Stella-Jones Inc.

Consolidated Financial Statements
December 31, 2018 and 2017
(expressed in thousands of Canadian dollars)

December 31, 2018 and 2017

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 International Financial Reporting Standards. Where necessary, Management has made judgments 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 of Directors exercises its responsibilities through the Audit Committee, which is comprised of five 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.

Brian McManus
President and Chief Executive Officer

Éric Vachon, CPA, CA
Senior Vice-President and Chief Financial Officer

Saint-Laurent, Québec
March 14, 2019

Independent auditor's report

To the Shareholders of Stella-Jones Inc.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Stella-Jones Inc. and its subsidiaries (together, the Company) as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS).

What we have audited

The Company's consolidated financial statements comprise:

- the consolidated statements of financial position as at December 31, 2018 and 2017;
- the consolidated statements of changes in shareholders' equity for the years then ended;
- the consolidated statements of income for the years then ended;
- the consolidated statements of comprehensive income for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

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

Independence

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

PricewaterhouseCoopers LLP
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Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis, which we obtained prior to the date of this auditor's report, and the information, other than the consolidated financial statements and our auditor's report thereon, included in the annual report.

Our opinion on the consolidated financial statements does not cover the other information, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them about all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Sonia Boisvert.

PricewaterhouseCoopers LLP[1]

Montréal, Quebec
March 14, 2019

[1] FCPA auditor, FCA, public accountancy permit No. A116853

Stella-Jones Inc.

Consolidated Statements of Financial Position

As at December 31, 2018 and 2017

(expressed in thousands of Canadian dollars)

	Note	2018 $	2017 $
Assets			
Current assets			
Cash		-	6,430
Accounts receivable	5	192,380	163,458
Derivative financial instruments	18	-	473
Inventories	6	838,558	718,462
Income taxes receivable		1,882	1,122
Other current assets		35,567	18,435
		1,068,387	908,380
Non-current assets			
Property, plant and equipment	7	551,785	466,056
Intangible assets	8	131,658	130,349
Goodwill	8	298,270	270,261
Derivative financial instruments	18	7,545	6,173
Other non-current assets		4,559	4,761
		2,062,204	1,785,980
Liabilities and Shareholders' Equity			
Current liabilities			
Accounts payable and accrued liabilities	9	133,259	111,206
Derivative financial instruments	18	4,381	-
Current portion of long-term debt	10	9,714	5,695
Current portion of provisions and other long-term liabilities	11	12,016	12,114
		159,370	129,015
Non-current liabilities			
Long-term debt	10	503,767	449,945
Deferred income taxes	15	92,557	72,408
Provisions and other long-term liabilities	11	13,959	11,392
Employee future benefits	16	7,393	7,675
Derivative financial instruments	18	3,748	-
		780,794	670,435
Shareholders' equity			
Capital stock	13	221,328	220,467
Contributed surplus		348	298
Retained earnings		909,060	809,022
Accumulated other comprehensive income		150,674	85,758
		1,281,410	1,115,545
		2,062,204	1,785,980
Commitments and contingencies	17		
Subsequent events	22		

Approved by the Board of Directors,

Katherine A. Lehman
Director

George J. Bunze, CPA
Director

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

Stella-Jones Inc.
Consolidated Statements of Change in Shareholders' Equity
For the years ended December 31, 2018 and 2017

(expressed in thousands of Canadian dollars)

	Capital stock $	Contributed surplus $	Retained earnings $	Accumulated other comprehensive income: Foreign currency translation adjustment $	Translation of long-term debts designated as net investment hedges $	Unrealized gains on cash flow hedges $	Total $	Total shareholders' equity $
Balance – January 1, 2018	220,467	298	809,022	150,620	(69,421)	4,559	85,758	1,115,545
Comprehensive income (loss)								
Net income for the year	-	-	137,597	-	-	-	-	137,597
Other comprehensive income (loss)	-	-	927	101,529	(37,602)	989	64,916	65,843
Comprehensive income (loss) for the year	-	-	138,524	101,529	(37,602)	989	64,916	203,440
Dividends on common shares	-	-	(33,290)	-	-	-	-	(33,290)
Employee share purchase plans	1,330	-	-	-	-	-	-	1,330
Repurchase of common shares (Note 13)	(469)	-	(5,196)	-	-	-	-	(5,665)
Share-based compensation (Note 13)	-	50	-	-	-	-	-	50
	861	50	(38,486)	-	-	-	-	(37,575)
Balance – December 31, 2018	221,328	348	909,060	252,149	(107,023)	5,548	150,674	1,281,410

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

Stella-Jones Inc.
Consolidated Statements of Change in Shareholders' Equity…continued
For the years ended December 31, 2018 and 2017

(expressed in thousands of Canadian dollars)

	Capital stock $	Contributed surplus $	Retained earnings $	Accumulated other comprehensive income				Total shareholders' equity $
				Foreign currency translation adjustment $	Translation of long-term debts designated as net investment hedges $	Unrealized gains on cash flow hedges $	Total $	
Balance – January 1, 2017	219,119	258	672,620	223,124	(92,532)	3,829	134,421	1,026,418
Comprehensive income (loss)								
Net income for the year	-	-	167,889	-	-	-	-	167,889
Other comprehensive income (loss)	-	-	(983)	(72,504)	23,111	730	(48,663)	(49,646)
Comprehensive income (loss) for the year	-	-	166,906	(72,504)	23,111	730	(48,663)	118,243
Dividends on common shares	-	-	(30,504)	-	-	-	-	(30,504)
Exercise of stock options	146	(47)	-	-	-	-	-	99
Employee share purchase plans	1,202	-	-	-	-	-	-	1,202
Share-based compensation (Note 13)	-	87	-	-	-	-	-	87
	1,348	40	(30,504)	-	-	-	-	(29,116)
Balance – December 31, 2017	220,467	298	809,022	150,620	(69,421)	4,559	85,758	1,115,545

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

Stella-Jones Inc.

Consolidated Statements of Income

For the years ended December 31, 2018 and 2017

(expressed in thousands of Canadian dollars, except earnings per common share)

	Note	2018 $	2017 $
Sales		2,123,893	1,886,142
Expenses			
Cost of sales		1,809,733	1,586,263
Selling and administrative		98,995	93,828
Other losses (gains), net		8,864	(1,337)
	14	1,917,592	1,678,754
Operating income		206,301	207,388
Financial expenses	14	19,102	19,009
Income before income taxes		187,199	188,379
Provision for (recovery of) income taxes			
Current	15	39,018	41,566
Deferred	15	10,584	(21,076)
		49,602	20,490
Net income for the year		137,597	167,889
Basic earnings per common share	13	1.98	2.42
Diluted earnings per common share	13	1.98	2.42

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

Stella-Jones Inc.

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2018 and 2017

(expressed in thousands of Canadian dollars)

	2018 $	2017 $
Net income for the year	137,597	167,889
Other comprehensive income		
Items that may subsequently be reclassified to net income		
Net change in gains (losses) on translation of financial statements of foreign operations	101,529	(81,920)
Income taxes on change in gains (losses) on translation of financial statements of foreign operations	-	9,416
Change in gains (losses) on translation of long-term debts designated as hedges of net investment in foreign operations	(34,332)	29,332
Income taxes on change in gains (losses) on translation of long-term debts designated as hedges of net investment in foreign operations	(3,270)	(6,221)
Change in gains on fair value of derivatives designated as cash flow hedges	1,372	1,026
Income taxes on change in gains on fair value of derivatives designated as cash flow hedges	(383)	(296)
Items that will not subsequently be reclassified to net income		
Remeasurements of post-retirement benefit obligations	1,209	(737)
Income taxes on remeasurements of post-retirement benefit obligations	(282)	(246)
	65,843	(49,646)
Comprehensive income for the year	203,440	118,243

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

Stella-Jones Inc.

Consolidated Statements of Cash Flows

For the years ended December 31, 2018 and 2017

(expressed in thousands of Canadian dollars)

	Note	2018 $	2017 $
Cash flows provided by (used in)			
Operating activities			
Net income for the year		137,597	167,889
Adjustments for			
Depreciation of property, plant and equipment	7	21,086	19,078
Amortization of intangible assets	8	17,016	16,656
Loss on derivative financial instruments		8,601	770
Financial expenses		19,102	19,009
Current income taxes expense	15	39,018	41,566
Deferred income taxes	15	10,584	(21,076)
Restricted stock units expense		7,189	4,549
Other		2,060	(199)
		262,253	248,242
Changes in non-cash working capital components and others			
Accounts receivable		(13,230)	(11,026)
Inventories		(56,716)	100,683
Income taxes receivable		-	(2,746)
Accounts payable and accrued liabilities		13,428	16,694
Asset retirement obligations		(2,304)	(3,369)
Provisions and other long-term liabilities		(1,968)	(1,494)
Other current assets		(15,335)	4,380
		(76,125)	103,122
Interest paid		(18,693)	(15,797)
Income taxes paid		(39,371)	(34,454)
		128,064	301,113
Financing activities			
Increase in deferred financing costs		(255)	(1,132)
Net change in syndicated credit facilities	12	18,742	(391,796)
Increase in long-term debt	12	-	195,870
Repayment of long-term debt	12	(6,705)	(11,507)
Repayment of non-competes payable	12	(1,745)	(2,156)
Dividends on common shares		(33,290)	(30,504)
Repurchase of common shares		(4,038)	-
Proceeds from issuance of common shares		1,330	1,301
		(25,961)	(239,924)
Investing activities			
Increase in other assets		(836)	(710)
Business acquisitions	4	(54,491)	(5,792)
Addition of intangible assets		(4,028)	(2,080)
Purchase of property, plant and equipment		(51,568)	(50,572)
Proceeds on disposal of assets		2,390	676
		(108,533)	(58,478)
Net change in cash and cash equivalents during the year		(6,430)	2,711
Cash and cash equivalents – Beginning of year		6,430	3,719
Cash and cash equivalents – End of year		-	6,430

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

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

1 Description of the business

Stella-Jones Inc. (the "Company") is a leading producer and marketer of pressure treated wood products. The Company supplies North America's railroad operators with railway ties and timbers, and the continent's electrical utilities and telecommunication companies with utility poles. The Company also manufactures and distributes residential lumber and accessories to retailers for outdoor applications, as well as industrial products which include marine and foundation pilings, construction timbers, wood for bridges and coal tar based products. The Company has treating and pole peeling facilities across Canada and the United States and sells its products primarily in these two countries. The Company's headquarters are located at 3100 de la Côte-Vertu Blvd., in Saint-Laurent, Quebec, Canada. The Company is incorporated under the *Canada Business Corporations Act*, and its common shares are listed on the Toronto Stock Exchange ("TSX") under the stock symbol SJ.

