2011

Consolidated Financial Statements

CANFOR CORPORATION

MANAGEMENT'S RESPONSIBILITY

The information and representations in these consolidated financial statements are the responsibility of management and have been approved by the Board of Directors. The consolidated financial statements were prepared by management in accordance with International Financial Reporting Standards and, where necessary, reflect management's best estimates and judgments at this time. It is reasonably possible that circumstances may arise which cause actual results to differ. Management does not believe it is likely that any differences will be material.

Canfor maintains systems of internal accounting controls, policies and procedures to provide reasonable assurance as to the reliability of the financial records and the safeguarding of its assets.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board carries out these activities primarily through its Audit Committee.

The Audit Committee is comprised of three Directors who are not employees of the Company. The Committee meets periodically throughout the year with management, external auditors and internal auditors to review their respective responsibilities, results of the reviews of internal accounting controls, policies and procedures and financial reporting matters. The external and internal auditors meet separately with the Audit Committee.

The consolidated financial statements have been reviewed by the Audit Committee and approved by the Board of Directors. The consolidated financial statements have been audited by PricewaterhouseCoopers LLP, the external auditors, whose report follows.

February 8, 2012

"*Don B. Kayne"*	"*Alan Nicholl*"
Don B. Kayne President and Chief Executive Officer	Alan Nicholl Senior Vice-President, Finance and Chief Financial Officer

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Canfor Corporation

We have audited the accompanying consolidated financial statements of Canfor Corporation and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2011, December 31, 2010 and January 1, 2010 and the consolidated statements of income, the consolidated statements of other comprehensive income (loss), the consolidated statements of cash flows, and the consolidated statements of changes in equity for the years ended December 31, 2011 and December 31, 2010, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

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

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Canfor Corporation and its subsidiaries as at December 31, 2011, December 31, 2010 and January 1, 2010 and their financial performance and their cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards.

"PricewaterhouseCoopers LLP"

Chartered Accountants
Vancouver, BC
February 8, 2012

Canfor Corporation
Consolidated Balance Sheets

(millions of Canadian dollars)	As at December 31, 2011	As at December 31, 2010	As at January 1, 2010
			(Note 31)
ASSETS			
Current assets			
Cash and cash equivalents	**$ 28.9**	$ 260.3	$ 133.4
Accounts receivable - Trade	**105.1**	146.9	137.2
- Other	**65.7**	54.2	41.9
Income taxes recoverable	**-**	-	45.5
Inventories (Note 5)	**348.3**	325.8	310.5
Prepaid expenses	**20.4**	28.1	21.0
Total current assets	**568.4**	815.3	689.5
Property, plant and equipment (Note 6)	**1,139.2**	1,049.1	1,077.7
Timber licenses (Note 7)	**530.1**	546.7	563.7
Goodwill and other intangible assets (Note 8)	**83.0**	84.5	92.4
Long-term investments and other (Note 9)	**62.8**	89.1	75.7
Deferred income taxes, net (Note 21)	**18.1**	9.4	7.3
Total assets	**$ 2,401.6**	$ 2,594.1	$ 2,506.3
LIABILITIES			
Current liabilities			
Operating loans (Note 11)	**$ -**	$ -	$ 0.6
Accounts payable and accrued liabilities (Note 10)	**290.5**	292.9	211.4
Current portion of long-term debt (Note 12)	**50.9**	82.5	34.0
Current portion of deferred reforestation obligations (Note 14)	**31.6**	31.6	27.8
Total current liabilities	**373.0**	407.0	273.8
Long-term debt (Note 12)	**188.1**	235.6	333.3
Retirement benefit obligations (Note 13)	**298.3**	272.2	233.5
Deferred reforestation obligations (Note 14)	**65.0**	60.6	67.4
Other long-term liabilities	**13.8**	17.5	18.3
Deferred income taxes, net (Note 21)	**103.3**	131.2	131.0
Total liabilities	**$ 1,041.5**	$ 1,124.1	$ 1,057.3
EQUITY			
Share capital (Note 17)	**$ 1,125.9**	$ 1,125.4	$ 1,124.7
Contributed surplus	**31.9**	31.9	31.9
Retained earnings	**(24.6)**	73.5	33.1
Accumulated foreign exchange translation differences	**(5.9)**	(10.3)	-
Total equity attributable to equity holders of the Company	**1,127.3**	1,220.5	1,189.7
Non-controlling interests	**232.8**	249.5	259.3
Total equity	**$ 1,360.1**	$ 1,470.0	$ 1,449.0
Total liabilities and equity	**$ 2,401.6**	$ 2,594.1	$ 2,506.3

Contingencies (Note 27)

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

APPROVED BY THE BOARD

"R.S. Smith" *"R.L. Cliff"*

Director, R.S. Smith Director, R.L. Cliff

Canfor Corporation
Consolidated Statements of Income

(millions of Canadian dollars, except per share data)	Year ended December 31, **2011**	2010
Sales	**$ 2,421.4**	$ 2,430.4
Costs and expenses		
Manufacturing and product costs	**1,629.8**	1,514.3
Freight and other distribution costs	**467.9**	428.0
Export taxes	**39.9**	40.0
Amortization	**169.3**	167.7
Asset impairments (Note 6)	**9.2**	-
Restructuring, mill closure and severance costs (Note 16)	**38.3**	32.4
Selling and administration costs	**58.6**	61.3
	2,413.0	2,243.7
Operating income	**8.4**	186.7
Finance expense, net (Note 19)	**(22.5)**	(26.8)
Foreign exchange gain (loss) on long-term debt and investments, net	**(5.0)**	14.7
Gain on derivative financial instruments (Note 30)	**3.5**	0.1
Other income, net (Note 20)	**5.9**	8.1
Net income (loss) before income taxes	**(9.7)**	182.8
Income tax recovery (expense) (Note 21)	**20.5**	(9.5)
Net income	**$ 10.8**	$ 173.3
Net income (loss) attributable to:		
Equity shareholders of the Company	**$ (56.6)**	$ 81.4
Non-controlling interests	**67.4**	91.9
Net income	**$ 10.8**	$ 173.3
Net income (loss) per common share: (in dollars)		
Attributable to equity shareholders of the Company		
- Basic and diluted (Note 22)	**$ (0.40)**	$ 0.57

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

Canfor Corporation
Consolidated Statements of Other Comprehensive Income (Loss)

(millions of Canadian dollars)	Year ended December 31, 2011	2010
Net income	**$ 10.8**	$ 173.3
Other comprehensive income (loss)		
Foreign exchange translation differences for foreign operations	**4.4**	(10.3)
Defined benefit plan actuarial losses	**(64.5)**	(61.6)
Income tax recovery on defined benefit plan actuarial losses	**14.2**	13.6
Other comprehensive income (loss), net of tax	**(45.9)**	(58.3)
Total comprehensive income (loss)	**$ (35.1)**	$ 115.0
Total comprehensive income (loss) attributable to:		
Equity shareholders of the Company	**$ (93.7)**	$ 30.1
Non-controlling interests	**58.6**	84.9
Total comprehensive income (loss)	**$ (35.1)**	$ 115.0

Consolidated Statements of Changes in Equity

(millions of Canadian dollars)	Year ended December 31, 2011	2010
Share capital		
Balance at beginning of year	**$ 1,125.4**	$ 1,124.7
Common shares issued on exercise of stock options	**0.5**	0.7
Balance at end of year (Note 17)	**$ 1,125.9**	$ 1,125.4
Contributed surplus		
Balance at beginning and end of year	**$ 31.9**	$ 31.9
Retained earnings		
Balance at beginning of year	**$ 73.5**	$ 33.1
Net income (loss) attributable to equity shareholders of the Company	**(56.6)**	81.4
Defined benefit plan actuarial losses, net of tax	**(41.5)**	(41.0)
Balance at end of year	**$ (24.6)**	$ 73.5
Accumulated foreign exchange translation differences		
Balance at beginning of year	**$ (10.3)**	$ -
Foreign exchange translation differences for foreign operations	**4.4**	(10.3)
Balance at end of year	**$ (5.9)**	$ (10.3)
Total equity attributable to equity holders of the Company	**$ 1,127.3**	$ 1,220.5
Non-controlling interests		
Balance at beginning of year	**$ 249.5**	$ 259.3
Net income attributable to non-controlling interests	**67.4**	91.9
Defined benefit plan actuarial losses attributable to non-controlling interests	**(8.8)**	(7.0)
Distributions to non-controlling interests	**(75.3)**	(94.7)
Balance at end of year	**$ 232.8**	$ 249.5
Total equity	**$ 1,360.1**	$ 1,470.0

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

Canfor Corporation
Consolidated Statements of Cash Flows

(millions of Canadian dollars)	Year ended December 31, 2011	2010
Cash generated from (used in):		
Operating activities		
Net income	**$ 10.8**	$ 173.3
Items not affecting cash:		
Amortization	**169.3**	167.7
Income tax (recovery) expense (Note 21)	**(20.5)**	9.5
Long-term portion of deferred reforestation obligation	**3.1**	(6.7)
Change in fair value of long-term investment (Note 9)	**(0.2)**	(6.3)
Foreign exchange (gain) loss on long-term debt and investments, net	**5.0**	(14.7)
Changes in mark-to-market value of derivative financial instruments	**(3.9)**	(1.7)
Employee future benefits	**(1.9)**	6.4
Net finance expense (Note 19)	**22.5**	26.8
Asset impairments (Note 6)	**9.2**	-
Mill closure provisions (Note 16)	**22.5**	17.3
Other, net	**(9.7)**	(10.4)
Salary pension plan contributions	**(37.3)**	(29.9)
Income taxes recovered (paid), net	**(0.3)**	45.9
Net change in non-cash working capital (Note 23)	**(5.6)**	4.4
	163.0	381.6
Financing activities		
Repayment of long-term debt (Note 12)	**(81.9)**	(35.1)
Finance expenses paid	**(18.9)**	(25.1)
Cash distributions paid to non-controlling interests	**(91.0)**	(79.0)
Other, net	**0.4**	(0.1)
	(191.4)	(139.3)
Investing activities		
Additions to property, plant and equipment	**(312.3)**	(142.2)
Reimbursements from Government under Green Transformation Program (Note 6)	**75.6**	20.2
Proceeds from redemption of asset-backed commercial paper (Note 9)	**29.8**	4.6
Other, net	**4.2**	3.1
	(202.7)	(114.3)
Foreign exchange gain (loss) on cash and cash equivalents of subsidiaries with different functional currency	**(0.3)**	(1.1)
Increase (decrease) in cash and cash equivalents	**(231.4)**	126.9
Cash and cash equivalents at beginning of year	**260.3**	133.4
Cash and cash equivalents at end of year	**$ 28.9**	$ 260.3

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

Canfor Corporation
Notes to the Consolidated Financial Statements

1. Reporting Entity

Canfor Corporation is a company incorporated and domiciled in Canada and listed on the Toronto Stock Exchange. The address of the Company's registered office is 100-1700 West 75th Avenue, Vancouver, British Columbia, Canada, V6P 6G2. The consolidated financial statements of the Company as at and for the year ended December 31, 2011 comprise the Company and its subsidiaries (together referred to as "Canfor" or "the Company") and the Company's interests in associates and jointly controlled entities.

Canfor is an integrated forest products company with facilities in Canada and the United States. The Company produces softwood lumber, pulp and paper products, oriented strand board, remanufactured lumber products and specialized wood products.

2. Basis of Preparation

Statement of compliance

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRSs" or "IFRS") as issued by the International Accounting Standards Board ("IASB"). These are the Company's first annual consolidated financial statements prepared in accordance with IFRSs and IFRS 1 *First-time Adoption of International Financial Reporting Standards* has been applied. An explanation of how the transition to IFRSs has affected the reported financial position, financial performance and cash flows of the Company is provided in note 31.

The consolidated financial statements were authorised for issue by the Board of Directors on February 8, 2012.

Basis of measurement

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

- Derivative financial instruments are measured at fair value;
- Financial instruments classified as fair value through profit and loss are measured at fair value;
- Asset retirement obligations and deferred reforestation obligations are measured at the discounted value of expected future cash flows; and
- The retirement benefit obligation recognized in the balance sheet in respect of a defined benefit pension plan is the net of the accrued benefit obligation and the fair value of the plan assets.

Use of estimates and judgments

The preparation of the consolidated financial statements in accordance with IFRSs requires management to make judgments, estimates and assumptions that effect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Canfor regularly reviews its estimates and assumptions; however, it is possible that circumstances may arise which cause actual results to differ from management estimates, and these differences could be material. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about the significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant affect on the amounts recognized in the consolidated financial statements is included in the applicable notes:

- Note 6 – Property, Plant and Equipment;
- Note 7 – Timber Licenses;
- Note 8 – Goodwill and Other Intangible Assets;
- Note 13 – Employee Future Benefits;

- Note 14 – Deferred Reforestation Obligations;
- Note 15 – Asset Retirement Obligations; and
- Note 21 – Income Taxes.

3. Significant Accounting Policies

The following accounting policies have been applied to the financial information presented.

Basis of consolidation

Subsidiaries are entities controlled by the Company. Control exists when Canfor is able to govern the financial and operating activities of those other entities to generate returns for the Company. Inter-company transactions, balances and unrealized gains and losses on transactions between different entities within the Company are eliminated. Significant subsidiaries include Canadian Forest Products Ltd. and New South Companies Inc. ("New South"), which are wholly owned, and Canfor Pulp Limited Partnership ("CPLP"), which is 50.2% owned. There were no changes to the percentage ownership interest during 2011 or 2010 for these entities.

Joint ventures are those entities over whose activities Canfor has joint control, established by contractual agreement and requiring unanimous consent for strategic financial and operating decisions. Joint ventures are proportionately consolidated. Canfor's joint ventures include a 50% interest in Canfor-LP OSB Limited Partnership.

