MANAGEMENT'S DISCUSSION & ANALYSIS

The following Management's Discussion and Analysis ("MD&A") and the Company's audited consolidated financial statements were approved by the Audit Committee and the Board of Directors on March 10, 2011. The MD&A provides a review of the significant developments and results of operations of the Company during the fiscal year ended December 31, 2010 compared with the fiscal year ended December 31, 2009. The MD&A should be read in conjunction with the Company's audited consolidated financial statements for the years ended December 31, 2010 and 2009 and the notes thereto.

The MD&A contains statements that are forward-looking in nature. Such statements involve known and unknown risks and uncertainties that may cause the actual results of the Company to be materially different from those expressed or implied by such forward-looking statements. Such items include, among others: general economic and business conditions, product selling prices, raw material and operating costs, changes in foreign currency rates and other factors referenced herein and in the Company's continuous disclosure filings.

The Company's audited consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and results are reported in Canadian dollars. All amounts in this MD&A are in Canadian dollars unless otherwise indicated.

Additional information, including the Company's annual information form, quarterly and annual reports, and supplementary information is available on SEDAR at **www.sedar.com.** Press releases and other information are also available in the Investor/ Media Centre section of the Company's Web site at **www.stella-jones.com**.

OUR BUSINESS

Stella-Jones Inc. (TSX: SJ) 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 manufactures the wood preservative creosote and other coal tar based products and provides the railroad industry with used tie pickup and disposal services. Switching, locomotive and railcar maintenance services are also offered, as is tie-derived boiler fuel. The Company also provides treated residential lumber products and customized services to lumber retailers and wholesalers for outdoor applications. Other treated wood products include marine and foundation pilings, construction timbers, highway guardrail posts and treated wood for bridges.

The Company operates eighteen wood treating plants, a coal tar distillery, three facilities providing railway tie pickup and disposal services, two distribution centres, two pole peeling facilities and has a 50% interest in a third pole peeling operation. These twenty-seven facilities are located in six Canadian provinces and fourteen American states. The Company's workforce currently numbers approximately 940 employees.

Stella-Jones enjoys a number of key attributes which should further enhance the Company's strategic positioning and competitive advantage in the wood treating industry. Among these are the ability to service clients from multiple plants, a solid financial position that allows the Company to stockpile and air-season green wood for major long-term contracts, a long-standing stable source of wood supply, and a registration to produce and sell the wood preservative, creosote.

OUR MISSION

Stella-Jones' objective is to be the performance leader in the wood preserving industry and a model corporate citizen, exercising environmental responsibility and integrity.

Stella-Jones will achieve these goals by focusing on customer satisfaction, core products, key markets, innovative work practices and the optimal use of its resources.

Stella-Jones is committed to providing a safe, respectful and productive environment for its employees, where problem solving, initiative and high standards of performance are rewarded.

NON-GAAP MEASURES

Operating earnings before amortization of capital and intangible assets (also referred to as earnings before interest, taxes, depreciation and amortization ["EBITDA"]), operating earnings, and cash flow from operations are financial measures not prescribed by Canadian generally accepted accounting principles ("GAAP") and are not likely to be comparable to similar measures presented by other issuers. Management considers it to be useful information to assist knowledgeable investors in evaluating the cash generating capabilities of the Company.

MAJOR ACHIEVEMENTS OF 2010

The most important achievement during the year was the acquisition, on April 1, 2010, of 100% of the shares of Tangent Rail Corporation ("Tangent"), a provider of wood crosstie supply chain services to the railroad industry. Tangent served the railroad industry with treated wood products, mainly railway ties, through facilities located in Warrior, Alabama; Terre Haute and Winslow, Indiana; Alexandria, Louisiana and McAlisterville, Pennsylvania. The wood preservative, creosote, was produced at its distilleries in Terre Haute, Indiana and Memphis, Tennessee. Lifecycle solutions, consisting of used tie pickup and disposal, were carried out at three facilities in Alabama, Minnesota and North Carolina. This acquisition expanded the Company's capabilities within the U.S. railway tie industry and provided the Company with creosote manufacturing operations.

The year ended December 31, 2010 marked the Company's tenth consecutive year of uninterrupted growth in revenues and net earnings. Revenues grew $149.9 million, or 36.5%, primarily as a result of the acquisition of Tangent, which contributed revenues of approximately $120.5 million over a nine-month period. Organically, sales increased approximately 13.0%, mainly reflecting greater demand in the Company's core product categories, while year-over-year fluctuations in the value of the Canadian dollar, Stella-Jones' reporting currency, versus the U.S. dollar, decreased the value of U.S. dollar denominated sales by about $23.8 million. Despite non-recurring items of approximately $5.7 million, net earnings grew 14.4% to reach $34.4 million.

Stella-Jones' solid performance once again generated strong cash flows in 2010, with cash flow from operations, before changes in non-cash working capital components, of $50.1 million, compared with $40.9 million in 2009. Although the Tangent acquisition was partially financed with debt, the Company maintained a sound balance sheet. As at December 31, 2010, the total long-term debt to equity ratio stood at 0.45:1, while the ratio of total debt to trailing 12-month EBITDA was 2.22:1.

KEY PERFORMANCE INDICATORS

For the years ended December 31	**2010**	2009	2008
(thousands of dollars, except per share data and ratios)	**$**	$	$
Sales	**561,046**	411,119	384,822
Gross profit	**103,618**	76,669	78,398
Net earnings	**34,395**	30,069	28,547
Basic net earnings per common share	**2.27**	2.38	2.29
Diluted net earnings per common share	**2.26**	2.37	2.25
Total assets	**521,633**	370,795	407,546
Total long-term debt*	**125,828**	87,080	105,759
Total long-term debt* to equity ratio	**0.45:1**	0.48:1	0.66:1
Total debt** to trailing 12-month EBITDA	**2.22**	2.43	3.21
Dividend per share	**0.38**	0.36	0.34

* Including current portion

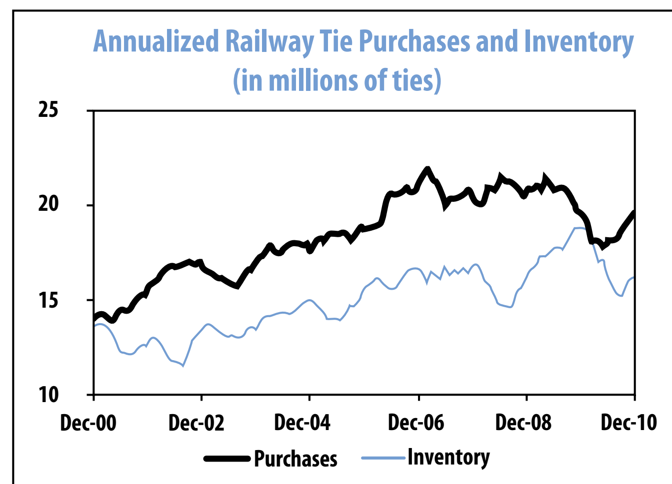
** Including short-term bank indebtedness

FOREIGN EXCHANGE

The table below shows exchange rates applicable to the periods ended December 31, 2010 and 2009. Average rates are used to translate sales and expenses for the periods mentioned, while closing rates translate assets and liabilities of self-sustaining foreign operations and monetary assets and liabilities of the Canadian operations.

