Consolidated Financial Statements

December 31, 2008 and 2007

Management's Statement of Responsibility for Financial Information

The consolidated financial statements contained in this Annual Report are the responsibility of management, and have been prepared in accordance with Canadian generally accepted accounting principles. Where necessary, management has made judgements and estimates of the outcome of events and transactions, with due consideration given to materiality. Management is also responsible for all other information in the Annual Report and for ensuring that this information is consistent, where appropriate, with the information and data included in the consolidated financial statements.

The Company maintains a system of internal controls to provide reasonable assurance as to the reliability of the financial records and safeguarding of its assets. The consolidated financial statements have been examined by the Company's independent auditors, PricewaterhouseCoopers LLP, and they have issued their report thereon.

The Board of Directors is responsible for overseeing management in the performance of its responsibilities for financial reporting. The Board exercises its responsibilities through the Audit Committee which is comprised of four independent directors. The Audit Committee meets from time to time with management and the Company's independent auditors to review the financial statements and matters relating to the audit. The Company's independent auditors have full and free access to the Audit Committee. The consolidated financial statements have been reviewed by the Audit Committee, who recommended their approval by the Board of Directors.

(Signed by)

Brian McManus
President and Chief Executive Officer

(Signed by)

George T. Labelle, CA
Senior Vice-President and Chief Financial Officer

Saint-Laurent, Quebec
March 12, 2009

Auditors' Report

To the Shareholders of Stella-Jones Inc.

We have audited the consolidated balance sheet of Stella-Jones Inc. as at December 31, 2008 and the consolidated statements of shareholders' equity, earnings, comprehensive income and cash flows for the year then ended. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2008 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The consolidated financial statements as at December 31, 2007 and for the year then ended were audited and reported on by other auditors who expressed an opinion without reservation on these consolidated financial statements in their report dated March 12, 2008

(Signed by)

Montréal, Quebec
March 12, 2009

[1] Chartered accountant auditor permit No. 9986

Consolidated Balance Sheets

As at December 31, 2008 and 2007

(expressed in thousands of dollars)	2008 $	2007 $
Assets		
Current assets		
Accounts receivable (Note 6)	**41,501**	26,411
Derivative financial instruments (Note 19)	**381**	658
Inventories (Note 7)	**223,199**	138,834
Prepaid expenses	**5,910**	2,266
Income taxes receivable	**3,778**	784
Future income taxes (Note 15)	**2,338**	619
	277,107	169,572
Capital assets (Note 8)	**108,763**	73,309
Derivative financial instruments (Note 19)	**347**	274
Intangible assets (Note 9)	**10,773**	—
Goodwill (Note 5(a))	**6,367**	—
Other assets (Note 10)	**3,343**	1,344
Future income taxes (Note 15)	**846**	357
	407,546	244,856
Liabilities and Shareholders' Equity		
Current liabilities		
Bank indebtedness (Note 11)	**81,560**	39,026
Accounts payable and accrued liabilities	**28,694**	21,856
Customer deposits	**2,971**	—
Derivative financial instruments (Note 19)	**266**	—
Future income taxes (Note 15)	**118**	289
Current portion of long-term debt (Note 12)	**4,914**	4,409
Current portion of asset retirement obligations (Note 13)	**717**	751
Current portion of non-compete payable (Note 5(a))	**969**	—
	120,209	66,331
Long-term debt (Note 12)	**100,845**	43,035
Future income taxes (Note 15)	**16,625**	5,968
Asset retirement obligations (Note 13)	**577**	467
Employee future benefits (Note 16)	**1,541**	1,298
Derivative financial instruments (Note 19)	**1,303**	—
Non-compete payable (Note 5(a))	**5,334**	—
	246,434	117,099
Shareholders' equity		
Capital stock (Note 14)	**49,910**	46,023
Contributed surplus	**1,905**	4,045
Retained earnings	**105,055**	80,745
Accumulated other comprehensive income (loss)	**4,242**	(3,056)
	161,112	127,757
	407,546	244,856

Commitments and contingencies (Note 18).

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

Approved by the Board of Directors

(Signed by)
Tom A. Bruce Jones, CBE
Director

(Signed by)
Richard Bélanger, FCA
Director

Consolidated Statements of Shareholders' Equity

For the years ended December 31, 2008 and 2007

(expressed in thousands of dollars, except number of shares in thousands)	2008 **#**	2007 #
Capital stock		
Number of shares outstanding – Beginning of year	**12,341**	12,298
Stock option plan	**14**	38
Stock option agreement	**200**	—
Share purchase plan	**10**	5
Number of shares outstanding – End of year	**12,565**	12,341
	$	$
Shares outstanding – Beginning of year	**46,023**	45,473
Stock option plan	**286**	367
Stock option agreement	**3,384**	—
Share purchase plan	**217**	183
Shares outstanding – End of year	**49,910**	46,023
Contributed surplus		
Balance – Beginning of year	**4,045**	2,417
Stock-based compensation	**741**	1,716
Exercise of stock options	**(2,881)**	(88)
Balance – End of year	**1,905**	4,045
Retained earnings		
Balance – Beginning of year	**80,745**	58,004
Net earnings for the year	**28,547**	25,700
Dividends on common shares	**(4,237)**	(2,959)
Balance – End of year	**105,055**	80,745
Accumulated other comprehensive income (loss)		
Balance – Beginning of year	**(3,056)**	(73)
Adoption of new accounting standards for financial instruments, net of taxes of $280	**—**	569
Other comprehensive income (loss)	**7,298**	(3,552)
Balance – End of year	**4,242**	(3,056)
Shareholders' equity	**161,112**	127,757

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

Consolidated Statements of Earnings

For the years ended December 31, 2008 and 2007

(expressed in thousands of dollars, except earnings per common share)	2008 $	2007 $
Sales	**384,822**	269,714
Expenses (income)		
Cost of sales (Note 7)	**306,424**	202,926
Selling and administrative	**20,365**	15,858
Foreign exchange loss (gain)	**(277)**	1,472
Amortization of capital assets and intangible assets	**8,365**	5,440
Gain on disposal of capital assets	**(19)**	(42)
	334,858	225,654
Operating earnings	**49,964**	44,060
Financial expenses		
Interest on long-term debt	**6,262**	3,051
Other interest	**2,472**	2,452
	8,734	5,503
Earnings before income taxes	**41,230**	38,557
Provision for (recovery of) income taxes (Note 15)		
Current	**10,971**	13,006
Future	**1,712**	(149)
	12,683	12,857
Net earnings for the year	**28,547**	25,700
Net earnings per common share (Note 14(b))	**2.29**	2.09
Diluted net earnings per common share (Note 14(b))	**2.25**	2.03

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

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2008 and 2007

(expressed in thousands of dollars)	2008 $	2007 $
Net earnings for the year	**28,547**	25,700
Other comprehensive income (loss)		
Net change in unrealized gains (losses) on translation of financial statements of self-sustaining foreign operation	**15,003**	(3,627)
Net change in unrealized losses on translation of long-term debt designated as a hedge of net investment in self-sustaining foreign operation	**(6,482)**	—
Change in fair value of derivatives designated as cash flow hedges	**(1,142)**	2,251
Income tax recovery (expense) on change in fair value of derivatives designated as cash flow hedges	**354**	(698)
Gain on cash flow hedges reclassed to sales	**(630)**	(2,168)
Income tax recovery on gain on cash flow hedges reclassed to sales	**195**	690
	7,298	(3,552)
Comprehensive income	**35,845**	22,148

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

Consolidated Statements of Cash Flows

For the years ended December 31, 2008 and 2007

(expressed in thousands of dollars)	**2008** **$**	2007 $
Cash flows from		
Operating activities		
Net earnings for the year	**28,547**	25,700
Adjustments for		
Amortization of capital assets	**7,052**	5,440
Amortization of intangible assets	**1,313**	—
Amortization of deferred financing charges	**57**	—
Change in fair value of debt	**773**	—
Gain on disposal of capital assets	**(19)**	(42)
Employee future benefits	**243**	186
Stock-based compensation	**741**	1,716
Unrealized foreign exchange loss on long-term debt	**388**	—
Future income taxes	**1,712**	(149)
Other	**248**	587
	41,055	33,438
Changes in non-cash working capital components		
Accounts receivable	**4,135**	8,366
Inventories	**(36,996)**	(21,749)
Prepaid expenses	**(3,809)**	1,106
Accounts payable and accrued liabilities	**(7,757)**	207
Customer deposits	**2,473**	—
Income taxes receivable	**(2,473)**	(3,855)
Asset retirement obligations	**76**	(119)
	(44,351)	(16,044)
	(3,296)	17,394
Financing activities		
Increase (decrease) in bank indebtedness	**20,560**	(984)
Increase in long-term debt	**46,794**	13,332
Repayment of long-term debt	**(10,838)**	(3,722)
Proceeds from issuance of common shares	**1,006**	472
Non-compete payable	**(950)**	—
Dividends on common shares	**(4,237)**	(2,959)
	52,335	6,139
Investing activities		
Increase in other assets	**(337)**	(284)
Business acquisitions, net of cash	**(38,220)**	(17,126)
Purchase of capital assets	**(10,392)**	(6,783)
Assets held for sale	**(272)**	—
Proceeds from disposal of capital assets	**182**	660
	(49,039)	(23,533)
Net change in cash and cash equivalents during the year	**—**	—
Cash and cash equivalents – Beginning and end of year	**—**	—
Supplemental disclosures		
Interest paid	**6,998**	5,296
Income taxes paid	**13,759**	16,636

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

1. Description of the Business

Stella-Jones Inc. (the "Company") is a North American producer and marketer of industrial treated wood products, specializing in the production of railway ties and timbers as well as wood poles supplied to electrical utilities and telecommunication companies. The Company also provides treated consumer lumber products and customized services to lumber retailers and wholesalers for outdoor applications. Other products include marine and foundation pilings, construction timbers, highway guardrail posts and treated wood for bridges. The Company is incorporated under the *Canada Business Corporations Act*; its common shares are listed on the Toronto Stock Exchange.

2. Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, its wholly owned Canadian subsidiaries, Guelph Utility Pole Company Limited, I.P.B.-W.P.I. International Inc., Stella-Jones Canada Inc. (formerly Bell Pole Canada Inc.) and its wholly owned US subsidiaries, Stella-Jones U.S. Holding Corporation, Stella-Jones Corporation ("SJ Corp"), The Burke-Parsons-Bowlby Corporation ("BPB"), and Stella-Jones U.S. Finance Corporation. The consolidated accounts of Stella-Jones Canada Inc. include a 50% interest in the accounts of Kanaka Creek Pole Company Limited ("Kanaka"), a joint venture which is accounted for under the proportionate consolidation method.

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to estimates and assumptions include the estimated useful life of assets, impairment of long-lived assets, future income taxes, stock-based compensation, pension and post-retirement benefits, legal liabilities, bad debts, allowance for doubtful accounts and environmental provisions. It is possible that actual results could differ from those estimates and such differences could be material. Estimates are reviewed periodically, and as adjustments become necessary, they are reported in earnings in the period in which they become known.

Revenue Recognition

Revenue from the sale of products and services is recognized when persuasive evidence of an arrangement exists, when products are shipped to customers or the services are rendered, when the risks and rewards related to the ownership of the product are assumed by the customer, when collection is considered reasonably assured and when the sales price is fixed or determinable.

Logs are harvested from timber licences operated by the Company as part of a process to procure raw material for processing and treatment of utility poles. Logs not meeting pole-quality standards are regularly harvested and sold to third parties. Proceeds from the sale of non-pole-quality logs are included in the cost of poles sold since the production of non-pole-quality logs are a by-product of the Company's pole raw material procurement operations. Sales of non-pole-quality logs totalled $13,023,124 for the year ended December 31, 2008 (2007 – $13,373,926).

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, bank balances and short-term liquid investments with maturities of three months or less.

Inventories

Inventories of raw materials are valued at the lower of average cost and net realizable value. Finished goods are valued at the lower of average cost and net realizable value and include the cost of raw materials, direct labour and manufacturing overhead expenses.

2. Significant Accounting Policies (Continued)

Capital Assets

Capital assets are recorded at cost less accumulated amortization. Amortization is calculated on a straight-line basis using rates based on the estimated useful lives of the assets, which are generally as follows:

Buildings	20 to 40 years
Production equipment	5 to 40 years
Rolling stock	3 to 10 years
Anti-pollution equipment	10 to 20 years
Office equipment	2 to 10 years

Roads are recorded at cost less accumulated amortization, which is provided on the basis of timber volumes harvested. Amortization amounts are charged to operations based on a pro rata calculation of timber volumes harvested over the estimated volumes to be harvested in the licensed area served by the road, and are applied against the historical cost.

Cutting rights are recorded at cost less accumulated amortization, which is provided on the basis of timber volumes harvested. Amortization amounts are charged to operations based on a pro rata calculation of timber volumes harvested over the estimated volumes to be harvested during a 40-year period, and are applied against the historical cost.

Standing timber costs are recorded at cost less accumulated amortization, which is provided on the basis of timber volumes harvested. In Canada, the Company has perpetual cutting rights where planning and site preparation costs for specific geographical areas are capitalized until the harvest process can begin. Amortization amounts are charged to operations based on a pro rata calculation of timber volumes harvested over the estimated volumes to be harvested in the specific area.

Intangible Assets

Intangible assets with finite useful lives are recorded at cost and are amortized on a straight-line basis over their useful lives. The amortization method and estimate of the useful life of an intangible asset are reviewed on an annual basis:

Customer relationships	3 to 10 years
Non-compete agreements	6 years

Business Combinations and Goodwill

The Company accounts for its business combinations using the purchase method of accounting. Under this method, the Company allocates the purchase price to tangible and intangible assets acquired and liabilities assumed based on estimated fair values at the date of acquisition, with the excess of the purchase price amount being allocated to goodwill. Goodwill is not amortized and will be subject to an annual impairment test, or more frequently if events or changes in circumstances indicate that it might be impaired. Testing for impairment is accomplished mainly by determining whether the fair value of a reporting unit, based on discounted estimated cash flows, exceeds the net carrying amount of that reporting unit as at the assessment date. If the fair value is greater than the net carrying amount, no impairment is necessary. In the event that the net carrying amount exceeds the sum of the discounted estimated cash flows, a second test must be performed whereby the fair value of the reporting unit's goodwill must be estimated to determine if it is less than its net carrying amount. Fair value of goodwill is estimated in the same way as goodwill was determined at the date of the acquisition, that is, the excess of the fair value of the reporting unit over the fair value of the identifiable net assets of the reporting unit.

Impairment of Long-lived Assets

Long-lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is recognized when their carrying value exceeds the total undiscounted cash flows expected from their use and eventual disposition. Any impairment loss would be determined as the excess of the carrying value of the assets over their fair value.

2. Significant Accounting Policies (Continued)

Asset Retirement Obligations

Reforestation obligations
The *Forest Act* (British Columbia) and the *Forests Act* (Alberta) require the industry to assume the costs of reforestation on certain harvest licences. Accordingly, the Company records the fair value of the cost of reforestation in the period in which the timber is harvested, with the fair value of the liability determined with reference to the present value of the estimated future cash flows. Reforestation costs are included in the costs of current production.

Site remediation obligations
Site remediation obligations relate to the discounted present value of estimated future expenditures associated with the obligations of restoring the environmental integrity of certain properties. The Company reviews estimates of future site remediation expenditures on an ongoing basis and records any revisions, along with accretion costs on existing obligations, in other expenses.

Income Taxes

The Company applies the liability method to account for income taxes. Under this method, future income taxes at the balance sheet date are determined using the differences between the accounting and tax bases of assets and liabilities and the substantively enacted income tax rates to be in effect when these differences are expected to reverse. Future tax assets are recognized when it is more likely than not that the assets will be realized.

Employee Future Benefits

Post-retirement benefit programs
The cost of future benefits earned by employees is established by actuarial calculations using the projected benefit method pro-rated on years of service based on management's best estimate of economic and demographic assumptions.

Defined benefit pension plan
The Company accrues obligations and related costs under defined benefit pension plans, net of plan assets. The cost of pensions earned by employees is actuarially determined using the projected benefits method pro-rated on service and management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and discount rates on obligations. For the purpose of calculating the expected return on plan assets, those assets are valued at fair market value. Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment. The excess of the net actuarial gain (loss) over 10% of the greater of the benefit obligations and the fair value of plan assets is amortized over the average remaining service life of the active employees.

When the restructuring of a benefit plan gives rise to both a curtailment and a settlement of obligations, the curtailment is accounted for prior to the settlement.

Stock-based Compensation and other Stock-based Payments

The Company accounts for stock options granted to employees using the fair value method. Under this method, compensation expense for stock options granted is measured at the fair value at the grant date using the Black-Scholes valuation model and is charged to operations over the vesting period of the options granted, with a corresponding credit to contributed surplus. Any consideration paid on the exercise of stock options is credited to capital stock together with any related stock-based compensation expense included in contributed surplus.

The obligation related to the stock appreciation rights is accounted for as a liability over the period that the right is acquired, is revalued at each balance sheet date and is presented in the consolidated balance sheet under Accounts payable and accrued liabilities.

Foreign Currency Transactions

Except for self-sustaining foreign operations, revenues and expenses denominated in a foreign currency are translated by applying exchange rates in effect at the transaction date. At year-end, monetary assets and liabilities denominated in a foreign currency are translated at the rate in effect at the balance sheet date. Any resulting foreign currency translation gains or losses are included in the consolidated statement of earnings.

2. Significant Accounting Policies (Continued)

The financial statements of Stella-Jones U.S. Holding Corporation, a self-sustaining foreign operation, are translated using the rate in effect at the balance sheet date for assets and liabilities, and the average exchange rates during the year for revenues and expenses. Adjustments arising from this translation are recorded in "Accumulated other comprehensive income (loss)" in shareholders' equity.

Financial Instruments

Financial assets and financial liabilities, including derivatives, are recognized on the consolidated balance sheet when the Company becomes a party to the contractual provisions of the financial instrument or non-financial derivative contract. All financial instruments are required to be measured at fair value on initial recognition except for certain related party transactions. Measurement in subsequent periods is dependent on the classification of the financial instruments as held for trading, held to maturity, available for sale, loans and receivables, or other financial liabilities. The held-for-trading classification is applied when an entity is "trading" in an instrument. Alternatively, the standard permits that any financial instrument be irrevocably designated as held for trading. The held-to-maturity classification is applied only if the asset has specified characteristics and the entity has the ability and intent to hold the asset until maturity. The loans and receivables classification is applied for assets that are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. The available-for-sale classification is applied for all non-derivative financial assets that do not belong in the other categories. Alternatively, the standard permits that any financial asset not classified as held for trading may be designated as available for sale. Significant transaction costs related to long-term credit facilities are capitalized and amortized over the life of the instrument. Other transaction costs related to short-term credit facilities are expensed in the period they are incurred.

Financial assets and financial liabilities classified as held for trading are measured at fair value with changes in those fair values recognized in the consolidated statement of earnings. Financial assets classified as held to maturity, loans and receivables, or other financial liabilities are subsequently measured at amortized cost using the effective interest rate method of amortization. Financial assets classified as available for sale are measured at fair value with unrealized gains and losses, including changes in foreign exchange rates, being recognized in the consolidated statement of comprehensive income. Investments in equity instruments classified as available for sale that do not have a quoted market price in an active market are measured at cost.

Derivative financial instruments are recorded on the consolidated balance sheet at fair value, including those derivatives that are embedded in financial or non-financial contracts. Changes in the fair values of derivative financial instruments are recognized in the consolidated statement of earnings with the exception of foreign exchange risk management contracts and derivatives designated as effective cash flow hedges, as further described below.