Associates are those entities in which Canfor exercises significant influence, but not control, over financial and operating policies. Unless circumstances indicate otherwise, significant influence is presumed to exist when Canfor holds between 20 and 50 percent of the voting power of another entity. Associates are accounted for using the equity method and are recognized initially at cost. The consolidated financial statements include Canfor's share of the post-acquisition income and expenses and equity movement of these equity accounted investees.

Cash and cash equivalents

Cash and cash equivalents include cash in bank accounts and highly liquid money market instruments with maturities of three months or less from the date of acquisition, and are valued at cost, which approximates market value. Interest is earned at variable rates dependent on amount, credit quality and term.

Financial instruments

Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through net income, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below:

Financial assets at fair value through net income - An instrument is classified at fair value through net income if it is held for trading or is designated as such upon initial recognition. Financial instruments at fair value through net income are measured at fair value, and changes therein are recognized in net income, with attributable transaction costs being recognized in net income when incurred. Included within this category is asset-backed commercial paper ("ABCP").

Available-for-sale financial assets - Canfor's investments in equity securities are classified as available-for-sale financial assets where it does not have control or significant influence over the investee. These instruments do not have a quoted market price in an active market. Any impairment loss on these investments is recorded through net income.

Loans and receivables - Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These are measured at amortized cost using the effective interest method, less any impairment losses. The effective interest method is used to spread the total costs of or income from a financial instrument over the life of the instrument. Financial assets included within this category for Canfor are trade and other receivables, and cash and cash equivalents. Cash and cash equivalents include cash in bank accounts and highly liquid money market instruments with maturities of three months or less from the date of acquisition.

Other liabilities - All of Canfor's financial liabilities are measured at amortized cost using the effective interest method.

Derivative financial instruments

Canfor uses derivative financial instruments in the normal course of its operations as a means to manage its foreign exchange, energy and commodity price risk. Canfor's policy is not to utilize derivative financial instruments for trading or speculative purposes.

Canfor's derivative financial instruments are not designated as hedges for accounting purposes. Consequently, such derivatives for which hedge accounting is not applied are carried on the balance sheet at fair value, with changes in fair value (realized and unrealized) being recognized in the statements of income outside of operating income as 'Gain (loss) on derivative financial instruments'.

The fair value of the derivatives is determined with reference to period end market trading prices for derivatives with comparable characteristics.

Inventories

Inventories include logs, lumber, oriented strand board, pulp, kraft paper, chips, and processing materials and supplies. These are measured at the lower of cost and net realizable value. The cost of inventories is based on the weighted average cost principle, and includes raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses.

Property, plant and equipment

Items of property, plant and equipment are measured at cost less accumulated amortization and impairment losses.

Cost includes expenditures which are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, borrowing costs, and any other costs directly attributable to bringing assets to be used in the manner intended by management.

The cost of replacing a major component of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to Canfor and its cost can be measured reliably. The carrying amount of the replaced component is removed. The costs of the day-to-day servicing of property, plant and equipment are recognized in net income as incurred.

Amortization is recognized in net income on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment, as set out in the table below. Land is not amortized. The significant majority of Canfor's amortization expense for property, plant and equipment relates to manufacturing and product costs.

Amortization methods, useful lives and residual values are reviewed, and adjusted if appropriate, at each reporting date. The following rates have been applied to Canfor's capital assets:

Buildings	5 to 50 years
Pulp and kraft paper machinery and equipment	20 years
Sawmill machinery and equipment	5 to 15 years
Oriented strand board machinery and equipment	10 to 20 years
Logging machinery and equipment	4 to 20 years
Logging roads and bridges	5 to 25 years
Mobile and other equipment	5 years

Timber licenses

Timber licenses include tree farm licenses, forest licenses and timber licenses that are renewable with the Province of British Columbia and Alberta when the relevant conditions are met. Timber licenses are carried at cost less accumulated amortization. Renewable licenses are amortized using the straight-line method over 50 years, while non-renewable licenses are amortized over the period of the license.

Other intangible assets

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of Canfor's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill is tested annually for impairment and carried at cost less any accumulated impairment losses.

On transition to IFRS, Canfor elected not to restate any business combinations under IFRS that occurred before the transition date of January 1, 2010. In respect of acquisitions prior to January 1, 2010, goodwill represents the amount recognized under previous Canadian generally accepted accounting principles ("GAAP").

Customer agreements

Canfor's customer agreements were acquired as part of the purchase of New South, and were recognized at fair value at the acquisition date. The customer agreements have a finite useful life and are carried at cost less accumulated amortization, which is recorded on a straight-line basis over 10 years.

Computer software

Software development costs relate to major software systems purchased or developed by the Company. These costs are amortized on a straight-line basis over periods not exceeding five years.

Government assistance

Government assistance relating to the acquisition of property, plant and equipment is recorded as a reduction of the cost of the asset to which it relates, with any amortization calculated on the net amount. Government assistance related to non-capital projects is recorded as a reduction of the related expenses.

Asset impairment

Canfor's property, plant and equipment, timber licenses and other intangible assets are reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, except for goodwill which is reviewed annually.

An impairment loss is recognized in net income at the amount the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows that are largely independent of cash inflows from other assets or groups of assets (cash-generating units or "CGU").

Non-financial assets, other than goodwill, for which an impairment was recorded in a prior period are reviewed for possible reversal of the impairment at each reporting date. When an impairment loss is reversed, the increased carrying amount of the asset cannot exceed the carrying amount that would have been determined (net of amortization) had no impairment loss been recognized in prior years.

For the purpose of impairment testing, goodwill is allocated to the Company's operating divisions which represent the lowest level within the Company at which the goodwill is monitored for internal management purposes.

Financial assets are reviewed at each reporting date to determine whether there is evidence indicating they are impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative impact on estimated future cash flows from that asset. An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. All impairment losses are recognized in net income.

Employee benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity makes contributions to a separate entity and has no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognized as an employee benefit expense in net income when they are due.

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. Canfor has various defined benefit plans that provide both pension and other retirement benefits to most of its salaried employees and certain hourly employees not covered by forest industry union plans. Canfor also provides certain health care benefits and pension bridging benefits to eligible retired employees.

The liability recognized in the balance sheet in respect of a defined benefit pension plan is the net of the accrued benefit obligation and the fair value of the plan assets. The accrued benefit obligation is calculated separately for each plan by estimating the amount of future benefit earned by employees in respect of their service in the current and prior periods; that benefit is discounted to determine its present value. The discount rate used to determine the present value of the obligation is the yield at the reporting date on high quality corporate bonds that have maturity dates approximating the terms of Canfor's obligations. The calculation is performed annually by a qualified actuary using the projected unit credit method and a measurement date of December 31. The pension deficit or surplus is adjusted on a quarterly basis for any material changes in underlying assumptions.

Canfor recognizes all actuarial gains and losses arising from defined benefit plans in other comprehensive income in the year in which they occur.

Provisions

Canfor recognizes a provision if, as a result of a past event, it has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. The provision recorded is management's best estimate of the expenditure required to settle the present obligation at the end of the reporting period. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The expense arising from the unwinding of the discount due to the passage of time is recorded as a finance cost. The main classes of provision recognized by Canfor are as follows:

Asset retirement obligations

Canfor recognizes a liability for asset retirement obligations in the period in which they are incurred. The site restoration costs are capitalized as part of the cost of the related item of property, plant and equipment and amortized on a basis consistent with the expected useful life of the related asset. Asset retirement obligations are discounted at the risk-free rate in effect at the balance sheet date.

Deferred reforestation obligations

Forestry legislation in British Columbia and Alberta requires Canfor to incur the cost of reforestation of its forest, timber and tree farm licenses and forest management agreements. Accordingly, Canfor records a liability for the costs of reforestation in the period in which the timber is harvested. In periods subsequent to the initial measurement, changes in the liability resulting from the passage of time and revisions to management's estimates are recognized in net income as they occur. Deferred reforestation obligations are discounted at the risk-free rate in effect at the balance sheet date.

Restructuring

A provision for restructuring is recognized when Canfor has approved a detailed and formal restructuring plan, which may include the indefinite or permanent closure of one of its operations, and the restructuring either has commenced or has been announced publicly. Provisions are not recognized for future operating costs.

Share-based compensation

Canfor has two share-based compensation plans, as described in note 18.

Compensation expense is recognized for Canfor's Deferred Share Unit ("DSU") Plans when the DSUs are granted, with a corresponding increase to liabilities. The liability is remeasured at each reporting date and at settlement date, with any changes in the fair value of the liability recognized as compensation expense in net income. The fair value of the DSUs is determined with reference to the market price of Canfor's shares as at the date of valuation.

The Company has a stock option performance plan, under which no stock options have been granted since 2002. As discussed in note 31, the Company has adopted the IFRS 1 exemption in relation to share-based payment transactions and has not restated any amount recorded in relation to its stock option performance plan on transition to IFRS, as all grants are fully vested at the date of transition. Cash consideration received from employees when they exercise the options is credited to share capital.

Revenue recognition

Canfor's revenues are derived from the sale of the following major product lines: lumber, oriented strand board, pulp, kraft paper, residual fibre and logs. Revenue is measured at the fair value of the consideration received or receivable net of applicable sales taxes, returns, rebates and discounts and after eliminating sales within the Company. Revenue is recognized when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible returns of the goods can be estimated reliably, there is no continuing management involvement with the goods, and the amounts of revenue can be measured reliably.

Amounts charged to customers for shipping and handling are recognized as revenue, and shipping and handling costs incurred by Canfor are reported as a component of cost of sales. Lumber export taxes are recorded as a component of cost of sales.

Income taxes

Income tax expense comprises current and deferred tax. Current and deferred tax are recognized in net income except to the extent that they relate to items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using the tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous periods.

Canfor recognizes deferred income tax in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is measured at tax rates expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred income tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Investment tax credits are credited to manufacturing and product costs in the period in which it becomes reasonably assured that the Company is entitled to them. Unused investment tax credits are recorded as other current or long-term assets in the Company's balance sheet, depending upon when the benefit is expected to be received.

Foreign currency translation

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 currency.

The majority of Canfor's sales and long-term debt is denominated in foreign currencies, principally the US dollar. Transactions in foreign currencies are translated to the functional currencies of the respective entities at exchange rates at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate on that date. Foreign currency differences arising on translation are recognized in net income.

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to the Canadian dollar at exchange rates at the reporting date. The income and expenses of foreign operations are translated to the Canadian dollar at exchange rates at the transaction dates. Foreign exchange differences are recognized in other comprehensive income, and recorded to the accumulated foreign exchange translation account. Canfor's foreign operations include New South and Canfor USA, both of which are wholly-owned subsidiaries based in the U.S.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. Segment results reported to the chief operating decision-maker include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise interest bearing liabilities, head office expenses, and income tax assets and liabilities. Segment capital expenditure is the total cost incurred during the period to acquire property, plant and equipment, timber licenses and intangible assets, other than goodwill.

4. Changes in Accounting Policy

Accounting standards issued and not applied

Unless otherwise noted, the following new or revised standards and amendments as adopted by the IASB are effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. Canfor has completed an initial review of the potential impact of these new standards on the Company, and is currently considering whether or not to adopt any of these in advance of the mandatory date.

Consolidation and interests in other entities

In May 2011, as part of its consolidation project, the IASB issued the following new suite of consolidation and related standards. The suite is intended to cover all aspects of interests in other entities from determination of how to account for interests in other entities to required disclosure of the interest in those entities. Early adoption is permitted provided that the entire suite of consolidation standards is adopted at the same time.

- IFRS 10, *Consolidated Financial Statements,* introduces a new single control model and single consolidation model built on a revised definition of control and criteria for assessment of consolidation. The new Standard requires an entity to consolidate an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvements with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12, *Consolidation – Special Purpose Entities,* and parts of IAS 27, *Consolidated and Separate Financial Statements.* IFRS 10 is not expected to have a material impact on amounts recorded in the financial statements of Canfor.

- IFRS 11, *Joint Arrangements,* redefines joint operations and joint ventures with a focus on the rights and obligations of an arrangement, rather than its legal form. The new Standard requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting, whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interest in joint ventures. IFRS 11 supersedes IAS 31, *Interests in Joint Ventures,* and SIC-13, *Jointly Controlled Entities – Non-monetary Contributions by Venturers.* Canfor is in the process of assessing the full impact of IFRS 11 on amounts recorded in the financial statements.

- IFRS 12, *Disclosure of Interests in Other Entities,* establishes disclosure requirements for interests in other entities, such as subsidiaries, joint arrangements, associates, and unconsolidated structured entities. The Standard carries forward existing disclosures and also introduces significant additional disclosures that address the nature of, and risks associated with, an entity's interests in other entities. IFRS 12 is not expected to have a material impact on amounts recorded in the financial statements of Canfor; the principal impact will be in the form of additional disclosures.

- There have been amendments to existing standards, including IAS 27 (2011), *Separate Financial Statements,* and IAS 28 (2011), *Investments in Associates and Joint Ventures.* IAS 27 (2011) addresses accounting for subsidiaries, jointly controlled entities and associates in non-consolidated financial statements. IAS 28 (2011) sets out the equity accounting for joint ventures, as well as associates, once the assessment of the arrangement has been made under IFRS 11. The amendments to IAS 27 are not expected to have a material impact on amounts recorded in the financial statements of the Company. Canfor is in the process of assessing the full impact of the amendments to IAS 28, which is dependent upon the assessment of the Company's joint arrangements under IFRS 11.