Cdn$/US$		**2010**		2009
	Average	**Closing**	Average	Closing
First Quarter	**1.0576**	**1.0158**	1.2389	1.2613
Second Quarter	**1.0250**	**1.0646**	1.1820	1.1630
Third Quarter	**1.0531**	**1.0290**	1.1118	1.0707
Fourth Quarter	**1.0253**	**0.9946**	1.0694	1.0510
Fiscal Year	**1.0403**	**0.9946**	1.1505	1.0510

INDUSTRY OVERVIEW



Source: Railway Tie Association

Railway ties

As reported by the Railway Tie Association, railway tie purchases increased 0.7% to 19.7 million ties in 2010, while industry inventory decreased by 2.5 million ties to 16.2 million ties as at December 31, 2010. This inventory reduction resulted in lower purchases in the early stages of 2010, but the gradual recovery of the North American economy led to higher purchase activity in the latter half of the year. As at December 31, 2010, the inventory-to-sales ratio stood at 0.84:1, a level in keeping with the average value of the previous decade.

In the last decade, volatile fuel prices and persistent highway congestion have increasingly caused shippers to favour rail, a more fuel efficient transportation mode, over trucks. The resulting surge in rail transportation volume, combined with an aging infrastructure, yielded increased demand for products and services related to the modernization and extension of the North American rail network, including railway ties.

Driven by the ongoing economic recovery, the number of carloads hauled on North American railroads increased by 9.4% in 2010, while the volume of intermodal trailers and containers was up 14.7% from 2009 levels, according to data released by the Association of American Railroads.

OPERATING RESULTS

Sales

Sales for the year ended December 31, 2010 totalled $561.0 million, an increase of $149.9 million, or 36.5%, over last year's sales of $411.1 million. The acquisition of Tangent contributed sales of approximately $120.5 million over a nine-month period. The conversion effect from fluctuations in the value of the Canadian dollar, Stella-Jones' reporting currency, versus the U.S. dollar, decreased the value of U.S. dollar denominated sales by about $23.8 million when compared with the previous year. Organically, sales increased approximately 13.0%, reflecting higher railway tie sales in the United States and Canada as well as greater utility pole sales in Canada.

Sales by product category

Railway ties

Railway tie sales for 2010 amounted to $283.2 million, an increase of $98.1 million, or 53.0% over sales of $185.1 million in 2009. These results reflect a nine-month contribution from the Tangent operations, which added tie sales of approximately $83.0 million, as well as increased market penetration. Excluding Tangent's sales and adjusting for a negative foreign exchange effect of $16.5 million due to a lower average conversion rate on U.S. dollar denominated tie sales, year-over-year comparable railway tie sales increased $31.7 million. While industry demand and pricing remained weak in the first quarter of 2010, the steady recovery in the North American economy resulted in improved market conditions as the year progressed. Railway tie sales accounted for 50.5% of the Company's total sales in 2010.

Utility poles

Utility pole sales amounted to $166.7 million in 2010, an increase of 11.4% over sales of $149.7 million in 2009. The progression is mainly due to higher sales of distribution poles in both Canada and the United States stemming from solid maintenance demand and greater market penetration. Meanwhile, sales of transmission poles rose in Canada, but were lower in the United States. The transmission pole market is more affected by the timing of orders, mostly for special projects. The negative conversion effect on U.S. dollar denominated sales reduced utility pole sales by approximately $4.8 million. Utility pole sales accounted for 29.7% of the Company's total sales in 2010.

Industrial products

Industrial product sales rose 81.7% in 2010, reaching $81.4 million, compared with $44.8 million in 2009. This $36.6 million increase is essentially attributable to Tangent's operations related to coal tar distillation and lifecycle solutions, including used tie pickup and disposal services. Excluding Tangent, sales declined marginally due to a negative conversion effect of approximately $2.5 million on U.S. dollar denominated sales. Industrial products represented 14.5% of overall sales in 2010.

Residential lumber

Sales in the residential lumber category totalled $29.8 million in 2010, down 5.6% from $31.5 million in 2009. The decrease reflects reduced renovation spending in Canada as a result of unfavourable weather during the peak summer period and the expiry of the home renovation tax credit program at the beginning of 2010. The Company does not sell residential lumber into the U.S. market. Residential lumber accounted for 5.3% of Stella-Jones' total sales in 2010.

Sales by destination

In 2010, sales in Canada grew 14.5% over 2009 levels, reaching $215.3 million, or 38.4% of Stella-Jones' total sales. The year-over-year sales increase of $27.3 million is entirely attributable to the Company's core railway tie and utility pole product categories.

Sales in the United States amounted to $345.7 million, or 61.6% of sales, representing an increase of $122.6 million, or 54.9%, over 2009. The increase reflects the Tangent acquisition and solid organic growth in the railway tie product category, partially offset by a lower conversion rate on U.S. dollar denominated sales. Sales of products exported to the United States from the Canadian-based facilities totalled $10.7 million in 2010, compared with $13.1 million in 2009, as the Company continues to optimize its asset base through plant specialization.

Gross profit

Gross profit reached $103.6 million or 18.5% of sales in 2010, up from $76.7 million or 18.6% of sales in 2009. The increase in gross profit dollars essentially reflects the contribution of the Tangent operations, partially offset by a lower average rate applied to convert gross profit from U.S. dollar denominated sales. The marginal reduction in gross profit as a percentage of sales mainly stems from a different product mix, more heavily weighted towards railway ties.

Cost of sales in 2009 also included $511,600 (US$468,600) for plant modifications and workforce reduction costs in connection with the termination of treating operations at the Stanton, Kentucky facility and the downsizing of the Spencer, West Virginia facility. Excluding these non-recurring items, gross profit for 2009 was $77.2 million, or 18.8% of sales.

Expenses

Selling and administrative expenses for 2010 were $29.6 million, compared with 2009 expenses of $20.4 million. This increase is attributable to expenses from the Tangent operations as well as to approximately $5.3 million in non-recurring expenses consisting of acquisition costs directly related to the purchase of Tangent, severance expenses, as well as a provision for an unfavourable legal judgement. Conversely, non-recurring net revenues of $2.6 million related to the sale of certain assets of the Terre Haute, Indiana facility were recorded in the fourth quarter. As a percentage of sales, selling and administrative expenses were 5.3% of sales in 2010, compared to 5.0% in the prior year.

During the year ended December 31, 2010, the Company recorded asset impairment charges of $3.0 million for the Spencer, West Virginia facility and the Ripley, West Virginia U.S. corporate office. These charges were mostly recorded in earnings during the second quarter. In the year ended December 31, 2009, asset impairment charges of $833,000 were recorded for the Stanton, Kentucky facility and the former Ripley, West Virginia U.S. corporate office.

Stella-Jones realized a foreign exchange loss of $44,000 for the year ended December 31, 2010, versus a foreign exchange gain of $1.4 million last year.

The Company's exposure to foreign exchange gains or losses from currency fluctuations is related to its sales and purchases in U.S. dollars by its Canadian based operations. Stella-Jones U.S. Holding Corporation, the Company's wholly-owned U.S. subsidiary, is a self-sustaining foreign operation and unrealized foreign exchange gains and losses on translating its financial statements are deferred in shareholders' equity. The Company monitors its transactions in U.S. dollars generated by Canadian based operations. Its basic hedging activity for economic purposes consists of entering into forward foreign exchange contracts for the sale of U.S. dollars and purchasing certain goods and services in U.S. dollars. The Company will also consider forward foreign exchange contracts for the purchase of U.S. dollars for significant purchases of goods and services that are not covered by natural hedges.

