# RESPONSIBILITY OF MANAGEMENT

The management of West Fraser Timber Co. Ltd. ("West Fraser", "we", "us" or "our") is responsible for the preparation, integrity, objectivity and reliability of the consolidated financial statements. The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and necessarily include amounts that represent the best estimates and judgments of management.

We maintain 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 the appropriate authorization and financial records are accurate and reliable.

Our independent auditor, which is appointed by the shareholders upon the recommendation of the Audit Committee and the Board of Directors, has completed its audit of the consolidated financial statements in accordance with generally accepted auditing standards in Canada and its 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 West Fraser. The Audit Committee meets regularly with representatives of management and of the auditor to review the consolidated financial statements and matters relating to the audit. The auditor has 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.

**Ted Seraphim**
President and
Chief Executive Officer

**Larry Hughes**
Vice-President, Finance
and Chief Financial Officer

February 13, 2014

# INDEPENDENT AUDITOR'S 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, 2013 and December 31, 2012 and the consolidated statements of earnings and comprehensive earnings, changes in shareholders' equity and cash flows for the years then ended, and the related notes, which comprise 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, 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, 2013 and December 31, 2012 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

**Chartered Accountants**

Vancouver, British Columbia

February 13, 2014

# CONSOLIDATED BALANCE SHEETS

**AS AT DECEMBER 31, 2013 AND 2012**

(IN MILLIONS OF CANADIAN DOLLARS, EXCEPT WHERE INDICATED)

| | 2013 | 2012 |
|---|---|---|
| **ASSETS** | | |
| **Current assets** | | |
| Cash and short-term investments (note 7) | $ 162 | $ 102 |
| Receivables (note 27) | 279 | 251 |
| Inventories (note 8) | 519 | 459 |
| Prepaid expenses | 11 | 11 |
| | 971 | 823 |
| **Property, plant and equipment** (note 9) | 1,144 | 959 |
| **Timber licences** (note 10) | 489 | 496 |
| **Goodwill and other intangibles** (note 11) | 321 | 330 |
| **Other assets** (note 12) | 83 | 24 |
| **Deferred income tax assets** (note 22) | 96 | — |
| | $ 3,104 | $ 2,632 |
| **LIABILITIES** | | |
| **Current liabilities** | | |
| Payables and accrued liabilities (note 13) | $ 385 | $ 322 |
| Income taxes payable | 30 | 20 |
| Reforestation and decommissioning obligations (note 14) | 39 | 43 |
| Current portion of long-term debt (note 15) | 319 | — |
| | 773 | 385 |
| **Long-term debt** (note 15) | 9 | 300 |
| **Other liabilities** (note 14) | 197 | 327 |
| **Deferred income tax liabilities** (note 22) | 178 | 128 |
| | 1,157 | 1,140 |
| **SHAREHOLDERS' EQUITY** | | |
| Share capital (note 17) | 602 | 602 |
| Accumulated other comprehensive earnings | 10 | (9) |
| Retained earnings | 1,335 | 899 |
| | 1,947 | 1,492 |
| | $ 3,104 | $ 2,632 |

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, 2013 AND 2012**

(IN MILLIONS OF CANADIAN DOLLARS, EXCEPT WHERE INDICATED)

| | | 2013 | | 2012 |
|---|---|---|---|---|
| **Sales** | $ | 3,474 | $ | 3,000 |
| **Costs and expenses** | | | | |
| Cost of products sold | | 2,260 | | 2,024 |
| Freight and other distribution costs | | 491 | | 477 |
| Export taxes | | 9 | | 48 |
| Amortization | | 160 | | 152 |
| Selling, general and administration | | 131 | | 115 |
| Equity-based compensation (note 18) | | 54 | | 61 |
| Restructuring charges (note 19) | | 24 | | — |
| | | 3,129 | | 2,877 |
| **Operating earnings** | | 345 | | 123 |
| Finance expense (note 20) | | (29) | | (28) |
| Exchange gain (loss) on long-term debt | | (21) | | 7 |
| Other income (note 21) | | 22 | | — |
| **Earnings before tax** | | 317 | | 102 |
| Tax recovery (provision) (note 22) | | 32 | | (25) |
| **Earnings** | $ | 349 | $ | 77 |
| **Earnings per share** (dollars) (note 24) | | | | |
| Basic and diluted[1] | $ | 4.07 | $ | 0.90 |
| **Cash dividends per share**[1] | $ | 0.28 | $ | 0.28 |
| **Comprehensive earnings** | | | | |
| Earnings | $ | 349 | $ | 77 |
| **Other comprehensive earnings** | | | | |
| Translation gain (loss) on foreign operations[2] | | 19 | | (3) |
| Actuarial gain (loss) on post-retirement benefits[3] | | 113 | | (42) |
| **Comprehensive earnings** | $ | 481 | $ | 32 |

1. Per share amounts have been retroactively adjusted to take into account the Stock Dividend described in note 17.
2. Recycled through earnings in the event of a disposal in net investment in foreign operations.
3. Adjusted through retained earnings. Net of income tax charge of $34 million (2012 – recovery of $14 million).

# CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

**FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**

(IN MILLIONS OF CANADIAN DOLLARS, EXCEPT WHERE INDICATED)

| | SHARE CAPITAL | | TRANSLATION | | |
|---|---|---|---|---|---|
| | NUMBER OF SHARES | AMOUNT | OF FOREIGN OPERATIONS | RETAINED EARNINGS | TOTAL EQUITY |
| **Balance – December 31, 2011** | 42,846,113 | $ 601 | $ (6) | $ 888 | $ 1,483 |
| **Changes in Shareholders' Equity for 2012** | | | | | |
| Translation loss on foreign operations | — | — | (3) | — | (3) |
| Actuarial loss on post-retirement benefits | — | — | — | (42) | (42) |
| Issuance of Common shares | 16,607 | 1 | — | — | 1 |
| Earnings for the year | — | — | — | 77 | 77 |
| Dividends | — | — | — | (24) | (24) |
| **Balance – December 31, 2012** | 42,862,720 | 602 | (9) | 899 | 1,492 |
| **Changes in Shareholders' Equity for 2013** | | | | | |
| Translation gain on foreign operations | **—** | **—** | **19** | **—** | **19** |
| Actuarial gain on post-retirement benefits | **—** | **—** | **—** | **113** | **113** |
| Issuance of Common shares | **5,309** | **1** | **—** | **—** | **1** |
| Common share repurchases | **(32,277)** | **(1)** | **—** | **(2)** | **(3)** |
| Earnings for the year | **—** | **—** | **—** | **349** | **349** |
| Dividends | **—** | **—** | **—** | **(24)** | **(24)** |
| **Balance – December 31, 2013** | **42,835,752** | **$ 602** | **$ 10** | **$ 1,335** | **$ 1,947** |

# CONSOLIDATED STATEMENTS OF CASH FLOWS

**FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**

(IN MILLIONS OF CANADIAN DOLLARS, EXCEPT WHERE INDICATED)

| | 2013 | 2012 |
|---|---|---|
| **Operating activities** | | |
| Earnings | $ 349 | $ 77 |
| Adjustments | | |
| Amortization | 160 | 152 |
| Finance expense | 29 | 28 |
| Exchange (gain) loss on long-term debt | 21 | (7) |
| Tax (recovery) provision | (32) | 25 |
| Income taxes received (paid) | (36) | 2 |
| Post-retirement expense | 54 | 51 |
| Contributions to post-retirement benefit plans | (106) | (72) |
| Other | (7) | (11) |
| Changes in non-cash working capital | | |
| Receivables | (15) | (22) |
| Inventories | (55) | (58) |
| Prepaid expenses | — | (2) |
| Payables and accrued liabilities | 57 | 41 |
| **Cash flows from operating activities** | 419 | 204 |
| **Financing activities** | | |
| Proceeds from long-term debt | 8 | — |
| Finance expense paid | (18) | (18) |
| Dividends | (24) | (24) |
| Common share repurchases | (3) | — |
| Other | (2) | — |
| **Cash flows from financing activities** | (39) | (42) |
| **Investing activities** | | |
| Acquisition (note 6) | — | (30) |
| Additions to capital assets | (338) | (159) |
| Government assistance (note 26) | 11 | 51 |
| Proceeds from disposal of capital assets | 2 | 9 |
| Other | (1) | 1 |
| **Cash flows from investing activities** | (326) | (128) |
| **Increase in cash** | 54 | 34 |
| **Foreign exchange effect on cash** | 6 | — |
| **Cash – beginning of year** | 102 | 68 |
| **Cash – end of year** | $ 162 | $ 102 |