2 Significant accounting policies

Basis of presentation

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and Chartered Professional Accountants Canada Handbook Part I – Accounting.

These consolidated financial statements were approved by the Board of Directors on March 14, 2019.

Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention, except for derivative financial instruments and certain long-term liabilities which are measured at fair value. The Company has consistently applied the same accounting policies for all periods presented, except for the newly adopted standards.

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

Principles of consolidation

Subsidiaries

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. The Company owns 100% of the equity interests of its subsidiaries. The significant subsidiaries are as follows:

Subsidiary	Parent	Country of incorporation
Stella-Jones U.S. Holding Corporation ("SJ Holding")	Stella-Jones Inc.	United States
Stella-Jones Corporation	Stella-Jones U.S. Holding Corporation	United States
McFarland Cascade Holdings, Inc. ("McFarland")	Stella-Jones Corporation	United States
Cascade Pole and Lumber Company	McFarland Cascade Holdings, Inc.	United States
McFarland Cascade Pole & Lumber Company	McFarland Cascade Holdings, Inc.	United States
Stella-Jones CDN Finance Inc.	Stella-Jones Inc.	Canada
Stella-Jones U.S. Finance II Corporation	Stella-Jones U.S. Holding Corporation	United States
Stella-Jones U.S. II LLC	Stella-Jones U.S. Holding Corporation	United States
Stella-Jones U.S. Finance III Corporation	Stella-Jones U.S. Holding Corporation	United States
Stella-Jones U.S. III LLC	Stella-Jones U.S. Holding Corporation	United States
Kisatchie Midnight Express, L.L.C	McFarland Cascade Holdings, Inc.	United States
Lufkin Creosoting Co., Inc.	McFarland Cascade Holdings, Inc.	United States

The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are de-consolidated from the date that control ceases.

Business combinations

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Company. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities assumed and the equity interests issued by the group. The consideration transferred also includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date.

The excess of the aggregate of the consideration transferred, the fair value of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the group’s share of the net identifiable assets acquired and liabilities assumed is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the consolidated statement of income. Accounting policies of the subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Company.

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

Foreign currency translation

a) Functional and presentation currency

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Canadian dollars, which is the Company's functional and presentation currency.

b) Foreign currency transactions

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Revenues and expenses denominated in a foreign currency are translated by applying the monthly average exchange rates. Monetary assets and liabilities denominated in foreign currencies are translated at the rate in effect at the statement of financial position date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities not denominated in the functional currency are recognized in the consolidated statement of income within other losses (gains), net, except for qualifying cash flow hedges which are recognized in other comprehensive income and deferred in accumulated other comprehensive income in shareholders' equity.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on translation are recognized in the consolidated statement of income, within other losses (gains), net, except for foreign currency differences arising on the translation of a financial liability designated as a hedge of a net investment, which are recognized in other comprehensive income.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at cost are translated at historical exchange rates.

c) Foreign operations

The financial statements of entities that have a functional currency different from that of the Company are translated using the rate in effect at the statement of financial position date for assets and liabilities, and the monthly average exchange rates during the year for revenues and expenses. Adjustments arising from this translation are recorded in accumulated other comprehensive income in shareholders' equity. Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at the financial position rate.

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

d) Hedges of net investments in foreign operations

Foreign currency differences arising on the translation of financial liabilities designated as a hedge of net investment in foreign operations are recognized in other comprehensive income to the extent that the hedge is effective, and are presented within equity. To the extent that the hedge is ineffective, such differences are recognized in the consolidated statement of income. When the hedged portion of a net investment (the subsidiary) is disposed of, the relevant amount in equity is transferred to the consolidated statement of income as part of the gain or loss on disposal.

Revenue recognition

The Company has adopted IFRS 15 *Revenue from Contracts with Customers* from January 1, 2018 which resulted in changes in accounting policies.

In accordance with the transition provisions in IFRS 15, the Company has adopted the new rules retrospectively.

The Company sells treated and untreated wood products (the “Products”), as well as wood treating services. Revenue from the sale of Products is recognized when the Company satisfies a performance obligation by transferring a promised Product to a customer. Products are considered to be transferred once the customer takes control of them, being either at the Company’s manufacturing site or at the customer’s location. Control of the Products refers to the ability to direct its use and obtain substantially all the remaining benefits from the Product.

The Company offers to treat wood products owned by third parties. Revenue from these treating services is recognized using the point in time criteria since there is a short manufacturing timeframe to treat wood products.

Product sales can be subject to retrospective volume discounts based on aggregate sales over a twelve-month period, per certain contractual conditions. Revenue from these sales is recognized based on the price specified in the contract, net of the estimated volume discounts. Accumulated experience is used to estimate and provide for the discounts, using the expected value method, and revenue is only recognized to the extent that it is highly probable that a significant reversal will not occur. A liability is recognized for expected volume discounts payable to customers in relation to sales transacted to the end of the reporting period.

Product sales may also be subject to retrospective price discounts based on aggregate sales over a twelve-month period, according to certain contractual conditions. Revenue from these sales is recognized based on the expected average sales price over the specified period. Accumulated experience is used to estimate and provide for the price discounts, using the expected value method, and revenue is only recognized to the extent that it is highly probable that specified contractual conditions will be met. The customer is invoiced at the contract price and a liability is recognized to adjust to the average price.

A receivable is recognized when control of the Products is transferred to the customer because it is at this point in time that the consideration becomes unconditional since only the passage of time remains before the payment is due.

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

Cash and cash equivalents

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

Accounts receivable

Accounts receivable are amounts due from customers from the sale of products or services rendered in the ordinary course of business. Accounts receivable are classified as current assets if payment is due within one year or less. Accounts receivable are recognized initially at fair value and subsequently measured at amortized cost, less credit loss provision.

Inventories

Inventories of raw materials are valued at the lower of weighted average cost and net realizable value. Finished goods are valued at the lower of weighted average cost and net realizable value and include the cost of raw materials, direct labour and manufacturing overhead expenses. Net realizable value is the estimated selling price less costs necessary to make the sale.

Property, plant and equipment

Property, plant and equipment are recorded at cost, including borrowing costs incurred during the construction period, less accumulated depreciation and impairment. The Company allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant parts, and depreciates separately each such part. Depreciation is calculated on a straight-line basis using rates based on the estimated useful lives of the assets.

	Useful life
Buildings	7 to 60 years
Production equipment	5 to 60 years
Rolling stock	3 to 20 years
Office equipment	2 to 10 years

The assets' residual values and useful lives are reviewed and adjusted, if appropriate, at the end of each reporting period.

Financial expenses

Borrowing costs are recognized as financial expenses in the consolidated statement of income in the period in which they are incurred. Borrowing costs attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets, until such time as the assets are substantially ready for their intended use.

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

Intangible assets

Intangible assets with finite useful lives are recorded at cost and are amortized over their useful lives. Intangible assets with indefinite useful lives are recorded at cost and are not amortized. The amortization method and estimate of the useful life of an intangible asset are reviewed on an annual basis:

	Method	**Use full life**
Software	Straight-line	10 years
Customer relationships	Straight-line	3 to 12 years
Customer relationships	Declining balance	4% to 20%
Non-compete agreements	Straight-line	3 to 5 years
Creosote registration	-	Indefinite

Standing timber costs are recorded at cost less accumulated amortization and impairment. Amortization 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.

Cutting rights are recorded at cost less accumulated amortization and impairment. Amortization 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 forty-year period and are applied against the historical cost.

The amortization expense is included in cost of sales in the consolidated statements of income.

The creosote registration is subject to an annual impairment test or more frequently if events or changes in circumstances indicate that it might be impaired.

Goodwill

In the context of an acquisition, goodwill represents the excess of the consideration transferred over the fair value of the Company’s share of the net identifiable assets, liabilities and contingent liabilities of the acquiree and the fair value of the non-controlling interest in the acquiree at the date of acquisition. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. For the purpose of impairment testing, goodwill is allocated to cash-generating units (“CGUs”) or groups of CGUs that are expected to benefit from the business combination in which the goodwill arose. The Company defines CGUs as either plants specialized in the treatment of utility poles and residential lumber or plants specialized in the treatment of railway ties.

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

Impairment

Impairments are recorded when the recoverable amounts of assets are less than their carrying amounts. The recoverable amount is the higher of an asset's fair value less cost of disposal and its value in use. Impairment losses are evaluated for potential reversals when events or changes in circumstances warrant such consideration, except goodwill.

Non-financial assets

The carrying values of non-financial assets with finite lives, such as property, plant and equipment and intangible assets with finite useful lives, are assessed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Long-lived assets that are not amortized are subject to an annual impairment test. The recoverable amount is the higher of an asset's fair value less costs of disposal and its value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGUs). Non-financial assets other than goodwill that have suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

Leases

The Company leases certain property, plant and equipment.

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases, net of any incentives received from the lessor, are charged to the consolidated statement of income on a straight-line basis over the term of the lease.

Leases of property, plant and equipment where the Company assumes substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Each finance lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in long-term debt. The interest element of the finance cost is charged to the consolidated statement of income over the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

The depreciable amount of a leased asset is allocated to each accounting period during the period of expected use on a systematic basis consistent with the depreciation policy the Company adopts for depreciable assets that are owned. If there is reasonable certainty that the Company will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset; otherwise, the asset is depreciated over the shorter of the lease term and its useful life.

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

Provisions

Provisions for site remediation and other provisions are recognized when the Company has a legal or constructive obligation as a result of past events, when it is probable that an outflow of resources will be required to settle the obligation and when a reliable estimate can be made of the amount of the obligation. If some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement is recorded in the consolidated statement of financial position as a separate asset, but only if it is virtually certain that reimbursement will be received.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as a financial expense.

The Company considers the current portion of the provision to be an obligation whose settlement is expected to occur within the next twelve months.

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 the accretion expense on existing obligations, in other losses (gains), net in the consolidated statement of income.

At each reporting date, the liability is remeasured for changes in discount rates and in the estimate of the amount, timing and cost of the work to be carried out.

Income taxes

The income tax expense or credit for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Company operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

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

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognized if they arise from the initial recognition of goodwill. Deferred income tax is also not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred tax assets are recognized only if it is probable that future taxable amounts will be available to utilize those temporary differences and losses.

Employee future benefits

Other post-retirement benefit programs

The Company provides other post-retirement healthcare benefits to certain retirees. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age and the completion of a minimum service period. The expected costs of these benefits are attributed from the date when service by the employee first leads to benefits under the plan, until the date when further service by the employee will lead to no material amount of further benefits. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to other comprehensive income in the period in which they arise.

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 unit credit method and Management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and discount rates on obligations. Past service costs from plan amendments are recognized in net income when incurred.