The non-cash loss on forward foreign exchange contracts resulting from the change in their mark-to-market values as at December 31, 2010, compared to September 30, 2010, totalled $64,000, whereas the non-cash gain from the change compared to December 31, 2009, was $19,000. As at December 31, 2010, the Company had no forward foreign exchange contracts outstanding.

Amortization of capital and intangible assets totalled $10.4 million in 2010, an increase of $1.6 million over 2009. This increase reflects the amortization of Tangent's capital and intangible assets, partially offset by a change in accounting estimates, applied prospectively from October 1, 2009, that increased the useful life of certain capital assets in order to better reflect the period over which they are consumed.

Financial expenses for 2010 amounted to $10.6 million, up from $8.5 million in 2009. The $2.1 million increase in financial expenses is due to higher borrowings to partially finance the acquisition of Tangent, partly offset by lower Canadian dollar interest charges on the conversion of U.S. dollar denominated debt.

Earnings before income taxes and income tax expense

Stella-Jones generated earnings before income taxes of $50.1 million, or 8.9% of sales, in 2010. This represents an increase of $8.3 million, or 19.8%, over earnings before income taxes of $41.8 million, or 10.2% of sales, in the prior year. Excluding non-recurring expenses and revenues as well as asset impairment charges, earnings before income taxes for 2010 were approximately $55.8 million, or 9.9% of sales, a percentage comparable with the level achieved a year earlier.

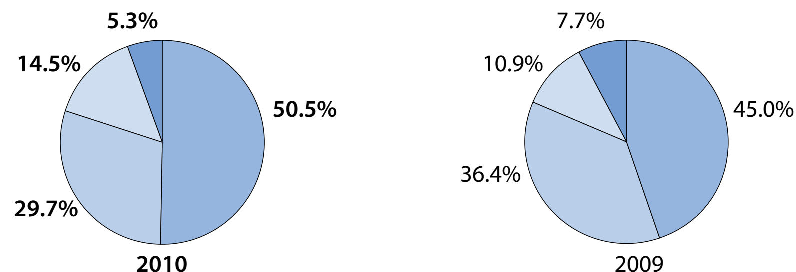
Stella-Jones' income tax expense totalled $15.7 million in 2010, representing an effective tax rate of 31.3%. In 2009, the income tax expense stood at $11.7 million, equivalent to an effective tax rate of 28.1%. The higher effective tax rate for 2010 is essentially related to a higher proportion of revenue generated in the United States that is subject to a higher statutory tax rate as well as to non-deductible items related to the Tangent acquisition.

Net earnings

Net earnings for the year totalled $34.4 million, or $2.26 per share, fully diluted, compared with $30.1 million, or $2.37 per share, fully diluted, in 2009. This represents a year-over-year increase in net earnings of $4.3 million, or 14.4%. The exchange of subscription receipts for common shares on April 1, 2010 to partially finance the Tangent acquisition increased the 2010 weighted average number of shares outstanding used for the calculation of fully diluted earnings per share by approximately 19.7% over 2009.

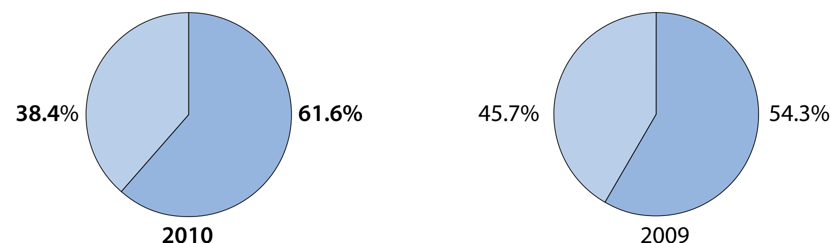
Sales by product (% of revenues)

- Railway Ties 50.5% (2009 – 45.0%)
- Utility Poles 29.7% (2009 – 36.4%)
- Industrial Products 14.5% (2009 – 10.9%)
- Residential Lumber 5.3% (2009 – 7.7%)



Sales by geographic region (% of revenues)

- United States 61.6% (2009 – 54.3%)
- Canada 38.4% (2009 – 45.7%)



BUSINESS ACQUISITION

On April 1, 2010, the Company completed the acquisition of 100% of the shares of Tangent, a provider of wood crosstie supply chain services to the railroad industry. Tangent served the railroad industry with treated wood products, mainly railway ties, through facilities located in Warrior, Alabama; Terre Haute and Winslow, Indiana; Alexandria, Louisiana and McAlisterville, Pennsylvania. The wood preservative, creosote, was produced at its distilleries in Terre Haute, Indiana and Memphis, Tennessee. Lifecycle solutions, consisting of used tie pickup and disposal, were carried out at three facilities in Alabama, Minnesota and North Carolina. This acquisition expanded the Company's capabilities within the U.S. railway tie industry and provided the Company with creosote manufacturing operations.

Total cash outlay associated with the acquisition was approximately $172.7 million (US$170.0 million), including cash on hand of $6.8 million (US$6.7 million) and excluding acquisition costs of approximately $2.0 million (US$2.0 million). This amount includes $90.4 million (US$89.0 million) paid to Tangent's shareholders, $81.3 million (US$80.1 million) used to reimburse Tangent's debts with financial institutions and $1.0 million (US$0.9 million) to pay accrued interest on these debts.

The acquisition has been accounted for using the acquisition 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. During the fourth quarter, the Company adjusted the value of certain assets as well as goodwill, future income tax liabilities and accrued liabilities. The results of operations of Tangent have been included in the Company's consolidated financial statements from the acquisition date.

The following is a summary of the net assets acquired at fair value as at the acquisition date. The original transaction was made in US dollars and converted into Canadian dollars as at the acquisition date.

	$
(tabular information presented in thousands of dollars)	
Assets acquired	
Non-cash working capital	48,603
Capital assets	22,734
Customer relationships	20,905
Customer backlog	670
Creosote registration	31,723
Non-deductible goodwill	70,239
Future income tax assets	615
	195,489
Liabilities assumed	
Accounts payable and accrued liabilities	5,290
Long-term debt	81,340
Site remediation obligation	1,311
Future income tax liabilities	23,983
Total consideration	83,565
Consideration	
Cash	172,694
Payment of accrued interest	(956)
Payment of long-term debt	(81,340)
Cash on hand	(6,833)
Purchase consideration for shares	83,565

The Company's valuation of intangible assets has identified customer relationships, a creosote registration and customer backlog. The assigned useful lives for customer relationships are between 6 to 10 years and 3 months for the customer backlog. The creosote registration is not subject to amortization as the Company considers it to have an infinite useful life.

Goodwill value is determined as the excess of the total consideration over the estimated fair value of tangible and intangible assets acquired as well as liabilities assumed. Goodwill is not amortized, not deductible for tax purposes and represents the future economic value associated with the increased railroad network access, acquired workforce and synergies with the Company's operations.

