| Exchange gain on long-term debt | | 16.9 | | 50.1 |
| Other expense (note 14) | | (8.4) | | (3.7) |
| **Earnings from continuing operations before income taxes** | | 238.6 | | (161.4) |
| **Recovery of (provision for) income taxes** (note 15) | | | | |
| Current | | (69.1) | | 36.0 |
| Future | | 0.3 | | (69.0) |
| | | (68.8) | | (33.0) |
| **Earnings from continuing operations** | | 169.8 | | (194.4) |
| **Loss from discontinued operations** (note 2) | | (3.6) | | (146.4) |
| **Earnings** | $ | 166.2 | $ | (340.8) |
| **Earnings per share** (dollars) (note 16) | | | | |
| Basic from continuing operations | $ | 3.97 | $ | (4.54) |
| Diluted from continuing operations | $ | 3.93 | $ | (4.54) |
| Basic after discontinued operations | $ | 3.88 | $ | (7.96) |
| Diluted after discontinued operations | $ | 3.84 | $ | (7.96) |
| **Comprehensive earnings** | | | | |
| **Earnings** | $ | 166.2 | $ | (340.8) |
| **Other comprehensive earnings** | | | | |
| Foreign exchange translation on investment in self-sustaining foreign operations | | (12.3) | | (61.5) |
| **Comprehensive earnings** | $ | 153.9 | $ | (402.3) |

# Consolidated Statement of Changes in Equity

For the years ended December 31, 2010 and 2009

| (In millions of Canadian dollars) | Issued capital Number of shares | Issued capital Amount | Translation of foreign operations | Retained earnings | Total equity |
|---|---|---|---|---|---|
| **Balance — January 1, 2009** | 42,805,086 | $ 599.4 | $ 1.7 | $ 1,428.9 | $ 2,030.0 |
| **Changes in equity for 2009** | | | | | |
| Foreign exchange translation loss on investment in self-sustaining foreign operations | — | — | (61.5) | — | (61.5) |
| Issuance of Common shares | 10,723 | 0.3 | — | — | 0.3 |
| Earnings for the year | — | — | — | (340.8) | (340.8) |
| Dividends | — | — | — | (9.8) | (9.8) |
| **Balance — December 31, 2009** | 42,815,809 | 599.7 | (59.8) | 1,078.3 | 1,618.2 |
| **Changes in equity for 2010** | | | | | |
| Foreign exchange translation loss on investment in self-sustaining foreign operations | **—** | **—** | **(12.3)** | **—** | **(12.3)** |
| Issuance of Common shares | **19,103** | **0.8** | **—** | **—** | **0.8** |
| Earnings for the year | **—** | **—** | **—** | **166.2** | **166.2** |
| Dividends | **—** | **—** | **—** | **(7.7)** | **(7.7)** |
| **Balance — December 31, 2010** | **42,834,912** | **$ 600.5** | **$ (72.1)** | **$ 1,236.8** | **$ 1,765.2** |

## Consolidated Statements of Cash Flows

For the years ended December 31, 2010 and 2009

| (In millions of Canadian dollars) | 2010 | 2009 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Earnings from continuing operations | $ 169.8 | $ (194.4) |
| Items not affecting cash | | |
| Amortization | 181.2 | 244.7 |
| Asset impairments | — | 16.9 |
| Gain on asset sales | (2.6) | (1.9) |
| Change in deferred maintenance | 15.1 | 9.0 |
| Change in deferred charges | (32.3) | (53.3) |
| Exchange gain on long-term debt | (16.9) | (50.1) |
| Change in reforestation obligations | 3.7 | (18.3) |
| Change in other long-term liabilities | 1.6 | 2.2 |
| Future income taxes | (0.6) | 69.6 |
| Other | 1.9 | 6.3 |
| | 320.9 | 30.7 |
| Net change in non-cash working capital items | 49.3 | 65.5 |
| | 370.2 | 96.2 |
| **Cash flows from financing activities** | | |
| Repayment of long-term debt | (100.3) | (150.1) |
| Proceeds from (repayment of) operating loans | (64.2) | 52.0 |
| Dividends | (7.7) | (9.8) |
| Other | (5.6) | 0.3 |
| | (177.8) | (107.6) |
| **Cash flows from investing activities** | | |
| Additions to property, plant, equipment and timber | (56.3) | (17.8) |
| Proceeds from disposal of property, plant, equipment and timber | 2.7 | 2.2 |
| Decrease in other assets | 0.6 | 4.9 |
| | (53.0) | (10.7) |
| **Change in cash from continuing operations** | 139.4 | (22.1) |
| **Change in cash from discontinued operations** (note 2) | 31.1 | 8.6 |
| **Cash — beginning of year** | (9.8) | 3.7 |
| **Cash — end of year** | $ 160.7 | $ (9.8) |
| **Cash consists of** | | |
| Cash and short-term investments | $ 163.1 | $ 12.0 |
| Cheques issued in excess of funds on deposit | (2.4) | (21.8) |
| | $ 160.7 | $ (9.8) |
| **Supplemental information** | | |
| ***Interest paid*** | $ 29.6 | $ 29.4 |
| ***Income taxes received** — net* | $ 66.1 | $ 18.8 |

# Notes to Consolidated Financial Statements

For the years ended December 31, 2010 and 2009

(in millions of Canadian dollars)

## 1. Nature of operations and significant accounting policies

### Nature of operations

The Company is an integrated wood products company producing lumber, wood chips, LVL, MDF, plywood, pulp and newsprint.

### Basis of presentation

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles. Certain comparative figures have been reclassified to conform to the current year's presentation.

### Principles of consolidation

These consolidated financial statements include the accounts of the Company and its subsidiaries after elimination of intercompany transactions and balances.

Investments in and operations of joint ventures are accounted for by the proportionate consolidation method.

### Financial instruments

Cash and short-term investments and derivatives are classified as held for trading and are measured at fair value at each balance sheet date with changes reflected in other income (expense).

Accounts receivable are classified as loans and receivables and are measured at amortized cost using the effective interest rate method.

Long-term investments are classified as available for sale and are measured at fair value if there is an active market or carried at cost if there is no active market. Changes in fair value are recognized through other comprehensive earnings. When the asset is sold or impaired the impact is recognized immediately in earnings and recycled from accumulated other comprehensive earnings.