Remeasurements consisting of actuarial gains and losses, the actual return on plan assets (excluding the net interest component) and any change in the asset ceiling are recognized in other comprehensive income. The amounts recognized in other comprehensive income are recognized immediately in retained earnings without recycling to the consolidated statements of income in subsequent periods.

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

Share-based compensation and other share-based payments

The Company operates a number of equity-settled and cash-settled share-based compensation plans under which it receives services from employees as consideration for equity instruments of the Company or cash payments.

Equity-settled plan

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 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. For grants of share-based awards with graded vesting, each tranche is considered a separate grant with a different vesting date and fair value. Any consideration paid on the exercise of stock options is credited to capital stock together with any related share-based compensation expense included in contributed surplus.

Cash-settled plan

The Company has restricted stock units (“RSUs”) and measures the liability incurred and the compensation expenses at fair value by applying the Black-Scholes valuation model. The compensation expenses are recognized in the consolidated statements of income over the vesting periods. Until the liability is settled, the fair value of that liability is remeasured at each reporting date, with changes in fair value recognized in the consolidated statements of income.

Financial instruments

IFRS 9, *Financial Instruments* replaces the provisions of IAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting.

The adoption of IFRS 9 from January 1, 2018 resulted in changes in accounting policies applied retrospectively.

The Company recognizes a financial asset or a financial liability in its statement of financial position when it becomes party to the contractual provisions of the instrument. At initial recognition, the Company measures a financial asset or a financial liability at its fair value plus or minus, in the case of a financial asset or a financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or the financial liability.

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

Financial assets

The Company will classify financial assets as subsequently measured at amortized cost, fair value through other comprehensive income or fair value through profit or loss, based on its business model for managing the financial asset and the financial asset's contractual cash flow characteristics. The three categories are defined as follows:

a) Amortized cost—a financial asset is measured at amortized cost if both of the following conditions are met:

- the asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

b) Fair value through other comprehensive income—financial assets are classified and measured at fair value through other comprehensive income if they are held in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets.

c) Fair value through profit or loss—any financial assets that are not held in one of the two business models mentioned in a) and b) are measured at fair value through profit or loss.

When, and only when, the Company changes its business model for managing financial assets it must reclassify all affected financial assets.

The Company's financial assets are comprised of cash, cash equivalents, accounts receivable and derivative financial instruments. Cash, cash equivalents and accounts receivable are measured at amortized cost. Derivative financial instruments that are not designated as hedging instruments are measured at fair value through profit or loss. Derivative financial instruments that are designated as hedging instruments are measured at fair value through other comprehensive income.

Financial liabilities

The Company's liabilities include accounts payable and accrued liabilities, bank indebtedness, long-term debt and derivative financial instruments. Accounts payable and accrued liabilities, bank indebtedness and long-term debt are measured at amortized cost. Derivative financial instruments that are not designated as hedging instruments are measured at fair value through profit or loss. Derivative financial instruments that are designated as hedging instruments are measured at fair value through other comprehensive income. After initial recognition, an entity cannot reclassify any financial liability.

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

Impairment

The Company assesses, on a forward-looking basis, the expected credit losses associated with its investment in debt securities carried at amortized cost and fair value through other comprehensive income. The impairment methodology applied depends on whether there has been a significant increase in credit risk. For trade receivables, the Company applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

Hedging transactions

As part of its hedging strategy, the Company considers derivative financial instruments such as foreign exchange forward contracts to limit its exposure under contracted cash inflows of sales denominated in U.S. dollars from its Canadian-based operations. The Company also considers interest rate swap agreements in order to reduce the impact of fluctuating interest rates on its short-term and long-term debt. These derivative financial instruments are treated as cash flow hedges for accounting purposes and are fair-valued through other comprehensive income.

The effective portion of changes in the fair value of derivative instruments that are designated and qualify as cash flow hedges is recognized in the cash flow hedge reserve within equity. The gain or loss relating to the ineffective portion is recognized immediately in profit or loss, within other income (expenses).

When forward contracts are used to hedge forecast transactions, the Company generally designates only the change in fair value of the forward contract related to the spot component as the hedging instrument. Gains or losses relating to the effective portion of the change in the spot component of the forward contracts are recognized in the cash flow hedge reserve within equity. The change in the forward element of the contract that relates to the hedged item is recognized within other comprehensive income in the costs of hedging reserve within equity. In some cases, the Company may designate the full change in fair value of the forward contract (including forward points) as the hedging instrument. In such cases, the gains or losses relating to the effective portion of the change in fair value of the entire forward contract are recognized in the cash flow hedge reserve within equity. Amounts accumulated in equity are reclassified in the periods when the hedged item affects profit or loss.

When a hedging instrument expires, or is sold or terminated, or when a hedge no longer meets the criteria for hedge accounting, any cumulative deferred gain or loss and deferred costs of hedging in equity at that time remains in equity until the forecast transaction occurs. When the forecast transaction is no longer expected to occur, the cumulative gain or loss and deferred costs of hedging that were reported in equity are immediately reclassified to profit or loss.

Earnings per share

Basic earnings per share is calculated by dividing the net income for the period attributable to equity owners of the Company by the weighted average number of common shares outstanding during the year.

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

Diluted earnings per share is calculated using the treasury stock method. Under this 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 period.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the senior management team, which makes strategic and operational decisions.

Change in accounting policies

The Company has adopted the following new standards, along with any consequential amendments, effective January 1, 2018. These changes were made in accordance with the applicable transitional provisions.

IFRS 15 – Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15, *Revenue from Contracts with Customers*, to specify how and when to recognize revenue as well as requiring the provision of more informative and relevant disclosures. IFRS 15 supersedes IAS 18, *Revenue*, IAS 11, *Construction Contracts*, and other revenue related interpretations. Note 2 provides a summary of the new revenue recognition accounting policy that was implemented retrospectively on January 1, 2018. The adoption of this new standard had no significant impact on the Company's consolidated financial statements.

IFRS 9 – Financial Instruments

The final version of IFRS 9, *Financial instruments,* was issued by the IASB in July 2014 and replaces IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 introduces a model for classification and measurement, a single, forward-looking expected loss impairment model and a substantially reformed approach to hedge accounting. The new single, principle-based approach for determining the classification of financial assets is driven by cash flow characteristics and the business model in which an asset is held. The new model also results in a single impairment model being applied to all financial instruments, which will require more timely recognition of expected credit losses. It also includes changes in respect of an entity's own credit risk in measuring liabilities elected to be measured at fair value, so that gains caused by the deterioration of an entity's own credit risk on such liabilities are no longer recognized in profit or loss. Note 2 provides a summary of the new financial instruments accounting policy that was implemented retrospectively on January 1, 2018. The adoption of this new standard had no significant impact on the Company's consolidated financial statements.

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

Impact of accounting pronouncements not yet implemented

IFRS 16 – Leases

In January 2016, the IASB released IFRS 16, *Leases*, to set out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a lease agreement. The standard supersedes IAS 17, *Leases*, and the related interpretations on leases: IFRIC 4, *Determining whether an arrangement contains a lease*, SIC 15, *Operating Leases – Incentives* and SIC 27, *Evaluating the substance of transactions in the legal form of a lease*. The standard is effective for annual periods beginning on or after January 1, 2019.

Under the new standard, the Company will recognize, in the statement of financial position, assets (right to use the leased assets) totalling approximately $119,000, equivalent to the discounted cash flows of the future minimum payments, and corresponding financial liabilities. The assets will be depreciated over the duration of the lease agreements, which has a weighted average of 78 months. The liabilities will be depleted upon contractual payment to the lessors and a corresponding financing expense will be recorded to the consolidated statement of income. The Company is currently assessing the impact of the new standard on its net income.

The Company will adopt IFRS 16 for its fiscal year beginning January 1, 2019 retrospectively without restatement of comparative amounts and will use the exemptions for short-term leases and leases for which the underlying asset is of low value.

IFRIC 23 – Uncertainty over Income Tax Treatments

In June 2017, the IASB issued IFRIC 23, *Uncertainty over Income Tax Treatments*. This interpretation specifies that if an entity concludes it is probable that the taxation authority will accept an uncertain tax treatment, it shall determine the tax result consistently with the tax treatment used or planned to be used in its income tax filing. If it is not probable, the entity shall reflect the effect of uncertainty for each uncertain tax treatment by using either of the following methods, depending on which one the entity expects to better predict the resolution of the uncertainty:

- most likely amount: single most likely amount in a range of possible outcomes;
- expected value: sum of the probability-weighted amounts in a range of possible outcomes.

An entity shall apply IFRIC 23 for annual reporting periods beginning on or after January 1, 2019, with earlier application permitted. The Company will not early adopt IFRIC 23 and does not expect a significant impact.

IFRS 3 – Business Combinations

In October 2018, the IASB issued amendments to the definition of a business in IFRS 3, *Business Combinations*. The objective of the amendments is to assist entities in determining whether a transaction should be accounted for as a business combination or as an asset. The amendments apply prospectively to acquisitions that occur in annual periods beginning on or after January 1, 2020, with earlier application permitted.

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

3 Critical accounting estimates and judgments

The preparation of financial statements in conformity with IFRS 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 revenue and expenses during the reporting period. Significant items subject to estimates and assumptions include the estimated useful life of assets, impairment of goodwill, determination of the fair value of the assets acquired and liabilities assumed in the context of an acquisition and impairment of long-lived assets. Management also makes estimates and assumptions in the context of business combination mainly with sale forecast, margin forecast, income tax rate and discount rate. 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 the consolidated statement of income in the period in which they become known.

4 Business acquisitions

a) On April 9, 2018, the Company completed the acquisition of substantially all of the operating assets employed in the business of Wood Preservers Incorporated ("WP"), located at its wood treating facility in Warsaw, Virginia. WP manufactures, sells and distributes marine and foundation pilings and treated wood utility poles.

   Total cash outlay associated with the acquisition was approximately $27,506 (US$21,609), excluding acquisition costs of approximately $423 recognized in the consolidated statement of income under selling and administrative expenses. The Company financed the acquisition through its existing syndicated credit facilities. The consideration transferred is also comprised of an unsecured promissory note bearing no interest and payable annually on the anniversary of the transaction in six instalments of US$500. This unsecured promissory note was recorded at a fair value of $3,339 (US$2,623), using an effective interest rate of 4.17%.

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

The following table is a final summary of the assets acquired, the liabilities assumed and the consideration transferred at fair value as at the acquisition date. No significant adjustments were made to the preliminary fair value determination. The original transaction was made in U.S. dollars and converted into Canadian dollars as at the acquisition date.