For any guarantee issued that meets the definition of a guarantee pursuant to Canadian Institute of Chartered Accountants ("CICA") Accounting Guideline 14, "Disclosure of Guarantees", the inception fair value of the obligation relating to the guarantee is recognized and amortized over the term of the guarantee. It is the Company's policy to not remeasure the fair value of the financial guarantee unless it qualifies as a derivative.

The Company has implemented the following classifications:

Cash and cash equivalents are classified as assets held for trading and are measured at fair value.

Accounts receivable and notes receivable are classified as loans and receivables. After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method. For the Company, the measured amount generally corresponds to original cost unless otherwise specified.

Bank indebtedness, accounts payable and accrued liabilities, and long-term debt are classified as other financial liabilities. After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method. For the Company, the measured amount generally corresponds to original cost unless otherwise specified.

Hedging Transactions

The Company enters into foreign exchange forward contracts to limit its exposure under contracted cash inflows and outflows of US dollars. The Company also enters into interest rate swaps in order to reduce the impact of fluctuating interest rates on its short-term and long-term debt. These contracts are treated as cash flow hedges for accounting purposes and are not held for trading or speculative purposes.

2. Significant Accounting Policies (Continued)

Effective derivative financial instruments held for cash flow hedging purposes are recognized at fair value, and the changes in fair value related to the effective portion of the hedge are recognized in other comprehensive income. The changes in fair value related to the ineffective portion of the hedge are immediately recorded in the consolidated statement of earnings. The changes in fair value of foreign exchange forward contracts and interest rate swaps recognized in other comprehensive income are reclassified in the consolidated statement of earnings under sales and interest on long-term debt respectively in the periods during which the cash flows constituting the hedged item affect earnings.

When the derivative financial instrument no longer qualifies as an effective hedge, or when the hedging instrument is sold or terminated prior to maturity, if applicable, hedge accounting is discontinued prospectively. Accumulated other comprehensive income related to a foreign exchange forward contract and interest swap hedges that cease to be effective are reclassified in the consolidated statement of earnings under foreign exchange gain or loss and interest on long-term debt respectively in the periods during which the cash flows constituting the hedged item affect earnings. Furthermore, if the hedged item is sold or terminated prior to maturity, hedge accounting is discontinued, and the related accumulated other comprehensive income is then reclassified in the consolidated statement of earnings at the original maturity date of the hedged item.

Effective September 26, 2008, the Company designated a portion of its US dollar-denominated long-term debt as a hedge of its net investment in a self-sustaining foreign operation. For such debt designated as a hedge of the net investment in a self-sustaining foreign operation, exchange gains and losses are recognized in “Accumulated other comprehensive income (loss)”.

Earnings per Share

Diluted earnings per share is calculated using the treasury stock method. Under the treasury stock method, earnings per share data are computed as if the options were exercised at the beginning of the year (or at the time of issuance, if later) and as if the funds obtained from exercise were used to purchase common shares of the Company at the average market price during the year.

3. Changes in Accounting Policies

The CICA issued the following new accounting standards which were adopted by the Company effective January 1, 2008:

- Handbook Section 3031, “Inventories”, replaces Section 3030, “Inventories”. The new Section prescribes measurement of inventories at the lower of cost and net realizable value. It provides guidance on the determination of cost, prohibits use in the future of the last in, first out method, and requires reversal of previous writedowns when there is a subsequent increase in the value of inventories. It also requires greater disclosure regarding inventories and cost of sales, including accounting policies, carrying values and the amount of any inventory writedowns. The additional disclosures required as a result of the adoption of this standard are included in Note 7.

- Handbook Section 3862, “Financial Instruments – Disclosures”, describes the required disclosures for the assessment of the significance of financial instruments for the entity’s financial position and performance and of the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. This Section and Section 3863, below, replace Section 3861, “Financial Instruments – Disclosure and Presentation”. The additional disclosures required as a result of the adoption of this standard are included in Note 19.

- Handbook Section 3863, “Financial Instruments – Presentation”, establishes standards for presentation of financial instruments and non-financial derivatives. It carries forward the presentation related requirements of Section 3861. The additional disclosures required as a result of the adoption of this standard are included in Note 19.

- Handbook Section 1535, “Capital Disclosures”, establishes standards for disclosing information about an entity’s capital and how it is managed. It describes the disclosure requirements of the entity’s objectives, policies and processes for managing capital, the quantitative data relating to what the entity regards as capital, whether the entity has complied with capital requirements, and, if it has not complied, the consequences of such non-compliance. The additional disclosures required as a result of the adoption of this standard are included in Note 20.

- Handbook Section 1400, “General Standards of Financial Statement Presentation”, establishes requirements to assess and disclose the Company’s ability to continue as a going concern. The adoption of this Section did not have an impact on the Company’s consolidated financial statements.

4. Impact of Accounting Pronouncements not yet Implemented

The CICA issued the following new accounting standard which will be adopted by the Company effective January 1, 2009:

- Handbook Section 3064, "Goodwill and Intangible Assets", will replace Section 3062, "Goodwill and Other Intangible Assets", and Section 3450, "Research and Development Costs". Section 1000, "Financial Statement Concepts", was amended according to Section 3064. This new Section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented companies. The Company is presently assessing the impact of these new accounting standards on its consolidated financial statements.

The CICA issued the following accounting standards which will be adopted by the Company effective January 1, 2011:

- Handbook Section 1582, "Business Combinations", which replaces Section 1581, "Business Combinations". The Section establishes standards for the accounting for a business combination. It provides the Canadian equivalent to the IFRS standard, IFRS 3 (Revised), "Business Combinations". The Section applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Earlier application is permitted. The Company is currently evaluating the impact of the adoption of this new accounting standard on its consolidated financial statements.

- Handbook Section 1601, "Consolidated Financial Statements", and Section 1602, "Non-controlling Interests", which together replace Section 1600, "Consolidated Financial Statements". Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of IFRS standard, IAS 27 (Revised), "Consolidated and Separate Financial Statements". Earlier adoption is permitted as of the beginning of a fiscal year. The Company is currently evaluating the impact of the adoption of these new accounting standards on its consolidated financial statements.

Additionally, in February 2008, Canada's Accounting Standards Board confirmed that the use of International Financial Reporting Standards ("IFRS") would be required for Canadian publicly accountable enterprises for years beginning on or after January 1, 2011. The Company is currently evaluating the impact of adopting IFRS on its consolidated financial statements.

5. Business Acquisitions

a) On April 1, 2008, the Company completed the acquisition of BPB through a merger of BPB with a wholly owned US subsidiary of the Company. BPB produces pressure treated wood products, primarily for the railroad industry. This acquisition included five treating plants located in DuBois, Pennsylvania; Goshen, Virginia; Spencer, West Virginia; and Stanton and Fulton, Kentucky.

Total consideration for the acquisition was approximately $44.0 million (US$43.0 million), including estimated acquisition costs of approximately $1.1 million (US$1.1 million), and cash on hand of $0.1 million (US$0.1 million). This amount includes $33.7 million (US$33.0 million) paid to BPB shareholders through the conversion of each outstanding share of common stock of BPB into the right to receive US$47.78 per share in cash, $3.5 million (US$3.4 million) representing an additional payment equal to BPB's audited net income for its fiscal year ended March 31, 2008, less any distributions to shareholders during that period and other post-closing adjustments, as well as an additional discounted amount of $5.8 million (US$5.7 million) guaranteed by a letter of credit to be paid in equal quarterly instalments over a six-year period with respect to non-compete agreements entered into with certain former BPB executives.

The acquisition has been accounted for using the purchase method and accordingly, the purchase price was allocated to the assets acquired and liabilities assumed based on management's estimate of their fair value as at the acquisition date. The results of operations of BPB have been included in the Company's consolidated financial statements from the acquisition date.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

5. Business Acquisitions (Continued)

The following is a final summary of the net assets acquired at fair values as at the acquisition date:

	$
Assets acquired	
Non-cash working capital	41,600
Capital assets	24,432
Cash surrender value of life insurance	325
Customer relationships	4,475
Non-compete agreements	5,814
Non-deductible goodwill	5,340
Future income tax assets	1,283
	83,269
Liabilities assumed	
Notes payable to banks	14,007
Accounts payable and accrued liabilities	6,858
Long-term debt	9,206
Interest-bearing employee deposits	2,134
Future income tax liabilities	7,030
	39,235
Total consideration	44,034
Consideration	
Cash, financed by debt	33,716
Purchase price adjustment paid in cash	3,478
Non-compete agreements payable	5,814
Cash on hand	(97)
Acquisition costs	1,123
Total consideration	44,034

The BPB acquisition was financed through additional borrowings of approximately $40.9 million (US$40.0 million), including the issuance of a $25.5 million (US$25.0 million) unsecured and non-convertible debenture to the *Fonds de solidarité des travailleurs du Québec (F.T.Q.)*, a $10.2 million (US$10.0 million) revolving term loan from a Canadian bank and a drawdown on an existing operating margin of $5.1 million (US$5.0 million). Details of the financing are available in Notes 11 and 12.

b) On February 28, 2007, the Company's wholly owned US subsidiary, SJ Corp, acquired the assets of the wood utility pole business of J.H. Baxter & Co. ("Baxter"). Assets acquired included the Baxter production plant located in Arlington, Washington, its pole peeling facility in Juliaetta, Idaho, as well as all inventories and accounts receivable relating to its wood pole business.