Cheques issued in excess of funds on deposit, operating loans, accounts payable and accrued liabilities, and long-term debt are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method. Financing charges are netted against debt and are amortized over the life of the debt.

### Use of estimates

The preparation of financial statements requires estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant areas requiring estimates are asset valuations, reforestation obligations, other asset retirement obligations, income taxes and employee future benefits. Actual amounts could differ materially from those estimates.

During 2010 the Company revised certain amortization rates which resulted in a reduction of amortization expense for the year of $13.0 million.

### Revenue recognition

Revenues are derived from product sales and are recognized upon the transfer of significant risks and rewards of ownership, provided collectibility is reasonably assured.

**Foreign currency translation**

*Self-sustaining foreign operations*

The Company translates its foreign subsidiaries financial statements using the current rate method. Under this method, all assets and liabilities of the foreign operations are translated into Canadian dollars at the period-end exchange rate and revenues and expenses are translated at average exchange rates during the reporting period. The resulting unrealized gains or losses are included in other comprehensive earnings.

*Translation of other foreign currency transactions*

Monetary assets and liabilities denominated in foreign currencies, including long-term debt, are translated into Canadian dollars at the period-end exchange rate. Income and expense items are translated at average exchange rates during the reporting period. The resulting gains or losses are recognized in earnings.

**Cash and short-term investments**

Cash and short-term investments consist of cash on deposit and short-term interest-bearing securities maturing within three months of the date of purchase.

**Inventories**

Inventories of logs, other raw materials and manufactured products are valued at the lower of average cost and net realizable value. Processing materials and supplies are valued at the lower of average cost and replacement cost.

**Property, plant, equipment and timber**

Property, plant, equipment and timber are stated at cost less accumulated amortization. Expenditures for additions and improvements are capitalized. Major manufacturing assets under construction include capitalized interest, where applicable. Government grants received that pertain to the construction of manufacturing assets are applied to reduce the cost of the asset. Expenditures for maintenance and repairs are charged to earnings. Upon retirement, disposal or destruction of an asset, the cost and related amortization are removed from the accounts and any gain or loss is recognized in earnings.

Property, plant and equipment are amortized on a straight-line basis over their estimated useful lives as follows:

| | |
|---|---|
| Buildings | 10 – 30 years |
| Manufacturing equipment and machinery | 10 – 20 years |
| Fixtures and other equipment | 3 – 10 years |

Timber rights and roads are amortized over periods not exceeding 40 years.

**Impairment of long-lived assets**

The Company reviews property, plant, equipment and timber for impairment whenever events or changes in circumstances indicate that the carrying amount may not be fully recoverable. Recoverability is assessed by comparing the carrying amount to the estimated future net cash flows the assets are expected to generate. If the carrying amount exceeds the estimated future cash flows, the asset is written down to fair value.

Fair value is determined based on the discounted estimated net future cash flows expected to be generated over the useful lives of the assets. Estimated net future cash flows are based on several estimates including the future selling price of products, future US/Canadian dollar exchange rates, future production rates, future input costs and future capital requirements. The estimated net future cash flows are discounted at rates that reflect the Company's cost of capital.

**Goodwill**

Goodwill represents the excess of the purchase price paid for an acquisition over the fair value of the net assets acquired. Goodwill is not amortized, but is subject to an impairment test annually or more frequently if events or circumstances indicate that it may be impaired.

Goodwill impairment is assessed by comparing the fair value of a reporting unit to the underlying carrying amount of the reporting unit's net assets, including goodwill. When the carrying amount of the unit exceeds its fair value, the fair value of the unit's goodwill is compared with its carrying amount to measure the amount of impairment loss, if any.

### Asset retirement obligations

The Company harvests timber under various timber rights that require the Company to conduct reforestation. Estimated future reforestation obligations are measured at fair value and accrued and charged to earnings when timber is harvested. The reforestation obligation is reviewed periodically and changes to estimates are recognized in earnings.

The Company records the estimated fair value of a liability for other asset retirement obligations in the period a reasonable estimate of fair value can be made. The fair value is added to the carrying amount of the associated asset and amortized over its useful life. The liability is accreted through charges to earnings and is reduced by actual costs of settlement.

### Share-based compensation

The Company's share option plan gives share option holders the right to elect to receive a cash payment in lieu of exercising an option to purchase Common shares. The Company records an expense or recovery in selling, general and administration expense for share options, based on the quoted market price of the Company's Common shares. If an option holder elects to purchase Common shares, both the exercise price and the accrued liability are credited to shareholders' equity.

The Company's phantom share unit plan provides for future cash payments to certain officers and employees based on the Company's share price at the vesting date and, in some cases, based on relative financial performance compared to a peer group of forest products companies. The Company records an expense or recovery in selling, general and administration expense over the vesting period based on the quoted market price of the Company's Common shares.

The directors' deferred share unit plan allows for settlement in cash or Common shares at the holder's option and, therefore, is accounted for as a liability. Fluctuations in the market price of the Common shares cause changes in the Company's obligations under the plan, the offset of which is recorded in selling, general and administration expense.

### Employee future benefits

The Company accrues for its obligations under employee benefit plans and the related costs net of plan assets.

The Company has adopted the following policies:

- The measurement date used for accounting purposes is October 31;
- The cost of pensions earned by employees is actuarially determined using the projected benefit method pro-rated for estimated service periods and management's estimate of expected plan investment performance, salary escalation and retirement ages of employees;
- For the purpose of calculating expected return, plan assets are valued at fair value;
- Past service costs arising from plan amendments and transitional obligations are amortized on a straight-line basis over the estimated average remaining service period of affected employees active at the date of the amendments; and
- The excess of the net actuarial gain (loss) over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the estimated average remaining service period of the active employees.

For defined contribution plans, pension expense is the amount of contributions the Company is required to make in respect of services rendered by employees.

### Income taxes

Future income taxes are provided for using the liability method. Under this method, future income taxes are recognized for temporary differences between the tax and financial statement bases of assets, liabilities and certain carry-forward items.

Future income tax assets are recognized only to the extent that it is more likely than not that they will be realized. Future income tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of substantive enactment.

## 2. Discontinued operations

In October 2009, the Company announced its decision to permanently close the Kitimat linerboard and kraft paper mill. In January 2010, the mill ceased operations. Accordingly, current and prior period results for this operation have been reclassified to discontinued operations.

