



**INTERFOR**

Building Value™

**2016**  
**Annual Report**

## CORRECTION NOTICE

This updated Annual Report corrects certain publishing and typographical issues that were identified in the previous version. The Company's 2016 Consolidated Financial Statements (financial statements) and Management's Discussion and Analysis (MD&A) filings are correct in all respects and remain unchanged. The issues arose from the process of compiling these documents into the Annual Report. In particular, the updated Annual Report reflects changes to a paragraph in the MD&A titled Balance Sheet and the following items in the financial statements: (i) operating earnings (loss) before restructuring costs; (ii) restructuring costs; (iii) total items that are or may be recycled to net earnings (loss); and (iv) note 26 (d) (ii). The result of these changes is that the updated Annual Report conforms with the Company's filed 2016 financial statements and MD&A.

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## FINANCIAL HIGHLIGHTS

(in millions of dollars, except share and per share amounts)

	2016	2015
<b>Financial Summary</b>		
Sales	1,792.7	1,687.4
Adjusted EBITDA <sup>(1)</sup>	199.6	91.7
Net earnings (loss)	65.6	(30.4)
<b>Per Share Data</b>		
Net earnings (loss) per common share		
- basic and diluted	0.94	(0.44)
Price range per share		
High	15.99	23.61
Low	8.67	8.86
Net book value per share	11.23	10.36
Operating cash flow per share before working capital change	2.75	0.96
Weighted average shares outstanding (millions)	70.0	69.5
<b>Financial Position</b>		
Total assets	1,301.6	1,389.8
Total debt	308.8	468.8
Total shareholders' equity	786.7	725.3
Invested capital <sup>(1)</sup>	1,076.2	1,177.6
<b>Financial Ratios (%)</b>		
Net debt as a % of invested capital, adjusted <sup>(1)</sup>	26.9%	38.4%
Pre-tax return (loss) on total assets <sup>(1)</sup>	6.2%	(1.9%)

Notes:

(1) See Glossary for definition.

***"With well-positioned mills, a strong balance sheet and momentum building in the South, Interfor is in great shape to deliver on our goal of building long-term value for our shareholders."***

***Message to Shareholders – February 2017***

**For further highlights, please see the Message to Shareholders and Management's Discussion and Analysis on the following pages.**

## MESSAGE TO SHAREHOLDERS

### **Overview**

2016 was a good year for Interfor. Better market conditions and prices were certainly a factor but the biggest gains came from the steps taken in mid-2015 to deal with the issues impacting our performance and from the resumption of operations at our mill at Castlegar in the B.C. Interior, which was rebuilt during 2015.

Highlights for 2016 include:

- Production remained flat at 2.5 billion board feet;
- Sales revenue increased 6% to \$1.79 billion;
- Earnings and cash flow improved significantly;
- The former Tacoma mill site was sold;
- Net debt was reduced by \$163 million; and
- A margin improvement initiative was launched in the U.S. South.

I believe the progress made in 2016 has put Interfor back on track to meet our goal of delivering above-average returns to our shareholders over time.

I invite you to read the material covered in the next few pages and later in this report and to form your own views on our progress.

Please feel free to forward any comments or questions you have to me directly at [duncan.davies@interfor.com](mailto:duncan.davies@interfor.com).

### **Production Volumes Flat; Higher Prices Contribute to Record Sales Revenue and EBITDA**

After rapid growth in the last three years, Interfor's production volumes were flat in 2016 as the Company focused on digesting its recent growth and bringing the rebuilt Castlegar mill back into production.

For the year, lumber production was 2.49 billion board feet compared with 2.50 billion board feet in 2015, with the Company's operations in Canada accounting for 35% of production and our mills in the U.S. accounting for 65%.

Sales volumes, including agency and wholesale activities, came in at 2.56 billion board feet in 2016 vs. 2.65 billion board feet the year prior.

Product prices were better across-the-board in 2016 as demand in the U.S. continued to grow and trading patterns adjusted to the currency shifts that impacted 2015.

All in, Interfor made \$65.6 million after-tax in 2016 on record sales of \$1.79 billion compared with a net loss of \$30.4 million on sales of \$1.69 billion in 2015.

EBITDA<sup>1</sup> reported before non-recurring items and share-based compensation expense came in at an all-time high of \$199.6 million versus \$91.7 million in 2015.

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<sup>1</sup> Refer to definition of Adjusted EBITDA in the Glossary

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### **Castlegar Sawmill Exceeds Expectations**

In November 2014 we announced a \$50 million upgrade to our sawmill at Castlegar in the B.C. Interior.

The project converted the mill from a 3-line operation to a 2-line facility using technology similar to that employed at our mills at Adams Lake, Grand Forks and Port Angeles, and avoided something in the range of \$20 million in maintenance capital that would otherwise have been required over the next few years.

The main elements of construction were completed in September 2015 and the mill resumed operations in the first week of October 2015.

I'm pleased to report that the mill ramped up quickly post-project and performed very well throughout the year, exceeding our expectations in almost every respect.

The rebuilt mill made a significant contribution to our financial results in 2016 and additional gains are expected as operations are fine-tuned in the years ahead.

### **Tacoma Mill Site Sold**

A key element of our improved performance in 2016 can be traced back to the decision made in mid-2015 to permanently close our Tacoma sawmill, which had been acquired using a contingent value structure earlier that year, as part of a transaction involving three other mills.

The final step in the Tacoma initiative was completed in November with the sale of the mill's property for cash proceeds of US\$31.5 million. Net proceeds were US\$20.4 million after taking account of transaction costs and the US\$10.0 million due to the former owner, which was paid following year-end.

The sale of the property triggered an after-tax gain of \$9.4 million, which was included in the Company's net earnings in 2016.

### **Strong Cash Flow Contributes to \$163 Million Reduction in Net Debt**

Maintaining a strong balance sheet has always been a key element of our management philosophy, with a target of maintaining a ratio of net debt to invested capital in the 30-40% range.

At year-end 2015 our debt ratio sat in the upper end of that range at 38.4%.

I'm pleased to report that net debt was reduced by \$162.8 million in 2016 to \$289.6 million, the equivalent of 26.9% of invested capital.

The gains in the Company's debt ratio and the corresponding increase in available liquidity (which improved from \$112 million at year-end 2015 to \$296 million at the end of 2016) provides additional protection against uncertainty and puts Interfor in a strong position to take advantage of additional value-creating opportunities in the years ahead.

### **Margin Improvement Initiative Launched in U.S. South**

There are two key pillars to Interfor's business strategy: growth through acquisition and operational excellence.

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In particular, we seek out opportunities for growth in attractive timber baskets and then apply our operating and capital projects skills to effect improvements in the performance, profitability and value of those operations.

We've done this a number of times in the past, most recently in the B.C. Interior at Grand Forks and Castlegar.

Those mills were acquired as part of a bankruptcy process in 2008. At the time, they were high cost facilities with out-dated equipment, poor productivity and a number of other challenges. Now, following a series of initiatives undertaken by our staff and crews in the area and the infusion of relatively modest amounts of capital, the mills are firmly positioned as top performers in the Interior region.

In 2013, we embarked on a similar program in the U.S. South.

Through a series of five separate transactions over a two and-a-half year period we acquired a total of nine mills in the U.S. South with aggregate production capacity of 1.3 billion board feet.

The U.S. South is a particularly interesting region. It constitutes the largest regional lumber market in North America and has abundant timber supply. At the same time, mills in the region often underperform mills in other jurisdictions from a productivity and efficiency standpoint.

Through our acquisitions we have established a major platform in the U.S. South with significant imbedded upside potential.

Our task now is to realize on that potential.

To that end, we have embarked on the first stage of a margin improvement initiative which we believe will deliver \$35 million in annualized EBITDA gains by the end of 2017, without any significant capital expenditures.

These gains will be delivered through increases in mill reliability and productivity, the volume of lumber recovered from each log and from gains in product mix and grade recovery.

With good progress already made, we are confident the target gains in EBITDA will be achieved by the end of this year.

Equally exciting are the second and third stage gains available in the region through the application of high return capital which we'll move to once the first stage gains have been solidified.

### **Softwood Dispute Creates Uncertainty; Interfor Well-Positioned**

The Softwood Lumber Agreement ("SLA") between Canada and the U.S. expired in October 2015. Following the expiry of a 12 month "standstill" provision which was built into the SLA, U.S. lumber producers had the right under U.S. trade law to file a petition against Canadian lumber imports. Not surprisingly, they did so in November, as they have done on four previous occasions in the last 35 years.

As a company that operates in both Canada and the U.S., we don't believe there is any substance to the U.S. claims. And that fact has been verified in each of the four

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previous cases by independent tribunals, most recently in 2006, which led ultimately to the signing of the SLA.

In our view, a dispute over trade in softwood lumber between Canada and the U.S. is a waste of time.

We understand the reality of U.S. trade law and how it's applied and, for that reason, have long advocated for a negotiated settlement between the parties.

We remain hopeful that saner heads will prevail and once the new U.S. administration gets up-to-speed, it will join with the Canadian government to make the negotiation of a new SLA a priority.

In the meantime, with two-thirds of our production capacity located in the U.S. and our Canadian mills in great shape, Interfor is well-positioned to withstand any disruption that may arise in the absence of a settlement.

### **Gillian Platt Appointed To Board of Directors**

In October 2016, Interfor's Board of Directors appointed Gillian Platt of Kelowna, B.C. as a director of the Company.

Gillian has more than 30 years of broad-based executive experience spanning a variety of industries, with a focus on human resources management, executive compensation, talent management and strategy.

Most recently she served as Executive Vice President and CHRO of Finning International Inc. where she was responsible for human resources and communications globally.

Gillian's background and expertise are ideally suited for a Company like ours, in the current stage of our development, and we are looking for a significant contribution from her in the years ahead.

Gillian has been nominated to stand for election as a director at the Company's Annual General Meeting in May.

### **Vision Remains Intact; Progress Being Made**

Trade issues aside, positive signs continue to emerge in the U.S. and offshore, laying the foundation for better markets in 2017 and beyond.

With well-positioned mills, a strong balance sheet and momentum building in the South, Interfor is in great shape to deliver on our goal of building long-term value for our shareholders.

In closing, I would like to thank our employees, Board of Directors and shareholders for their on-going support.

I look forward to reporting to you on our progress again this time next year.

Duncan Davies  
President & CEO  
February, 2017

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Prepared as of February 9, 2017

**This Management's Discussion and Analysis ("MD&A") provides a review of financial condition and results of operations as at and for the three and twelve months ended December 31, 2016 ("Q4'16" and "2016", respectively). It should be read in conjunction with the audited consolidated financial statements of Interfor Corporation and its subsidiaries ("Interfor" or the "Company") for the year ended December 31, 2016, and the notes thereto which have been prepared in accordance with International Financial Reporting Standards ("IFRS"). This MD&A contains certain non-GAAP measures which, within the Non-GAAP Measures section, are discussed, defined and reconciled to figures reported in the Company's consolidated financial statements. This MD&A has been prepared as of February 9, 2017.**

**All figures are stated in Canadian Dollars, unless otherwise noted, and references to US\$/USD are to the United States Dollar. For definitions of technical terms and abbreviations used within this MD&A, refer to the Glossary in the Company's 2016 Annual Report.**

### **Forward-Looking Statements**

This MD&A contains information and statements that are forward-looking in nature, including, but not limited to, statements about the Company's business outlook, objectives, plans, strategic priorities and other statements that are not historical facts. A statement Interfor makes is forward-looking when it uses what is known today, to make a statement about the future. Forward-looking statements are included under the headings "Overview of 2016", "Outlook", "Liquidity", "Capital Resources", "Off-Balance Sheet Arrangements", "Financial Instruments and Other Instruments", "Accounting Policy Changes" and "Risks and Uncertainties", and such statements may include words such as "believes", "will", "could", "should", "expected", "anticipate", "intend", "forecast", "target", "outlook" and "strategy". Such forward-looking statements are based on Interfor's current expectations and certain assumptions, including assumptions regarding lumber, log and wood chip prices; the Company's ability to compete on a global basis; the availability and cost of log supply; the absence of natural or man-made disasters; currency exchange rates; no material changes in government regulation; the availability of the Company's allowable annual cut ("AAC"); the outcome of aboriginal claims and treaty settlements; the Company's ability to export its products; the outcome of the softwood lumber dispute between Canada and the U.S.; stumpage rates payable to the Province of British Columbia; environmental effects of the Company's operations; the absence of labour disruptions and the assumptions described under the heading "Critical Accounting Estimates" herein. Such forward-looking statements involve known and unknown risks and uncertainties that, if they eventuate, may cause Interfor's actual results to be materially different from those expressed or implied by those forward-looking statements. Such risks and uncertainties include lumber, log and wood chip price volatility; global competition; reduction of availability or increase in cost of log supply; natural or man-made disasters; foreign currency exchange rate fluctuations; changes in government regulation; reductions to the Company's AAC; aboriginal claims or treaty settlements impacting the Company's forest tenures; export and other trade barriers; the softwood lumber dispute between Canada and the U.S.; increases in stumpage rates payable to the Province of British Columbia; environmental effects of the Company's operations; labour disruptions; and other factors referenced herein. Readers are cautioned not to place undue reliance on forward-looking information or statements. Interfor undertakes no obligation to update such forward-looking information or statements, except as required by law.

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## Overview of 2016

### Q4'16 Results

Interfor recorded net earnings in Q4'16 of \$26.6 million, or \$0.38 per share, compared to \$15.1 million, or \$0.22 per share in Q3'16 and a loss of \$3.5 million, or \$0.05 per share in Q4'15. Adjusted net earnings in Q4'16 were \$17.7 million or \$0.25 per share, compared to \$20.7 million, or \$0.30 per share in Q3'16 and \$4.5 million, or \$0.06 per share in Q4'15.

Adjusted EBITDA was \$51.3 million on sales of \$442.3 million in Q4'16 versus \$58.1 million on sales of \$457.6 million in Q3'16.

For the year, net earnings were \$65.6 million, or \$0.94 per share, compared to a loss of \$30.4 million or \$0.44 per share in 2015. Adjusted EBITDA was a record \$199.6 million, eclipsing the previous record set in 2014.

Notable items in the quarter included:

- Strong Cash Flow and Proceeds from Tacoma Sale contributes to \$57.4 million in Net Debt Reduction
  - Interfor generated \$49.0 million in cash from operations, after considering working capital changes in Q4'16.
  - The sale of the former sawmill property in Tacoma, Washington closed in Q4'16 with cash proceeds of US\$31.5 million. The net proceeds are approximately US\$20.4 million after taking account of transaction costs and the US\$10.0 million due to the former owner that was paid in January, 2017.
  - Capital spending was \$19.8 million in Q4'16.
  - The resulting free cash flow contributed to a reduction in net debt to \$289.6 million, or 26.9% of invested capital. For the year, net debt was reduced by \$162.8 million.
- Mixed Lumber Prices and Lower Canadian Dollar
  - Key benchmark lumber prices were mixed in Q4'16. The Southern Pine Composite increased US\$11 to US\$393 per mfbm as stronger prices for 2x4 and 2x8 more than offset weaker prices for 2x6, 2x10 and 2x12. At the same time, the Western SPF Composite and KD H-F Stud 2x4 9' benchmarks declined US\$6 to US\$305 per mfbm and US\$18 to US\$318 per mfbm respectively.
  - The Canadian Dollar weakened by 2.2% to US\$0.750 quarter-over-quarter thereby offsetting, in part, the drop in SPF and H-F prices.
- Seasonal Operating Schedules Impact Production and Sales Volumes
  - In Q4'16, Interfor reduced its operating schedules across several regions in line with normal seasonal practice. Lumber production of 607 million board feet was 21 million board feet lower than the preceding quarter. Sales of Interfor-produced lumber were 598 million board feet in Q4'16 versus 627 million board feet in Q3'16.
  - In Q4'16, the B.C. and Northwest regions accounted for 209 million board feet (which equated to operating rates of 92% in the B.C. Interior and 47% on the B.C. Coast) and 137 million board feet (which equated to an operating rate of 86%) of production respectively in Q4'16 compared with 238 million board feet and 141 million board feet respectively in Q3'16. Operating rates in the South region were up slightly in Q4'16, with production increasing to 260 million board feet (which equated to an operating rate of 78%) from 248 million board feet in the preceding quarter.

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- In addition, severe winter weather conditions adversely impacted certain of the operations in B.C. and the Northwest during late December and continued into January, impacting productivity and conversion costs in those regions.
  - Progress on Optimization Initiatives Sets the Foundation to Capture Target EBITDA Gains
    - In early 2016, Interfor launched a Business Optimization Initiative to capture additional margin opportunities across the Company's operating platform, with a particular focus on the South region, where \$35 million in annualized EBITDA gains were targeted by year-end 2017.
    - Good progress was made during Q4'16 with productivity levels across the South region up 9% versus Q1'16 and lumber recovery up more than 5%. Good progress is being made as well on the initiative to improve product mix and grade recovery.
    - The Company believes the target uplift in EBITDA will be realized over the course of 2017, as operating rates in the South region increase to 90% or more, which is expected by Q4'17.

### **Outlook**

Interfor expects demand for lumber to continue to grow over the mid-term as the U.S. housing market recovers and market promotion efforts in North America and offshore take full effect. In addition, the Company is focused on a series of targeted initiatives related to margin improvement opportunities across its operations in both the U.S. and Canada that should contribute to Interfor's financial results.

Interfor's strategy of maintaining a diversified portfolio of lumber operations allows the Company to both reduce risk and maximize returns on invested capital over the business cycle. Interfor will continue its disciplined approach to production, cost control, inventory management and capital spending. At the same time, Interfor will remain alert to growth opportunities to position the Company for long term success.

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**Financial and Operating Highlights** <sup>(1)</sup>

Unit	For the 3 months ended			For the year ended Dec. 31			
	Dec. 31 2016	Dec. 31 2015	Sept. 30, 2016	2016	2015	2014	
<b>Financial Highlights</b> <sup>(2)</sup>							
Total sales	\$MM	442.3	411.4	457.6	1,792.7	1,687.4	1,447.2
Lumber	\$MM	363.5	325.0	374.8	1,458.3	1,361.2	1,177.3
Logs, residual products and other	\$MM	78.8	86.4	82.8	334.4	326.2	269.9
Operating earnings (loss)	\$MM	22.3	(6.3)	20.1	75.9	(35.9)	36.1
Net earnings (loss)	\$MM	26.6	(3.5)	15.1	65.6	(30.4)	40.7
Net earnings (loss) per share, basic and diluted	\$/share	0.38	(0.05)	0.22	0.94	(0.44)	0.62
Adjusted net earnings (loss) <sup>(3)</sup>	\$MM	17.7	4.5	20.7	58.7	(18.9)	60.7
Adjusted net earnings (loss) per share, basic and diluted <sup>(3)</sup>	\$/share	0.25	0.06	0.30	0.84	(0.27)	0.92
Adjusted EBITDA <sup>(3)</sup>	\$MM	51.3	35.8	58.1	199.6	91.7	169.3
Adjusted EBITDA margin <sup>(3)</sup>	%	11.6%	8.7%	12.7%	11.1%	5.4%	11.7%
Total assets	\$MM	1,300.1	1,389.8	1,326.8	1,300.1	1,389.8	1,068.5
Total debt	\$MM	308.8	468.8	365.3	308.8	468.8	220.4
Pre-tax return on total assets <sup>(3)</sup>	%	7.4%	-1.0%	6.5%	6.2%	-1.9%	6.4%
Net debt to invested capital <sup>(3)</sup>	%	26.9%	38.4%	31.8%	26.9%	38.4%	24.1%
<b>Operating Highlights</b>							
Lumber production	million fbm	607	568	628	2,490	2,497	2,222
Total lumber sales	million fbm	619	615	647	2,561	2,652	2,282
Lumber sales - Interfor produced	million fbm	598	586	627	2,469	2,544	2,217
Lumber sales - wholesale and commission	million fbm	21	29	20	92	108	65
Lumber - average selling price <sup>(4)</sup>	\$/thousand fbm	588	529	580	570	513	516

## Notes:

- (1) Figures in this table may not equal or sum to figures presented elsewhere due to rounding.
- (2) Financial information presented for interim periods in this MD&A is prepared in accordance with IFRS and is unaudited.
- (3) Refer to the Non-GAAP Measures section of this MD&A for definitions and reconciliations of these measures to figures reported in the Company's consolidated financial statements.
- (4) Gross sales before export taxes.

**Summary of Fourth Quarter 2016 Financial Performance**Sales

Interfor recorded \$442.3 million of total sales, up 7.5% from \$411.4 million in the fourth quarter of 2015, driven by the sale of 619 million board feet of lumber at an average price of \$588 per mfbm. Lumber sales volume increased 4 million board feet, or 0.7%, while average selling price increased \$59 per thousand board feet, or 11.1%, as compared to the same quarter of 2015.

The increase in the average selling price of lumber reflects higher prices across all benchmark products in Q4'16 as compared to Q4'15. The Southern Pine Composite and KD HF Stud 2x4 9' benchmark improved US\$50 to US\$393 per mfbm and US\$24 to US\$318 per mfbm, respectively. The Western SPF Composite was up US\$49 to US\$305 per mfbm.

Sales generated from logs, residual products and other decreased by \$7.6 million or 8.8% compared to the same quarter of 2015. Nearly all of this decrease is related to the Q4'15 disposal of log inventories as the Tacoma sawmill wound down operations, partially offset by lower chip prices across all regions except the U.S. South in Q4'16.

Operations

Production costs increased by \$15.5 million or 4.2% over Q4'15, primarily due to higher log costs on average in all regions except the U.S. South and higher conversion costs in the U.S. South operations as work continues on optimization initiatives.

Lumber production of 607 million board feet in Q4'16 was 39 million board feet higher than Q4'15.

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Production from the Company's nine U.S. South sawmills totaled 260 million board feet in Q4'16, up 17 million board feet compared to Q4'15, primarily as a result of severe weather events which impacted the Georgetown mill significantly in Q4'15.

Canadian production totaled 209 million board feet in Q4'16, up 24 million board feet as compared to Q4'15. The increase in Canadian production primarily reflects efficiency gains at the rebuilt Castlegar sawmill, which was in start-up in Q4'15.

Production from the Company's U.S. Northwest operations totaled 137 million board feet in Q4'16, representing a decline of 1 million board feet from Q4'15.

Depreciation of plant and equipment was largely unchanged from Q4'15 as a result of comparable production levels in both periods. Depletion and amortization of timber, roads and other was down \$2.9 million from the comparable quarter of 2015 as a result of reduced conventional logging on the B.C. Coast in Q4'16.

#### Corporate and Other

Selling and administration expenses were \$9.6 million, down \$0.7 million from the fourth quarter of 2015 which included certain IT infrastructure improvement costs.

The \$0.2 million long term incentive compensation expense is due primarily to the vesting of awards in Q4'16. The Q4'15 long term incentive compensation expense of \$9.3 million mostly reflects the impact of a 49.0% increase in the market price for Interfor Common Shares during the quarter.

Restructuring charges in Q4'16 relate to \$1.2 million in impairment charges on surplus equipment, \$0.6 million in costs associated with the closure of the Tacoma sawmill, and \$0.5 million for the settlement of a defined benefit pension plan. In Q4'15, the Company took an impairment charge of \$1.2 million on equipment replaced in 2016 as a result of changes to government regulations.

Finance costs decreased to \$4.1 million from \$5.5 million in the fourth quarter, 2015. Free cash flow was used to reduce the average debt level which decreased interest costs.

Other foreign exchange gains of \$1.1 million in Q4'16 and \$0.5 million in Q4'15 resulted primarily from unrealized gains on short-term intercompany funding.

Other income increased by \$13.6 million in Q4'16, primarily as the result of the sale of the Tacoma sawmill property which completed on November 30, 2016.

#### Income Taxes

The Company recorded an income tax expense of \$7.2 million in Q4'16, comprised of a \$0.1 million current tax expense and a \$7.1 million deferred tax expense. The Company started to recognize deferred tax expense in respect of its Canadian operations in Q4'16 following full recognition of previously unrecognized assets for non-capital loss carry-forwards.

#### Net Earnings (Loss)

The Company recorded net earnings of \$26.6 million or \$0.38 per share, compared to a net loss of \$3.5 million or \$0.05 per share in the comparable period, 2015. Adjusted net earnings were \$17.7 million or \$0.25 per share compared with \$4.5 million or \$0.06 per share in Q4'15.

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## **Summary of 2016 Financial Performance**

### Sales

Interfor recorded \$1.8 billion in total sales, up 6.2% from \$1.7 billion in 2015, driven by the sale of 2.6 billion board feet of lumber at an average price of \$570 per mfbm. Lumber sales volume decreased 91 million board feet, or 3.4%, while average selling price increased \$57 per thousand board feet, or 11.0%, as compared to 2015.

The sales volume decline was affected by temporary operating shift modifications and downtime taken for capital and business optimization projects at several mills in the U.S. South, along with the closure of the Tacoma sawmill, partially offset by the inclusion of a full year of sales volume in 2016 from the sawmills acquired in 2015 and a full year of production from the rebuilt Castlegar sawmill.

The increase in the average selling price of lumber reflects higher prices across all benchmark products in 2016 as compared to 2015. The Southern Pine Composite and KD HF Stud 2x4 9' benchmark improved US\$25 to US\$382 per mfbm and US\$30 to US\$335 per mfbm, respectively. The Western SPF Composite was up US\$16 to US\$295 per mfbm.

Sales realizations were also impacted by the strengthening of the U.S. Dollar against the Canadian dollar by 3.6% on average.

Sales generated from logs, residual products and other increased by \$8.2 million or 2.5% compared to 2015 as a result of increased log exports in 2016 offsetting the impact of relatively low prices realized on the disposal of log inventories at the exited Tacoma sawmill.

### Operations

Production costs declined by \$4.1 million or 0.3% as compared to 2015, explained primarily by the 3.4% decrease in lumber sales volume, lower log costs at the Company's U.S. operations and lower conversion costs in the B.C. Interior, somewhat offset by higher log costs in Canadian operations, higher conversion costs in the U.S. South operations as they continue to work on optimization initiatives, and the stronger U.S. Dollar on average.

Lumber production of 2.5 billion board feet in 2016 was 7 million board feet lower than in 2015.

Production from the Company's nine U.S. South sawmills totaled 1.0 billion board feet in 2016, down 15 million board feet compared to 2015, with inclusion of a full year's production from the three sawmills acquired in 2015 offset by temporary adjustments to operating schedules across the U.S. South platform to implement a series of capital and optimization initiatives.

Canadian production totaled 877 million board feet in 2016, up 92 million board feet as compared to 2015. The increase in Canadian production primarily reflects efficiency gains at the Castlegar sawmill, after its rebuild was substantially completed in Q4'15.

Production from the Company's U.S. Northwest operations totaled 570 million board feet in 2016, representing a decline of 84 million board feet from 2015, resulting from closure of the Tacoma sawmill, and reduced operating hours at Molalla.

As the Softwood Lumber Agreement ("SLA") expired on October 12, 2015, there were no export taxes in 2016. Export taxes of \$5.2 million in 2015 were incurred in respect of lumber shipments from the Company's Canadian operations to the U.S. under the SLA.

Depreciation of plant and equipment was \$76.1 million, up 6.4% from 2015. The majority of this increase is explained by incremental depreciation on the rebuilt Castlegar sawmill and the inclusion of a full year's depreciation on four sawmills acquired in 2015.

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Depletion and amortization of timber, roads and other was \$34.9 million, down 6.9% as compared with 2015, as a result of a reduction in log production and a higher percentage of heli-logging on the B.C. Coast in 2016.

#### Corporate and Other

Selling and administration expenses were \$43.1 million, down \$3.7 million from 2015. 2015 included \$2.1 million of non-recurring acquisition and integration costs and \$0.9 million for certain IT infrastructure improvements.

The \$4.6 million long term incentive compensation expense in 2016 mainly reflects a 7.6% increase in the market price of Interfor Common Shares over the same period, coupled with the impact of incentive awards maturing. The \$5.4 million long term incentive compensation recovery in 2015 resulted from a 36.0% decrease in the market price of Interfor Common Shares over the same period, partially offset by the impact of incentive awards maturing.

In 2015, the Company recognized restructuring charges of \$10.1 million, including severance, an onerous contract, site closure costs and write-downs of inventories related to closure of the Tacoma sawmill. An additional impairment charge of \$2.8 million was recorded on equipment to be replaced in 2016 as a result of changes to government regulations. Interfor also sold substantially all of the assets of its Beaver-Forks operation, located on the Olympic Peninsula in Washington, resulting in a reversal of a \$1.2 million impairment previously recorded.

In 2016, Interfor recorded additional restructuring charges of \$4.3 million for the Tacoma site, including further site closure costs and write-downs of inventories, and an impairment of buildings. Additional restructuring charges of \$3.0 million relate to a number of costs, the most significant of which is a \$1.2 million impairment charge on surplus equipment.

Finance costs increased to \$18.6 million from \$17.6 million in 2015 as a result of a higher average level of debt outstanding in 2016 as compared to 2015, together with the impact of a stronger U.S. Dollar.