The following table presents a roll forward of the intangible assets and goodwill net book value balances from December 31, 2009 to December 31, 2010:

(tabular information presented in thousands of dollars)	Intangible assets				
	Customer Relationships $	Non-compete Agreements $	Creosote Registration $	Total Intangible assets $	Goodwill $
Year ended December 31, 2009					
Cost	4,603	5,980	—	10,583	5,494
Accumulated amortization	(1,259)	(1,744)	—	(3,003)	—
Net book amount as at December 31, 2009	3,344	4,236	—	7,580	5,494
Year ended December 31, 2010					
Opening net book balance	**3,344**	**4,236**	—	**7,580**	**5,494**
Addition of Tangent customer relationships	**20,905**	—	—	**20,905**	—
Addition of Tangent customer backlog	**670**	—	—	**670**	—
Addition of Tangent creosote registration	—	—	**31,723**	**31,723**	—
Addition of Tangent goodwill	—	—	—	—	**70,239**
Amortization	**(3,586)**	**(986)**	—	**(4,572)**	—
Exchange differences	**(473)**	**(185)**	**(662)**	**(1,320)**	**(1,760)**
Net book amount as at December 31, 2010	**20,860**	**3,065**	**31,061**	**54,986**	**73,973**

Financing for the transaction was secured through an $80,050,000 private placement of subscription receipts which successfully closed on March 15, 2010, as well as through the issuance to the Solidarity Fund QFL of a $25,395,000 (US$25,000,000) unsecured, subordinated and non-convertible debenture, the addition of a $40,632,000 (US$40,000,000) syndicated bank term facility which successfully closed on March 24, 2010, and the increase of existing operating debt facilities. Underwriting and legal fees related to the private placement of subscription receipts amounted to $3,147,000, generating net proceeds of $76,903,000. The subscription receipts were exchanged as at the close of business, April 1, 2010, for common shares in the share capital of the Company on the basis of one common share per subscription receipt. Holders of subscription receipts did not need to take any action in order to receive the common shares to which they were entitled. As the subscription receipts were sold on a private placement basis, these common shares were subject to regulatory restrictions on resale until July 16, 2010.

Tangent's sales and net earnings before income taxes in the nine-month period ended December 31, 2010 were $120,456,000 and $8,923,000, respectively. On a pro forma basis, Management's estimate of the sales and net earnings before income taxes of the combined Company and Tangent's operations, for the twelve-month period ended December 31, 2010, would have been approximately $601,360,000 and $54,924,000, respectively, had the Tangent acquisition occurred as of January 1, 2010. To arrive at the pro forma estimates, Management has considered the financing structure resulting from the acquisition as well as other acquisition adjustments.

QUARTERLY RESULTS

The Company's sales follow a seasonal pattern, with railway tie, utility pole and industrial lumber shipments strongest in the second and third quarters to provide industrial end users with product for their summer maintenance projects. Residential lumber treatment sales also follow a similar seasonal pattern. In the fall and winter seasons, there tends to be less activity; thus the first and fourth quarters are typically characterized by relatively lower sales levels.

After posting lower sales in the first quarter of 2010, compared with the corresponding period in 2009, the acquisition of Tangent, combined with a healthier North American economy, resulted in solid year-over-year revenue growth in the final nine months of 2010. These gains were achieved in spite of the stronger year-over-year value of the Canadian dollar, Stella-Jones' reporting currency, against the U.S. dollar, which reduced the conversion rate applicable to the Company's revenue stream generated in U.S. dollars. Year-over-year variations in operating earnings essentially reflected the same factors, as well as synergies and efficiencies stemming from the integration of the Tangent operations.

The table below sets forth selected financial information for the Company's last eight quarters ending with the most recently completed financial year:

2010 **For the quarters ended** (thousands of dollars, except per share data)	**March 31** **$**	**June 30** **$**	**Sept. 30** **$**	**Dec. 31** **$**	**Total** **$**
Sales	**99,360**	**167,317**	**161,298**	**133,071**	**561,046**
Operating earnings before amortization of capital and intangible assets [1]	**12,266**	**14,202**	**22,498**	**22,033**	**70,999**
Operating earnings [1]	**10,500**	**11,325**	**19,522**	**19,297**	**60,644**
Net earnings	**5,814**	**5,610**	**12,218**	**10,753**	**34,395**
Net earnings per common share					
Basic	**0.46**	**0.35**	**0.77**	**0.68**	**2.27**
Diluted	**0.46**	**0.35**	**0.77**	**0.67**	**2.26**

2009 For the quarters ended (thousands of dollars, except per share data)	March 31 $	June 30 $	Sept. 30 $	Dec. 31 $	Total $
Sales	111,954	129,104	104,671	65,390	411,119
Operating earnings before amortization of capital and intangible assets [1]	15,924	20,976	15,272	6,851	59,023
Operating earnings [1]	13,313	18,475	13,376	5,104	50,268
Net earnings	7,687	11,021	8,320	3,041	30,069
Net earnings per common share					
Basic	0.61	0.87	0.66	0.24	2.38
Diluted	0.61	0.87	0.65	0.24	2.37

[1] Operating earnings before amortization of capital and intangible assets and operating earnings are financial measures not prescribed by Canadian generally accepted accounting principles ("GAAP") and are not likely to be comparable to similar measures presented by other issuers. Management considers they represent useful information for comparison with other similar operations in our industry, as they present financial results related to industry practice, not affected by non-cash charges or capital structure. Operating earnings before amortization of capital and intangible assets and operating earnings are readily reconcilable to net earnings presented in our Canadian GAAP financial statements, as there are no adjustments for unusual or non-recurring items.

Note: due to rounding, the sum of results for the quarters may differ slightly from the total shown for the full year.

Fourth quarter results

Sales for the fourth quarter of 2010 reached $133.1 million, up from $65.4 million reported for the same period in 2009. This $67.7 million increase is attributable to a $37.1 million contribution from the Tangent operations, solid demand for the Company's core products and strong advanced deliveries of railway ties. Of note, sales in the fourth quarter of 2009 were negatively affected by soft demand in most product categories and little advanced shipments of railway ties. The stronger year-over-year value of the Canadian dollar, Stella-Jones' reporting currency, decreased the value of U.S. dollar denominated sales by approximately $2.1 million.

Fourth quarter sales of railway ties amounted to $62.4 million, up from $22.1 million a year earlier. This increase reflects a $26.6 million contribution from the Tangent operations and stronger industry demand. The fourth quarter of 2009 also witnessed a significant reduction in advanced deliveries to Class 1 railway operators for their regular maintenance programs of the following year, as purchases were deferred to keep tie inventory levels down. Utility pole sales reached $48.7 million, compared with $31.1 million in the fourth quarter of 2009. This increase is mostly attributable to higher sales of distribution and transmission poles in Canada. Industrial product sales amounted to $19.8 million, up from $10.1 million a year earlier, due essentially to a $10.6 million contribution from the Tangent operations. Finally, residential lumber sales rose 5.6% to $2.2 million, up from $2.1 million last year.

Gross profit in the fourth quarter of 2010 totalled $27.2 million, or 20.5% of sales, compared with $10.6 million, or 16.2% of sales, in the corresponding period in 2009. The increase in gross profit dollars essentially reflects the contribution of the Tangent operations and strong organic growth, partially offset by a lower average rate applied to convert gross profit from U.S. dollar denominated sales. The increase in gross profit as a percentage of sales principally reflects the improved plant efficiencies from higher volumes, lower costs for certain raw materials, and higher selling prices.

Net earnings for the period totalled $10.8 million, or $0.67 per share, fully diluted, compared with $3.0 million, or $0.24 per share, fully diluted, in the fourth quarter of 2009.

BALANCE SHEET

The Company's working capital at December 31, 2010 was $192.4 million, an increase of $22.3 million over a working capital balance of $170.1 million at December 31, 2009. Current assets amounted to $272.2 million at the end of 2010 compared with $254.6 million twelve months earlier. Most of this increase is attributable to accounts receivable related to Tangent's operations and the reduction in bank indebtedness.

