

# **WESTERN FOREST PRODUCTS INC.**



**Annual Information Form – February 25, 2009**

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## **FORWARD-LOOKING STATEMENTS AND INFORMATION**

*This Annual Information Form contains statements which constitute forward-looking statements and forward-looking information within the meaning of applicable securities laws. Those statements and information appear in a number of places in this document and include statements and information regarding our current intent, belief or expectations primarily with respect to market and general economic conditions, future costs, expenditures, available harvest levels and our future operating performance, objectives and strategies. Such statements and information may be indicated by words such as “estimate”, “expect”, “anticipate”, “plan”, “intend”, “believe”, “should”, “may” and similar words and phrases. Readers are cautioned that it would be unreasonable to rely on any such forward-looking statements and information as creating any legal rights, and that the statements and information are not guarantees and may involve known and unknown risks and uncertainties, and that actual results and objectives and strategies may differ or change from those expressed or implied in the forward-looking statements or information as a result of various factors. Such risks and uncertainties include, among others: general economic conditions, competition and selling prices, changes in foreign currency exchange rates, labour disruptions, natural disasters, relations with First Nations groups, changes in laws, regulations or public policy, misjudgments in the course of preparing forward-looking statements or information, changes in opportunities and other factors. The information contained in this Annual Information Form, including, without limitation, the information set forth under the heading “Business of the Company” and “Risk Factors” and the information contained in our consolidated financial statements and accompanying management’s discussion and analysis for the year ended December 31, 2008, identifies important factors that could cause such differences. All written and oral forward-looking statements or information attributable to us or persons acting on our behalf are expressly qualified in their entirety by the foregoing cautionary statements. Except as required by law, Western Forest Products Inc. does not expect to update forward-looking statements or information as conditions change.*

## THE COMPANY

In this Annual Information Form, unless the context otherwise requires, “Western”, “Company”, “we”, “us”, “our” and similar terms refer to Western Forest Products Inc. and its subsidiaries.

Western’s business is timber harvesting and lumber manufacturing for worldwide markets. Western’s operations are located in the Coastal region of British Columbia. Western’s head office is located at 3rd Floor, 435 Trunk Road, Duncan, British Columbia, V9L 2P9 and the registered office is located at Suite 3000, 1055 West Georgia Street, Vancouver, British Columbia, V6E 3R3.

The Company was incorporated as 4204247 Canada Inc. under the Canada Business Corporations Act on April 27, 2004 and changed its name to Western Forest Products Inc. on June 21, 2004. On July 27, 2004, Western acquired the solid wood assets and certain pulp assets of Doman Industries Limited (“Doman”) and certain related companies. Western commenced business on July 28, 2004 and on August 3, 2004, the Common Shares began trading on the Toronto Stock Exchange and trade under the symbol “WEF”. In June 2006, Western’s articles were amended to create non-voting shares.

As at February 25, 2009 Tricap Management Limited (“Tricap”), an indirect wholly-owned subsidiary of Brookfield Asset Management (“BAM”) owns 63,026,544 (49%) of the Company’s Common Shares and 338,945,860 (100%) of the Non-Voting Shares.

Certain other terms used in this Annual Information Form are defined under “*Glossary of Certain Terms*”, which can be found at the end of this document, starting at page 36. All information in this Annual Information Form is as of February 25, 2009, unless otherwise indicated. All dollar amounts are expressed in Canadian dollars, unless otherwise indicated.

## SUBSIDIARIES

On May 1, 2006, Western acquired all of the issued and outstanding shares of Cascadia Forest Products Ltd. (“Cascadia”). Immediately after the acquisition, Western and Cascadia amalgamated with two of Western’s subsidiaries, WFP Western Lumber Ltd. and Mid-Island Reman Inc. The amalgamated company continued as Western Forest Products Inc. On March 1, 2007, Western amalgamated with its wholly-owned subsidiary, Western Pulp Limited. The amalgamated company continues to be called Western Forest Products Inc.

The principal subsidiaries of the Company are:

| <b>Name</b>                        | <b>Jurisdiction of Incorporation</b> | <b>Percentage owned</b> |
|------------------------------------|--------------------------------------|-------------------------|
| MacMillan Bloedel Kabushiki Kaisha | Japan                                | 100%                    |
| Western Lumber Sales Limited       | Canada                               | 100%                    |
| WFP Quatsino Navigation Limited    | Canada                               | 100%                    |

MacMillan Bloedel Kabushiki Kaisha has offices in Tokyo and Osaka and sells Western’s lumber products to Japanese wholesale and manufacturing customers. Western Lumber Sales Limited sells the Company’s lumber products to customers in the United States. WFP Quatsino Navigation Limited is the beneficial owner of a number of the Company’s non-core assets.