# INDEX OF NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**


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# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**

(IN MILLIONS OF CANADIAN DOLLARS, EXCEPT WHERE INDICATED)

## 1. NATURE OF OPERATIONS

West Fraser Timber Co. Ltd. ("West Fraser", "we", "us" or "our") is an integrated wood products company producing lumber, wood chips, LVL, MDF, plywood, pulp and newsprint with facilities in western Canada and the southern United States. Our executive office is located at 858 Beatty Street, Suite 501, Vancouver, British Columbia. West Fraser was formed by articles of amalgamation under the *Business Corporations Act* (British Columbia) and is registered in British Columbia, Canada. Our Common shares are listed for trading on the Toronto Stock Exchange under the symbol WFT.

## 2. STATEMENT OF COMPLIANCE

These consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board and were authorized for publication by our Board of Directors on February 13, 2014.

## 3. SIGNIFICANT ACCOUNTING POLICIES

### Basis of measurement

Our consolidated financial statements have been prepared on the historical cost basis, except for the following significant items:

- Derivative financial instruments which are measured at fair value;
- Share option liability which is measured using the Black-Scholes valuation model;
- Reforestation and decommissioning obligations which are measured at the present value of expected future cash flows required to discharge those obligations; and
- Post-retirement benefits which are actuarially determined, with plan assets measured at fair value and accrued benefit obligations measured using the projected unit credit method.

### Basis of consolidation

These consolidated financial statements include the accounts of West Fraser and its wholly-owned subsidiaries after elimination of intercompany transactions and balances. Principal operating subsidiaries are West Fraser Mills Ltd., West Fraser, Inc., Blue Ridge Lumber Inc., Sundre Forest Products Inc. and West Fraser Newsprint Ltd.

Our 50% joint operations, Alberta Newsprint Company and Cariboo Pulp & Paper Company, are accounted for by the proportionate consolidation method.

### Financial instruments

Our financial assets are categorized as loans and receivables and our financial liabilities are categorized as other financial liabilities. All financial assets and liabilities, except for derivatives, are initially measured at fair value and subsequently measured at amortized cost using the effective interest rate method. Derivatives are measured at fair value through earnings with changes reflected in other income. A list of our financial assets and liabilities is included in note 27.

Deferred financing charges are amortized over the life of the associated debt.

### Use of estimates

The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Significant areas requiring estimates include recoverability of long-lived assets and goodwill, reforestation and decommissioning obligations, employee future benefits, equity-based compensation, income taxes and litigation. Actual amounts could differ materially from these and other estimates, the impact of which would be recorded in future periods.

### 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**

West Fraser's functional and presentation currency is Canadian dollars.

*U.S. operations*

Assets and liabilities of our U.S. operations have a functional currency of U.S. dollars and are translated at the period-end exchange rate. Revenues and expenses are translated at average exchange rates during the reporting period. The resulting unrealized translation gains or losses are included in other comprehensive earnings.

*Translation of other foreign currency balances and transactions*

Monetary assets and liabilities denominated in foreign currencies, including long-term debt, are translated at the period-end exchange rate. Income and expense items are translated at the average or transaction date exchange rates during the reporting period. The resulting translation gains or losses are included in other income.

**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 and equipment**

Property, plant and equipment are stated at historical cost, less accumulated amortization and impairment losses. Expenditures for additions and improvements are capitalized. Borrowing costs are capitalized when the asset construction period exceeds 12 months and the borrowing costs are directly attributable to 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 included 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 | 6 – 20 years |
| Fixtures, mobile and other equipment | 3 – 10 years |
| Roads | Not exceeding 40 years |
| Major maintenance shutdowns | 12 to 36 months |

**Timber licences and other intangibles**

Timber licences and other intangible assets are stated at historical cost, less accumulated amortization and impairment losses, and are amortized on a straight-line basis over their estimated useful lives as follows:

| | |
|---|---|
| Timber licences | 40 years |
| Power purchase agreement | Over the life of the agreement |
| Software | 3 – 5 years |
| Non-replaceable timber rights | As timber is logged |

**Impairment of property, plant, equipment, timber licences and other intangibles**

We review property, plant, equipment, timber licences and other intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be fully recoverable. For the purpose of impairment testing, property, plant, equipment, timber licences and other intangible assets are separated into cash generating units ("CGU"). We have identified each of our mills as a CGU for impairment testing of property, plant, equipment and other intangibles. Timber licences are tested for impairment by combining CGUs within the economic area of the related licence.

Recoverability is assessed by comparing the CGU carrying amount to the discounted estimated net future cash flows the assets are expected to generate. If the carrying amount exceeds the discounted estimated net future cash flows, the assets of the CGU are written down to the higher of fair value less costs to sell and value-in-use (being the present value of the estimated net future cash flows of the relevant asset or CGU).

Estimated net future cash flows are based on several assumptions concerning future circumstances including selling prices of products, U.S./Canadian dollar exchange rates, production rates, input costs and capital requirements. The estimated net future cash flows are discounted at rates reflective of market risk.

Where an impairment loss subsequently reverses, the carrying amount of the asset or CGU is increased to the lesser of the revised estimate of its recoverable amount and the carrying amount that would have been recorded had no impairment loss been previously recognized.

### 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 its CGU to the underlying carrying amount of the CGU's net assets, including goodwill. When the carrying amount of the CGU exceeds its fair value, the fair value of the CGU's goodwill is compared with its carrying amount. An impairment loss is recognized for any excess of the carrying value of goodwill over its fair value.

### Reforestation and decommissioning obligations

Timber is harvested under various timber licences that require us to conduct reforestation. Future reforestation obligations are measured at the present value of the expenditures expected to be required to settle the obligations and are accrued and charged to earnings when timber is harvested. The reforestation obligation is reviewed periodically and changes to estimates are credited or charged to earnings.

We record the present value of a liability for decommissioning obligations in the period that a reasonable estimate can be made. The present value of the liability is added to the carrying amount of the associated asset and amortized over its useful life or, if there is no associated asset, it is expensed. Decommissioning obligations are reviewed annually and changes to estimates result in an adjustment of the carrying amount of the associated asset or, where there is no asset, they are credited or charged to earnings.

Reforestation and decommissioning obligations are discounted at the risk-free rate at the balance sheet date and accreted over time through periodic charges to earnings. The liabilities are reduced by actual costs of settlement.

### Government assistance

Government assistance received that relates to the construction of manufacturing assets is applied to reduce the cost of those assets. Government assistance received that relates to operational expenses is applied to reduce the amount charged to earnings for the operating item.

### Equity-based compensation

West Fraser'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. We estimate the fair value of outstanding options using the Black-Scholes valuation model at each balance sheet date and record the resulting expense or recovery, over the vesting period, through a charge to earnings. The vesting period over which the expense or recovery is recorded is the lesser of five years from the date the option was granted and the time period until the option holder reaches eligible retirement age. If the option holder is eligible to retire, the expense or recovery is charged to earnings immediately.