The acquisition was accounted for using the purchase method and accordingly, the purchase price was allocated to the assets acquired and liability assumed based on management's estimate of their fair value as at the acquisition date. Baxter's results of operations have been included in the Company's consolidated financial statements from the acquisition date.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

5. Business Acquisitions (Continued)

The following is a final summary of the net assets acquired at fair values:

	$
Assets acquired	
Accounts receivable	3,792
Inventories	9,850
Prepaid expenses	144
Capital assets	11,494
	25,280
Liability assumed	
Obligation under capital lease	279
Total consideration	25,001
Consideration	
Cash, including transaction costs of $386,528	16,976
Receivable from vendor	(169)
Long-term subordinated note payable to vendor	8,174
Reserve amount for transaction costs, included in accounts payable	20
Total consideration	25,001

Financing for the transaction was provided by a subordinated vendor note of US$8.0 million (recognized at a fair value of US$7.0 million) as well as additional debt funding under existing and new banking facilities. The new banking facilities comprise an increase of US$5.0 million in the operating line of credit of SJ Corp as well as a new five-year term loan of US$4.0 million, both arranged with its existing US banker.

6. Accounts Receivable

	2008	2007
	$	$
Trade	**40,069**	25,321
Other	**1,432**	1,090
	41,501	26,411

7. Inventories

	2008	2007
	$	$
Raw materials	**177,440**	107,691
Finished goods	**45,759**	31,143
	223,199	138,834

The inventory cost included in cost of sales as at December 31, 2008 is $268,997,581 (2007 – $180,890,691).

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

8. Capital Assets

			2008
	Cost	**Accumulated Amortization**	**Net**
	$	**$**	**$**
Land	**8,648**	**—**	**8,648**
Roads	**2,188**	**760**	**1,428**
Cutting rights	**6,505**	**271**	**6,234**
Standing timber	**4,140**	**1,198**	**2,942**
Buildings	**24,645**	**4,281**	**20,364**
Production equipment	**74,653**	**22,376**	**52,277**
Rolling stock	**8,569**	**2,693**	**5,876**
Anti-pollution equipment	**15,817**	**5,941**	**9,876**
Office equipment	**2,357**	**1,239**	**1,118**
	147,522	**38,759**	**108,763**

			2007
	Cost	Accumulated Amortization	Net
	$	$	$
Land	5,192	—	5,192
Roads	1,989	569	1,420
Cutting rights	6,505	132	6,373
Standing timber	3,545	500	3,045
Buildings	13,847	3,346	10,501
Production equipment	53,426	18,646	34,780
Rolling stock	2,828	1,826	1,002
Anti-pollution equipment	15,650	5,171	10,479
Office equipment	1,597	1,080	517
	104,579	31,270	73,309

The net book value of assets held under capital leases as at December 31 is as follows:

	2008	2007
	$	$
Cost	**1,551**	324
Accumulated amortization	**55**	42
Net book value	**1,496**	282

9. Intangible Assets

The Company has recognized intangible assets as part of the purchase price allocation of the BPB acquisition. The acquisition cost of intangible assets, which consist of customer relationships and non-compete agreements, is initially evaluated at fair value, which subsequently becomes the cost. The presentation in the consolidated balance sheet is at cost less accumulated amortization and the related amortization expense is included in amortization in the consolidated statement of earnings.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

9. Intangible Assets (Continued)

Customer relationships comprise long-term agreements with certain customers and ongoing business relationships. The acquisition cost was established based on future benefits associated with these relationships. Intangible assets associated with long-term customer agreements are amortized over the terms of the agreements, which are between three to five years. Intangible assets associated with ongoing business relationships are amortized over ten years.

Certain former BPB executives entered into non-compete agreements with the Company. The acquisition cost was established based on the discounted value of future payments using a discount rate of 10.2%. For cash flow purposes, this has been treated as a non-cash transaction. The intangible asset associated with the non-compete agreements is amortized on a straight-line basis over the terms of the agreements, which are six years.

The amortization expenses for customer relationships and the non-compete agreements were $550,668 and $762,732 respectively as at December 31, 2008. The net book value of these assets was as follows:

	Cost $	Accumulated Amortization $	Net $
Customer relationships	**5,335**	**626**	**4,709**
Non-compete agreements	**6,930**	**866**	**6,064**
	12,265	**1,492**	**10,773**

10. Other Assets

	2008 **$**	2007 $
Advances against third party cutting rights	**322**	202
Notes receivable	**277**	360
Accrued benefit asset (note 16(b))	**1,086**	782
Assets held for sale	**1,633**	—
Other	**25**	—
	3,343	1,344

Included in assets held for sale is an office building and underlying land that were acquired from BPB. They were recorded at a fair value of $606,663. These assets are considered redundant as a new office is being constructed on newly acquired land. The Company has also decided to sell a building and its underlying land located at Christina Lake, British Columbia. The net book value of these assets is $671,629.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

11. Bank Indebtedness

	2008 $	2007 $
Demand operating loan arranged with a Canadian bank (Notes 11(a) and 20)	**32,302**	21,494
Demand operating loan arranged with a US bank (Notes 11(b) and 20)	**46,166**	14,817
Proportionate share of Kanaka demand operating loan (Note 11(c))	**3,092**	2,715
	81,560	39,026

a) The Company has available a credit facility arranged with a Canadian bank, renewable annually, comprising a maximum demand operating loan of $50,000,000 (2007 – $50,000,000), of which $10,899,718 was available as at December 31, 2008. The credit facility also includes a term loan facility of $6,900,000, a bid and performance bond guarantee facility of up to a maximum of $5,000,000, a $5,027,706 capital lease facility, a demand revolving line of credit in the amount of $5,963,000 for the purchase of foreign exchange forward contracts with an aggregate nominal value of $25,100,000 and an interest rate swap facility for up to the full amount outstanding under the term loans. On January 5, 2009, the demand revolving line of credit for the purchase of foreign exchange forward contracts was increased to $12,024,000, with the aggregate nominal value of the foreign exchange forward contracts increasing to $34,000,000.

The interest rate on the operating loan was at the bank's prime rate for Canadian dollar advances, increasing to the bank's prime rate plus 0.25% on January 1, 2009 and thereafter, at bankers' acceptance ("BA") rates plus a stamping fee of 1.05% per annum for Canadian BA advances, increasing to a stamping fee of 1.50% as at January 1, 2009 and thereafter. For US dollar advances, the interest rate was the bank's US base rate, which will become the bank's US base rate plus 0.25% on January 1, 2009 or LIBOR plus 1.50%. As collateral, the bank holds moveable hypothecs and general security agreements over the universality of the Company's Canadian assets, creating a first charge over all of its Canadian current assets of $142,506,329 as at December 31, 2008 and a second ranking charge over all of the Canadian capital assets of $53,089,202 as at December 31, 2008, subject to prior loans approved by the Canadian bankers. The bank also holds a first ranking security under Section 427 of the Bank Act over the Company's Canadian inventories.

b) Stella-Jones US Holding Corporation, Stella-Jones Corporation and The Burke-Parsons-Bowlby Corporation (collectively, "the US subsidiaries") have available a credit facility arranged with a US bank, renewable annually, comprised of a maximum demand operating loan of US$45,000,000 (2007 – US$20,000,000), of which US$7,097,434 was available as at December 31, 2008. On April 1, 2008, the demand operating loan was increased to US$40,000,000, and subsequently on December 9, 2008, it was increased to US$45,000,000 to ensure that the Company had sufficient credit facilities to support the additional working capital arising from the BPB acquisition. The operating line of credit bears interest at the bank's prime rate minus 0.50% or LIBOR plus 1.50%.

As collateral for the US demand operating loan, the US bank holds a first security interest on all non-real estate assets of the US subsidiaries (except for certain equipment) having a net book value of US$120,045,756 as at December 31, 2008. The bank also has a second security interest on certain equipment of the US subsidiaries having a net book value of US$35,047,024 as at December 31, 2008. There is no recourse to the Canadian parent company in the event of default by the US subsidiaries. The Canadian parent company has signed an inventory repurchase agreement with the US bank whereby the parent company has agreed to purchase any or all inventory of the US subsidiaries, at book value, upon an event of default by the US subsidiaries, if requested by the US bank.

c) The Company includes in its consolidated financial statements its 50% proportionate share of Kanaka, which has a credit facility with a Canadian bank comprising a $7,000,000 demand operating loan. The demand operating loan bears interest at the bank's prime rate plus 0.25%, the bank's US base rate plus 0.25%, LIBOR plus 1.1375% or bankers' acceptances plus 1.1375%. One half of the indebtedness, up to a maximum of $5.0 million has been guaranteed by Stella-Jones Canada Inc. and the Company. The Company has also provided an Environmental Indemnity Agreement to the bank with respect to the Maple Ridge property, the site of Kanaka's operations, with liability limited to one half of the monies which become due and owing to the bank under such indemnity.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

12. Long-term Debt (Note 20)

	2008	2007
	$	$
Term loans with a Canadian bank (Note 12(a))	**3,654**	4,768
Revolving term loan with a Canadian bank (Note 12(b))	**23,768**	11,588
Term loan with a US bank (Note 12(c))	**11,572**	3,886
Unsecured and non-convertible debenture (Note 12(d))	**10,000**	10,000
Unsecured and non-convertible debenture (Note 12(e))	**4,000**	4,333
Unsecured and non-convertible debenture (Note 12(f))	**30,450**	—
Promissory note (Note 12(g))	**913**	743
Promissory note (Note12(h))	**1,053**	992
Subordinated note (Note 12(i))	**8,323**	6,981
Bond (Note 12(j))	**5,728**	—
Promissory note (Note 12(k))	**508**	—
Promissory note (Note 12(l))	**447**	—
Mortgage loans (Note 12(m))	**4,317**	3,930
Obligations under capital leases (Note 12(n))	**1,609**	223
	106,342	47,444
Deferred financing charges	**(583)**	—
	105,759	47,444
Less: Current portion of long-term debt	**4,982**	4,409
Less: Current portion of deferred financing charges	**(68)**	—
	100,845	43,035

a) The Company has available three term loans of $2,3000,000, $2,7000,000 and $1,900,000 arranged with a Canadian bank.