The Company’s other 100% owned subsidiaries are Cascadia Fibre Supply Ltd., Western Forest Products Pty. Ltd. and WFP Forest Products Ltd. The Company also has a 50% equity interest in Strathcona Helicopters Ltd. and Timber Crest Estates Limited. Strathcona Helicopters Ltd. ceased operations in May 2008 and will be wound up following the liquidation of its remaining assets and liabilities.

## DEVELOPMENT OF THE BUSINESS

### Company Profile and Strategy

Western is a major integrated softwood forest products company operating in the coastal region of British Columbia. The Company's long-term business objective is to create superior value for shareholders by building a margin-focused lumber business of sufficient size and scale to compete successfully in global softwood lumber markets. To achieve this, our strategy is to own the permits to harvest high quality Crown-owned coastal timberlands, to operate efficient, low-cost converting facilities and to produce and sell high-value softwood lumber in demand by global markets. We seek to manage our business with a focus on operating cash flow and maximizing the value of our fibre resource through the production cycle, from the planning of our logging operations to the production, marketing and sale of our lumber products.

Western's business includes the harvesting of timber, reforestation, forest management, the manufacture and sale of lumber and wood chips, and the sale of logs not consumed in the manufacturing process. Western's lumber products are currently sold in over 30 countries worldwide. The sawmills process high-quality logs, including hemlock, Douglas fir and western red cedar, into primarily long-length, wide-width and higher-grade lumber, commodity grades of lumber and residual wood chips that are sold externally and used for pulp production. The value-added lumber remanufacturing plants dry, saw and trim lumber for use in producing higher-value products such as mouldings, frames and paneling.

Our business comprises eight sawmills with in excess of 1.6 billion board feet of annual lumber capacity, four remanufacturing plants and timberland operations with approximately 7.5 million cubic metres of allowable annual cut ("AAC"), before temporary AAC reductions, from high-quality replaceable Crown-owned tenures on Vancouver Island, the British Columbia mainland coast and the Haida Gwaii / Queen Charlotte Islands. Approximately 0.3 million cubic metres of additional AAC is available from our adjacent privately owned timberlands and non-replaceable Crown tenures.

### Summary History

Following incorporation and the initial acquisition of the assets of Doman Industries Limited in 2004, the Company undertook a series of restructuring activities including the closure of its Silvertree sawmill in 2005, the exit from the pulp business in early 2006 and ceasing operations at the log merchandiser, which was used primarily to supply whole log wood chips to the Company's Squamish pulp mill. These properties, other than the site of the former pulp mill at Squamish, have since been sold.

Western subsequently expanded its forest operations through two acquisitions. On March 17, 2006, the Company purchased the Englewood Logging Division and on May 1, 2006, Western acquired all of the issued and outstanding shares of Cascadia Forest Products Ltd.

With the closing of the Cascadia and Englewood acquisitions and completion of the restructuring activities, the Company focused on the integration of its ongoing business operations. Western made organizational changes that reduced management staff by approximately 110 positions. The corporate and administration groups were consolidated at Duncan on Vancouver Island, the logging operations centralized in Campbell River, also on Vancouver Island, and the sales organizations were brought together in one office in Vancouver. Integration provided the opportunity for the consolidation of timberlands operations to increase productivity, reduce fixed costs per unit logged and optimize log flows from the timberlands to sawmills, taking advantage of shorter barging and towing distances available with the new timber tenure and mill configuration. Western closed the New Westminster sawmill in February 2007 and sold the property in March 2008.

During 2007 and 2008 the Company has continually focused on operational improvements beyond the restructuring mentioned above and accordingly, has reduced costs. The costs of harvesting have been reduced through the rationalization of logging operations. Recovery rates of lumber produced from logs have been increased with the benefit of previous capital investments and refined sawmilling techniques. In addition, systems and processes have been improved, reducing costs across the organization.