Employee benefits

- IAS 19, *Employee Benefits,* has been amended to make changes to the recognition and measurement of defined benefit pension expense and termination benefits and to enhance the disclosure of all employee benefits. Pension benefit cost will be split between (i) the cost of benefits accrued in the current period (service cost) and benefit changes (past-service costs (including plan amendments, settlements and curtailments)); and (ii) finance expense or income. Interest cost and expected return on plan assets, which currently reflect different rates, will be replaced with a net interest amount that is calculated by applying one discount rate to the net defined benefit liability (asset). The principal impact on the Company of this portion of the amended standard is expected to be an increase in net finance cost as the Company's return on plan assets will effectively be estimated at a lower rate.

  The amended standard also requires immediate recognition of actuarial gains and losses in other comprehensive income as they arise, without subsequent recycling to net income. This is consistent with the Company's current accounting policy.

  In addition, under the amended standard, the impact of plan amendments related to past service will no longer be recognized over a vesting period but instead will be recognized immediately in the period of a plan amendment. A number of other amendments have been made to recognition, measurement and classification including redefining short-term and other long-term benefits, guidance on the treatment of taxes related to benefit plans, guidance on risk/cost sharing features, and expanded disclosures. Canfor is in the process of assessing the full impact of IAS 19 on amounts recorded in the financial statements and related disclosures.

Other standards and amendments

- IFRS 9, *Financial Instruments,* addresses classification and measurement of financial assets and financial liabilities, and is effective January 1, 2015, with earlier adoption permitted. The Standard replaces the multiple category and measurement models in IAS 39, *Financial Instruments – Recognition and Measurement*. The new Standard limits the number of categories for classification of financial assets to two: amortized cost and fair value through profit or loss. The requirements for financial liabilities are largely in line with IAS 39. IFRS 9 also replaces the models for measuring equity instruments. Equity instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. The ability to recognize unquoted equity instruments at cost under IAS 39 is eliminated. IFRS 9 is not expected to have a material impact on amounts recorded in the financial statements of Canfor.
- IFRS 13, *Fair Value Measurement,* is a comprehensive standard for fair value measurement and disclosure for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received on sale of an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and does not always reflect a clear measurement basis or consistent disclosures. IFRS 13 is not expected to have a material impact on amounts recorded in the financial statements of Canfor.
- IAS 1, *Presentation of Financial Statements,* has been amended to require entities to separate items presented in other comprehensive income ("OCI") into two groups, based on whether or not items may be recycled to net income in the future. Entities that choose to present OCI items before tax will be required to show the amount of tax related to the two groups separately. The amendment is effective for annual periods beginning on or after July 1, 2012, with earlier application permitted. IAS 1 is not expected to have a material impact on amounts recorded in the financial statements of Canfor.

5. Inventories

(millions of Canadian dollars)		**As at December 31, 2011**		As at December 31, 2010		As at January 1, 2010
Finished products	**$**	**186.3**	$	169.7	$	164.7
Logs		**55.9**		53.9		39.9
Residual fibre		**17.3**		17.4		22.3
Processing materials and supplies		**88.8**		84.8		83.6
	$	**348.3**	$	325.8	$	310.5

In 2011, costs of raw materials, consumables and changes in finished products recognized as manufacturing and product costs amounted to $766.0 million (2010 - $749.0 million). The above inventory balances are stated after inventory write-downs from cost to net realizable value. Write-downs at December 31, 2011 totaled $15.5 million (December 31, 2010 - $3.2 million; January 1, 2010 - $25.7 million).

6. Property, Plant and Equipment

(millions of Canadian dollars)		**Land**		**Pulp and kraft paper mills**		**Sawmills, plywood and OSB plants**		**Logging assets and other equipment**		**Total**
Cost										
Balance at January 1, 2010	$	42.5	$	1,380.4	$	1,317.5	$	221.6	$	2,962.0
Additions[1]		5.3		24.5		98.3		2.1		130.2
Disposals		(2.2)		(5.8)		(74.0)		(34.4)		(116.4)
Effect of movements in exchange rates		(0.9)		-		(5.4)		-		(6.3)
Balance at December 31, 2010	$	44.7	$	1,399.1	$	1,336.4	$	189.3	$	2,969.5
Additions[1]		2.0		85.8		155.5		6.7		250.0
Disposals		-		(42.6)		(31.5)		(1.6)		(75.7)
Effect of movements in exchange rates		0.4		-		2.6		-		3.0
Balance at December 31, 2011	$	47.1	$	1,442.3	$	1,463.0	$	194.4	$	3,146.8
Amortization and impairment losses										
Balance at January 1, 2010	$	(7.0)	$	(824.4)	$	(853.5)	$	(199.4)	$	(1,884.3)
Amortization for the year		-		(66.7)		(75.3)		(5.1)		(147.1)
Disposals		-		5.4		67.7		34.4		107.5
Effect of movements in exchange rates		-		-		3.5		-		3.5
Balance at December 31, 2010	$	(7.0)	$	(885.7)	$	(857.6)	$	(170.1)	$	(1,920.4)
Amortization for the year		-		(67.3)		(77.6)		(4.3)		(149.2)
Impairment losses		-		-		(7.9)		(0.8)		(8.7)
Disposals		-		41.6		29.5		1.3		72.4
Effect of movements in exchange rates		-		-		(1.7)		-		(1.7)
Balance at December 31, 2011	$	(7.0)	$	(911.4)	$	(915.3)	$	(173.9)	$	(2,007.6)
Carrying amounts										
At January 1, 2010	$	35.5	$	556.0	$	464.0	$	22.2	$	1,077.7
At December 31, 2010	$	37.7	$	513.4	$	478.8	$	19.2	$	1,049.1
At December 31, 2011	**$**	**40.1**	**$**	**530.9**	**$**	**547.7**	**$**	**20.5**	**$**	**1,139.2**

[1] Net of capital expenditures by CPLP that are financed by the government-funded Green Transformation Program.

Included in the above are assets under construction in the amount of $33.3 million (December 31, 2010 – $12.2 million; January 1, 2010 – $10.2 million), which as at December 31, 2011 are not amortized.

In October 2009, the Canadian federal government announced the introduction of a Pulp and Paper Green Transformation Program (the “Program”) designed to reimburse funds spent by Canadian kraft pulp producers on qualifying energy and environmental capital projects. CPLP was allocated $122.2 million from this Program, most of which related to the installation of a recovery boiler and precipitator upgrade at the Northwood pulp mill. As of December 31, 2011 CPLP has spent its full allocation under the Program. During 2011, CPLP received reimbursements totaling $75.6 million, and $19.7 million was receivable at year end. These projects are expected to provide economic and environmental benefits to CPLP’s operations.

Impairment loss

The Company reviews the carrying values of its long-lived assets, including property, plant and equipment and timber licenses, on a regular basis as events or changes in circumstances may warrant. A review of the carrying values of the Company's sawmill and panel operations and various other assets was undertaken in 2010 and 2011 as a result of the ongoing difficult market conditions and global economic uncertainty.

The recoverable amounts of property, plant and equipment, and timber licenses for impairment assessment purposes were determined using a discounted cash flow calculation to estimate their fair value less costs to sell, using cash flows forecast for periods up to 10 years. Key assumptions used in these cash flow forecasts included forecast prices and foreign exchange rates which the Company's management determined with reference to external publications including Resource Information Systems, Inc. ("RISI") and Forest Economic Advisors ("FEA") publications. A pre-tax discount rate of 11.0% and inflation rate of 2.0% were used for the purposes of the calculations in 2011 and 2010, and the opening balance sheet.

As a result of its review and circumstances specific to certain assets, impairment charges totaling $9.2 million were recorded in 2011 relating to certain of the Company's lumber and panel assets, with $7.2 million related to lumber assets and $2.0 million related to panel assets. $8.7 million of this impairment was recorded in relation to property, plant and equipment, with the remaining $0.5 million recorded against other inventory.

No impairments were recorded in 2010. However, in its IFRS opening balance sheet as at January 1, 2010, the Company recorded impairments of $46.6 million in relation to timber licenses and $9.4 million in relation to property, plant and equipment. These impairments all related to the lumber segment and principally reflect the impact of the Mountain Pine Beetle epidemic on the Company's BC Interior operations.

7. Timber Licenses

(millions of Canadian dollars)		
Cost		
Balance at January 1, 2010, December 31, 2010 and December 31, 2011	$	840.2
Amortization and impairment losses		
Balance at January 1, 2010	$	(276.5)
Amortization for the year		(17.0)
Balance at December 31, 2010	$	(293.5)
Amortization for the year		(16.6)
Balance at December 31, 2011	$	(310.1)
Carrying amounts		
At January 1, 2010	$	563.7
At December 31, 2010	$	546.7
At December 31, 2011	**$**	**530.1**

An impairment loss of $46.6 million was recognized on timber licenses at the IFRS opening balance sheet date of January 1, 2010 as set out in note 6.

8. Goodwill and Other Intangible Assets

(millions of Canadian dollars)	Goodwill	Customer Agreements	Other	Total
Cost				
Balance at January 1, 2010	$ 73.3	$ 27.3	$ 25.4	$ 126.0
Additions	-	-	0.4	0.4
Disposals	-	-	(2.4)	(2.4)
Effect of movement in exchange rates	(3.7)	(1.3)	-	(5.0)
Balance at December 31, 2010	$ 69.6	$ 26.0	$ 23.4	$ 119.0
Additions	-	-	0.2	0.2
Effect of movement in exchange rates	1.6	0.5	-	2.1
Balance at December 31, 2011	$ 71.2	$ 26.5	$ 23.6	$ 121.3
Amortization				
Balance at January 1, 2010	$ -	$ (10.5)	$ (23.1)	$ (33.6)
Amortization for the year	-	(2.6)	(1.0)	(3.6)
Disposals	-	-	2.2	2.2
Effect of movement in exchange rates	-	0.5	-	0.5
Balance at December 31, 2010	$ -	$ (12.6)	$ (21.9)	$ (34.5)
Amortization for the year	-	(2.6)	(0.9)	(3.5)
Effect of movement in exchange rates	-	(0.3)	-	(0.3)
Balance at December 31, 2011	$ -	$ (15.5)	$ (22.8)	$ (38.3)
Carrying amounts				
At January 1, 2010	$ 73.3	$ 16.8	$ 2.3	$ 92.4
At December 31, 2010	$ 69.6	$ 13.4	$ 1.5	$ 84.5
At December 31, 2011	**$ 71.2**	**$ 11.0**	**$ 0.8**	**$ 83.0**

Goodwill relates to Canfor's U.S. subsidiary, New South Companies Inc., and is denominated in US dollars. Goodwill is not allocated any level lower than the New South company and therefore this is considered to be the CGU for the purposes of the review of goodwill for impairment. The recoverable amount of the goodwill is determined based on an assessment of the fair value less costs to sell of the CGU. This is estimated using a discounted cash flow model to value the New South company.

As part of this process, assumptions are made in relation to forecast prices and exchange rates. Price forecasts are determined with reference to RISI and FEA publications and management estimates, and forecast exchange rates are based on forecasts from various recognized authorities. Given the inherent uncertainty regarding longer term prices and foreign exchange rates, management considers various possible scenarios and assigns probabilities to the likelihood of occurrence of each of these. A pre-tax discount rate of 11.0% and inflation rate of 2.0% were used for the purposes of the discounted cash flow calculations in 2011 and 2010. The net present value of the future expected cash flows is compared to the carrying value of the Company's investment in these assets, including goodwill, at year end.

Based upon management's analysis, no impairment of goodwill was required in 2011, 2010 or the opening balance sheet.

9. Long-Term Investments and Other

(millions of Canadian dollars)	As at December 31, 2011	As at December 31, 2010	As at January 1, 2010
Asset-backed commercial paper ("ABCP")	**$ 11.8**	$ 40.9	$ 41.1
Other investments	**24.3**	26.5	27.3
Investment tax credits	**8.6**	6.4	-
Defined benefit plan assets	**3.0**	3.4	4.2
Other deposits, loans and advances	**15.1**	11.9	3.1
	$ 62.8	$ 89.1	$ 75.7

In 2011, the Company recorded a gain of $0.2 million (2010 - $6.3 million) arising from a change in the fair value of its US dollar denominated investment in ABCP, due to an increase in the fair value of the ABCP assets. In addition, net proceeds of $29.8 million were received from the redemption of certain ABCP assets in 2011 (2010 - $4.6 million). The remaining movement in this balance over the period relates to foreign exchange.

Other investments includes the Company's 33.3% investment in Lakeland Mills Ltd. and Winton Global Lumber Ltd. The Company does not exercise significant influence with respect to this investment.

10. Accounts Payable and Accrued Liabilities

(millions of Canadian dollars)	As at December 31, 2011	As at December 31, 2010	As at January 1, 2010
Trade payables and accrued liabilities	**$ 159.7**	$ 139.2	$ 97.6
Accrued payroll and related liabilities	**73.2**	72.9	67.9
Derivative financial instruments	**1.8**	6.7	5.4
Restructuring, mill closure and severance costs	**27.1**	17.4	13.7
Interest and distributions payable	**6.9**	24.0	8.5
Other	**21.8**	32.7	18.3
	$ 290.5	$ 292.9	$ 211.4

11. Operating Lines

(millions of Canadian dollars)	As at December 31, 2011	As at December 31, 2010	As at January 1, 2010
Canfor (excluding CPLP)			
Principal operating lines	**$ 350.0**	$ 350.0	$ 355.0
Facility A	**12.9**	12.7	13.5
Facility B	**-**	29.7	35.7
Other	**-**	1.1	1.4
Total operating lines - Canfor (excluding CPLP)	**362.9**	393.5	405.6
Drawn	**-**	-	(0.6)
Letters of credit (principally unregistered pension plans)	**(17.2)**	(17.3)	(18.1)
Total available operating lines - Canfor (excluding CPLP)	**$ 345.7**	$ 376.2	$ 386.9
CPLP			
Main bank loan facility	**$ 40.0**	$ 40.0	$ 40.0
Bridge loan credit facility	**30.0**	-	-
Facility for BC Hydro letter of credit	**10.4**	13.2	16.0
Total operating lines - CPLP	**80.4**	53.2	56.0
Letters of credit (for general business purposes)	**(0.5)**	(0.5)	(0.5)
BC Hydro letter of credit	**(10.4)**	(13.2)	(16.0)
Total available operating lines - CPLP	**$ 69.5**	$ 39.5	$ 39.5
Consolidated			
Total operating lines	**$ 443.3**	$ 446.7	$ 461.6
Total available operating lines	**$ 415.2**	$ 415.7	$ 426.4

In August 2011, the Company extended the maturity of its principal operating line from October 31, 2013 to October 31, 2015. The general terms and conditions of the new facility are similar to the previous facility. Interest is payable at floating rates based on lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin that varies with the Company's net debt to total capitalization ratio.