If an option holder elects to purchase Common shares, both the exercise price and the accrued liability are credited to shareholders' equity.

### Post-retirement benefits

We record a post-retirement asset or liability for our employee defined benefit pension and other retirement benefit plans by netting our plan assets with our plan obligations, on a plan-by-plan basis.

The cost of defined benefit pensions and other retirement benefits earned by employees is actuarially determined using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using market yields from high quality Canadian corporate bonds with cash flows that approximate expected benefit payments at the balance sheet date. Plan assets are valued at fair value at each balance sheet date.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive earnings in the period in which they arise.

Past service costs arising from plan amendments are recognized immediately.

The finance amount on net post-retirement balances is classified as finance expense.

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

### Income taxes

The tax expense for the period is comprised of current and deferred tax. Tax is recognized in the statement of earnings, except to the extent that it relates to items recognized in other comprehensive earnings in which case it is recognized in other comprehensive earnings.

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

Deferred tax assets are recognized only to the extent that it is probable that they will be realized. Deferred income tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of substantive enactment.

## 4. CHANGES IN ACCOUNTING POLICIES

We have adopted the following new and revised standards, along with any consequential amendments, effective January 1, 2013. These changes were made in accordance with the applicable transitional provisions.

*IFRS 10 – Consolidated Financial Statements*

In May 2011 IFRS 10 was issued which provides a single model to be applied in the control analysis for all investees and supersedes International Accounting Standards ("IAS") 27 – *Consolidated and Separate Financial Statements* and Standing Interpretations Committee – 12 *Consolidation – Special Purpose Entities*. The adoption of this standard did not result in any changes to our consolidation accounting.

*IFRS 11 – Joint Arrangements*

In May 2011 IFRS 11 was issued which provides guidance for determining if a joint arrangement is a joint venture or joint operation. The standard requires that joint ventures be accounted for by the equity method as opposed to the choice, previously available under IAS 31 – *Interests in Joint Ventures*, of applying the equity method or proportionate consolidation. Joint operations are required to be accounted for using the proportionate consolidation method. The adoption of this standard did not result in any changes to our joint arrangement accounting.

*IFRS 12 – Disclosure of Interests in Other Entities*

In May 2011 IFRS 12 was issued which sets out the required disclosures for companies that have adopted IFRS 10 and 11 described above. It requires disclosure of information that helps users to evaluate the nature, risks and financial effects associated with a company's interests in subsidiaries, associates and joint arrangements. These changes have been incorporated into the notes of these consolidated financial statements.

*IFRS 13 – Fair Value Measurement*

In May 2011 IFRS 13 was issued which defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. Prior to the introduction of the standard, there was no single source of guidance on fair value measurement. The adoption of IFRS 13 did not require any adjustments to our valuation techniques used to measure fair value and did not result in any measurement adjustments.

*IAS 19 – Amendment, Employee Benefits*

In June 2011 IAS 19 was amended, resulting in significant changes to the recognition and measurement of post-retirement and termination benefits. The most significant change was to replace interest cost and expected return on plan assets with a net interest amount that is calculated by applying the obligation discount rate to the net defined benefit asset or liability.

Under the standard, the net finance amount on employee future benefits can be reported in the statement of earnings as finance expense or as salaries and wages within operating earnings. We have classified these costs as finance expense.

The effect of adopting the amended standard is as follows:

| | PREVIOUS STANDARD | CHANGE | AMENDED STANDARD |
|---|---|---|---|
| **January 1 to December 31, 2013** | | | |
| Post-retirement and other long-term employee benefits expense | **$ 35** | **$ 9** | **$ 44** |
| Finance expense | **—** | **10** | **10** |
| Tax recovery | **(9)** | **(4)** | **(13)** |
| | **$ 26** | **$ 15** | **$ 41** |
| Actuarial gain on post-retirement benefits – net of tax | **$ (98)** | **$ (15)** | **$ (113)** |
| Basic and diluted earnings per share[1] | **$ 4.24** | **$ (0.17)** | **$ 4.07** |
| **January 1 to December 31, 2012** | | | |
| Post-retirement and other long-term employee benefits expense | $ 39 | $ 4 | $ 43 |
| Finance expense | — | 9 | 9 |
| Tax recovery | (10) | (3) | (13) |
| | $ 29 | $ 10 | $ 39 |
| Actuarial loss on post-retirement benefits – net of tax | $ 52 | $ (10) | $ 42 |
| Basic and diluted earnings per share[1] | $ 1.01 | $ (0.11) | $ 0.90 |

1. Per share amounts have been retroactively adjusted to take into account the Stock Dividend described in note 17.

There is no impact on balance sheet amounts resulting from the amended standard.

## 5. ACCOUNTING STANDARDS ISSUED BUT NOT YET APPLIED

*IFRS 9 – Financial Instruments*

In November 2009 IFRS 9 was issued and in October 2010 was further amended. IFRS 9 addresses classification and measurement of financial assets and replaces the multiple category and measurement models in IAS 39 – *Financial Instruments: Recognition and Measurement* for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive earnings. In December 2009 IFRS 9 was deferred. We do not expect this standard to have a significant effect on our consolidated financial statements.

There are no other standards or amendments or interpretations to existing standards issued but not yet effective that are expected to have a material impact on our consolidated financial statements.

## 6. ACQUISITION

On October 31, 2012 West Fraser acquired a sawmill and the associated timber licences located in Alberta for $30 million. We accounted for the transaction as an acquisition of a business and have allocated the purchase price based on the estimated fair value of the assets acquired and the liabilities assumed. The purchase price allocation is as follows:

| | | 2012 |
|---|---|---|
| Current assets | $ | 8 |
| Current liabilities | | (4) |
| Property, plant and equipment | | 8 |
| Timber licences | | 22 |
| Long-term liabilities | | (4) |
| Cash consideration | $ | 30 |

## 7. CASH AND SHORT-TERM INVESTMENTS

Included within cash and short-term investments is $24 million of restricted cash related to capital projects that are currently underway. The restricted cash is expected to be released within 12 months.

## 8. INVENTORIES

| | | **2013** | | 2012 |
|---|---|---|---|---|
| Logs and other raw materials | **$** | **160** | $ | 131 |
| Manufactured products | | **261** | | 235 |
| Processing materials and supplies | | **98** | | 93 |
| | **$** | **519** | $ | 459 |

Inventories at December 31, 2013 were written down by $6 million (December 31, 2012 – $3 million) to reflect net realizable value being lower than cost.

The carrying amount of inventory recorded at net realizable value was $27 million at December 31, 2013 (December 31, 2012 – $22 million), with the remaining inventory recorded at cost.