The results of the discontinued operations are as follows:

| | 2010 | 2009 |
|---|---|---|
| Sales | $ 71.8 | $ 259.3 |
| Operating loss | $ (20.3) | $ (211.0) |
| Gain on foreign currency contracts | – | 9.8 |
| Other income (expense) | 15.8 | (9.9) |
| Loss before income tax | (4.5) | (211.1) |
| Income tax recovery | 0.9 | 64.7 |
| Loss | $ (3.6) | $ (146.4) |
| Cash flows from operating activities | $ 16.4 | $ 9.7 |
| Cash flows from investing activities | 14.7 | (1.1) |
| Increase in cash | $ 31.1 | $ 8.6 |

Included in discontinued operations for 2009 are restructuring charges of $41.7 million and asset impairments of $140.0 million.

## 3. Investment in joint ventures

The Company's joint ventures are Alberta Newsprint Company (50%) and Cariboo Pulp and Paper Company (50%). The combined proportionate share of the joint ventures is as follows:

| | 2010 | 2009 |
|---|---|---|
| Current assets | $ 64.7 | $ 61.9 |
| Non-current assets | 103.1 | 116.3 |
| Total assets | 167.8 | 178.2 |
| Current liabilities | (20.6) | (21.1) |
| Non-current liabilities | (17.0) | (17.7) |
| Equity | $ 130.2 | $ 139.4 |
| Sales | $ 218.1 | $ 177.0 |
| Costs and expenses | (184.2) | (186.6) |
| Earnings before income taxes | $ 33.9 | $ (9.6) |
| Cash flows from operating activities | $ 46.3 | $ 10.3 |
| Cash flows from investing activities | $ (1.9) | $ (4.9) |

The Company has business transactions with certain of its joint venture participants and entities related to them. All transactions are at market prices and on normal business terms.

## 4. Inventories

| | 2010 | 2009 |
|---|---|---|
| Logs and other raw materials | $ 92.1 | $ 76.5 |
| Manufactured products | 194.6 | 241.0 |
| Processing materials and supplies | 85.7 | 90.2 |
| | $ 372.4 | $ 407.7 |

Inventories at December 31, 2010 were written down by $3.8 million (2009 – $16.0 million) to reflect net realizable value being lower than cost.

(in millions of Canadian dollars)

## 5. Property, plant, equipment and timber

| | Cost | Accumulated amortization | Net |
|---|---|---|---|
| | | | **2010** |
| Manufacturing plant, equipment and machinery | **$ 2,771.6** | **$ 1,857.4** | **$ 914.2** |
| Construction-in-progress | **12.8** | **—** | **12.8** |
| Timber rights and roads | **788.1** | **244.0** | **544.1** |
| Other | **37.2** | **6.5** | **30.7** |
| | **$ 3,609.7** | **$ 2,107.9** | **$ 1,501.8** |

| | Cost | Accumulated amortization | Net |
|---|---|---|---|
| | | | 2009 |
| Manufacturing plant, equipment and machinery | $ 2,821.4 | $ 1,765.1 | $ 1,056.3 |
| Construction-in-progress | 2.6 | — | 2.6 |
| Timber rights and roads | 767.6 | 233.5 | 534.1 |
| Other | 36.2 | 5.1 | 31.1 |
| | $ 3,627.8 | $ 2,003.7 | $ 1,624.1 |

## 6. Other assets

| | **2010** | 2009 |
|---|---|---|
| Power purchase agreement | **$ 73.2** | $ 80.5 |
| Advances for timber and timber deposits | **3.4** | 5.7 |
| Investments and other | **5.0** | 2.7 |
| | **$ 81.6** | $ 88.9 |

### Power purchase agreement

The Company has entered into a power purchase agreement to acquire a portion of the electricity generated from a power plant in Alberta at substantially predetermined prices. The Company's share of electricity capacity to 2020 is expected to be approximately 115 megawatts per year. The Company sells the electricity acquired at prevailing market prices. At the same time, the Company's Alberta operations purchase electricity at prevailing market prices. The cost of the power purchase agreement is amortized over its term.

## 7. Restructuring charges

Restructuring charges relate to the closure of the Kitimat linerboard and kraft paper mill and certain indefinitely idled sawmills. A reconciliation of restructuring charges included in accounts payable and accrued liabilities is as follows:

| | **2010** | 2009 |
|---|---|---|
| Accrued liability — beginning of year | **$ 34.1** | $ — |
| Paid during the year | **(35.1)** | — |
| Change in estimate | **5.5** | 34.1 |
| Accrued liability — end of year | **$ 4.5** | $ 34.1 |

## 8. Long-term debt and operating loans

### Long-term debt

| | 2010 | 2009 |
|---|---|---|
| Term note due March 2010; interest at floating rates | $ — | $ 100.0 |
| US$300 million senior notes due October 2014; interest at 5.2% | 298.4 | 315.3 |
| Note payable due in instalments to 2020; interest at 5.5% | 2.7 | 2.7 |
| | 301.1 | 418.0 |
| Less: Current portion | (0.3) | (100.3) |
| Deferred financing costs | (1.3) | (1.8) |
| | $ 299.5 | $ 315.9 |

Required principal repayments are disclosed in note 18.

### Operating loans

The Company has $505 million (2009 – $605 million) in revolving lines of credit available, of which $8.8 million (net of deferred financing costs of $6.2 million) was drawn as at December 31, 2010 (2009 – $78.7 million – net of deferred financing costs of $2.2 million). Interest is payable at floating rates based on Prime, US base, Bankers' Acceptances or LIBOR at the Company's option. The Company has also issued letters of credit in the amount of $35.4 million (2009 – $33.4 million) that are supported by this facility. The revolving lines of credit include a $500 million committed facility maturing in December 2014.

The $500 million committed facility and the US$300 million senior notes are secured by the Company's assets.

## 9. Other liabilities

| | 2010 | 2009 |
|---|---|---|
| Post-retirement obligations (note 12) | $ 70.1 | $ 65.7 |
| Timber damage deposits | 13.9 | 15.6 |
| Reforestation obligations – long-term | 54.4 | 51.9 |
| Other asset retirement obligations – long-term | 15.2 | 26.0 |
| Other long-term liabilities | 7.0 | 7.7 |
| | $ 160.6 | $ 166.9 |

### Asset retirement obligations

The Company's asset retirement obligations relate to its responsibility for reforestation under various timber rights, landfill closures and other site remediation costs.