Amounts owing under the $2,3000,000 term loan are repayable in 19 equal consecutive principal repayments of $82,143 on each three-month anniversary of the date on which the initial advance was made (December 28, 2005), and a balloon repayment of $739,283 constituting the twentieth and final payment of the residual capital balance on December 28, 2010. Subsequent to an interest rate swap agreement, the loan bears interest at a fixed rate of 5.81% over its term.

Amounts owing under the $2,700,000 term loan are repayable in 19 equal consecutive principal repayments of $96,429 on each three-month anniversary of the date on which the initial advance was made (February 1, 2006), and a balloon repayment of $867,849 constituting the twentieth and final payment of the residual capital balance on February 1, 2011. Subsequent to an interest rate swap agreement, the loan bears interest at a fixed rate of 5.85% over its term.

Amounts owing under the $1,900,000 term loan are repayable in 19 equal consecutive principal repayments of $100,000 on each three-month anniversary of the date on which the initial advance was made (December 19, 2005) and shall, in any event, be repaid in full by September 30, 2010. The loan bears interest at a fixed rate of 5.93% over its term.

b) As part of the financing for the BPB acquisition, the Company entered into a new two-year revolving term loan with a Canadian bank comprising a Canadian dollar loan of $11,587,500 and a new US dollar loan of US$10,000,000 as well as an amount not exceeding US$5,000,000 to purchase foreign exchange forward contracts. The new revolving term loan facility matures February 16, 2010. The US$10,000,000 term loan was designated as a hedge of net investment in a self-sustaining foreign operation. As at December 31, 2007, the Company had a two-year revolving term loan comprising a Canadian dollar loan of $11,587,500 and an amount not exceeding US$5,000,000 to purchase foreign exchange forward contracts. This revolving term loan facility was to have matured February 28, 2009.

12. Long-term Debt (Note 20) (Continued)

For loans in Canadian dollars, the credit facility bears interest at the bank's prime rate plus 0.25% or bankers' acceptance rate plus 1.40% and for loans in US dollars, the credit facility bears interest at the bank's US base rate plus 0.25% or LIBOR plus 1.40%. Previously the revolving term loan did not offer financing conditions for US dollar loans. As collateral, the bank holds moveable hypothecs and general security agreements creating a first charge over all of the Company's Canadian capital assets of $53,089,202 as at December 31, 2008 and a second ranking charge over all of the Canadian current assets of $142,506,329 as at December 31, 2008. Amounts owing under the revolving term loan are payable at maturity which can be extended each year for one additional year, upon the Company's request and subject to the bank's approval. Starting January 2008, the credit facility will be increased by the equivalent amount of the capital payments of the term facilities provided by the credit facility in Note 12(a) to a maximum of $27,500,000 as at January 2011.

c) As part of the financing of the BPB acquisition, the US subsidiaries entered into a US$10,000,000 term loan agreement with a US bank. A portion of the proceeds of the loan were used to repay existing term loans to SJ Corp of US$1,100,000 and US$4,000,000 with the balance applied against outstanding bank indebtedness of the US subsidiaries. The new term loan is repayable in 84 consecutive monthly instalments of US$119,048. The loan is subject to two interest rate swaps of US$5,000,000 each, fixing the rates at 5.80% and 5.54% over the term of the loan.

   As collateral, the bank has a first priority security interest on certain equipment of the US subsidiaries having a net book value of US$35,047,024 as at December 31, 2008. The bank also has a second priority security interest on the accounts receivable and inventories of the US subsidiaries having a book value of US$98,293,058 as at December 31, 2008.

d) Unsecured and non-convertible debenture bearing interest at 7.72%, repayable in five consecutive annual principal repayments of $1,000,000 beginning July 1, 2011 and a final payment of $5,000,000 on July 1, 2016.

e) Unsecured and non-convertible debenture bearing interest at 7.0%, repayable after December 31, 2006 in five consecutive annual principal repayments of $333,333 and a final payment of $3,000,000 on December 21, 2012.

f) Unsecured and non-convertible debenture bearing interest at 7.89%, repayable in five consecutive annual principal repayments of US$2,500,000 starting on April 1, 2013 and a final payment of US$12,500,000 on April 1, 2018. This loan was arranged as part of the financing of the BPB acquisition. This debenture was designated as a hedge of net investment in a self-sustaining foreign operation.

g) SJ Corp borrowed US$750,000 from the Company's majority shareholder, Stella Jones International S.A., by way of a subordinated promissory note. The note is for a term of six years, bears interest at LIBOR plus 4.5% and is repayable in full on the sixth annual anniversary of the date of disbursement or August 3, 2011. The note is unsecured and subordinated in right of payment to the prior payment in full of the US subsidiaries' loans to all of its secured lenders.

h) As part of a previous acquisition, SJ Corp assumed an unsecured promissory note payable. The imputed interest rate of the note is 8.0%. The note is payable in quarterly instalments of US$52,891 including interest and matures on October 1, 2013.

i) Pursuant to the business acquisition of February 28, 2007, SJ Corp issued a note payable to Baxter. The note is subordinated to existing lenders and bears interest at 5.0%. The note is repayable in five annual principal repayments of US$500,000 with a final payment of US$5,500,000 on the sixth anniversary date. The note was initially recorded at a fair value of $6,981,288 using an interest rate of 8.0%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

j) Pursuant to the BPB acquisition, the US subsidiaries assumed a bond issue in favour of the County of Fulton, Kentucky (the Burke-Parsons-Bowlby Project), Series 2006, repayable in annual principal repayments of US$200,000 starting on July 2008 through July 2011, US$300,000 starting July 2012 through July 2019 and US$400,000 starting July 2020 through July 2026. The bond bears interest at a variable rate based on the SIFMA Municipal Swap Index. The rate as at December 31, 2008 was 1.60% (March 31, 2008 – 2.38%). The bond is secured by substantially all assets of BPB's Fulton facility, which have a net book value of US$7,431,022 as at December 31, 2008. The bond was initially recorded in the consolidated financial statements at a fair value of US$4,835,379 using an interest rate of 6.50%. The difference between the face value and the fair value of the bond is being accreted on an effective yield basis over its term.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

12. Long-term Debt (Note 20) (Continued)

In order to provide security for the timely payment of the principal and interest due on the bond, the US subsidiaries entered into a US$5,866,740 irrevocable letter of credit with the bank that is also the trustee for the Series 2006 Bond Indenture, at an annual fee of 1.0% of the outstanding loan balance. The letter of credit expires on August 15, 2009.

k) Pursuant to the BPB acquisition, the US subsidiaries assumed a promissory note payable to Hickman-Fulton Rural Electric Cooperative Corporation, bearing interest at a fixed rate of 3.0% and repayable in 84 equal monthly instalments of principal and interest of approximately US$6,604 starting January 15, 2008. The note is secured by a US$500,000 irrevocable letter of credit issued by a regional financial institution and expires December 17, 2017. The note was initially recorded in the consolidated financial statements at a fair value of US$462,344 using an interest rate of 5.55%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

l) Pursuant to the BPB acquisition, the US subsidiaries assumed a promissory note payable to Hickman-Fulton Rural Electric Cooperative Corporation, bearing no interest and repayable in 108 equal monthly instalments of US$4,167 starting January 1, 2009. The note is secured by a US$450,000 irrevocable letter of credit issued by a regional financial institution and expires December 17, 2017. The note was initially recorded in the consolidated financial statements at a fair value of US$354,217 using an interest rate of 6.0%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

m) The mortgage loans bear interest at a weighted average rate of 6.3% as at December 31, 2008 (2007 – 7.2%) and certain specific capital assets with a net book value of $5,638,867 (2007 – $6,880,152) have been pledged as collateral. The mortgage loans include loans denominated in US dollars amounting to US$3,407,858 (2007 – US$2,970,328). The loans are repayable in monthly instalments of $95,705 including interest and mature at various dates to January 2018.

n) The repayment requirements on the long-term debt during the next five years and thereafter are as follows:

	Capital leases				
Years	Minimum payments $	Interest $	Principal $	Principal $	Principal repayments $
2009	189	78	111	5,199	5,310
2010	233	70	163	5,764	5,927
2011	111	63	48	7,058	7,106
2012	111	61	50	7,649	7,699
2013	272	49	223	13,507	13,730
Thereafter	1,105	91	1,014	67,826	68,840
	2,021	412	1,609	107,003	108,612
Fair value adjustment	—	—	—	(2,270)	(2,270)
	2,021	412	1,609	104,733	106,342

o) The aggregate fair value of the Company’s long-term debt was estimated at $109,660,000 as at December 31, 2008 (2007 – $49,500,000) based on discounted future cash flows, using interest rates available to the Company for issues with similar terms and average maturities.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

13. Asset Retirement Obligations

Stella-Jones Canada Inc. has asset retirement obligations relating to reforestation and site remediation that have been estimated using a credit-adjusted risk-free rate of 4.5% (2007 – 6.9%) to approximate the present value of future expenditures.

Reforestation

Reforestation obligations represent discounted cash flow estimates of future silviculture costs relating to areas logged that are the Company's responsibility to reforest.

	2008	2007
	$	$
Reforestation obligations – Beginning of year	**1,160**	1,237
Changes to reforestation estimates and accretion expense	**708**	711
Expenditures	**(622)**	(788)
Reforestation obligations – End of year	**1,246**	1,160
Less: Current portion	**669**	693
	577	467

Future non-discounted reforestation expenditures are estimated at between $320,000 and $700,000 in each of the next three years. There are uncertainties in estimating future reforestation costs due to potential regulatory changes as well as the impact of weather-related changes on reforested areas. Accordingly, the actual cost of reforestation may differ from current estimates.

The Company has contracts whereby third party licensees that harvest certain areas assume the responsibility for reforestation. Should the third party licensees fail to perform, the Company is responsible for these additional future reforestation costs, which are currently estimated to be $507,082 (2007 – $488,409). Payments, if any, required as a result of this contingency will be expensed in the period in which they are determined and are not included in the provision for reforestation noted above.