Other foreign exchange gain of \$1.5 million is comprised primarily of foreign exchange gains on short term intercompany funding. Other foreign exchange loss of \$1.7 million in 2015 is comprised primarily of foreign exchange losses on foreign exchange forward contracts.

Other income of \$14.1 million is comprised primarily of a gain on the sale of the Tacoma sawmill property which completed on November 30, 2016. Other income of \$0.8 million in 2015 is comprised primarily of the gain on sale of timber tenures in the B.C. Interior.

#### Income Taxes

The Company recorded an income tax expense of \$7.2 million in 2016, comprised of \$0.9 million of current taxes and a \$6.4 million deferred income tax expense. The Company started to recognize deferred tax expense in respect of its Canadian operations in Q4'16 following full recognition of previously unrecognized assets for non-capital loss carry-forwards.

#### Net Earnings (Loss)

The Company recorded net earnings of \$65.6 million or \$0.94 per share, compared to a net loss of \$30.4 million or \$0.44 per share in 2015. Adjusted net earnings were \$58.7 million or \$0.84 per share compared with an Adjusted net loss of \$18.9 million or \$0.27 per share in 2015.

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**Summary of Quarterly Results<sup>(1)</sup>**

Unit	2016				2015				
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1	
<b>Financial Performance (Unaudited)</b>									
Total sales	\$MM	442.3	457.6	458.8	433.9	411.4	430.8	429.7	415.4
Lumber	\$MM	363.5	374.8	371.1	348.9	325.0	343.3	352.2	340.7
Logs, residual products and other	\$MM	78.8	82.8	87.7	85.0	86.4	87.5	77.5	74.7
Operating earnings (loss)	\$MM	22.3	20.1	30.0	3.5	(6.3)	(11.6)	(25.8)	7.8
Net earnings (loss)	\$MM	26.6	15.1	23.2	0.8	(3.5)	(6.1)	(20.6)	(0.2)
Net earnings (loss) per share, basic and diluted	\$/share	0.38	0.22	0.33	0.01	(0.05)	(0.09)	(0.29)	(0.00)
Adjusted net earnings (loss) <sup>(2)</sup>	\$MM	17.7	20.7	17.5	2.7	4.5	(16.6)	(10.3)	3.5
Adjusted net earnings (loss) per share, basic and diluted <sup>(2)</sup>	\$/share	0.25	0.30	0.25	0.04	0.06	(0.24)	(0.15)	0.05
Adjusted EBITDA <sup>(2)</sup>	\$MM	51.3	58.1	56.9	33.4	35.8	11.5	12.7	31.8
Shares outstanding - end of period	million	70.0	70.0	70.0	70.0	70.0	70.0	70.0	70.0
Shares outstanding - weighted average	million	70.0	70.0	70.0	70.0	70.0	70.0	70.0	67.8
<b>Operating Performance</b>									
Lumber production	million fbm	607	628	637	618	568	618	672	639
Total lumber sales	million fbm	619	647	658	637	615	686	719	632
Lumber sales - Interfor produced	million fbm	598	627	634	609	586	663	688	607
Lumber sales - wholesale and commission	million fbm	21	20	24	28	29	23	31	25
Lumber - average selling price <sup>(3)</sup>	\$/thousand fbm	588	580	564	548	529	500	490	539
Average USD/CAD exchange rate <sup>(4)</sup>	1 USD in CAD	1.3341	1.3050	1.2886	1.3732	1.3354	1.3089	1.2297	1.2412
Closing USD/CAD exchange rate <sup>(4)</sup>	1 USD in CAD	1.3427	1.3117	1.3009	1.2971	1.3840	1.3394	1.2474	1.2683

## Notes:

- (1) Figures in this table may not add due to rounding.
- (2) Refer to the Non-GAAP Measures section of this MD&A for definitions and reconciliations of these measures to figures reported in the Company's consolidated financial statements.
- (3) Gross sales before export taxes.
- (4) Based on Bank of Canada foreign exchange rates.

The Company's quarterly financial trends are most impacted by seasonality, levels of lumber production, log costs, market prices for lumber and the USD/CAD foreign currency exchange rate.

Logging operations are seasonal due to a number of factors including weather, ground conditions and fire season closures. Generally, the Company's B.C. Coastal logging operations experience higher production levels in the latter half of the first quarter, throughout the second and third quarters and in the first half of the fourth quarter. Logging in the U.S. South follows a similar pattern. Logging activity in the B.C. Interior is generally higher in the first half of the first quarter, slows during spring break-up and increases in the third and fourth quarters. Sawmill operations are dependent on the availability of logs from our logging operations and our suppliers. In addition, the market demand for lumber and related products is generally lower in the winter due to reduced construction and renovation activities, which increase during the spring, summer and fall.

Four sawmills acquired on March 1, 2015, and one sawmill acquired on June 19, 2015, have all contributed to the growth in production and sales. The permanent closure of the Tacoma sawmill impacted production and sales subsequent to May 22, 2015.

The volatility of the Canadian Dollar against the U.S. Dollar also impacted results. A weaker Canadian Dollar increases the lumber sales realizations of Canadian operations and increases net earnings or losses of U.S. operations when translated to Canadian Dollars.

## Liquidity

### Balance Sheet

Interfor strengthened its financial position throughout 2016, with strong cash flow generated from operations and proceeds received from the monetization of the Tacoma sawmill property used to repay debt and fund capital projects. Net debt at December 31, 2016 was \$289.6 million, or 26.9% of invested capital, representing a decrease of \$162.8 million from the level of net debt at December 31, 2015.

A strengthening of the Canadian Dollar against the U.S. Dollar by 3.0% contributed \$16.1 million to the net debt reduction in 2016 over 2015 as all debt held was denominated in U.S. Dollars.

Thousands of dollars	For the 3 months ended December 31,		For the year ended December 31,	
	2016	2015	2016	2015
<b>Net debt</b>				
Net debt, period opening, CAD	\$ 346,929	\$ 461,474	\$ 452,303	\$ 202,553
Net drawing (repayment) on credit facilities, CAD	(66,178)	(19,207)	(143,882)	182,949
Impact on U.S. Dollar denominated debt from (strengthening) weakening CAD	9,678	14,592	(16,056)	65,391
Decrease (increase) in cash and equivalents, CAD	(878)	(4,556)	(2,814)	1,410
Net debt, period ending, CAD	\$ 289,551	\$ 452,303	\$ 289,551	\$ 452,303
<b>Net debt components by currency</b>				
U.S. Dollar debt, period opening, USD	\$ 274,709	\$ 345,957	\$ 338,699	\$ 190,000
Net drawing (repayment) on credit facilities, USD	(44,709)	(7,258)	(108,699)	148,699
U.S. Dollar debt, period ending, USD	230,000	338,699	230,000	338,699
Spot rate, period end			1.3427	1.3840
U.S. Dollar debt expressed in CAD			308,821	468,759
Canadian Dollar debt, including bank indebtedness, CAD			-	-
Canadian Dollar operating line, CAD			-	-
Total debt, CAD			308,821	468,759
Cash and cash equivalents, CAD			(19,270)	(16,456)
Net debt, period ending, CAD			\$ 289,551	\$ 452,303

As at December 31, 2016, the Company had net working capital of \$136.1 million and available liquidity of \$296.3 million, including cash and borrowing capacity on operating and term line facilities.

On February 9, 2016, the Company extended the maturity of its Operating Line and Revolving Term Line from February 27, 2017 to May 19, 2019 and amended certain other terms, resulting in an increase in the maximum borrowing available under the financing agreement. On June 15, 2016, the Company extended the maturity of its U.S. Operating Line from May 1, 2017 to May 1, 2018.

These resources, in addition to cash generated from operations, will be used to support working capital requirements, debt servicing commitments and capital expenditures. We believe that Interfor will have sufficient liquidity to fund operating and capital requirements for the foreseeable future.



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### Cash Flow from Operating Activities

The Company generated \$192.6 million of cash flow from operations before changes in working capital in 2016, or a \$125.7 million increase over 2015. Incremental cash flow generated from increased sales margins coupled with the strengthened U.S. Dollar, elimination of export taxes and reductions in selling and administration costs were slightly offset by a reduction in sales volumes. In 2015, increased sales volumes were offset by reduced sales margins and increases in export taxes and selling and administration costs.

There was a net cash inflow from operations after changes in working capital of \$199.3 million in 2016, with \$6.7 million of cash generated from operating working capital. In 2015, \$34.5 million of cash was generated from operating working capital, with \$101.4 million of total cash generated from operations.

### Cash Flow from Investing Activities

Investing activities totaled \$36.2 million in 2016, net of \$41.4 million in proceeds on the disposal of property, plant and equipment, resulting primarily from the monetization of the Tacoma sawmill property. Spending included \$52.1 million for property, plant and equipment, timber licenses and other intangibles, and \$24.6 million for development of logging roads. Discretionary improvements of \$17.8 million during 2016 included \$7.6 million for the finalization of the Castlegar sawmill rebuild.

In 2015, total investing activities of \$333.3 million included \$170.8 million for the Simpson acquisition, \$43.7 million for the Monticello acquisition, \$8.7 million for payment of the contingent purchase price to Keadle Lumber Enterprises Inc., \$95.3 million for property, plant and equipment, timber licenses and other intangibles and \$26.1 million for development of logging roads.

Spending of \$11.3 million on investments and other assets in 2016 related primarily to fixed income and equity investments purchased for treasury management purposes, the majority of which were disposed of within the year, resulting in proceeds on the disposal of investments of \$10.3 million.

### Cash Flow from Financing Activities

Net repayments under the Company's credit facilities were \$143.9 million, as the Company utilized surplus cash generated from operations and the proceeds from the Tacoma sawmill property sale to reduce debt. Cash used for financing activities totaled \$162.2 million in 2016.

In 2015, net drawings on the Company's credit facilities were \$182.9 million and net proceeds from issuance of 3.3 million shares were \$63.2 million, leading to total cash from financing activities of \$229.7 million in 2015. This includes \$151.3 million drawn on the Company's credit facilities to fund the Simpson and Monticello acquisitions.

### Summary of Contractual Obligations

The estimated cash payments due in respect of contractual and legal obligations as at December 31, 2016, including major capital improvements are summarized as follows:

Thousands of Canadian dollars	Total	Payments due by Period			
		Up to 1 Year	2-3 Years	4-5 Years	After 5 Years
Trade accounts payable and accrued liabilities	\$ 112,592	\$ 112,592	\$ -	\$ -	\$ -
Income taxes payable	317	317	-	-	-
Contingent future payment <sup>(1)</sup>	13,427	13,427	-	-	-
Reforestation liability	39,419	11,609	10,226	8,141	9,443
Long term debt	308,821	-	40,281	44,756	223,784
Provisions and other liabilities	38,817	11,008	5,662	2,150	19,997
<u>Operating leases and capital commitments</u>	<u>66,820</u>	<u>19,570</u>	<u>23,320</u>	<u>10,220</u>	<u>13,710</u>
<b>Total obligations</b>	<b>\$ 580,213</b>	<b>\$ 168,523</b>	<b>\$ 79,489</b>	<b>\$ 65,267</b>	<b>\$ 266,934</b>

Notes:

(1) Relates to Simpson acquisition and was paid on January 13, 2017.

### Capital Resources

The following table summarizes Interfor's credit facilities and availability as of December 31, 2016:

Thousands of Canadian dollars	Operating Line	Revolving Term Line	Senior Secured Notes	U.S. Operating Line	Total
Available line of credit	\$ 65,000	\$ 200,000	\$ 268,540	\$ 67,135	\$ 600,675
Maximum borrowing available	\$ 65,000	\$ 200,000	\$ 268,540	\$ 65,627	\$ 599,167
Less:					
Drawings	-	40,281	268,540	-	308,821
Outstanding letters of credit included in line utilization	10,026	-	-	3,296	13,322
<u>Unused portion of facility</u>	<u>\$ 54,974</u>	<u>\$ 159,719</u>	<u>\$ -</u>	<u>\$ 62,331</u>	<u>\$ 277,024</u>
Add cash and cash equivalents					19,270
<u>Available liquidity at Dec. 31, 2016</u>					<u>\$ 296,294</u>

As of December 31, 2016, the Company had commitments for capital expenditures totaling \$7.9 million for both maintenance and discretionary capital projects.

### Transactions between Related Parties

Other than transactions in the normal course of business with key management personnel, the Company had no transactions between related parties in the year ended December 31, 2016.

### Off-Balance Sheet Arrangements

The Company has off-balance sheet arrangements which include letters of credit and surety performance bonds, primarily for timber purchases. At December 31, 2016, such instruments aggregated \$45.7 million (December 31, 2015 - \$47.4 million). Off-balance sheet arrangements have not had, and are not reasonably likely to have, any material impact on the Company's current or future financial condition, results of operations or cash flows.

## **Financial Instruments and Other Instruments**

From time to time, the Company employs financial instruments, such as interest rate swaps and foreign currency contracts, to manage exposure to fluctuations in interest rates and foreign currency exchange rates. The Company's policy is to not use derivatives for trading or speculative purposes. Risk management strategies and relationships are formally documented and assessed on a regular, ongoing basis to ensure derivatives are effective in offsetting changes in fair values or cash flows of hedged items. The counter-parties for all derivative contracts existing at December 31, 2016, are the Company's Canadian bankers who are highly-rated, thereby mitigating the risk of credit loss on such instruments.

### **Interest Rate Swaps**

As at December 31, 2016, Interfor had drawn a total of \$40.3 million of floating rate debt, excluding letters of credit, on its credit facilities. The Company's facilities bear interest at the bank prime rate plus a premium, or, at the Company's option, at rates for Bankers' Acceptances for Canadian Dollar loans or at LIBOR for U.S. Dollar loans, in all cases dependent upon a financial ratio.

Two of the Company's interest rate swaps matured on April 14, 2016. Two interest rate swaps remained outstanding at December 31, 2016 each with a notional value of US\$25,000,000. Under these two interest rate swaps, maturing February 27, 2017, the Company pays an amount based on a fixed annual interest rate of 0.84% and receives a 90 day LIBOR which is recalculated at set interval dates

These interest rate swaps convert a portion of the Company's floating-rate interest expense to fixed-rate interest expense and have been designated as cash flow hedges. The fair value of these interest rate swaps at December 31, 2016, being an asset of less than \$0.1 million (measured based on Level 2 of the fair value hierarchy), has been recorded in Trade accounts receivable and other (2015 - \$0.1 million) and a negligible loss (2015 - \$0.1 million) has been recognized in Other comprehensive income.

Based on the Company's average debt level during 2016, the sensitivity of a 100 basis point increase in interest rates would result in an approximate decrease of \$0.3 million in Net earnings.

### **Foreign Currency Contracts**

The Company is exposed to currency risk on cash and cash equivalents, accounts receivable, accounts payable and provisions and long term debt that are denominated in a currency other than the respective functional currencies of the Company's domestic and foreign operations, primarily Canadian and U.S. Dollars, but also the Euro, Sterling and Yen. The Company uses foreign currency exchange contracts to manage its currency risk from time to time. The Company routinely assesses its foreign exchange exposure by reviewing outstanding contracts, pending order files and working capital denominated in foreign currencies.

As at December 31, 2016, the Company had no outstanding foreign currency exchange contract obligations (2015 - nil). All foreign currency gains or losses on foreign currency contracts in 2016 have been recognized in Other foreign exchange gain (loss) in Net earnings.

Unrealized gains and losses arising upon translation of net foreign currency investment positions in U.S. Dollar functional currency foreign operations, together with any gain or losses arising from hedges of those net investment positions, to the extent effective, are credited or charged to net change in unrealized foreign currency translation gains (losses) in the Consolidated Statement of Comprehensive Income. Upon sale, reduction or substantial liquidation of an investment position, the previously recorded net unrealized gains (losses) thereon in the Translation reserve are reclassified to the Consolidated Statement of Earnings.

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As at December 31, 2016, the Company had designated the US\$30.0 million drawn under its Revolving Term Line and US\$200.0 million drawn under its Senior Secured Notes as hedges against the net investment in its U.S. operations.

The Company recorded a \$7.9 million unrealized foreign exchange loss on translation of its U.S. operations with a U.S. Dollar functional currency, net of revaluations of debt designated as hedges against the net investment in U.S. operations, to Other comprehensive income in 2016 (2015 - \$56.5 million gain).

### **Outstanding Shares**

As of December 31, 2016, Interfor had 70,030,455 Common Shares issued and outstanding. These shares are listed on the Toronto Stock Exchange under the symbol IFP.

### **Controls and Procedures**

The Company's management, under the supervision of the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), has evaluated the design and effectiveness of the Company's disclosure controls and procedures. Based on this evaluation, the CEO and CFO have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2016.

The Company's management, under the supervision of the CEO and CFO, has evaluated the design and effectiveness of the Company's internal controls over financial reporting ("ICFR") based on the criteria established within the 2013 COSO framework. Based on this evaluation, the CEO and CFO have concluded that the Company's ICFR were effective as of December 31, 2016.

The CEO and CFO acknowledge responsibility for the design of ICFR and confirm that there were no changes in these controls that occurred during the year ended December 31, 2016, which materially affected, or are reasonably likely to materially affect, the Company's ICFR.

### **Critical Accounting Estimates**

The Company's financial statements include critical accounting estimates made by management. Management is required to make various assumptions about matters that are highly uncertain at the time accounting estimates are made; the use of different assumptions could have a material impact on the Company's financial condition and performance. These critical accounting estimates are described below.

*Valuation of Inventories.* Lumber inventories are valued at the lower of cost and net realizable value on a specific product basis. Log inventories are valued at the lower of cost and net realizable value on a specific boom or sort basis. The unit net realizable value for lumber inventories and B.C. Coast log inventories is determined by reference to the average sales values by specific product in the period immediately following the reporting date. The unit realizable value for B.C. Interior and U.S. log inventories is determined by reference to the value of the projected lumber and residual outturns. The unit cost for lumber is based on a three month moving average cost, lagged by one month and adjusted for abnormal costs, as in the case of a curtailment. The unit cost for B.C. Coast logs is based on a twelve month moving average cost lagged one month and for B.C. Interior logs is based on the three month moving average cost, both adjusted for abnormal costs. The unit cost for U.S. logs is based on purchase cost. The Company records a charge to operating earnings when net realizable value is lower than carrying value. Downward movements in commodity prices could result in a material write-down of log and/or lumber inventories at any given time.

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*Recoverability of Property, Plant and Equipment, Logging Roads and Bridges, Timber licences, Other Intangible Assets, and Goodwill.* Interfor's assessment of recoverability of property, plant and equipment, logging roads, bridges, timber licences and other intangible assets is made with reference to projections of future cash flows to be generated by its operations. The assessment of recoverability of goodwill is also made with reference to projections of future cash flows to be generated by the related cash generating unit. In both cases the projected cash flows are discounted to estimate the recoverable amount of the related assets.

The Company conducts a review of external and internal sources of information to assess existence of any impairment indicators. External factors include adverse changes in expected future prices, costs and other market and economic factors. Internal factors include changes in the expected useful life of the asset or changes to the planned capacity of the asset.

Key assumptions used are based on industry sources, including Forest Economic Advisors, LLC, as well as management estimates. Assumptions encompass lumber and residual chip sales prices, applicable foreign exchange rates, operating rates of the assets, raw material and conversion costs, the level of sales to the U.S. from Canada, the export tax rate, future capital required to maintain the assets in their current operating condition, and other items.

A high degree of uncertainty exists in these assumptions and, as such, any significant change in assumptions could result in a conclusion that the carrying value of these assets may not be recovered, which could necessitate a material charge against operating earnings.

Appropriate discount rates are determined by reference to current market conditions, specific company factors and asset specific factors. The inflation rate applied within the cash flow projections represents the published Bank of Canada consumer price index.

Interfor assesses the recoverability of Property, Plant and Equipment, Logging Roads and Bridges, Timber Licences and Other Intangible Assets whenever events or circumstances indicate that the carrying value may not be recoverable. Goodwill is tested for impairment annually, and whenever events or changes in circumstances indicate that impairment may exist. The Company assessed the recoverability of goodwill as at December 31, 2016 and concluded that there was no impairment.

*Reforestation and Other Forestry-related Liabilities.* Crown legislation requires the Company to complete reforestation activities on its forest and timber tenures. Accordingly, Interfor records the estimated liability for reforestation as timber is cut, and includes these expenses in the cost of current production. The estimate of future reforestation costs is based on detailed prescriptions of reforestation as prepared by Registered Professional Foresters employed or contracted by the Company. Considerations include the specifics of the areas logged and the treatments prescribed for those areas, as well as the timing and success rates of the planned activities. Estimates of reforestation liabilities could be materially impacted by forest fires, wildlife grazing, unfavourable weather conditions, changing legislative requirements and standards, or inaccurate projections, which could result in a charge against operating earnings.

The Company also has a legal obligation to deactivate certain roads constructed for access to timber, once that access is no longer required. Accordingly, Interfor accrues the cost of road deactivation as related timber is cut, including those expenses in the cost of current production. The estimate of future road deactivation cost is based on comprehensive plans prepared by Professional Foresters and Engineers employed by Interfor and includes such considerations as road structure and terrain. Estimates of road deactivation liabilities could be materially impacted by unfavourable terrain, changing legislative requirements and standards, or inaccurate projections, which could result in a charge against operating earnings. Each of these estimates is reviewed regularly on an ongoing basis.

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*Pension and Other Post-retirement Benefits.* The Company sponsors two defined benefit pension plans for those hourly employees not covered by forest industry union plans. It also sponsors two post-retirement medical and life insurance plans and a non-contributory defined benefit pension plan for a former senior executive.

The Company retains independent actuarial consultants to value the defined pension benefit obligations, the post-retirement medical and life insurance obligations and related plan asset values. Actuarial assumptions used in the valuation of plan obligations and assets include assumptions for the discount rate used in calculations of net present value of obligations, expected rates of return on plan assets to be used to fund obligations, and assumed rates of increase for employee compensation and health care costs. Actual experience can vary materially from estimates and could result in a material charge against operating earnings as well as necessitate a current cash funding requirement.

*Income Taxes.* The Company's provision for income taxes, both current and deferred, is based on various judgments, assumptions and estimates including the tax treatment of transactions recorded in the Company's consolidated financial statements. Interfor records provisions for income taxes based on the respective tax rules and regulations in the jurisdictions in which the Company operates. Due to the number of variables associated with the judgments, assumptions and estimates, and differing tax rules and regulations across the multiple jurisdictions, the precision and reliability of the resulting estimates are subject to uncertainties and may change as additional information becomes known.

Income tax assets and liabilities, both current and deferred, are measured according to the income tax legislation that is expected to apply when the asset is realized or the liability settled. Deferred income tax assets and liabilities are comprised of the tax effect of temporary differences between the carrying amount and tax basis of assets and liabilities, tax loss carry forwards and tax credits. Assumptions underlying the composition of deferred income tax assets and liabilities include estimates of future results of operations and the timing of the reversal of temporary differences as well as the tax rates and laws in the applicable jurisdictions at the time of the reversal. The composition of deferred income tax assets and liabilities is reasonably likely to change from period to period due to the uncertainties surrounding these assumptions.

### **Accounting Policy Changes**

A number of new standards, and amendments to existing standards and interpretations, were not yet effective for the year ended December 31, 2016, and have not been applied in preparing the Company's 2016 annual audited consolidated financial statements. The following pronouncements are considered by the Company to be the most significant of several pronouncements that may affect the financial statements:

IFRS 9, *Financial Instruments*, will replace the multiple classification and measurement models in IAS 39, *Financial Instruments: Recognition and Measurement*, with a single model that has only two classification categories: amortized cost and fair value. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted.

IFRS 15, *Revenue from Contracts with Customers*, will replace all existing IFRS revenue requirements and is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted.

The Company is still in the process of assessing IFRS 9 and IFRS 15, but does not currently believe either will have a significant impact on its financial statements.

IFRS 16, *Leases*, eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Under the

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new standard, operating leases become an on-balance sheet liability that attracts interest, together with a corresponding right-of-use asset. In addition, lessees will recognize a front-loaded pattern of expense for most leases, even when cash rentals are constant. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. The Company has not yet completed an assessment of the impact of this standard on its financial statements.

### Non-GAAP Measures

This MD&A makes reference to the following non-GAAP measures: Adjusted net earnings (loss), Adjusted net earnings (loss) per share, EBITDA, Adjusted EBITDA, Pre-tax return on total assets and Net debt to invested capital, which are used by the Company and certain investors to evaluate operating performance and financial position. These non-GAAP measures do not have any standardized meaning prescribed by IFRS and are therefore unlikely to be comparable to similar measures presented by other issuers.

The following table provides a reconciliation of these non-GAAP measures to figures as reported in the Company's audited consolidated financial statements prepared (unaudited for interim periods) in accordance with IFRS:

Thousands of Canadian dollars except number of shares and per share amounts	For the 3 months ended			For the year ended Dec. 31		
	Dec. 31 2016	Dec. 31 2015	Sept. 30, 2016	2016	2015	2014
<b>Adjusted Net Earnings (Loss)<sup>(1)</sup></b>						
Net earnings (loss)	\$ 26,550	\$ (3,507)	\$ 15,093	\$ 65,643	\$ (30,386)	\$ 40,690
Add:						
Restructuring costs and capital asset write-downs	2,281	2,866	1,492	7,280	12,829	24,129
Other foreign exchange loss (gain)	(1,072)	(473)	(792)	(1,468)	1,651	2,651
Long term incentive compensation expense (recovery)	199	9,335	8,321	4,551	(5,431)	23,933
Other income	(14,452)	(863)	(7)	(14,094)	(757)	37
Beaver sawmill post-closure wind-down costs	128	6	6	145	365	1,083
Tacoma sawmill post-acquisition losses and closure costs	(13)	698	94	764	11,009	-
Income tax effect of above adjustments	4,895	(2,564)	(1,408)	2,008	(9,311)	(10,951)
Recognition of previously unrecognized deferred tax assets	(769)	(983)	(2,134)	(6,171)	1,136	(20,902)
Adjusted net earnings (loss)	\$ 17,747	\$ 4,515	\$ 20,665	\$ 58,658	\$ (18,895)	\$ 60,670
Weighted average number of shares - basic and diluted ('000)	70,030	70,030	70,030	70,030	69,488	66,005
Adjusted net earnings (loss) per share	\$ 0.25	\$ 0.06	\$ 0.30	\$ 0.84	\$ (0.27)	\$ 0.92
<b>Adjusted EBITDA</b>						
Net earnings (loss)	\$ 26,550	\$ (3,507)	\$ 15,093	\$ 65,643	\$ (30,386)	\$ 40,690
Add:						
Depreciation of plant and equipment	18,534	18,482	18,624	76,092	71,492	55,167
Depletion and amortization of timber, roads and other	7,833	10,734	9,441	34,895	37,478	28,912
Restructuring costs and capital asset write-downs	2,281	2,866	1,492	7,280	12,829	24,129
Finance costs	4,074	5,459	4,379	18,602	17,569	8,915
Other foreign exchange loss (gain)	(1,072)	(473)	(792)	(1,468)	1,651	2,651
Income tax expense (recovery)	7,236	(6,943)	1,445	7,207	(24,017)	(16,230)
EBITDA	65,436	26,618	49,682	208,251	86,616	144,234
Add:						
Long term incentive compensation expense (recovery)	199	9,335	8,321	4,551	(5,431)	23,933
Other income	(14,452)	(863)	(7)	(14,094)	(757)	37
Beaver sawmill post-closure wind-down costs	128	6	6	145	363	1,075
Tacoma sawmill post-acquisition losses and closure costs	(13)	698	94	764	10,928	-
Adjusted EBITDA	\$ 51,298	\$ 35,794	\$ 58,096	\$ 199,617	\$ 91,719	\$ 169,279
<b>Pre-tax return on total assets</b>						
Operating earnings (loss) before restructuring costs	\$ 24,617	\$ (3,461)	\$ 21,610	\$ 83,170	\$ (23,111)	\$ 60,192
Total assets <sup>(2)</sup>	1,326,792	1,383,751	1,337,569	1,345,722	1,229,160	946,325
Pre-tax return on total assets <sup>(3)</sup>	7.4%	(1.0%)	6.5%	6.2%	(1.9%)	6.4%
<b>Net debt to invested capital</b>						
Net debt						
Total debt	\$ 308,821	\$ 468,759	\$ 365,321	\$ 308,821	\$ 468,759	\$ 220,419
Cash and cash equivalents	(19,270)	(16,456)	(18,392)	(19,270)	(16,456)	(17,866)
Total net debt	\$ 289,551	\$ 452,303	\$ 346,929	\$ 289,551	\$ 452,303	\$ 202,553
Invested capital						
Net debt	\$ 289,551	\$ 452,303	\$ 346,929	\$ 289,551	\$ 452,303	\$ 202,553
Shareholders' equity	786,667	725,254	745,333	786,667	725,254	636,480
Total invested capital	\$1,076,218	\$1,177,557	\$1,092,262	\$1,076,218	\$1,177,557	\$ 839,033
Net debt to invested capital <sup>(4)</sup>	26.9%	38.4%	31.8%	26.9%	38.4%	24.1%

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Notes:

- (1) Certain historical periods have been recast to exclude the recognition of previously unrecognized deferred tax assets from Adjusted net earnings.
- (2) Total assets at period beginning for three month periods; average of opening and closing total assets for twelve month periods.
- (3) Annualized rate.
- (4) Net debt to invested capital as of the period end.