The value of accounts receivable was $56.3 million as at December 31, 2010 compared with $30.2 million at the same date in 2009. This increase essentially reflects the addition of Tangent's accounts receivable as well as stronger year-over-year demand for the Company's core products in the fourth quarter, partially offset by a lower conversion rate applicable to U.S. dollar denominated receivables. Excluding Tangent, accounts receivable would have been $40.6 million as at December 31, 2010.

Inventories stood at $205.3 million, down from $212.6 million a year earlier. This decrease is due to strong demand for the Company's products and the impact of local currency depreciation on U.S. based inventory which more than offset the addition of Tangent's inventory. Excluding the latter, inventories would have been $172.1 million.

Because of the long periods required to air season wood, which can occasionally exceed nine months before a sale is concluded, inventories are a significant component of working capital. However, solid relationships and long-term contracts with certain customers enable the Company to better ascertain inventory requirements. The Company believes that its cash flow from operations and available operating lines of credit are adequate to meet its working capital requirements for the foreseeable future.

Capital assets stood at $114.0 million as at December 31, 2010, compared with $96.9 million as at December 31, 2009. This $17.1 million increase is essentially related to the addition of Tangent's capital assets, partially offset by local currency depreciation on U.S. based capital assets. Excluding Tangent, the value of capital assets would have been $91.6 million.

Owing to the Tangent acquisition, the value of intangible assets and goodwill reached $55.0 million and $74.0 million, respectively, as at December 31, 2010. Intangible assets include customer relationships, the discounted value of the non-compete agreements and Tangent's creosote registration. As at December 31, 2009, intangible assets and goodwill were $7.6 million and $5.5 million, respectively.

Bank indebtedness at the end of 2010 totalled $31.9 million, down from $56.1 million at the end of 2009. This $24.2 million reduction mainly results from a solid cash flow generation and improved working capital. As at December 31, 2010, the credit facilities supporting bank indebtedness include a $50.0 million demand operating loan ($50.0 million as at December 31, 2009), as well as a US$75.0 million demand operating loan (US$45.0 million as at December 31, 2009), both made available by a syndicate of bank lenders. Combined availability under the Company's Canadian and U.S. demand operating loans was $84.1 million as at December 31, 2010.

The Company believes that these demand operating loans, combined with its funds from operations in the next quarters, will be adequate to meet its cash requirements for the foreseeable future. However, future acquisitions, if any, may require new sources of financing.

As at December 31, 2010, the Company's long-term debt, including the current portion, amounted to $125.8 million, up from $87.1 million as at December 31, 2009. This increase is essentially due to the issuance to the Solidarity Fund QFL of a US$25.0 million (Cdn$25.4 million) unsecured, subordinated and non-convertible debenture and the addition of a US$40.0 million (Cdn$40.6 million) term facility to partially finance the acquisition of Tangent. These factors were partially offset by scheduled principal repayments of $9.3 million, an accelerated repayment of a $10.0 million unsecured and non-convertible debenture owing to the Solidarity Fund QFL, an accelerated payment of US$3.0 million on the new US$40.0 million term loan, an accelerated payment of $1.5 million on a revolving term loan with a Canadian bank and accelerated payments of US$1.1 million on capital leases, as well as favourable currency movements that decreased the conversion rate of U.S. dollar denominated long-term debt into Canadian currency. All of the unscheduled payments were made in the fourth quarter.

Shareholders' equity was $281.4 million as at December 31, 2010 compared with $180.0 million as at December 31, 2009. This increase of $101.4 million is mostly attributable to net proceeds of $76.9 million from the issuance of subscription receipts to partially finance the acquisition of Tangent and strong earnings generation of $34.4 million, partially offset by dividend payments on common shares totalling $6.0 million. The subscription receipts were exchanged, without additional payment, into common shares of the Company on a one-for-one basis upon completion of the acquisition on April 1, 2010. Book value stood at $17.67 per common share as at December 31, 2010, up from $14.19 per share as at December 31, 2009.

LIQUIDITY AND CAPITAL RESOURCES

The following table sets forth summarized cash flow components for the periods indicated:

Summary of cash flows (thousands of dollars)	**Fiscal Year Ended**	
	December 31, 2010	December 31, 2009
	$	$
Operating activities	**81,608**	40,481
Financing activities	**7,775**	(36,220)
Investing activities	**(89,383)**	(4,261)
Cash and cash equivalents	**—**	—

The Company's activities, acquisitions and capital expenditures are primarily financed by cash flows from operating activities, the use of cash raised from operating lines of credit and long-term debt, and the issuance of common shares. The Company's operating lines of credit are demand operational facilities that are renewable annually and are subject to review by the Company's bankers at intervals no greater than one year. The Company anticipates no difficulties in its ability to renew these demand operating facilities.

Cash flow from operating activities before changes in non-cash working capital components was $50.1 million for the year ended December 31, 2010, compared with $40.9 million for the prior year. This increase mostly reflects higher net earnings for the period as well as a positive variation in non-cash expenses resulting from asset impairment charges and the reversal of a gain on derivative financial instruments recognized in 2009.

Changes in non-cash working capital components provided liquidity of $31.5 million compared with a liquidity reduction of $0.5 million a year ago. The improvement essentially results from a $31.3 million decrease in inventories. In addition, an $11.6 million increase in accounts receivable was partially offset by a $9.8 million increase in accounts payable and accrued liabilities; both factors reflect higher business activity. As a result, operating activities provided liquidity of $81.6 million for the year ended December 31, 2010, versus $40.5 million a year earlier.

Financing activities for the year ended December 31, 2010 provided funds of $7.8 million, as opposed to requiring liquidity of $36.2 million for the corresponding period a year earlier. Main factors explaining this cash generation include proceeds from the $76.9 million issuance of subscription receipts to partially finance the Tangent acquisition, which were to a large extent offset by a net decrease in long-term debt totalling $37.9 million, which includes the repayment of the Tangent debt on the date of acquisition, and a decrease in short-term bank indebtedness of $23.1 million.

Investing activities required $89.4 million in cash during 2010, of which $83.6 million is attributable to the Tangent acquisition. Purchases of capital assets totalled $6.1 million, mainly for the addition of various equipment upgrades and expansion. For the year ended December 31, 2009, cash flows from investing activities reduced liquidity by $4.3 million.

The following table details the maturities of the financial obligations as at December 31, 2010:

(in thousands of dollars)	Carrying Amount $	Contractual Cash flow $	Less than 1 year $	1 – 3 years $	4 – 5 years $	After 5 years $
Bank indebtedness[1]	31,923	32,736	32,736	—	—	—
Accounts payable and accrued liabilities	33,266	33,266	33,266	—	—	—
Long-term debt obligations[1]	125,828	160,148	17,903	36,741	59,689	45,815
Interest rate swaps						
Outflow	—	2,635	1,136	1,042	457	—
Inflow	—	(1,443)	(433)	(595)	(415)	—
Other contractual obligations	—	23,705	5,785	6,893	2,128	8,899
Non-compete agreements	4,041	4,041	1,243	2,486	312	—
Total	195,058	255,088	91,636	46,567	62,171	54,714

[1] Amounts include capital and interest

SHARE AND STOCK OPTION INFORMATION

As at December 31, 2010, the capital stock issued and outstanding consisted of 15,922,668 common shares (12,684,325 as at December 31, 2009). The following table presents the outstanding capital stock activity for the year ended December 31, 2010:

Year Ended December 31, 2010	Number of shares (in '000s)
Balance – Beginning of period	12,684
Stock option plan	25
Exchange of subscription receipts for common shares	3,202
Employee share purchase plans	12
Balance – End of period	**15,923**

As at March 10, 2011, the capital stock issued and outstanding consisted of 15,931,668 common shares. As at December 31, 2010, the number of outstanding options to acquire common shares issued under the Company's Stock Option Plan was 181,000 (December 31, 2009 – 197,785) of which 128,300 (December 31, 2009 – 126,185) were exercisable. As at March 10, 2011, the number of outstanding options was 172,000, of which 119,300 were exercisable.