## 9. PROPERTY, PLANT AND EQUIPMENT

| | MANUFACTURING PLANT, EQUIPMENT & MACHINERY | CONSTRUCTION-IN-PROGRESS | ROADS AND BRIDGES | OTHER | TOTAL |
|---|---|---|---|---|---|
| **As at December 31, 2011** | $ 827 | $ 45 | $ 35 | $ 29 | $ 936 |
| Additions | 79 | 60 | 11 | — | 150 |
| Acquisition | 8 | — | — | — | 8 |
| Disposals | — | — | — | (4) | (4) |
| Amortization[1] | (119) | — | (8) | (1) | (128) |
| Foreign exchange | (3) | — | — | — | (3) |
| Transfers | 44 | (44) | — | — | — |
| As at December 31, 2012 | $ 836 | $ 61 | $ 38 | $ 24 | $ 959 |
| **As at December 31, 2012** | | | | | |
| Cost | $ 2,679 | $ 61 | $ 97 | $ 31 | $ 2,868 |
| Accumulated amortization | (1,843) | — | (59) | (7) | (1,909) |
| Net | $ 836 | $ 61 | $ 38 | $ 24 | $ 959 |
| As at December 31, 2012 | $ 836 | $ 61 | $ 38 | $ 24 | $ 959 |
| Additions | **147** | **165** | **10** | **—** | **322** |
| Amortization[1] | **(121)** | **—** | **(13)** | **—** | **(134)** |
| Asset impairment | **(13)** | **—** | **—** | **—** | **(13)** |
| Foreign exchange | **10** | **—** | **—** | **—** | **10** |
| Transfers | **28** | **(28)** | **—** | **—** | **—** |
| As at December 31, 2013 | **$ 887** | **$ 198** | **$ 35** | **$ 24** | **$ 1,144** |
| **As at December 31, 2013** | | | | | |
| Cost | **$ 2,845** | **$ 198** | **$ 107** | **$ 31** | **$ 3,181** |
| Accumulated amortization | **(1,958)** | **—** | **(72)** | **(7)** | **(2,037)** |
| Net | **$ 887** | **$ 198** | **$ 35** | **$ 24** | **$ 1,144** |

1. Amortization of $133 million relates to cost of products sold and $1 million relates to selling, general and administration expense (2012 – $126 million and $2 million, respectively).

## 10. TIMBER LICENCES

| | TIMBER LICENCES |
|---|---|
| **As at December 31, 2011** | $ 490 |
| Acquisition | 22 |
| Amortization[1] | (16) |
| As at December 31, 2012 | $ 496 |
| **As at December 31, 2012** | |
| Cost | $ 673 |
| Accumulated amortization | (177) |
| Net | $ 496 |
| As at December 31, 2012 | $ 496 |
| Additions | **20** |
| Amortization[1] | **(17)** |
| Disposals | **(10)** |
| As at December 31, 2013 | **$ 489** |
| **As at December 31, 2013** | |
| Cost | **$ 681** |
| Accumulated amortization | **(192)** |
| Net | **$ 489** |

1. Amortization relates to cost of products sold.

## 11. GOODWILL AND OTHER INTANGIBLES

| | GOODWILL | POWER PURCHASE AGREEMENT | OTHER | TOTAL |
|---|---|---|---|---|
| **As at December 31, 2011** | $ 264 | $ 66 | $ 6 | $ 336 |
| Additions | — | — | 2 | 2 |
| Amortization[1] | — | (7) | (1) | (8) |
| As at December 31, 2012 | $ 264 | $ 59 | $ 7 | $ 330 |
| **As at December 31, 2012** | | | | |
| Cost | $ 264 | $ 115 | $ 25 | $ 404 |
| Accumulated amortization | — | (56) | (18) | (74) |
| Net | $ 264 | $ 59 | $ 7 | $ 330 |
| As at December 31, 2012 | $ 264 | $ 59 | $ 7 | $ 330 |
| Amortization[1] | **—** | **(7)** | **(2)** | **(9)** |
| As at December 31, 2013 | **$ 264** | **$ 52** | **$ 5** | **$ 321** |
| **As at December 31, 2013** | | | | |
| Cost | **$ 264** | **$ 115** | **$ 25** | **$ 404** |
| Accumulated amortization | **—** | **(63)** | **(20)** | **(83)** |
| Net | **$ 264** | **$ 52** | **$ 5** | **$ 321** |

1. Amortization of $8 million relates to cost of products sold and $1 million relates to selling, general and administration expense (2012 – $7 million and $1 million, respectively).

### Goodwill

We have attributed $218 million of goodwill to a CGU made up of our Canadian lumber operations and $46 million of goodwill to a CGU made up of our plywood and LVL operations.

For the purpose of the annual impairment test of goodwill, the fair value of CGUs has been determined based on value-in-use calculations. These calculations use pre-tax cash flow projections based on the 2014 operating plan, a forecast of 2015 and 2016 and trend level earnings for subsequent years, all approved by management. Assumptions were developed by management based on industry sources, including Forest Economic Advisors, LLC, Resource Information Systems, Inc., and other industry analysts, taking into account management's best estimates.

### Power purchase agreement

West Fraser has an interest in a power purchase agreement to acquire a portion of the electricity generated from a power plant in Alberta at substantially predetermined prices. Our share of electricity capacity to 2020 is expected to be approximately 115 megawatts per year. We sell the electricity acquired at prevailing market prices at the same time as our Alberta operations purchase electricity at prevailing market prices. The cost of the power purchase agreement is amortized over its term.

## 12. OTHER ASSETS

| | 2013 | 2012 |
|---|---|---|
| Post-retirement (note 16) | **$ 72** | $ 14 |
| Deferred financing costs on lines of credit | **4** | 4 |
| Other | **7** | 6 |
| | **$ 83** | $ 24 |

## 13. PAYABLES AND ACCRUED LIABILITIES

| | | 2013 | | 2012 |
|---|---|---|---|---|
| Trade accounts | **$** | **188** | $ | 163 |
| Equity-based compensation | | **98** | | 80 |
| Compensation | | **54** | | 47 |
| Severance | | **10** | | — |
| Dividends | | **6** | | — |
| Interest | | **4** | | 4 |
| Other | | **25** | | 28 |
| | **$** | **385** | $ | 322 |

## 14. OTHER LIABILITIES

| | | 2013 | | 2012 |
|---|---|---|---|---|
| Post-retirement (note 16) | **$** | **82** | $ | 215 |
| Reforestation | | **66** | | 69 |
| Decommissioning | | **22** | | 16 |
| Other | | **27** | | 27 |
| | **$** | **197** | $ | 327 |

### Reforestation and decommissioning obligations

Reforestation and decommissioning obligations relate to our responsibility for reforestation under various timber licences, landfill closures and other site remediation costs.

Changes in reforestation and decommissioning obligations are as follows:

| | Reforestation | | | | Decommissioning | | | |
|---|---|---|---|---|---|---|---|---|
| | | 2013 | | 2012 | | 2013 | | 2012 |
| Beginning of year | **$** | **112** | $ | 111 | **$** | **16** | $ | 15 |
| Liabilities recognized | | **39** | | 42 | | **—** | | — |
| Liabilities settled | | **(48)** | | (46) | | **—** | | — |
| Acquired obligation | | **—** | | 4 | | **—** | | — |
| Change in estimates | | **2** | | 1 | | **6** | | 1 |
| End of year | | **105** | | 112 | | **22** | | 16 |
| Less: current portion | | **(39)** | | (43) | | **—** | | — |
| | **$** | **66** | $ | 69 | **$** | **22** | $ | 16 |

The total undiscounted amount of the estimated cash flows required to satisfy these obligations is $138 million (2012 – $136 million). The cash flows have been discounted using interest rates ranging from 1.13% to 1.95% (2012 – 1.14% to 1.38%).

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 33 years.

## 15. LONG-TERM DEBT AND OPERATING LOANS

### Long-term debt

| | | 2013 | | 2012 |
|---|---|---|---|---|
| US$300 million senior notes due October 2014; interest at 5.2% | **$** | **319** | $ | 299 |
| US$8 million note payable due October 2020; interest at 2% | | **8** | | — |
| Note payable due in instalments to 2020; interest at 5.5% | | **2** | | 2 |
| | | **329** | | 301 |
| Current portion | | **(319)** | | — |
| Deferred financing costs | | **(1)** | | (1) |
| | **$** | **9** | $ | 300 |

Required principal repayments are disclosed in note 27.

**Operating loans**

We have $530 million in revolving lines of credit which were undrawn as at December 31, 2013 (December 31, 2012 – undrawn). Deferred financing costs related to these lines of $4 million are included in other assets at December 31, 2013 (December 31, 2012 – $4 million).