Changes in asset retirement obligations are as follows:

| | Reforestation | | Other | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| Asset retirement obligations – opening | $ 89.7 | $ 108.0 | $ 29.7 | $ 14.8 |
| Liabilities purchased | 1.9 | – | — | – |
| Liabilities recognized | 35.8 | 31.0 | — | 12.8 |
| Liabilities settled | (35.2) | (37.1) | (4.4) | (0.1) |
| Accretion expense | 4.1 | 4.0 | 1.1 | 0.8 |
| Change in estimates | (1.0) | (16.2) | (4.5) | 1.4 |
| Asset retirement obligations – ending | 95.3 | 89.7 | 21.9 | 29.7 |
| Less: Current portion | (40.9) | (37.8) | (6.7) | (3.7) |
| | $ 54.4 | $ 51.9 | $ 15.2 | $ 26.0 |

(in millions of Canadian dollars)

The total undiscounted amount of the estimated cash flows required to satisfy these obligations is $143.1 million (2009 – $150.8 million). The cash flows have been discounted using inflation and credit-adjusted rates ranging from 3.25% to 5.65% to determine fair value.

The timing of the reforestation payments is based on the estimated period required to attain free to grow status in a given area, which is generally between 12 to 15 years. Payments relating to landfill closures and site remediation are expected to occur over periods ranging up to 30 years.



### 10. Share capital

Authorized

200,000,000 Common shares, without par value
20,000,000 Class B Common shares, without par value
10,000,000 Preferred shares, issuable in series, without par value

Issued

| | 2010 Number | 2010 Amount | 2009 Number | 2009 Amount |
|---|---|---|---|---|
| Common | **40,028,434** | **$ 600.2** | 40,009,331 | $ 599.4 |
| Class B Common | **2,806,478** | **0.3** | 2,806,478 | 0.3 |
| Total Common | **42,834,912** | **$ 600.5** | 42,815,809 | $ 599.7 |

**Share capital transactions during 2010**

The Company issued 19,103 Common shares for $0.8 million.

**Share capital transactions during 2009**

The Company issued 10,723 Common shares for $0.3 million.

**Rights and restrictions of Common shares**

Common shares and Class B Common shares are equal in all respects except that each Class B Common share may at any time be exchanged for one Common share.

**Dividends payable**

Dividends declared and unpaid at December 31, 2010 amounted to $2.6 million (2009 – $1.3 million) and are included in accounts payable and accrued liabilities.

**Share option plan**

The Company has a share option plan for its directors, officers and employees under which it may grant options to purchase up to 5,005,506 Common shares of which 709,893 remain available for issuance. The exercise price of a share option is the closing price of a Common share on the trading day immediately preceding the grant date. Options vest at the earlier of the date of retirement or death and 20% per year from the grant date, and expire after 10 years. The Company has recorded an expense of $27.1 million (2009 – expense of $3.4 million) in selling, general and administration expense related to the share option plan.

A summary of the activity in the share option plan is presented below:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | Number of options | Weighted average exercise price (dollars) | Number of options | Weighted average exercise price (dollars) |
| Outstanding – beginning of year | **3,181,954** | **$ 35.19** | 2,852,028 | $ 36.63 |
| Granted | **—** | **$ —** | 452,500 | $ 24.71 |
| Exercised | **(835,582)** | **$ 28.68** | (56,870) | $ 26.41 |
| Expired/cancelled | **(27,000)** | **$ 38.69** | (65,704) | $ 33.40 |
| Outstanding – end of year | **2,319,372** | **$ 37.49** | 3,181,954 | $ 35.19 |
| Exercisable – end of year | **1,602,048** | **$ 40.04** | 2,076,313 | $ 36.21 |

The following table summarizes information about the share options outstanding at December 31, 2010:

| Ranges of exercise price (dollars) | Number outstanding | Weighted average remaining contractual life (years) | Weighted average exercise price (dollars) | Number of exercisable options | Weighted average exercise price (dollars) |
|---|---|---|---|---|---|
| $24.71 | 415,500 | 8.1 | $ 24.71 | 83,260 | $ 24.71 |
| $33.30 – $33.47 | 769,442 | 4.4 | $ 33.37 | 553,558 | $ 33.40 |
| $37.65 – $41.19 | 441,900 | 4.7 | $ 40.27 | 387,660 | $ 40.24 |
| $45.20 | 394,500 | 6.1 | $ 45.20 | 279,540 | $ 45.20 |
| $51.56 | 298,030 | 4.1 | $ 51.56 | 298,030 | $ 51.56 |
| | 2,319,372 | 5.4 | $ 37.49 | 1,602,048 | $ 40.04 |

**Phantom share unit plan**

The Company has recorded an expense of $7.0 million (2009 – $nil) in selling, general and administration expense related to the phantom share unit plan. As at December 31, 2010, 196,145 (2009 – nil) units were outstanding.

**Directors' deferred share unit plan**

Each non-employee director of the Company may elect to receive all or a portion of his or her fee in the form of deferred share units that vest immediately. Units are redeemable, in cash or for Common shares, only following resignation or retirement (including failure to be re-elected as a director) and must be redeemed by December 15 of the following year or in certain cases a shorter time period. As at December 31, 2010, 51,096 (2009 – 46,113) units were outstanding.

## 11. Asset impairment and restructuring charges

In 2009, the Company recorded asset impairment charges of $16.9 million and restructuring charges of $5.2 million related to certain sawmill assets due to weak market conditions.

## 12. Employee future benefits

The Company maintains defined benefit and defined contribution pension plans covering a majority of its employees. The defined benefit plans provide pension benefits based either on length of service or on earnings and length of service. The total pension expense for the defined benefit plans is $31.7 million (2009 – $33.4 million) with total funding contributions of $61.9 million (2009 – $92.6 million). The Company also provides group life insurance, medical and extended health benefits to certain employee groups for which it contributed $2.1 million (2009 – $2.1 million).

The total pension expense and funding contributions for the defined contribution pension plans is $1.8 million (2009 – $1.8 million).