	$
Assets acquired	
Accounts receivable	3,923
Inventories	8,485
Property, plant and equipment	18,212
Customer relationships	242
Goodwill	1,061
	31,923
Liabilities assumed	
Deferred income tax liabilities	424
Total net assets acquired and liabilities assumed	31,499
Consideration transferred	
Cash	27,506
Consideration payable	654
Unsecured promissory note	3,339
Consideration transferred	31,499

The Company's valuation of intangible assets has identified customer relationships which are amortized at a declining rate of 4.00%. Significant assumptions used in the determination of intangible assets, as defined by Management, include year-over-year sales growth, discount rate and operating income before depreciation and amortization margin. Goodwill is amortized and is deductible for U.S. tax purposes, and represents the future economic value associated with the enhanced procurement network, acquired workforce and synergies with the Company's operations. Goodwill is allocated to a CGU defined as plants specialized in the treatment of utility poles and residential lumber.

In the period from April 9, 2018 to December 31, 2018, sales and net income for the Warsaw plant amounted to $28,760 and $1,859, respectively. Pro forma information for the twelve-month period ended December 31, 2018, had the WP acquisition occurred as of January 1, 2018, cannot be estimated as Management does not have all the required discrete financial information for the first three months of the year.

b) On February 9, 2018, the Company completed the acquisition of substantially all of the operating assets employed in the business of Prairie Forest Products ("PFP"), a division of Prendiville Industries Ltd., located at its wood treating facility in Neepawa, Manitoba, as well as at its peeling facility in Birch River, Manitoba. PFP manufactures treated wood utility poles as well as treated residential lumber.

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

Total cash outlay associated with the acquisition was approximately $26,985 excluding acquisition costs of approximately $425 of which $159 and $266 were recognized respectively in the 2017 and 2018 consolidated statements of income under selling and administrative expenses. The Company financed the acquisition through its existing syndicated credit facilities.

The following table is a final summary of the assets acquired, the liabilities assumed and the consideration transferred at fair value as at the acquisition date. No significant adjustments were made to the preliminary fair value determination.

Assets acquired	**$**
Inventories	10,536
Property, plant and equipment	7,763
Customer relationships	5,880
Goodwill	3,995
Deferred income tax assets	229
	28,403
Liabilities assumed	
Site remediation provision	1,418
Total net assets acquired and liabilities assumed	26,985
Consideration transferred	
Cash	26,985
Consideration transferred	26,985

The Company's valuation of intangible assets has identified customer relationships which are amortized at a declining rate of 10.00%. Significant assumptions used in the determination of intangible assets, as defined by Management, include year-over-year sales growth, discount rate and operating income before depreciation and amortization margin. Goodwill is amortized and is deductible for Canadian tax purposes, and represents the future economic value associated with the enhanced procurement network, acquired workforce and synergies with the Company's operations. Goodwill is allocated to a CGU defined as plants specialized in the treatment of utility poles and residential lumber.

In the period from February 9, 2018 to December 31, 2018, sales and net income for the Neepawa plant amounted to $31,657 and $890, respectively. Pro forma information for the twelve-month period ended December 31, 2018, had the PFP acquisition occurred as of January 1, 2018, cannot be estimated as Management does not have all the required discrete financial information for the first month of the year.

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

5 Accounts receivable

	Note	2018 $	2017 $
Trade receivables		184,376	159,964
Less: Credit loss provision		(2,209)	(991)
Trade receivables – net		182,167	158,973
Amounts receivable from related parties	20	454	-
Other receivables		9,759	4,485
		192,380	163,458

The aging of gross trade receivables at each reporting date was as follows:

	2018 $	2017 $
Current	113,783	98,355
Past due 1-30 days	51,214	43,416
Past due 31-60 days	11,251	9,230
Past due more than 60 days	8,128	8,963
	184,376	159,964

6 Inventories

	2018 $	2017 $
Raw materials	516,742	423,312
Finished goods	321,816	295,150
	838,558	718,462

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

7 Property, plant and equipment

	Land $	Buildings $	Production equipment $	Rolling stock $	Others $	Total $
As at January 1, 2017						
Cost	45,981	113,768	356,892	29,815	12,584	559,040
Accumulated depreciation	-	(16,542)	(64,602)	(12,901)	(6,404)	(100,449)
Net book amount	45,981	97,226	292,290	16,914	6,180	458,591
Year ended December 31, 2017						
Opening net book amount	45,981	97,226	292,290	16,914	6,180	458,591
Business acquisitions	204	941	3,353	301	9	4,808
Additions	4,384	4,250	35,337	1,130	2,663	47,764
Disposals	(143)	(235)	(998)	(629)	(4)	(2,009)
Depreciation	-	(3,066)	(10,231)	(4,276)	(1,505)	(19,078)
Exchange differences	(1,974)	(5,516)	(15,343)	(884)	(303)	(24,020)
Closing net book amount	48,452	93,600	304,408	12,556	7,040	466,056
As at December 31, 2017						
Cost	48,452	112,272	376,203	27,944	14,762	579,633
Accumulated depreciation	-	(18,672)	(71,795)	(15,388)	(7,722)	(113,577)
Net book amount	48,452	93,600	304,408	12,556	7,040	466,056
Year ended December 31, 2018						
Opening net book amount	48,452	93,600	304,408	12,556	7,040	466,056
Business acquisitions	1,121	7,823	12,797	4,117	117	25,975
Additions	1,630	3,165	43,919	669	1,031	50,414
Disposals	(1,622)	-	(478)	(853)	(3)	(2,956)
Depreciation	-	(3,406)	(12,260)	(4,272)	(1,148)	(21,086)
Exchange differences	2,618	7,416	21,386	1,189	773	33,382
Closing net book amount	52,199	108,598	369,772	13,406	7,810	551,785
As at December 31, 2018						
Cost	52,199	131,933	457,904	32,998	16,959	691,993
Accumulated depreciation	-	(23,335)	(88,132)	(19,592)	(9,149)	(140,208)
Net book amount	52,199	108,598	369,772	13,406	7,810	551,785

8 Intangible assets and goodwill

The intangible assets include customer relationships, non-compete agreements, cutting rights, standing timber, a favourable land lease agreement, software and a creosote registration.

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.

The acquisition cost of the non-compete agreements was established based on the discounted value of future payments using a discount rate of 2.95%.

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

Impairment tests for goodwill

Goodwill is allocated for impairment testing purposes to CGUs which reflect how it is monitored for internal management purposes.

The recoverable amount of a CGU is determined based on fair value less cost to dispose ("FVLCTD") calculations. FVLCTD calculations use cash flow projections based on financial budgets covering a five-year period that are based on the latest budgets for revenue and cost as approved by senior management. Cash flow projections beyond five years are based on Management's forecasts and assume a growth rate not exceeding gross domestic product for the respective countries. Post-tax cash flow projections are discounted using a real post-tax discount rate of 8.00%. One percent real growth rates are assumed in perpetuity for most of the businesses given the commodity nature of the majority of the products (i.e. volume growth is assumed to be offset by real price declines). The assumptions used in calculating FVLCTD have considered the current economic environment.

The carrying value of goodwill is allocated to the following CGUs:

CGUs	2018 $	2017 $
Plants specialized in the treatment of utility poles and residential lumber	144,546	128,898
Plants specialized in the treatment of railway ties	153,724	141,363
	298,270	270,261

Impairment tests for intangible assets with indefinite useful life

The only intangible asset with indefinite useful life is the creosote registration. This registration provides the Company with the right to produce and import creosote out of its Memphis, Tennessee facility. The Company's approach to creosote supply is to produce a portion of its requirements and to buy the remainder on the open market. As a result, the creosote registration procures the advantage of being able to produce, which is less expensive than buying on the market. Moreover, when procuring creosote on the market, the import feature of the registration enables the Company to negotiate better pricing.

The recoverable amount of the creosote registration is determined based on value-in-use calculations. Value-in-use calculations use cash flow projections based on financial budgets covering a five-year period that are based on the latest forecasts for cost savings as approved by senior management. Cash flow projections beyond five years are based on internal management forecasts and assume a growth rate not exceeding domestic product for the respective countries. Pre-tax cash flow projections are discounted using a real pre-tax discount rate of 10.10%. One percent real growth rates are assumed in perpetuity for most of the business given the commodity nature of the majority of the products (i.e. volume growth is assumed to be offset by real price declines).

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

The net book amount of these intangible assets and goodwill was as follows:

	Intangible assets							
	Cutting rights $	Customer relationships $	Non-compete agreements $	Software $	Others $	Creosote registration $	Total $	Goodwill $
As at January 1, 2017								
Cost	6,821	157,626	17,413	7,140	7,903	41,933	238,836	287,367
Accumulated amortization	(1,455)	(66,208)	(10,764)	(2,081)	(5,955)	-	(86,463)	-
Net book amount	5,366	91,418	6,649	5,059	1,948	41,933	152,373	287,367
Year ended December 31, 2017								
Opening net book balance	5,366	91,418	6,649	5,059	1,948	41,933	152,373	287,367
Business acquisitions	-	-	-	-	-	-	-	844
Additions	-	-	-	1,603	477	-	2,080	-
Amortization	(176)	(13,445)	(1,839)	(677)	(519)	-	(16,656)	-
Exchange differences	-	(4,255)	(368)	-	(70)	(2,755)	(7,448)	(17,950)
Closing net book amount	5,190	73,718	4,442	5,985	1,836	39,178	130,349	270,261
As at December 31, 2017								
Cost	6,821	148,740	16,270	8,743	8,310	39,178	228,062	270,261
Accumulated amortization	(1,631)	(75,022)	(11,828)	(2,758)	(6,474)	-	(97,713)	-
Net book amount	5,190	73,718	4,442	5,985	1,836	39,178	130,349	270,261
Year ended December 31, 2018								
Opening net book balance	5,190	73,718	4,442	5,985	1,836	39,178	130,349	270,261
Business acquisitions	-	6,122	-	-	-	-	6,122	5,599
Additions	-	-	-	869	3,159	-	4,028	-
Amortization	(256)	(12,193)	(1,612)	(831)	(2,124)	-	(17,016)	-
Exchange differences	-	4,363	298	-	88	3,426	8,175	22,410
Closing net book amount	4,934	72,010	3,128	6,023	2,959	42,604	131,658	298,270
As at December 31, 2018								
Cost	6,821	165,931	17,692	9,612	11,557	42,604	254,217	298,270
Accumulated amortization	(1,887)	(93,921)	(14,564)	(3,589)	(8,598)	-	(122,559)	-
Net book amount	4,934	72,010	3,128	6,023	2,959	42,604	131,658	298,270

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

9 Accounts payable and accrued liabilities

	Note	2018	2017
		$	$
Trade payables		53,021	41,373
Amounts due to related parties	20	54	380
Accrued expenses		60,815	51,761
Other payables		19,369	17,692
		133,259	111,206