## **Risks and Uncertainties**

The Company is exposed to many risks and uncertainties in conducting its business including, but not limited to the factors described below.

### Price Volatility

The Company's operating results are affected by fluctuations in the selling prices for lumber, logs and wood chips. Prices are affected by such factors as the general level of economic activity in the markets in which the Company sells its products, interest rates, construction activity (in particular, housing starts in the United States, Canada, Japan and China), and log and chip supply/demand relationships. The Company's financial results may be significantly affected by changes in the selling prices of its products.

### Competition

The markets for the Company's products are highly competitive on a global basis and producers compete primarily on the basis of price. In addition, a majority of the Company's lumber production is sold in markets where the Company competes against many producers of approximately the same or larger capacity. Some of the Company's competitors have greater financial resources and a number are, in certain product lines, lower-cost producers.

Factors which affect the Company's competitive position include:

- foreign currency exchange rates;
- the cost of labour;
- costs of harvesting or purchasing logs;
- the ability to secure a quality log supply matched to a sawmill's requirements;
- the quality of its products and customer service;
- the ability to secure space on vessels for overseas shipments and on trucks and railcars for North American shipments;
- the existence and rate of export taxes payable on sales from Canada to the United States; and
- its ability to maintain high operating rates to leverage fixed manufacturing costs.

If the Company is unable to successfully compete on a global basis, its financial condition could suffer.

### Availability and Cost of Log Supply

The log requirements of the Company's sawmills are met using logs harvested from its timber tenures, by long term trade and purchase agreements and by purchases on the open market and through timber sale bids. Logs produced but unsuitable for use in the Company's sawmills are either traded for suitable logs or sold on the open market. Operating at normal capacity, the Company's Canadian sawmills generally purchase less than 40% of their log requirements either through purchase agreements or on the open market. The Company relies almost entirely on purchased fibre through purchase agreements for its U.S. based sawmills, with a small volume occasionally supplied by the Company's Canadian coastal logging operations for the sawmill located on Washington's Olympic Peninsula. As a result, fluctuations in the price,

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quality or availability of log supply can have a material effect on the Company's business, financial position, results of operations and cash flow. In addition, weather-related issues can restrict timely access to log supply.

The Company relies on third-party independent contractors to harvest timber in areas over which it holds timber tenures. Increases in rates charged by these independent contractors or the limited availability of these independent contractors may increase the Company's timber harvesting costs.

Additionally, in order to ensure uninterrupted access to logs harvested from its timber tenures in Canada, the Company must also focus on the continuous development of road networks. This encompasses an integrated plan by foresters, engineers and logging operations personnel to identify future logging areas and develop the engineering for roads. The Company expects to fund its ongoing road development with cash generated from operations and through utilization of its existing credit facilities.

#### Natural or Man-Made Disasters

The Company's operations are subject to adverse natural or man-made events such as forest fires, severe weather conditions, climate change, timber disease and insect infestation and earthquake activity. These events could damage or destroy the Company's physical facilities or timber supply and similar events could also affect the facilities of the Company's suppliers or customers. Any such damage or destruction could adversely affect the Company's financial results due to decreased production output or increased operating costs. Although management believes it has reasonable insurance arrangements in place to cover certain of such incidents, there can be no assurance that these arrangements will be sufficient to fully protect the Company against such losses. As is common in the industry, the Company does not insure loss of standing timber for any cause.

#### Currency Exchange Sensitivity

The Company's Canadian operations ordinarily sell approximately 80% of their lumber into export markets, with the majority of these sales denominated in U.S. Dollars and, to a lesser extent, in Japanese Yen. While the Canadian operations also incur some U.S. Dollar-denominated expenses, primarily for ocean freight and other transportation and for equipment operating leases, the majority of expenses are incurred in Canadian Dollars. The Company's operations in the United States transact primarily in U.S. Dollars.

An increase in the value of the Canadian Dollar relative to the U.S. Dollar would reduce the amount of revenue in Canadian Dollars realized by the Company from lumber sales made in U.S. Dollars. This would reduce the Company's operating margin and the cash flow available to fund operations. Consequently, a significant strengthening of the Canadian Dollar against the U.S. Dollar could have a material adverse effect on the Company's business, financial condition, results of operations and cash flows.

#### Government Regulation

The Company's operations are subject to extensive provincial, state, federal or other laws and regulations that apply to most aspects of its business activities. Where applicable, the Company is required to obtain approvals, permits and licences for its operations as a condition to operate.

From time to time, changes in government policy or regulation may impact the Company's operations. Until the details of all such changes are announced and implemented, the full impact of these changes on the Company's production, costs, financial position and results of operations cannot be determined.

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### Allowable Annual Cut ("AAC")

The Company holds cutting rights in British Columbia ("B.C.") that represent an AAC of approximately of 3.7 million cubic metres. Of this amount, 3.65 million cubic metres is in the form of replaceable tenures (4 Tree Farm Licences and 19 Forest Licences). The remaining portion is held in non-replaceable Timber Licences that will expire over time.

The AAC is regulated by the Ministry of Forests, Lands and Natural Resource Operations and is subject to a periodic Timber Supply Review process to make determinations that set harvesting rates for each tenure. Many factors affect the AAC, including timber inventory, operable land base, growth rates, regulations, forest health, land use and environmental and social considerations.

Reductions in the Company's AAC from any new protected areas are subject to compensation once these areas have been formally removed. Currently there is a Government plan in 2017 to set aside some additional area for conservation purposes in the Mid Coast region that may affect some of the Company's Timber Licences and trigger a claim for compensation. The timber volume impacted has not been finalized, and the amount of compensation is not known at this time.

Proposed regulatory changes in 2017 to meet new Ecosystem Based Management ("EBM") requirements in the Central Coast of B.C. will also impact the Company's timber supply, and these are not compensable. The AAC impact, once these changes take effect, will be approximately a 6% reduction of the company's timber supply in B.C.

The amount of timber available for harvest in the south-central portion of the B.C. Interior is expected to decline over the next 10 years as the surplus of dead pine stands from the pine beetle epidemic become no longer useable. A portion of Interfor's tenures can expect some modest AAC declines over this period, but they are not expected to have a material impact on our internal supply.

### Aboriginal Issues

Aboriginal groups have claimed aboriginal title and rights over substantial portions of B.C., including areas where the Company's forest tenures are situated, creating uncertainty as to the status of competing property rights. The Federal and Provincial governments have been seeking to negotiate settlements with aboriginal groups throughout B.C. in order to resolve aboriginal rights and title claims. In addition, the governments have entered, and may continue to enter, into interim measure (reconciliation) agreements with aboriginal groups. Any interim measures, agreements or settlements that may result from the treaty process may involve a combination of cash, resources, grants of conditional rights to resources on public lands and rights of self-government. The impact of aboriginal claims or treaty settlements on the Company's forest tenures or the amounts of compensation to the Company, if any, cannot be estimated at this time.

The courts have also established that the Crown has a duty to consult with aboriginal groups and, where appropriate, accommodate aboriginal interests. However, questions of responsibility and appropriateness of balancing interests will continue to evolve as the parties try to address these long-standing and complex issues. The Government of B.C. has been working to improve the functional relationship between the Crown and aboriginal groups prior to treaty settlement. The Province of B.C. and some First Nations groups on the coast of B.C. have signed Reconciliation Protocols that provide a shared decision making process for resource and land use, as well as new forest sector opportunities. These agreements overlap portions of the Company's coastal tenures. The agreements will be assessed and monitored in the years ahead to determine the extent of any implications on those operations.

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### Softwood Lumber Trade

The Company's financial results are dependent on continued access to the U.S. market for the portion of Company's products that are manufactured in Canada and exported to the U.S. Tariffs and other trade barriers that restrict or prevent access represent a continuing risk to the Company's Canadian based operations. Approximately 15% of Interfor's total softwood lumber sales would be exposed to duties and/or trade restrictions imposed by the U.S.

The Softwood Lumber Agreement implemented by the federal governments of Canada and the United States in 2006, expired on October 12, 2015. As part of that agreement the U.S. government agreed to a standstill period, where it would not take any trade action against Canada for a twelve month period following expiry. On November 25, 2016, the U.S. Coalition filed a petition with the U.S. Department of Commerce ("DoC") and the U.S. International Trade Commission ("ITC") seeking countervailing and anti-dumping duties on Canadian softwood lumber imports to the U.S.

On January 6, 2017, the ITC determined that there is a reasonable indication that the U.S. industry is materially injured by the imports of softwood lumber products from Canada. As a result, the DoC will commence its anti-dumping and countervailing duty investigations on imports of these products.

The DoC is expected to announce its ruling in the Countervailing Duty ("CVD") investigation in the second quarter of 2017. A ruling in the Anti-dumping Duty ("AD") investigation is expected to come approximately 60 days thereafter. If the DoC rules that "critical circumstances" apply, duties could be applied retroactively up to 90 days prior to the preliminary determinations. It is not anticipated that this would give rise to a liability as at December 31, 2016.

While dialogue continues between the U.S. and Canada, there is no assurance there will be any new trade agreement forthcoming or whether a new trade agreement could adversely affect the Company's Canadian operations. Canada is expected to defend itself vigorously in any trade action taken by the U.S.

### Stumpage Fees

The Province of B.C. charges stumpage fees to companies that harvest timber from Crown land. Stumpage payments for a harvesting area are based on a competitive market pricing system ("MPS") that has been established for both the coast and interior regions of B.C.

The stumpage system is complex and the subject of discussion involving, among other things, lumber trade agreements between Canada and the United States. The primary variable in the MPS is log pricing established through open market bidding for standing timber. In addition to bid prices, there are a number of operational and administrative factors that determine an individual stumpage rate for each cutting permit.

Periodic changes in the Provincial government's administrative policy can affect the market price for timber and the viability of individual logging operations. There can be no assurance that current changes or future changes will not have a material impact on stumpage rates.

### Environment

The Company has incurred, and will continue to incur, costs to minimize environmental impact, prevent pollution and for continuous improvement of its environmental performance. The Company may discover currently unknown environmental problems or conditions relating to its past or present operations, or it may be faced with an unforeseen environmental liability in the future. This may require site or other remediation costs to maintain compliance or correct violations of environmental laws and regulations or result in governmental or private claims for

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damage to person, property or the environment, which could have a material adverse effect on the Company's financial condition and results of operations.

#### Labour Disruptions

Production disruptions resulting from walkouts or strikes by unionized employees could result in lost production and sales, which could have a material adverse impact on the Company's business. The Company believes that its current labour relations are stable and does not anticipate any related disruptions to its operations in the foreseeable future.

The Company depends on a variety of third parties that employ unionized workers to provide critical services to the Company. Labour disputes by these third parties could lead to disruptions at the Company's facilities. The Company's Acorn, Hammond, Grand Forks, and Castlegar sawmill employees are members of the Canadian United Steelworkers union ("USW"). The collective agreement with the Southern Interior USW agreement (Grand Forks and Castlegar) expires on June 30, 2018, while the USW agreement for the B.C. Coast (Acorn and Hammond) expires on June 15, 2019. The Company also has 22 employees in the B.C. Interior who are members of the Canadian Marine Service Guild ("CMSG"). The collective agreement with the CMSG expires September 30, 2019.

In 2015, the Company acquired sawmills in Meldrim, Georgia and Longview, Washington where employees were represented by the American USW and the International Association of Machinist and Aerospace Workers ("IAM"), respectively. The American USW at the Meldrim sawmill was decertified on April 28, 2016, while the IAM collective agreement expires on November 15, 2020.

#### **Additional Information**

Additional information relating to the Company and its operations, including the Company's Annual Information Form, can be found on its website at [www.interfor.com](http://www.interfor.com) and on SEDAR at [www.sedar.com](http://www.sedar.com).

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## **CONSOLIDATED FINANCIAL STATEMENTS**

### **MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS**

Management is responsible for the integrity and fair presentation of the accompanying consolidated financial statements. The financial statements were prepared in accordance with International Financial Reporting Standards and, where necessary, are based in part on management's best estimates and judgements. Financial information included elsewhere in the 2016 Annual Report is consistent with that disclosed in the consolidated financial statements.

Management maintains a system of internal accounting control which it believes provides reasonable assurance that financial records are reliable and form a proper basis for preparation of financial statements. The internal accounting control process includes communications to employees of Interfor's standards for ethical business conduct.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. The Board exercises this responsibility primarily through its Audit Committee, the members of which are neither officers nor employees of Interfor. The Audit Committee meets periodically with management and the independent Auditors to satisfy itself that each group is properly discharging its responsibilities and to review the consolidated financial statements and the independent Auditors' report thereon. The Company's independent Auditors have full and free access to the Audit Committee. The Audit Committee reports its findings to the Board of Directors for consideration in approving the consolidated financial statements for issuance to the shareholders. The Committee also makes recommendations to the Board with respect to the appointment and remuneration of the independent Auditors.

The consolidated financial statements have been examined by the independent Auditors, KPMG LLP, whose report follows.

*"Duncan K. Davies"*

President and Chief Executive Officer

*"John A. Horning"*

Executive Vice President and Chief Financial  
Officer

February 09, 2017

## **CONSOLIDATED FINANCIAL STATEMENTS**

### **INDEPENDENT AUDITORS' REPORT**

To the Shareholders

We have audited the accompanying consolidated financial statements of Interfor Corporation (the "Company") which comprise the consolidated statements of financial position as at December 31, 2016 and December 31, 2015, the consolidated statements of earnings (loss), comprehensive income, changes in equity and cash flows for the years ended December 31, 2016 and December 31, 2015, and notes, comprising 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.

#### *Auditors' Responsibility*

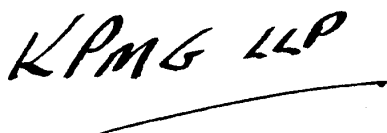
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits to obtain 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 our 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, we consider internal control relevant to the Company'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 consolidated financial position of Interfor Corporation as at December 31, 2016 and December 31, 2015, and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2016 and December 31, 2015 in accordance with International Financial Reporting Standards.



KPMG LLP, Chartered Accountants

February 09, 2017  
Vancouver, Canada

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## Consolidated Statements of Financial Position

(Expressed in thousands of Canadian Dollars)

As at December 31, 2016 and 2015

	Note	December 31 2016	December 31 2015
<b>Assets</b>			
Current assets:			
Cash and cash equivalents	10	\$ 19,270	\$ 16,456
Trade accounts receivable and other		95,059	95,218
Income tax receivable	19	222	459
Inventories	6	154,535	155,740
Prepayments and other		14,016	15,512
Investments and other assets	7	2,911	-
Assets held for sale	5	-	27,836
		286,013	311,221
Employee future benefits	22(d)	2,471	1,570
Investments and other assets	7	2,341	3,191
Property, plant and equipment	4, 8	730,981	777,590
Logging roads and bridges	9	20,739	20,611
Timber licences	9	69,273	72,429
Other intangible assets	9	19,017	23,601
Goodwill	9	156,502	160,914
Deferred income taxes	19	14,311	18,669
		\$1,301,648	\$1,389,796
<b>Liabilities and Shareholders' Equity</b>			
Current liabilities:			
Trade accounts payable and provisions	11, 22(d)	\$ 138,029	\$ 130,840
Reforestation liability	12	11,609	11,052
Income taxes payable	19	317	398
		149,955	142,290
Reforestation liability	12	25,931	25,074
Long term debt	10	308,821	468,759
Employee future benefits	22(d)	8,136	8,391
Provisions and other liabilities	11	21,290	20,028
Deferred income taxes	19	848	-
Equity:			
Share capital	13	555,388	553,559
Contributed surplus		7,999	7,665
Translation reserve		69,574	77,425
Hedge reserve		11	62
Retained earnings		153,695	86,543
		786,667	725,254
		\$ 1,301,648	\$ 1,389,796

Commitments and contingencies (*note 20*); Subsequent events (*note 5, 20 (c)*).

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board of Directors:

"L. Sauder", Director

"D.W.G. Whitehead", Director

**Consolidated Statements of Earnings (Loss)**  
 (Expressed in thousands of Canadian Dollars, except earnings per share)  
 Years ended December 31, 2016 and 2015

	<i>Note</i>	2016	2015
Sales		\$1,792,712	\$1,687,375
Costs and expenses:			
Production		1,550,912	1,554,975
Selling and administration	4	43,092	46,756
Long term incentive compensation expense (recovery)	11	4,551	(5,431)
Export taxes		-	5,216
Depreciation of plant and equipment	8, 14	76,092	71,492
Depletion and amortization of timber, roads and other	9, 14	34,895	37,478
		<u>1,709,542</u>	<u>1,710,486</u>
Operating earnings (loss) before restructuring costs		83,170	(23,111)
Restructuring costs	18	(7,280)	(12,829)
Operating earnings (loss)		75,890	(35,940)
Finance costs	16	(18,602)	(17,569)
Other foreign exchange gain (loss)		1,468	(1,651)
Other income	17	14,094	757
		<u>(3,040)</u>	<u>(18,463)</u>
Earnings (loss) before income taxes		72,850	(54,403)
Income tax expense (recovery):	19		
Current		853	614
Deferred		6,354	(24,631)
		<u>7,207</u>	<u>(24,017)</u>
Net earnings (loss)		<u>\$ 65,643</u>	<u>\$ (30,386)</u>
Net earnings (loss) per share, basic and diluted	21	<u>\$ 0.94</u>	<u>\$ (0.44)</u>

See accompanying notes to consolidated financial statements.



## Consolidated Statements of Comprehensive Income

(Expressed in thousands of Canadian Dollars)

Years ended December 31, 2016 and 2015

	<i>Note</i>	2016	2015
Net earnings (loss)		\$ 65,643	\$ (30,386)
Other comprehensive income (loss):			
Items that will not be recycled to Net earnings (loss):			
Defined benefit plan actuarial gains (losses), net of tax	<i>19, 22</i>	1,509	(629)
Items that are or may be recycled to Net earnings (loss):			
Foreign currency translation differences for foreign operations, net of tax		(7,851)	56,475
Loss in fair value of interest rate swaps	<i>16, 26</i>	(51)	(71)
Total items that are or may be recycled to Net earnings (loss)		(7,902)	56,404
Total other comprehensive income (loss), net of tax		(6,393)	55,775
Comprehensive income		\$ 59,250	\$ 25,389

See accompanying notes to consolidated financial statements.

### Consolidated Statements of Changes in Equity

(Expressed in thousands of Canadian Dollars)

Years ended December 31, 2016 and 2015

	<i>Note</i>	Common Shares	Contributed Surplus	Translation Reserve	Hedge Reserve	Retained Earnings	Total Equity
Balance at December 31, 2014		\$ 490,363	\$ 7,476	\$ 20,950	\$ 133	\$ 117,558	\$ 636,480
Net loss:		-	-	-	-	(30,386)	(30,386)
Other comprehensive income (loss):							
Foreign currency translation differences for foreign operations, net of tax		-	-	56,475	-	-	56,475
Defined benefit plan actuarial losses, net of tax	22	-	-	-	-	(629)	(629)
Loss in fair value of interest rate swaps	26	-	-	-	(71)	-	(71)
Contributions:							
Share issuance, net of share issue costs	4, 13(a)	63,196	-	-	-	-	63,196
Stock options	13(b)	-	189	-	-	-	189
Balance at December 31, 2015		553,559	7,665	77,425	62	86,543	725,254
Net earnings:		-	-	-	-	65,643	65,643
Other comprehensive income (loss):							
Foreign currency translation differences for foreign operations, net of tax		-	-	(7,851)	-	-	(7,851)
Defined benefit plan actuarial gains, net of tax	22	-	-	-	-	1,509	1,509
Loss in fair value of interest rate swaps	26	-	-	-	(51)	-	(51)
Contributions:							
Deferred income tax on share issue costs	13(a), 19	1,829	-	-	-	-	1,829
Stock options	13(b)	-	334	-	-	-	334
Balance at December 31, 2016		\$ 555,388	\$ 7,999	\$ 69,574	\$ 11	\$ 153,695	\$ 786,667

See accompanying notes to consolidated financial statements.

## Consolidated Statements of Cash Flows

(Expressed in thousands of Canadian Dollars)

Years ended December 31, 2016 and 2015

	Note	2016	2015
Cash provided by (used in):			
Operating activities:			
Net earnings (loss)		\$ 65,643	\$ (30,386)
Items not involving cash:			
Depreciation of plant and equipment	8	76,092	71,492
Depletion and amortization of timber, roads and other	9	34,895	37,478
Income tax expense (recovery)	19	7,207	(24,017)
Finance costs	16	18,602	17,569
Other assets		(217)	639
Reforestation liability	12	559	1,612
Other liabilities and provisions		789	(8,252)
Stock options	13(b)	334	189
Reversal of write-down of plant and equipment	18	-	(1,195)
Write-down of plant and equipment	8, 18	2,172	2,812
Unrealized foreign exchange losses (gains)		596	(337)
Other income	17	(14,095)	(758)
		192,577	66,846
Cash generated from (used in) operating working capital:			
Trade accounts receivable and other		(2,666)	8,748
Inventories		(2,338)	48,717
Prepayments and other		704	3,017
Trade accounts payable and accrued liabilities		11,702	(24,986)
Income taxes paid		(707)	(965)
		199,272	101,377
Investing activities:			
Additions to property, plant and equipment	8	(50,393)	(93,832)
Additions to logging roads	9	(24,631)	(26,133)
Additions to timber and other intangible assets	9	(1,682)	(1,500)
Acquisitions	4	-	(223,263)
Proceeds on disposal of property, plant and equipment	5, 17	41,437	12,509
Proceeds on disposal of investments	17	10,342	-
Investments and other assets		(11,324)	(1,033)
		(36,251)	(333,252)
Financing activities:			
Issuance of capital stock, net of share issue expenses	4, 13(a)	-	63,196
Interest payments		(17,174)	(16,186)
Debt refinancing costs		(1,112)	(292)
Change in operating line components of long term debt	10	(11,663)	10,057
Additions to long term debt	10	56,974	362,582
Repayments of long term debt	10	(189,193)	(189,691)
		(162,168)	229,666
Foreign exchange gain on cash and cash equivalents held in a foreign currency		1,961	799
Increase (decrease) in cash and cash equivalents		2,814	(1,410)
Cash and cash equivalents, beginning of year		16,456	17,866
Cash and cash equivalents, end of year		\$ 19,270	\$ 16,456

See accompanying notes to consolidated financial statements.

**1. Nature of operations:**

Interfor Corporation and its subsidiaries (the "Company" or "Interfor") produce wood products in British Columbia, the U.S. Northwest and the U.S. South for sale to markets around the world.

Interfor Corporation exists under the *Business Corporations Act* (British Columbia) with shares listed on the Toronto Stock Exchange. Its head office, principal address and records office are located at Suite 3500, 1055 Dunsmuir Street, Vancouver, British Columbia, Canada, V7X 1H7.

These consolidated financial statements of the Company as at and for the years ended December 31, 2016 and 2015 comprise the accounts of Interfor Corporation and its subsidiaries.

**2. Basis of Preparation:**

## (a) Statement of compliance:

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and were approved by the Board of Directors on February 09, 2017.

## (b) Basis of measurement:

These consolidated financial statements have been prepared on the historical cost basis except for the following material items in the Statements of Financial Position:

- (i) Liabilities for cash-settled share-based payment arrangements are measured at fair value; and
- (ii) Employee benefit plan assets and liabilities are recognized as the net of the fair value of the plan assets and the present value of the defined benefit obligations on a plan by plan basis.

## (c) Functional and presentation currency:

These consolidated financial statements are presented in Canadian Dollars, which is the parent company's functional currency. Certain of the Company's subsidiaries have a functional currency of the U.S. Dollar and are translated to Canadian Dollars. All financial information presented in Canadian Dollars has been rounded to the nearest thousand except number of shares and per share amounts.

## (d) Use of estimates and judgements:

The preparation of these consolidated financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of certain assets, liabilities, revenues and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized, on a prospective basis, in the period in which the estimates are revised.

## 2. Basis of Preparation (continued):

### (d) Use of estimates and judgements (continued):

Significant areas requiring the use of management estimates relate to the determination of restructuring, reforestation, road deactivation, environmental and tax obligations, share-based compensation, recoverability of assets, rates for depreciation, depletion and amortization, fair values of assets and liabilities acquired in business combinations and impairment analysis of non-financial assets including goodwill.

Information about the use of management estimates that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the following notes:

<i>Note 3(e)</i>	Inventories
<i>Note 3(f)</i>	Assets held for sale
<i>Note 3(j)</i>	Impairment of non-financial assets
<i>Note 3(k)</i>	Reforestation and other decommissioning provisions
<i>Note 3(n)</i>	Cash-settled share based compensation
<i>Note 3(o)</i>	Equity-settled share based compensation
<i>Note 4</i>	Acquisitions
<i>Note 9</i>	Roads and bridges, timber tenures, other intangible assets and goodwill
<i>Note 12</i>	Reforestation liability

## 3. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

### (a) Basis of consolidation:

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries from their respective dates of acquisition or incorporation. All intercompany balances, including unrealized income and expenses arising from intercompany transactions have been eliminated upon consolidation.

The Company measures goodwill in business acquisitions at the acquisition date as the fair value of the consideration transferred including any non-controlling interest less the fair value of the identifiable assets acquired and liabilities assumed, all measured as of the acquisition date. When the excess is negative, a bargain purchase gain is recognized immediately in Net earnings. Transaction costs, other than those associated with the issuance of debt or equity securities, are expensed as incurred.

### (b) Foreign currency:

#### (i) Foreign currency transactions:

Transactions in foreign currencies are translated to the functional currency of the respective entity at transaction date exchange rates. Monetary assets and liabilities denominated in foreign currencies are revalued using the exchange rate at the reporting date.

**3. Significant accounting policies (continued):**

## (b) Foreign currency (continued):

## (i) Foreign currency transactions (continued):

Foreign exchange differences arising on revaluation are recognized in Net earnings. Where revaluations relate to trade accounts receivables those foreign exchange differences are adjusted to Sales in the Statement of Earnings; where revaluations relate to trade accounts payables those foreign exchange differences are adjusted to Production costs in the Statement of Earnings.

## (ii) Foreign operations:

Certain of the Company's subsidiaries have a functional currency of the U.S. Dollar. Revenues and expenses of such foreign operations are translated to Canadian Dollars at the transaction date exchange rate, or at average rates for the period which approximate the transaction date, as appropriate. Assets and liabilities are translated into Canadian Dollars at exchange rates in effect at the reporting date. Related foreign currency translation differences are recognized in Other comprehensive income, and recorded to the Translation reserve in Equity.

Foreign currency translation differences residing in the Translation reserve will be released to Net earnings upon the reduction of the net investment in foreign operations through the sale, reduction or substantial liquidation of an investment position.

Monetary receivables from a foreign operation, the settlement of which are neither planned nor likely in the foreseeable future are considered to form part of the net investment in the foreign operation. Related foreign exchange translation differences are recognized in Other comprehensive income and presented in the Translation reserve in Equity.

## (iii) Hedge of net investment in a foreign operation:

Financial liabilities denominated in foreign currencies are from time to time designated as a hedge of the Company's net investments in foreign operations.

Foreign currency differences arising on the revaluation of a financial liability designated as a hedge of a net investment in a foreign operation are recognized in Foreign currency translation differences in Other comprehensive income to the extent that the hedge is effective, and presented in the Translation reserve in Equity. To the extent that the hedge is ineffective, such differences are recognized in Other foreign exchange gain (loss) in Net earnings.

When the Company terminates the designation of the hedging relationship and discontinues its use of hedge accounting, any accumulated unrealized foreign exchange differences remaining in the Translation reserve and subsequent unrealized foreign exchange differences are recorded in Other foreign exchange gain (loss) in Net earnings. When the hedged net investment is disposed of, the relevant amount in the Translation reserve is reclassified to Net earnings.

### 3. Significant accounting policies (continued):

(c) Financial instruments:

(i) Non-derivative financial instruments:

Non-derivative financial instruments comprise cash and cash equivalents, trade and other receivables, certain investments and advances, trade accounts payable and accrued liabilities, provisions, and loans and borrowings including long term debt.

Cash and cash equivalents and trade and other receivables are designated as loans and receivables and are initially measured at fair value plus any direct transaction costs and thereafter at amortized cost using the effective interest rate method, less any impairment losses.

Certain investments are classified as held for trading and are measured at fair value.

Trade payables and accrued liabilities, provisions, and loans and borrowings including long term debt are designated as other financial liabilities and are initially measured at fair value and thereafter at amortized cost using the effective interest rate method.

There are no financial instruments classified as held-to-maturity.

(ii) Derivative financial instruments:

The Company at times uses derivative financial instruments for economic hedging purposes in the management of foreign exchange and interest rate risks. The Company does not utilize derivative financial instruments for trading or speculative purposes.

The Company has chosen not to designate derivative foreign currency exchange contracts as hedges for accounting purposes. Consequently, these derivative financial instruments, designated as held-for-trading, are carried on the Statements of Financial Position at fair value, with changes in fair value being recorded in Other foreign exchange gain (loss) in Net earnings.