## **Significant Developments Since January 2006**

The second half of 2007 and all of 2008 have seen very difficult market conditions for our products. U.S. dimension lumber markets remain extraordinarily weak and the Japanese housing market has also slowed bringing greater competition as many wood producers look for alternate markets. As a result, during 2008, the Company operated at less than two thirds of normal operating levels due to harvesting and sawmilling curtailments. Western's weaker operating results and liquidity position during this period reflect these depressed market conditions, a stronger Canadian dollar as well as the impact of a lengthy strike during the summer of 2007.

On January 22, 2009 the Company closed a Rights Offering pursuant to a final short-form prospectus dated December 10, 2008 to all shareholders raising \$50.0 million before issue expenses. Also on January 22, 2009 the proceeds were applied to reduce the revolving credit line outstanding at that time. Tricap purchased approximately \$49.1 million of the shares offered. Western exercised its option to permit the exercise of only that portion of the rights owned by Tricap that would result in it holding not more than 49% of the Common Shares of the Company after consideration of the Rights Offering. For the number of Common Shares that would otherwise have been issued to Tricap, Western delivered Non-Voting Shares to Tricap in lieu of an equivalent number of Common Shares.

On March 20, 2008 Western closed the sale of the site of its former New Westminster sawmill, a non-core asset, for cash sale proceeds of \$39.8 million.

On March 14, 2008, the Company closed a new financing providing \$175.0 million in term facilities. The proceeds retired the Brookfield Bridge Lending Fund Inc. ("BBLF") facilities which amounted to \$72.5 (US\$73.5 million) and \$101.8 million at that time. The new financing agreement provided for two secured term facilities: a \$75.0 million revolving term facility and a \$100.0 million non-revolving term facility. The revolving term facility is due on or before March 13, 2011 and the non-revolving term debt is due on or before September 9, 2009. During 2008 the Company repaid \$46.3 million of the non-revolving portion of the debt from the proceeds of non-core asset sales.

In the second quarter of 2007, the site of the former Duke Point log merchandiser was sold for proceeds of \$8.2 million. The proceeds were applied to reduce the Company's term debt at that time. The log merchandiser ceased operating in July 2006 and had previously been used primarily to supply whole log wood chips to the Company's former Squamish pulp mill.

In February, 2007 Western permanently closed the New Westminster sawmill and re-opened the Saltair sawmill whose operations had been indefinitely suspended in October, 2005.

Early in 2007, the Company commenced an initiative to market specific non-core assets. These include the following non-core assets remaining unsold at this time: The higher and better use lands situated in the south of Vancouver Island, the gravel holdings in the Port McNeill area of Vancouver Island, the site of the former pulp mill at Squamish, and the higher and better use lands in the north of Vancouver Island. In addition, during 2008 the Company engaged professional advisors to assess the marketability of approximately 26,500 hectares of private forestry lands located in various regions throughout Vancouver Island. There can be no assurance that any sales will be completed or when any sales may ultimately occur.

On January 31, 2007 the Minister of Forests and Range agreed to the withdrawal of approximately 28,300 hectares of the Company's private land from TFLs 6, 19 and 25.

During November 2006, the Company received \$124.4 million (U.S.\$109.6 million) representing its total anti-dumping duty and countervailing duty refund and interest following the implementation of a Softwood Lumber Agreement between Canada and the United States on October 12, 2006.

On July 13, 2006, the Company's revolving credit line was amended to increase the maximum amount that can be borrowed from \$100.0 million to \$150.0 million.

On May 1, 2006, the Company acquired Cascadia Forest Products Ltd. from Trilon Bancorp Inc. a wholly-owned subsidiary of Brookfield Asset Management Inc. ("BAM"), for final cash consideration of \$202.2 million. Cascadia was a coastal British Columbia integrated lumber producer that harvested timber and produced high-value, high-quality wood products for customers worldwide. Cascadia was the largest Crown tenure holder in coastal British Columbia, with an allowable annual cut ("AAC") of approximately 3.6 million cubic metres and one of the largest

lumber producers on the British Columbia coast, owning and operating four specialized sawmills with an aggregate annual production capacity of approximately 570 million board feet of lumber, a “custom cut” operation and four remanufacturing facilities.