In September 2013, our $500 million revolving line of credit was extended until September 30, 2018. In addition, we have a $25 million demand line of credit dedicated to letters of credit and a $5 million demand line of credit dedicated to a jointly owned newsprint operation. Interest on the three facilities is payable at floating rates based on Prime, U.S. base, Bankers' Acceptances or LIBOR at our option. As at December 31, 2013, letters of credit in the amount of $46 million have been issued under these facilities.

In April 2013, the security on our assets was removed following a rating upgrade to investment grade by one of our external debt rating agencies. The result is that all debt is unsecured except the $5 million joint operation demand line of credit, which is secured by that joint operation's current assets.

## 16. POST-RETIREMENT BENEFITS

We maintain defined benefit and defined contribution pension plans covering a majority of our employees. The defined benefit plans generally do not require employee contributions and provide a guaranteed level of pension payable for life based either on length of service or on earnings and length of service, and in most cases do not increase after commencement of retirement.

The defined benefit pension plans are operated in Canada and the U.S. under broadly similar regulatory frameworks. The majority are funded arrangements where benefit payments are made from plan assets which are held in trust. Responsibility for the governance of the plans, including investment and contribution decisions, resides with our pension committee which reports to the Board of Directors. For the registered defined benefit pension plans, regulations set minimum requirements for contributions for benefit accruals and the funding of deficits.

The actual return on plan assets is a gain of $153 million for the year ended December 31, 2013 (2012 – $73 million).

The total pension expense for the defined benefit plans is $49 million (2012 – $46 million). In 2013 we made contributions of $92 million (2012 – $59 million). We expect to contribute approximately $40 million to our defined benefit pension plans during 2014. We also provide group life insurance, medical and extended health benefits to certain employee groups, for which we contributed $3 million (2012 – $3 million).

The total pension expense and funding contributions for the defined contribution pension plans is $11 million (2012 – $10 million).

Our defined benefit pension plan obligations are either wholly or partially funded and our other retirement benefit plans continue to be unfunded. The status of the defined benefit pension plans and other retirement benefit plans, in aggregate, is as follows:

| | DEFINED BENEFIT PENSION PLANS | | OTHER RETIREMENT BENEFIT PLANS | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| **Accrued benefit obligations** | | | | |
| Benefit obligations – opening | **$ 1,168** | $ 1,049 | **$ 51** | $ 49 |
| Current service cost | **42** | 40 | **1** | 1 |
| Finance cost on obligation | **54** | 53 | **2** | 2 |
| Benefits paid | **(57)** | (52) | **(3)** | (3) |
| Actuarial (gain) loss due to change in discount rate | **(43)** | 83 | **(1)** | 2 |
| Actuarial (gain) due to other | **—** | (4) | **(2)** | — |
| Other | **—** | (1) | **—** | — |
| Benefit obligations – ending | **$ 1,164** | $ 1,168 | **$ 48** | $ 51 |
| **Plan assets** | | | | |
| Fair value – opening | **$ 1,018** | $ 939 | **$ —** | $ — |
| Finance income on plan assets | **47** | 47 | **—** | — |
| Actuarial gain due to returns on plan assets being higher than finance income | **106** | 26 | **—** | — |
| Employer contributions | **92** | 59 | **3** | 3 |
| Benefits paid | **(57)** | (52) | **(3)** | (3) |
| Other | **1** | (1) | **—** | — |
| Fair value – ending | **$ 1,207** | $ 1,018 | **$ —** | $ — |
| **Funded status**[1] | | | | |
| Post-retirement assets | **$ 77** | $ 14 | **$ —** | $ — |
| Actuarial loss due to impact of minimum funding requirement [2] | **(5)** | — | **—** | — |
| Post-retirement assets (note 12) | **72** | 14 | **—** | — |
| Post-retirement liabilities (note 14) | **(34)** | (164) | **(48)** | (51) |
| | **$ 38** | $ (150) | **$ (48)** | $ (51) |

1. Plans in a surplus position are classified as assets and plans in a deficit position are shown as liabilities on the balance sheet.
2. Some of our plans have a surplus that is not recognized on the basis that future economic benefits may not be available to us in the form of a reduction in future contributions or a cash refund.

| | DEFINED BENEFIT PENSION PLANS | | OTHER RETIREMENT BENEFIT PLANS | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| **Expense** | | | | |
| Current service cost | **$ 42** | $ 40 | **$ 1** | $ 1 |
| Net finance expense | **7** | 6 | **2** | 2 |
| | **$ 49** | $ 46 | **$ 3** | $ 3 |

**Assumptions and sensitivities**

The weighted average duration of the defined benefit pension obligations is 15 years. The expected maturity analysis of the undiscounted defined benefit pension plans at December 31, 2013 is as follows:

| | 2014 | 2015 | 2016 TO 2018 | THEREAFTER | TOTAL |
|---|---|---|---|---|---|
| Defined benefit pension plans | $ 57 | $ 57 | $ 174 | $ 2,214 | $ 2,502 |

The estimation of post-retirement benefit obligations involves a high degree of judgment for matters such as discount rate, employee service periods, compensation escalation rates, expected retirement ages of employees, expected health-care costs and other variable factors. These estimates are reviewed annually with independent actuaries. The significant actuarial assumptions used to determine our balance sheet date post-retirement assets and liabilities and our post-retirement benefit plan expenses are as follows:

| | DEFINED BENEFIT PENSION PLANS | | OTHER RETIREMENT BENEFIT PLANS | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| Benefit obligations: | | | | |
| Discount rate | **4.75%** | 4.50% | **4.75%** | 4.50% |
| Future compensation rate increase | **3.50%** | 3.50% | **n/a** | n/a |
| Benefit expense: | | | | |
| Discount rate – beginning of year | **4.50%** | 5.00% | **4.50%** | 5.00% |
| Future compensation rate increase | **3.50%** | 3.50% | **n/a** | n/a |

Health-care benefit costs, shown under other retirement benefit plans, are funded on a pay-as-you-go basis. The actuarial assumptions for extended health-care costs are estimated to increase 10% per year for two years, grading down 0.5% per year for years three to twelve, to 5% per year thereafter. The actuarial assumptions for medical service plan costs are estimated to increase by 4% per year.

The impact of a change in these assumptions on our post-retirement obligations is as follows:

| | OBLIGATIONS |
|---|---|
| Discount rate | |
| Decrease in assumption from 4.75% to 4.25% | $ 88 |
| Increase in assumption from 4.75% to 5.25% | $ (82) |
| Rate of increase in future compensation | |
| Decrease in assumption from 3.5% to 3.0% | $ (18) |
| Increase in assumption from 3.5% to 4.0% | $ 18 |
| Health-care cost trend rates | |
| Increase in assumption by 1.0% | $ 3 |
| Decrease in assumption by 1.0% | $ (3) |

Each sensitivity has been calculated on the basis that all other variables remain constant. When calculating the sensitivity of the defined benefit obligation, the same methodology is applied as was used to generate the financial statement asset/liability.

**Assets**

The weighted average asset allocations of the defined benefit plans at December 31, by asset category, are as follows:

| | ACCEPTABLE RANGE | NORMAL POLICY | **2013** | 2012 |
|---|---|---|---|---|
| Canadian equities | 20% – 50% | 30% | **31%** | 32% |
| Foreign equities | 0% – 50% | 30% | **32%** | 28% |
| Fixed income investments | 25% – 75% | 40% | **35%** | 40% |
| Other investments | | | **2%** | — |
| | | | **100%** | 100% |

### Risk management practices

The defined benefit pension plans' investments are exposed to various risks. These risks include market risk (including foreign currency risk, interest rate risk and price risk), credit risk and liquidity risk. The pension committee manages these risks in accordance with a Statement of Investment Policies, Guidelines, Objectives and Procedures of the Pension Plans Master Investment Trust. The following are some specific risk management practices employed:

- Monitoring credit exposure of counterparties;
- Monitoring adherence to asset allocation guidelines and permitted categories of investments; and
- Monitoring performance of investment managers and asset performance against benchmarks.