The Company at times holds derivative interest rate swaps to hedge its interest rate risk exposures and may designate these financial instruments as the hedging instrument in a cash flow hedge of fluctuations in market interest rates associated with specific drawings under its long term debt. The effective portion of changes in the fair value of the derivative are recognized in Other comprehensive income and presented in the Hedging reserve in Equity. Any ineffective portion of changes in the fair value of the derivative is recognized immediately in Net earnings.

(iii) Share capital:

Shares are classified as equity. Incremental costs directly attributable to the issuance of Shares and share options are recognized as a deduction from equity, net of any tax effects.

(d) Cash and cash equivalents:

Cash and cash equivalents consist of cash on deposit and short-term interest bearing securities with maturities at their purchase date of three months or less.

**3. Significant accounting policies (continued):****(e) Inventories:**

Lumber inventories are valued at the lower of cost and net realizable value on a specific product basis. Cost is determined as the weighted average of cost of production on a three month rolling average, lagged by one month and adjusted for abnormal costs, as in the case of a curtailment. Net realizable value is the estimated selling price in the normal course of business, less estimated costs of completion and selling expenses.

Log inventories are valued at the lower of cost and net realizable value on a specific boom basis where logs are boomed, or in aggregate on a species and sort basis where the logs are not boomed.

Cost for internally produced log inventories is determined as the weighted average cost of logging on a twelve month rolling average, lagged by one month, for the B.C. Coast and on a three month rolling average for the B.C. Interior, and adjusted for abnormal costs, as in the case of a curtailment. Log inventories purchased from external sources are valued at acquisition cost.

Net realizable value of logs is based on either market replacement cost or, for logs designated for lumber processing, on estimated net realizable value less estimated costs of completion and selling expenses.

Other inventories consist primarily of supplies which are recorded at lower of cost and replacement cost, which approximates net realizable value.

**(f) Assets held for sale:**

Non-current assets, or disposal groups comprising assets and liabilities, are classified as held-for-sale if available for immediate sale and if it is highly probable that their carrying amount will be recovered primarily through sale rather than through continuing use.

Such assets, or disposal groups, are measured at the lower of their carrying amount and fair value less costs to sell. Any impairment loss on a disposal group is allocated first to goodwill, and then to the remaining assets and liabilities on a pro rata basis, except that losses are not allocated to inventories, financial assets, deferred tax assets or employee benefit assets, which continue to be measured in accordance with the Company's other accounting policies. Impairment losses on initial classification as held for sale and subsequent gains and losses on remeasurement are recognized in Net earnings.

Once classified as held for sale, intangible assets and property, plant and equipment are no longer amortized or depreciated.

**(g) Property, plant and equipment:**

Property, plant and equipment are recorded at cost less accumulated depreciation and impairment losses. Depreciation on machinery and equipment is provided on the basis of hours operated relative to the asset's lifetime estimated operating hours.

Depreciation on all other assets is provided on a straight-line basis (ranging from 2.5% to 33% per year) over the estimated useful lives of the assets.

Depreciation methods, useful lives and residual values are reviewed annually and adjusted, if appropriate.



**3. Significant accounting policies (continued):**

## (g) Property, plant and equipment (continued):

Maintenance costs are recorded as expenses as incurred, with the exception of programs that extend the useful life of an asset or increase its value, for which costs are capitalized.

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, being those requiring a substantial period of time prior to availability for their intended use, are capitalized.

## (h) Logging roads and bridges:

Logging roads and bridges are recorded at cost less accumulated amortization and impairment losses. Road and bridge amortization is computed on the basis of timber cut relative to available timber.

Amortization methods, useful lives and residual values are reviewed annually and adjusted, if appropriate.

## (i) Intangible assets:

## (i) Timber licences:

Timber licences are recorded at cost less accumulated depletion and impairment losses. Timber licence depletion is computed on the basis of timber cut relative to available timber. Tree farm and forest licences are depleted on a straight-line basis over 40 years. Amortization rates are reviewed annually to ensure they are aligned with estimates of remaining economic useful lives of the associated intangible assets.

## (ii) Goodwill:

Goodwill is measured at cost less accumulated impairment losses. See Note 3(a) for the policy on measurement of goodwill at initial recognition.

## (iii) Other intangible assets:

Other intangible assets are recorded at cost less accumulated amortization and impairment losses. Amortization on other intangible assets is provided on a straight-line basis ranging from five to ten years, being the estimated useful lives of the assets. Amortization rates are reviewed annually to ensure they are aligned with estimates of remaining economic useful lives of the associated intangible assets.

## (j) Impairment of non-financial assets:

The Company's non-financial assets are reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. Impairment tests are carried out annually for goodwill or when an indicator of impairment is identified.

External indicators of impairment include adverse changes in expected future prices, costs and other market and economic factors. Internal indicators include changes in the expected useful life of an asset or changes to the planned capacity of an asset.

An impairment loss is charged to Net earnings if an asset's carrying amount exceeds its recoverable amount. The recoverable amount is calculated based on the higher of its fair value less direct costs to sell and its value in use.

### 3. Significant accounting policies (continued):

(j) Impairment of non-financial assets (continued):

Fair value is determined as the amount that would be obtained from the sale, net of direct selling costs, of the asset in an arm's length transaction between knowledgeable and willing parties. Value in use is determined as the present value of the estimated future cash flows expected to arise from the continued use of the asset in its present form and its eventual disposal and does not consider future capital enhancements.

For purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash inflows that are largely independent of the cash inflows from other assets or groups of assets (cash generating units or "CGU"). Goodwill is allocated to CGU's or groups of CGU's expected to benefit from it.

Impairment losses recognized for a CGU are first allocated to reduce the carrying amount of goodwill, if any, assigned to the CGU, and then to reduce the carrying amounts of the other assets in the CGU on a pro-rata basis.

Non-financial assets, other than goodwill, for which an impairment was previously recognized, 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 the impairment never been recognized.

An impairment loss recorded against goodwill is not reversed.

(k) Reforestation and other decommissioning provisions:

Forestry legislation in British Columbia requires the Company to incur the cost of reforestation on its forest, timber and tree farm licences and to deactivate logging roads once harvesting is complete and access is no longer required. Accordingly, the Company records the fair value of the costs of reforestation and road deactivation in the period in which the timber is cut, with the fair value of the liability determined with reference to the present value of estimated future cash flows.

Provisions are measured at the expected value of future cash flows, discounted to their present value and determined according to the probability of alternative estimates of cash flows occurring for each operation. The measurement under IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, is based on best estimates and can be based on internal or external costs, depending upon which is most likely. Significant judgements and estimates are involved in forming expectations of future activities and the amount and timing of the associated cash flows. Those expectations are formed based on existing regulatory requirements and the expertise of Registered Professional Foresters and Engineers employed or contracted by the Company. Examples of considerations include the specifics of the areas logged and the treatments prescribed for those areas, as well as the timing and success rates of the planned activities in terms of reforestation; and road structure and terrain for road deactivation.

Discount rates reflect the risks specific to the decommissioning provision. Adjustments are made to decommissioning provisions each period for changes in the estimated timing or amount of cash flows, changes in the discount rate and the unwinding of the discount. As such, the discount rate reflects the current risk-free rate given that risks are incorporated into the future cash flow estimates.

### 3. Significant accounting policies (continued):

(k) Reforestation and other decommissioning provisions (continued):

In periods subsequent to the initial measurement, changes in the liability resulting from the passage of time are recognized as Finance costs and revisions to fair value calculations are recognized as Production costs in Net earnings as they occur.

(l) Environmental costs:

Environmental expenditures are expensed or capitalized depending upon their future economic benefit. Expenditures to prevent future environmental contamination are capitalized as plant and equipment. Expenditures that relate to an existing condition caused by past operations are expensed. Liabilities are recorded when rehabilitation efforts are likely to be required and the costs can be reasonably estimated.

Provisions are measured at the expected value of future cash flows, discounted to their present value and determined according to the probability of alternative estimates of cash flows using a current risk-free rate. The unwinding of the discount is recognized as a Finance cost in Net earnings.

(m) Employee benefits:

Defined benefit pension and other post-retirement benefit obligation accruals are estimated using actuarial methods and assumptions, including management's best estimates of the discount rate, salary escalation, and health care costs and are calculated using the projected unit credit method.

Plan assets are valued at fair value.

Actuarial gains and losses arise from actual experience being different from the assumptions, or changes in actuarial assumptions used to determine the defined benefit asset or obligation, are recognized in Other comprehensive income in the year in which they occur.

Pension expenses for defined contribution plans are limited to the Company's contribution to the plans in respect of services rendered by employees, as the Company has no legal or constructive obligation to pay further amounts. Plans administered by the government and the industry-wide unionized employees' pension plan are treated as defined contribution plans.

(n) Cash-settled share based compensation:

The Company has a Share Appreciation Rights ("SAR") Plan, a Deferred Share Unit ("DSU") Plan and a Total Shareholder Return ("TSR") Plan for directors, officers and certain other eligible employees. The Company uses the fair value method of accounting for obligations under the SAR, DSU and TSR Plans.

Compensation expense is recorded for SARs over the vesting period based on the estimated fair value of the SARs at the date of grant. Fair value is measured using a Black-Scholes option pricing model and is adjusted to reflect the number of SARs expected to vest.

Compensation expense is recorded for DSUs either at the time of the grant, in the case of DSUs which vest immediately, or over the performance period, in the case of DSUs with deferred vesting, based on the fair value at the date of the grant.

**3. Significant accounting policies (continued):**

## (n) Cash-settled share based compensation (continued):

Compensation expense is recorded for TSRs over the performance period based on the estimated fair value of the TSRs at the date of the grant. Fair value is measured using a combination of call options which are valued using a Black-Scholes pricing model.

The fair value of the SARs, DSUs and TSRs are subsequently measured at each reporting date with any changes in fair value reflected in the Long term incentive compensation expense in Net earnings. Liabilities are recorded in Trade accounts payable and provisions and Provisions and other liabilities on the Statements of Financial Position.

## (o) Equity-settled share based compensation:

The Company has a Stock Option Plan for its key employees and directors. The Company uses the fair value method of accounting for obligations under this Plan.

The grant-date fair value of options is recognized as an incentive compensation expense, with a corresponding increase in contributed surplus, over the vesting period. The fair value of the options is determined using the Black-Scholes option pricing model which takes into account, as of the grant date, the exercise price, the expected life of the options, the current price of the underlying stock and its expected volatility, expected dividends on the shares, and the risk-free interest rate over the expected life of the option. Cash consideration received from employees when they exercise the options is credited to share capital, as is the previously calculated fair value included in contributed surplus.

## (p) Sales revenue:

The Company recognizes sales when the product is shipped and title passes. Sales are recorded on a gross basis, including amounts charged to customers for freight, wharfage and handling costs. Actual costs of export taxes, freight, wharfage and handling are recorded to Export taxes and Production, respectively, in Net earnings.

## (q) Finance income and costs:

Finance income comprises net interest income on funds invested.

Finance costs comprise net interest expense on borrowings, the unwinding of the discount on decommissioning provisions, net interest on defined benefit plans, the amortization of prepaid finance costs and other related transaction costs.

## (r) Income tax:

Income tax expense comprises current and deferred income taxes. Current and deferred income taxes are recognized in Net earnings except to the extent that they relate to a business combination, or 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 year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to income tax payable in respect of previous years.

### 3. Significant accounting policies (continued):

(r) Income tax (continued):

Deferred income tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for taxation purposes. Deferred income tax is not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred income tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill.

Deferred income tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred income tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different taxable entities, but the intention is to settle current tax liabilities and assets on a net basis or tax assets and liabilities will be realized simultaneously.

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.

(s) Earnings per share:

Basic earnings per share is computed by dividing Net earnings by the weighted average number of common shares outstanding during the reporting period. Diluted earnings per share is determined by adjusting Net earnings and the weighted average number of common shares outstanding during the reporting period for the effects of all dilutive potential common shares, including outstanding stock options, if any.

(t) New standards and interpretations not yet adopted:

A number of new standards, and amendments to standards and interpretations, are not yet effective for the year ended December 31, 2016, and have not been applied in preparing these consolidated financial statements. The following pronouncements are considered by the Company to be the most significant of several pronouncements that may affect the financial statements.

IFRS 9, *Financial Instruments*, will replace the multiple classification and measurement models in IAS 39, *Financial Instruments: Recognition and Measurement*, with a single model that has only two classification categories: amortized cost and fair value. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted.

IFRS 15, *Revenue from Contracts with Customers*, will replace all existing IFRS revenue requirements and is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted.

### 3. Significant accounting policies (continued):

(t) New standards and interpretations not yet adopted (continued):

The Company is still in the process of assessing IFRS 9 and IFRS 15, but does not currently believe either will have a significant impact on its financial statements.

IFRS 16, *Leases*, eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Under the new standard, operating leases become an on-balance sheet liability that attracts interest, together with a corresponding right-of-use asset. In addition, lessees will recognize a front-loaded pattern of expense for most leases, even when cash rentals are constant. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. The Company has not yet completed an assessment of the impact of this standard on its financial statements.

### 4. Acquisitions:

In 2013, the Company acquired the Thomaston sawmill operations from Keadle Lumber Enterprises, Inc. ("Keadle"). Upon acquisition, the Company agreed to pay additional consideration of US\$7,000,000, contingent upon receipt of an upgrade to the air permit which allows the Company to operate a second shift. Approval was received on February 28, 2014, and a payment of \$8,743,000 was made on February 27, 2015.

On March 1, 2015, Interfor concluded the acquisition of sawmill operations in Meldrim, Georgia; Georgetown, South Carolina; Longview, Washington; and Tacoma, Washington from Simpson Lumber Company, LLC ("Simpson"), pursuant to an Asset Purchase Agreement ("APA") for total consideration of US\$146,088,000 (\$182,654,000).

Consideration per the APA included a series of future payments tied to the financial performance of the Tacoma sawmill with a minimum payment of US\$10,000,000. The Company recorded a discounted provision of US\$9,464,000 (\$11,833,000) in Provisions and other liabilities in the Consolidated Statements of Financial Position as part of the acquisition and recorded accretion expense of US\$476,000 in 2016 (2015 – US\$238,000) in Finance costs in Net earnings.

As at December 31, 2016, the provision of US\$10,000,000 was revalued at the year-end exchange rate to \$13,427,000 (2015 - US\$9,643,000 revalued at the year end exchange rate to \$13,345,000) and recorded in Trade accounts payable and provisions in the Consolidated Statement of Financial Position.

On June 19, 2015, Interfor concluded the acquisition of sawmill operations in Monticello, Arkansas from The Price Lumber Company, Inc. ("Monticello"), for total consideration of US\$35,627,000 (\$43,699,000).

**4. Acquisitions (continued):**

These acquisitions have been accounted for as business combinations and the value of the consideration transferred was allocated as follows:

	Note	Simpson	Monticello	Keadle	Total
Net assets acquired:					
Current assets		\$ 57,661	\$ 2,900	\$ -	\$ 60,561
Property, plant and equipment	8	129,227	40,846	-	170,073
		186,888	43,746	-	230,634
Current liabilities assumed		(4,234)	(47)	-	(4,281)
		\$ 182,654	\$ 43,699	\$ -	\$ 226,353
Consideration funded by:					
Cash		\$ -	\$ -	\$ 8,743	\$ 8,743
Revolving Term Loan	10(a)	107,625	43,675	-	151,300
Current liabilities		-	24	-	24
Cash consideration from Common Share issuance	13(a)	63,196	-	-	63,196
Cash consideration		170,821	43,699	8,743	223,263
Contingent future payments	11	11,833	-	-	11,833
Provisions and other liabilities	11	-	-	(8,743)	(8,743)
		\$ 182,654	\$ 43,699	\$ -	\$ 226,353

Transaction costs of \$2,105,000 related to the acquisitions were included in Selling and administration expenses in Net earnings in 2015.

For the period of March 1 to December 31, 2015, Simpson and Monticello contributed sales of \$183,502,000 and a net loss of \$31,564,000 to the Company's results, including a \$13,238,000 net loss at the Tacoma sawmill. If the acquisitions had occurred on January 1, 2015, management estimates that Sales and Net loss for 2015 would have been \$1,745,323,000 and \$37,753,000, respectively. In determining these amounts, management has assumed that the fair value adjustments that arose on the acquisition dates would have been the same if the acquisitions had occurred on January 1, 2015.

**5. Assets held for sale:**

	2016	2015
Opening balance	\$ 27,836	\$ -
Additions	-	26,239
Impairment	(1,018)	-
Disposals	(25,947)	-
Exchange rate movements	(871)	1,597
Ending Balance	\$ -	\$ 27,836

On July 30, 2015, the Company announced a plan to exit its sawmilling operation located in Tacoma, Washington and classified US\$20,113,000 of the Tacoma sawmill property and buildings as assets held for sale (note 8).

On December 22, 2015, the Company entered into a purchase and sales agreement to sell the remaining real estate assets, subject to customary closing conditions. The sale of the Tacoma property was completed on November 30, 2016 for net proceeds of \$40,830,000 (note 17) and on January 13, 2017, the minimum contingent amount of US\$10,000,000 (note 4) was paid to Simpson, with no further amounts due. US\$900,000 was paid into escrow to be used for environmental remediation, if required. Any unused funds as at November 30, 2021, if any, will be returned to the Company and recognized as additional proceeds at that time.

**6. Inventories:**

	2016	2015
Logs	\$ 80,726	\$ 69,980
Lumber	58,739	69,046
Other	15,070	16,714
	\$ 154,535	\$ 155,740

Inventory expensed in the period includes production costs, depreciation of plant and equipment, and depletion and amortization of timber, roads and other. The inventory write-down to record inventory at the lower of cost and net realizable value at December 31, 2016, was \$7,922,000 (2015 - \$11,961,000).



**7. Other investments and assets:**

	2016	2015
Investments designated as fair value through profit and loss	\$ 2,911	\$ 1,528
Deferred financing fees, net of accumulated amortization	2,078	1,663
Timber deposits and other	263	-
	<b>\$ 5,252</b>	<b>\$ 3,191</b>
Current	\$ 2,911	-
Long term	2,341	3,191
	<b>\$ 5,252</b>	<b>\$ 3,191</b>

## Notes to Consolidated Financial Statements

Years ended December 31, 2016 and 2015

(Tabular amounts expressed in thousands of Canadian dollars, except number of shares and per share amounts)

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### 8. Property, plant and equipment:

Cost	Note	Land	Buildings	Machinery and Equipment	Mobile Equipment	Computer Equipment	Site Improvements	Other	Projects in Process	Total
Balance at December 31, 2014		\$ 41,401	\$ 95,872	\$ 644,288	\$ 27,891	\$ 28,324	\$ 56,470	\$ 10,574	\$ 12,415	\$ 917,235
Additions		1,772	424	6	16	2,124	320	4,777	86,671	96,110
Acquisitions		30,485	16,199	99,549	1,844	6,152	2,723	186	12,935	170,073
Disposals		(643)	(5,873)	(30,868)	(1,936)	(4,317)	(1,803)	(957)	-	(46,397)
Transfers		334	15,194	65,936	2,157	5,471	6,974	(1,228)	(95,992)	(1,154)
Reclassification to assets held for sale	5	(25,066)	(1,044)	-	(1)	-	(23)	(135)	-	(26,269)
Exchange rate movements		3,667	10,359	81,701	2,034	3,807	5,071	741	2,357	109,737
Balance at December 31, 2015		\$ 51,950	\$ 131,131	\$ 860,612	\$ 32,005	\$ 41,561	\$ 69,732	\$ 13,958	\$ 18,386	\$ 1,219,335
Additions		-	-	(2)	-	133	-	23	49,142	49,296
Disposals		(64)	(150)	(2,396)	(740)	(860)	-	(304)	(100)	(4,614)
Transfers		-	4,771	19,368	351	3,505	1,706	23	(31,361)	(1,637)
Exchange rate movements		(578)	(2,102)	(16,039)	(414)	(626)	(1,000)	(139)	(436)	(21,334)
Balance at December 31, 2016		\$ 51,308	\$ 133,650	\$ 861,543	\$ 31,202	\$ 43,713	\$ 70,438	\$ 13,561	\$ 35,631	\$ 1,241,046
Accumulated Depreciation			Buildings	Machinery and Equipment	Mobile Equipment	Computer Equipment	Site Improvements	Other		Total
Balance at December 31, 2014			\$ 39,754	\$ 268,445	\$ 15,004	\$ 20,161	\$ 27,225	\$ 5,268		\$ 375,857
Depreciation			5,926	50,076	3,793	5,351	4,748	1,598		71,492
Disposals			(4,991)	(25,048)	(1,487)	(4,294)	(1,816)	(957)		(38,593)
Transfers			138	(592)	(3)	349	1,694	(1,586)		-
Impairment			37	2,775	-	-	-	-		2,812
Reversal of impairment			-	(1,195)	-	-	-	-		(1,195)
Reclassification to assets held for sale	5		(23)	-	(1)	-	-	(6)		(30)
Exchange rate movements			2,848	23,691	805	2,072	1,796	190		31,402
Balance at December 31, 2015			\$ 43,689	\$ 318,152	\$ 18,111	\$ 23,639	\$ 33,647	\$ 4,507		\$ 441,745
Depreciation			6,796	53,527	3,276	6,072	5,003	1,418		76,092
Disposals			(86)	(1,564)	(596)	(677)	-	(284)		(3,207)
Transfers			-	(27)	-	27	-	-		-
Impairment			-	1,154	-	-	-	-		1,154
Exchange rate movements			(463)	(4,389)	(162)	(344)	(329)	(32)		(5,719)
Balance at December 31, 2016			\$ 49,936	\$ 366,853	\$ 20,629	\$ 28,717	\$ 38,321	\$ 5,609		\$ 510,065
Net book value at										
December 31, 2015		\$ 51,950	\$ 87,442	\$ 542,460	\$ 13,894	\$ 17,922	\$ 36,085	\$ 9,451	\$ 18,386	\$ 777,590
December 31, 2016		51,308	83,714	494,690	10,573	14,996	32,117	7,952	35,631	730,981

There were no borrowing costs capitalized in 2016 (2015 - \$477,000). Additions in 2016 include \$2,912,000 of accrued contract costs (2015 - \$4,009,000; 2014 - \$1,731,000).

**9. Roads and bridges, timber tenures, other intangible assets and goodwill:**

Cost	Note	Roads and Bridges	Timber Licences	Other Intangibles	Goodwill
Balance at December 31, 2014		\$ 69,400	\$ 129,353	\$ 33,419	\$ 137,873
Additions		26,133	589	911	-
Transfers		-	-	1,154	-
Disposals		(832)	(11,508)	(137)	-
Exchange rate movements		341	-	4,922	23,918
Balance at December 31, 2015		95,042	118,434	40,269	161,791
Additions		24,631	195	1,487	-
Transfers		-	-	1,637	-
Disposals		(824)	-	(18)	-
Exchange rate movements		(69)	-	(916)	(4,412)
Balance at December 31, 2016		\$ 118,780	\$ 118,629	\$ 42,459	\$ 157,379
Accumulated amortization		Roads and Bridges	Timber Licences	Other Intangibles	Goodwill
Balance at December 31, 2014		\$ 47,156	\$ 50,329	\$ 9,022	\$ 877
Amortization		27,285	3,891	6,302	-
Disposals		(178)	(8,215)	(137)	-
Exchange rate movements		168	-	1,481	-
Balance at December 31, 2015		74,431	46,005	16,668	877
Amortization		24,478	3,351	7,066	-
Disposals		(824)	-	(6)	-
Exchange rate movements		(44)	-	(286)	-
Balance at December 31, 2016		\$ 98,041	\$ 49,356	\$ 23,442	\$ 877
Net book value at					
December 31, 2015		\$ 20,611	\$ 72,429	\$ 23,601	\$ 160,914
December 31, 2016		20,739	69,273	19,017	156,502

For the purpose of impairment testing, goodwill components of \$13,078,000 and \$143,424,000 are attributable to the Coastal Whitewood cash-generating unit ("CWW CGU") and the U.S. Southeast cash-generating units ("SE CGU's"), respectively.

The recoverable amounts for the goodwill impairment assessments were based on the CGU's (or groups of CGU's) value in use and were determined by discounting the future cash flows generated from the continuing use of the units for a period of twenty years. The cash flows were projected based on past experience, actual operating results and the five year business plan in the assessment for both 2015 and 2016. Due to the cyclical nature of the forest industry, cash flows for a further 15 years were extrapolated based on an average trend year.

The recoverable amount of both the CWW CGU and the SE CGU as at December 31, 2016, and December 31, 2015 were determined to be higher than the related carrying amount and no impairment has been recognized.

## 9. Roads and bridges, timber tenures, other intangible assets and goodwill (continued):

Key assumptions used are based on industry sources, including Forest Economic Advisors, LLC, as well as management estimates. These assumptions include lumber and residual chip sales prices, applicable foreign exchange rates, operating rates of the assets, raw material and conversion costs, the level of sales to the U.S. from Canada, the export tax rate and the future capital required to maintain the assets in their current operating condition.

A post-tax discount rate of 10.5 percent (2015 – 10.5 percent) was applied in determining the recoverable amount of each CGU assessed. The discount rate was estimated with the assistance of external experts, past experience, and the industry average weighted average cost of capital. An inflation rate of 1.3 percent (2015 – 1.0 percent) is applied to the projected cash flows for years four through twenty.

The values assigned to key assumptions represent management's assessment of future trends in the forest industry and are based on both external sources and internal historical data.

## 10. Cash and borrowings:

	Operating Line	Revolving Term Line	Senior Secured Notes	U.S. Operating Line	Total
2016					
Available line of credit	\$ 65,000	\$ 200,000	\$ 268,540	\$ 67,135	\$ 600,675
Maximum borrowing available	65,000	200,000	268,540	65,627	599,167
Drawings	-	40,281	268,540	-	308,821
Outstanding letters of credit included in line utilization	10,026	-	-	3,296	13,322
Unused portion of line	\$ 54,974	\$ 159,719	\$ -	\$ 62,331	\$ 277,024
2015					
Available line of credit	\$ 65,000	\$ 200,000	\$ 276,800	\$ 69,200	\$ 611,000
Maximum borrowing available	62,820	183,723	276,800	69,200	592,543
Drawings	-	179,920	276,800	12,039	468,759
Outstanding letters of credit included in line utilization	9,396	-	-	2,290	11,686
Unused portion of line	\$ 53,424	\$ 3,803	\$ -	\$ 54,871	\$ 112,098

Minimum principal amounts due on long term debt are follows:

2017	\$ -
2018	-
2019	40,281
2020	-
2021	44,756
Thereafter	223,784
	\$ 308,821

**10. Cash and borrowings (continued):**

## (a) Operating Line and Revolving Term Line:

The Canadian Operating Line of credit and Revolving Term Line ("the Lines") may be drawn in either CAD\$ or US\$ advances, and bear interest at bank prime plus a margin or, at the Company's option, at rates for Bankers' Acceptances or LIBOR based loans plus a margin, and in all cases dependent upon a financial ratio of total debt divided by trailing twelve months' trailing EBITDA<sup>1</sup>. The amount available under the Operating Line is subject to a borrowing base calculation dependent on certain accounts receivable and inventories.

The Lines are secured by a general security agreement which includes a security interest in all accounts receivable and inventories, charges against timber tenures and mortgage security on certain sawmills. The Lines are subject to certain financial covenants including a minimum working capital requirement, a maximum ratio of total debt to total capitalization and a minimum net worth calculation.

As at December 31, 2015, maximum borrowings available under the Company's Lines were restricted by a financial covenant in the underlying credit agreement. In the table above, this limitation has been applied to the Lines' limits. This restriction was removed based on changes to the agreement terms effective on February 9, 2016.

On February 9, 2016, the Company extended the maturity of the Lines from February 27, 2017 to May 19, 2019 and on September 22, 2016, further amended certain other terms.

As at December 31, 2016, the Lines were drawn by US\$30,000,000 (2015 - US\$130,000,000) revalued at the year end exchange rate to \$40,281,000 (2015 - \$179,920,000, and by \$10,026,000 (2015 - \$9,396,000) representing outstanding letters of credit.

All outstanding U.S. Dollar drawings under the Lines have been designated as a hedge against the Company's investment in its U.S. operations and foreign exchange gains of \$7,420,000 for the year ended December 31, 2016 (2015 - \$30,649,000 losses) arising on revaluation of the Lines were recognized in Foreign currency translation differences in Other comprehensive income.

As at December 31, 2016, \$214,693,000 (2015 - \$57,227,000) of available credit on the Lines was unused.

## (b) Senior Secured Notes:

The Company's Senior Secured Notes consist of Series A and Series B Senior Secured Notes (each \$US50,000,000 and bearing interest at 4.33% and 4.02%, respectively) and Series C Senior Secured Notes (US\$100,000,000, bearing interest at 4.17%). As at December 31, 2016, US\$200,000,000 of Senior Secured Notes were outstanding (2015 - US\$200,000,000) and revalued at the quarter-end exchange rate to \$268,540,000 (2015 - \$276,800,000).