Also on May 1, 2006 Western raised \$295 million on the closing of an offering of rights to acquire subscription receipts exchangeable for Common Shares (the “2006 Rights Offering”). The 2006 Rights Offering proceeds were primarily used to fund the acquisition of Cascadia. The 2006 Rights Offering was qualified by Western’s short form prospectus dated January 31, 2006. Pursuant to a standby agreement with Tricap dated November 10, 2005 and the agreement governing the subscription rights, Tricap purchased approximately \$85.0 million of the subscription receipts not acquired by other rightsholders. Western exercised its option to permit the exercise of only that portion of the rights owned by Tricap that would result in it holding 49% of the Common Shares of the Company after consideration of the 2006 Rights Offering. For that number of Common Shares that would otherwise have been issued to Tricap, Western delivered Non-Voting Shares to Tricap in lieu of an equivalent number of Common Shares.

On March 17, 2006, the Company purchased the Englewood Logging Division, consisting of Tree Farm Licence 37 (“TFL 37”) on Vancouver Island and certain related assets formerly owned by Canfor, from a newly formed partnership (the “Partnership”) of Canadian Forest Products Ltd. and Oji Paper Canada Ltd. for \$45 million plus the value of certain log inventories. The Englewood Logging Division, which is located on northern Vancouver Island, comprised approximately 844,000 cubic metres of annual harvesting rights under TFL 37, 6,800 hectares of private lands in TFL 37 and existing capital improvements and infrastructure, machinery, equipment and railway rolling stock.

Also on March 17, 2006, Western executed a 40-year fibre supply agreement with the Partnership. As consideration for entering into this long-term fibre supply agreement, the Company received a chip price premium of \$80 million, of which a non-refundable \$35 million was paid to Western in cash on March 17, 2006. The balance of \$45 million of the chip price premium will be set off against the consideration due on the acquisition of the Englewood Logging Division. Western granted a security interest in TFL 37 and related assets to the Partnership that may be discharged by Western after the tenth anniversary of the agreement, except in certain circumstances. Enforcement of that security may be commenced in certain circumstances of default, including a failure to supply a minimum of 200,000 volumetric units of wood chips in any year and a minimum of 900,000 volumetric units over any three-year period, or certain other defaults specified in the Fibre Supply Agreement.

On March 10, 2006, Western redeemed in full its US\$221 million 15% secured bonds from the proceeds of senior secured credit facilities from BBLF a lender related to Tricap, the Company’s largest shareholder. The credit facilities from BBLF consisted of two term facilities, a four-year US\$187.5 million facility and a one-year \$90 million facility, which was subsequently extended for a second year. The balance outstanding was repaid from the proceeds of new term facilities on March 14, 2008.

On January 26, 2006 pulp production at the Company’s Squamish pulp mill ceased and site shut-down was substantially completed by March 9, 2006. The Company sold substantially all the pulp production equipment and has listed the Squamish site for sale as part of its asset sales initiative.

### **Changes Expected for 2009**

For additional information regarding changes expected to the Company’s business in 2009 see Western’s “2008 Management’s Discussion and Analysis”, in particular “Outlook”, which is incorporated by reference herein and which is available on SEDAR at [www.sedar.com](http://www.sedar.com) .

## **BUSINESS OF THE COMPANY**

### **Overview**

Western's business is the harvesting of timber and the manufacture and sale of lumber for worldwide markets. The sawmills process high-quality logs, including hemlock, Douglas fir and western red cedar, into primarily long-length, wide-width and higher-grade lumber, commodity grades of lumber and residual wood chips that are sold externally and used for pulp production. The value-added lumber remanufacturing plants dry, saw and trim lumber for use in producing higher-value products such as mouldings, frames, panelling and Asian squares.

We believe that the efficient utilization of our timber resources is essential. The timberlands operations seek to supply the Company's sawmills with a low-cost supply of fibre of the appropriate species and log characteristics to enable the efficient manufacture of lumber to meet customers' needs. In addition to supplying Western's sawmills with logs harvested from its timber tenures, the Company also buys, sells and trades logs on the open market to ensure sufficient fibre supply to meet the cutting profile of its sawmills.

Operating results have been and continue to be affected by a number of factors, including economic conditions in the United States, Japan and Canada, which are the leading markets for the Company's lumber products. Changes in the demand for our products in these markets and in the value of the Canadian dollar relative to the US dollar and, to a lesser degree, the Japanese Yen and the Euro can have a significant impact on our financial results. In all of these markets, our competition is of a global nature as we increasingly face competing products from various regions.