(in millions of Canadian dollars)

The status of the defined benefit pension plans and other benefit plans, in aggregate, is as follows:

| | Pension plans | | Other benefit plans | |
|---|---|---|---|---|
| | **2010** | 2009 | **2010** | 2009 |
| **Expense** | | | | |
| Current service cost | **$ 25.6** | $ 22.5 | **$ 0.3** | $ 0.6 |
| Interest cost on earned benefit obligations | **51.0** | 49.6 | **2.7** | 3.3 |
| Actual gain on plan assets | **(86.9)** | (87.3) | **–** | – |
| Actual actuarial loss on benefit obligations | **135.7** | 53.6 | **4.1** | 17.3 |
| Curtailment loss | **2.1** | – | **0.2** | – |
| Other | **–** | (0.3) | **–** | – |
| Expense before adjustments | **127.5** | 38.1 | **7.3** | 21.2 |
| Difference between expected return and actual return on plan assets | **35.9** | 44.2 | **–** | – |
| Difference between net actuarial gain or loss recognized and actual gain or loss on benefit obligations | **(132.0)** | (49.2) | **(3.9)** | (17.9) |
| Difference in other | **0.3** | 0.3 | **(2.0)** | 0.5 |
| Net expense | **$ 31.7** | $ 33.4 | **$ 1.4** | $ 3.8 |
| **Accrued benefit obligations** | | | | |
| Projected benefit obligations – opening | **$ 782.9** | $ 701.2 | **$ 42.2** | $ 44.2 |
| Current service cost | **25.6** | 22.5 | **0.3** | 0.6 |
| Interest cost | **51.0** | 49.6 | **2.7** | 3.3 |
| Benefits paid | **(47.1)** | (43.0) | **(2.1)** | (2.1) |
| Actuarial loss | **135.7** | 53.6 | **4.1** | 17.3 |
| Plan transfers, curtailments and other | **(2.8)** | (1.0) | **(1.5)** | (21.1) |
| Projected benefit obligations – ending | **$ 945.3** | $ 782.9 | **$ 45.7** | $ 42.2 |
| **Plan assets** | | | | |
| Fair value – opening | **$ 746.6** | $ 643.1 | **$ –** | $ – |
| Actual gain on plan assets | **86.9** | 87.3 | **–** | – |
| Contributions | **93.3** | 59.6 | **2.1** | 2.1 |
| Benefits paid | **(47.1)** | (43.0) | **(2.1)** | (2.1) |
| Plan transfers and other | **(0.3)** | (0.4) | **–** | – |
| Fair value – ending | **$ 879.4** | $ 746.6 | $ **–** | $ – |
| **Funded status of the plans** | | | | |
| Deficit | **$ (65.9)** | $ (36.3) | **$ (45.7)** | $ (42.2) |
| Contributions after measurement date | **8.1** | 39.5 | **–** | – |
| | **(57.8)** | 3.2 | **(45.7)** | (42.2) |
| Unamortized net actuarial loss | **209.6** | 115.5 | **9.2** | 6.5 |
| Unamortized past service costs | **2.7** | 5.7 | **(18.2)** | (21.1) |
| Unamortized net transitional amount | **(1.9)** | (2.0) | **–** | 1.4 |
| Net accrued benefit asset (liability) | **$ 152.6** | $ 122.4 | **$ (54.7)** | $ (55.4) |
| **Represented by** | | | | |
| Deferred pension costs | **$ 168.0** | $ 132.7 | **$ –** | $ – |
| Post-retirement obligations (note 9) | **(15.4)** | (10.3) | **(54.7)** | (55.4) |
| | **$ 152.6** | $ 122.4 | **$ (54.7)** | $ (55.4) |

The significant actuarial assumptions used are as follows:

| | Pension plans | | Other benefit plans | |
|---|---|---|---|---|
| | **2010** | 2009 | **2010** | 2009 |
| To determine benefit obligations at end of year | | | | |
| Discount rate | **5.50%** | 6.50% | **5.50%** | 6.50% |
| Expected rate of return on plan assets | **6.50%** | 7.00% | **n/a** | n/a |
| Rate of increase in future compensation | **3.50%** | 3.50% | **n/a** | n/a |
| To determine benefit expense for the year | | | | |
| Discount rate | **6.50%** | 7.25% | **6.50%** | 7.25% |
| Expected rate of return on plan assets | **7.00%** | 7.00% | **n/a** | n/a |
| Rate of increase in future compensation | **3.50%** | 3.50% | **n/a** | n/a |

The Company funds health care benefit costs, shown under other benefit plans, on a pay-as-you-go basis. The actuarial assumptions are for extended health care cost increases of 10% per year for five years, grading down to 4.5% per year thereafter, with no increase in the medical services plan.

A 1% increase or decrease in the assumed health care cost trend rates would have the following effects for 2010:

| | Increase | Decrease |
|---|---|---|
| Total of service and interest cost | $ 0.1 | $ (0.1) |
| Accrued benefit obligations | $ 1.9 | $ (1.8) |

**Assets**

The weighted average asset allocations of the defined benefit plans at the measurement date, by asset category, are as follows:

| | **2010** | 2009 |
|---|---|---|
| Equity investments | **60%** | 53% |
| Fixed income investments | **39%** | 47% |
| Other investments | **1%** | – |
| | **100%** | 100% |

**Actuarial valuations**

Actuarial valuations of the pension plans are generally required every three years. The most recent valuations and the next scheduled valuations for principal defined benefit plans are as follows:

| Last actuarial valuation date | Scheduled valuation date | Benefit obligations | Fair value of assets |
|---|---|---|---|
| December 31, 2007 | December 31, 2010 | 47% | 43% |
| December 31, 2009 | December 31, 2010 | 2% | 2% |
| December 31, 2008 | December 31, 2011 | 43% | 46% |
| November 01, 2010 | November 01, 2011 | 2% | 4% |
| December 31, 2009 | December 31, 2012 | 6% | 5% |
| | | 100% | 100% |

## 13. Interest expense

| | **2010** | 2009 |
|---|---|---|
| Long-term interest expense | **$ (16.3)** | $ (26.2) |
| Current interest expense – net | **(10.3)** | (0.3) |
| | **$ (26.6)** | $ (26.5) |

(in millions of Canadian dollars)