<sup>1</sup> EBITDA represents earnings before interest, taxes, depreciation, depletion, amortization and non-cash asset revaluations as defined under the agreement.

**10. Cash and borrowings (continued):**

## (b) Senior Secured Notes (continued):

The Senior Secured Notes are subject to certain financial covenants including a minimum working capital requirement, a maximum ratio of total debt to total capitalization and a minimum net worth calculation. Total payments of US\$33,333,000 (US\$16,667,000 for each of the Series A and Series B Senior Secured Notes) are required on each of June 26, 2021 and 2022, with the balance due on June 26, 2023 for the Series A and B Senior Secured Notes. Payments of US\$33,333,000 are required on each of March 26, 2024 and 2025, with the balance due on March 26, 2026 for the Series C Senior Secured Notes. In conjunction with the modifications to the Operating Line and Revolving Term Line effective February 9, 2016, as per note 10(a), certain terms and conditions of the Senior Secured Notes were also modified. All other terms and conditions remained unchanged.

The Senior Secured Notes have been designated as a hedge against the Company's investment in its U.S. operations and unrealized foreign exchange gains of \$8,260,000 (2015 - \$32,760,000 losses) arising on their revaluation were recognized in Foreign currency translation differences in Other comprehensive income for the year ended December 31, 2016.

## (c) U.S. Operating Line:

The U.S. Operating Line bears interest at rates for LIBOR based loans plus a margin and is secured by accounts receivable and inventories of wholly-owned subsidiary, Interfor U.S. Inc. The U.S. Operating Line is subject to a minimum net worth covenant, with borrowing levels subject to a collateral calculation dependent upon certain accounts receivable and inventories. On June 15, 2016, the Company extended the maturity of its U.S. Operating Line from May 1, 2017 to May 1, 2018 with no other significant changes.

As at December 31, 2016, the U.S. Operating Line was drawn by US\$2,455,000 including outstanding letters of credit, revalued at the year-end exchange rate to \$3,296,000 (2015 - US\$10,354,000 revalued at the year-end exchange rate to \$14,330,000).

As at December 31, 2016, \$62,331,000 (US\$46,422,000) of the available U.S. Operating Line was unused (2015 - \$54,871,000, US\$39,647,000).

## (d) Cash and cash equivalents:

At December 31, 2016, \$515,000 of the Company's cash balances are restricted (2015 - \$1,299,000).

**11. Provisions and other liabilities:**

2016	Note	Current	Non-current	Total
Restructuring	11(a), 18	\$ 987	\$ 1,618	\$ 2,605
Road deactivation	11(a)	221	4,158	4,379
Environmental	11(a)	56	753	809
Cash-settled share based compensation				
SAR Plan	11(b)	5,904	385	6,289
TSR Plan	11(c)	1,188	1,625	2,813
DSU Plan	11(d)	1,515	9,468	10,983
Storm damage remediation funds	11(e)	220	236	456
Contingent future payment	4, 5	13,427	-	13,427
Retained compensation liabilities	11(f)	-	1,076	1,076
Lease incentives and other		1,075	1,971	3,046
		\$ 24,593	\$ 21,290	\$ 45,883
<hr/>				
2015	Note	Current	Non-current	Total
Restructuring	11(a), 18	\$ 494	\$ 1,681	\$ 2,175
Road deactivation	11(a)	392	3,776	4,168
Environmental	11(a)	56	770	826
Cash-settled share based compensation				
SAR Plan	11(b)	6,089	879	6,968
TSR Plan	11(c)	4,189	1,525	5,714
DSU Plan	11(d)	-	8,651	8,651
Storm damage remediation funds	11(e)	224	291	515
Contingent future payment	4, 5	13,345	-	13,345
Retained compensation liabilities	11(f)	2,665	40	2,705
Lease incentives and other		179	2,415	2,594
		\$ 27,633	\$ 20,028	\$ 47,661

The current portion of provisions and other liabilities is included in Trade accounts payable and provisions in the Statements of Financial Position.

**(a) Provisions:**

Forestry legislation in British Columbia requires the Company to deactivate logging roads once harvesting is complete and access is no longer required. Accordingly, the Company records the fair value of the costs of road deactivation in the period in which the timber is harvested, with the fair value of the liability determined with reference to the present value of estimated future cash flows.

Environmental provisions are made when rehabilitation efforts are likely required and the costs can be reasonably estimated.

Provisions are measured at the expected value of future cash flows, discounted to their present value and determined according to the probability of alternative estimates of cash flows using a current risk-free discount rate. The unwinding of the discount is recognized as a Finance cost in Net earnings.

**11. Provisions and other liabilities (continued):**

## (a) Provisions (continued):

Provisions are measured at the expected value of future cash flows, discounted to their present value and determined according to the probability of alternative estimates of cash flows using a current pre-tax discount rate that reflects the risks specific to the liability. The unwinding of the discount is recognized as a Finance cost in Net earnings.

	Note	Restructuring	Road deactivation	Environmental
Balance at December 31, 2014		\$ 2,125	\$ 4,051	\$ 828
Provisions made during year	18	4,131	346	-
Expenditures made during year		(4,556)	(218)	-
Unwind of discount		-	58	10
Changes in estimated future expenditures		-	(69)	(12)
Exchange rate movements		475	-	-
Balance at December 31, 2015		2,175	4,168	826
Provisions made during year	18	1,370	446	-
Expenditures made during year		(895)	(143)	-
Unwind of discount		-	46	8
Changes in estimated future expenditures		-	(138)	(25)
Exchange rate movements		(45)	-	-
Balance at December 31, 2016		\$ 2,605	\$ 4,379	\$ 809

## (b) Share Appreciation Rights Plan:

Awards under the SAR Plan have been granted to directors, officers and certain employees of the Company. The vesting of SARs occurs at a rate of 40% two years after granting and 20% per annum thereafter. SARs expire ten years after the date of grant. The SAR Plan uses notional units that are valued based on the Company's Common Share price on the Toronto Stock Exchange. The units are exercisable for cash and recorded as liabilities. Under the SAR Plan, awards will be expensed over the vesting periods based on the estimated fair value of the SARs at the date of grant. Fair value is measured using a Black-Scholes option pricing model and is adjusted to reflect the number of SARs expected to vest. Fair value of the SARs is subsequently measured at each reporting date with any change in fair value resulting in a change in the measure of the compensation for the award, which is amortized over the remaining vesting periods.



**11. Provisions and other liabilities (continued):**

## (b) Share Appreciation Rights Plan (continued):

Details of the Company's SAR Plan for the years ended December 31, 2016 and 2015 are as follows:

	2016		2015	
	Units	Weighted average strike price	Units	Weighted average strike price
Outstanding, beginning of year	929,808	\$ 7.52	1,113,953	\$ 7.35
Granted	6,053	15.01	-	-
Exercised	(173,800)	4.96	(149,100)	5.77
Expired or cancelled	(23,862)	12.63	(35,045)	9.52
Outstanding, end of year	738,199	\$ 8.02	929,808	\$ 7.52
Units exercisable, end of year	533,389	\$ 6.73	509,250	\$ 5.03

Weighted average fair value assumptions for grants made in 2016 and 2015 are as follows:

	2016	2015
Risk-free interest rate	0.87%	-
Expected life	6.7 years	-
Annualized volatility	41%	-
Dividend rate	0%	-
Termination rate	6%	-
Grant date fair value	\$15.01	-

Details of units outstanding under the SAR Plan at December 31, 2016 are as follows:

Strike price	Units outstanding			Units exercisable	
	Number outstanding, December 31, 2016	Weighted average remaining unit life (yrs)	Weighted average strike price	Number exercisable, December 31, 2016	Weighted average strike price
\$1.38-\$4.64	212,250	4.1	\$ 3.64	168,950	\$ 3.39
\$4.77-\$5.40	109,000	2.6	4.92	108,000	4.91
\$6.01-\$8.02	104,300	3.6	6.18	104,300	6.18
\$9.18-\$17.43	312,649	6.4	12.69	152,139	12.12
	738,199		\$ 8.02	533,389	\$ 6.73

For the year ended December 31, 2016, the Company recorded a Long term incentive compensation expense in respect of the SAR Plan of \$1,010,000 (2015 - recovery of \$4,730,000).

**11. Provisions and other liabilities (continued):**

## (c) Total Shareholder Return Plan:

Under terms of the TSR Plan, a participant will receive a target number of performance share units ("PSUs") based on a target award divided by the value of the Company's Common Shares at the effective date of the grant. The number of PSUs which will ultimately vest will be in a range from 50% to 150% of the original grant based on total shareholder return over a three year performance period.

The number of PSU's outstanding at December 31, 2016 and 2015 are as follows:

	2016	2015
Outstanding, beginning of year	518,199	709,214
Granted	237,497	144,975
Matured	(209,647)	(335,990)
Cancelled	-	-
Outstanding, end of year	546,049	518,199

Compensation expense is recorded for the TSR Plan over the performance period based on the estimated fair value of the TSR Plan payable at the date of the grant. The fair value of obligations under the TSR Plan is subsequently measured at each reporting date with any changes in fair value reflected in Long term incentive compensation expense in Net earnings.

Fair value of the TSR Plan is measured using a combination of call options which are valued using a Black-Scholes pricing model with weighted average assumptions for grants as follows:

	2016	2015
Risk-free interest rate	0.8%	0.9%
Expected life	3 years	3 years
Annualized volatility	46% to 56%	47% to 56%
Dividend rate	0.00%	0.00%
Termination rate	0.00%	0.00%
Grant date fair value	\$1,532	\$2,340

For the year ended December 31, 2016, the Company recorded Long term incentive compensation expense under the TSR Plan of \$1,289,000 (2015 - \$655,000).

## (d) Deferred Share Unit Plan:

The Company's directors and certain officers participate in the DSU Plan. The DSU Plan, which allows for immediate or deferred vesting, is intended to provide a better link between share performance and compensation for the participants, in that DSUs either increase or decrease in value in a direct relationship with the market price of the Company's Common Shares.

DSUs may be granted directly to directors or officers of the Company at the discretion of the Board of Directors, who are required to take DSU's as payment of at least 60% of their annual retainer.

For performance periods ending prior to 2016, participants in the TSR Plan had the option to elect, subject to the approval of the Company's Board of Directors, to receive their award in DSUs at the end of the performance period.

**11. Provisions and other liabilities (continued):**

## (d) Deferred Share Unit Plan (continued):

The number of DSUs outstanding at December 31, 2016 and 2015 are as follows:

	2016		2015	
	Units	Average unit value	Units	Average unit value
Outstanding, beginning of year	622,951	\$14.06	551,249	\$21.27
Granted <sup>1</sup>	116,124	13.62	157,973	18.73
Exercised	(14,157)	11.67	(86,271)	21.91
Outstanding, end of year	724,918	\$15.15	622,951	\$14.06

<sup>1</sup>Fair value at the date of the grants.

Changes to the market value of the Company's Common Shares subsequent to issuance of awards results in adjustments to the compensation accrual and Long term incentive compensation expense in Net earnings. For the year ended December 31, 2016, the Company recorded an expense of \$1,775,000 (2015 - recovery of \$2,835,000) in respect of the DSU Plan, of which a \$916,000 expense (2015 - recovery of \$3,795,000) was recorded in Long term compensation and a \$860,000 expense (2015 - \$960,000), related to payment for director's fees, was recorded in Selling and administration.

## (e) Storm damage remediation funds:

In 2011, the Company settled with its insurers for recovery of certain losses relating to storm damage suffered in 2010. An amount of \$1,576,000 was set up as a provision for future remediation on roads and bridges. Under the terms of the insurance settlement, the insurance proceeds must be used for remediation. As at December 31, 2016, \$456,000 (2015 - \$515,000) of this provision remains unspent.

## (f) Retained compensation liabilities:

Upon acquisition of the Tolleson sawmills on March 17, 2014, the Company assumed incentive payments payable to certain senior management over a four year period. The incentive is earned and recognized as a liability over the incentive period. For the year ended December 31, 2016, the Company recorded a long term incentive compensation expense of \$1,029,000 (2015 - \$2,240,000) in respect of the retained compensation liabilities. The liability of US\$801,000 (2015 - US\$1,954,000) was revalued at the year-end exchange rate to \$1,076,000 (2015 - \$2,705,000).

**12. Reforestation liability:**

The Company has an obligation to reforest areas harvested under various timber rights. The obligation is incurred as logging occurs and the fair value of the liability for reforestation is determined with reference to the present value of estimated future cash flows required to settle the obligation.

Changes in the reforestation liability for the years ended December 31 are as follows:

	2016	2015
Reforestation liability, beginning of year	\$ 36,126	\$ 32,896
Reforestation expense on current logging and market logging agreements	12,605	12,888
Reforestation expenditures	(10,924)	(9,691)
Unwind of discount	302	360
Changes in estimated future reforestation expenditures	(569)	(327)
	<u>\$ 37,540</u>	<u>\$ 36,126</u>
Consisting of:		
Current reforestation liability	\$ 11,609	\$ 11,052
Long term reforestation liability	25,931	25,074
	<u>\$ 37,540</u>	<u>\$ 36,126</u>

The total undiscounted amount of the estimated future expenditures required to settle the reforestation obligation, adjusted for inflation, at December 31, 2016 is \$39,419,000 (2015 - \$37,848,000). The reforestation expenditures are expected to occur over the next one to fifteen years and have been discounted at a long term risk-free interest rate of 2% (2015 - 2%). Reforestation expense resulting from obligations arising from current logging and changes in estimated future expenditures are included in Production costs for the year and expense related to the unwinding of the discount is included in Finance costs.

**13. Share capital:**

(a) Share transactions:

Authorized capital at December 31, 2016 consists of:

- 150,000,000 Common Shares ("Shares") without par value; and
- 5,000,000 Preference Shares without par value.

Share transactions during 2016 and 2015 were as follows:

Issued and Fully Paid	Note	Number	Amount
Balance, December 31, 2014		66,730,455	490,363
Share issuance, net of share issue costs	4	3,300,000	63,196
Balance, December 31, 2015		70,030,455	553,559
Deferred income tax on share issue costs	19	-	1,829
Balance, December 31, 2016		70,030,455	\$ 555,388

**13.Share capital (continued):**

## (a) Share transactions (continued):

On January 27, 2015, the Company closed a bought deal public offering of subscription receipts (the "Subscription Receipts") through a syndicate of underwriters. The Company issued an aggregate of 3,300,000 Subscription Receipts (including 300,000 Subscription Receipts issued pursuant to the exercise of the over-allotment option) at a price of \$20.10 per Subscription Receipt, for cash proceeds, net of share issue costs, of \$63,196,000. In connection with the completion of the Simpson acquisition (note 4), each Subscription Receipt was exchanged, for no additional consideration, for one Common Share of the Company. The shares were issued on March 2, 2015.

At December 31, 2016, 1,631,740 Shares are reserved for possible future issuance pursuant to the stock option plan.

## (b) Equity-settled share based compensation:

The Company has a stock option plan for its key employees and directors under which options may be granted to purchase up to 1,631,740 Shares, of which 1,450,215 remain available for issuance. The vesting of the options occurs at a rate of 40% two years after granting and 20% per annum thereafter. Options expire ten years after the date of the grant. The exercise price of a stock option is at a price not less than the closing price of a Common Share on the trading day immediately preceding the grant date.

Details of the Company's stock option plan for the years ended December 31, 2016 and 2015 are as follows:

	2016		2015	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding, beginning of year	64,175	\$ 21.77	-	\$ -
Granted	130,879	10.61	78,926	21.85
Exercised	-	-	-	-
Expired or cancelled	(13,529)	16.76	(14,751)	22.22
Outstanding, end of year	181,525	\$ 14.10	64,175	\$ 21.77
Options exercisable, end of year	-	\$ -	-	\$ -

**13. Share capital (continued):**

(b) Equity-settled share based compensation (continued):

Weighted average fair value assumptions for grants made in 2016 and 2015 are as follows:

	2016	2015
Risk-free interest rate	0.8%	1.3%
Expected life	6.7 years	8.2 years
Annualized volatility	43%	45%
Dividend rate	0%	0%
Termination rate	6%	12%
Grant date fair value	\$4.63	\$10.48

Details of options outstanding under the option plan at December 31, 2016 are as follows:

Strike price	Number outstanding, December 31, 2016	Units outstanding		Units exercisable	
		Weighted average remaining unit life (yrs)	Weighted average exercise price	Number exercisable, December 31, 2016	Weighted average strike price
\$9.77-\$15.01	124,936	9.2	\$ 10.65	-	\$ -
\$17.26-\$22.22	56,589	8.2	\$ 21.70	-	\$ -
	181,525		\$ 14.10	-	\$ -

The Company recognized an expense of \$334,000 for the year ended December 31, 2016 (2015 -\$189,000) in Contributed surplus.

**14. Depreciation, depletion, and amortization:**

Depreciation, depletion and amortization allocated by function are as follows:

	2016	2015
Production	\$ 102,539	\$ 100,988
Selling and administration	8,448	7,982
	\$ 110,987	\$ 108,970

**15. Personnel expenses:**

	Note	2016	2015
Wages and salaries		\$ 232,342	\$ 219,362
Government administered pensions and unemployment insurance		13,071	12,817
Workers' compensation insurance		6,182	7,505
Contributions to defined contribution plans	22	9,866	10,948
Expenses related to defined benefit plans	22	1,648	1,304
Cash-settled share based payment transactions and other long term compensation expense	11	4,551	5,431
Medical, dental, group insurance and other		36,796	34,027
		\$ 304,456	\$ 291,394

**16. Finance costs:**

Recognized in Net earnings (loss):

	2016	2015
Interest on borrowing	\$ (16,659)	\$ (16,034)
Net interest on defined benefit plans	(428)	(11)
Unwind of discount on provisions	(832)	(667)
Amortization of deferred finance costs	(683)	(857)
	<b>\$ (18,602)</b>	<b>\$ (17,569)</b>

Recognized in Other comprehensive income:

	2016	2015
Effective portion of changes in fair value of interest rate swap	\$ (51)	\$ (71)

**17. Other income:**

	2016	2015
Gain (loss) on disposal of surplus equipment, licences and roads	\$ 14,072	\$ 758
Gain (loss) on lumber futures trading	22	(1)
	<b>\$ 14,094</b>	<b>\$ 757</b>

On November 30, 2016, Interfor completed the sale of its former sawmill in Tacoma, Washington for net proceeds of \$40,830,000 and a gain of \$15,012,000.

During 2016, Interfor also sold fixed income investments for proceeds of \$10,342,000 and recognized a gain of \$23,000.

**18. Restructuring costs:**

	Note	2016	2015
Tacoma sawmill:			
Write-down of inventories	5	\$ 1,533	\$ 6,475
Write-down of buildings	5	1,018	-
Severance		-	3,016
Site closure costs		1,738	574
Onerous contract		-	64
Beaver-Forks operation:			
Write-down (reversal of write-down) of plant and equipment	8	-	(1,195)
Severance		-	5
Onerous contract (recovery)		(82)	175
Write-down of inventories		-	32
Other			
Write-down of equipment	8	1,155	2,812
Severance		955	871
Onerous contract		497	-
Other		466	-
		\$ 7,280	\$ 12,829

On July 30, 2015, the Company announced a plan to exit the Tacoma sawmill (note 4), classified the assets as Assets held for sale (note 5) and recorded related restructuring charges. Inventory write-downs reflect extraordinary declines in fair value of inventory subsequent to decision date.

In December, 2015, the Company recorded an impairment against operating equipment replaced in 2016 for regulatory compliance.

In December, 2016, the Company recorded an impairment against surplus operating equipment.

**19. Income taxes:**

Income tax expense is as follows:

	2016	2015
Current tax expense:		
Current year	\$ 802	\$ 895
Adjustments for prior periods	51	(281)
	853	614
Deferred income tax expense (recovery):		
Origination and reversal of temporary differences	12,525	(25,767)
Change in unrecognized deferred income tax assets	(6,171)	1,136
	6,354	(24,631)
	\$ 7,207	\$ (24,017)



**19. Income taxes (continued):**

Income tax expense (recovery) recognized in Other comprehensive income is as follows:

	2016	2015
Defined benefit plan actuarial losses	\$ -	\$ (376)
Foreign currency translation differences for foreign operations	691	(321)
	\$ 691	\$ (697)

Income tax expense (recovery) recognized in Equity is as follows:

	2016	2015
Amortized and unamortized share issuance costs	\$ (1,829)	\$ -

The reconciliation of income taxes at the statutory rate to the income tax expense (recovery) is as follows:

	2016	2015
Income tax expense (recovery) at the statutory rate of 26.00% (2015 - 26.00%)	\$ 18,941	\$ (14,145)
Change in unrecognized deferred income tax assets	(6,171)	1,136
Entities with different tax rates and foreign rate adjustments	(4,884)	(12,702)
Income Tax Credit	(715)	-
Other	36	1,694
	\$ 7,207	\$ (24,017)

The statutory tax rate did not change from 2015.

The Company has the following non-capital loss carryforwards that are available to reduce future taxable income:

- Canadian non-capital loss carry-forwards which total approximately \$101,215,000 (2015 - \$125,000,000), and expire between 2029 and 2036.
- U.S. net operating loss carry-forwards which total approximately US\$175,176,000 (2015 - US\$179,000,000), and expire between 2023 and 2035.

*Unrecognized deferred income taxes:*

As at December 31, 2016, the Company has unrecognized deferred income tax assets in relation to accrued foreign exchange losses on U.S. Dollar denominated debt. These losses, if realized, will result in allowable capital losses which can be applied against the taxable portion of capital gains, if any, arising in future years.

As at December 31, 2015, the Company had unrecorded deferred income tax assets related to non-capital loss carry-forwards, accrued and realized foreign exchange losses on U.S. Dollar denominated debt, actuarial pension losses and unamortized share issuance costs.

**19. Income taxes (continued):**

Deferred income tax assets related to the Company's Canadian operations are not recognized in respect of the following:

	2016	2015
Non-capital losses carried forward	\$ -	\$ 27,313
Deductible temporary differences	8,009	15,466
	\$ 8,009	\$ 42,779

Recognized deferred income taxes:

December 31, 2016	Opening Balance	Recognized in Income Tax Expense	Recognized in Other Comprehensive Income (loss)	Recognized in Shareholder's Equity	Ending Balance
Deferred income tax assets					
Losses	\$ 117,627	\$ (3,986)	\$ -	\$ 1,137	\$ 114,778
Reserves	20,494	870	-	-	21,364
Tax credits	111	759	-	-	870
Share issue costs	-	-	-	692	692
Other	2,520	2,152	-	-	4,672
Deferred income tax liabilities					
Capital assets	(122,228)	(6,149)	-	-	(128,377)
Foreign currency translation differences for foreign operations	145	-	(681)	-	(536)
<b>Total</b>	<b>\$ 18,669</b>	<b>\$ (6,354)</b>	<b>\$ (681)</b>	<b>\$ 1,829</b>	<b>\$ 13,463</b>
December 31, 2015	Opening Balance	Recognized in Income Tax Expense	Recognized in Other Comprehensive Income (loss)	Recognized in Shareholder's Equity	Ending Balance
Deferred income tax assets					
Losses	\$ 72,304	\$ 45,323	\$ -	\$ -	\$ 117,627
Reserves	25,965	(5,847)	376	-	20,494
Tax credits	955	(844)	-	-	111
Other	2,538	(18)	-	-	2,520
Deferred income tax liabilities					
Capital assets	(108,245)	(13,983)	-	-	(122,228)
Foreign currency translation differences for foreign operations	(176)	-	321	-	145
<b>Total</b>	<b>\$ (6,659)</b>	<b>\$ 24,631</b>	<b>\$ 697</b>	<b>\$ -</b>	<b>\$ 18,669</b>

Represented by the following:

	2016	2015
Deferred income tax assets	\$ 14,311	\$ 18,669
Deferred income tax liabilities	(848)	-
	\$ 13,463	\$ 18,669

**20. Commitments and contingencies:**

## (a) Operating leases and contractual obligations:

The Company is obligated under various operating leases and contracts requiring minimum annual payments in each of the next five years as follows:

2017	\$ 19,570
2018	12,790
2019	10,530
2020	5,430
2021	4,790

## (b) Surety Performance Bonds:

The Company has posted \$32,375,000 in surety performance bonds, with various expiry dates extending through January, 2025.

## (c) Softwood Lumber Agreement:

The Canada-U.S Softwood Lumber Agreement ("SLA") expired on October 12, 2015, eliminating export taxes on Canadian softwood lumber shipments to the United States.

On November 25, 2016, the U.S. Lumber Coalition ("Coalition") filed a petition with the U.S. Department of Commerce ("DoC") and the U.S. International Trade Commission ("ITC") seeking countervailing and anti-dumping duties on Canadian softwood lumber imports to the U.S.

On January 6, 2017, the ITC determined that there is a reasonable indication that the U.S. industry is materially injured by the imports of softwood lumber products from Canada. As a result, the DoC will commence its anti-dumping and countervailing duty investigations on imports of these products.

The DoC is expected to announce its ruling in the Countervailing Duty ("CVD") investigation in the second quarter, 2017. A ruling in the Anti-dumping Duty ("AD") investigation is expected to come approximately 60 days thereafter.

If the DoC rules that "critical circumstances" apply, duties could be applied retroactively up to 90 days prior to the preliminary determinations. It is not anticipated that this would give rise to a liability as at December 31, 2016.

## (d) Timber Licence:

A Timber Licence held by Interfor for harvesting within the B.C. Coast region (the "Licence") is expected to be cancelled (or taken) by the Government of B.C., following the passing into law of the Great Bear Rainforest (Forest Management) Act (the "Act") and regulations, which took effect January 1, 2017.

If the Licence is taken, Interfor would be entitled to compensation from the Government of B.C. based upon the value of the harvesting rights under the Licence. Although it is not practicable at this time to estimate the value or form of compensation that would be received by Interfor if the Licence were taken, it is expected that such compensation would exceed the net book value of the Licence as at December 31, 2016.

## (e) Other contingencies:

The Company is subject to a number of claims arising in the normal course of business in respect of which either an adequate provision has been made or for which no material liability is expected.

**21. Net earnings per share:**

Net earnings per share is based on the earnings attributable to shareholders and a weighted average number of Shares, as defined in note 13, outstanding for the year.

The reconciliation of the numerator and denominator is determined as follows:

	2016			2015		
	Net earnings	Weighted average number of Shares	Per Share	Net loss	Weighted average number of Shares	Per Share
Issued Shares at December 31		70,030			66,730	
Effect of Shares issued on: March 2, 2015		-			2,758	
Basic and diluted earnings (loss) per share	\$ 65,643	70,030	\$ 0.94	\$ (30,386)	69,488	\$ (0.44)

**22. Employee future benefits and other post-retirement plans:**

The Company maintains a number of savings and retirement plans that are available to employees that meet certain eligibility requirements.

**(a) Defined contribution plans:**

In Canada, salaried employees of the Company are provided with the opportunity to make voluntary contributions to a Registered Retirement Savings Plan ("RRSP") based on a percentage of an employee's earnings. The Company matches employees' RRSP contributions with contributions to a Deferred Profit Sharing Plan ("DPSP") with the employee's future retirement benefits based on these contributions along with investment earnings on the contributions.

For the DPSP, the Company's funding obligations are satisfied upon making cash contributions to an employee's account. For 2016, the pension expense for this plan is equal to the Company's contribution of \$1,639,000 (2015 - \$1,785,000).

For certain eligible employees of the Canadian Merchant Services Guild ("CMSG"), the Company makes required contributions based on a percentage of earnings into a defined contribution plan. For 2016, the pension expense is equal to the Company's contribution of \$49,000 (2015 - \$44,000).

Employees of two wholly-owned U.S. operating subsidiaries of the Company, contribute a percentage of their earnings to a 401(k) plan which the Company matches and which vest immediately. The Company's funding obligations are satisfied upon making cash contributions to an employee's account. For 2016, the pension expense for this plan is equal to the Company's contribution of \$4,267,000 (2015 - \$4,374,000).

**(b) Unionized employees' pension plan:**

The Company contributes to an industry-wide benefit plan for unionized employees based on a predetermined amount per hour worked by an employee. For 2016, the pension expense for these plans is equal to the Company's contribution of \$3,352,000 (2015 - \$3,499,000). As there is insufficient information available to enable the Company to account for this plan as a defined benefit plan, the plan has been accounted for as a defined contribution plan. The Company's liability is limited to its contributions.

**22. Employee future benefits and other post-retirement plans (continued):**

## c) Supplementary pension plans:

The Company provides supplementary pension benefits to certain members of its senior management in the form of a notional extension to the DPSP in Canada and the 401(k) plan in the U.S. These commitments are not funded but are fully accrued by the Company, with a portion of the commitments being secured by irrevocable letters of credit.

During 2016 the Company recorded an expense of \$559,000 (2015 - \$738,000) in respect of these plans.

The accrued liabilities of this plan are included in the Company's Statements of Financial Position as follows:

	2016	2015
Trade accounts payable and provisions	\$ 721	\$ 418
Employee future benefits obligation	5,499	5,644
	<b>\$ 6,220</b>	<b>\$ 6,062</b>

## d) Defined benefit plans:

The Company and the non-union hourly employees at the Adams Lake operations make contributions to a defined benefit pension plan that provides pension benefits upon retirement. The plan entitles a retired employee to receive monthly payments based on a schedule of defined benefit accruals for different periods of service.