Demand for dimension lumber products is significantly impacted by the level of U.S. housing starts. The supply of dimension lumber to the United States is primarily tied to the levels of U.S. housing starts and North American lumber production, the ability or inability of certain competitors to shift production between different lumber markets and, between May 2002 and October 2006, countervailing and antidumping duties, and since October 2006 export taxes, imposed upon Canadian producers of softwood lumber exports to the United States. Another key market for structural lumber is Japan; consequently, the conditions of the Japanese economy and competition from other supply regions in the world also have a significant impact on the demand for our lumber products.

### **Forest Products Industry**

British Columbia is one of the world's leading forest products regions, with recent annual lumber shipments amounting to approximately 12 billion board feet per year and pulp and paper shipments of approximately six million tonnes per year, supported by a current annual allowable timber harvest of approximately 84 million cubic metres. Catastrophic wildfires in the southern interior of the Province in 2003 and 2004 as well as the mountain pine beetle epidemic in the central and northern interior in the past three years have led to temporary increases in the AAC in these areas in order to salvage dead and dying timber.

British Columbia has two major forest regions, coastal and interior, which are differentiated by climate, terrain and forest type and have given rise to two distinctly different segments of the forest industry. Historically, just less than one-third of British Columbia's timber harvest has originated from the coastal region. In contrast to the interior forests, the British Columbia coastal forests are distinguished by a wet maritime climate, rugged topography and a variety of high-value coastal forest species with highly productive growing sites. Over the past decade, the coastal timber harvest has declined as a result of the establishment of new parks and protected areas and AAC reductions to conform harvest levels to long-term sustainable yields.

The forest products industry categorizes lumber into either hardwoods or softwoods. Softwoods such as hemlock, spruce, pine and fir are used primarily in construction due to their strength, light weight and ease of nailing. Cedar is a softwood used where appearance and decay resistance are valued such as for decks, panelling and doors. The forest industry also grades lumber into various classifications according to quality. The two broad categories within which all grades fall, based upon the absence or presence of defects and the grain of the wood, are upper-grade lumber and commodity-grade lumber, respectively. Upper-grade lumber is substantially clear of defects and, on the British Columbia Coast, obtained largely from mature timber in areas which have not been previously harvested.

## Forest Resources

### Fibre Supply

The Company's fibre requirements are primarily met with logs harvested from Western's timber tenures and private lands, supplemented by logs purchased on the open market, and log trading activities. The Company's fibre supply department ensures an adequate supply of suitable logs for our manufacturing plants. Western engages in log trading activities to correct imbalances in the supply and demand in terms of the size, grade and species of logs.

All of Western's timber harvesting operations are located in the coastal region of British Columbia. In a normal operating year approximately 95% of the Company's logging is conducted on government timberlands allocated to us under our tree farm licences ("TFLs") and, to a lesser extent, under our forest licences ("FLs") and timber licences ("TLs"). Approximately 5% of Western's logging takes place on our private lands.

Western's timber tenures contain a substantial amount of presently harvestable mature timber stands located in areas that have never been commercially harvested. We believe that these stands are particularly valuable, as the substantial size of the trees should allow production of a high volume of upper-grade lumber. Upper-grade lumber is sold based upon appearance for use in the manufacture of doors, window frames, panelling, mouldings and siding.

The long-term species distribution of our mature timber resources is approximately 58% hemlock and balsam, 24% cedar, 11% Douglas fir, 5% cypress and 2% spruce and other minor species. Production in 2008 was approximately 56% hemlock and balsam, 27% cedar, 11% Douglas fir, 5% cypress, 1% spruce and other minor species.

The available cut, including the AAC of TFLs and FLs, actual cut, log supply and log usage for each of the last three years are set out in the following table (figures include operations acquired with the acquisition of the Englewood Logging Division on March 17, 2006 and of Cascadia commencing on May 1, 2006):

|                                    | Actual Cut <sup>(1)</sup>          |                                    |                                    | Available Cut <sup>(2)</sup><br>as at December 31 |       |       |
|------------------------------------|------------------------------------|------------------------------------|------------------------------------|---|-------|-------|
|                                    | Year Ended<br>December<br>31, 2008 | Year Ended<br>December<br>31, 2007 | Year Ended<br>December<br>31, 2006 | 2008  | 2007  | 2006  |
| <i>(thousands of cubic metres)</i> |                                    |                                    |                                    |   |       |       |
| TFLs                               | 3,719                              | 4,457                              | 5,191                              | 6,543   | 6,555 | 6,718 |
| FLs                                | 466                                | 482                                | 415                                | 578   | 578   | 656   |
| Other lands <sup>(3)</sup>         | 423                                | 360                                | 156                                | 324   | 324   | 119   |
| Total log production               | 4,608                              | 5,299                              | 5,762                              | 7,445   | 7,457 | 7,493 |
| Total logs purchased               | 673                                | 967                                | 654                                | -   | -     | -     |
| Total logs consumed                | 3,420                              | 3,452                              | 4,169                              | -   | -     | -     |
| Total logs sold                    | 2,077                              | 2,369                              | 2,084                              | -   | -     | -     |