Site Remediation

Site remediation obligations represent discounted cash flow estimates relating to future environmental remediation costs of former treating sites.

	2008	2007
	$	$
Site remediation obligations – Beginning of year	**58**	100
Changes to site remediation estimates	**—**	—
Expenditures	**(10)**	(42)
Site remediation obligations – End of year	**48**	58
Less: Current portion	**48**	58
	—	—

13. Asset Retirement Obligations (Continued)

Total asset retirement obligations

	2008 $	2007 $
Reforestation obligations	**1,246**	1,160
Site remediation obligations	**48**	58
	1,294	1,218
Less: Current portion	**717**	751
	577	467

14. Capital Stock

a) Capital stock consists of the following:

Authorized
An unlimited number of preferred shares issuable in series
An unlimited number of common shares

b) Earnings per share
Net earnings per common share are calculated using the weighted average number of common shares outstanding during the year. Diluted net earnings per common share are calculated using the weighted average number of common shares outstanding during the year based on the application of the treasury stock method for the calculation of the dilutive effect of stock options, warrants and other dilutive securities.

The following table provides the reconciliation between net earnings per common share and diluted net earnings per common share:

	2008	2007
Net earnings applicable to common shares	**$ 28,547**	$ 25,700
Weighted average number of common shares outstanding*	**12,483**	12,324
Effect of dilutive stock options*	**212**	366
Weighted average number of diluted common shares outstanding*	**12,695**	12,690
Net earnings per common share	**$ 2.29**	$ 2.09
Diluted net earnings per common share	**$ 2.25**	$ 2.03

* Number of shares are presented in thousands.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

14. Capital Stock (Continued)

c) Stock option plan

The Company has a stock option plan (the "Plan") for directors, officers and employees whereby the Board of Directors or a committee appointed for such purpose may, from time to time, grant to directors, officers or employees of the Company options to acquire common shares in such numbers, for such terms and at such exercise prices as are determined by the Board of Directors or such committee. The stated purpose of the Plan is to secure for the Company and its shareholders the benefits of incentives inherent in share ownership by directors, officers and employees of the Company.

Under the Plan adopted on June 13, 1994 and amended on May 3, 1995, March 15, 2001 and May 3, 2007, the aggregate number of common shares in respect of which options may be granted is 1,200,000 and no optionee is able to hold options to purchase common shares exceeding 5% of the number of common shares outstanding from time to time. One-fifth of the options granted may be exercised within each year following the grant date. The exercise price of an option shall not be lower than the closing price of the common shares on the Toronto Stock Exchange on the last trading day preceding the granting of the option, and the term of the option may not exceed ten years. Options will not be assignable and will terminate, in the case of an employee, either 30 or 180 days following cessation of service with the Company depending on the circumstances of such cessation, and in the case of a director who is not an employee of the Company, either 30 or 180 days following the date on which such optionee ceases to be a director of the Company, depending on the circumstances.

Changes in the number of options outstanding under the Plan were as follows:

		2008		2007
		$		$
	Number of options	**Weighted average exercise price**	Number of options	Weighted average exercise price
Outstanding – Beginning of year	**162,070**	**18.17**	183,355	13.15
Exercised	**(14,285)**	**13.38**	(37,785)	7.37
Granted	**—**	**—**	22,500	39.58
Forfeited	**—**	**—**	(6,000)	13.00
Outstanding – End of year	**147,785**	**18.63**	162,070	18.17
Options exercisable – End of year	**93,285**	**15.97**	76,570	13.84

The following options were outstanding under the Plan as at December 31, 2008:

	Options outstanding		**Options exercisable**		
Year granted	**Number of options**	**Weighted average exercise price $**	**Number of options**	**Weighted average exercise price $**	**Expiration date**
2001	**18,285**	**2.15**	**18,285**	**2.15**	**2011**
2005	**43,000**	**13.00**	**31,000**	**13.00**	**2015**
2006	**64,000**	**19.78**	**35,000**	**19.76**	**2016**
2007	**22,500**	**39.58**	**9,000**	**39.58**	**2017**
	147,785		**93,285**		

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

14. Capital Stock (Continued)

d) Stock option agreement

On May 6, 2003, with the objective of assisting the Company in recognizing the significant contributions that its President and Chief Executive Officer ("President") has made to the Company, and in order to provide incentives for him to continue to make significant contributions to the Company, 300,000 options were granted to the President under a stock option agreement ("Agreement").

The Agreement provides that the options are exercisable at a price of $2.99 in whole or in part commencing on May 6, 2008, or earlier in the event of a triggering event, that is, a loss or change in control of the Company, the closing of a going private transaction, or the occurrence of termination without cause. The right to exercise these options terminates on May 6, 2013 or, in the case of a triggering event, within 30 days of the event.

In 2006, the President, on his own initiative, unconditionally and irrevocably waived his right under his Agreement to settle stock options for cash. As a result, the amount recorded as a long-term liability of $3,480,000 net of the related future income taxes of $1,218,000 was eliminated and a corresponding amount was included in contributed surplus.

On May 6, 2008, the options under the Agreement became fully vested and shortly thereafter, 200,000 options were exercised. The total stock-based compensation expenses relating to the Agreement amounted to $433,936 (2007 – $1,483,140).

e) Stock-based compensation

The Company records expenses for the fair value of the stock options granted under the Plan using the Black-Scholes option pricing model. This model determines the fair value of stock options granted and amortizes it to earnings over the vesting period.

No new options were granted during 2008. In 2007, 22,500 options were granted, their fair value was $422,730, and the expense amortized to earnings was $28,182. The fair value was estimated with the following weighted average assumptions:

	2008	2007
Risk-free interest rate	—	4.2%
Dividend yield	—	0.6%
Expected lives	—	7.8 years
Volatility	—	42.6%
Weighted average of fair value of options granted during the year	—	$18.79

In 2008, the total expense relating to stock-based compensation amortized to earnings was $307,264 (2007 – $241,962).

f) Employee share purchase plans

The aggregate number of common shares reserved for issuance under the Company's two employee share purchase plans is 180,000.

Under the first plan, Company employees who are Canadian residents are eligible to purchase common shares from the Company at a price of 90% of the market value. Employees who hold common shares in the employee share purchase plan for 18 months following the date of acquisition of such shares receive additional common shares of the Company equivalent to 10% of the amount of their contributions made on the date of acquisition. In 2008, 7,517 shares (2007 – 4,693) were issued to Canadian resident employees at an average price of $22.30 per share (2007 – $34.00).

Under the second plan, Company employees who are US residents are eligible to purchase common shares from the Company at a price equal to the market value. Employees who hold common shares in the employee share purchase plan for 18 months following the date of acquisition of such shares receive additional common shares of the Company equivalent to 10% of the amount of their contributions made on the date of acquisition. In 2008, 2,035 shares (2007 – 595) were issued to US resident employees at an average price of $24.20 per share (2007 – $40.08).

As at December 31, 2008, the total number of shares issued under these plans is 142,430 (2007 – 132,878).

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

14. Capital Stock (Continued)

g) On November 12, 2007 and August 31, 2005, the Company granted stock appreciation rights to senior management with the base price being the trading price per share on the Toronto Stock Exchange at the close of trading on the grant date. Details are as follows:

Grant date	November 12, 2007	August 31, 2005
Number of rights granted	300,000	15,000
Base price	$39.74	$9.53

Stock appreciation rights granted November 12, 2007 will become enforceable on November 12, 2013. Stock appreciation rights granted August 31, 2005 were repriced on December 22, 2008 from the initial base price of $9.53 to $15.60. On the reprice date, 12,000 stock appreciation rights immediately vested and the remaining 3,000 will vest within the year following this date.

The stock appreciation rights may become enforceable earlier in the event of a triggering event.

As at December 31, 2008, the share price used to value the stock appreciation rights is $16.40 and the change in liability is as follows:

	2008	2007
	$	$
Balance – Beginning of year	**465**	129
Liability adjustment	**(455)**	336
Balance – End of year	**10**	465

15. Income Taxes

The earnings before income taxes computed for the years ended December 31 were as follows:

	2008	2007
	$	$
Canada	**27,917**	26,399
US	**13,313**	12,158
	41,230	38,557

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

15. Income Taxes (Continued)

The provision for (recovery of) income taxes includes the following current and future amounts:

	2008 $	2007 $
Current		
Canada	**7,412**	8,679
US	**3,559**	4,327
Total current expense	**10,971**	13,006
Future		
Canada	**909**	(357)
US	**803**	208
Total future expense (recovery)	**1,712**	(149)
	12,683	12,857

The effective income tax rate differs from the basic Canadian federal and provincial statutory tax rate due to the following:

	2008	2007
Statutory tax rate	**31.62%**	34.05%
	$	$
Income tax expense at statutory rate	**13,037**	13,127
Income tax expense (recovery) resulting from		
Future tax adjustments due to rate enactments	**(162)**	(679)
Manufacturing and processing credit	**(242)**	(110)
Effect of different tax rates	**695**	419
Dividends deductible from a related party	**(545)**	—
Stock-based compensation	**234**	579
Non-deductible portion of foreign exchange loss	**70**	—
Unrecorded tax benefit on foreign exchange loss	**61**	—
Other	**(465)**	(479)
	12,683	12,857
Effective tax rate	**30.76%**	33.35%

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

15. Income Taxes (Continued)

Significant components of the future income tax assets and liabilities are as follows:

	2008 $	2007 $
Future income tax assets due to		
Accrued liabilities	**2,255**	742
Employee future benefits	**414**	175
Derivative financial instruments and other	**515**	59
	3,184	976
Future income tax liabilities due to		
Capital assets	**(16,260)**	(5,968)
Derivative financial instruments	**(226)**	(289)
Other assets	**(257)**	—
	(16,743)	(6,257)