### 14. Other income (expense)

| | 2010 | 2009 |
|---|---|---|
| Foreign exchange loss — net | $ (7.4) | $ (8.9) |
| Gain on asset sales | 2.6 | 1.9 |
| Dividend income | 0.8 | 0.5 |
| Loss on derivative financial instruments | (4.7) | (0.6) |
| Other — net | 0.3 | 3.4 |
| | $ (8.4) | $ (3.7) |

### 15. Income taxes

The effective tax rate on earnings from continuing operations is different from the statutory tax rates as follows:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | Amount | % | Amount | % |
| Income taxes at statutory rates | $ (68.0) | (28.5) | $ 48.4 | 30.0 |
| Non-taxable amounts | 6.8 | 2.9 | 8.1 | 5.0 |
| Rate differentials between jurisdictions and on specified activities | 10.4 | 4.3 | 12.7 | 7.9 |
| Rate differential on loss carry-backs | — | — | 5.8 | 3.6 |
| Reduction in statutory income tax rates | — | — | 4.7 | 2.9 |
| Change in deductibility of cash payments on share options | (9.7) | (4.1) | — | — |
| Valuation allowance | (5.8) | (2.4) | (113.8) | (70.5) |
| Other | (2.5) | (1.0) | 1.1 | 0.7 |
| | $ (68.8) | (28.8) | $ (33.0) | (20.4) |

The components of future income taxes are as follows:

| | 2010 | 2009 |
|---|---|---|
| Property, plant, equipment and timber | $ (220.7) | $ (234.7) |
| Asset retirement obligations | 25.9 | 27.6 |
| Employee future benefits | (22.6) | (15.1) |
| Loss carry-forwards | 3.5 | 1.6 |
| Other | (0.4) | 3.4 |
| | $ (214.3) | $ (217.2) |

The Company has loss carry-forwards not recognized for accounting purposes that expire in various amounts in the years 2021 to 2030.

### 16. Earnings per share

Basic earnings per share are calculated based on earnings available to Common shareholders, as set out below, using the weighted average number of Common shares and Class B Common shares outstanding. Diluted earnings per share assume the exercise of share options, using the treasury stock method.

When there is a net loss, the exercise of stock options would result in a calculated diluted earnings per share that is anti-dilutive. Accordingly, these shares have not been included in the total weighted average shares for the purpose of calculating diluted earnings per share.

| | 2010 | 2009 |
|---|---|---|
| **Earnings available to shareholders** | | |
| From continuing operations | **$ 169.8** | $ (194.4) |
| After discontinued operations | **$ 166.2** | $ (340.8) |
| **Weighted average number of shares** | | |
| Basic | **42,822,949** | 42,807,980 |
| Share options | **426,938** | n/a |
| Diluted | **43,249,887** | 42,807,980 |
| **Earnings per share** (dollars) | | |
| Basic from continuing operations | **$ 3.97** | $ (4.54) |
| Diluted from continuing operations | **$ 3.93** | $ (4.54) |
| Basic after discontinued operations | **$ 3.88** | $ (7.96) |
| Diluted after discontinued operations | **$ 3.84** | $ (7.96) |

### 17. Commitments

#### a) Operating leases

The Company is committed to make payments under certain operating leases for equipment, land, buildings and office space. The payments required under these leases are as follows:

| | |
|---|---|
| 2011 | $ 2.4 |
| 2012 | 1.3 |
| 2013 | 0.2 |
| 2014 | 0.1 |
| 2015 | 0.1 |
| | $ 4.1 |

#### b) Product purchase and sale commitments

The Company has long-term purchase and sale contracts with minimum annual volume commitments. All contracts are at market prices and on normal business terms.

#### c) Capital expenditures

The Company has capital commitments at December 31, 2010 of $29.0 million, of which $27.5 million is expected to be refunded by the government of Canada as part of the green transformation program. This program provides funding for approved capital projects to improve the energy efficiency and environmental performance of Canadian pulp and paper mills.

(in millions of Canadian dollars)

## 18. Financial instruments

### a) Carrying and fair value of financial instruments by category

| | | Held for trading | | Loans & receivables | | Other financial liabilities | | Carrying value | | 2010 Fair value |
|---|---|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | | | |
| Cash and short-term investments | $ | 163.1 | $ | — | $ | — | $ | 163.1 | $ | 163.1 |
| Accounts receivable | | — | | 246.0 | | — | | 246.0 | | 246.0 |
| | $ | 163.1 | $ | 246.0 | $ | — | $ | 409.1 | $ | 409.1 |
| **Financial liabilities** | | | | | | | | | | |
| Cheques issued in excess of funds on deposit | $ | — | $ | — | $ | 2.4 | $ | 2.4 | $ | 2.4 |
| Operating loans (note 8) | | — | | — | | 15.0 | | 15.0 | | 15.0 |
| Accounts payable and accrued liabilities | | — | | — | | 258.0 | | 258.0 | | 258.0 |
| Long-term debt (note 8) (1) | | — | | — | | 301.1 | | 301.1 | | 302.5 |
| | $ | — | $ | — | $ | 576.5 | $ | 576.5 | $ | 577.9 |

| | | Held for trading | | Loans & receivables | | Other financial liabilities | | Carrying value | | 2009 Fair value |
|---|---|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | | | |
| Cash and short-term investments | $ | 12.0 | $ | — | $ | — | $ | 12.0 | $ | 12.0 |
| Accounts receivable | | | | | | | | | | |
| Trade and other | | — | | 194.4 | | — | | 194.4 | | 194.4 |
| Derivatives | | 6.2 | | — | | — | | 6.2 | | 6.2 |
| | $ | 18.2 | $ | 194.4 | $ | — | $ | 212.6 | $ | 212.6 |
| **Financial liabilities** | | | | | | | | | | |
| Cheques issued in excess of funds on deposit | $ | — | $ | — | $ | 21.8 | $ | 21.8 | $ | 21.8 |
| Operating loans (note 8) | | — | | — | | 80.9 | | 80.9 | | 80.9 |
| Accounts payable and accrued liabilities | | | | | | | | | | |
| Trade and other | | — | | — | | 249.1 | | 249.1 | | 249.1 |
| Derivatives | | 3.5 | | — | | — | | 3.5 | | 3.5 |
| Long-term debt (note 8) (1) | | — | | — | | 418.0 | | 418.0 | | 383.9 |
| | $ | 3.5 | $ | — | $ | 769.8 | $ | 773.3 | $ | 739.2 |

(1) The fair value of the long-term debt is based on rates currently available to the Company for long-term debt with similar terms and remaining maturities.