The Company makes contributions to a defined benefit pension plan that provides pension benefits to certain eligible employees of the CMSG upon retirement. The plan provides a retired employee a monthly payment based on a percentage of their average earnings at retirement, and their years of service. In addition, the Company provides post-retirement medical and life insurance benefits to certain eligible CMSG retirees.

The Company maintains a non-contributory defined benefit pension plan for a former senior executive.

The Company provides post retirement life insurance benefits to eligible retirees of a wholly-owned subsidiary, Seaboard Shipping Company Limited ("SSCL"). In addition, specified individuals at SSCL received a supplemental pension based on a percentage of final average earnings at retirement, and years of service. Effective December 12, 2016, the supplemental pension was settled and all liabilities were paid out through the purchase of an annuity.

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

The most recent and the next scheduled actuarial valuations for funding purposes for the significant pension plans are:

	Most Recent Valuation	Next Scheduled Valuation
Adams Lake Pension Plan	December 31, 2013	December 31, 2016
CMSG Pension Plan	December 31, 2013	December 31, 2016

**22. Employee future benefits and other post-retirement plans (continued):**

## (d) Defined benefit plans (continued):

The significant pension plans are subject to the statutory requirements (including minimum funding requirements) of their respective jurisdictions and the Income Tax Act. Each plan's pace of funding is determined by the Company, subject to the statutory minimums and maximums.

In 2016, the Company paid contributions of \$1,150,000 (2015 - \$698,000), and in lieu of making cash special payments to fund certain deficits, posted letters of credits totaling \$2,555,000 (2015 - \$2,464,000). In 2017, the Company expects to pay contributions of \$803,000 to its defined benefit plans, and hold a total of \$2,555,000 of letters of credit.

The following summarizes the pension and other post-retirement obligations:

	Pension Benefits		Other Post-retirement Benefits	
	2016	2015	2016	2015
<b>Defined benefit obligation:</b>				
Beginning of year	\$ 51,505	\$ 48,729	\$ 1,813	\$ 1,700
Service cost	944	920	51	45
Employee contributions	377	339	-	-
Interest cost	1,875	1,990	91	67
Benefit payments	(1,986)	(2,094)	(66)	(48)
Actuarial loss due to:				
Financial assumptions	48	1,593	-	49
Experience adjustment	126	28	-	-
Settlements	(1,680)	-	-	-
<b>End of year</b>	<b>\$ 51,209</b>	<b>\$ 51,505</b>	<b>\$ 1,889</b>	<b>\$ 1,813</b>
<b>Plan assets:</b>				
Beginning of year	\$ 52,020	\$ 50,575	\$ -	\$ -
Interest on plan assets	1,925	1,995	-	-
Employer contributions	1,084	650	66	48
Employee contributions	377	339	-	-
Benefit payments	(1,986)	(2,094)	(66)	(48)
Administration costs	(146)	(110)	-	-
Actuarial gain	1,683	665	-	-
Settlements	(2,146)	-	-	-
<b>End of year</b>	<b>\$ 52,811</b>	<b>\$ 52,020</b>	<b>\$ -</b>	<b>\$ -</b>

**22. Employee future benefits and other post-retirement plans (continued):**

(d) Defined benefit plans (continued):

The following summarizes the balances recognized on the Statements of Financial Position:

	Pension Benefits		Other Post-retirement Benefits	
	2016	2015	2016	2015
Fair value of plan assets	\$ 52,811	\$ 52,020	\$ -	\$ -
Present value of unfunded obligations	(345)	(371)	(1,889)	(1,813)
Present value of funded obligation	(50,864)	(51,134)	-	-
Net employee future benefits asset (liability)	\$ 1,602	\$ 515	\$ (1,889)	\$ (1,813)
Employee future benefits asset	\$ 2,471	\$ 1,570	\$ -	\$ -
Trade accounts payable and provisions	(71)	(71)	(50)	(50)
Employee future benefits obligation	(798)	(984)	(1,839)	(1,763)
Net employee future benefits asset (liability)	\$ 1,602	\$ 515	\$ (1,889)	\$ (1,813)

The following table shows the Company's net expense recognized in the Statement of Earnings and the actuarial (gains) losses recognized in Other comprehensive income:

	Pension Benefits		Other Post-retirement Benefits	
	2016	2015	2016	2015
Statement of Earnings				
Production expense	\$ 1,090	\$ 1,030	\$ 51	\$ 45
Finance (income) costs	(50)	(5)	91	67
Restructuring costs	466	-	-	-
	\$ 1,506	\$ 1,025	\$ 142	\$ 112
Other comprehensive income (loss)				
Actuarial gains (losses)	\$ 1,509	\$ (956)	\$ -	\$ (49)

Plan assets consist of:

Asset category	2016	2015
Investment Funds		
Canadian Equity	\$ 15,787	\$ 13,735
Global	16,766	16,946
Money Market	985	831
Fixed Income	18,715	19,050
Balanced	457	483
Cash	101	8
Other	-	967
Total	\$ 52,811	\$ 52,020

**22. Employee future benefits and other post-retirement plans (continued):**

## (d) Defined benefit plans (continued):

The plan assets held in investment funds are managed by third party investment managers and the fair values of these investments have been determined based on the unit price of the underlying funds. As such, all investment funds are categorized as Level 2 in the fair value hierarchy.

Actuarial assumptions used in accounting for the Company maintained benefit plans (expressed as weighted averages) are:

	Pension Benefits		Other Post-retirement Benefits	
	2016	2015	2016	2015
Defined benefit obligation as of December 31				
Discount rate	3.75%	3.75%	3.75%	3.75%
Compensation increases <sup>1</sup>	3.50%	3.50%	-	-
Pension expense				
Discount rate	3.75%	3.99%	3.75%	3.96%
Compensation increases <sup>1</sup>	3.50%	3.50%	-	-

<sup>1</sup>Compensation increases only relate to the CMSG plan.

For measurement purposes at December 31, 2016, the Company has assumed a 5.36% health care cost trend in 2017 grading down to 4.38% in 2021 (2015 – 5.60% health care cost trend in 2016 grading down to 4.38% in 2021).

	Pension Benefits	Other Post-retirement Benefits
Effect of 1% decrease in discount rate on defined benefit obligation	\$ 7,321	\$ 247

The sensitivity to the discount rate has been determined assuming all other assumptions remain unchanged. An increase in the discount rate would have an opposite effect of similar magnitude.

The weighted average durations of the defined benefit pension plans and other post-retirement benefit plans is fifteen years.

Through its defined benefit pension plans and other post-retirement benefits, the Company is exposed to a number of risks, the most significant of which are detailed below:

*Asset liability mismatch* – The defined benefit plan obligations are calculated using a discount rate set with reference to corporate bond yields. While the Adams Lake and CMSG pension plans hold some fixed income investments, both plans hold a significant proportion of equities, which are expected to outperform corporate bonds in the long term. However, in the short term, there will be volatility in the funded status of the plans.

*Life expectancy* – The majority of obligations are to provide benefits for the life of the member, so increases in life expectancy would result in increased obligations.



**23. Related party transactions:**

Key management personnel are comprised of the Company's directors and executive officers.

The remuneration of key management personnel was as follows:

	2016	2015
Salary and short-term employee benefits	\$ 6,013	\$ 4,838
Post-employment benefits	512	729
Share-based compensation expense (recovery)	3,112	(3,447)
	<b>\$ 9,637</b>	<b>\$ 2,120</b>

Obligations in relation to key management personnel, including directors, are as follows:

	2016	2015
Trade accounts payable and provisions	\$ 3,947	\$ 5,669
Employee future benefits obligation	3,998	3,591
Provisions and other liabilities	10,840	10,239
	<b>\$ 18,785</b>	<b>\$ 19,499</b>

**24. Segmented information:**

The Company manages its business as a single operating segment, solid wood. The Company harvests and purchases logs which are sorted by species, size and quality and then either manufactured into lumber products at the Company's sawmills, or sold. Substantially all operations are located in British Columbia, Canada and the Northwest and Southeast regions of the U.S.

The Company sells to both foreign and domestic markets as follows:

	2016	2015
United States	\$ 1,248,684	\$ 1,144,927
Canada	234,308	236,517
Japan	137,795	140,900
China/Taiwan	91,606	110,828
Other export	80,319	54,203
	<b>\$ 1,792,712</b>	<b>\$ 1,687,375</b>

Sales by product line are as follows:

	2016	2015
Lumber	\$ 1,458,296	\$ 1,361,192
Logs	179,275	174,090
Wood chips and other by products	145,608	141,717
Ocean freight and other	9,533	10,376
	<b>\$ 1,792,712</b>	<b>\$ 1,687,375</b>

**24.Segmented information (continued):**

Non-current assets by geographic location are as follows:

	2016	2015
United States	\$ 666,839	\$ 709,002
Canada	348,796	369,573
	<b>\$ 1,015,635</b>	<b>\$ 1,078,575</b>

**25.Capital management:**

The Company's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Company monitors the pre-tax return on total assets, which it defines as operating earnings before restructuring and capital asset write-downs, divided by the average of Total assets for the period.

The Company seeks to maintain a balance between the higher returns that might be possible with the leverage afforded by higher borrowing levels and the security afforded by a sound capital position. The Company's target is to create value for its shareholders over the long term through increases in share value.

There were no changes in the Company's approach to capital management during 2016. Under its debt financing agreements, the Company cannot exceed a total debt to total capitalization ratio, with total debt defined as the total of indebtedness, including letters of credit, and long term debt, net of cash and cash equivalents up to a limit; and total capitalization defined as total debt plus shareholders' equity and subordinated debt, excluding non-controlling interests, deferred income taxes, and a maximum of \$20 million cumulative (from January 1, 2012) non-cash asset revaluations. The financial covenants under the debt financing agreements also carry a minimum working capital, a minimum net worth requirement and a minimum EBITDA coverage ratio contingent on the total debt to total capitalization ratio.

The Company is in compliance with all of its debt covenants and expects to remain in compliance.

**26.Financial instruments:****(a) Fair value of financial instruments:**

At December 31, 2016, the fair value of the Company's long term debt exceeded its carrying value by \$7,378,000 (2015 – below carrying value by \$8,188,000), measured based on the level 2 of the fair value hierarchy. The fair values of other financial instruments approximate their carrying values due to their short-term nature.

**(b) Derivative financial instruments:**

Derivative financial instruments in an asset position are classified as Trade accounts receivable and other in the Statements of Financial Position, while derivative financial instruments in a liability position are classified as Trade accounts payable and provisions. Financial instrument assets and liabilities are not netted for purposes of presentation in the financial statements.

**26. Financial instruments (continued):**

## (b) Derivative financial instruments (continued):

The Company may use a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, interest rates and lumber prices. These include foreign currency forward, collar and option contracts, and interest rate swaps.

Two of the Company's interest rate swaps matured on April 14, 2016. Two interest rate swaps remained outstanding at December 31, 2016, each with a notional value of US\$25,000,000. Under these two interest rate swaps, maturing February 27, 2017, the Company pays an amount based on a fixed annual interest rate of 0.84% and receives a 90 day LIBOR which is recalculated at set interval dates. At December 31, 2016, the fair value of the Company's interest rate swaps was an asset of \$10,000 (December 31, 2015 – \$61,000 asset). Fair value of the Company's interest rate swaps are measured based on Level 2 of the fair value hierarchy.

In respect of its trading in foreign currency exchange contracts and interest rate swaps, the Company does not expect any credit losses in the event of non-performance by counterparties as the counterparties are the Company's bankers, which are all highly rated.

As at December 31, 2016, the Company had no outstanding obligations under foreign currency contracts.

The following table summarizes the gain (loss) on derivative financial instruments for the years ended December 31, 2016 and 2015.

	2016	2015
Foreign exchange collars and forward contracts <sup>1</sup>	\$ 271	\$ (1,420)
Interest rate swaps <sup>2</sup>	(51)	(71)
Lumber futures <sup>3</sup>	(1)	(1)
<b>Total gain (loss), net</b>	<b>\$ 219</b>	<b>\$ (1,492)</b>

<sup>1</sup> Recognized in Other foreign exchange gain (loss) in Net earnings.

<sup>2</sup> Recognized in Other comprehensive income.

<sup>3</sup> Recognized in Other income in Net earnings.

**26. Financial instruments (continued):**

## (c) Hedge of investment in foreign operations:

As at December 31, 2016, U.S. Dollar borrowings under the Revolving Term Line and Senior Secured Notes were designated as hedges against the Company's investment in its U.S. operations with unrealized foreign exchange gains (losses) recorded in Other comprehensive income as follows:

Designation date	Opening balance <sup>1</sup>	Additions <sup>1</sup>	Payments <sup>1</sup>	Closing balance <sup>1</sup>	Unrealized foreign exchange gains (losses) <sup>2</sup>	
					2016	2015
June 26, 2013 <sup>4</sup>	50,000	-	-	50,000	2,065	(11,195)
March 13, 2014 <sup>3</sup>	75,000	-	(67,000)	8,000	4,414	(17,313)
December 17, 2014 <sup>4</sup>	50,000	-	-	50,000	2,065	(11,195)
January 14, 2015 <sup>3</sup>	10,000	-	(10,000)	-	352	(1,892)
February 26, 2015 <sup>3</sup>	-	-	-	-	-	(4,112)
March 16, 2015 <sup>4</sup>	100,000	-	-	100,000	4,130	(10,370)
March 30, 2015 <sup>3</sup>	10,000	-	(10,000)	-	704	(1,260)
May 12, 2015 <sup>3</sup>	35,000	-	(35,000)	-	2,516	(6,073)
October 5, 2016 <sup>3</sup>	-	22,000	-	22,000	(566)	-
	\$330,000	\$ 22,000	\$(122,000)	\$230,000	\$ 15,680	\$(63,410)

<sup>1</sup>Denominated in U.S. Dollars.

<sup>2</sup>Denominated in Canadian Dollars.

<sup>3</sup>Drawn on Revolving Term Line.

<sup>4</sup>Drawn on Senior Secured Notes.

Repayments were de-designated as a hedge of the Company's investment in its U.S. operations.

## (d) Financial risk management:

Financial instrument assets include cash and cash equivalents, trade and other receivables and certain investments and advances. Cash and cash equivalents and trade and other receivables are designated as loans and receivables and are initially measured at fair value plus any direct transaction costs and thereafter at amortized cost using the effective interest rate method, less any impairment losses.

Certain Other investments and advances are classified as held for trading and are measured at fair value.

Financial instrument liabilities include bank indebtedness, accounts payable and other provisions, long term debt, and certain other long term liabilities. All financial liabilities are designated as other liabilities and are initially measured at fair value plus any direct transaction costs and subsequently at amortized cost using the effective interest method.

There are no financial instruments classified as held-to-maturity.

The use of financial instruments exposes the Company to credit, liquidity and market risk.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits.

**26. Financial instruments (continued):**

## (d) Financial risk management (continued):

Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Company's activities. Through its standards and procedures, management has developed a control environment in which employees are clear on roles and obligations and management regularly monitors compliance with its risk management policies and procedures.

## (i) Credit risk:

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

*Accounts receivable*

The Company's exposure to credit risk is dependent upon individual characteristics of each customer. Each new customer is assessed for creditworthiness before payment and delivery terms and conditions are offered, with such review encompassing any external ratings, and bank and other references. Purchase limits are established for each customer, and are regularly reviewed. In some cases, where customers fail to meet the Company's benchmark creditworthiness, the Company may choose to transact with the customer based on standard industry terms.

Most North American sales are conducted under standard industry terms. All lumber sales outside of the North American markets are either insured as to 90% of the receivable amounts by the Export Development Corporation or are secured by documentary collections or irrevocable letters of credit.

The Company regularly reviews the collectability of its accounts receivable and establishes an allowance for doubtful accounts based on its best estimate of any potentially uncollectible accounts. Historically, the Company has managed its credit tightly and has experienced minimal bad debts. Based on this past experience and its detailed review of trade accounts receivable past due which were considered uncollectible, no reserve in respect of doubtful accounts was recorded as at December 31, 2016 (2015 - \$67,000).

*Deposits*

The Company limits its exposure to credit risk by only investing in liquid securities and only with counterparties that have a high credit rating. As such, management does not expect any counterparty to fail to meet its obligations.

*Guarantees*

The Company did not provide any guarantees in 2016.

*Exposure to credit risk*

The carrying amount of financial assets represents the maximum credit exposure for receivables in North America. As all log and lumber sales outside of the North American markets are typically insured by the Export Development Corporation to 90% or secured by irrevocable letters of credit, credit exposure for these sales is limited.

**26. Financial instruments (continued):**

## (d) Financial risk management (continued):

## (i) Credit risk (continued):

Accounts receivable carrying values at the reporting date by geographic region were as follows:

	2016	2015
United States	\$ 61,755	\$ 62,148
Canada	14,243	16,233
Japan	5,312	5,837
China/Taiwan	7,397	5,523
Other	6,352	5,477
	\$ 95,059	\$ 95,218

## (ii) Liquidity risk:

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company ensures, as far as possible, that it will always have sufficient liquidity to meet obligations when due and monitors cash flow requirements daily and projections weekly. Weekly debt graphs are reviewed by senior management to monitor cash balances and debt line utilizations.

The Company also maintains an Operating Line, a Revolving Term Line and a U.S. Operating Line that can be drawn on to meet obligations.

The estimated cash payments due in respect of contractual and legal obligations including capital commitments are summarized as follows:

	Total	Payments due by period			
		Up to 1 year	2-3 years	4-5 years	After 5 years
Trade accounts payable and accrued liabilities	\$ 112,592	\$ 112,592	\$ -	\$ -	\$ -
Income taxes payable	317	317	-	-	-
Contingent future payment	13,427	13,427	-	-	-
Reforestation liability	39,419	11,609	10,226	8,141	9,443
Long term debt	308,821	-	40,281	44,756	223,784
Provisions and other liabilities	38,817	11,008	5,662	2,150	19,997
Operating leases and capital commitments	66,820	19,570	23,320	10,220	13,710
<b>Total obligations</b>	<b>\$ 580,213</b>	<b>\$ 168,523</b>	<b>\$ 79,489</b>	<b>\$ 65,267</b>	<b>\$ 266,934</b>

## (iii) Market risk:

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

**26. Financial instruments (continued):**

(d) Financial risk management (continued):

*Currency risk*

The Company is exposed to currency risk on cash and cash equivalents, accounts receivable, accounts payable and provisions, long term debt and intercompany loans that are denominated in a currency other than the respective functional currencies of the Company's domestic and foreign operations, primarily Canadian and U.S. Dollars, but also the Euro, Sterling and Yen. The Company may use foreign currency exchange forward, collar and option contracts to manage its currency risk from time to time. The Company routinely assesses its foreign exchange exposure by reviewing outstanding contracts, pending order files and working capital denominated in foreign currencies.

At December 31, 2016, the Company has U.S. Dollar drawings under its Revolving Term Line and Senior Secured Notes of US\$230,000,000 (2015 – US\$330,000,000). These U.S. Dollar drawings have been designated as a hedge against the Company's net investment in its U.S. operations.

As at December 31, the Company's accounts receivable were denominated in the following currencies (in thousands):

2016	CAD	USD	Japanese ¥
Accounts receivable	18,072	20,614	19,230
Accounts receivable held by foreign subsidiaries with USD functional currency	-	36,559	-
	18,072	57,173	19,230
2015	CAD	USD	Japanese ¥
Accounts receivable	18,292	18,526	17,678
Accounts receivable held by foreign subsidiaries with USD functional currency	-	36,909	-
	18,292	55,435	17,678

As at December 31, 2016, the domestic operations of the Company held cash and cash equivalents of US\$7,503,000 (2015 – US\$5,118,000). Cash and cash equivalents held by foreign subsidiaries totaled US\$5,195,000 (2015 – US\$320,000).

**26. Financial instruments (continued):**

(d) Financial risk management (continued):

(iii) Market risk (continued):

Based on the Company's net exposure to foreign currencies as at December 31, 2016, including U.S. Dollar denominated cash and cash equivalents, long term debt and other financial instruments, the sensitivity of the U.S. Dollar balances to the Company's net annual earnings is as follows:

U.S. Dollar	\$0.01 increase vs CAD	\$29,000 decrease in net earnings
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Based on the Company's net exposure to foreign currencies as at December 31, 2016, in respect of its net investment in U.S. subsidiaries, the sensitivity of the U.S. Dollar balances to the Company's Other comprehensive income is as follows:

U.S. Dollar	\$0.01 increase vs CAD	\$2,564,000 increase in OCI
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*Interest rate risk*

The Company has reduced its exposure to changes in interest rates on borrowings by entering into interest rate swaps, as described in Note 26(b). The intent of these swaps is to convert floating-rate interest expense to fixed-rate interest expense. In addition, the Company issued US\$200,000,000 of Senior Secured Notes (note 10(b)), which bear interest at fixed rates ranging from 4.02 to 4.33%.

Based on the Company's average debt level during 2016, the sensitivity of a 100 basis point increase in interest rates would result in an approximate decrease of \$343,000 in net earnings.

*Other market price risk*

The Company does not enter into commodity contracts other than to meet the Company's expected usage and sale requirements and such contracts are not settled net.



## **ANNUAL INFORMATION FORM**

**Prepared as of February 9, 2017**

### **FORWARD LOOKING INFORMATION**

This Annual Information Form contains information and statements that are forward-looking in nature, including, but not limited to, statements about the Company's business outlook, objectives, plans, strategic priorities and other statements that are not historical facts. A statement Interfor makes is forward-looking when it uses what is known today, to make a statement about the future. Forward-looking statements may include words such as "will", "could", "should", "expected", "anticipate", "intend", "forecast", "target", "outlook" and "strategy". Such forward-looking statements are based on Interfor's current expectations and certain assumptions, including assumptions regarding lumber, log and wood chip prices; the Company's ability to compete on a global basis; the availability and cost of log supply; the absence of natural or man-made disasters; currency exchange rates; no material changes in government regulation; the availability of the Company's allowable annual cut ("AAC"); the outcome of aboriginal claims and treaty settlements; the Company's ability to export its products; the outcome of the softwood lumber dispute between Canada and the U.S.; stumpage rates payable to the Province of British Columbia; environmental effects of the Company's operations; the absence of labour disruptions; and the assumptions described under the heading "Critical Accounting Estimates" in Interfor's 2016 annual Management's Discussion & Analysis, which is available on [www.sedar.com](http://www.sedar.com) and [www.interfor.com](http://www.interfor.com). Such forward-looking statements involve known and unknown risks and uncertainties that, if they eventuate, may cause Interfor's actual results to be materially different from those expressed or implied by those forward-looking statements. Such risks and uncertainties include lumber, log and wood chip price volatility; global competition; reduction of availability or increase in cost of log supply; natural or man-made disasters; foreign currency exchange rate fluctuations; changes in government regulation; reductions of the Company's AAC; aboriginal claims or treaty settlements impacting the Company's forest tenures; export and other trade barriers; the softwood lumber dispute between Canada and the U.S.; increases in stumpage rates payable to the Province of British Columbia; environmental effects of the Company's operations; labour disruptions; and other factors referenced herein and in Interfor's 2016 annual Management's Discussion & Analysis under the heading "Risks and Uncertainties". Readers are cautioned not to place undue reliance on forward-looking information or statements. Interfor undertakes no obligation to update such forward-looking information or statements, except as required by law.

### **DESCRIPTION OF THE BUSINESS**

Interfor is a leading global supplier of lumber products. The Company has annual production capacity of approximately 3 billion board feet and offers one of the most diverse lines of lumber products to customers in North America, the Asia-Pacific region and Europe.

The Company has sawmilling operations in British Columbia, Washington, Oregon, Georgia, South Carolina and Arkansas. Interfor also owns value-added remanufacturing facilities in Washington and Georgia.

### **COMPANY HISTORY AND DESCRIPTION**

Our business originated in the 1930's with a sawmill in Whonnock, about 48 kilometres east of Vancouver B.C. Since that time, we have made significant investments to expand, upgrade and diversify our production facilities and timber base through capital programs and the acquisition of manufacturing plants and timber resources.

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The Company was incorporated under the *Company Act* (British Columbia) on May 6, 1963 and, on December 1, 1979, was amalgamated with subsidiary Whonnock Forest Products Limited. On January 1, 1988, a change in name from Whonnock Industries Limited to International Forest Products Limited occurred. On February 10, 2006 we transitioned under the *Business Corporations Act* (British Columbia). Effective on May 6, 2014, the Company's name was changed to Interfor Corporation. Our head office and our registered and records offices are located at Suite 3500, 1055 Dunsmuir Street, Vancouver, British Columbia, V7X 1H7.

Our significant indirectly wholly-owned subsidiary, Interfor U.S. Inc., is incorporated in the State of Washington and owns and operates our U.S. sawmills. Interfor Cedarprime Inc. (incorporated in the State of Washington) is also an indirectly wholly owned subsidiary of Interfor. Directly wholly-owned subsidiaries include Interfor U.S. Holdings Inc. (incorporated in Washington), Interfor Sales & Marketing Ltd. (incorporated in British Columbia), Interfor Japan Ltd. (incorporated in British Columbia), Interfor Insurance Corporation (incorporated in Barbados), and Seaboard Shipping Company Limited (incorporated in British Columbia).

## **RECENT DEVELOPMENTS**

### **2014**

On March 14, 2014, Interfor acquired all of the outstanding common shares of Tolleson Ilim Lumber Company from Ilim Timber Continental, S.A. for total consideration of \$188.5 million, comprising \$126.9 million in cash and 3,680,000 Common Shares valued at \$61.6 million. This acquisition added two sawmills located in Perry and Preston, Georgia, and a remanufacturing facility in Perry, Georgia.

On June 27, 2014, the Company announced a curtailment of its Beaver-Forks operation on the Olympic Peninsula in Washington State. Following a comprehensive strategic review, permanent closure of the operation and consolidation of production at Interfor's Port Angeles facility was announced on July 31, 2014.

On November 6, 2014, Interfor announced a \$50 million capital project to upgrade its sawmill in Castlegar, B.C to convert the Castlegar mill to a two line operation with state-of-the-art technology and optimization. The project was substantially completed by the end of 2015.

On December 17, 2014, the Company completed a US\$50 million term debt financing with Prudential Capital Group. The senior secured notes carry an annual interest rate of 4.02% and have a final maturity of June 26, 2023.

On December 18, 2014, Interfor signed an agreement to acquire four sawmills from Simpson Lumber Company, LLC, for consideration of US\$94.7 million, plus working capital and contingent future consideration.

### **2015**

On January 27, 2015, Interfor closed a bought deal public offering of subscription receipts (the "Subscription Receipts") through a syndicate of underwriters. The Company issued an aggregate of 3,300,000 Subscription Receipts at a price of \$20.10 per Subscription Receipt, for aggregate gross proceeds of \$66.3 million (the "Offering"). Each Subscription Receipt entitled the holder thereof, for no additional consideration and without further action, to one Common Share upon closing of the acquisition of four sawmills and associated working capital from Simpson Lumber Company, LLC ("Simpson"). Net proceeds of the Offering were used to partially fund this acquisition.

On March 1, 2015, Interfor completed its acquisition of four sawmills and associated working capital from Simpson. The sawmills are located in Tacoma, Washington; Longview, Washington; Meldrim, Georgia and Georgetown, South Carolina.

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On March 16, 2015, the Company completed a US\$100 million term debt financing of Senior Secured Notes with Prudential Capital Group. The Senior Secured Notes carry an annual interest rate of 4.17% and have a final maturity of March 26, 2026. The proceeds were used to reduce the drawings under the Company's Revolving Term Line. In conjunction with this financing, Interfor decreased the credit available under its Revolving Term Line from \$250 million to \$200 million, without change to other terms and conditions.

On April 27, 2015, Interfor extended the maturity date of its U.S. Operating Line from April 28, 2015, to May 1, 2017, and increased the credit available under that line from US\$30 million to US\$50 million to provide enhanced financial flexibility.

On May 22, 2015, Interfor curtailed operations at its Tacoma sawmill as a result of challenging lumber and log market conditions. Following a comprehensive strategic review, the Company announced its decision on July 30, 2015, to exit the mill. The Tacoma sawmill accounted for 47 million board feet of production in 2015 since acquisition.

On June 19, 2015, Interfor closed its acquisition of a sawmill and associated working capital in Monticello, Arkansas, from Price Lumber Company. This acquisition increased Interfor's U.S. South production capacity to 1.3 billion board feet and raised the proportion of Interfor's total capacity in the U.S. South to more than 40%.

## **2016**

The capital project to upgrade the Company's sawmill in Castlegar, B.C. was substantially complete by the end of 2015 and it was operating at its designed productivity level to start 2016.

On February 9, 2016, Interfor renewed and extended its Canadian Operating Line of credit and Revolving Term Line to a new maturity date of May, 2019. The commitment amount, security and pricing grid remained unchanged, but the renewal included a number of improved provisions to provide enhanced financial flexibility and liquidity.