## 17. 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

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | NUMBER | | AMOUNT | NUMBER | | AMOUNT |
| Common | **40,554,274** | **$** | **602** | 40,281,242 | $ | 602 |
| Class B Common | **2,281,478** | | **—** | 2,581,478 | | — |
| Total Common | **42,835,752** | **$** | **602** | 42,862,720 | $ | 602 |

During 2013 300,000 (2012 – 200,000) Class B Common shares were exchanged for Common shares.

On September 12, 2013 our Board of Directors authorized the initiation of a normal course issuer bid to repurchase for cancellation up to 1,000,000 Common shares or approximately 2.5% of our issued and outstanding Common shares. The normal course issuer bid expires September 16, 2014.

In September 2013 we repurchased 32,277 Common shares at a cost of approximately $3 million.

### Stock dividend

On December 10, 2013 the Board of Directors declared a stock dividend (the "Stock Dividend") of one Common share for each issued and outstanding Common share and Class B Common share in the capital of the Company, which has the same effect as a two-for-one stock split. The Stock Dividend was paid on January 13, 2014 to shareholders of record on December 31, 2013. For comparative purposes the Stock Dividend has been applied retroactively to earlier periods so that the number of shares used to calculate earnings per share is doubled resulting in earnings per share for 2013 and prior years being half of the amount that would otherwise have been reported.

On January 13, 2014 we issued 42,835,752 Common shares pursuant to the Stock Dividend. Also on January 13, 2014 the number of options and units outstanding under our share option, phantom share, and directors' deferred share unit plans were doubled and the exercise price of outstanding share options was halved to reflect the Stock Dividend.

### 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. Certain circumstances or corporate transactions may require the approval of the holders of our Common shares and Class B Common shares on a separate class by class basis.

## 18. EQUITY-BASED COMPENSATION

West Fraser has a share option plan, a phantom share unit plan and a directors' deferred share unit plan which are described below. The compensation cost included in earnings for these plans in 2013 was a charge of $54 million (2012 – $61 million). The units and pricing information below are before any adjustments for the Stock Dividend.

### Share option plan

West Fraser has a share option plan for its officers and employees under which options may be granted to purchase up to 5,005,506 Common shares of which 287,048 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. We have recorded an expense of $44 million (2012 – $45 million) related to the share option plan.

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

| | 2013 | | 2012 | |
|---|---|---|---|---|
| | **NUMBER** | **WEIGHTED AVERAGE PRICE** | NUMBER | WEIGHTED AVERAGE PRICE |
| Outstanding – beginning of year | **1,497,152** | **$ 39.29** | 1,956,967 | $ 37.92 |
| Granted | **99,975** | **$ 81.64** | 168,470 | $ 47.35 |
| Exercised | **(338,741)** | **$ 40.78** | (628,285) | $ 37.20 |
| Outstanding – end of year | **1,258,386** | **$ 42.25** | 1,497,152 | $ 39.29 |
| Exercisable – end of year | **876,415** | **$ 37.44** | 1,051,286 | $ 38.64 |

The following table summarizes information about the share options outstanding at December 31, 2013:

| **EXERCISE PRICE RANGE** (DOLLARS) | **NUMBER OF OUTSTANDING OPTIONS** (NUMBER) | **WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE** (YEARS) | **WEIGHTED AVERAGE EXERCISE PRICE** | **NUMBER OF EXERCISABLE OPTIONS** (NUMBER) | **WEIGHTED AVERAGE EXERCISE PRICE** |
|---|---|---|---|---|---|
| $24.71 | 297,600 | 5.1 | $ 24.71 | 231,300 | $ 24.71 |
| $33.30 – $39.00 | 254,175 | 4.1 | $ 33.97 | 254,175 | $ 33.97 |
| $41.19 – $47.35 | 373,114 | 5.2 | $ 45.52 | 239,258 | $ 44.50 |
| $51.50 – $51.56 | 233,522 | 5.2 | $ 51.52 | 151,682 | $ 51.53 |
| $81.64 | 99,975 | 9.1 | $ 81.64 | — | $ — |
| | 1,258,386 | 5.3 | $ 42.25 | 876,415 | $ 37.44 |

The weighted average share price at the date of exercise for share options exercised during the year was $90.76 per share (2012 – $64.93 per share).

The accrued liability related to the share option plan, determined by applying the Black-Scholes valuation model, is $78 million at December 31, 2013 (December 31, 2012 – $51 million). The weighted average fair value of the options using the Black-Scholes valuation model was $61.72 per option at December 31, 2013 (December 31, 2012 – $33.90 per option).

The inputs to the option model are as follows:

| | **2013** | 2012 |
|---|---|---|
| Share price on balance sheet date | **$103.52** | $70.58 |
| Weighted average exercise price | **$42.25** | $39.29 |
| Expected dividend | **$0.56** | $0.56 |
| Expected volatility | **35.72%** | 38.22% |
| Weighted average interest rate | **1.21%** | 1.24% |
| Weighted average expected remaining life in years | **2.0** | 3.7 |

The expected dividend on our shares was based on the annualized dividend rate at each period-end. Expected volatility was based on five years of historical data. The interest rate for the life of the options was based on the implied yield available on government bonds with an equivalent remaining term at each period-end. Historical data was used to estimate the expected life of the options and forfeiture rates.

The intrinsic value of options issued under the share option plan at December 31, 2013 was $75 million (December 31, 2012 – $46 million). The intrinsic value is determined based on the difference between the period-end share price and the exercise price, multiplied by the sum of the related vested options plus unvested options for those holders eligible to retire.

**Phantom share unit plan**

Our phantom share unit plan is intended to supplement or, in whole or in part, replace the granting of share options as long-term incentives for officers and employees. The plan provides for two types of units which vest on the third anniversary of the grant date. A restricted share unit pays out based on the Common share price over the 20 trading days immediately preceding its vesting date (the "vesting date value"). A performance share unit pays out at a value between 0% and 200% of its vesting date value contingent upon West Fraser's performance relative to a peer group of companies over the three-year performance period. Officers and employees granted units under the plan are also entitled to additional units to reflect cash dividends paid on Common shares from the applicable grant date until payout.

We record an expense or recovery through earnings over the vesting period based on the quoted market price of our Common shares at each balance sheet date. The expense or recovery is charged over three years from the issuance date. We have recorded an expense of $7 million (2012 – $14 million) related to the phantom share unit plan. The number of units outstanding as at December 31, 2013 was 176,930 (December 31, 2012 – 337,765), including performance share units totalling 36,600 (December 31, 2012 – 72,390).

**Directors' deferred share unit plan**

We have a deferred share unit plan ("DSU Plan") which provides a structure for non-employee directors to accumulate an equity-like holding in West Fraser. The DSU Plan allows directors to participate in the growth of West Fraser by providing a deferred payment based on the value of a Common share at the time of redemption. Each director receives deferred share units ("Units") in payment of an annual equity retainer and may elect to receive Units in payment of up to 100% of other fees earned. The Units are issued based on our Common share price at the time of issue. Additional Units are issued to take into account the value of dividends paid on Common shares from the date of issue to the date of redemption. Units are redeemable only after a director retires, resigns or otherwise leaves the board. The redemption value is equal to the Common share price at the date of redemption. A holder of Units may elect to redeem Units in cash or receive Common shares having an equivalent value. The number of Units outstanding as at December 31, 2013 was 61,017 (December 31, 2012 – 71,156).