16. Employee Future Benefits

The Company recognizes cost for several types of employee future benefits. Post-retirement benefits are offered to certain retired employees and consist of group health and dental care, life insurance and complementary retirement benefits. Stella-Jones Canada Inc. contributes to a multi-employer plan for certain hourly employees and to three defined benefit pension plans for salaried and certain non-union hourly wage employees. All other active employees are entitled to a group registered retirement savings plan to which the Company matches 1.5 times employee contributions to a maximum of 4%. The recognized cost for employee future benefits was as follows:

	2008 $	2007 $
Post-retirement benefits	**256**	231
Defined benefit pension plans	**136**	130
Contributions to multi-employer plan	**322**	244
Contributions to group retirement savings plans	**1,145**	647

a) The post-retirement benefits program is not funded. The Company measures its accrued benefit obligations for accounting purposes as at December 31 of each year. The most recent actuarial valuation of this plan was as at January 1, 2006, and the next required valuation will be as at January 1, 2009. The following information pertains to the Company's defined benefit plan as established by independent actuaries:

	2008 $	2007 $
Accrued benefit obligation		
Balance – Beginning of year	**1,974**	1,749
Current service cost	**118**	110
Interest cost on obligation	**109**	92
Benefit payments	**(30)**	(28)
Actuarial (gain) loss	**(519)**	51
Balance – End of year	**1,652**	1,974
Plan assets		
Fair value – Beginning of year	**—**	—
Employer contributions	**30**	28
Benefits paid	**(30)**	(28)
Fair value – end of year	**—**	—
Net obligation – End of year	**1,652**	1,974
Unamortized net actuarial loss	**(98)**	(662)
Unamortized past service costs	**(13)**	(14)
Accrued benefit obligation	**1,541**	1,298

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

16. Employee Future Benefits (Continued)

The significant assumptions used are as follows:

	2008 %	2007 %
Accrued benefit obligation and benefit cost as at December 31		
Discount rate	**6.75**	5.25
Rate of compensation increase	**4.00**	4.00

For measurement purposes, a 10% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2008. This rate is assumed to decrease gradually by 0.5% per year, to reach 5%. An increase or decrease of 1% in this rate would have the following impact:

	Increase of 1%	Decrease of 1%
Impact on accrued benefit obligation	**342**	268
Impact on benefit cost	**58**	44

The elements of the Company's defined benefit plan costs recognized in the year are as follows:

	2008 $	2007 $
Current service cost	**118**	110
Interest cost	**109**	92
Actuarial (gain) loss	**(519)**	51
Elements of employee future benefit cost before adjustments to recognize the long-term nature of employee future benefit cost	**(292)**	253
Adjustments to recognize the long-term nature of employee future benefit cost		
Difference between net actuarial loss (gain) and actuarial loss (gain)	**547**	(23)
Amortization of past service costs	**1**	1
Defined benefit costs recognized	**256**	231

b) The Stella-Jones Canada Inc. defined benefit pension plans base the benefits on the length of service and final average earnings. The Company measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year. The most recent actuarial valuation of one of the pension plans for funding purposes was as at December 31, 2007, which will be updated December 31, 2010. The actuarial valuation date for the two other pension plans is December 31, 2008, which will be updated December 31, 2011.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

16. Employee Future Benefits (Continued)

Information about Stella-Jones Canada Inc.'s defined benefit plans other than the multi-employer defined benefit plan, in aggregate, is as follows:

	2008 $	2007 $
Accrued benefit obligation		
Balance – Beginning of year	**10,686**	10,721
Current service cost	**406**	437
Interest cost on obligation	**558**	531
Benefit payments	**(505)**	(653)
Actuarial gain	**(3,813)**	(350)
Balance – End of year	**7,332**	10,686
Plan assets		
Fair value – Beginning of year	**10,933**	11,191
Actual return on plan assets	**(1,803)**	(95)
Employer contributions	**455**	491
Benefits paid	**(506)**	(654)
Fair value – End of year	**9,079**	10,933
Funded status – Plan surplus	**1,747**	247
Unamortized net actuarial gain (loss)	**661**	(535)
Accrued benefit asset, included in other assets (Note 10)	**1,086**	782

Unamortized actuarial gains and losses that exceed the greater of 10% of the market value of assets and the accrued benefit obligation are amortized over the estimated average remaining service lifetime of active plan members.

Included in the above accrued benefit obligation and fair value of plan assets at year-end are the following amounts in respect of benefit plans that are not fully funded:

	2008 $	2007 $
Accrued benefit obligation	**(1,577)**	(3,610)
Fair value of plan assets	**1,415**	3,188
Funded status – Plan deficit	**(162)**	(422)

Percentage of plan assets consist of the following for the year ended December 31:

	2008 %	2007 %
Equity securities	**55**	55
Debt securities	**40**	41
Short-term investments and cash	**5**	4
	100	100

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

16. Employee Future Benefits (Continued)

The significant weighted average assumptions used are as follows:

	2008	2007
	%	%
Accrued benefit obligation as at December 31		
Discount rate	**7.50**	5.25
Rate of compensation increase	**4.00**	4.00
Benefit costs for the year ended December 31		
Discount rate	**5.25**	5.00
Expected long-term rate of return on plan assets	**7.50**	7.50
Rate of compensation increase	**4.00**	4.00

The elements of Stella-Jones Canada Inc.'s defined benefit plan costs recognized in the year are as follows:

	2008	2007
	$	$
Current service cost, net of employee contributions	**392**	428
Interest cost	**558**	531
Actual return on plan assets	**1,803**	95
Actuarial gain	**(3,813)**	(350)
Elements of employee future benefit cost before adjustments to recognize the long-term nature of employee future benefit cost	**(1,060)**	704
Adjustments to recognize the long-term nature of employee future benefit cost		
Difference between expected return and actual return on plan asset for the year	**(2,621)**	(929)
Difference between net actuarial loss (gain) and actual actuarial loss (gain)	**3,817**	355
Defined benefit costs recognized	**136**	130

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

17. Interest in Joint Venture

The consolidated financial statements include the Company's 50% proportionate share, as indicated below, of the revenues, expenses, assets and liabilities of its Kanaka joint venture:

	2008 $	2007 $
Assets		
Current assets		
Accounts receivable	**121**	331
Other receivable	**200**	145
Inventories	**1,942**	1,603
Prepaid expenses	**20**	14
	2,283	2,093
Capital assets	**842**	666
Other assets	**67**	72
Total assets	**3,192**	2,831
Liabilities		
Current liabilities		
Bank indebtedness	**3,092**	2,715
Accounts payable and accrued liabilities	**100**	116
Total liabilities	**3,192**	2,831
Earnings		
Sales	**5,011**	3,660
Cost of sales	**5,011**	3,660
Net earnings	**—**	—
Cash flows provided by (used in)		
Operating activities	**(101)**	232
Financing activities	**355**	(43)
Investing activities	**(254)**	(189)
	—	—

18. Commitments and Contingencies

a) The Company is involved from time to time in various claims and legal proceedings arising in the ordinary course of business. It is the opinion of management that a final determination of these proceedings cannot be made at this time but should not materially affect the Company's financial position or results of operations.

b) The Company has issued guarantees, other than those disclosed elsewhere in these financial statements, amounting to $14,788,448 (2007 – $4,588,466) under letters of credit and various bid and performance bonds. The Company's management does not believe these guarantees are likely to be called on. As a result, no provisions have been recorded in the consolidated financial statements.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

18. Commitments and Contingencies (Continued)

c) Future minimum payments under operating leases related to land, equipment and rolling stock are as follows:

	$
2009	2,822
2010	2,443
2011	1,755
2012	983
2013	823
Thereafter	11,720

d) The Company's operations are subject to Canadian federal and provincial as well as US federal and state environmental laws and regulations governing, among other matters, air emissions, waste management and wastewater effluent discharges. The Company takes measures to comply with such laws and regulations. However, the measures taken are subject to the uncertainties of changing legal requirements, enforcement practices and developing technological processes.

19. Financial Instruments

Financial Instruments, Carrying Values and Fair Values

The Company has determined that the fair value of its short-term financial assets and financial liabilities approximates their respective carrying amounts as at the balance sheet date because of the short-term maturity of those instruments. The fair values of the long-term receivables and interest-bearing financial liabilities also approximate their respective carrying amounts. The fair value of foreign exchange forward contracts and swap agreements has been recorded using mark-to-market information as supplied by a financial institution.

Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers.

The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer. Management believes that the credit risk of accounts receivable is limited for the following reasons:

- Geographically, there is no concentration of credit risk.
- The Company deals primarily with utility and telecommunication companies, and other major corporations.

The following table summarizes the age of trade receivables as at December 31:

	2008	2007
	$	$
Past due less than 30 days	**23,374**	13,106
Past due 31 to 60 days	**10,204**	8,663
Past due 61 to 90 days	**4,457**	2,665
Past due more than 90 days	**2,278**	1,116
Total accounts receivable	**40,313**	25,550
Allowance for doubtful accounts	**(244)**	(229)
	40,069	25,321

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

19. Financial Instruments (Continued)

Management has established a credit policy under which each new customer is analyzed individually for creditworthiness before the Company's standard payment and delivery terms and conditions are offered. The Company's review includes external ratings, where available, and credit references from other suppliers. Purchase limits are established for each customer, which represent the maximum open amount not requiring additional approval from management. A monthly review of the accounts receivable aging is performed by management for each selling location. Customers that fail to meet the Company's benchmark creditworthiness may transact with the Company only on a prepayment basis. As at December 31, 2008, details of the allowance for doubtful accounts are as follows:

	2008 **$**	2007 $
Balance – Beginning of year	**229**	33
Provision	**458**	229
Bad debt writeoff	**(480)**	(27)
Foreign exchange adjustments	**37**	(6)
Balance – End of year	**244**	229

In 2008, the Company had one customer representing 19% of its sales (2007 – 15%). As at December 31, 2008, the accounts receivable balance from this customer was $6,103,420 (2007 – $3,637,533).