DIVIDENDS

On March 10, 2011, the Board of Directors declared a semi-annual dividend of $0.24 per common share payable on May 13, 2011 to shareholders of record at the close of business on April 1, 2011. On August 11, 2010, the Board of Directors declared a semi-annual dividend of $0.20 per common share.

The declaration, amount and date of any future dividends will continue to be considered by the Board of Directors of the Company based upon and subject to the Company's earnings and financial requirements, covenants in its loan documentation and other conditions prevailing at the time. There can be no assurance as to the amount or timing of such dividends in the future.

COMMITMENTS AND CONTINGENCIES

The Company is from time to time involved 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.

The Company has issued guarantees amounting to $30,722,896 (2009 – $14,583,548) 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 and, as such, no provisions have been recorded in the financial statements.

The Company's operations are subject to Canadian Federal and Provincial as well as U.S. 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.

CURRENT ECONOMIC CONDITIONS

Operations

The Company's core railway tie and utility pole product categories are integral to the North American basic transportation and utility infrastructure. Such infrastructure needs to be regularly maintained, which provides Stella-Jones with relatively steady demand for its core products. In periods of economic growth, the Company may also benefit from additional demand stemming from expansions to the railway and telecommunication networks.

Based on current market conditions, Management continues to expect business activity to further improve in the upcoming quarters. Increased freight volume on North American railroads should lead to greater investments in the continental rail network, including ties, as operators constantly seek optimal line efficiency. Demand is expected to steadily progress in utility poles, as regular maintenance projects provide a stable business flow for distribution poles, while the vigour of the transmission pole market is more correlated to the timing of orders, mostly for special projects.

Liquidity

As at December 31, 2010, the Company is in full compliance with its debt covenants and contractual obligations. In addition, it has a combined availability under the Company's Canadian and U.S. demand operating loans of $84.1 million as at December 31, 2010.

Management considers that substantially all receivables are fully collectible as major customers, mainly Class 1 railroad operators and large-scale utility service providers, have good credit standing and limited history of default. Nevertheless, Management is providing additional focus on accounts receivable collection and credit extensions. As at December 31, 2010, 58.3% of accounts receivable were current (58.8% as at December 31, 2009) and only 5.8% were past due more than 60 days (2.3% as at December 31, 2009).

Despite acquiring Tangent, inventories decreased during 2010 largely due to strong demand for the Company's products. To ensure efficient treatment operations, given that air-dried wood reduces treatment cycles, inventory turnover has historically been relatively low. Nevertheless, Management continuously monitors the levels of inventory and market demand for its products. Production is adjusted accordingly to optimize efficiency and capacity utilization.

RISKS AND UNCERTAINTIES

Environmental laws and regulations

The Company is subject to a variety of environmental laws and regulations, including those relating to emission to the air, discharges into water, releases of hazardous and toxic substances, and remediation of contaminated sites ("Environmental Laws"). These Environmental Laws require the Company to obtain various environmental registrations, licenses, permits and other approvals, as well as carry out inspections, compliance testing and meet timely reporting requirements in order to operate its manufacturing and operating facilities.

The enforcement of these Environmental Laws by regulatory agencies will continue to affect the Company's operations by imposing operating and maintenance costs and capital expenditures required for compliance. Failure to comply could result in civil or criminal enforcement actions which could result, among others, in the payment of substantial fines, often calculated on a daily basis, or in extreme cases, the disruption or suspension of operations at the affected facility. To mitigate this risk, the Company dedicates ongoing financial expenditures and carries out localized training and internal inspections of its facilities in order to ensure compliance with applicable plant specific permits and Environmental Laws. The potential financial impact of all environmental protection and compliance expenditures on the Company during the year 2011 is not expected to be material.

Under various federal, provincial, state and local laws and regulations, the Company could, as the owner, lessor or operator, be liable for the costs of removal or remediation of contamination at its sites. The remediation costs and other costs required to clean up or treat contaminated sites could be substantial. However, in certain cases, the Company benefits from indemnities from the former owners of its sites. Contamination on and from the Company's sites may subject it to liability to third parties or governmental authorities for injuries to persons, property or the environment and could adversely affect the Company's ability to sell or rent its properties or to borrow money using such properties as collateral.

The possibility of major changes in environmental laws and regulations is another risk faced by the Company. While it is not possible to predict the outcome and nature of these changes, they could substantially increase the Company's capital expenditures and compliance costs at the facilities affected. Management believes that its commitment to the environmental integrity of the Company's plants and operations, supported by significant investments toward that end, will allow the Company to continue to meet the applicable regulatory requirements.

Environmental Litigation

While the Company has been party to environmental litigation in the past, which have included, among others, claims for adverse physical effects and diminution of property value, the outcomes and associated costs have not been material. There is, however, no guarantee that this will continue to be the case in the future, as the result of disputes regarding environmental matters and conclusions of environmental litigation cannot be predicted.

Reputational Risk

The Company's business has grown and its image strengthened, in large part by its consistent production and delivery of high quality products, while maintaining as well, a high level of environmental responsibility. Claims of environmentally irresponsible practices by regulatory authorities or local communities could harm the reputation of the Company. Adverse publicity resulting from actual or perceived violations of Environmental Laws could negatively impact customer loyalty, reduce demand, lead to a weakening of confidence in the marketplace and ultimately, a reduction of the Company's share price. These effects could result even if the allegations are not valid and the Company is not found liable.

Availability and cost of raw materials

Management considers that the Company may be affected by the industry-wide concerns of long-term availability of competitively priced wood and potential fluctuations in wood prices. Nevertheless, the Company's overall competitiveness in this industry is strengthened by its access to a high quality timber supply provided by its long-term cutting licenses and its long-standing relationships with private woodland owners and other suppliers.

In addition, there are a limited number of suppliers for certain of the preservatives that the Company employs in its production process, which lessens the availability of alternate sources of supply in the event of unforeseen shortages or disruptions of production. The Company is mitigating this risk by researching and identifying alternate suppliers outside of its traditional sources of supply. The April 2010 acquisition of Tangent, along with its registration for the production of the wood preservative, creosote, has further mitigated this risk.

Currency risk

The Company is exposed to currency risks due to its export of goods manufactured in Canada. These risks are, for the most part, covered by purchases of goods and services denominated in U.S. dollars. The Company may also use foreign exchange forward contracts to hedge contracted net cash inflows and outflows of U.S. dollars.

Interest rate fluctuations

As at December 31, 2010, the Company had limited exposure to interest rate risk on long-term debt after giving effect to its interest rate swaps; 35.0% (2009 – 14.0%) of the Company's long-term debt is at variable 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.

Credit risk

The geographic distribution of customers and procedures regarding commercial risk management limit the concentration of credit risks. Trade accounts receivable include an element of credit risk should the counterparty be unable to meet its obligations. The Company reduces this risk by dealing primarily with utility and telecommunication companies and other major corporations.