Facility A, which was for US$12.7 million at December 31, 2011, expired in January 2012, and was non-recourse to the Company under normal circumstances, except for an amount of US$6.7 million. The ABCP assets of the Company had been pledged as security to support this credit facility which had similar terms to the other operating lines, except that the interest rate was plus or minus a margin.

The terms of CPLP's principal bank loan facility include interest payable at floating rates that vary depending on the ratio of net debt to operating earnings before interest, taxes, amortization and certain other non-cash items, and is based on lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin. The maturity date of this facility is November 30, 2013.

CPLP also has a $30.0 million bridge loan credit facility with a maturity date of December 31, 2012 to fund timing differences between expenditures and reimbursements for projects funded under the Canadian Federal Government Green Transformation Program. The bridge facility terms are similar to CPLP's main facility, with interest and other costs at prevailing market rates. CPLP also has a separate facility with a maturity date of November 30, 2013 to cover a $10.4 million standby letter of credit issued to BC Hydro.

As at December 31, 2011, the Company and CPLP were in compliance with all covenants relating to their operating lines of credit and no amounts were drawn on the Company's or CPLP's available operating lines.

All borrowings of CPLP (operating loans and long-term debt) are non-recourse to other entities within the Company.

12. Long-Term Debt

Canfor has the following long-term debt, all of which is unsecured:

Summary of long-term debt

(millions of Canadian dollars)	**As at December 31, 2011**	As at December 31, 2010	As at January 1, 2010
Privately placed senior notes			
Canfor Corporation			
US$97 million, interest at 8.03%, repayable in 3 equal annual installments commencing March 1, 2009	**$ -**	$ 32.2	$ 67.7
US$50 million, interest at 6.18%, repayable April 1, 2011	**-**	49.7	52.3
US$50 million, interest at 6.33%, repayable February 2, 2012	**50.9**	49.7	52.3
US$75 million, interest at 5.42%, repayable April 1, 2013	**76.2**	74.6	78.5
Canfor Pulp Limited Partnership			
US$110 million, interest at 6.41%, repayable November 30, 2013	**111.9**	109.4	115.1
Other long-term obligations	**-**	2.5	1.4
	$ 239.0	$ 318.1	$ 367.3
Less: current portion	**(50.9)**	(82.5)	(34.0)
Long-term portion	**$ 188.1**	$ 235.6	$ 333.3

In 2011, the Company repaid $31.5 million (US$32.3 million) of 8.03% interest rate privately placed senior notes and $48.1 million (US$50.0 million) of 6.18% interest rate privately placed senior notes, as well as $2.3 million of other long-term debt obligations.

Fair value of total long-term debt

The fair value of total long-term debt at December 31, 2011 was $246.6 million (December 31, 2010 – $332.4 million; January 1, 2010 – $377.4 million). The fair value was determined using prevailing market rates for long-term debt with similar characteristics and risk profiles.

Scheduled long-term debt repayments and interest payments

Long-term debt repayments and interest payments for the next two years are as follows:

(millions of Canadian dollars)	Debt Repayments	Interest Payments
2012	$ 50.9	$ 11.6
2013	188.1	7.6
	$ 239.0	$ 19.2

On February 2, 2012, the Company repaid $49.9 million (US$50.0 million) of 6.33% interest rate privately placed senior notes.

13. Employee Future Benefits

Canfor has several funded and unfunded defined benefit plans, as well as defined contribution plans, that provide pension, other retirement and post-employment benefits to substantially all salaried employees and certain hourly employees. The defined benefit plans are based on years of service and final average salary. Canfor's other post-retirement benefit plans are non-contributory and include a range of health care and other benefits. Canfor also provides pension bridge benefits to certain eligible former employees.

Total cash payments for employee future benefits for 2011 were $71.9 million (2010 – $64.5 million), consisting of cash contributed by Canfor to its funded pension plans, cash payments directly to beneficiaries for its unfunded other benefit plans, cash contributed to its defined contribution plans, and cash contributed to forest industry union defined benefit plans.

Defined benefit plans

Canfor measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year.

In 2011, Canfor had five registered defined benefit plans for which actuarial valuations are performed every three years. The most recent actuarial valuation for funding purposes of Canfor's single largest pension plan was as of December 31, 2010, and the next required plan valuation is currently scheduled for December 31, 2013.

Information about Canfor's defined benefit plans, in aggregate, is as follows:

Defined Benefit Plan Assets

	2011		2010	
(millions of Canadian dollars)	**Pension Benefit Plans**	**Other Benefit Plans**	Pension Benefit Plans	Other Benefit Plans
Fair market value of plan assets				
Beginning of year	**$ 513.5**	**$ -**	$ 466.8	$ -
Actual return on plan assets	**10.2**	**-**	45.6	-
Canfor contributions	**48.3**	**5.5**	38.7	5.1
Employee contributions	**0.8**	**-**	0.9	-
Benefit payments	**(42.9)**	**(5.5)**	(38.5)	(5.1)
End of year	**$ 529.9**	**$ -**	$ 513.5	$ -

Plan assets consist of the following:	**As at December 31, 2011**	As at December 31, 2010	As at January 1, 2010
	Percentage of Plan Assets		
Asset category			
Equity securities	**61%**	63%	58%
Debt securities	**39%**	36%	41%
Other	**-**	1%	1%
	100%	100%	100%

Defined Benefit Plan Obligations

(millions of Canadian dollars)	**2011 Pension Benefit Plans**	**2011 Other Benefit Plans**	2010 Pension Benefit Plans	2010 Other Benefit Plans
Accrued benefit obligation				
Beginning of year	**$ 608.0**	**$ 150.8**	$ 553.6	$ 123.7
Current service cost	**10.2**	**1.8**	8.8	1.7
Interest cost	**32.7**	**8.3**	33.7	8.0
Employee contributions	**0.8**	**-**	0.9	-
Benefit payments	**(42.9)**	**(5.5)**	(38.5)	(5.1)
Actuarial loss (gain)	**21.5**	**19.2**	49.5	22.0
Other	**1.3**	**(0.1)**	-	0.5
End of year	**$ 631.6**	**$ 174.5**	$ 608.0	$ 150.8

Of the defined benefit plan obligation of $631.6 million (December 31, 2010 – $608.0 million; January 1, 2010 – $553.6 million), $12.2 million relates to plans that are wholly unfunded and $619.4 million relates to plans that are wholly or partly funded (December 31, 2010 - $12.3 million and $595.7 million, respectively; January 1, 2010 - $11.7 million and $541.9 million, respectively). At December 31, 2011, certain liabilities for unregistered plans were secured by a letter of credit in the amount of $12.2 million (December 31, 2010 - $12.2 million; January 1, 2010 - $12.9 million).

The total obligation for the other benefit plans of $174.5 million (December 31, 2010 - $150.8 million; January 1, 2010 - $123.7 million) is unfunded.

Reconciliation of Funded Status of Benefit Plans to Amounts Recorded in the Financial Statements

(millions of Canadian dollars)	**December 31, 2011 Pension Benefit Plans**	**December 31, 2011 Other Benefit Plans**	December 31, 2010 Pension Benefit Plans	December 31, 2010 Other Benefit Plans	January 1, 2010 Pension Benefit Plans	January 1, 2010 Other Benefit Plans
Fair market value of plans assets	**$ 529.9**	**$ -**	$ 513.5	$ -	$ 466.8	$ -
Accrued benefit obligation	**(631.6)**	**(174.5)**	(608.0)	(150.8)	(553.6)	(123.7)
Funded status of plans – surplus (deficit)	**$ (101.7)**	**$ (174.5)**	$ (94.5)	$ (150.8)	$ (86.8)	$ (123.7)
Unamortized past service costs	**-**	**0.1**	-	-	-	0.1
Effect of limit on recognition of asset	**-**	**-**	(4.1)	-	(3.8)	-
Accrued benefit liability	**$ (101.7)**	**$ (174.4)**	$ (98.6)	$ (150.8)	$ (90.6)	$ (123.6)
Pension bridge benefits	**(16.8)**	**-**	(18.4)	-	(15.9)	-
Other pension plans	**(2.4)**	**-**	(1.0)	-	0.8	-
Total accrued benefit liability, net	**$ (120.9)**	**$ (174.4)**	$ (118.0)	$ (150.8)	$ (105.7)	$ (123.6)

The net accrued benefit liability is included in Canfor's balance sheet as follows:

(millions of Canadian dollars)	**December 31, 2011** **Pension Benefit Plans**	**Other Benefit Plans**	December 31, 2010 Pension Benefit Plans	Other Benefit Plans	January 1, 2010 Pension Benefit Plans	Other Benefit Plans
Long-term investments and other	**$ 3.0**	**$ -**	$ 3.4	$ -	$ 4.2	$ -
Retirement benefit obligations	**(123.9)**	**(174.4)**	(121.4)	(150.8)	(109.9)	(123.6)
Total accrued benefit liability, net	**$ (120.9)**	**$ (174.4)**	$ (118.0)	$ (150.8)	$ (105.7)	$ (123.6)

The following table shows the experience adjustments arising on plan liabilities and assets as a result of the differences between actuarial assumptions made at the beginning of the year and the actual experience during the year:

(millions of Canadian dollars)	**2011** **Pension Benefit Plans**	**Other Benefit Plans**	2010 Pension Benefit Plans	Other Benefit Plans
Experience gain (loss) arising on plan liabilities	**$ 3.7**	**$ (9.8)**	$ 22.6	$ (8.4)
Experience gain (loss) arising on plan assets	**$ (28.1)**	**$ -**	$ 11.8	$ -

Components of pension cost

The following table shows the before tax impact on net income and other comprehensive income of the Company's pension and other defined benefit plans:

(millions of Canadian dollars)	**2011** **Pension Benefit Plans**	**Other Benefit Plans**	2010 Pension Benefit Plans	Other Benefit Plans
Recognized in net income				
Current service cost	**$ 10.2**	**$ 1.8**	$ 8.8	$ 1.7
Interest cost	**32.7**	**8.3**	33.7	8.0
Expected return on plan assets	**(38.1)**	**-**	(33.9)	-
Other	**1.1**	**(0.1)**	-	0.5
Total, included in staff costs	**$ 5.9**	**$ 10.0**	$ 8.6	$ 10.2
Recognized in other comprehensive income				
Actuarial loss (gain) immediately recognized	**$ 49.5**	**$ 19.2**	$ 37.7	$ 22.0
Effect of limit on recognition of asset	**(4.1)**	**-**	0.4	-
Total pension cost recognized in other comprehensive income	**$ 45.4**	**$ 19.2**	$ 38.1	$ 22.0

In addition to the amounts shown above, the expense recorded in net income for the bridge benefits in 2011 was $1.3 million (2010 - $2.6 million), and $1.4 million was credited to other comprehensive income (2010 – expense of $1.5 million). Excluded from the above table are the amounts relating to a defined benefit pension plan of New South and Canfor USA.

The expected return on plan assets is determined by taking into account the expected returns on the assets based on the Company's current investment policy.

Significant assumptions

The actuarial assumptions used in measuring Canfor's benefit plan provisions and benefit costs are as follows:

	December 31, 2011		December 31, 2010		January 1, 2010	
	Pension Benefit Plans	**Other Benefit Plans**	Pension Benefit Plans	Other Benefit Plans	Pension Benefit Plans	Other Benefit Plans
Accrued benefit obligations at reporting date:						
Discount rate	**5.00%**	**5.30%**	5.50%	5.75%	6.25%	6.75%
Rate of compensation increases	**3.00%**	**n/a**	3.00%	n/a	3.00%	n/a
Benefit costs for year ended December 31:						
Discount rate	**5.50%**	**5.75%**	6.25%	6.75%	n/a	n/a
Expected return on plan assets	**7.00%**	**n/a**	7.50%	n/a	n/a	n/a
Future salary increases	**3.00%**	**n/a**	3.00%	n/a	n/a	n/a

Assumed health care cost trend rates

(weighted average assumptions)	**December 31, 2011**	December 31, 2010	January 1, 2010
Initial health care cost trend rate	6.33%	6.95%	7.15%
Ultimate health care cost trend rate	4.50%	4.20%	4.20%
Year ultimate rate is reached	2029	2029	2029

Sensitivity analysis

Assumed health care cost trend rates have a significant effect on the amounts reported for the other benefit plans. A one percentage point change in assumed health care cost trend rates would have the following effects for 2011:

(millions of Canadian dollars)	1% Increase	1% Decrease
Effect on accrued benefit obligation	$ 30.0	$ 24.1
Effect on the aggregate service and interest cost	$ 1.9	$ 1.5

For the Company's single largest pension plan, a one percentage point increase in the rate of return on plan assets over the year would reduce the funded deficit by an estimated $4.0 million. A one percentage point increase in the discount rate used in calculating the actuarial estimate of future liabilities would reduce the funded deficit by an estimated $50.0 million. These changes would only impact the Company's funding requirements in years where a new actuarial funding valuation was performed and approval for a change in annual funding contributions was obtained from the regulator.