### b) Financial risk management

The Company's activities result in exposure to a variety of financial risks including risks related to commodity prices, currency fluctuation, credit, liquidity and interest rates.

*Commodity prices*

The Company's financial performance is principally dependent on the demand for and selling prices of its products. Both are subject to significant fluctuations. The markets for lumber, wood chips, LVL, MDF, plywood, pulp and newsprint are highly volatile and are affected by factors such as global economic conditions including the strength of the US housing market, changes in industry production capacity, changes in world inventory levels and other factors beyond the Company's control.

*Currency fluctuation*

Most of the Company's products are sold at prices denominated in US dollars or based on prevailing US dollar prices, and a significant portion of its operational costs and expenses are incurred in Canadian dollars. Therefore, an increase in the value of the Canadian dollar relative to the US dollar reduces the revenue in Canadian dollar terms realized by the Company from sales made in US dollars, which reduces operating margin and the cash flow available to fund operations. US dollar-denominated debt and operations in the US provide a partial offset to exchange exposure.

From time to time, the Company uses derivatives to manage its exposure to US dollar exchange fluctuations and commodity prices. The Company does not utilize derivative financial instruments for trading or speculative purposes and it does not apply hedge accounting.

Impact of US dollar currency fluctuation on financial instruments

The US dollar balance sheet exposure, excluding self-sustaining foreign operations, at December 31, 2010 was as follows:

| | | 2010 |
|---|---|---|
| Net working capital | US$ | 146.6 |
| Long-term debt | | (300.0) |
| | US$ | (153.4) |

There were no foreign currency contracts outstanding at December 31, 2010.

Based on the US dollar balance sheet exposure at December 31, 2010, with other variables unchanged, a $0.01 increase in US dollars compared to Canadian dollars would have resulted in a $1.5 million increase in earnings. A $0.01 decrease in US dollars compared to Canadian dollars would have resulted in a $1.5 million decrease in earnings.

*Credit*

Credit risk arises from the non-performance by counterparties of contractual financial obligations. Investments of cash and short-term investments and derivative contracts are primarily made using major banks and only made with counterparties meeting certain credit-worthiness criteria. Credit risk for trade and other accounts receivable is managed through established credit monitoring activities. Customer credit limits are established and monitored and ongoing evaluations of key customer financial condition are performed. In certain market areas, the Company has undertaken additional measures to reduce credit risk, including credit insurance, letters of credit and prepayments. At December 31, 2010 approximately 59% of trade accounts receivable were covered under these additional measures. Bad debt expense of $nil (2009 – $1.6 million) was recorded for the year. The ageing analysis of trade accounts receivable is presented below:

| | 2010 | 2009 |
|---|---|---|
| Trade accounts receivable — gross | | |
| Current | $ 166.7 | $ 133.0 |
| Past due 1 to 30 days | 35.6 | 40.7 |
| Past due 31 to 60 days | 1.0 | 1.0 |
| Past due over 60 days | 3.3 | 0.3 |
| | 206.6 | 175.0 |
| Allowance for doubtful accounts | (0.6) | (0.5) |
| Trade accounts receivable — net | 206.0 | 174.5 |
| Other receivables | 40.0 | 26.1 |
| Accounts receivable | $ 246.0 | $ 200.6 |

*Liquidity*

The Company manages liquidity by maintaining adequate cash and short-term investment balances and by having appropriate lines of credit available. In addition, the Company regularly monitors and reviews both actual and forecasted cash flows. Refinancing risks are managed by ensuring long-term debt has a balanced maturity schedule where possible.

(in millions of Canadian dollars)

The following table summarizes the aggregate amount of contractual future cash outflows for long-term debt:

| | 2011 | 2012 | 2013 | 2014 | 2015 | There-after | Total |
|---|---|---|---|---|---|---|---|
| Long-term debt (note 8) | $ 0.3 | $ 0.3 | $ 0.3 | $ 298.7 | $ 0.3 | $ 1.2 | $ 301.1 |
| Interest on debt (1) | 16.4 | 16.3 | 16.3 | 13.0 | 0.1 | 0.2 | 62.3 |
| | $ 16.7 | $ 16.6 | $ 16.6 | $ 311.7 | $ 0.4 | $ 1.4 | $ 363.4 |

(1) Assumes debt level, foreign exchange rate and floating interest rates remain at balance sheet date levels and rates.

*Interest rates*

Interest rate risk relates mainly to cash and short-term investments and floating rate debt. The general practice of the Company is to fund its long-term capital with debt at fixed rates and various maturities. In addition, the Company has revolving lines of credit available that bear interest at floating rates on amounts drawn.

At December 31, 2010, with other variables unchanged, a 1% change in interest rates would not have a significant impact on earnings or other comprehensive earnings.

## 19. Capital disclosures

The Company's business is cyclical and is subject to significant changes in cash flow over the business cycle. In addition, financial performance can be materially influenced by changes in product prices and the relative values of the Canadian and US dollar. The Company's objective in managing capital is to ensure adequate liquidity and financial flexibility at all times, particularly at the bottom of the business cycle and in a strong Canadian dollar environment.

The Company's main policy relating to capital management is to maintain a strong balance sheet and otherwise meet financial tests that are commonly applied by rating agencies for investment grade issuers of public debt. The Company's debt is currently rated at below investment grade by major rating agencies primarily due to the poor economic fundamentals of the North American forest products industry. The Company believes that the goal of returning to an investment grade rating is an appropriately conservative approach in the context of the Company's cyclical business.

The Company monitors and assesses its financial performance in order to ensure that its net debt levels are prudent taking into account the anticipated direction of the business cycle. When financing acquisitions, the Company combines debt and equity financing in a proportion that is intended to maintain an investment grade rating for debt throughout the cycle. Long-term debt repayments are arranged, where possible, on a staggered basis that takes into account the uneven nature of anticipated cash flows. The Company has also established committed revolving lines of credit that provide liquidity and flexibility when capital markets are restricted.