On June 15, 2016, the Company extended the maturity of its U.S. Operating Line from May 1, 2017 to May 1, 2018, without significant change to other terms.

On November 30, 2016, Interfor closed the sale of the Tacoma sawmill property for gross proceeds of US\$32.4 million. Net cash proceeds from the sale of the property were US\$20.4 million after taking into account transaction costs and US\$10 million of contingent consideration owed to Simpson, from which Interfor acquired the sawmill in March 2015.

## **MANUFACTURING AND TIMBER SUPPLY**

We operate five sawmills in B.C. and have U.S. operations comprising two sawmills and one remanufacturing plant in Washington, two sawmills in Oregon, one sawmill in South Carolina, one sawmill in Arkansas, and seven sawmills and one remanufacturing plant in Georgia. These operations produce a wide range of products for sale in North American and offshore markets. The products range from commodity structural lumber through to specialty products, such as exterior decking and siding, machine stress rated products, industrial timbers and a wide range of appearance grade items.

The mills are capable of cutting logs of various species and grades ranging in diameter from 4 inches to 80 inches. Many of our manufacturing facilities have recently been upgraded and modified to improve the matching of timber resources with customers' lumber requirements.

Rated capacity and production of lumber for each region is set out in the following table:

Sawmills	Present Rated Capacity (1)	Production for years ended December 31,		
		2016	2015	2014
		(millions of board feet)		
<b>B.C. Coast</b> <sup>(2)</sup>	320	159	164	198
<b>B.C. Interior</b>	750	717	620	744
<b>U.S. Northwest</b> <sup>(3,4)</sup>	635	570	655	539
<b>U.S. Southeast</b> <sup>(5)</sup>	1,325	1,042	1,058	741
<b>Total</b>	<b>3,030</b>	<b>2,488</b>	<b>2,497</b>	<b>2,222</b>

(1) Based on two shifts per day and adjusted for regional operating parameters.

(2) Volumes include lumber custom-cut at third party facilities under the direction of Hammond management amounting to 11, 13 and 14 million board feet in 2014, 2015 and 2016 respectively.

(3) The Beaver and Tacoma sawmills were curtailed on June 27, 2014 and May 22, 2015, respectively.

(4) The Longview and Tacoma sawmills were acquired on March 1, 2015. The Tacoma mill was permanently curtailed in August, 2015 and is not included in rated capacity. Volumes reported are Interfor only.

(5) The Perry and Preston sawmills were acquired March 14, 2014. The Meldrim and Georgetown sawmills were acquired on March 1, 2015. The Monticello sawmill was acquired on June 19, 2015. Volumes reported are Interfor only.

## CANADIAN OPERATIONS

### B.C. Coast

We own and operate two sawmill operations within the B.C. Coast region. Our Hammond operation is located on the Fraser River in Maple Ridge, B.C. and consists of a three-line sawmill, a planer mill and dry kilns. This facility is focused on western red cedar and supplies siding, decking, fascia and timbers for both offshore and North American markets. Our Acorn operation is located on leased land in Delta, B.C. and consists of a log dewatering and merchandizing system, a sawmill, a planer mill and dry kilns. This sawmill specializes in sizes and grades of lumber for use in Japanese traditional housing made primarily from hemlock and Douglas-fir logs.

### B.C. Interior

We own and operate three sawmill operations within the B.C. Interior region with timber tenures having a total AAC of 1,888,000 cubic metres. Our Adams Lake operation is located near Kamloops, B.C., while our Castlegar and Grand Forks operations are located in the southern interior of B.C. These mills manufacture kiln-dried lumber for the U.S. and Canadian construction markets as well as for offshore markets, and have the capability to cut Douglas-fir, spruce-pine-fir ("SPF"), fir-larch, western red cedar and hemlock dimension lumber. The Castlegar operation includes a transportation system for transporting logs on Arrow Lake.

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## B.C. Timber Supply

In the Province of British, the government or “Crown” owns 95% of the timberlands from which the majority of our timber is harvested. The remaining 5% of timberland is private land which is primarily located on Vancouver Island and held by a few large industrial forest landowners.

Forest and timber harvesting operations on Crown land in B.C. are regulated under the *Forest and Range Practices Act (British Columbia)* and the *Forest Act (British Columbia)*. The Government of B.C. is responsible for setting the AAC, approving forest development plans and cutting permits, determining the stumpage system and managing compliance and enforcement.

The Province provides for the use of Crown forest land through the granting of various forms of timber tenures. These tenure agreements provide timber harvesting rights in exchange for annual rent to cover general administration and fire preparedness obligations and stumpage fees payable to the Crown.

Our Company is required to manage forest resources under our tenures in accordance with the requirements of the applicable laws and regulations. Forest management of our tenures is guided by a team of forest professionals that are engaged in a wide array of activities such as resource planning, forest development, road building and harvesting, reforestation, forest protection and environmental certification.

We hold various Forest Licence (“FL”), Tree Farm Licence (“TFL”) and Timber Licence (“TL”) tenures that currently provide for an AAC of approximately of 3.7 million cubic meters. The majority of Interfor’s tenures are long-term (15 and 25 year) renewable agreements that are generally replaced every five years.

Our timber supply needs are met by a combination of logs harvested from our own timber tenures, long-term trade and supply agreements, and log purchases on the open market. When operating at normal capacity, our mills in B.C. currently acquire approximately one-third of their log supply from external sources.

On the B.C. Coast, we harvest a variety of species consisting primarily of western hemlock, amabilis fir, western red cedar and Douglas-fir. In the B.C. Interior, the species mix consists of spruce, pine, fir, Douglas-fir, larch and cedar. The harvest is derived from both old growth and second growth stands. Whereas one-third of the harvest currently comes from second growth stands on the B.C. Coast, this amount is expected to increase significantly over the next several decades. Logging operations are seasonal due to a number of factors including weather, ground conditions and fire season closures.

The following table shows our AAC under our FL and TFL tenures and other cutting rights and the volume of timber harvested under our FLs and TFLs and other cutting rights for the periods specified. It also presents the volume of log purchases and sales during the period.

<b>B.C. Timber Supply</b>	<b>Years ended December 31,</b>			
	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
	(thousands of cubic metres)			
<b>Allowable Annual Cut</b> <sup>(1)</sup>				
– Forest Licences	2,775	2,775	2,775	2,775
– Tree Farm Licences	875	875	875	875
– Non Replaceable Forest Licences	-	-	220	220
– Discretionary Annual Harvest Levels <sup>(2)</sup>	50	50	80	40
<b>Total AAC</b>	<b>3,700</b>	<b>3,700</b>	<b>3,950</b>	<b>3,910</b>
<b>Log Production</b>				
– Coast <sup>(3)</sup>	1,308	1,331	1,523	
– Interior	1,657	1,708	1,517	
<b>Total Log Production</b>	<b>2,965</b>	<b>3,039</b>	<b>3,040</b>	
<b>Log Purchases</b>	<b>1,199</b>	<b>1,112</b>	<b>1,395</b>	
<b>Log Sales</b>	<b>1,296</b>	<b>1,453</b>	<b>1,440</b>	

(1) AAC status at the beginning of each year (includes a provision for non-recoverable fibre).

(2) Includes Timber Licence tenures.

(3) 2016 volumes include production volume of 16,000 cubic metres of third party timber sales managed by Interfor (2015 – 30,000 cubic metres, 2014 – 48,000 cubic metres).

## **U.S. OPERATIONS**

### **U.S. Northwest**

We own and operate four sawmill operations in the U.S. Northwest. Three of these operations, located in Port Angeles, Washington, Longview, Washington and Molalla, Oregon, produce stud lumber for the U.S. construction market. Both the Port Angeles and Molalla sawmills produce kiln-dried stud lumber from hemlock and Douglas-fir logs while the Longview sawmill produces green Douglas-fir stud lumber with a focus on servicing home centers. Port Angeles also produces lumber in 12 foot lengths for the U.S. market and is capable of producing metric sizes for export.

Our Gilchrist sawmill located in Gilchrist, Oregon, processes lodgepole and ponderosa pine to produce a wide range of specialty and industrial lumber products. This sawmill has an on-site cogeneration plant to produce electricity for its own use as well as steam for its dry kilns. At this location, we own and operate a short line railroad to connect to a mainline for shipment of lumber.

We also own and operate a value-added cedar remanufacturing facility in Sumas, Washington.

## U.S. Southeast

We own and operate nine sawmill operations in the U.S. South. Seven of these sawmills are located in Georgia (Baxley, Eatonton, Swainsboro, Thomaston, Preston, Perry and Meldrim), one is located in Georgetown, South Carolina and another in Monticello, Arkansas. These nine sawmills produce southern yellow pine lumber in a range of dimensions from 2x4 through 2x12 products, with 4x4 products also produced at certain mills.

We also own and operate a value-added southern yellow pine remanufacturing facility in Perry, Georgia.

## U.S. Timber Supply

### *U.S. Northwest*

Timber supply in the U.S. Northwest ("NW") is sourced from a broad distribution of forest land ownership (forest industrial lands; small private landowners; and State and Federal lands). These sources represent a long-term supply base from which mills purchase their timber supply. In 2016, approximately 58% of the log supply in the NW came from land that is owned by industrial and small private landowners, while the remainder was sourced from State, Federal and tribal lands.

Our timber supply requirements at the Port Angeles sawmill are weighted to western hemlock with lesser volumes of Douglas-fir. At our Longview location, we only purchase Douglas-fir. Douglas-fir is the prominent species, with smaller volumes of western hemlock and white fir at the Molalla sawmill. All three of our western Oregon and Washington sawmills depend on private industrial landowners and small private landowners for the majority of their supply. The remainder of their supply is comprised of timber from State, Federal, and tribal lands.

At the Gilchrist sawmill, log purchases consist primarily of lodgepole pine and ponderosa pine that are harvested from second growth forests and the thinning of young stands from surrounding National Forests. This volume is supplemented with purchases from industrial and non-industrial private lands.

### *U.S. Southeast*

Timber in the U.S. South is sourced primarily from privately held timberlands with only minor volumes coming from publicly owned timberlands. Private timberland ownership includes non-industrial private owners, timber real estate investment trusts ("timber REITs") and various institutional investors such as pension funds, who are typically represented by a timberland investment management organization ("TIMO"). Both timber REITs and TIMOs are considered industrial timberland owners. Interfor's sawmills in the U.S. South purchase timber comprised exclusively of southern yellow pine, originating from each of these sources.

The total 2017 log supply requirement for the mills in the U.S. is estimated to be supplied from the following sources:

<b>Expected Sources of Timber 2017</b>	<b>U.S. Northwest</b>	<b>U.S. South</b>
State, Federal and tribal lands	35%	1%
Industrial lands	58%	29%
Private lands	<u>7%</u>	<u>70%</u>
	<u>100%</u>	<u>100%</u>

## **SALES, MARKETING AND COMPETITIVE POSITION**

The global markets for the Company's products are highly competitive and producers compete primarily on the basis of price. In addition, a majority of Interfor's lumber production is sold into markets where competitors have the same or larger capacity and may be lower cost producers.

The following table shows our lumber sales by geographic area and total sales by product line for the past three years:

	<b>Years ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	(thousands of dollars)		
Lumber			
— U.S.A.	\$1,098,106	\$ 996,683	\$ 770,153
— Japan	123,878	124,252	107,561
— Canada	92,248	94,483	103,599
— China	59,102	66,581	109,205
— Other export	60,179	47,104	46,812
Offshore transportation and handling	24,783	32,089	39,928
	<u>1,458,296</u>	<u>1,361,192</u>	<u>1,177,258</u>
Logs	179,275	174,090	144,770
Wood chips and other residuals	145,608	141,717	105,506
Ocean freight, contract services and other	9,533	10,376	19,623
<b>Total sales</b>	<u><u>\$1,792,712</u></u>	<u><u>\$1,687,375</u></u>	<u><u>\$1,447,157</u></u>

### **Lumber Sales**

Like other commodities, the demand for lumber is cyclical. It is affected by factors such as interest rates, foreign currency exchange rates, freight rates, government tariffs and import policies, and overall demand.

In order to diminish the impact of rapid cyclical changes in any one market, we strategically target worldwide markets and offer a diverse range of products. Interfor also has a specific customer and product base in various countries, providing a diversified sales profile. Many of our operations are strategically located close to ports which allow us to fully realize on the opportunities that are available to us in our overseas markets.

Product and market diversification is particularly important as the variability inherent in the log resource produces a much wider spectrum of product sizes and quality. A continuing priority for our Company is to develop products and markets that more fully realize the potential for higher grades, special dimensions and value-added items.

Lumber sales and marketing activities are organized into two sales groups to leverage global expertise: Export and North America. Interfor Japan Ltd., with an office in Tokyo, has developed niche markets and has increased sales directly to end-users for the Japan market. We also have an office in France to serve Continental Europe and Middle Eastern markets, and a representative in China to support that country's growing demand for wood.

The primary market for our cedar product line continues to be North America where markets are serviced through a combination of regional wholesale distributors and direct retail sales. Gains have been made, however, in diversifying cedar sales into offshore markets in Europe, China, Japan and Australia.



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In North America, we currently service our customer base from three sales locations. Our cedar products are sold out of our office in Burnaby, B.C. Our office in Bellingham, Washington services our North American customers for products produced by our sawmills in Canada and the U.S. Northwest. Finally, our office in Peachtree City, Georgia services our customers for products produced by our sawmills in the U.S. South. In 2017, the Bellingham office will be relocated to Canada. Each of these offices leverages our regional knowledge of market segments and distribution channels.

### **Log Sales**

We purchase and sell logs in order to obtain the appropriate size, grade and species of log to suit market conditions and each mill's cutting profile. We buy or trade logs through agreements and open market transactions and sell logs that are either unsuitable for cutting or in excess of our manufacturing requirements.

### **Wood Chips and Other Residuals Sales**

As a by-product of lumber production, our sawmills produce wood chips and other residuals. Essentially all of our wood chips produced in B.C. are sold under short-term and long-term contracts to pulp producers. In general, wood chips produced on the B.C. Coast are sold at prices related to current Northern Bleached Softwood Kraft ("NBSK") pulp prices, while the wood chips produced in the B.C. Interior are sold at current market prices for chips. Chips from our U.S. Northwest and U.S. South operations are sold to pulp and paper producers or fibre board manufacturers under short-term arrangements, with the exception of the Baxley, Georgetown, Meldrim, Gilchrist, Longview and Port Angeles sawmills which each have a long-term contract with a pulp and paper producer.

### **DISTRIBUTION**

We use various modes of surface transportation to deliver our lumber products. Shipments to export markets are done by container and break-bulk vessels while shipments of lumber within North America are done by truck and rail. In 2016, break-bulk shipments were transported under contract with an independent ocean carrier and this same arrangement is in place for 2017. Chips and logs are normally delivered by tug and barge or by truck. In Gilchrist, Oregon, and in Grand Forks, B.C. we own short line railroads that connect to Class 1 railroads for shipping lumber and chips.

### **HUMAN RESOURCES**

In B.C., we directly employ approximately 1,162 people in our logging and manufacturing operations and corporate offices. The Canadian United Steel Workers ("USW") is the certified bargaining agent for approximately 556 of these people. The agreement with the USW for the B.C. Coast has an expiry date of June 14, 2019, while the Southern Interior USW agreement expires on June 30, 2018. The Canadian Marine Service Guild ("CMSG") represents 22 employees, and their collective agreement expires September 30, 2019.

In the U.S., we employ approximately 1,694 employees in our sawmill and remanufacturing operations in Washington, Oregon, Georgia, Arkansas, South Carolina and in our offices located in Bellingham, Washington and Peachtree City, Georgia. The International Association of Machinists ("IAM") is the certified bargaining agent for approximately 92 of these people employed in the Longview, Washington sawmill.

The IAM collective agreement expires on November 15, 2020.

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## **THE ENVIRONMENT**

Interfor is committed to responsible stewardship of the environment. We maintain an Environmental Management System ("EMS") for all of our woodlands and manufacturing facilities. The EMS provides a structure for identifying, addressing and managing environmental issues. Audits are performed regularly in both the woodlands and manufacturing operations to verify its effectiveness.

### *Regulatory Compliance*

Interfor operates in compliance with extensive provincial, state, federal or other laws and regulations that apply to most aspects of our business activities.

### *Forest Management Certification*

Interfor has achieved the internationally recognized Sustainable Forestry Initiative ("SFI") forest management certification for all of our B.C. woodlands operations. Independent third party certification audits are conducted by KPMG Performance Registrar Inc.

### *Chain of Custody and Responsible Purchasing*

Interfor maintains Chain-of-Custody ("CoC") certifications at certain mills and fibre sourcing procedures that track logs coming from sustainably managed forests through the manufacturing process.

### *Coast Forest Conservation Initiative*

Interfor is a member of the Coast Forest Conservation Initiative ("CFCI") – a collaborative effort of five B.C. forest product businesses committed to finding new approaches to forest conservation and management in B.C.'s Central and North Coast. CFCI collaborates with the Rainforest Solution Project (a group of environmental organizations) in a forum known as the Joint Solutions Project ("JSP"). JSP works with the B.C. Government and First Nations on strategic items related to the implementation of ecosystem based management ("EBM"). The joint work done by JSP is a major step towards fulfilling the landmark Great Bear Rainforest agreement announced by the province in 2016.

### *First Nations*

First Nations ("FN") groups have claimed Aboriginal title and rights over substantial portions of British Columbia. Interfor tenures overlap with the traditional territories of over 60 different FN groups. The Company's operations in B.C. account for approximately 30% of its total lumber production.

Interfor has a number of agreements and initiatives with FN in B.C., and remains committed to working with FN to develop economic opportunities of mutual benefit. Each FN group is notified prior to development activities as part of the Forest Stewardship Planning process.

### *Mountain Pine Beetle*

The Mountain Pine Beetle ("MPB") infestation has resulted in the mortality of a significant portion of the mature pine trees in the B.C. Interior. The greatest impact has been in the central interior region where there is a high percentage (over 60%) of pine in the forest. Interfor operations are in the southern interior which have a much lower percentage of pine (less than 30%) and are less affected by the MPB. The longer term timber supply impacts of the MPB are not expected to have a significant impact on the Company's operating areas.

### *Reforestation and Other Forestry-related Liabilities.*

Crown legislation requires the Company to complete reforestation activities on its forest and timber tenures. Accordingly, Interfor records the estimated liability for reforestation as timber is cut, and includes these expenses in the cost of current production. The estimate of future

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reforestation costs is based on detailed prescriptions of reforestation as prepared by Registered Professional Foresters employed or contracted by the Company. Considerations include the specifics of the areas logged and the treatments prescribed for those areas, as well as the timing and success rates of the planned activities. Estimates of reforestation liabilities are reviewed annually or more frequently if required, and can be materially impacted by forest fires, wildlife grazing, unfavourable weather conditions, changing legislative requirements and standards, or inaccurate projections, which could result in a charge against operating earnings.

The Company also has a legal obligation to deactivate certain roads constructed for access to timber, once that access is no longer required. Accordingly, Interfor accrues the cost of road deactivation as related timber is cut, including those expenses in the cost of current production. The estimate of future road deactivation cost is based on comprehensive plans prepared by professional foresters and engineers employed by Interfor and includes such considerations as road structure and terrain. Estimates of road deactivation liabilities are reviewed annually or more frequently if required, and can be materially impacted by unfavourable terrain, changing legislative requirements and standards, or inaccurate projections, which could result in a charge against operating earnings.

#### *Continual Improvement*

Each year a formal management review of the Company's sustainable forest management program and performance is completed as part of the process of continual improvement.

Additional information about our environmental work and third party certification is available on our website at [www.interfor.com](http://www.interfor.com).

### **RESEARCH AND DEVELOPMENT**

We contribute to and participate in industry research organizations that have made numerous technical developments beneficial to us in areas such as sawing technology, drying techniques and anti-sap stain applications. We also are committed to applied research and development in the areas of environment, health and safety, forest management, and product and market development. We also conduct product and market research on our own in Canada and the U.S.

### **RISK FACTORS**

Discussion of risk factors relating to the Company and its operations is included under the heading Risks and Uncertainties within Interfor's 2016 annual Management's Discussion and Analysis prepared as of February 09, 2017, which is incorporated by reference herein and available on SEDAR at [www.sedar.com](http://www.sedar.com).

### **CAPITAL STRUCTURE**

The authorized share structure of the Company consists of:

- 150,000,000 Common Shares without Par Value with Special Rights and Restrictions ("Common Shares"); and
- 5,000,000 Preference Shares without Par Value with Special Rights and Restrictions ("Preference Shares").

As at February 9, 2017 there were 70,030,455 Common Shares outstanding. There were no Preference Shares outstanding.

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**Common Shares**

Each holder of a Common Share is entitled to receive notice of and to attend and vote in person or by proxy at all meetings of the shareholders of the Company and is entitled to one vote for each such share held.

Each holder of a Common Share is entitled to receive such dividends as the directors may in their sole discretion declare from time to time. No holder of a Common Share will be entitled to any dividend other than or in excess of the dividends declared by the directors. Subject to any special rights or restrictions as to dividends attached to any Preference Shares issued and outstanding from time to time, the directors have the discretion to declare dividends on the Common Shares.

In the event of the liquidation, dissolution or winding-up of the Company or other distribution of its assets for the purpose of winding up its affairs, holders of the Common Shares will not receive any amount, property or asset, until the holders of the Preference Shares and any other class or series of shares entitled to receive assets of the Company in priority to the holders of the Common Shares, have first received the amount to which they are entitled. Thereafter, the holders of the Common Shares will be entitled to all remaining property and assets of the Company on a share for share basis.

**Preference Shares**

The Preference Shares may be issued in one or more series. The directors may by resolution fix the number of Preference Shares in each series, determine the designation of the Preference Shares of each series, and attach special rights and restrictions to the Preference Shares of each series.

The Preference Shares rank in priority over the Common Shares and any other shares ranking junior to the Preference Shares with respect to the payment of dividends and the distribution of assets of the Company in the event of the liquidation, dissolution or winding-up of the Company.

The registered holders of the Preference Shares shall not be entitled as a class to receive notice of or to attend or to vote at any meeting of shareholders of the Company, except in the event of matters affecting the priority rights or any other rights or restrictions attaching to the Preference Shares.

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**MARKET FOR SECURITIES OF THE COMPANY**

The Common Shares are listed on the Toronto Stock Exchange ("TSX") under the symbol IFP. The following table sets out the market price range and trading volumes of the Common Shares on the TSX for the periods indicated:

<b>Toronto Stock Exchange (TSX) 2016 Trading Volumes Ticker: IFP</b>			
<b>Month</b>	<b>\$ Low</b>	<b>\$ High</b>	<b>Volume</b>
January	8.96	14.19	9,288,577
February	8.67	11.24	7,512,936
March	11.05	14.52	7,401,891
April	10.75	14.53	9,241,946
May	10.48	13.74	7,090,033
June	10.21	13.33	7,243,624
July	10.90	14.94	5,838,105
August	14.32	15.99	6,393,442
September	13.79	15.94	4,685,717
October	14.18	15.83	4,770,610
November	13.54	15.20	3,531,182
December	14.16	15.85	2,427,988

**SECURITIES SUBJECT TO CONTRACTUAL RESTRICTION ON TRANSFER**

<b>Designation of class</b>	<b>Number of securities that are subject to a contractual restriction on transfer</b>	<b>Percentage of class</b>
Common Shares	3.68 million <sup>1</sup>	5.25%

**Note 1:** Until one year after the date that the Interfor director designated by Ilim Timber Continental, S.A. ("Ilim") has ceased to be a director of Interfor, Ilim may not sell or otherwise transfer its Common Shares (other than a pledge to an acceptable third party lender) without the prior written consent of Interfor.

**TRANSFER AGENT**

The transfer agent for our Common Shares is Computershare Investor Services Inc. at its principal offices in Vancouver, British Columbia.

**MATERIAL CONTRACTS**

The following material contracts were entered into by the Company during or after 2016, or before 2016 but are still in effect:

1. First Amendment dated February 6, 2015, and Second Amendment dated February 23, 2015, to the Asset Purchase Agreement between Simpson Lumber Company, LLC and Interfor U.S. Inc., amending the Asset Purchase Agreement, dated December 18, 2014, between Simpson Lumber Company, LLC and Interfor U.S. Inc. for the acquisition of four sawmills located in Meldrim, Georgia, Georgetown, South Carolina, Longview, Washington and Tacoma, Washington for total consideration of approximately US\$94.7 million, plus working capital and contingent future payments. The transaction closed on March 1, 2015.

2. Interfor February 2016 Amended and Restated Credit Agreement, dated for reference February 9, 2016, between the Company, each of the lenders named therein and Royal Bank of Canada in its capacity as the arranger and agent, which extended the maturity of the Company's US Operating Line and Revolving Term Line from February 27, 2017 to May 19, 2019. All other terms remained substantially unchanged except for an increase in the maximum ratio of total debt to total capitalization, which resulted in an increase in the maximum borrowing available under the credit agreement.
3. Second Amendment dated as of February 9, 2016 to Amended and Restated Note Purchase and Private Shelf Agreement dated as of March 16, 2015, between the Company and the Prudential Capital Group for a US\$100 million term debt financing with Prudential Capital Group. The senior secured notes carry an annual interest rate of 4.17% and have a final maturity date of March 26, 2026. The proceeds were used to reduce drawings under the Company's bank credit facilities.

All of these contracts are available on [www.sedar.com](http://www.sedar.com).

## **DIRECTORS AND OFFICERS**

### **Directors of the Company**

The following table sets out the Company's directors as of February 9, 2017, their respective municipalities of residence, positions and offices held with the Company, principal occupations within the past five years and the period during which each director has served as a director:

<b>Name and Municipality of Residence</b>	<b>Director Since</b>	<b>Positions Held and Principal Occupations</b>	<b>From</b>	<b>To</b>
<b>DUNCAN K. DAVIES</b> Vancouver, BC, Canada	November 1998	President and Chief Executive Officer Interfor Corporation	2000	Present
<b>PAUL HERBERT</b> Germantown, TN, USA	March 2014	Director Ilim Timber Incorporated, Ilim Timber Europe and Ener1 Inc., all private companies owned by a shareholder of Ilim Group, Russia's largest forest pulp & paper company	2013	Present
		Chief Executive Officer Ilim Group	2007	2013
<b>JEANE HULL</b> Sheridan, WY, USA	May 2014	Director Cloud Peak Energy Inc. (NYSE: CLD)	2017	Present
		Executive Vice President and Chief Technical Officer Peabody Energy Corporation, a private-sector coal company	2011	2015
<b>PETER M. LYNCH</b> Toronto, ON, Canada	October 2006	Chair Dieffenbacher USA, Inc., a manufacturer and designer of press and forming systems	2017	Present
		President & CEO Dieffenbacher USA, Inc.	2013	2016
		Independent Business Consultant	2010	2013

<b>Name and Municipality of Residence</b>	<b>Director Since</b>	<b>Positions Held and Principal Occupations</b>	<b>From</b>	<b>To</b>
<b>GORDON. H. MacDOUGALL</b> West Vancouver, BC, Canada	February 2007	Director Connor, Clark & Lunn Financial Group, an asset management company.	2014	Present
		Vice Chair Connor, Clark & Lunn Investment Management Ltd.	2006	2014
		Partner Connor, Clark & Lunn Investment Management Partnership	1986	2014
<b>J. EDDIE McMILLAN</b> Pensacola, FL, USA	October 2006	Independent Business Consultant	2002	Present
<b>THOMAS V. MILROY</b> Toronto, ON, Canada	February 2016	Director Restaurant Brands International Inc. (TSX/NYSE: QSR, TSX: QSP)	2014	Present
		Director Tim Hortons Inc.	2013	2014
		Managing Director Generation Capital Limited, a private investment company	2015	Present
		Chief Executive Officer BMO Capital Markets	2008	2014
<b>GILLIAN PLATT</b> Kelowna, BC, Canada	October 2016	Director CRH plc (LSE: CRH, ISE: CRG, NYSE: CRH), an Irish based building materials group	2017	Present
		Executive Vice President and Chief Human Resources Officer Finning International Inc., a distributor of Caterpillar products and support services	2014	2016
		Principal Gillian Platt & Associates, executive advisory and coaching practice	2013	2014
		Executive Vice President, Human Resources Aviva North America, a multi-national insurance company	2011	2012
<b>E. LAWRENCE SAUDER</b> Vancouver, BC, Canada	April 1984	Chair Metrie Canada Ltd. (formerly Sauder Industries Limited), a manufacturer and distributor of interior finishings	2010	Present
		Chief Executive Officer, Metrie Canada Ltd. (formerly Sauder Industries Limited), a manufacturer and distributor of building products	2010	2014
		Chair Hardwoods Distribution Inc. (TSX: HWD), a distributor of wood products	2008	Present

Name and Municipality of Residence	Director Since	Positions Held and Principal Occupations	From	To
DOUGLAS W.G. WHITEHEAD West Vancouver, BC, Canada	April 2007	Director Finning International Inc. (TSX: FTT), a distributor of Caterpillar products and support services	2008	Present
		Director Belkorp Industries Inc.	2000	Present
		Director Kal Tire	2012	Present

To our knowledge, two of the Company's directors have in the last 10 years been an officer or director of a company that was subject to bankruptcy or similar proceedings or securities regulatory sanctions described in National Instrument 51-102 *Continuous Disclosure Obligations* while that person was acting in that capacity, or that resulted from an event that occurred while that person was acting in that capacity. From 1993 to 2010, Mr. Lynch was an executive officer and director of Grant Forest Products Inc. ("Grant Forest"). On June 25, 2009, Grant Forest and certain affiliated entities filed and obtained protection under the Companies' Creditors Arrangement Act in order to restructure their business affairs and on November 27, 2015, Grant Forest filed for bankruptcy. From April 2011 to July 31, 2015, Ms. Hull was the Executive Vice President and Chief Technical Officer of Peabody Energy Corporation ("Peabody"). Peabody filed for Chapter 11 bankruptcy protection on April 13, 2016.