As at December 31, 2011, Canfor estimated that it will make contribution payments of $52.6 million to its defined benefit plans in 2012.

Defined contribution and other plans

The total cost recognized in 2011 for Canfor's defined contribution plans was $7.0 million (2010 - $5.1 million).

Canfor contributes to various forest industry union defined benefit pension plans providing both pension and other retirement benefits. These plans are accounted for as defined contribution plans. Contributions to these plans, not included in the cost recognized for defined contribution plans above, amounted to $15.1 million in 2011 (2010 - $14.4 million).

Other

Canfor's total employee benefits expense includes expense for salaries and wages, benefits and employee future benefits. The total employee benefits expense in 2011 was $436.7 million (2010 - $430.1 million).

14. Deferred Reforestation Obligations

The following table provides a reconciliation of the deferred reforestation obligations as at December 31, 2011 and 2010:

(millions of Canadian dollars)		**2011**		2010
Reforestation obligations at beginning of year	**$**	**92.2**	$	95.2
Expense for year		**29.1**		23.4
Accretion expense		**1.2**		1.1
Changes in estimates		**(1.1)**		(4.9)
Paid during the year		**(24.8)**		(22.6)
Reforestation obligations at end of year	**$**	**96.6**	$	92.2
Less: current portion		**(31.6)**		(31.6)
Long-term portion	**$**	**65.0**	$	60.6

The total undiscounted amount of the estimated cash flows required to settle the obligations at December 31, 2011 was $100.7 million (December 31, 2010 - $100.4 million; January 1, 2010 - $102.8 million) with payments spread over 15 years. Due to the general long-term nature of the liability, the most significant area of uncertainty in estimating the provision is the future costs that will be incurred. The estimated cash flows have been adjusted for inflation and discounted using risk-free rates ranging from 1.0% to 2.3% at December 31, 2011.

15. Asset Retirement Obligations

The following table provides a reconciliation of the asset retirement obligations as at December 31, 2011 and 2010:

(millions of Canadian dollars)		**2011**		2010
Asset retirement obligations at beginning of year	**$**	**6.3**	$	5.7
Accretion expense		**0.6**		0.4
Paid during the year		**(0.1)**		-
Change in estimate		**(0.2)**		0.2
Asset retirement obligations at end of year	**$**	**6.6**	$	6.3

Canfor's asset retirement obligations include $3.1 million in relation to landfill closure costs at CPLP. These obligations represent estimated undiscounted future payments of $7.2 million to remediate the landfills at the end of their useful lives. The payments are expected to occur at periods ranging from 7 to 40 years and have been discounted at risk-free rates ranging from 1.5% to 2.5%.

Canfor has certain assets that have indeterminable retirement dates and, therefore, there is an indeterminate settlement date for the related asset retirement obligations. As a result, no asset retirement obligations are recorded for these assets. These assets include wastewater and effluent ponds that will have to be drained once the related operating facility is closed and storage sites for which removal of chemicals, fuels and other related materials will be required once the related operating facility is closed. When the retirement dates of these assets become determinable and an estimate of fair value can be made, an asset retirement obligation will be recorded.

It is possible that changes in future conditions could require a material change in the recognized amount of the asset retirement obligations.

The asset retirement obligations balance is included in other long-term liabilities on the balance sheet.

16. Restructuring, Mill Closure and Severance Costs

Restructuring, mill closure and severance costs represent costs associated with the indefinite or permanent closures of facilities and staff reductions. The expense for the year ended December 31, 2011 amounted to $38.3 million (2010 - $32.4 million). Of the 2011 expense, $11.9 million related to severance and other costs for the closure of the Rustad sawmill, and $10.6 million related to severance and other costs for the closure of the Tackama mill, both of which were announced in the fourth quarter of 2011 and took effect in January 2012. Of the 2010 expense, $17.3 million related to severance and other costs for the closure of the Clear Lake sawmill, which was announced in the third quarter of 2010 and took effect in January 2011. The significant majority of the remaining 2011 and 2010 expense related to: the ongoing costs of the Company's indefinitely idled Radium sawmill and PolarBoard panel operation; costs of the Rustad sawmill and Tackama panel operation prior to closure; and the costs of the Company's Vavenby sawmill prior to the restart in the third quarter of 2011.

The following table provides a breakdown of the restructuring, mill closure and severance costs by business segment:

(millions of Canadian dollars)	**2011**	2010
Lumber	**$ 21.2**	$ 29.1
Unallocated and other	**17.1**	3.3
	$ 38.3	$ 32.4

The following table provides a reconciliation of the restructuring, mill closure and severance liability for the years ended December 31, 2011 and 2010:

(millions of Canadian dollars)	**2011**	2010
Accrued liability at beginning of year	**$ 18.4**	$ 19.1
Costs accrued in the year [1]	**21.8**	26.5
Paid during the year	**(11.9)**	(27.2)
Accrued liability at end of year	**$ 28.3**	$ 18.4

[1] Excluding non-cash expenses and recoveries related to provisions for capital asset and inventory write-downs resulting from indefinite and permanent mill closures.

17. Share Capital

Authorized

10,000,000 preferred shares, with a par value of $25 each
1,000,000,000 common shares without par value

Issued and Fully Paid

(millions of Canadian dollars, except number of shares)	**2011**		2010	
	Number of Shares	**Amount**	Number of Shares	Amount
Common shares, beginning of year	**142,669,347**	**$ 1,125.4**	142,589,297	$ 1,124.7
Stock options exercised (Note 18)	**52,417**	**0.5**	80,050	0.7
Common shares, end of year	**142,721,764**	**$ 1,125.9**	142,669,347	$ 1,125.4

The holders of common shares are entitled to vote at all meetings of shareholders of the Company, except meetings at which only holders of preferred shares would be entitled to vote. The common shareholders are entitled to receive dividends as and when declared on the common shares. The holders of preferred shares are not generally entitled to receive notice of, or to attend or vote at, general meetings of shareholders of the Company. Preferred shareholders are entitled to preference over the common shares with respect to payment of dividends and upon any distribution of assets in the event of liquidation, dissolution and winding-up of the Company.

As at December 31, 2011, 38,667 common shares are reserved for issue under the stock options disclosed in note 18.

18. Share-Based Compensation

Canfor has two share-based compensation plans, which are described below:

Deferred share unit plans

On January 1, 2002, the Company implemented a Deferred Share Unit Plan for non-employee directors of the Company. A Deferred Share Unit ("DSU") is a right granted to a non-employee director to receive one common share of the Company, purchased on the open market, or the cash equivalent at their option, on a deferred payment basis. The maximum number of DSUs outstanding under the plan is 1,000,000. Effective July 27, 2011, the Board determined to cease the issuance of DSUs for non-employee directors.

The value of the DSUs, when redeemed, is equal to the market value of the shares on the redemption date, including the value of dividends paid on the Company's common shares, if any, as if they had been reinvested in additional DSUs on each payment date. The DSUs may only be redeemed upon a director's retirement from the Company, its subsidiaries or any affiliated entity. The total credit recorded in relation to the DSUs for 2011 was $0.1 million due to the revaluation of existing units (2010 – expense of $0.5 million). The value of outstanding DSUs at December 31, 2011 was $1.2 million (December 31, 2010 - $1.3 million; January 1, 2010 - $0.8 million).

In addition, in May 2007, the Company implemented a Deferred Share Unit Plan for the Company's former CEO (the "CEO Plan"). Pursuant to the terms of the plan, the former CEO received his annual salary in DSUs. The value of the DSUs when redeemed equalled the market value of the shares on the redemption date. The DSUs under the CEO Plan were redeemed during 2011 when the former CEO ceased employment with the Company. The CEO Plan ceased to be in use at that date. The total credit recorded in relation to the CEO Plan for 2011 was $0.3 million (2010 - $2.0 million expense).

Stock option performance plan

The Company has a stock option performance plan pursuant to which stock options were granted to selected senior officers. No new stock options were granted in 2010 or 2011. The stock option performance plan provided for the issuance of up to a maximum of 5.8 million common shares at an exercise price equal to the market price of the Company's common shares on the date of grant. However, there are various criteria that limit the amount of options exercisable during each option year within the option period. The options are for a term of 10 years and vest equally over three years. All options have fully vested. A summary of the status of the plan as of December 31, 2011 and 2010, and changes during the years ending on those dates, is presented below:

	2011			2010		
	Number of Shares		**Weighted Average Exercise Price**	Number of Shares		Weighted Average Exercise Price
Outstanding at beginning of year	**97,418**	**$**	**9.73**	200,468	$	9.34
Exercised	**(52,417)**	**$**	**9.72**	(80,050)	$	8.73
Cancelled	**(6,334)**	**$**	**9.09**	(23,000)	$	9.80
Outstanding at end of year	**38,667**	**$**	**9.85**	97,418	$	9.73

The options outstanding and exercisable at December 31, 2011 have an exercise price in the range of $9.80 to $10.10 (2010 - $8.30 to $10.10) and a weighted average remaining life of 0.12 years (2010 - 1.04 years). Subsequent to year end, 35,667 of the options outstanding at December 31, 2011 were exercised or cancelled with the remaining expected to be exercised or cancelled before the end of the second quarter of 2012.

19. Finance Expense, Net

(millions of Canadian dollars)		**2011**		2010
Finance expense	**$**	**(24.4)**	$	(28.9)
Less: Interest income		**1.9**		2.1
Finance expense, net	**$**	**(22.5)**	$	(26.8)

Finance expense, net is comprised of:

(millions of Canadian dollars)		**2011**		2010
Short-term finance expense, net	**$**	**(7.2)**	$	(5.8)
Long-term finance expense, net		**(15.3)**		(21.0)
Finance expense, net	**$**	**(22.5)**	$	(26.8)

For the year ended December 31, 2011, short-term finance expense, net is comprised of stand-by fees for operating loans and letter of credit charges of $7.2 million (2010 - $6.5 million) and accretion expense related to the Company's asset retirement and deferred reforestation obligations of $1.8 million (2010 - $1.2 million), offset by interest income on cash and cash equivalents of $1.8 million (2010 - $1.9 million). Long-term finance expense, net relates substantially to interest expense on long-term debt.

20. Other Income, Net

(millions of Canadian dollars)		**2011**		2010
Foreign exchange gain (loss) on translation of working capital	**$**	**2.0**	$	(4.9)
Increase in fair value of asset-backed commercial paper (Note 9)		**0.2**		6.3
Gain on sale of operating assets of Howe Sound Pulp and Paper Limited Partnership		**-**		5.5
Gain on fair value adjustment for royalty receivable		**2.2**		-
Other, net		**1.5**		1.2
Total other income, net	**$**	**5.9**	$	8.1

In October 2010, Howe Sound Pulp and Paper Limited Partnership (now called 6382 Pulp and Paper Limited Partnership), a kraft pulp and newsprint mill operation jointly owned by Canfor and Oji Paper Co. Ltd., completed the sale of all of its operating assets. As a result of the sale, Canfor recorded a gain of $5.5 million in 2010. During 2011, the Company recognized a $2.2 million positive fair value adjustment related to a royalty agreement associated with the sale.

21. Income Taxes

The components of income tax recovery (expense) are as follows:

(millions of Canadian dollars)		**2011**		2010
Current	**$**	**(1.7)**	$	2.2
Deferred		**22.2**		(11.7)
Income tax recovery (expense)	**$**	**20.5**	$	(9.5)

The reconciliation of income taxes calculated at the statutory rate to the actual income tax provision is as follows:

(millions of Canadian dollars)		**2011**		2010
Income tax recovery (expense) at statutory rate 2011 – 26.5% (2010 – 28.5%)	**$**	**2.6**	$	(52.1)
Non-taxable income related to non-controlling interests in limited partnerships		**17.9**		26.1
Entities with different income tax rates and other tax adjustments		**1.0**		1.4
Tax recovery (expense) at rates other than statutory rate		**(0.9)**		3.4
Permanent difference from capital gains and losses and other non-deductible items		**(0.1)**		11.7
Income tax recovery (expense)	**$**	**20.5**	$	(9.5)

The tax effects of the significant components of temporary differences that give rise to future income tax assets and liabilities are as follows:

(millions of Canadian dollars)		**As at December 31, 2011**		As at December 31, 2010		As at January 1, 2010
Deferred income tax assets						
Accruals not currently deductible						
Current	**$**	**16.2**	$	16.3	$	12.4
Non-current		**18.9**		18.2		20.6
Derivative financial instruments						
Current		**0.1**		0.7		0.7
Non-current		**-**		-		0.4
Loss carryforwards		**66.4**		30.0		34.7
Retirement benefit obligations		**62.6**		57.7		50.3
Other		**1.5**		2.0		8.4
	$	**165.7**	$	124.9	$	127.5
Deferred income tax liabilities						
Depreciable capital assets	**$**	**(235.5)**	$	(225.9)	$	(230.9)
Other intangible assets		**(4.4)**		(5.5)		(6.8)
Unrealized foreign exchange gains on debt						
Current		**(2.0)**		(4.2)		(1.7)
Non-current		**(3.6)**		(6.1)		(8.2)
Other		**(5.4)**		(5.0)		(3.6)
	$	**(250.9)**	$	(246.7)	$	(251.2)
Total deferred income taxes, net	**$**	**(85.2)**	$	(121.8)	$	(123.7)
Less: Entities in a net deferred tax asset position		**18.1**		9.4		7.3
Deferred income taxes liability, net	**$**	**(103.3)**	$	(131.2)	$	(131.0)

Deferred income tax assets are recognized for tax loss carry-forwards to the extent that the realization of the related tax benefit through future taxable profits is probable. This assumption is based on management's best estimate of future circumstances and events. If these estimates and assumptions changed in the future, the value of the deferred income tax assets could be reduced, resulting in an income tax expense.