## 19. RESTRUCTURING CHARGES

On October 24, 2013 we announced our intention to permanently close our Houston, B.C. sawmill. The closure is expected to be complete in the second quarter of 2014 and the resulting restructuring charges are as follows:

| | 2013 |
|---|---|
| Asset impairment | $ 13 |
| Severance | 10 |
| Decommissioning obligations | 1 |
| | $ 24 |

## 20. FINANCE EXPENSE

| | 2013 | 2012 |
|---|---|---|
| Interest expense | $ (20) | $ (20) |
| Interest income | 1 | 1 |
| Finance expense on employee future benefits | (10) | (9) |
| | $ (29) | $ (28) |

## 21. OTHER INCOME

| | 2013 | 2012 |
|---|---|---|
| Foreign exchange gain (loss) – net | $ 10 | $ (5) |
| Gain on asset sales | 11 | 4 |
| Other – net | 1 | 1 |
| | $ 22 | $ — |

## 22. TAX PROVISION

The major components of income tax included in comprehensive earnings are as follows:

| | | 2013 | | 2012 |
|---|---|---|---|---|
| **Earnings** | | | | |
| Current tax | **$** | **(49)** | $ | (24) |
| Deferred tax | | **81** | | (1) |
| Tax recovery (provision) | **$** | **32** | $ | (25) |
| **Other comprehensive earnings** | | | | |
| Current tax on post-retirement actuarial gains and losses | **$** | **—** | $ | 4 |
| Deferred tax on post-retirement actuarial gains and losses | | **(34)** | | 10 |
| Tax recovery (provision) | **$** | **(34)** | $ | 14 |
| **Tax provision on comprehensive earnings** | **$** | **(2)** | $ | (11) |

The tax recovery (provision) differs from the amount that would have resulted from applying the Canadian statutory income tax rates to earnings before tax as follows:

| | | 2013 | | 2012 |
|---|---|---|---|---|
| Income tax expense at statutory rate of 25.75% (2012 – 25%) | **$** | **(82)** | $ | (26) |
| Non-taxable amounts | | **(12)** | | (9) |
| Rate differentials between jurisdictions and on specified activities | | **(10)** | | (1) |
| Recognized tax assets | | **140** | | 11 |
| Increase in statutory tax rate | | **(2)** | | — |
| Other | | **(2)** | | — |
| Tax recovery (provision) | **$** | **32** | $ | (25) |

Of the following components of deferred income taxes, $10 million of the deferred tax assets and $11 million of the deferred tax liabilities are expected to be recovered within 12 months:

| | | 2013 | | 2012 |
|---|---|---|---|---|
| Property, plant, equipment and intangibles | **$** | **224** | $ | 210 |
| Reforestation and decommissioning obligations | | **(28)** | | (28) |
| Post-retirement benefits | | **(24)** | | (55) |
| Tax loss carry-forwards | | **(101)** | | — |
| Other | | **11** | | 1 |
| | **$** | **82** | $ | 128 |
| Represented by | | | | |
| Deferred income tax assets | **$** | **(96)** | $ | — |
| Deferred income tax liabilities | | **178** | | 128 |
| | **$** | **82** | $ | 128 |

Deferred income tax assets of $101 million have been recognized for non-capital loss carry-forwards of $261 million that expire in various amounts in the years 2023 to 2031.

## 23. EMPLOYEE COMPENSATION

Our employee compensation expense includes salaries and wages, employee future benefits, termination costs and bonuses, where applicable. Total compensation expense is $668 million (2012 – $601 million).

Salaries, benefits and incentive compensation expense for key management (directors and officers) is $9 million (2012 – $6 million). In addition, various equity-based compensation plans are offered to key management. See note 18 for additional details.

## 24. EARNINGS PER SHARE

Basic earnings per share is 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 after adjusting for the Stock Dividend (note 17).

Diluted earnings per share is calculated based on earnings available to Common shareholders adjusted to remove the actual share option expense charged to earnings and after deducting a notional charge for share option expense assuming the use of the equity settled method, as set out below. The diluted weighted average number of shares is calculated using the treasury stock method. When earnings available to Common shareholders for diluted earnings per share are greater than earnings available to Common shareholders for basic earnings per share, the calculation is anti-dilutive and diluted earnings per share are deemed to be the same as basic earnings per share.

| | **2013** | 2012 |
|---|---|---|
| **Earnings** | | |
| Basic | **$ 349** | $ 77 |
| Share option expense | **44** | 45 |
| Equity settled share option adjustment | **(3)** | (3) |
| Diluted | **$ 390** | $ 119 |
| **Weighted average number of shares** (thousands) | | |
| Basic | **85,712** | 85,714 |
| Share options | **1,628** | 1,111 |
| Diluted | **87,340** | 86,825 |
| **Earnings per share** (dollars) | | |
| Basic and diluted | **$ 4.07** | $ 0.90 |

## 25. COMMITMENTS

### Operating leases

We are committed to make payments under certain operating leases for equipment, land, buildings and office space. Operating lease costs expensed during the year were $4 million (2012 – $4 million). The future payments required under operating leases are as follows:

| | |
|---|---|
| 2014 | $ 2 |
| 2015 | 2 |
| 2016 | 2 |
| 2017 | 1 |
| Thereafter | 6 |
| | $ 13 |

### Product purchase and sale commitments

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

### Capital commitments

Capital commitments at December 31, 2013 are $79 million.

## 26. GOVERNMENT ASSISTANCE

### Construction of manufacturing assets

Government assistance of $11 million (2012 – $51 million) was received for capital projects and recorded as a reduction to property, plant and equipment.

### Operational expenses

Government assistance of $12 million (2012 – $14 million) was recorded as a reduction to cost of products sold. The government assistance related primarily to research and development, bioenergy producer credits and apprentice tax credits.

## 27. FINANCIAL INSTRUMENTS

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

| 2013 | LOANS & RECEIVABLES | OTHER FINANCIAL LIABILITIES | CARRYING VALUE | FAIR VALUE |
|---|---|---|---|---|
| **Financial assets** | | | | |
| Cash and short-term investments | $ 162 | $ — | $ 162 | $ 162 |
| Receivables | 279 | — | 279 | 279 |
| | $ 441 | $ — | $ 441 | $ 441 |
| **Financial liabilities** | | | | |
| Payables and accrued liabilities | $ — | $ 385 | $ 385 | $ 385 |
| Long-term debt (note 15)[1] | — | 329 | 329 | 341 |
| | $ — | $ 714 | $ 714 | $ 726 |

1. The fair value of the long-term debt is based on rates available to us at December 31, 2013 for long-term debt with similar terms and remaining maturities.

| 2012 | LOANS & RECEIVABLES | OTHER FINANCIAL LIABILITIES | CARRYING VALUE | FAIR VALUE |
|---|---|---|---|---|
| **Financial assets** | | | | |
| Cash and short-term investments | $ 102 | $ — | $ 102 | $ 102 |
| Receivables | 251 | — | 251 | 251 |
| | $ 353 | $ — | $ 353 | $ 353 |
| **Financial liabilities** | | | | |
| Payables and accrued liabilities | $ — | $ 322 | $ 322 | $ 322 |
| Long-term debt (note 15)[1] | — | 301 | 301 | 313 |
| | $ — | $ 623 | $ 623 | $ 635 |

1. The fair value of the long-term debt is based on rates available to us at December 31, 2012 for long-term debt with similar terms and remaining maturities.

### b) Financial risk management

Our activities result in exposure to a variety of financial risks including risks related to currency fluctuation, credit, liquidity and interest rates.

*Currency fluctuation*

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

From time to time, we use derivatives to manage our exposure to U.S. dollar exchange fluctuations and commodity prices. We do not utilize derivative financial instruments for trading or speculative purposes.