The term of office for all current directors will end at the conclusion of the next Annual General Meeting of the Company's shareholders. The next Annual General Meeting is scheduled for Thursday, May 4, 2017.

### Committees of the Board

The table below lists the committees of Interfor's board of directors and their members as of February 9, 2017:

Committees	Members
Audit	Douglas Whitehead (Chair) Jeane Hull Eddie McMillan Tom Milroy
Corporate Governance & Nominating Committee	Eddie McMillan (Chair) Gord MacDougall Peter Lynch Paul Herbert
Management Resources & Compensation Committee	Gord MacDougall (Chair) Lawrence Sauder Peter Lynch Gillian Platt Doug Whitehead
Environment & Safety Committee	Jeane Hull (Chair) Paul Herbert Tom Milroy Gillian Platt Lawrence Sauder



## Officers of the Company

The following table sets out the Company's officers as of February 9, 2017, their respective municipalities of residence and their principal occupations for at least the last five years:

<b>Name and Municipality of Residence</b>	<b>Positions Held and Principal Occupations</b>	<b>From</b>	<b>To</b>
<b>DUNCAN K. DAVIES</b> Vancouver, BC, Canada	President & Chief Executive Officer Interfor Corporation	2000	Present
<b>JOHN A. HORNING</b> West Vancouver, BC, Canada	Executive Vice President & Chief Financial Officer Interfor Corporation	2014	Present
	Senior Vice President & Chief Financial Officer Interfor Corporation	2002	2014
<b>MARTIN L. JURAVSKY</b> Toronto, ON, Canada	Senior Vice President, Corporate Development and Strategy Interfor Corporation	2014	Present
	Vice President, Corporate Development and Strategy Interfor Corporation	2013	2014
	Business Consultant	2012	2013
<b>IAN M. FILLINGER</b> Kamloops, BC, Canada	Senior Vice President, Head of Operations Interfor Corporation	2015	Present
	Senior Vice President, Canadian Operations Interfor Corporation	2014	2015
	Vice President, Canadian Operations Interfor Corporation	2013	2014
	Senior General Manager Interfor Corporation	2013	2013
	General Manager, Adams Lake & Coastal Manufacturing Interfor Corporation	2012	2013
	General Manager, Adams Lake Division Interfor Corporation	2005	2012
<b>MARK W. STOCK</b> North Vancouver, BC, Canada	Senior Vice President, Human Resources Interfor Corporation	2014	Present
	Vice President, Human Resources Interfor Corporation	2012	2014
	Vice President, Global Human Resources Tree Island Industries Ltd.	2007	2012
<b>BART BENDER</b> West Vancouver, BC, Canada	Senior Vice President, Sales & Marketing Interfor Corporation	2015	Present
	Senior Vice President, Operations Ainsworth Lumber Co.	2014	2015
	Vice President, Sales Ainsworth Lumber Co.	2012	2014
	General Manager, Sales Ainsworth Lumber Co.	2002	2012

<b>XENIA KRITSOS</b> Vancouver, BC, Canada	General Counsel & Corporate Secretary Interfor Corporation	2015	Present
	General Counsel & Corporate Secretary Coalspur Mines Limited	2013	2015
	Senior Legal Counsel Hunter Dickinson Services Inc.	2009	2013

### **SHAREHOLDINGS OF DIRECTORS AND OFFICERS**

As at December 31, 2016, the directors and officers of the Company as a group owned, directly or indirectly, or exercised control of or direction over 921,657 Common Shares representing approximately 1.32% of the outstanding Common Shares.

### **INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS**

Since the commencement of our most recently completed financial year, and for the three most recently completed financial years, no director or executive officer of the Company, no person or company that is the direct or indirect beneficial owner of, or who exercises control or direction over, more than 10% of the Company's voting securities or any associate or affiliate of such persons, has had any material interest in any transaction involving the Company.

### **LEGAL PROCEEDINGS**

We are not a party to, and our property is not the subject of, any material legal proceedings that took place in 2016, are currently underway, or which we know to be contemplated. In November 2016, U.S. softwood lumber producers filed antidumping and countervailing duty petitions with the U.S. Department of Commerce ("DOC"), alleging that dumped and subsidized Canadian imports are causing material injury to the U.S. domestic industry. Although Interfor has not been selected as a mandatory respondent in either of the antidumping or countervailing duty investigations, the outcome of these investigations will likely affect Interfor.

### **INTEREST OF EXPERTS**

KPMG LLP are the external auditors of the Company and have confirmed that they are independent with respect to the Company within the meaning of the Rules of Professional Conduct of Institute of Chartered Professional Accountants of British Columbia and the applicable rules and regulations thereunder.

### **AUDIT COMMITTEE INFORMATION**

The Company's Audit Committee (the "Committee") is mandated to oversee the accounting and financial reporting processes of the Company and audits of its financial statements in accordance with the Board's objectives. The Committee's functions include:

- reviewing and, if appropriate, recommending approval by the Board of the Company's annual and quarterly financial statements, management's discussion and analysis and earnings press releases;
- reviewing and approving disclosures required to be included in the Company's Annual Information Form and Management Information Circular relating to the Audit Committee and audit and non-audit services and fees;
- reviewing the process for certification, and the certification, of the interim and annual financial statements by the Chief Executive Officer and Chief Financial Officer;

- 
- reviewing all public disclosure containing financial results or financial information;
  - reviewing matters related to internal controls over financial reporting of the Company and ensuring the Company has adequate internal controls procedures in place;
  - reviewing the principal risks of the Company, other than the risks associated with the Company's compensation policies and practices, and ensuring that an effective risk management strategy is in place;
  - reviewing the Company's derivatives policies and activities, including details of exposures to banks and other counterparties;
  - overseeing the activities of and directly communicating with the Company's external auditor;
  - satisfying itself that adequate procedures are in place for the review of the public disclosure of financial information extracted or derived from the Company's financial statements and periodically assessing the adequacy of those procedures;
  - establishing and periodically reviewing the policies and procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, and the confidential, anonymous submissions by the employees of the Company regarding questionable accounting or auditing matters;
  - reviewing and approving the Company's hiring policies regarding partners, employees and former partners and employees of the former and present Auditor; and
  - reviewing the Company's insurance programs, including the Company's directors' and officers' insurance coverage, and making recommendations for their renewal or replacement.

The Committee's Terms of Reference, attached as Appendix "A" to this Annual Information Form, sets out its duties and responsibilities.

The Committee met four times in 2016, in conjunction with regularly scheduled Board meetings.

### **Members' Financial Literacy, Expertise and Simultaneous Service**

The board of directors has determined that the members of the Audit Committee during 2016 were, and all current members of the Audit Committee are, financially literate and independent as defined in *National Instrument 52-110 – Audit Committees*. The table below indicates the relevant education and experience of each member of the Audit Committee:

## Relevant Education and Experience

Director	Past Occupation
<p><b>Douglas W.G. Whitehead</b> Chair of the Audit Committee since May 2012</p>	<p>Mr. Whitehead is currently a director of Finning International Inc. (TSX: FTT) ("Finning"), Belcorp Industries Inc. and Kal Tire. From 2008 to 2016 Mr. Whitehead was Board Chair, and from 2000 to 2008 he was the President and Chief Executive Officer, of Finning. Prior to joining Finning, Mr. Whitehead held a number of senior executive positions with Fletcher Challenge Canada, including President and Chief Executive Officer, Senior Vice President and Chief Operating Officer and Vice President of the Crown Packaging Division. Previously, he served as director of Inmet Mining Corporation, Ballard Power Systems Inc., Terasen Inc., Fletcher Challenge Canada, Finlay Forest Industries and Timberwest Forest Limited. Mr. Whitehead holds a Bachelor of Applied Science (Engineering) from the University of British Columbia and a Master of Business Administration from the University of Western Ontario.</p>
<p><b>Jeane Hull</b> Member since April 2016</p>	<p>Ms. Hull is currently a director of Cloud Peak Energy Inc. (NYSE: CLD). From 2011 to 2015, she was Executive Vice President and Chief Technical Officer at Peabody Energy Corporation, a private-sector coal company. Prior to joining Peabody in 2007, she held numerous management, engineering and operations positions with Rio Tinto and its affiliates, lastly as COO of the Kennecott Utah Copper business. Prior thereto, she spent 12 years with Mobil Mining and Minerals, and Mobil Chemical Company. She is Chair of the University of Wyoming School of Energy Resources Council. She also serves on the Advisory Board for South Dakota School of Mines and Technology. She holds a Bachelor of Science (Civil Eng.) from South Dakota School of Mines &amp; Technology and a Master of Business Administration from Nova Southeastern University.</p>
<p><b>Eddie McMillan</b> Member since April 2016</p>	<p>Mr. McMillan is an independent business consultant. From 1998 until his retirement in 2002, he was Executive Vice President – Wood Products Group of Willamette Industries Inc., a forest products company. Prior to 1998, Mr. McMillan held various management positions with Willamette Industries Inc. Over the years, he has served as a director of Forest Express, Inc. and has been associated with numerous industry association boards, including the American Plywood Association, National Particleboard Association, Particleboard and MDF Institute, Southern Forest Products Association, Western Wood Products Association, National Association of Lumber Wholesalers and the American Forest and Paper Association. He holds a Bachelor of Science (Accounting/Business Administration) from Louisiana Tech University.</p>
<p><b>Tom Milroy</b> Member since April 2016</p>	<p>Mr. Milroy is a director of Restaurant Brands International Inc. (TSX/NYSE: QSR, TSX: QSP) and has served on that board since 2014. Prior to that, he was a director of Tim Hortons Inc. from August 2013 to December 2014. He is currently Managing Director of Generation Capital Limited, a private investment company. From March 2008 to October 2014, he served as Chief Executive Officer of BMO Capital Markets, where he was responsible for all of BMO's business involving corporate, institutional and government clients globally. Mr. Milroy holds a Bachelor of Law and Master of Law from Cambridge University, an LLB from Dalhousie University, and a Bachelor of Arts from McGill University. He has also completed the Advanced Management Program at the Harvard Business School. Mr. Milroy is a member of the Law Society of Upper Canada.</p>

## AUDIT FEES

The Committee annually recommends the appointment of the Company's external auditors and approves the annual audit plan and compensation of the external auditors for all audit, audit related and non-audit services. In the case of non-audit services, the services and compensation are approved by the Committee before the services commence.

KPMG LLP, Chartered Professional Accountants, Vancouver, are the independent auditors of the Company. Fees paid or accrued to KPMG LLP for audit and other services for the years ended December 31, 2015 and December 31, 2016, were as follows:

	<b>2016</b>	<b>2015</b>
<b>Audit fees</b>		
Fees billed for professional services rendered.	\$538,200	\$581,256
<b>Audit-related fees</b>		
Audit-related fees consist principally of fees for professional services rendered with respect to audits of a defined benefit pension plan and subsidiary companies (2016 and 2015) and bought deal financing involvement (2015).	46,826	183,738
<b>Tax fees</b>		
Tax fees consist of fees for tax compliance services, planning and related services, personal tax (foreign and domestic) compliance and planning advice, indirect tax recovery audit contingency fees which are based on percentage of recoveries (2016 and 2015), and advice on setup of Insurance Captive (2015).	43,177	88,731
<b>All Other fees</b>		
Forestry certification (2016 and 2015); advice on leading practice for IT procurement (2015).	66,300	99,800
<b>TOTAL</b>	<b>\$694,503</b>	<b>\$953,525</b>

## **CODE OF ETHICS**

We have adopted a code of ethics that applies to our directors, officers and employees. A copy of the code, entitled "Code of Conduct & Ethics", can be found on our website at [www.interfor.com](http://www.interfor.com).

## **ADDITIONAL INFORMATION**

Additional information relating to the Company, including directors' and officers' remuneration and indebtedness, principal holders of the Company's securities and securities authorized for issuance under equity compensation plans, is contained in the Company's Information Circular for its most recent annual meeting of shareholders that involved the election of directors.

Additional financial information about the Company is provided in the Company's audited consolidated financial statements and Management's Discussion and Analysis for the year ended December 31, 2016.

Copies of the documents referred to above and additional information relating to the Company are available on SEDAR at [www.sedar.com](http://www.sedar.com), on the Company's website [www.interfor.com](http://www.interfor.com) and may also be obtained upon request from:

Interfor Corporation  
 General Counsel & Corporate Secretary  
 3500-1055 Dunsmuir Street  
 Vancouver, British Columbia  
 Canada, V7X 1H7  
 Telephone: 604 689 6800  
 Facsimile: 604 689 6825  
 E-mail: [corporatesecretary@interfor.com](mailto:corporatesecretary@interfor.com)

## Appendix "A"

**AUDIT COMMITTEE  
Terms of Reference****PURPOSE**

The Audit Committee has been established by the Board and under powers delegated to it by the Board is mandated to oversee the accounting and financial reporting processes of the Company and audits of its financial statements in accordance with the Board Objective.

**COMPOSITION AND TERM OF OFFICE**

1. The Audit Committee shall consist of four or more Directors.
2. All members of the Audit Committee shall be independent within the meaning of *National Instrument 52-110* ("**NI 52-110**").
3. All members must be financially literate within the meaning of NI 52-110 or become financially literate within a reasonable period following appointment and at least one member should have accounting or related expertise.
4. The Chair of the Audit Committee along with other Audit Committee members will be appointed annually by the Board following the AGM to hold office until the next AGM, unless any member becomes unable to serve or is removed by the Board. A casual vacancy may be filled and additional members may be appointed at any time by the Board to hold office until the next AGM.
5. A quorum shall consist of a simple majority.

**DUTIES AND RESPONSIBILITIES**

The Audit Committee shall perform the following functions, as well as any other functions specifically authorized by the Board:

**Financial Disclosure, Risk Management and Internal Controls**

1. Review the following documents before the public disclosure of same by the Company, and, if appropriate, recommend approval by the Board of the Company's:
  - a. annual and quarterly financial statements;
  - b. Management's Discussion and Analysis; and
  - c. annual and interim earnings press releases.

The review will involve direct discussions with Management and the Company's external auditor (the "**Auditor**"), including an opportunity for an in-camera meeting with the Auditor independent of Management.

2. Review and approve the disclosures required by applicable securities laws to be included in the Company's Annual Information Form and Management Information Circular relating to the Audit Committee and audit and non-audit services and fees.
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3. Review the process for certification of the interim and annual financial statements by the Chief Executive Officer (“**CEO**”) and Chief Financial Officer (“**CFO**”) and the certification made by the CEO and CFO.
4. Review all news releases announcing financial results, containing financial information based on unreleased financial results or non-GAAP financial measures or providing earnings guidance, forward-looking financial information and future-oriented financial information or financial outlooks before the public disclosure of same by the Company.
5. Review financial information contained in any prospectus, take-over bid circular, issuer bid circular, rights offering circular and any other document that the Audit Committee is to review before the public disclosure of same by the Company, and, if appropriate, recommend approval by the Board.
6. Review matters related to internal controls over financial reporting of the Company and ensure the Company has adequate procedures in place in respect thereof. Ensure that the necessary measures are taken to follow up suggestions from the Auditor’s reports.
7. Review the principal risks of the Company, other than the risks associated with the Company’s compensation policies and practices, and ensure that an effective risk management strategy is in place.
8. Review the Company’s derivatives policies and activities, including details of exposures to banks and other counterparties.

#### **External Auditor**

9. Review and recommend to the Board the appointment of the Auditor to be nominated for the purposes of preparing or issuing an Auditor’s report and performing other audit, review or attest services for the Company.
10. Establish the mandate of the Auditor, including the annual engagement, audit plan, audit scope and compensation for the audit services, subject to shareholder approval.
11. Oversee the activities of the Auditor. The Auditor shall report directly to the Audit Committee.
12. Directly communicate and meet with the Auditor, with and without Management present, to discuss the results of their examinations.
13. Review the independence of the Auditor, any rotation of the partners assigned to the audit in accordance with applicable laws and professional standards, the internal quality control findings of the Auditor’s firm and peer reviews.
14. Review the performance of the Auditor, including the relationship between the Auditor and Management and the evaluation of the lead partner of the Auditor.
15. Resolve disagreements between Management and the Auditor regarding financial reporting.
16. Review material written communications between the Auditor and Management.

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**Non-Audit Services**

17. Pre-approve non-audit services. The Audit Committee may delegate to one or more of its members the authority to pre-approve non-audit services. The pre-approval of non-audit services by any member to whom authority has been delegated shall be presented to the Committee at its first scheduled meeting following such pre-approval.

**Company Policies**

18. Satisfy itself that adequate procedures are in place for the review of the public disclosure of financial information extracted or derived from the Company's financial statements and periodically assess the adequacy of those procedures.
19. Establish and periodically review the policies and procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, and the confidential, anonymous submissions by the employees of the Company regarding questionable accounting or auditing matters.
20. Review and approve the Company's hiring policies regarding partners, employees and former partners and employees of the former and present Auditor.

**Insurance**

21. Review the Company's insurance programs, including the Company's directors' and officers' insurance coverage, and make recommendations for their renewal or replacement.

**MEETINGS AND PROCEDURES**

1. The Audit Committee shall meet a minimum of four (4) times per year and, subject to these Terms of Reference and applicable law, otherwise establish its procedures and govern itself as the members of the Audit Committee may see fit in order to carry out and fulfill its duties and responsibilities hereunder. Extraordinary meetings of the Audit Committee may be called at the request of a member on the Audit Committee or the Chair of the Board to be held at such times and places as the person calling such meeting may determine.
  2. A majority of members of the Audit Committee will constitute a quorum (provided that a quorum shall not be less than two (2) members). Decisions of the Audit Committee will be by an affirmative vote of the majority of those members of the Audit Committee voting at a meeting. In the event of an equality of votes, the Chair will not have a casting or deciding vote. The Audit Committee may also act by resolution in writing signed by all the members of the Audit Committee.
  3. The Audit Committee shall appoint a Secretary who shall keep minutes or other records of its meetings and proceedings.
  4. The Chair of the Audit Committee shall report to the Board at its next regular meeting the Audit Committee's deliberations and recommendations, if any, requiring the Board's approval.
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**OTHER MATTERS**

1. The Audit Committee is authorized to engage any outside advisor it deems necessary to carry out its duties and responsibilities and to arrange payment of the advisor's compensation by the Company.
2. The Audit Committee may, at the request of the Board or at its own initiative, investigate such other matters as it considers appropriate in furtherance of the Audit Committee's purpose.

## GLOSSARY

**Unless otherwise noted, all financial references in this Annual Report are in Canadian Dollars.**

**“Adjusted EBITDA”** EBITDA excluding long term incentive compensation, other income (expense), Beaver sawmill post-closure wind-down costs and Tacoma sawmill post-acquisition losses and closure costs.

**“Adjusted Net Earnings”** Net earnings (loss) before restructuring costs, asset write-downs and other costs, other foreign exchange gains (losses), long term incentive compensation, other income (expense), Beaver sawmill post-closure wind-down costs, Tacoma sawmill post-acquisition losses and closure costs, the income tax effect of the aforementioned adjustments, and recognition of previously unrecognized deferred tax assets.

**“Allowable Annual Cut (AAC)”** The average annual volume of timber which the holder of a licence from the Province of British Columbia may harvest on Crown land under the licence in a five-year control period.

**“Cash flow from operations”** Cash flow provided by operating activities before considering changes in operating working capital.

**“Custom cutting”** An arrangement under which a mill contracts to cut logs owned by a customer into products of specifications defined by the customer.

**“Crown”** Administrative agency of the provincial government of British Columbia

**“EBITDA”** Earnings before finance costs, income taxes, depreciation, depletion, amortization, restructuring costs, asset write-downs and other costs, and other foreign exchange gains (losses).

**“Forest Licence”** Replaceable, volume-based timber cutting rights for a specific volume of Crown timber within a Timber Supply area.

**“Invested Capital”** The total of Net debt and shareholders’ equity.

**“m<sup>3</sup>”** A measure of one cubic metre of solid wood, British Columbia metric scale, as determined under the *Forest Act*, equal to 35.3 cubic feet of solid wood.

**“mfbm”** or **“Mbf”** One thousand foot board measure equal to one thousand square feet of lumber, one inch thick.

**“Net debt”** The total of long term debt and bank indebtedness, less cash and cash equivalents.

**“Pre-tax return on total assets”** Earnings (loss) before income taxes, restructuring costs, asset write-downs and other costs, other foreign exchange gains (losses) and other income (expense), divided by the average of opening and closing total assets for annual periods or by opening total assets for three month periods.

**“Silviculture”** The art and science of controlling the establishment, growth, composition, health and quality of forests.

**“Stumpage”** A charge assessed by the provincial government on all Crown timber harvested.

**“Sustained yield (sustainable log supply)”** The yield that a forest area can produce on an ongoing basis without impairment of the long-term productivity of the land.

**“Timber Licence”** Non-replaceable, area based, Crown timber cutting rights.

**“Tree Farm Licence”** A renewable 25-year licence to manage a forest area to yield an annual harvest on a sustainable basis.

**“Value-added product”** A commodity or other product that has been further processed to increase financial value.

**“Whitewood”** Includes the Coastal species Hemlock, Balsam Fir, Douglas-Fir and Spruce; the term whitewood is used on the British Columbia Coast to differentiate the above species from Western Red Cedar and Yellow Cedar.

## DIRECTORS

### As of March 15, 2017

**Duncan K. Davies**

Vancouver, BC, Canada

**Jeane Hull**

Sheridan, WY, US

**Gordon H. MacDougall**

West Vancouver, BC, Canada

**Thomas V. Milroy**

Toronto, ON, Canada

**E. Lawrence Sauder**

Vancouver, BC, Canada

**Paul Herbert**

Germantown, TN, US

**Peter M. Lynch**

Toronto, ON, Canada

**J. Eddie McMillan**

Pensacola, FL, US

**Gillian Platt**

Kelowna, BC, Canada

**Douglas W.G. Whitehead**

West Vancouver, BC, Canada

## OFFICERS

### As of March 15, 2017

**E. Lawrence Sauder**

Chair

**John A. Horning**

Executive Vice President &  
Chief Financial Officer

**Ian M. Fillinger**

Senior Vice President, Head of Operations

**Bart Bender**

Senior Vice President, Sales & Marketing

**Duncan K. Davies**

President & Chief Executive Officer

**Martin L. Juravsky**

Senior Vice President, Corporate  
Development & Strategy

**Mark W. Stock**

Senior Vice President, Human Resources

**Xenia Kritsos**

General Counsel & Corporate Secretary

## CORPORATE INFORMATION

<b>Stock Exchange</b> Common Shares listed on The Toronto Stock Exchange Symbol: IFP	<b>Auditors</b> KPMG LLP, Vancouver, BC	<b>Transfer Agent</b> Computershare Investor Services Inc. Vancouver, BC and Toronto, ON
<b>Investor Contact</b> Martin Juravsky Senior Vice President, Corporate Development & Strategy Tel: (604) 689-6873 <a href="mailto:martin.juravsky@interfor.com">martin.juravsky@interfor.com</a>	<b>Corporate Office</b> Tel: (604) 689-6800 Fax: (604) 688-0313 P.O. Box 49114 3500-1055 Dunsmuir Street Vancouver, BC V7X 1H7	

## SALES AND MARKETING

<b>North America – Cedar</b> Tel: (604) 422-3400 Fax: (604) 422-3244 1600 - 4720 Kingsway Metrotower II Burnaby, BC, Canada V5H 4N2	<b>North America – Southern Yellow Pine</b> Tel: (770) 282-3250 Fax: (770) 486-6837 700 Westpark Drive Peachtree City, GA, US 30269	<b>North America - Whitewood</b> Tel: (360) 788-2200 Fax: (360) 788-2210 2211 Rimland Drive, Suite 220 Bellingham, WA, US 98226
<b>China</b> Tel: +86-21-6333-6268 Fax: +86-21-6333-6290 Unit 1007, Tower No. 1 No. 268 Zhongshan South Road Shanghai, 200010, China	<b>Japan</b> Tel: 03-5641-2351 Fax: 03-5641-2383 Kasahara Bldg. 6F, 1-7-7 Nihonbashi, Ningyocho, Chuo-ku Tokyo, Japan 103 - 0013	<b>Europe</b> Tel: +33-2-40-32-05-25 Fax: +33-2-40-32-02-25 ZI Cheviré 7 rue de l'Houmaille 44340 BOUGUENNAIS, France
<b>Export – All Species/Inquiries</b> Tel: (604) 422-3468 Fax: (604) 422-3250 1600-4720 Kingsway Metrotower II Burnaby, BC, Canada V5H 4N2		

## OPERATIONS AND LOCATIONS

<p><b>Acorn Division (Sawmill)</b> Tel: (604) 581-0494 Fax: (604) 581-5757 9355 Alaska Way Delta, BC V4C 4R7</p>	<p><b>Adams Lake Division (Sawmill and Woodlands)</b> Tel: (250) 679-3234 Fax: (250) 679-3545 9200 Holding Road Chase, BC V0E 1M2</p>	<p><b>Baxley Division (Sawmill)</b> Tel: (912) 367-3671 Fax: (912) 367-1500 1830 Golden Isles East Baxley, GA 31513</p>
<p><b>Castlegar Division (Sawmill and Woodlands)</b> Tel: (250) 365-4400 Fax: (604) 422-3252 P.O. Box 3728 2705 Arrow Lakes Drive Castlegar, BC V1N 3W4</p>	<p><b>Cedarprime (Remanufacturing)</b> Tel: (360) 988-2120 Fax: (360) 988-2126 601C West Front Street Sumas, WA 98295</p>	<p><b>Coastal Woodlands Division (Woodlands)</b> Tel: (250) 286-1881 Fax: (250) 286-3412 1250A Ironwood Street Campbell River, BC V9W 6H5</p>
<p><b>Eatonton Division (Sawmill)</b> Tel: (706) 485-4271 Fax: (706) 485-3879 370 Dennis Station Road SW Eatonton, GA 31024</p>	<p><b>Georgetown Division (Sawmill)</b> Tel: (843) 546-6138 Fax: (843) 527-4033 2701 Indian Hut Road Georgetown, SC 29440-9146</p>	<p><b>Gilchrist Division (Sawmill)</b> Tel: (541) 433-2222 Fax: (541) 433-9581 P.O. Box 638 #1 Sawmill Road Gilchrist, OR 97737</p>
<p><b>Grand Forks Division (Sawmill and Woodlands)</b> Tel: (250) 443-2400 Fax: (604) 422-3253 P.O. Box 39 570 68th Ave. Grand Forks, BC V0H 1H0</p>	<p><b>Hammond Division (Sawmill)</b> Tel: (604) 465-5401 Fax: (604) 422-3221 20580 Maple Crescent Maple Ridge, BC V2X 1B1</p>	<p><b>Longview Division (Sawmill)</b> Tel: (360) 575-3600 Fax: (360) 575-3628 540 3<sup>rd</sup> Ave. Longview, WA 98632</p>
<p><b>Meldrim Division (Sawmill)</b> Tel: (912) 748-7310 Fax: (912) 748-8354 911 Old River Road Bloomingdale, GA 31302</p>	<p><b>Molalla Division (Sawmill)</b> Tel: (503) 829-9131 Fax: (503) 829-5481 15555 S. Hwy. 211 Molalla, OR 97038</p>	<p><b>Monticello Division (Sawmill)</b> Tel: (870) 224-7200 Fax: (870) 367-7924 211 Old Troy Road Monticello, AR 71655</p>
<p><b>Perry Division (Sawmill &amp; Remanufacturing)</b> Tel: (478) 987-2105 Fax: (478) 987-5773 903 Jernigan Street Perry, GA 31069-3435</p>	<p><b>Port Angeles Division (Sawmill)</b> Tel: (360) 457-6266 Fax: (360) 457-1486 243701 Highway 101 West Port Angeles, WA 98363</p>	<p><b>Preston Division (Sawmill)</b> Tel: (229) 828-4265 Fax: (229) 828-4370 378 Tolleson Road Preston, GA 31824</p>
<p><b>Swainsboro Division (Sawmill)</b> Tel: (912) 562-4441 Fax: (912) 562-3621 8796 Highway 297 Swainsboro, GA 30401</p>	<p><b>Thomaston Division (Sawmill)</b> Tel: (706) 648-4900 Fax: (706) 646-3534 75 Ben Hill Road Thomaston, GA 30286</p>	

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