In addition to the amounts recorded to net income, a tax recovery of $14.2 million was recorded to other comprehensive income for the year ended December 31, 2011 (December 31, 2010 – recovery of $13.6 million) in relation to actuarial losses on defined benefit employee compensation plans.

22. Earnings Per Share

Basic net income (loss) per share is calculated by dividing the net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is calculated by dividing the net income (loss) available to common shareholders by the weighted average number of common shares during the period using the treasury stock method. Under this method, proceeds from the potential exercise of stock options are assumed to be used to purchase the Company's common shares. When there is a net loss, the exercise of stock options would result in a calculated diluted net loss per share that is anti-dilutive.

	Year ended December 31, **2011**	2010
Weighted average number of common shares	**142,698,624**	142,613,920
Incremental shares from potential exercise of options[1]	**4,023**	573
Diluted number of common shares [1]	**142,698,624**	142,614,493

[1] Where the addition of share options to the total shares outstanding has an anti-dilutive impact on the diluted net income (loss) per share calculation, those share options have not been included in the total common shares outstanding for purposes of the calculation of diluted net income (loss) per share.

23. Net Change in Non-Cash Working Capital

(millions of Canadian dollars)		**2011**		2010
Accounts receivable	**$**	**36.6**	$	(3.7)
Inventories		**(22.6)**		(16.8)
Prepaid expenses		**6.1**		(7.1)
Accounts payable, accrued liabilities and current portion of deferred reforestation obligations		**(25.7)**		32.0
Net (decrease) increase in working capital	**$**	**(5.6)**	$	4.4

24. Related Party Transactions

Canfor undertakes transactions with various related entities. These transactions are in the normal course of business and are generally on the same terms as those accorded to unrelated third parties, except where noted otherwise.

Associates

Howe Sound Pulp and Paper Limited Partnership ("HSLP")

Canfor had certain transactions with HSLP, of which Canfor was a joint owner, until HSLP sold its operating assets in October 2010 (note 20). Canfor, through CPLP, marketed the pulp production of HSLP for which it received commissions under the terms of its agency sales agreement. This commission amounted to $1.8 million for the year ended December 31, 2010. Canfor also provided management, fibre supply and other services to HSLP at cost during 2010.

Lakeland Mills Ltd.

Canfor purchases chips and lumber from Lakeland Mills Ltd., in which Canfor has a 33.3% interest. In 2011, Canfor purchased $11.5 million in chips (2010 - $6.1 million in chips and $1.4 million in lumber). The balance owed to Lakeland Mills Ltd. outstanding at December 31, 2011 was $0.9 million (December 31, 2010 - $0.4 million; January 1, 2010 - $0.4 million).

Key Management Personnel

Key management includes members of the Board of Directors and the Senior Executive management team. The compensation expense for key management for services is as follows:

(millions of Canadian dollars)		**2011**		2010
Short-term benefits	**$**	**4.0**	$	3.9
Post-employment benefits		**0.3**		0.3
Restructuring costs		**1.0**		-
Other long-term benefits		**0.3**		0.8
Share-based payments		**(0.4)**		2.5
	$	**5.2**	$	7.5

Short-term benefits for most members of the Board of Directors include an annual retainer as well as attendance fees. As described in note 18, members of the Board and the former CEO previously received deferred share units, which are included within share-based payments above. Share-based payments also reflect share price revaluations on the deferred share units.

Other Related Parties

Post-employment benefit plans

During the year, Canfor made contributions to certain post-employment benefit plans for the benefit of Canfor employees. Note 13 Employee Future Benefits contains further details.

As at December 31, 2011, the Company had entered into an agreement with Jim Pattison Lease to provide lease management services in 2012. Jim Pattison Lease is a related party to the Company. There were no material transactions with the party during the year and no material amounts were outstanding at December 31, 2011.

25. Joint Venture

Canfor and Louisiana-Pacific Canada Ltd. jointly own Peace Valley OSB ("Canfor-LP OSB"), a limited partnership which owns and operates an oriented strand board ("OSB") plant in Fort St. John, BC. Canfor has agreed to supply 330,000 cubic metres of timber annually to the joint venture from its existing timber tenure in the area where the mill is located. During 2011, Canfor paid net capital contributions of $6.0 million to Canfor-LP OSB (2010 – net distributions of $5.3 million).

The following balances, which represent Canfor's 50% ownership interest in Canfor-LP OSB, have been proportionately consolidated in Canfor's consolidated financial statements:

(millions of Canadian dollars)	**As at December 31, 2011**	As at December 31, 2010	As at January 1, 2010
Balance sheets			
Current assets	**$ 5.7**	$ 5.8	$ 5.2
Non-current assets	**79.4**	89.4	99.4
Current liabilities	**(3.5)**	(3.2)	(2.9)
Net assets	**$ 81.6**	$ 92.0	$ 101.7

(millions of Canadian dollars)	**2011**	2010
Statements of income (loss)		
Sales	**$ 44.8**	$ 55.6
Costs and expenses	**(61.1)**	(60.1)
Net loss	**$ (16.3)**	$ (4.5)

26. Segment Information

Canfor has two reportable segments, as described below, which offer different products and are managed separately because they require different production processes and marketing strategies. The following summary describes the operations of each of the Company's reportable segments:

- *Lumber* - Includes logging operations, and manufacture and sale of various grades, widths and lengths of lumber products.
- *Pulp and paper* – Includes purchase of residual fibre, and production and sale of pulp and paper products, including northern bleached softwood kraft ("NBSK") and bleached chemi-thermo mechanical pulp ("BCTMP"). This segment includes 100% of CPLP and the Taylor pulp mill.

Sales between segments are accounted for at prices that approximate fair value. These include sales of residual fibre from the lumber segment to the pulp and paper segment for use in the pulp production process.

The Company's panels business does not meet the criteria to be reported fully as a separate segment. Sales for panels operations for the year ended December 31, 2011 were $46.8 million (2010 - $55.6 million).

Information regarding the operations of each reportable segment is included in the table below. The accounting policies of the reportable segments are the same as described in note 3.

The Company's interest-bearing liabilities are not considered to be segment liabilities but rather are managed centrally by the treasury function. Other liabilities are not split by segment for the purposes of allocating resources and assessing performance.

(millions of Canadian dollars)		Lumber	Pulp & Paper	Unallocated & Other	Elimination Adjustment		Consolidated
Year ended December 31, 2011							
Sales to external customers	**$**	**1,317.1**	**1,057.5**	**46.8**	**-**	**$**	**2,421.4**
Sales to other segments	**$**	**127.1**	**-**	**-**	**(127.1)**	**$**	**-**
Operating income (loss)	**$**	**(80.7)**	**150.1**	**(61.0)**	**-**	**$**	**8.4**
Amortization	**$**	**83.9**	**68.0**	**17.4**	**-**	**$**	**169.3**
Capital expenditures[1]	**$**	**155.3**	**156.2**	**0.8**	**-**	**$**	**312.3**
Identifiable assets	**$**	**1,413.8**	**812.3**	**175.5**	**-**	**$**	**2,401.6**
Year ended December 31, 2010							
Sales to external customers	$	1,255.2	1,119.6	55.6	-	$	2,430.4
Sales to other segments	$	129.8	-	-	(129.8)	$	-
Operating income (loss)	$	23.9	192.7	(29.9)	-	$	186.7
Amortization	$	82.8	67.3	17.6	-	$	167.7
Capital expenditures[1]	$	88.1	53.9	0.2	-	$	142.2
Identifiable assets	$	1,343.4	878.9	371.8	-	$	2,594.1

[1] Capital expenditures represent cash paid for capital assets during the period. Pulp & Paper includes capital expenditures by CPLP that are financed by the government-funded Green Transformation Program.

Geographic information

Canfor operates manufacturing facilities in Canada and the U.S. Canfor's products are marketed worldwide, with sales made to companies in a number of different countries. In presenting information on the basis of geographical location, revenue is based on the geographical location of customers and assets are based on the geographical location of the assets.

(millions of Canadian dollars)	**2011**	2010
Sales by location of customer		
Canada	**$ 291.4**	$ 300.1
Asia	**965.5**	766.8
United States	**956.4**	1,114.8
Europe	**166.1**	201.0
Other	**42.0**	47.7
	$ 2,421.4	$ 2,430.4

(millions of Canadian dollars)	**2011**	2010
Capital assets and goodwill by location		
Canada	**$ 1,590.9**	$ 1,523.7
United States	**149.4**	141.6
Asia and Other	**0.2**	0.1
	$ 1,740.5	$ 1,665.4

27. Contingencies

On January 18, 2011, the U.S. triggered the arbitration provision of the 2006 Softwood Lumber Agreement ("SLA") by delivering a Request for Arbitration. The U.S. claims that the province of British Columbia ("BC") has not properly applied the timber pricing system grandparented in the SLA. The U.S. also claims that subsequent to 2006, BC made additional changes to the timber pricing system which had the effect of reducing timber prices. The claim focuses on substantial increases in Grade 4 (non sawlog or low grade) volumes commencing in 2007. It is alleged that timber was scaled and graded as Grade 4 that did not meet the criteria for that grade, and was accordingly priced too low.

As the arbitration is a state-to-state international dispute under the SLA, Canada is preparing a defence to the claim with the assistance of the BC provincial government and the BC lumber industry. In August 2011, the U.S. filed a detailed statement of claim with the arbitration panel, which Canada responded to in November 2011. The U.S. subsequently filed a reply, to which Canada filed a response in early February 2012. A hearing before the arbitration panel is currently expected before the end of the first quarter of 2012. It is not possible at this time to predict the outcome or the value of any final claim, and accordingly no provision has been recorded by the Company.

Canfor has other contingent liabilities in respect of legal claims arising in the ordinary course of business. It is not anticipated that any material liabilities will arise from such contingent liabilities.

28. Commitments

At the end of the year, Canfor had contractual commitments for the acquisition of property, plant and equipment for $21.7 million (December 31, 2010 - $32.9 million; January 1, 2010 - $30.2 million). These commitments are expected to be settled over the following year.

Canfor has committed to operating leases for property, plant and equipment. As at December 31, 2011 and 2010 and January 1, 2010, the future minimum lease payments under these operating leases were as follows:

(millions of Canadian dollars)		**As at December 31, 2011**		As at December 31, 2010		As at January 1, 2010
Within one year	**$**	**9.4**	$	12.8	$	15.1
Between one and five years		**12.5**		19.8		22.5
After five years		**0.2**		1.1		0.7
Total	**$**	**22.1**	$	33.7	$	38.3

During the year ended December 31, 2011, $16.9 million (2010 - $18.7 million) was recognized as an expense in the income statement in respect of operating leases.

In addition to the above commitments, the Company has several operational agreements with minimum usage requirements. No issues were identified with meeting these obligations.

Acquisition of Tembec assets

In November 2011, the Company signed an agreement to acquire Tembec Industries Ltd.'s ("Tembec") southern British Columbia Interior wood products assets, for a purchase price including normal working capital of $60 million. The purchase will include Tembec's Elko and Canal Flats sawmills, approximately 1.1 million cubic metres of combined Crown, private land and contract allowable cut, and a long-term agreement to provide residual fibre supply for Tembec's Skookumchuck pulp mill. The transaction is subject to various customary closing conditions including regulatory approval and is currently scheduled to close at the end of the first quarter of 2012.

29. Financial Risk and Capital Management

Financial Risk Management

Canfor is exposed to a number of risks as a result of holding financial instruments. These risks include credit risk, liquidity risk and market risk.

Canfor's Risk Management Committee manages risk in accordance with a Board approved Price Risk Management Controls Policy. This policy provides the framework for risk management related to commodity price, foreign exchange, interest rate and counterparty credit risk of Canfor.

Credit risk:

Credit risk is the risk of financial loss to Canfor if a customer, bank or third party to a derivative instrument fails to meet its contractual obligations.

Financial instruments that are subject to credit risk include cash and cash equivalents, accounts receivable, and long-term investments and other. Cash and cash equivalents includes cash held through major Canadian and international financial institutions as well as temporary investments with an original maturity date of three months or less. The cash and cash equivalents balance at December 31, 2011 is $28.9 million (December 31, 2010 - $260.3 million; January 1, 2010 - $133.4 million).

Canfor utilizes credit insurance to mitigate the risk associated with some of its trade receivables. As at December 31, 2011, approximately 60% of the outstanding trade receivables are covered by credit insurance (December 31, 2010 – 65%; January 1, 2010 – 65%). Canfor's trade receivable balance at December 31, 2011 is $105.1 million, net of an allowance for doubtful accounts of $2.8 million (December 31, 2010 - $146.9 million and $2.5 million, respectively; January 1, 2010 - $137.2 million and $2.1 million, respectively). At December 31, 2011, approximately 99% of the trade accounts receivable balance was within Canfor's established credit terms (December 31, 2010 – 99%; January 1, 2010 – 97%).

Liquidity risk:

Liquidity risk is the risk that Canfor will be unable to meet its financial obligations on a current basis. Canfor manages liquidity risk through regular cash-flow forecasting in conjunction with an adequate committed operating loan facility.

At December 31, 2011, Canfor had no amounts drawn on its operating lines (December 31, 2010 - nil; January 1, 2010 - $0.6 million), accounts payable and accrued liabilities of $290.5 million (December 31, 2010 - $292.9 million; January 1, 2010 - $211.4 million) and current debt obligations of $50.9 million (December 31, 2010 - $82.5 million; January 1, 2010 - $34.0 million), all of which fall due for payment within one year of the balance sheet date.

Market risk:

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in interest rates, foreign currency and commodity prices.

(i) Interest rate risk:

Canfor is exposed to interest rate risk through its current financial assets and financial obligations bearing variable interest rates. Canfor's cash and cash equivalents include term deposits with original maturity dates of three months or less.