- (1) The actual cut represents total log production with tenure assignment using the Harvest Billing System. Residue volume, which contributes to the total AAC, is not included in the amounts reported.
- (2) The available cut for the TFLs and FLs is the AAC determined by the British Columbia's Chief Forester as of December 31 and is not the average for the year. These AACs incorporate any temporary Part 13 reductions put in place by the Provincial Chief Forester.
- (3) 223,700 m<sup>3</sup> of available cut is attributed to private managed forest lands outside of TFLs and 100,000 m<sup>3</sup> to TLs outside of TFLs following FR Act reductions.

In 2008 Western had 12 forest operations managing active logging and forestry operations. These are located on Vancouver Island, the South, Central and North Coast Mainland and the Haida Gwaii / Queen Charlotte Islands. Approximately 80% of the 2008 log production originated from Vancouver Island. For historical and legal reasons, logging is conducted by a combination of Company and contractor operations. Western plans the majority and co-ordinates all of the timber production from the various operating sites.

Saw logs are sorted according to size, grade and species and directed to sawmills or, if the logs are not suitable for our manufacturing programs, sold on the open market. The pulp log volume produced from Western's timber tenures and private lands, and all residual chips produced from sawmilling operations, are fully committed under long-term fibre supply agreements. These agreements commonly require the delivery of minimum periodic chip volumes. In addition, Western has a number of long-term commitments for the sale or trade of saw logs to third parties. Most of the Company's saw log trade agreements involve the exchange of our saw logs for residual chips.

Bundle booms and self-dumping log barges are contracted to transport logs by water to manufacturing plants and to the Vancouver Log Market.

### **Timber Tenures**

Approximately 95% of all forest resources in British Columbia are owned by the Province and administered by the Ministry of Forests. Subject to provincial legislation and related regulations and Constitutional obligations to Aboriginal peoples (see "*Risk Factors – First Nations Land Claims*"), rights to harvest timber on such land may be granted on behalf of the Province by the Ministry of Forests in the form of timber tenures. Western's timber tenures comprise TFLs, FLs and TLs.

A TFL is a replaceable timber tenure that requires the licensee to manage a specified area of timberland on a sustained yield basis. TFLs are granted for 25-year terms and, subject to satisfactory performance of obligations under the TFL agreement by the licensee, are replaced by the Minister of Forests every five to 10 years with a new TFL with a 25-year term, subject to satisfactory performance by the TFL holder of its legal and licence obligations. Approximately 90% of the Company's allowable annual cut comes from six TFLs. Western expects to have TFLs 25 and 44 replaced in 2009. Replacement is subject to the Province completing consultation with various stakeholders and potentially affected First Nations (See "*First Nations Relations*").

Other parts of the Province's timberlands not designated as TFLs are organized into timber supply areas ("TSAs"). FLs are issued within each TSA with the AAC being determined at the TSA level and the overall harvest for the TSA being allocated and managed by the Ministry of Forests on a sustained-yield basis. FLs are volume-based tenures which authorize a specified volume of timber to be cut within a specific TSA. FLs generally have a term of 15 years and are replaceable every five to 10 years with a new FL with a term of 15 years, subject to satisfactory performance by the licensee of its legal and licence obligations. While we hold 11 FLs, only six had allowable annual cuts in 2008 as a result of the Forestry Revitalization Plan ("FR Plan") volume take-backs under the FR Act. The FR Plan take-backs reduced the AAC on five licences to zero by the end of 2005, but left Western with the licences and certain associated liabilities. All of Western's six active FLs were replaced in 2007 and 2008 for 15-year terms.

TLs are area-based tenures with various fixed terms. TLs within a TFL are managed on an integrated basis with other timberlands within the same TFL and the land remains part of the TFL when the TL expires. Harvesting from TLs external to TFLs is subject to the practice guidelines of the Ministry of Forests, but timing is at our discretion within the term.