One key measurement used by the Company to monitor its capital position is net debt to total capital, calculated as follows at December 31:

| | **2010** | 2009 |
|---|---|---|
| Net debt | | |
| Cash and short-term investments | **$ (163.1)** | $ (12.0) |
| Cheques issued in excess of funds on deposit | **2.4** | 21.8 |
| Operating loans | **8.8** | 78.7 |
| Current portion of long-term debt | **0.3** | 100.3 |
| Long-term debt | **299.5** | 315.9 |
| | **147.9** | 504.7 |
| Shareholders' equity | **1,765.2** | 1,618.2 |
| Total capital | **$ 1,913.1** | $ 2,122.9 |
| Net debt to total capital | **8%** | 24% |

## 20. Segmented information

The segmentation of manufacturing operations into lumber, panels and pulp and paper is based on a number of factors, including similarities in products, production processes and economic characteristics. Transactions between segments are at market prices and on normal business terms. The accounting policies of each segment are those described in note 1.

| **2010** | Lumber | Panels | Pulp & paper | Corporate and other | Consolidated |
|---|---|---|---|---|---|
| Sales at market prices | | | | | |
| To external customers | $ 1,621.4 | $ 401.2 | $ 863.3 | $ — | $ 2,885.9 |
| To other segments | 93.6 | 8.2 | — | — | |
| | $ 1,715.0 | $ 409.4 | $ 863.3 | $ — | |
| EBITDA[1] | $ 228.4 | $ 57.0 | $ 187.2 | $ (34.7) | $ 437.9 |
| Amortization | (103.2) | (19.9) | (55.0) | (3.1) | (181.2) |
| Operating earnings | 125.2 | 37.1 | 132.2 | (37.8) | 256.7 |
| Interest expense — net | (16.7) | (2.8) | (7.2) | 0.1 | (26.6) |
| Exchange gain on long-term debt | — | — | — | 16.9 | 16.9 |
| Other income (expense) | (0.2) | (1.0) | (7.5) | 0.3 | (8.4) |
| Earnings from continuing operations before income taxes | $ 108.3 | $ 33.3 | $ 117.5 | $ (20.5) | $ 238.6 |
| Total capital employed [1] | $ 1,364.2 | $ 294.0 | $ 589.6 | $ 200.9 | $ 2,448.7 |
| Total assets before goodwill | $ 1,292.9 | $ 276.8 | $ 651.7 | $ 329.9 | $ 2,551.3 |
| Goodwill | 217.6 | 46.1 | — | — | 263.7 |
| Total assets | $ 1,510.5 | $ 322.9 | $ 651.7 | $ 329.9 | $ 2,815.0 |
| Capital expenditures from continuing operations | $ 46.9 | $ 1.5 | $ 7.0 | $ 0.9 | $ 56.3 |

[1] **Non GAAP measures:**

a) EBITDA is defined as operating earnings plus amortization and asset impairments.

b) Capital employed is defined as total assets less current non-interest bearing liabilities at year-end.

| 2009 | Lumber | Panels | Pulp & paper | Corporate and other | Consolidated |
|---|---|---|---|---|---|
| Sales at market prices | | | | | |
| To external customers | $ 1,285.0 | $ 390.4 | $ 677.1 | $ — | $ 2,352.5 |
| To other segments | 95.3 | 6.7 | — | — | |
| | $ 1,380.3 | $ 397.1 | $ 677.1 | $ — | |
| EBITDA[1] | $ (31.3) | $ 48.3 | $ 60.2 | $ 3.1 | $ 80.3 |
| Amortization | (141.3) | (34.6) | (65.3) | (3.5) | (244.7) |
| Asset impairments | (16.9) | — | — | — | (16.9) |
| Operating earnings | (189.5) | 13.7 | (5.1) | (0.4) | (181.3) |
| Interest income (expense) — net | (18.1) | (3.0) | (6.4) | 1.0 | (26.5) |
| Exchange gain on long-term debt | — | — | — | 50.1 | 50.1 |
| Other income (expense) | 3.5 | (0.9) | (5.4) | (0.9) | (3.7) |
| Earnings from continuing operations before income taxes | $ (204.1) | $ 9.8 | $ (16.9) | $ 49.8 | $ (161.4) |
| Total capital employed[1] | $ 1,383.2 | $ 306.8 | $ 631.4 | $ 175.8 | $ 2,497.2 |
| Total assets before goodwill | $ 1,291.2 | $ 288.9 | $ 720.3 | $ 249.0 | $ 2,549.4 |
| Goodwill | 217.6 | 46.1 | — | — | 263.7 |
| Total assets | $ 1,508.8 | $ 335.0 | $ 720.3 | $ 249.0 | $ 2,813.1 |
| Capital expenditures from continuing operations | $ 9.7 | $ 1.1 | $ 6.2 | $ 0.8 | $ 17.8 |

[1] **Non GAAP measures:**

a) EBITDA is defined as operating earnings plus amortization and asset impairments.

b) Capital employed is defined as total assets less current non-interest bearing liabilities at year-end.

(in millions of Canadian dollars)

The geographic distribution of property, plant, equipment, timber and goodwill and external sales is as follows:

| | Property, plant, equipment, timber and goodwill by geographic area | | Sales by geographic area(2) | |
|---|---|---|---|---|
| | **2010** | 2009 | **2010** | 2009 |
| Canada | **$ 1,574.4** | $ 1,657.1 | **$ 704.1** | $ 594.3 |
| United States | **191.1** | 230.7 | **1,409.8** | 1,161.1 |
| China | **–** | – | **354.3** | 274.4 |
| Other Asia | **–** | – | **281.8** | 213.4 |
| Other | **–** | – | **135.9** | 109.3 |
| | **$ 1,765.5** | $ 1,887.8 | **$ 2,885.9** | $ 2,352.5 |

(2) Sales are attributed to areas based on the location of product delivery by the Company.

## 21. Contingency

On January 18, 2011 the United States requested arbitration with Canada under the provisions of the Softwood Lumber Agreement ("SLA") over its concern that the province of British Columbia ("B.C.") is charging too low a price for certain timber harvested on public lands in the B.C. interior.

The Company believes that Canada and B.C. are complying with their obligations under the SLA and intends to cooperate fully with the B.C. and Canadian governments in defending this claim. The results of the arbitration process are not determinable at this point in time and accordingly no provision has been recorded by the Company.