OFF-BALANCE SHEET ARRANGEMENTS AND FINANCIAL INSTRUMENTS

For details pertaining to off-balance sheet arrangements and financial instruments, refer to Note 19 to the Company's audited consolidated financial statements for the year ended December 31, 2010.

SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES

The Company's significant accounting policies are described in Note 2 to the December 31, 2010 audited consolidated financial statements.

The Company prepares its consolidated financial statements in conformity with Canadian GAAP which 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 dates of the financial statements and the reported amounts of revenues and expenses during the reported periods. 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.

Significant items subject to estimates and assumptions include the estimated useful life of assets, impairment of long-lived assets and business combinations.

CHANGES IN ACCOUNTING POLICIES

The CICA issued the following new accounting standards which were adopted by the Company effective January 1, 2010:

Section 1582, "Business Combinations", replaces Section 1581 of the same title. The new Section establishes standards for the accounting for a business combination. It provides the Canadian equivalent to International Financial Reporting 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. The Company applied this new standard effective January 1, 2010, as early adoption is permitted. As a result of the application of this new accounting standard, previously capitalized transaction costs of approximately $328,000 were expensed in the current period. Effective January 1, 2010, expenses of a similar nature are recorded to results in the period in which they occurred.

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 International Accounting Standard ("IAS") 27 (Revised), "Consolidated and Separate Financial Statements". The Company applied these new standards effective January 1, 2010, as early adoption is permitted. Their adoption had no significant impact on the Company's consolidated financial statements.

UPCOMING CHANGES TO ACCOUNTING POLICIES

The Company will cease to prepare its financial statements in accordance with Canadian GAAP as set out in Part V of the CICA Handbook – Accounting, for the periods beginning on January 1, 2011, when it will start to apply, as its primary basis of accounting, IFRS as published by the International Accounting Standards Board ("IASB") and set out in Part I of the CICA Handbook – Accounting. Consequently, future accounting changes to Canadian GAAP are not discussed in the consolidated financial statements as they will normally never be applied by the Company.

INTERNATIONAL FINANCIAL REPORTING STANDARDS

In February 2008, the Canadian Accounting Standards Board ("AcSB") confirmed that Canadian publicly listed companies will be required to use IFRS in the preparation of financial statements for fiscal years beginning on or after January 1, 2011. IFRS uses a conceptual framework similar to Canadian GAAP, but there are significant differences in recognition, measurement and disclosures.

Management has established an IFRS implementation team to develop an IFRS changeover plan. In 2008, a preliminary diagnostic analysis (phase I) was prepared by external consultants who identified the key areas where changes in accounting policy may have some impact on the Company's consolidated financial statements.

The Company is presently in the phase II stage of its changeover plan, which includes a definition of roles and responsibilities, a review of the differences between current Canadian GAAP (as applied by the Company) and IFRS, and the analysis of possible options regarding adoption. Phase II is practically completed and the consequences of most of the changes have been determined. Management is presently in the process of finalizing the Company's opening balance sheet as of January 1, 2010 to precisely establish and document the changes to be made to accounting principles and computer systems, training requirements, internal control mechanisms for financial reporting and the repercussions on the Company's business activities. The preparation of the transition to IFRS note, including the reconciliation between Canadian GAAP and IFRS, is also in process. That note will be included in the Company's March 31, 2011 interim unaudited consolidated financial statements.

In the period leading up to the changeover, the Company continues to monitor standards to be issued by the IASB, because the IASB work plan expects the completion of several projects in calendar year 2011.

Set out below are the key areas where changes in accounting policies may impact the Company's consolidated financial statements. It is intended to highlight those areas the Company believes to be most significant. However, the analysis of changes is still in process and not all decisions have been finalized since alternative accounting policies are available.

Property, plant and equipment

IAS 16 – Property, plant and equipment permits assets to be measured based on either a cost model or a revaluation model. Under a revaluation model, an item of property, plant and equipment is carried at a revalued amount, being the fair value at the date of the revaluation.

The property, plant and equipment ("capital assets") review and analysis has been completed. The Company plans to continue to use the cost model under IFRS. No significant adjustment is expected from the adoption of this standard.

Leases

The company undertook a detailed review of material lease arrangements in order to determine the appropriate lease classification under IFRS.

After reviewing lease contracts subject to IAS 17, the Company concluded that finance and operational leases are properly classified.

Cutting rights and standing timber

Cutting rights contracts have been analyzed to determine if they should be considered under IAS 17, Leases or under IAS 38, Intangible Assets. This analysis has been completed and Management concluded that cutting rights should be recorded under intangible assets.

As at December 31, 2009, cutting rights were accounted for as part of capital assets. Under IFRS, the Company will have to reclassify these assets from capital assets to intangible assets on the balance sheet. This reclassification will be for a net book value of $6.1 million. Standing timber, will, under IAS 38, also have to be reclassified under intangible assets. This reclassification will be for a net book value of $3.1 million.

Joint ventures

Under Canadian GAAP, the 50% interest that the Company has in Kanaka Creek Pole Company Limited ("Kanaka") is accounted for under the proportionate consolidation method. Essentially, 50% of the balance sheet and profit and loss statement of Kanaka are added to the Company's consolidated financial statements. An exposure draft (ED 9) proposes to remove the option to use the proportionate consolidation method for jointly controlled entities. However, the new standard is not published yet and since there might be changes between ED 9 and the final standard, the Company has decided to wait before making any adjustment to its accounting policy regarding joint ventures.

The documentation for joint venture accounting is in place and no additional disclosures will be required, based on the current standards.

Financial instruments

Effective January 1, 2008, the Company adopted CICA handbook Section 3862 – Financial Instruments - Disclosure and handbook Section 3863 - Financial Instruments - Presentation. These new sections were introduced to better harmonize Canadian GAAP to IFRS by incorporating many of the concepts found in IAS 32 - Financial Instruments Presentation and IAS 39 - Financial Instruments Recognition and Measurement. Under IAS 39, the Company must prepare a retrospective and prospective quantitative effectiveness test. This analysis has been prepared by an external consultant and reviewed by Management. Management has determined that hedging relationships qualifying for hedge accounting under Canadian GAAP also qualify under IFRS.

Employee future benefits

In August 2009, Stella-Jones mandated Morneau Sobeco, Human Resource Consultants, to perform an analysis of adopting IAS 19 – Pensions and Other Employee Benefits. Based on the conclusion of their report, the Company has made a decision concerning the various approaches for addressing actuarial gains and losses under IAS 19. The Company has decided to reflect actuarial gains and losses in the statement of other comprehensive income. As a result, a total unamortized actuarial gain related to Stella-Jones' pension plans of $307,000 as of January 1, 2010 will be reflected on the balance sheet upon transition.

Stella-Jones also mandated Towers Watson to perform the same analysis regarding the post-retirement benefits. As a result, there will be two adjustments to the opening balance sheet as of January 1, 2010: an unamortized actuarial loss of $1.1 million and a gain of $549,000 related to the attribution period.

Share-based payments

The Company has a stock option plan, employee share purchase plans and restricted stock units ("RSUs") that will be subject to IFRS 2 – Share-Based Payments. Under this standard, the expense related to these arrangements must be recognized based on a financial model such as Black-Scholes. The stock option plan is currently calculated based on the Black-Scholes model. IFRS also requires the use of the graded vesting method for grants with vesting periods greater than one year. Currently, Stella-Jones accounts for the costs under the straight-line method for Canadian GAAP. As a result of that change of method, there will be an adjustment to the opening balance sheet of $347,000 in retained earnings.