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, on a long-term basis, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring losses or risking damage to its reputation.

The Company ensures that it has sufficient credit facilities to support working capital, meet expected operational expenses and service financial obligations. Inventories are a significant component of working capital because of the long periods required to air season wood, which can occasionally exceed nine months before a sale is made. Details regarding the Company's operating lines of credit can be found in Note 11.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

19. Financial Instruments (Continued)

The Company monitors all financial liabilities and ensures it will have sufficient liquidity to meet these future payments. Bank indebtedness consists of demand operating facilities that are subject to periodic review by the Company's bankers at intervals of no greater than one year. In December 2008, the Company's banker for the US operating line amended its credit facilities and approved an increase to its demand operating line to US$45,000,000, from US$40,000,000. Subsequent to year-end, the Company's Canadian bankers amended the interest rate structure, with no change in the amount available of the operating facility and approved an increase to the credit availability for the purchase of foreign exchange forward contracts. The following table details the maturities of the financial liabilities as at December 31, 2008:

	Less than 1 year	1 to 3 Years	4 to 5 Years	More than 5 years	Total
	$	$	$	$	$
Bank indebtedness	81,560	—	—	—	81,560
Accounts payable and accrued liabilities	28,694	—	—	—	28,694
Long-term debt obligations	5,199	12,822	21,156	67,826	107,003
Interest on long-term debt obligations	6,150	11,534	9,721	9,937	37,342
Capital lease obligations	189	344	383	1,105	2,021
Interest on capital lease obligations	78	133	110	91	412
Foreign exchange forward contracts					
Outflow	5,319	3,234	—	—	8,553
Inflow	(5,603)	(3,410)	—	—	(9,013)
Non-compete agreements	1,523	3,046	3,046	381	7,996
	123,109	27,703	34,416	79,340	264,568

Market Risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

Currency Risk

The Company's exposure to foreign exchange gains or losses from currency fluctuations is related to sales and purchases in US dollars by its Canadian-based operations and to US dollar-denominated long-term debt held by its Canadian companies. The Company monitors its transactions in US dollars generated by Canadian-based operations. Its basic hedging activity consists of entering into foreign exchange forward contracts for the sale of US dollars and purchasing certain goods and services in US dollars. The Company will also consider foreign exchange forward contracts for the purchase of US dollars for significant purchases of goods and services that are not covered by natural hedges.

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

19. Financial Instruments (Continued)

The following table summarizes the Company's derivative financial instruments relating to the sale of foreign currencies through forward foreign exchange contracts as at December 31:

	Foreign exchange forward contracts	Notional amount US$	Average exchange rate	Notional equivalent CA$	Fair value CA$
					2008
Short-term asset	**Sell US$/Buy CA$**	**10,000**	**1.2538**	**12,538**	**381**
Long-term asset	**Sell US$/Buy CA$**	**10,000**	**1.2433**	**12,433**	**347**
Short-term liability	**Sell US$/Buy CA$**	**4,600**	**1.1563**	**5,319**	**(266)**
Long-term liability	**Sell US$/Buy CA$**	**2,800**	**1.1550**	**3,234**	**(144)**
		27,400	**1.2235**	**33,524**	**318**

	Foreign exchange forward contracts	Notional amount US$	Average exchange rate	Notional equivalent CA$	Fair value CA$
					2007
Short-term liability	Sell US$/Buy CA$	4,000	1.1593	4,637	658
Long-term liability	Sell US$/Buy CA$	1,800	1.1497	2,070	257
		5,800	1.1563	6,707	915

The contracts mature at various dates up to December 31, 2010.

A 10% strengthening of the US dollar against the Canadian dollar would have decreased the net gain on foreign exchange forward contracts recognized in other comprehensive income by approximately $31,878 as at December 31, 2008. For a 10% weakening of the US dollar against the Canadian dollar, there would be an equal and opposite impact on the gain.

The following table provides information on the impact of a 10% strengthening of the US dollar against the Canadian dollar on net earnings and comprehensive income for the year ended December 31, 2008. For a 10% weakening of the US dollar against the Canadian dollar, there would be an equal and opposite impact on net earnings and comprehensive income.

	$
Gain to net earnings	**560**
Comprehensive income	**528**

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

19. Financial Instruments (Continued)

This analysis considers the foreign exchange variance impact on assets and liabilities denominated in US dollars which are on the balance sheet of the Canadian entities:

	2008
	$
Assets	
Accounts receivables	2,037
Foreign exchange forward contracts	728
	2,765
Liabilities	
Accounts payable and accrued liabilities	2,884
Foreign exchange forward contracts	410
	3,294

The foreign exchange impact for the US dollar-denominated long-term debt, in the Canadian entities, has been excluded from the sensitivity analysis for other comprehensive income, as the long-term debt is designated as a hedge against the investment in the self-sustaining US subsidiary.

Interest Rate Risks

As at December 31, 2008, the Company has limited exposure to interest rate risk on long-term debt as after giving effect to its interest rate swaps, 92.7% of the Company's long-term debt is at fixed rates.

The Company enters into interest rate swaps in order to reduce the impact of fluctuating interest rates on its short-term and long-term debt. These swap agreements require the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based. The Company designates its interest rate hedge agreements as cash flow hedges of the underlying debt. Interest expense on the debt is adjusted to include the payments made or received under the interest rate swaps.

Bank indebtedness comprises demand operating loans as defined in Note 11. The financing of these loans is tied to the Canadian bank's prime rate, the US bank's base rate or LIBOR. The impact of a 10% increase in these rates on the average annual balance of the bank indebtedness would have increased the interest expense by $247,166 for the year ended December 31, 2008.

The following table summarizes the Company's interest rate swap agreements as at December 31:

			2008
Notional amount	Fixed rate	Maturing date	Notional equivalent
	%		CA$
CA$2,300	5.81	December 2010	2,300
CA$2,700	5.85	February 2011	2,700
US$5,000	5.80	July 2015	6,090
US$5,000	5.54	July 2015	6,090
US$1,000	4.69	December 2015	1,218

			2007
Notional amount	Fixed rate	Maturing date	Notional equivalent
	%		CA$
CA$2,300	5.81	December 2010	2,300
CA$2,700	5.85	February 2011	2,700
US$1,100	7.23	September 2010	1,090

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

19. Financial Instruments (Continued)

The fair value of the interest rate swap agreements based on cash settlement requirements as at December 31, 2008 is a loss of $1,159,153 (2007 – gain of $16,643), which is recorded in long-term liabilities under derivative financial instruments. A 10% decrease in interest rates as at December 31, 2008 would have increased the loss recognized in other comprehensive income by approximately $115,915. For a 10% increase in the interest rates, there would be an equal and opposite impact on the loss.

20. Capital Disclosure

The Company's objective in managing capital is to ensure sufficient liquidity to pursue its organic growth strategy and undertake selective acquisitions, while at the same time taking a conservative approach to financial leverage and management of financial risk. The Company manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, or acquire or sell assets to improve its financial performance and flexibility.

The Company's capital is composed of long-term debt and shareholders' equity which includes capital stock.

	2008	2007
	$	$
Long-term debt, including current portion	**105,759**	47,444
Shareholders' equity	**161,112**	127,757
Total capital	**266,871**	175,201
Long-term debt to equity ratio	**0.66:1**	0.37:1

The Company's primary uses of capital are to finance increases in non-cash working capital and capital expenditures for capacity expansion as well as acquisitions. The Company currently funds these requirements out of its internally-generated cash flows and operating lines of credit. However, future corporate acquisitions may require new sources of financing.

The primary measure used by the Company to monitor its financial leverage is the long-term debt to equity ratio, which it aims to maintain within a range of 0.30:1 to 0.75:1. The long-term debt to equity ratio is defined as long-term debt including the current portion divided by shareholders' equity. As at December 31, 2008, the long-term debt to equity ratio was 0.66:1 (2007 – 0.37:1).

The Company is subject to certain covenants on its bank indebtedness and on certain long-term debt. The covenants include a working capital ratio, debt to tangible net worth ratio, a minimum fixed charge coverage ratio and a minimum requirement for earnings before interest, taxes and amortization. The Company monitors the ratios on a monthly basis. The ratios are also reviewed by the Company's Audit Committee and Board of Directors on a quarterly basis. Other than the covenants required for the credit facilities, the Company is not subject to any externally imposed capital requirements.

21. Related Party Transactions

The Company had the following transactions with related parties:

	2008	2007
	$	$
Parent company		
Marketing and technical service fees paid	**200**	200
Interest on promissory note	**64**	76
Ultimate shareholders		
Marketing and technical service fees paid	**100**	100

(tabular amounts expressed in thousands of dollars, except as otherwise indicated)

21. Related Party Transactions (Continued)

These transactions occurred in the normal course of operations and have been measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

As at December 31, 2008, the consolidated balance sheet includes the following amounts with related parties:

	2008	2007
	$	$
Accounts payable to parent company	**79**	77
Accounts payable to ultimate shareholders	**25**	25

22. Segment Information

The Company operates within one dominant business segment: the production and sale of pressure treated wood. Operating plants are located in the Canadian provinces of Nova Scotia, Quebec, Ontario, Alberta and British Columbia, and in the US states of Pennsylvania, Virginia, West Virginia, Kentucky, Wisconsin and Washington. The Company also operates a distribution centre in the province of Newfoundland and Labrador.

Sales attributed to countries based on location of customer are as follows:

	2008	2007
	$	$
Canada	**180,052**	163,122
US	**204,770**	106,592
	384,822	269,714

Capital assets attributed to the countries based on location are as follows:

	2008	2007
	$	$
Canada	**55,124**	53,327
US	**53,639**	16,937
	108,763	70,264

Intangible assets having a net book value of $10,773,515 and goodwill having a value of $6,367,481 are attributed to the Company's US operations.

23. Comparative Figures

Certain comparative figures have been reclassified in order to comply with the basis of presentation adopted in the current year.