10 Long-term debt

	Note	2018	2017
		$	$
Syndicated credit facilities	10(a)	273,055	232,083
Unsecured senior notes	10(b)	204,630	188,176
Unsecured promissory notes	10(c)	17,930	15,944
Secured promissory note	10(d)	7,321	7,422
Unsecured promissory note	10(e)	3,936	7,000
Unsecured promissory note	10(f)	3,596	-
Secured promissory note	10(g)	1,540	2,278
Unsecured promissory note	10(h)	1,506	2,008
Unsecured promissory note	10(i)	572	844
Unsecured promissory note	10(j)	-	586
		514,086	456,341
Deferred financing costs		(605)	(701)
		513,481	455,640
Less: Current portion of long-term debt		9,810	5,791
Less: Current portion of deferred financing costs		(96)	(96)
Total current portion of long-term debt		9,714	5,695
		503,767	449,945

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

a) The Company's syndicated credit facilities consist of (i) an unsecured revolving facility in the amount of US$325,000 made available to the Company and SJ Holding (the "Borrowers"), a wholly-owned subsidiary of the Company until February 27, 2023 and (ii) an unsecured term facility in the amount of US$100,000 made available to the Company until February 26, 2019. The syndicated credit facilities are made available to the Borrowers by a syndicate of lenders under a fifth amended and restated credit agreement (the "Credit Agreement") dated as of February 26, 2016, as amended on May 18, 2016 and March 15, 2018. As at December 31, 2018 the syndicated credit facilities provided financing up to US$425,000 of which US$213,729 was available. Additionally, the Credit Agreement makes available an accordion option whereas upon request, the Company could increase the revolving facility by US$350,000.

Borrowings under the syndicated credit facilities may be obtained in the form of Canadian prime rate loans, bankers' acceptances ("BAs"), U.S. base rate loans, LIBOR loans in U.S. dollars and letters of credit. The interest rate margin with respect to Canadian prime rate loans and U.S. base rate loans will range from 0.00% to 1.25% based on the Credit Agreement's pricing grid. The interest rate margin with respect to BAs, LIBOR loans and fees for letters of credit will range from 1.00% to 2.25% based on the Credit Agreement's pricing grid.

The Company enters into interest rate swap agreements in order to reduce the impact of fluctuating interest rates on its debt. Details of the outstanding interest rate swap agreements as at December 31, 2018 are provided in Note 18, Financial instruments.

As at December 31, 2018, borrowings by Canadian entities denominated in U.S. dollars represented $170,525 (US$125,000) and the total amount was designated as a hedge of net investment in foreign operations.

The Company has demand loan agreements, with two banks participating in the syndicated credit facilities, providing financing up to US$50,000 under terms and conditions similar to those under the Credit Agreement. This indebtedness, if required by the Company, will be presented under short term liabilities as the banks have the option to request reimbursement of their loans at any time. As at December 31, 2018 no amounts were drawn under the demand loan facilities.

In order to maintain the syndicated credit facilities and the demand loans in place, the Company needs to comply with affirmative covenants, negative covenants, reporting requirements and financial ratios consisting of a net funded debt to EBITDA ratio of no more than 3.50:1 and an interest coverage ratio equal to or greater than 3.00:1. As at December 31, 2018, the Company was in full compliance with these covenants, requirements and ratios. Additionally, the Credit Agreement prohibits the Company from paying dividends aggregating in any one year in excess of 50.00% of the Company's consolidated net income for the preceding year if the net funded debt to EBITDA ratio is greater than 3.25:1. In the case where the net funded debt to EBITDA ratio is equal or lower than 3.25:1, there are no restrictions to the payment of dividends, so long as the Company is otherwise in compliance with the terms of the Credit Agreement.

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

b) On January 17, 2017, the Company concluded a US$150,000 private placement with certain U.S. investors. Pursuant to the private placement, the Company entered into a note purchase agreement providing for the issuance by Stella-Jones Inc. of senior notes - series A in the aggregate amount of US$75,000 bearing interest at 3.54% payable in a single instalment at maturity on January 17, 2024 and senior notes – series B in the aggregate amount of US$75,000 bearing interest at 3.81%, payable in a single instalment at maturity on January 17, 2027. Such notes are unsecured and proceeds were used to reimburse a portion of the revolving credit facility. The notes were designated as hedges of net investment in foreign operations.

In order to maintain the senior notes in place, the Company needs to comply with affirmative covenants, negative covenants, reporting requirements and financial ratios comprised of the net funded debt to EBITDA ratio of not more than 3.50:1, the interest coverage ratio equal to or greater than 2.50:1 and a priority debt to equity ratio not more than 15.00%. As at December 31, 2018, the Company was in full compliance with these covenants, requirements and ratios.

c) Pursuant to two business acquisitions dated June 3, 2016, the Company issued two unsecured promissory notes totalling $18,256 (US$14,104) bearing interest at 1.41%. The notes are payable in three instalments, including interest, totalling US$3,000 in June 2019 and 2020 and US$9,000 in June 2021. The notes were initially recorded at a fair value totalling $15,676 (US$12,112) using an effective interest rate of 5.00%. The difference between the face value and the fair value of the notes is being accreted on an effective yield basis over its term.

d) As part of a business acquisition dated June 3, 2016, the Company assumed a promissory note bearing interest at 5.76%, secured by the land of the Pineville facility and having a balance of US$5,685. The note is payable in quarterly instalments, including interest, of US$163, up to July 2028. The note was initially recorded at a fair value of $8,775 (US$6,780) using an effective interest rate of 4.00%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

e) Pursuant to a business acquisition dated May 22, 2014, the Company issued an unsecured promissory note of $15,466 (US$14,169) bearing interest at 1.93%. The note is payable in five equal annual instalments, including interest, of US$3,000, up to May 2019. The note was initially recorded at a fair value of $13,426 (US$12,301) using an effective interest rate of 7.00%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

f) As part of WP acquisition completed on April 9, 2018, the Company recorded an unsecured promissory note of $3,596 (US$3,000) bearing no interest. The unsecured promissory note is payable annually on the anniversary of the transaction in six instalments of US$500, until April 2024 and was recorded at a fair value of $3,339 (US$2,623) using an effective interest rate of 4.17%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

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

g) Pursuant to a business acquisition completed on October 1, 2015, the Company recorded a secured promissory note of $5,800 bearing no interest. The secured promissory note is payable in five annual instalments of $2,900 in October 2016, $500 in October 2017 and $800 in October 2018, 2019 and 2020, respectively. The secured promissory note was initially recorded at a fair value of $5,430 using an interest rate of 2.91%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

The secured promissory note is guaranteed by irrevocable letters of credit in the same amount and with the same maturity date as the future payments.

h) Pursuant to a business acquisition dated September 1, 2015, the Company issued an unsecured promissory note of $3,993 (US$3,000) bearing no interest. The note is payable in five equal annual instalments of US$600, up to September 2020. The note was initially recorded at a fair value of $3,275 (US$2,460) using an effective interest rate of 7.00%. The difference between the face value and the fair value of the note is being accreted on an effective yield basis over its term.

i) As part of the WPI acquisition completed on December 19, 2017, the Company recorded an unsecured promissory note of $900 bearing no interest. The unsecured promissory note is payable in quarterly installments of $75 in March, June, September and December of each year, up to December 2020. The unsecured promissory note was initially recorded at a fair value of $844 using an effective interest rate of 3.29%. 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 a business acquisition completed on December 4, 2015, the Company issued an unsecured promissory note of $1,939 (US$1,451) bearing interest at 1.68%. The note was payable in three equal annual instalments, including interest, of US$500, up to December 2018. The note was initially recorded at a fair value of $1,754 (US$1,312) using an effective interest rate of 7.00%. The difference between the face value and the fair value of the note was being accreted on an effective yield basis over its term. This debt was reimbursed in 2018 in accordance with the agreement.

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

	Principal
	$
2019	10,433
2020	7,002
2021	13,355
2022	1,298
2023	274,390
Thereafter	208,975
	515,453
Fair value adjustment	(1,367)
	514,086

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

l) The aggregate fair value of the Company's long-term debt was estimated at $501,950 as at December 31, 2018 (2017 – $453,478) based on discounted future cash flows, using interest rates available to the Company for issues with similar terms and average maturities.

11 Provisions and other long-term liabilities

	Provisions			Other long-term liabilities			
	Site remediation $	Others $	Total $	RSUs $	Non-competes payable $	Total $	Grand total $
Balance as at January 1, 2017	16,487	3,664	20,151	2,956	7,963	10,919	31,070
Additions	911	1,786	2,697	727	-	727	3,424
Business acquisitions	58	-	58	-	-	-	58
Provision reversal	(2,331)	(106)	(2,437)	-	-	-	(2,437)
Payments	(2,183)	(1,504)	(3,687)	(1,435)	(2,156)	(3,591)	(7,278)
Interest accretion	-	-	-	-	155	155	155
Exchange differences	(898)	(134)	(1,032)	-	(454)	(454)	(1,486)
Balance as at December 31, 2017	12,044	3,706	15,750	2,248	5,508	7,756	23,506
Additions	1,519	506	2,025	5,597	-	5,597	7,622
Business acquisitions	1,418	-	1,418	-	-	-	1,418
Provision reversal	(830)	(523)	(1,353)	-	-	-	(1,353)
Payments	(2,867)	(537)	(3,404)	(1,539)	(1,745)	(3,284)	(6,688)
Interest accretion	-	-	-	-	124	124	124
Exchange differences	812	142	954	-	392	392	1,346
Balance as at December 31, 2018	12,096	3,294	15,390	6,306	4,279	10,585	25,975

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

Analysis of provisions and other long-term liabilities:

	2018 $	2017 $
Current		
Provisions	9,294	9,141
Other long-term liabilities	2,722	2,973
Total current	12,016	12,114
Non-current		
Provisions	6,095	6,609
Other long-term liabilities	7,864	4,783
Total non-current	13,959	11,392
	25,975	23,506

Provisions

Site remediation

Site remediation obligations represent discounted cash flow estimates relating to future environmental remediation costs of current and former treating sites for a period ranging from one to fifteen years. These discounted cash flows have been estimated using pre-tax rates between 3.24% and 3.45% that reflect current market assessment of the time value of money and the risk specific to the obligation.

As of December 31, 2018, a total site remediation provision of $12,096 (2017 - $12,044) was recorded to support the ongoing compliance efforts.

Other long-term liabilities

Restricted stock units

The Company has a long-term incentive plan, for certain executives and key employees, under which grants of RSUs are permitted upon the Company attaining a minimum 12.50% return on capital employed. When this condition is met, the number of RSUs granted is based on a percentage of the individual's salary, divided by the average trading price of the Company's common shares on the TSX for the five days immediately preceding the grant date.