For the employee share purchase plans, there will be no impact upon transition.

Under IFRS, Stella-Jones will have to use a Black-Scholes valuation model to measure the liability related to its RSUs (instead of the intrinsic value under Canadian GAAP). That change of method will have no impact on the opening balance sheet. Afterwards, the liability will be re-measured every quarter.

Borrowing costs

IAS 23 requires the Company to capitalize borrowing costs on certain qualifying assets. Stella-Jones is evaluating the impact focusing on assets that will take more than six months to build. At that time, upon IFRS conversion, the Company is not expecting IAS 23 to have a material impact on its financial statements.

Asset retirement obligations

Under the British Columbia Forest Act and the Alberta Forests Act, the Company is obligated to assume the costs related to reforestation on certain harvest licenses and to incur remediation costs for certain sites.

The Company modified the Asset retirement obligation calculations in 2008 and current disclosure adequately meets IAS 37 – Provisions, Contingent Liabilities and Contingent Assets. There are proposed changes to IAS 37 that may require the Company to perform other assessments.

Business combinations and goodwill

Effective July 1, 2009, IFRS 3 becomes the reference document to guide corporations through business combinations.

Under IFRS 1, the Company has the option to retroactively apply IFRS 3 to all business combinations or may chose to apply the standard prospectively only to those acquisitions that occur after the date of transition. The Company has decided to apply the standard prospectively. In addition, the Company has elected to early adopt a new standard under Canadian GAAP from January 1, 2010 which would align the accounting for business combinations under Canadian GAAP to IFRS.

Impairment

IAS 36 – Impairment of Assets uses a one-step approach for testing and measuring asset impairment. Asset carrying values are being compared to the higher of the value in use and fair value less disposal costs. Value in use is defined as being equal to the present value of future cash flows expected to be derived from the asset. The use of discounted cash flows under IFRS to test and measure asset impairment differs from Canadian GAAP where undiscounted future cash flows are used to compare against the asset's carrying value to determine if impairment exists.

As of December 2009, a goodwill impairment test model has been prepared and no impairment adjustment was required. The IFRS documentation has also been completed.

First time adoption of IFRS

In addition, as a first time adopter of IFRS, the Company is required to apply IFRS 1 "First time adoption of International Financial Reporting Standards". IFRS 1 provides a number of selected optional exemptions that the Company has evaluated. The most significant election is the recognition through opening retained earnings of the cumulative translation adjustments on self-sustaining foreign operations. As of January 1, 2010, the cumulative translation adjustment on self-sustaining foreign operations will be deemed to be nil. The amount of $1.8 million will be reclassed from accumulated other comprehensive income to retained earnings.

Impact on information systems

The Company has assessed the information requirements of IFRS reporting. During the fourth quarter of 2009, the diagnostic analysis regarding current information systems was completed. Changes have been made to ensure that dual reporting of both Canadian GAAP and IFRS was possible in 2010 and new reports have been created to meet IFRS disclosure requirements.

Impact on internal controls over financial reporting and disclosure

The Canadian Securities Administrators' National Instrument 52-109 sets out rules that public companies are required to follow concerning internal controls over financial reporting and disclosure controls and procedures. In compliance with these rules, Management's approach was to identify, review and potentially modify, as considered necessary, certain key controls that may be impacted by changes due to IFRS conversion. Affected key controls were evaluated and have been tested using a risk based approach to ensure they were properly designed and were operating effectively in order to ensure that no material errors would be generated from the changeover to IFRS.

Impact on business activities

The effects of IFRS conversion on the Company's debt covenants are being reviewed. It is not expected that the conversion to IFRS will significantly impact these covenants.

DISCLOSURE CONTROLS

The Company maintains appropriate information systems, procedures and controls to ensure that information used internally and disclosed externally is complete, accurate, reliable and timely. The disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed in its various reports are recorded, processed, summarized and reported accurately.

The President and Chief Executive Officer and the Senior Vice-President and Chief Financial Officer of the Company have evaluated, or caused the evaluation of, under their direct supervision, the effectiveness of the Company's disclosure controls and procedures (as defined in National Instrument 52-109 - Certification of Disclosure in Issuer's Annual and Interim Filings) as at December 31, 2010, and have concluded that such disclosure controls and procedures were designed and operating effectively.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

Management has evaluated the design and effectiveness of its internal controls and procedures over financial reporting (as defined in National Instrument 52-109 - Certification of Disclosure in Issuer's Annual and Interim Filings) for the year ended December 31, 2010. The evaluation was based on the "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). This evaluation was performed by the President and Chief Executive Officer and the Senior Vice-President and Chief Financial Officer of the Company with the assistance of other Company Management and staff to the extent deemed necessary. Based on this evaluation, the President and Chief Executive Officer and the Senior Vice-President and Chief Financial Officer concluded that the internal controls and procedures over financial reporting were appropriately designed and operating effectively.

The Company did not make any material changes to the design of internal controls over financial reporting during the twelve months ended December 31, 2010 that have had a material effect on the Company's internal controls over financial reporting.

In spite of its evaluation, Management does recognize that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance and not absolute assurance of achieving the desired control objectives. In the unforeseen event that lapses occur in disclosures or the execution of internal controls and procedures and/or mistakes happen of a material nature, the Company intends to take the steps necessary to minimize the consequences thereof.

RELATED PARTY TRANSACTIONS

In 2010, the Company paid a total of $300,000 (2009 - $300,000) to its parent company and ultimate shareholders with respect to marketing and technical services fees and incurred interest expense of $32,000 (2009 - $52,000) with respect to loans from the same parties, as detailed in Note 21 to the December 31, 2010 audited consolidated financial statements.

These transactions were with the majority shareholder, Stella Jones International S.A. (marketing services and interest on promissory note) and the ultimate shareholders, Stella S.p.A. and James Jones & Sons Ltd. (technical services and interest on loans). The majority shareholder and ultimate shareholders have extensive international experience in the forest products and wood treating industries and Management considers the amounts paid with respect to the various transactions to be reasonable and competitive.

OUTLOOK

As global economic conditions continue to improve, Management expects demand for the Company's core products to further accelerate in the upcoming year. However, the strong deliveries in the latter part of the fourth quarter are expected to slightly soften first quarter results.

In the railway tie market, increased freight volume on North American railroads should lead to greater investments in the continental rail network, as operators constantly seek optimal line efficiency. Meanwhile, demand is expected to steadily progress in utility poles, as regular maintenance projects provide a stable business flow for distribution poles, while the strength of the transmission pole market is more correlated to the timing of orders, mostly for special projects.

The successful integration of the Tangent operations will continue to be a major performance driver in 2011. This transaction solidified Stella-Jones' position as the second largest North American provider of railway ties and the Company is poised to realize the full potential of its expanded network. Organically, Stella-Jones will strive to capture more of its existing clients' business in the railway tie and utility pole markets across North America, while diligently seeking new market opportunities. The Company will also remain focused on improving operating efficiencies throughout the organization.

The Company will continue to focus on cash generation and to maintain a prudent use of leverage, as a solid balance sheet will favourably position Stella-Jones to continue its acquisition strategy. The Company's long-term strategic vision, focused on continental expansion and consolidation, remains intact. Stella-Jones will continue to seek targets in its core railway tie and utility pole markets that meet its stringent investment requirements, provide synergistic opportunities, and, most of all, add value for shareholders.

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