In November 2004 Western applied to the Minister of Forests to have approximately 28,300 hectares of the Company's private land withdrawn from TFLs 6, 19 and 25 and on January 31, 2007 these private lands were withdrawn. The AACs of the three TFLs were reduced by 202,100 cubic metres as of the withdrawal date to reflect the contribution that these private lands had made to the timber inventory and long term sustainable productivity of these TFLs. The majority of these private lands will continue to be regulated under the *Private Managed Forest Land Act* (British Columbia) and regulation as well as other provincial and federal statutes. Consistent with our focus on harvesting Crown-owned coastal timberlands, Western continues to review opportunities to realize greater value from these lands. Included in the private timberlands in various locations on Vancouver Island is approximately 4,000 hectares of higher and better use lands currently intended for sale. The Company will also continue to review the private land best suited for ongoing timberlands operations to determine their highest-value contribution.

### **Timber Available For Harvest**

The AACs for TFLs and TSAs are determined by the Chief Forester of the Province and are intended to reflect timber conditions, regional and local economic and social interests, and environmental considerations. Legislation requires the Chief Forester for British Columbia to review sustainable timber harvesting levels in

each TSA and TFL in the Province every five years and to issue a “determination” relating to the same, which may recommend reductions or increases in the AAC of the TSA or TFL.

Under Part 13 of the *Forest Act* (British Columbia) (the “Forest Act”), if the Minister of Forests determines that it is in the public interest, the Province can “designate” areas of Crown land for up to 10 years and then suspend or vary permits, licences and plans in force within the area. At the same time, the Provincial Chief Forester can reduce the AAC of a timber tenure by an amount attributable to the designated Part 13 area. Part 13 is generally applied in support of land use planning or environmental reserves.

On December 12, 2007, the Province of British Columbia and the Council of the Haida Nation entered into a Strategic Land Use Agreement (“SLUA”) regarding land use objectives and new Part 13 protected areas on the Queen Charlotte Islands. Western currently has an annual cut on the Queen Charlotte Islands of approximately 509,000 cubic metres, not including the area temporarily protected under Part 13. At the present time, the impact of the SLUA on Western's operations is unknown because a number of issues remain to be determined though a further process of detailed strategic planning which is expected to take up to two years to complete. However, Western believes that a substantial portion of its current cut level on the Queen Charlotte Islands could be adversely affected. Preliminary conversations have begun with the Provincial Government with respect to the form and process through which compensation should be provided for reduction in the harvest level, but there can be no assurance that adequate compensation will be received.

### **Stumpage Charges**

Stumpage is the fee that the Province charges forest companies to harvest timber from Crown land in British Columbia. Since February 29, 2004, stumpage for the coastal region has been set using the Coast Market Pricing System (“CMPS”), which uses the results from British Columbia Timber Sales auctions to predict the value of Crown timber harvested under long-term tenures. Effective January 15, 2009, the British Columbia Ministry of Forests and Range updated the Market Pricing System (MPS) which sets stumpage rates for Crown timber harvested on the province’s coast. The new MPS equation has been updated to more accurately reflect the current auction market for Crown timber as well as licensee obligations, such as reforestation costs, under their Crown forest tenures.

The following table illustrates the relationship of stumpage expenses relative to the total log production for each of the last three years (2006 figures include operations acquired on the acquisition of Englewood and Cascadia commencing March 17, 2006 and May 1, 2006 respectively):

|  | Year Ended December 31, |        |        |
|--|-------------------------|--------|--------|
|  | 2008                    | 2007   | 2006   |
| Log production ( <i>thousand's of cubic metres</i> ) | 4,608                   | 5,299  | 5,762  |
| Stumpage ( <i>\$ millions</i> )                      | \$85.9                  | \$85.4 | \$49.1 |

### **Forest Management**

Western manages forest tenures and privately-owned forest lands according to sustainable forest management principles, which include a commitment to meeting government standards. As part of the rights and responsibilities that accompany Western's Crown tenures, staff carry out or supervise pre-harvest planning, road-building and harvesting operations and follow-up silviculture treatments to establish free-growing second-growth stands of trees.