Changes in the market interest rates do not have a significant impact on Canfor's results of operations due to the short-term nature of the respective financial assets and obligations and because all long-term debt is based on fixed rates of interest.

Canfor currently does not use derivative instruments to reduce its exposure to interest rate risk.

(ii) Currency risk:

Canfor is exposed to foreign exchange risk primarily related to the US dollar, as Canfor's products are sold principally in US dollars and all long-term debt is denominated in US dollars. In addition, Canfor holds financial assets and liabilities primarily related to New South, based in South Carolina, in US dollars.

An increase (decrease) in the value of the Canadian dollar by US$0.01 would result in a pre-tax: (i) loss (gain) of approximately $0.6 million in relation to working capital balances denominated in US dollars at year end (including cash, accounts receivable and accounts payable); (ii) loss (gain) of approximately $0.1 million in relation to the ABCP denominated in US dollars at year end; and a (iii) gain (loss) of approximately $2.0 million in relation to long-term debt denominated in US dollars at year end.

A portion of the currency risk associated with US dollar denominated sales is naturally offset by US dollar denominated expenses and the US dollar denominated debt. A portion of the remaining exposure is covered by foreign exchange collar contracts that effectively limit the minimum and maximum Canadian dollar recovery related to the sale of those US dollars.

Canfor had the following foreign exchange derivatives at December 31, 2011 and 2010 and January 1, 2010:

	As at December 31, 2011		As at December 31, 2010		As at January 1, 2010	
	Notional Amount	**Exchange Rates**	Notional Amount	Exchange Rates	Notional Amount	Exchange Rates
US Dollar Collars	(millions of US dollars)	(protection/topside, per dollar)	(millions of US dollars)	(protection/topside, per dollar)	(millions of US dollars)	(protection/topside, per dollar)
0-12 months US Dollar Collars	**$ 256.8**	**$ 0.9500/$ 1.1461**	$ -	$ -	$ 12.0	$ 1.0500/$ 1.2200
US Dollar Forwards	(millions of US dollars)	(range of rates, per dollar)	(millions of US dollars)	(range of rates, per dollar)	(millions of US dollars)	(range of rates, per dollar)
0-12 months US Dollar Forward Contracts	**$ 70.9**	**$0.9984 – $1.0470**	$ 68.4	$ 0.9940 - $1.0678	$ 86.0	$ 1.0302 - $1.0723

(iii) Energy price risk:

Canfor is exposed to energy price risk relating to purchases of natural gas and diesel oil for use in its operations.

The exposure is hedged up to 100% through the use of floating to fixed swap contracts or option contracts with maturity dates up to a maximum of three years. In the case of diesel, Canfor uses heating oil and brent contracts to hedge its exposure.

As at December 31, 2011, the Company had 5.3 million gallons of heating oil collars, which primarily will be settled in 2012, with weighted average protection of $2.55 per gallon and topside of $2.95 per gallon, and 65.2 thousand barrels of brent collars, which primarily will be settled in 2012, with weighted average protection of $84.00 per barrel and topside of $109.00 per barrel.

As at December 31, 2010, the Company had 1.1 million gigajoules of current natural gas floating to fixed swap contracts with an average rate of $8.04 per gigajoule, and 2.6 million gallons of current diesel floating to fixed swap contracts with an average rate of $2.22 per gallon.

As at January 1, 2010, the Company had 3.2 million gigajoules of natural gas floating to fixed swap contracts, which were primarily current, with an average rate of $7.53 per gigajoule, and 2.0 million gallons of diesel floating to fixed swap contracts, which were primarily current, with an average rate of $2.49 per gallon.

(iv) Commodity price risk:

Canfor is exposed to commodity price risk related to sale of lumber, pulp, paper, and oriented strand board. From time to time, Canfor enters into futures contracts on the Chicago Mercantile Exchange for lumber and forward contracts direct with customers for pulp. Under the Price Risk Management Controls Policy, up to 15% of lumber sales and 5% of pulp sales may be sold in this way.

	As at December 31, 2011		As at December 31, 2010		As at January 1, 2010	
	Notional Amount	**Average Rate**	Notional Amount	Average Rate	Notional Amount	Average Rate
Lumber	(MMfbm)	(US dollars per Mfbm)	(MMfbm)	(US dollars per Mfbm)	(MMfbm)	(US dollars per Mfbm)
Future Sales Contracts						
0 – 12 Months	**59.7**	**$ 286.10**	68.4	$ 294.71	55.8	$ 242.3

An increase (decrease) in the futures market price of lumber of US$10 per Mfbm would result in a pre-tax gain (loss) of approximately $0.6 million in relation to the lumber futures held at year end.

Capital management

Canfor's objectives when managing capital are to maintain a strong balance sheet and a globally competitive cost structure that ensure adequate liquidity to maintain and develop the business throughout the commodity price cycle.

Canfor's capital is comprised of net debt and shareholders' equity:

(millions of Canadian dollars)	**As at December 31, 2011**	As at December 31, 2010	As at January 1, 2010
Total debt (including operating loans)	**$ 239.0**	$ 318.1	$ 367.9
Less: Cash and cash equivalents	**(28.9)**	(260.3)	(133.4)
Net debt	**$ 210.1**	$ 57.8	$ 234.5
Total equity	**1,360.1**	1,470.0	1,449.0
	$ 1,570.2	$ 1,527.8	$ 1,683.5

The Company has certain financial covenants in its debt obligations that stipulate maximum net debt to total capitalization ratios and minimum net worth amounts based on total shareholders' equity. The net debt to total capitalization is calculated by dividing total debt less cash and cash equivalents, by shareholders' equity plus total debt less cash and cash equivalents. Debt obligations are held by various entities within the Canfor group and the individual debt agreements specify the entities within the group that are to be included in the covenant calculations.

Separately, CPLP has leverage and interest coverage ratios calculated by reference to operating earnings before interest, taxes and amortization.

Canfor's strategy is to ensure it remains in compliance with all of its existing debt covenants, so as to ensure continuous access to capital, and management reviews results and forecasts to monitor Canfor's compliance. Canfor was in compliance with all its debt covenants for the years ended December 31, 2011 and 2010.

There were no changes in the Company's approach to capital management in the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

30. Financial Instruments

Classification and measurement of financial instruments

Canfor's cash and cash equivalents, accounts receivable, other deposits, loans and advances, operating loans, accounts payable and accrued liabilities, and long-term debt are measured at amortized cost subsequent to initial recognition.

ABCP and derivative instruments are measured at fair value. IFRS 7, *Financial Instruments: Disclosures,* requires classification of these items within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 – Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly;

Level 3 – Inputs that are not based on observable market data.

The following table summarizes Canfor's financial instruments at December 31, 2011 and 2010 and January 1, 2010, and shows the level within the fair value hierarchy in which they have been classified (for financial instruments measured at fair value):

(millions of Canadian dollars)	Fair Value Hierarchy Level	**As at December 31, 2011**	As at December 31, 2010	As at January 1, 2010
Financial assets				
Held for trading				
ABCP	Level 2	**$ 11.8**	$ 40.9	$ 41.1
Derivative financial instruments	Level 2	**1.6**	2.6	1.9
Loans and receivables				
Cash and cash equivalents	n/a	**28.9**	260.3	133.4
Accounts receivable (excluding derivatives)	n/a	**169.2**	198.5	177.2
Other deposits, loans and advances	n/a	**15.1**	11.9	3.1
Available for sale				
Investments in other entities	n/a	**24.3**	26.5	27.3
		$ 250.9	$ 540.7	$ 384.0
Financial liabilities				
Held for trading				
Derivative financial instruments	Level 2	**$ 1.8**	$ 6.7	$ 7.7
Other liabilities				
Operating loans	n/a	**-**	-	0.6
Accounts payable and accrued liabilities (excluding derivatives)	n/a	**288.7**	286.2	206.0
Long-term debt	n/a	**239.0**	318.1	367.3
		$ 529.5	$ 611.0	$ 581.6

Derivative financial instruments

The Company uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, lumber prices and energy costs. At December 31, 2011, the fair value of derivative financial instruments was a net liability of $0.2 million (December 31, 2010 – net liability of $4.1 million; January 1, 2010 – net liability of $5.8 million). The fair value of these financial instruments was determined based on prevailing market rates for instruments with similar characteristics.

The following table summarizes the gain (loss) on derivative financial instruments for the years ended December 31, 2011 and 2010:

(millions of Canadian dollars)		**2011**		2010
Foreign exchange collars and forward contracts	**$**	**(2.7)**	$	4.0
Natural gas swaps		**(0.2)**		(5.2)
Diesel options and swaps		**0.8**		0.8
Lumber futures		**5.6**		0.5
Gain on derivative financial instruments	**$**	**3.5**	$	0.1

The following table summarizes the fair market value of the derivative financial instruments included in the balance sheets at December 31, 2011 and 2010 and January 1, 2010:

(millions of Canadian dollars)		**As at December 31, 2011**		As at December 31, 2010		As at January 1, 2010
Foreign exchange collars and forward contracts	**$**	**(0.4)**	$	1.6	$	1.6
Natural gas swaps		**-**		(4.7)		(6.8)
Diesel options and swaps		**(0.2)**		1.0		(0.9)
Lumber futures		**0.4**		(2.0)		0.3
Total asset (liability)		**(0.2)**		(4.1)		(5.8)
Less: current portion		**(0.2)**		(4.1)		(3.5)
Long-term portion	**$**	**-**	$	-	$	(2.3)

31. Transition to International Financial Reporting Standards ("IFRS")

These financial statements are the first annual consolidated financial statements prepared by the Company under IFRS. The Company's transition date to IFRS was January 1, 2010 and accordingly the Company has prepared its opening IFRS balance sheet as at that date. In preparing its opening IFRS balance sheet and comparative information for 2010, the Company has adjusted amounts previously reported in financial statements prepared in accordance with previous Canadian GAAP ("previous GAAP").

The differences identified are detailed in the following sections, which include a reconciliation of the Company's closing balance sheet at the end of 2009 under previous GAAP with its provisional opening balance sheet under IFRS on January 1, 2010. Reconciliations of total comprehensive income and equity from previous GAAP to IFRS for the year ended December 31, 2010 then follow.

The accounting changes resulting from the transition to IFRS do not impact the Company's compliance with any of its financial covenants with respect to its debt obligations.

31.1 Optional exemptions from full retrospective application followed by the Company

The Company has applied IFRS 1, *First-time Adoption of IFRS,* in preparing these consolidated financial statements. Canfor has elected to apply the following optional exemptions from full retrospective application under IFRS:

(a) Business combinations exemption

Canfor has applied the business combinations exemption and accordingly has not restated business combinations that took place prior to the January 1, 2010 transition date.

(b) Employee benefits exemption

Canfor has elected to recognize all cumulative actuarial gains and losses on its various defined benefit pension and post-retirement non-pension plans as at January 1, 2010, in equity.

(c) Accumulated foreign currency translation differences exemption

Canfor has elected to set its cumulative foreign exchange translation amount to zero at January 1, 2010. Under previous GAAP, this amount was included in Accumulated Other Comprehensive Income (Loss). This exemption has been applied to all foreign subsidiaries with functional currency other than Canadian dollars.

(d) Share-based payments exemption

The Company has elected to apply the share-based payment exemption. IFRS 2, *Share-based Payment,* has not been applied to the options granted under the stock option performance plan as these were all fully vested as at January 1, 2010.

In addition to these optional exemptions, Canfor has also ensured that all estimates at January 1, 2010 are consistent with estimates made at the same date under previous GAAP, as required by IFRS 1.

31.2 Presentation of non-controlling interests

Under previous GAAP, the Company adopted, as of January 1, 2010, three new inter-related accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA"). These were Handbook Sections 1582, *Business Combinations*; 1601, *Consolidated Financial Statements*; and 1602, *Non-controlling Interests*.

The adoption of Section 1602 resulted in the reclassification of non-controlling interests on Canfor's balance sheet from long-term liabilities into equity. As this adjustment was made under previous GAAP as of January 1, 2010, it is not included in the opening balance sheet reconciliation below, but should be taken into account when comparing the December 31, 2009 financial statements to the opening IFRS balance sheet as at January 1, 2010.

31.3 Reconciliations between IFRS and previous GAAP

This section consists of a number of reconciliations between IFRS and previous GAAP which quantify the effect of the Company's transition to IFRS. The reconciliations include balance sheets as at January 1, 2010 and December 31, 2010. A reconciliation of total comprehensive income under previous GAAP to IFRS for the year ended December 31, 2010, and an explanation of the material adjustments to the statement of cash flows, are also provided.