Impact of U.S. dollar currency fluctuation

| The U.S. dollar balance sheet exposure at December 31, 2013 was as follows: | 2013 |
|---|---|
| **Canadian operations** | |
| Net working capital | US$ 189 |
| Long-term debt | (300) |
| | US$ (111) |
| **U.S. operations** | |
| Net investment | US$ 468 |

Based on these balances, with other variables unchanged, a $0.01 increase in the exchange rate for one U.S. dollar into Canadian currency would have resulted in a $1 million increase in earnings and an increase of $5 million in the translation gain on foreign operations. A $0.01 decrease in this rate would have resulted in a $1 million decrease in earnings and a decrease of $5 million in the translation gain on foreign operations.

*Credit*

Credit risk arises from the non-performance by counterparties of contractual financial obligations. Investments in 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 receivables is managed through established credit monitoring activities. Customer credit limits are established and monitored. Ongoing evaluations of key customer financial conditions are performed. In certain market areas we have undertaken additional measures to reduce credit risk including credit insurance, letters of credit and prepayments. At December 31, 2013 approximately 58% of trade accounts receivable were covered by at least some of these additional measures. We have historically experienced minimal customer defaults and, as a result, consider the credit quality of the trade accounts receivable at December 31, 2013 to be high. A bad debt recovery of $1 million (2012 – $2 million expense) was recorded for the year. The aging analysis of trade accounts receivable is presented below:

| | **2013** | 2012 |
|---|---|---|
| Trade accounts receivable – gross | | |
| Current | **$ 216** | $ 194 |
| Past due 1 to 30 days | **11** | 8 |
| Past due 31 to 60 days | **1** | 1 |
| Past due over 60 days | **1** | — |
| | **229** | 203 |
| Allowance for doubtful accounts | **—** | (1) |
| Trade accounts receivable – net | **229** | 202 |
| Other | **50** | 49 |
| Receivables | **$ 279** | $ 251 |

*Liquidity*

We manage liquidity by maintaining adequate cash and short-term investment balances and by having appropriate lines of credit available. In addition, we regularly monitor and review both actual and forecasted cash flows. Refinancing risks are managed by ensuring long-term debt has a balanced maturity schedule where possible.

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

| | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | Total |
|---|---|---|---|---|---|---|---|
| Long-term debt (note 15) | $ 319 | $ — | $ — | $ — | $ — | $ 10 | $ 329 |
| Interest on debt[1] | 13 | — | — | — | — | — | 13 |
| | $ 332 | $ — | $ — | $ — | $ — | $ 10 | $ 342 |

1. Assumes debt level, foreign exchange rate and floating interest rates remain at December 31, 2013 levels and rates.

*Interest rates on financial instruments*

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

At December 31, 2013, with other variables unchanged, a 1% change in interest rates would not have a significant impact on earnings or other comprehensive earnings.

## 28. CAPITAL DISCLOSURES

Our 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 U.S. dollar. Our 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.

Our 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. Our debt is currently rated as investment grade by three major rating agencies.

We monitor and assess our financial performance in order to ensure that net debt levels are prudent taking into account the anticipated direction of the business cycle. When financing acquisitions, we combine 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. We have also established committed revolving lines of credit that provide liquidity and flexibility when capital markets are restricted.

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

| | 2013 | 2012 |
|---|---|---|
| Net debt | | |
| Cash and short-term investments | $ (162) | $ (102) |
| Deferred financing costs | (4) | (4) |
| Long-term debt[1] | 328 | 300 |
| | 162 | 194 |
| Shareholders' Equity | 1,947 | 1,492 |
| Total capital | $ 2,109 | $ 1,686 |
| Net debt to total capital | 8% | 12% |

1. Balance sheet presentation is net of deferred financing fees, where applicable.

## 29. SEGMENT AND GEOGRAPHICAL 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 3.

| | LUMBER | PANELS | PULP & PAPER | CORPORATE & OTHER | TOTAL |
|---|---|---|---|---|---|
| **2013** | | | | | |
| Sales at market prices | | | | | |
| To external customers | $ 2,234 | $ 460 | $ 780 | $ — | $ 3,474 |
| To other segments | 81 | 7 | — | — | |
| | $ 2,315 | $ 467 | $ 780 | $ — | |
| EBITDA[1] | $ 437 | $ 43 | $ 103 | $ (54) | $ 529 |
| Amortization | (99) | (15) | (45) | (1) | (160) |
| Restructuring charges | (24) | — | — | — | (24) |
| Operating earnings | 314 | 28 | 58 | (55) | 345 |
| Finance expense | (15) | (5) | (9) | — | (29) |
| Exchange loss on long-term debt | — | — | — | (21) | (21) |
| Other income (expense) | 16 | 1 | 8 | (3) | 22 |
| Earnings before tax | $ 315 | $ 24 | $ 57 | $ (79) | $ 317 |
| Total assets | $ 2,082 | $ 293 | $ 615 | $ 114 | $ 3,104 |
| Total liabilities | $ 313 | $ 48 | $ 108 | $ 688 | $ 1,157 |
| Capital employed[1] | $ 1,939 | $ 268 | $ 544 | $ (62) | $ 2,689 |
| Capital expenditures | $ 281 | $ 5 | $ 71 | $ 1 | $ 358 |

1. Non-IFRS measures:
   a) EBITDA is defined as operating earnings plus amortization and restructuring charges.
   b) Capital employed is defined as total assets less current non interest bearing liabilities at year-end.

| | LUMBER | PANELS | PULP & PAPER | CORPORATE & OTHER | TOTAL |
|---|---|---|---|---|---|
| 2012 | | | | | |
| Sales at market prices | | | | | |
| To external customers | $ 1,783 | $ 442 | $ 775 | $ — | $ 3,000 |
| To other segments | 72 | 6 | — | — | |
| | $ 1,855 | $ 448 | $ 775 | $ — | |
| EBITDA[1] | $ 176 | $ 54 | $ 109 | $ (64) | $ 275 |
| Amortization | (86) | (16) | (47) | (3) | (152) |
| Operating earnings | 90 | 38 | 62 | (67) | 123 |
| Finance expense | (13) | (4) | (9) | (2) | (28) |
| Exchange gain on long-term debt | — | — | — | 7 | 7 |
| Other income (expense) | (4) | — | 1 | 3 | — |
| Earnings before tax | $ 73 | $ 34 | $ 54 | $ (59) | $ 102 |
| Total assets | $ 1,691 | $ 293 | $ 584 | $ 64 | $ 2,632 |
| Total liabilities | $ 279 | $ 46 | $ 110 | $ 705 | $ 1,140 |
| Capital employed[1] | $ 1,572 | $ 270 | $ 520 | $ (72) | $ 2,290 |
| Capital expenditures | $ 114 | $ 5 | $ 38 | $ 2 | $ 159 |
| Acquisition | $ 30 | $ — | $ — | $ — | $ 30 |

1. Non-IFRS measures:
   a) EBITDA is defined as operating earnings plus amortization and restructuring charges.
   b) Capital employed is defined as total assets less current non interest bearing liabilities at year-end.

The geographic distribution of non-current assets and external sales is as follows:

| | NON-CURRENT ASSETS | | SALES BY GEOGRAPHIC AREA[1] | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| Canada | **$ 1,796** | $ 1,647 | **$ 821** | $ 747 |
| United States | **337** | 162 | **1,761** | 1,435 |
| China | **—** | — | **537** | 513 |
| Other Asia | **—** | — | **263** | 201 |
| Other | **—** | — | **92** | 104 |
| | **$ 2,133** | $ 1,809 | **$ 3,474** | $ 3,000 |

1. Sales distribution is based on the location of product delivery.