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

The RSUs are full-value phantom shares payable in cash on the third anniversary of their date of grant, provided the individual is still employed by the Company. The amount to be paid is determined by multiplying the number of RSUs by the six-month average trading price of the Company's common shares on the TSX immediately preceding the anniversary.

The RSUs granted on March 16, 2015 reached their third year anniversary on March 16, 2018 and were fully paid.

On March 21, 2016 and March 19, 2018, the Company granted a total of 47,667 RSUs to certain executives and key employees as part of the long-term incentive plan. No RSUs were granted in 2017.

On March 13, 2018, the Remuneration Committee and Board of Directors departed from the RSU award calculation and granted a special long-term incentive to senior management totalling 200,000 RSUs. Subsequently, on May 7, 2018, a special long-term incentive award of 7,632 RSUs was given to a newly added member of the senior management team.

On May 2, 2018, as an incentive to continue on as President and Chief Executive Officer ("President and CEO") of the Company, the Company granted 200,000 RSUs to the President and CEO, with an effective grant date of May 7, 2018. Vesting dates are May 7, 2019 (for the first 60,000 RSUs); May 7, 2020 (for the second 60,000 RSUs) and May 7, 2021 (for the final 80,000 RSUs), subject to additional terms and conditions relating to resignation, disability, death and others. No further RSUs will be granted to the President and CEO prior and up to May 7, 2021, the final vesting date.

On May 6, 2013, as part of a five-year incentive agreement and pursuant to its long-term incentive plan, the Company granted 400,000 RSUs to the President and CEO, with a vesting date of May 6, 2016. The compensation expense related to the five-year agreement was recognized in the consolidated statement of income over a five-year period. On May 6, 2016, the full amount of $19,106 was paid under these RSUs. The difference between the amount paid and the expense recognized in the consolidated statement of income has been recorded as a prepaid expense and amortized over the remaining two-year period. As of December 31, 2018, the prepaid balance was nil (2017 - $1,592).

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

12 Cash flow information

The following table presents the movements in the liabilities from financing activities for the years ended December 31, 2017 and 2018:

	Liabilities from financing activities			
	Long-term debt $	Syndicated credit facilities $	Non-competes payable $	Total $
Balance as at January 1, 2017	(47,898)	(646,487)	(7,963)	(702,348)
Cash flows	(184,363)	391,796	2,156	209,589
Foreign exchange adjustments	8,704	22,608	454	31,766
Other non-cash movements	-	-	(155)	(155)
Balance as at December 31, 2017	(223,557)	(232,083)	(5,508)	(461,148)
Cash flows	6,705	(18,742)	1,745	(10,292)
Foreign exchange adjustments	(22,740)	(22,230)	(392)	(45,362)
Other non-cash movements	(833)	-	(124)	(957)
Balance as at December 31, 2018	(240,425)	(273,055)	(4,279)	(517,759)

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

13 Capital stock

	2018	2017
Number of common shares outstanding – Beginning of year*	69,342	69,303
Stock option plan*	-	10
Employee share purchase plans*	31	29
Repurchase of common shares*	(105)	-
Number of common shares outstanding – End of year*	69,268	69,342

* Number of common shares is presented in thousands.

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

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

	2018	2017
Net income applicable to common shares	$137,597	$167,889
Weighted average number of common shares outstanding*	69,352	69,324
Effect of dilutive stock options*	8	9
Weighted average number of diluted common shares outstanding*	69,360	69,333
Basic earnings per common share **	$1.98	$2.42
Diluted earnings per common share **	$1.98	$2.42

* Number of shares is presented in thousands.

** Basic and diluted earnings per common share are presented in dollars per share.

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

c) Normal Course Issuer Bid

On December 18, 2018 the TSX accepted the Company's Notice of Intention to Make a Normal Course Issuer Bid. The Normal Course Issuer Bid was initiated for a twelve-month period starting on December 20, 2018. During this period, the Company may purchase for cancellation up to 3,000,000 common shares. As at December 31, 2018, the Company repurchased 105,000 common shares for cancellation in consideration of $4,038 representing an average price of $38.15 per common share. As at December 31, 2018, the Company had unsettled transactions to repurchase 42,000 common shares for a cash consideration of $1,627 representing an average price of $39.05 per common share. As of December 31, 2018, the Company recorded a financial liability with an offset amount in equity in the amount of $1,627. The settlement of these transactions occurred in early January 2019 and the cancellation of the corresponding common share was done at the same time.

d) 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 ("Committee") 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.

The aggregate number of common shares in respect of which options may be granted is 4,800,000 and no optionee may hold options to purchase common shares exceeding 5.00% of the number of common shares issued and outstanding from time to time. The exercise price of an option shall not be lower than the closing price of the common shares on the TSX on the last trading day immediately preceding the date of the granting of the option. Each option shall be exercisable during a period established by the Board of Directors or Committee, and the term of the option may not exceed 10 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.

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

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

	2018		2017	
	Number of options*	Weighted average exercise price** $	Number of options*	Weighted average exercise price** $
Outstanding – Beginning of year	45	40.05	55	34.57
Exercised	-	-	(10)	9.90
Granted	-	-	-	-
Outstanding – End of year	45	40.05	45	40.05
Options exercisable – End of year	39	38.67	33	36.79

The following options were outstanding under the Plan as at December 31, 2018:

	Options outstanding		Options exercisable		
Date granted	**Number of options***	**Exercise price** $**	**Number of options***	**Exercise price** $**	**Expiration date**
May 2013	15	22.13	15	22.13	May 2023
November 2015	30	49.01	24	49.01	November 2025
	45		39		

* Number of options is presented in thousands.

** Exercise price is presented in dollars per option.

e) Share-based compensation

The Company records expenses related to 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 income over the vesting period. No options were granted during 2018. The 2018 expense recorded for share-based compensation amortized to earnings was $50 (2017 – $87).

f) Employee share purchase plans

The aggregate number of common shares reserved for issuance under the Company’s two employee share purchase plans is 1,000,000.

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

Under the first plan, Company employees who are Canadian residents are eligible to purchase common shares from the Company at an amount equal to 90.00% of the market price. Employees who hold common shares in the employee share purchase plan for eighteen months following the date of acquisition of such shares receive additional common shares of the Company equivalent to 10.00% of the amount of their contributions made on the date of acquisition. In 2018, 17,591 common shares (2017 – 15,621) were issued to Canadian resident employees at an average price of $37.02 per share (2017 – $39.52).

Under the second plan, Company employees who are U.S. residents are eligible to purchase common shares from the Company at market price. Employees who hold common shares in the employee share purchase plan for eighteen months following the date of acquisition of such shares receive additional common shares of the Company equivalent to 10.00% of the amount of their contributions made on the date of acquisition. In 2018, 13,889 common shares (2017 – 13,167) were issued to U.S. resident employees at an average price of $40.11 per share (2017 – $41.65).

14 Expenses by nature

	2018	**2017**
	$	**$**
Raw materials and consumables	1,537,542	1,324,289
Employee benefit expenses	143,473	135,302
Depreciation and amortization	38,102	35,734
Other expenses incurred in manufacturing process	43,746	54,148
Freight	105,513	91,430
Other expenses	49,216	37,851
	1,917,592	1,678,754

	2018	**2017**
	$	**$**
Employee benefit expenses		
Salaries, wages and benefits	127,587	123,355
Share options granted to directors and employees	50	87
RSUs	7,189	4,549
Pension costs	2,259	1,990
Group registered retirement savings plans	6,388	5,321
	143,473	135,302

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

Employee benefit expenses are included in cost of sales and selling and administrative expenses.

	2018	2017
	$	**$**
Financial expenses		
Interest on syndicated credit facilities	10,168	9,596
Interest on promissory notes and non-compete agreements	1,797	2,613
Interest on unsecured senior notes	7,137	6,800
	19,102	19,009

15 Income taxes

	2018	2017
	$	**$**
Current tax		
Current tax on income for the year	38,710	40,450
Adjustments in respect of prior years	308	1,116
Total current tax	39,018	41,566
Deferred tax		
Origination and reversal of temporary differences	10,965	12,379
Impact of change in tax rate	(191)	(30,094)
Adjustments in respect of prior years	(190)	(3,361)
Total deferred tax	10,584	(21,076)
Income tax expense	49,602	20,490

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

The tax on the Company's income before income tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to income of the consolidated entities as follows:

	2018 $	2017 $
Income before income tax	187,199	188,379
Tax calculated at domestic tax rates of 26.46% (2017 – 26.24%) applicable to income in the respective countries	49,533	49,431
Tax effects of:		
Difference in tax rate of foreign subsidiaries	454	12,930
Income not subject to tax	(5,368)	(7,759)
Expenses not deductible for tax purposes	5,062	409
Remeasurement of deferred tax – change in tax rate	(191)	(30,094)
Adjustments in respect of prior years	118	(2,245)
Exchange revaluation of deferred tax	(6)	(462)
Manufacturing and processing tax credit	-	(1,720)
Income tax expense	49,602	20,490

The analysis of deferred tax assets and deferred tax liabilities is as follows:

	2018 $	2017 $
Deferred tax assets		
To be recovered after more than 12 months	2,894	5,554
To be recovered within 12 months	11,454	8,243
Deferred tax liabilities		
To be reversed after more than 12 months	(106,905)	(86,081)
To be reversed within 12 months	-	(124)
Deferred tax liability, net	(92,557)	(72,408)

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

The gross movement on the deferred income tax account is as follows:

	2018 $	2017 $
As at January 1	(72,408)	(101,171)
Recognized in the statement of income	(10,584)	21,076
Recognized in other comprehensive income	(3,935)	2,697
Business acquisitions	(2)	140
Exchange differences	(5,628)	4,850
As at December 31	(92,557)	(72,408)

The movement in deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

	Reserves $	Deferred pension benefits $	Cumulative losses $	Unrealized foreign exchange on debts and translation of foreign operations $	Others $	Total $
Deferred tax assets						
As at January 1, 2017	12,480	2,165	2,232	-	96	16,973
Recognized in the statement of income	(3,606)	112	(2,232)	2,231	(96)	(3,591)
Recognized in other comprehensive income	-	(246)	-	1,150	-	904
Business acquisitions	180	-	-	-	-	180
Exchange differences	(589)	(80)	-	-	-	(669)
As at December 31, 2017	8,465	1,951	-	3,381	-	13,797
Recognized in the statement of income	120	165	-	(17)	2,152	2,420
Recognized in other comprehensive income	-	(282)	-	(3,270)	-	(3,552)
Business acquisitions	1,094	-	-	-	-	1,094
Exchange differences	615	68	-	(94)	-	589
As at December 31, 2018	10,294	1,902	-	-	2,152	14,348

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

	Property, plant and equipment $	Intangible assets $	Unrealized foreign exchange on debts and translation of foreign operations $	Others $	Total $
Deferred tax liabilities					
As at January 1, 2017	(79,785)	(34,330)	(2,049)	(1,982)	(118,146)
Recognized in the statement of income	15,684	8,371	-	612	24,667
Recognized in other comprehensive income	-	-	2,049	(256)	1,793
Business acquisitions	(40)	-	-	-	(40)
Exchange differences	4,272	1,524	-	(275)	5,521
As at December 31, 2017	(59,869)	(24,435)	-	(1,901)	(86,205)
Recognized in the statement of income	(13,158)	35	-	119	(13,004)
Recognized in other comprehensive income	-	-	-	(383)	(383)
Business acquisitions	(1,096)	-	-	-	(1,096)
Exchange differences	(4,610)	(1,607)	-	-	(6,217)
As at December 31, 2018	(78,733)	(26,007)	-	(2,165)	(106,905)

As of December 31, 2018, the Company did not recognize deferred income tax assets of $1,925 (2017 – nil) in respect of capital losses amounting to $14,579 (2017 – nil) that can be carried forward indefinitely against future taxable capital gains.