(i) Reconciliation of opening balance sheet as at January 1, 2010

As at January 1, 2010 (millions of Canadian dollars)	Previous GAAP	Note (section iv)	Effect of transition to IFRS	**IFRS**
ASSETS				
Current assets				
Cash and cash equivalents	$ 133.4		$ -	**$ 133.4**
Accounts receivable - Trade	137.2		-	**137.2**
- Other	41.9		-	**41.9**
Income taxes recoverable	45.5		-	**45.5**
Deferred income taxes, net	11.4	a	(11.4)	**-**
Inventories	311.3	c	(0.8)	**310.5**
Prepaid expenses	36.4	b	(15.4)	**21.0**
Total current assets	717.1		(27.6)	**689.5**
Property, plant and equipment		b	20.8	
		c	(9.4)	
		d	(610.3)	
	1,676.6		(598.9)	**1,077.7**
Timber licenses		c	(46.6)	
		d	610.3	
	-		563.7	**563.7**
Goodwill and other intangible assets		e	(114.8)	
		d	16.8	
	190.4		(98.0)	**92.4**
Long-term investments and other		b	(5.4)	
		d	(16.8)	
		e	4.2	
	93.7		(18.0)	**75.7**
Deferred income taxes, net	-	a	7.3	**7.3**
	$ 2,677.8		$ (171.5)	**$ 2,506.3**

As at January 1, 2010 (millions of Canadian dollars)	Previous GAAP	Note (section iv)	Effect of transition to IFRS	IFRS
LIABILITIES				
Current liabilities				
Operating bank loans	$ 0.6		$ -	**$ 0.6**
Accounts payable and accrued liabilities	211.4		-	**211.4**
Current portion of long-term debt	34.0		-	**34.0**
Current portion of deferred reforestation obligations	27.8		-	**27.8**
Total current liabilities	273.8		-	**273.8**
Long-term debt	333.3		-	**333.3**
Retirement benefit obligations		e	101.3	
		e	132.2	
	-		233.5	**233.5**
Deferred reforestation obligations		f	60.3	
		f	7.1	
	-		67.4	**67.4**
Other long-term liabilities		f	(60.3)	
		e	(132.2)	
		f	1.0	
	209.8		(191.5)	**18.3**
Deferred income taxes, net		a	(11.4)	
		c	(14.2)	
		e	(49.5)	
		f	(2.0)	
		a	7.3	
	200.8		(69.8)	**131.0**
	$ 1,017.7		$ 39.6	**$ 1,057.3**
EQUITY				
Share capital	$ 1,124.7		$ -	**$ 1,124.7**
Contributed surplus	31.9		-	**31.9**
Retained earnings		c	(42.6)	
		e	(148.4)	
		f	(6.1)	
		g	(16.0)	
	246.2		(213.1)	**33.1**
Accumulated foreign exchange translation differences	(16.0)	g	16.0	**-**
Total equity attributable to equity holders of the Company	1,386.8		(197.1)	**1,189.7**
Non-controlling interests	273.3	e	(14.0)	**259.3**
Total equity	$ 1,660.1		$ (211.1)	**$ 1,449.0**
	$ 2,677.8		$ (171.5)	**$ 2,506.3**

(ii) Reconciliation of comprehensive income for year ended December 31, 2010

(millions of Canadian dollars)	Note (section iv)		Year ended December 31, 2010
Net income			
Previous GAAP		$	161.3
Lower amortization of property, plant and equipment and timber licenses in period, net of tax	c		5.2
Lower pension expense for period, net of tax	e		7.3
Higher accretion expense, net of tax	f		(0.5)
Net income under IFRS		**$**	**173.3**
Other comprehensive income (loss)			
Previous GAAP		$	(10.3)
Actuarial losses on defined benefit plans during the period, net of tax	e		(48.0)
Other comprehensive income (loss) under IFRS		**$**	**(58.3)**

(iii) Reconciliation of balance sheet at December 31, 2010

As at December 31, 2010 (millions of Canadian dollars)		Previous GAAP	Note (section iv)		Effect of transition to IFRS		**IFRS**
ASSETS							
Current assets							
Cash and cash equivalents	$	260.3		$	-	**$**	**260.3**
Accounts receivable - Trade		146.9			-		**146.9**
- Other		54.2			-		**54.2**
Deferred income taxes, net		12.4	a		(12.4)		**-**
Inventories		326.6	c		(0.8)		**325.8**
Prepaid expenses		38.8	b		(10.7)		**28.1**
Total current assets		839.2			(23.9)		**815.3**
Property, plant and equipment			b		13.8		
			c		(7.6)		
			d		(588.1)		
		1,631.0			(581.9)		**1,049.1**
Timber licenses			c		(41.4)		
			d		588.1		
		-			546.7		**546.7**
Goodwill and other intangible assets			e		(134.8)		
			d		13.4		
		205.9			(121.4)		**84.5**
Long-term investments and other			b		(3.1)		
			d		(13.4)		
			e		3.4		
		102.2			(13.1)		**89.1**
Deferred income taxes, net		-	a		9.4		**9.4**
	$	2,778.3		$	(184.2)	**$**	**2,594.1**

As at December 31, 2010 (millions of Canadian dollars)	Previous GAAP	Note (section iv)	Effect of transition to IFRS	IFRS
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities	$ 292.9		$ -	**$ 292.9**
Current portion of long-term debt	82.5		-	**82.5**
Current portion of deferred reforestation obligations	31.6		-	**31.6**
Total current liabilities	407.0		-	**407.0**
Long-term debt	235.6		-	**235.6**
Retirement benefit obligations		e	132.3	
		e	139.9	
	-		272.2	**272.2**
Deferred reforestation obligations		f	53.0	
		f	7.6	
	-		60.6	**60.6**
Other long-term liabilities		f	(53.0)	
		e	(139.9)	
		f	1.1	
	209.3		(191.8)	**17.5**
Deferred income taxes, net		a	(12.4)	
		c	(12.3)	
		e	(60.6)	
		f	(2.2)	
		a	9.4	
	209.3		(78.1)	**131.2**
	$ 1,061.2		$ 62.9	**$ 1,124.1**
EQUITY				
Share capital	$ 1,125.4		$ -	**$ 1,125.4**
Contributed surplus	31.9		-	**31.9**
Retained earnings		c	(37.5)	
		e	(182.7)	
		f	(6.5)	
		g	(16.0)	
	316.2		(242.7)	**73.5**
Accumulated foreign exchange translation differences	(26.3)	g	16.0	**(10.3)**
Total equity attributable to equity holders of the Company	1,447.2		(226.7)	**1,220.5**
Non-controlling interests	269.9	e	(20.4)	**249.5**
Total equity	$ 1,717.1		$ (247.1)	**$ 1,470.0**
	$ 2,778.3		$ (184.2)	**$ 2,594.1**

(iv) Explanatory notes for reconciliations

The following explanations are referenced in the reconciliations in sections (i) to (iii) of this note:

(a) Classification of all deferred income taxes as non-current assets (liabilities)

International Accounting Standard 1 ("IAS 1") requires that all deferred income tax balances be presented as non-current assets or liabilities on the balance sheet under IFRS. Previous GAAP required amounts to be shown as current assets or liabilities depending on the classification of the assets and liabilities to which the deferred income tax balances relate.

The effect of this reclassification on the Company's opening balance sheet was to move $11.4 million of deferred income taxes included within current assets to be offset against deferred income taxes in non-current liabilities. At December 31, 2010, the amount reclassified was $12.4 million.

In addition, assets and liabilities are now separately shown where no right of offset exists resulting in a reclassification of $7.3 million at January 1, 2010 and $9.4 million at December 31, 2010.

(b) Reclassification of deferred maintenance costs to property, plant and equipment

CPLP carries out scheduled major maintenance shutdowns at its mills at regular intervals where the period between shutdowns can be longer than 12 months. Under previous GAAP, the costs of such shutdowns were initially recorded as a prepaid expense (with current and long-term components) and amortized over the period until the next scheduled major shutdown. Under IFRS, these costs are considered to be a part of property, plant and equipment, and are also amortized over the period between shutdowns.

The effect of this on the Company's opening balance sheet was to reclassify $20.8 million into property, plant and equipment, with $15.4 million being removed from prepaid expenses, and $5.4 million from long-term investments and other (reflecting the long-term portion). At December 31, 2010, $13.8 million was reclassified into property, plant and equipment, with $10.7 million from prepaid expenses and $3.1 million from long-term investments and other.

The reclassification of these maintenance costs results in the related expense being moved from manufacturing and product costs to amortization. For the year ended December 31, 2010, the amount of the reclassification on the income statement was $18.7 million.

(c) Recognition of impairment provisions against property, plant and equipment and timber licenses

There are differences in the methodology used to determine if an asset should be impaired under IFRS compared to that under previous GAAP. The previous GAAP rules provided for a two-step test, with no impairment being required if the undiscounted future expected cash flows relating to an asset exceeded the carrying value of that asset. Under IFRS, the undiscounted cash flows are not considered and an impairment is recorded where the recoverable amount (defined as the higher of 'value in use' and 'fair value less costs to sell') is below the asset's carrying value. As a result, impairments were required for certain assets under IFRS that were not recorded under previous GAAP.

The effect at the date of transition was to decrease the book value of certain sawmill assets included within property, plant and equipment by $9.4 million and timber licenses by $46.6 million. An impairment of $0.8 million was also recorded against capital spares inventory. A corresponding adjustment to deferred income taxes of $14.2 million was also recorded, with the net amount of $42.6 million being charged to opening equity.

These impairments had the impact of reducing the overall amortization expense by $7.0 million ($5.2 million after-tax) for the 2010 year.

At December 31, 2010, the impact of these opening balance sheet impairments, after amortization, was to reduce property, plant and equipment by $7.6 million, timber licenses by $41.4 million and capital spares inventory by $0.8 million. The deferred income tax adjustment was $12.3 million, with the net amount of $37.5 million being charged to equity. No additional impairments were required at December 31, 2010 under IFRS.

(d) Reclassification of timber licenses and customer agreements

Under previous GAAP, the Company reported its timber licenses as a component of property, plant, equipment and timber. This is inconsistent with IFRS, and accordingly these balances have been reclassified to intangible assets. As a result of this reclassification, $610.3 million (before the above impairment) has been moved from property, plant, equipment and timber to timber licenses in the opening balance sheet, and $588.1 million at December 31, 2010.

In addition, customer agreements of $16.8 million in the opening balance sheet (December 31, 2010 - $13.4 million) have been reclassified from long-term investments and other to intangible assets (under goodwill and other intangible assets).

(e) Recognition of unamortized actuarial losses at date of transition to IFRS into equity

Under IFRS, the Company's accounting policy is to recognize all actuarial gains and losses, arising on its defined benefit pension and other non-pension post-retirement plans, immediately in other comprehensive income. At the date of transition, all previously unrecognized cumulative actuarial gains and losses were recognized in retained earnings.

This resulted in a charge to retained earnings in the opening balance sheet of $148.4 million, and a charge to non-controlling interests of $14.0 million reflecting non-controlling interests in CPLP. Pension assets recorded under previous GAAP of $110.6 million were removed, and liabilities of $101.3 million were recorded to reflect the actual funding position of the defined benefit pension plans. Remaining pension assets of $4.2 million were transferred from deferred charges to long-term investments and other. The long-term deferred income tax liability was reduced by $49.5 million as a result of these adjustments. In addition, $132.2 million was reclassified from other long-term liabilities into the retirement benefit obligations line item on the balance sheet, reflecting liabilities in relation to non-pension post-retirement plans.

Under previous GAAP, actuarial gains and losses were deferred and taken through the income statement over a number of years. As Canfor has elected to recognize these immediately through other comprehensive income under IFRS, the defined benefit expense in the income statement is reduced by $7.3 million for the full year in 2010. The after-tax charge through other comprehensive income was $48.0 million for the full year in 2010.

At December 31, 2010 the differences in retained earnings and non-controlling interests under IFRS compared to previous GAAP were $182.7 million and $20.4 million, respectively. Pension assets of $131.4 million were removed and a liability of $132.3 million was recorded, with remaining pension assets of $3.4 million reclassified to long-term investments and other. The long-term deferred income tax liability was reduced by $60.6 million as a result of these adjustments. In addition, $139.9 million was reclassified in relation to non-pension post-retirement plans.

Further, the Company has elected to apply the optional exemption from disclosure of certain pension balances and experience adjustments prior to the date of transition to IFRS.

(f) Change in discount rates for provisions

The Company has elected to present the long-term deferred reforestation provision as a separate item on the balance sheet in the current year. Previously, this was included in other long-term liabilities. The amount of the Company's deferred reforestation obligations of $60.3 million at January 1, 2010 was reclassified to a separate line item on the balance sheet.

Under previous GAAP, long-term provisions were discounted at the credit-adjusted risk-free rate in effect at the date the liability was recorded, whereas under IFRS these are discounted at the risk-free rate in effect at the balance sheet date. This results in a lower discount rate being used to value the Company's deferred reforestation and asset retirement obligations, with increases of $7.1 million and $1.0 million, respectively, to these provisions at January 1, 2010.

A corresponding adjustment to deferred income taxes of $2.0 million was recorded related to the change in both provisions, with the net amount of $6.1 million being charged to opening equity.

During 2010, the difference in discount rates used resulted in an after-tax expense that was higher by $0.4 million and $0.1 million, respectively, for the deferred reforestation and the asset retirement obligations. In addition, the expense related to the unwinding over time of the discount on the Company's deferred reforestation obligation was reclassified from manufacturing and product costs into finance expense.

At December 31, 2010, the deferred reforestation obligation under previous GAAP of $53.0 million was increased by $7.6 million due to different discount rates being used, and the asset retirement obligation was increased by $1.1 million. A corresponding adjustment to deferred income taxes of $2.2 million was recorded related to the change in both provisions, with the net amount of $6.5 million being charged to equity for the year ended December 31, 2010.

These adjustments represent a change from the preliminary January 1, 2010 and December 31, 2010 balance sheets as previously disclosed.

(g) Reset of the accumulated foreign translation account to zero at transition

In accordance with IFRS 1, the Company has elected to deem all foreign currency translation differences that arose prior to the date of transition in respect of entities with functional currencies other than the Canadian dollar to be nil at the date of transition. This resulted in a credit of $16.0 million to accumulated foreign translation differences and a charge of the same amount to retained earnings.

(v) Explanation of material adjustments to the statement of cash flows

The impact of the transition to IFRS on the statement of cash flows is to reclassify certain items between cash flow categories. One of the main reclassifications relates to interest payments and receipts which were classified as operating activities under previous GAAP, but are shown as financing and investing activities, respectively, under IFRS.

In addition, the reclassification of certain of CPLP's major maintenance costs to property, plant and equipment under IFRS has an impact on the statement of cash flows. Under previous GAAP, these costs were shown under operating activities as deferred maintenance spending, whereas under IFRS they are included in additions to property, plant and equipment under investing activities.