Deferred income tax liabilities have not been recognized for the withholding tax and other taxes that would be payable on the unremitted earnings of certain subsidiaries. Such amounts are permanently reinvested. Unremitted earnings totaled $461,407 as at December 31, 2018 (2017 – $398,767).

16 Employee future benefits

For its Canadian operations, the Company recognizes costs for several types of employee future benefits.Post-employment benefits are offered to certain retired employees and consist of group health and dental care, life insurance and complementary retirement benefits. The Company 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.

For its U.S. operations, the Company’s wholly-owned subsidiary, McFarland, contributes to two defined benefit pension plans.

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

All other active employees are entitled to a group registered retirement savings plan to which the Company matches one and a half times the employee contribution. The Company's contribution cannot exceed 6.00% of the employee's annual base salary. The recognized costs for employee future benefits were as follows:

	2018 $	2017 $
Post-retirement benefits	167	156
Defined benefit pension plans	1,467	1,411
Contributions to multi-employer plan	625	423
Contributions to group registered retirement savings plans	6,388	5,321

The net amount recognized on the consolidated statement of financial position is detailed as follows:

	2018 $	2017 $
Liabilities		
Accrued benefit liability included in employee future benefits	(5,185)	(5,174)
Accrued benefit obligation, included in employee future benefits	(2,208)	(2,501)
	(7,393)	(7,675)

a) The post-retirement benefits program is not funded and, since June 1, 2011, this program is closed to new participants. For this program, 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 December 1, 2018, and the next required valuation will be as at December 1, 2021.

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

The following information as established by independent actuaries pertains to the Company's post-retirement benefits program:

	2018	2017
	$	$
Accrued benefit obligation		
Balance – Beginning of year	2,501	2,219
Current service cost	80	68
Interest cost	87	88
Benefits payments	(71)	(62)
Remeasurement adjustments		
Plan experience	(237)	-
Changes in financial assumptions	(152)	188
Balance – End of year	2,208	2,501
Plan assets		
Employer's contributions	71	62
Benefits paid	(71)	(62)
Fair value – End of year	-	-
Accrued benefit obligation	2,208	2,501

The significant assumptions used are as follows:

	2018	2017
	%	%
Accrued benefit obligation as at December 31		
Discount rate	3.90	3.40
Benefit costs for the year ended December 31		
Discount rate	3.40	3.90

For measurement purposes, a 6.50% annual rate of increase in the per capita cost of covered health care benefits was assumed starting in 2015. This rate is assumed to decrease gradually by 0.38% per year, to reach 5.00% in 2020. An increase or decrease of 1.00% in this rate would have the following impact:

	Increase of 1%	Decrease of 1%
	$	$
Impact on accrued benefit obligation	27	(24)
Impact on benefit costs	3	(2)

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

The items of the Company's post-retirement benefits program costs recognized during the year are as follows:

	2018 $	2017 $
Current service cost	80	68
Interest cost	87	88
Post-retirement benefits program costs recognized	167	156

Consolidated statement of comprehensive income	**2018** **$**	**2017** **$**
Year ended December 31		
Actuarial gains (losses)	389	(188)
Total recognized in other comprehensive income before income tax	389	(188)

Accumulated actuarial gains (losses) recognized in other comprehensive income	**2018** **$**	**2017** **$**
Balance of actuarial losses as at January 1	(352)	(228)
Net actuarial gains (losses) recognized in the year, net of tax	286	(124)
Balance of actuarial losses as at December 31	(66)	(352)

b) The Company's Canadian defined benefit pension plans base the benefits on the length of service and final average earnings. The McFarland defined benefit pension plans base the benefits on the length of service and flat dollar amounts payable monthly. The Company measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year.

Actuarial valuations are updated every three years, and the latest valuations performed for the five existing pension plans are as follows:

		Date of last actuarial valuation
Plan 1	Canadian pension plan - Closed to new participants	December 31, 2016
Plan 2	Canadian pension plan - Closed to new participants	December 31, 2017
Plan 3	Canadian pension plan - Closed to new participants	December 31, 2018
Plan 4	American pension plan - Closed to new participants	December 31, 2018
Plan 5	American pension plan	December 31, 2018

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

Information about the Company's defined benefit pension plans other than the multi-employer defined benefit plan, in aggregate, is as follows:

	2018	**2017**
	$	**$**
Accrued benefit obligation		
Balance – Beginning of year	29,402	27,440
Current service cost	1,038	1,025
Interest cost	1,055	1,076
Benefits payments	(1,406)	(821)
Remeasurement adjustments		
Plan experience	20	(947)
Changes in demographic assumptions	(31)	330
Changes in financial assumptions	(1,726)	1,949
Exchange difference	861	(650)
Balance – End of year	29,213	29,402
Plan assets		
Fair value – Beginning of year	24,228	22,906
Interest income on plan assets	590	665
Return on plan asset excluding interest income	(738)	513
Employer's contributions	933	1,102
Employee's contributions	36	35
Effect of asset ceiling	(193)	263
Benefits paid	(1,406)	(821)
Exchange difference	578	(435)
Fair value – End of year	24,028	24,228
Accrued benefit liability	(5,185)	(5,174)

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:

	2018	**2017**
	$	**$**
Accrued benefit obligation	(29,140)	(13,309)
Fair value of plan assets	21,384	7,652
Funded status – Plan deficit	(7,756)	(5,657)

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

The percentage of plan assets consists of the following for the year ended December 31:

	2018	**2017**
	%	**%**
Listed equity securities	27.00	31.00
Listed debt securities	42.00	42.00
Guaranteed insurance contracts	30.00	26.00
Short-term investments and cash	1.00	1.00
	100.00	100.00

The significant weighted average assumptions used are as follows:

	2018	**2017**
	%	**%**
Accrued benefit obligation as at December 31		
Discount rate	3.90	3.50
Rate of compensation increase	3.25	3.25
Benefit costs for the year ended December 31		
Discount rate	3.50	3.90

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

	2018	**2017**
	$	**$**
Current service cost, net of employee's contributions	1,002	1,000
Interest cost	1,055	1,076
Interest income on plan assets	(590)	(665)
Defined benefit plan expense	1,467	1,411

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

Expected contributions to the defined benefit pension plans for the year ending December 31, 2019 are $1,081.

Consolidated statement of comprehensive income	**2018**	**2017**
	$	**$**
Year ended December 31		
Actuarial gains (losses)	820	(549)
Total recognized in other comprehensive income before income tax	820	(549)

Accumulated actuarial losses recognized in other comprehensive income	**2018**	**2017**
	$	**$**
Balance of actuarial losses as at January 1	(4,012)	(3,153)
Net actuarial gain (losses) recognized in the year, net of tax	641	(859)
Balance of actuarial losses as at December 31	(3,371)	(4,012)

17 Commitments and contingencies

a) The Company has issued guarantees amounting to $29,716 (2017 – $19,036) 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.

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

	$
2019	30,236
2020	25,572
2021	21,366
2022	16,059
2023	10,091
Thereafter	29,451
	132,775

c) 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.

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

18 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 carrying amounts as at the consolidated statement of financial position dates 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 carrying amounts unless otherwise disclosed elsewhere in these consolidated financial statements.

The fair value of interest rate swap agreements, foreign exchange forward contract agreements and derivative commodity contracts have been recorded using mark-to-market information. The following table provides a summary of these fair values which are detailed further in this note:

	2018	2017
	$	$
Current assets		
Derivative commodity contracts	-	473
	-	473
Non-current assets		
Interest rate swap agreements	7,545	6,173
	7,545	6,173
Current liabilities		
Derivative commodity contracts	4,381	-
	4,381	-
Non-current liabilities		
Derivative commodity contracts	3,748	-
	3,748	-

Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. At December 31, 2018, the Company's credit exposure consists primarily of the carrying amount of cash and cash equivalents, accounts receivable and derivative financial instruments.

Credit risk associated with cash and cash equivalent, and derivative financial instruments is minimised by dealing with creditworthy financial institutions.

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

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 because the Company deals primarily with railroad companies, public service companies and utility and telecommunication companies as well as other major corporations.

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.

Note 5 provides details on the receivable aging as well as on the credit loss provision for the years ended December 31, 2018 and 2017. The Company's largest customer had sales representing 16.60% of the total sales for the twelve-month period ending December 31, 2018 (2017 – 15.60%) and an account receivable balance of $5,678 as at December 31, 2018 (2017 – $6,152). The sales for this customer are included in the residential lumber product category.

Price risk

The Company is exposed to commodity price risk on diesel and petroleum. The Company uses derivative commodity contracts based on the New York Harbor Ultra Low Sulfur Diesel Heating Oil to help manage its cash flows with regards to these commodities. The Company does not designate these derivatives as cash flow hedges of anticipated purchases of diesel and petroleum. Gains or losses from these derivative financial instruments are recorded in the consolidated statements of income under other losses (gain), net. The following table summarizes the derivative commodity contracts as at December 31, 2018 and 2017:

				2018
Hedged item	**Gallons**	**Effective date**	**Maturity date**	**Fixed rate**
Diesel and petroleum	6,000,000*	January 2019	December 2019	US$2.23
Diesel and petroleum	6,000,000*	January 2020	December 2020	US$2.23

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

2017

Hedged item	Gallons	Effective date	Maturity date	Fixed rate
Diesel and petroleum	600,000*	January 2018	December 2018	US$1.72
Diesel and petroleum	600,000*	January 2018	December 2018	US$1.61

* Represents a volume evenly split throughout the year

The fair value of the above derivative commodity hedges based on cash settlement requirements as at December 31, 2018 is a total liability of $8,129 of which $4,381 is recorded under current liabilities and $3,748 recorded under non-current liabilities (2017 – a current asset of $473) in the consolidated statement of financial position. The fair value of these hedge agreements was determined by obtaining mark-to-market values as at December 31, 2018 and 2017 from a third party. This type of measurement falls under Level 2 in the fair value hierarchy as per IFRS 7, *Financial Instruments: Disclosures.* A description of each level of the hierarchy is as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for these assets or liabilities, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Inputs for the assets or liabilities that are not based on observable market data (unobservable inputs).

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.

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

The Company monitors all financial liabilities and ensures it will have sufficient liquidity to meet these future payments. The operating activities of the Company are the primary source of cash flows. The Company also has syndicated credit facilities (Note 10(a)) made available by a syndicate of lenders which can be used for working capital and general corporate requirements. As at December 31, 2018, an amount of $291,569 (US$213,729) (2017 - $354,489 (US$282,574)) was available under the Company's syndicated credit facilities. The following table details the maturities of the financial liabilities as at December 31:

						2018
	Carrying amount	**Contractual cash flows**	**Less than 1 year**	**Between 1 and 3 years**	**Between 3 and 5 years**	**More than 5 years**
	$	**$**	**$**	**$**	**$**	**$**
Accounts payable and accrued liabilities	133,259	133,259	133,259	-	-	-
Long-term debt obligations	513,481	601,849	25,507	51,683	303,142	221,517
Derivative commodity contracts	8,129	8,354	4,108	4,246	-	-
Non-competes payable	4,279	4,570	1,603	2,967	-	-
	659,148	748,032	164,477	58,896	303,142	221,517

						2017
	Carrying amount	**Contractual cash flows**	**Less than 1 year**	**Between 1 and 3 years**	**Between 3 and 5 years**	**More than 5 years**
	$	**$**	**$**	**$**	**$**	**$**
Accounts payable and accrued liabilities	111,206	111,206	111,206	-	-	-
Long-term debt obligations	455,640	538,383	20,067	42,321	265,193	210,802
Non-competes payable	5,508	5,896	1,694	2,948	1,254	-
	572,354	655,485	132,967	45,269	266,447	210,802

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.

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

Currency risk

The Company's exposure to foreign exchange gains or losses from currency fluctuations is related to sales and purchases in U.S. dollars by its Canadian-based operations and to U.S. dollar-denominated long-term debt held by its Canadian company. The Company monitors its transactions in U.S. dollars generated by Canadian-based operations and enters into hedging transactions when required to mitigate its currency risk. The Company's basic hedging activity consists of entering into foreign exchange forward contracts for the sale of U.S. dollars and the purchase of certain goods and services in U.S. dollars. The Company also considers foreign exchange forward contracts for the purchase of U.S. dollars for significant purchases of goods and services that were not covered by natural hedges.

The following table provides information on the impact of a 10.00% strengthening of the U.S. dollar against the Canadian dollar on net income, comprehensive income and equity for the years ended December 31, 2018 and 2017. For a 10.00% weakening of the U.S. dollar against the Canadian dollar, there would be an equal and opposite impact on net income, comprehensive income and equity:

	2018 $	2017 $
Decrease (increase) of net income	385	(806)
Increase of equity	37,895	37,352

This analysis considers the impact of foreign exchange variance on financial assets and financial liabilities denominated in U.S. dollars which are on the consolidated statement of financial position of the Canadian entities:

	2018 $	2017 $
Assets		
Cash	-	11,484
Accounts receivable	900	2,545
Inventories	820	-
	1,720	14,029
Liabilities		
Accounts payable and accrued liabilities	5,566	5,968
	5,566	5,968

The foreign exchange impact for the U.S. dollar-denominated long-term debt, in the Canadian entities, has been excluded for the most part from the sensitivity analysis for other comprehensive income, as the long-term debt is designated as a hedge of net investment in foreign operations (Note 10).

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

Interest rate risk

As at December 31, 2018, the Company has mitigated its exposure to interest rate risk on long-term debt after giving effect to its interest rate swap agreements; 96.00% (2017 – 100.00%) of the Company's long-term debt is at fixed rates.

The Company enters into interest rate swap agreements in order to reduce the impact of fluctuating interest rates on its short- 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 swap agreements.

The syndicated credit facilities defined in Note 10(a) is made available by a syndicate of bank lenders. The financing of these loans is tied to the Canadian bank's prime rate, the BA rate, the U.S. bank's base rate or LIBOR. The Company has minimized its exposure to interest rate fluctuations by entering into interest rate swaps as detailed below. The impact of a 10.00% increase in these rates on the closing annual balance of the syndicated credit facilities, for borrowings that have not been swapped, would have increased interest expense by $370 for the year ended December 31, 2018 (2017 – $146).

The following tables summarize the Company's interest rate swap agreements as at December 31:

					2018
Notional amount	**Related debt instrument**	**Fixed rate %**	**Effective date**	**Maturity date**	**Notional equivalent CA$**
US$85,000	Syndicated credit facilities	1.68*	December 2015	April 2021	115,957
US$100,000	Syndicated credit facilities	1.06*	December 2017	December 2021	136,420

					2017
Notional amount	**Related debt instrument**	**Fixed rate %**	**Effective date**	**Maturity date**	**Notional equivalent CA$**
US$85,000	Syndicated credit facilities	1.68*	December 2015	April 2021	106,633
US$100,000	Syndicated credit facilities	1.06*	December 2017	December 2021	125,450

* Plus applicable spread of 1.00% to 2.25% based on pricing grid included in the Credit Agreement.

The Company's interest rate swap agreements are designated as cash flow hedges. The cash flow hedge documentation allows the Company to substitute the underlying debt as long as the hedge effectiveness is demonstrated. As at December 31, 2018, all cash flow hedges were effective.

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

The fair value of these financial instruments has been determined by obtaining mark-to-market values as at December 31, 2018 from different third parties. This type of measurement falls under Level 2 in the fair value hierarchy as per IFRS 7, *Financial Instruments: Disclosures.* The fair value of the interest rate swap agreements based on cash settlement requirements as at December 31, 2018 is a non-current asset of $7,545 recorded in the consolidated statement of financial position (2017 – a non-current asset of $6,173). A 10.00% decrease in interest rates as at December 31, 2018 would have reduced the net gain recognized in other comprehensive income by approximately $755 (2017 – $617). For a 10.00% increase in the interest rates, there would be an equal and opposite impact on the net gain.

19 Capital disclosures

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 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 total debt, which includes bank indebtedness, and shareholders' equity, which includes capital stock.

	2018	**2017**
	$	**$**
Total debt	513,481	455,640
Shareholders' equity	1,281,410	1,115,545
Total capital	1,794,891	1,571,185
Total debt to total capitalization ratio	0.29:1	0.29:1

The Company's primary uses of capital are to finance 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 its syndicated credit facilities. However, future corporate acquisitions may require new sources of financing.

The primary measure used by the Company to monitor its financial leverage is the total debt to total capitalization ratio, which it aims to maintain within a range of 0.20:1 to 0.50:1. The total debt to total capitalization ratio is defined as total debt divided by total capital.

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

20 Related party transactions

a) Transactions

The Company had the following transactions with related parties:

	2018 $	2017 $
Stella Jones International S.A.*		
Marketing and technical service fees paid	-	200
Stella International S.A. and James Jones & Sons Limited**		
Marketing and technical service fees paid	62	100
Other		
Legal fees charged by a firm in which a director of the Company is a partner	499	838

* As of December 31, 2017, Stella Jones International S.A. held, directly or indirectly, approximately 38.30% of the outstanding common shares of the Company. Pursuant to a secondary offering closed on February 21, 2018, the percentage of outstanding common shares held by Stella International S.A. was reduced to 31.10%. On August 14, 2018, Stella Jones International S.A. sold its remaining share ownership in the Company through a bought public offering and concurrent private placement.

** Stella International S.A. and James Jones & Sons Limited hold 51.00% and 49.00% of all voting shares of Stella Jones International S.A., respectively.

These transactions occurred in the normal course of operations and have been measured at fair value.

As at December 31, the consolidated statement of financial position includes the following amounts with related parties:

	2018 $	2017 $
Accounts receivable from Stella Jones International S.A.	454	-
Accounts payable to Stella International S.A. and James Jones & Sons	-	(25)
Accounts payable to Stella Jones International S.A.	-	(50)
Accounts payable to a firm in which a director of the Company is a partner	(54)	(305)
	400	(380)

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

b) Key management compensation

Key management includes certain directors (executive and non-executive), and certain senior management. The compensation paid or payable to key management for employee services is as follows:

	2018 $	2017 $
Salaries, compensation and benefits	5,010	4,728
Share-based payments	5,293	4,063
	10,303	8,791

21 Segment information

The Company operates within two business segments which are the production and sale of pressure-treated wood and the procurement and sales of logs and lumber.

The pressure-treated wood segment includes railway ties, utility poles, residential lumber and industrial products.

The logs and lumber segment comprises of the sales of logs harvested in the course of the Company's procurement process that are determined to be unsuitable for use as utility poles. Also included in this segment is the sale of excess lumber to local home-building markets. Assets and net income related to the logs and lumber segment are nominal.

Operating plants are located in six Canadian provinces and nineteen American states. The Company also operates a large distribution network across North America.

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

	2018 $	2017 $
Canada	679,642	561,905
U.S.	1,444,251	1,324,237
	2,123,893	1,886,142

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

Sales by product as at December 31 are as follows:

	2018 $	2017 $
Pressure-treated wood		
Railway ties	662,414	651,549
Utility poles	724,950	653,946
Residential lumber	474,680	366,225
Industrial products	109,035	94,516
Logs and lumber	152,814	119,906
	2,123,893	1,886,142

Property, plant and equipment, intangible assets and goodwill attributed to the countries based on location are as follows:

	2018 $	2017 $
Property, plant and equipment		
Canada	124,246	114,819
U.S.	427,539	351,237
	551,785	466,056
Intangible assets		
Canada	33,977	29,974
U.S.	97,681	100,375
	131,658	130,349
Goodwill		
Canada	19,403	14,864
U.S.	278,867	255,397
	298,270	270,261

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

22 Subsequent events

a) On January 14, 2019, the Company obtained a one-year extension of its unsecured revolving facility to February 27, 2024. This extension was granted through an amendment to the fifth amended and restated credit agreement dated as of February 26, 2016, as amended on May 18, 2016 and March 15, 2018.

b) On March 14, 2019, the Board of Directors declared a quarterly dividend of $0.14 per common share payable on April 26, 2019 to shareholders of record at the close of business on April 5, 2019.