Pre-harvest planning includes a wide spectrum of activities from the collection of inventory and assessment data to the development of higher-level Management Plans for TFLs and Forest Stewardship Plans for specific planning areas within TFLs or FLs. These plans take a broad range of timber and non-timber factors into account, including but not limited to: wildlife, fisheries, water quality, soil sensitivity, terrain stability, visual quality, biodiversity, archaeological sites and cultural features, cave and karst features, timber species distribution and value. These higher-level plans provide direction for the development of site-specific plans and lead to the applications for specific road-building and harvesting permits.

Following harvest, we ensure all disturbed areas are reforested and conduct follow-up surveys and silvicultural treatments to ensure that these harvested areas meet free-growing requirements within specified timelines. Should a developing stand be damaged prior to being declared free growing we are responsible for taking the

necessary corrective actions to meet free growing requirements. Substantially all of these basic silviculture requirements are carried out at our expense. Once free-growing, young stands are left to develop without further attention into second-growth forests ready for subsequent harvest.

Our tenures are managed by a staff of registered professional foresters and engineers who are involved in planning and inventory, road and bridge development, harvesting, silviculture and forest health and protection programs. We operate the Saanich Forestry Centre, which includes a three million-seedling nursery and a tree seed orchard that produces select seed for reforestation.

The forests on our timber tenures are at risk of damage from natural and human caused forest fires. To deal with this hazard we have equipment and trained personnel ready to handle initial attack and fire suppression. We are also required to pay a fire preparedness levy to the Ministry of Forests each year. Should a fire start as a result of our activities, and we did not willfully cause or contribute to the fire by our act or omission, payment of this fee means that we will not be charged for any Ministry initial attack costs or the fire suppression costs associated with the wildfire once the Ministry has assumed fire control. Further, Western will not be charged for damages to Crown resources if the Company has been duly diligent. We remain responsible for fire-fighting on our private lands, whether inside or outside of TFLs, regardless of origin or cause. Western has entered into a cost-sharing agreement with the Crown for our private lands which will reduce individual incident costs of mobilizing helicopters and aerial water tankers.

### **Manufacturing Facilities**

We own eight operating sawmills and four operating value-added remanufacturing facilities. Our high-quality timber supply (western red cedar, hemlock, balsam, Douglas fir, yellow cedar and spruce) and the particular design of our sawmills enable us to produce specialty products such as upper-grade lumber, lumber with long lengths (over 20 feet) and wide widths (over 10 inches), western red cedar lumber, baby squares and beams used in traditional Japanese housing. These products typically command premium prices compared to commodity construction grades, such as SPF 2x4 lumber. Much of the softwood timber in North America is not capable of producing substantial quantities of these specialty products.

All of our operating sawmills are located on Vancouver Island on land we own other than the Nanaimo sawmill, which is located on a 7.0-hectare site that includes 1.3 hectares owned by the Company and 5.7 hectares that are leased. All of Western's sawmills have adjacent water lots which are leased from the Province of British Columbia or a public Port Authority and some have barge and dock loading facilities to handle water-borne shipments of sawmill products. Our sawmill configuration provides significant flexibility, enabling us to change cut programs and log flows between different sawmills.

- The Nanaimo sawmill, which is capable of processing logs in the 12- to 60-inch diameter range, produces a range of high-value specialty lumber products, along with material for the traditional Japanese market. The mill primarily cuts hemlock.
- The Duke Point mill, also in the Nanaimo municipality, is capable of processing 12- to 60-inch diameter logs, and is highly grade and species flexible, cutting high value cedar through to hemlock dimension as markets and log supply requires.
- The Ladysmith and Saltair sawmills are located adjacent to each other in Ladysmith. The Ladysmith sawmill is capable of processing logs in the 4- to 25-inch diameter range. It primarily cuts hemlock for the U.S. structural dimension market. The Saltair sawmill, which re-opened on February 12, 2007, is capable of processing logs in the 6- to 30-inch diameter range. The mill primarily cuts cedar for the Canadian and U.S. markets and fir and hemlock for the Japanese and European markets.
- The Alberni Pacific sawmill, which is located in Port Alberni, is capable of processing logs in the 12- to 60-inch diameter range and currently produces a range of high-value specialty lumber products, along with material for the traditional Japanese market. The mill primarily cuts hemlock.
- The Somass sawmill, located in Port Alberni, is capable of processing logs in the 15- to 108-inch diameter range and cuts high-value cedar for worldwide markets.
- The Chemainus sawmill is capable of processing logs in the 10- to 60-inch range. The mill cuts high-value fir for the Japanese market, and cedar for the North American market.

- The Cowichan Bay sawmill, which is located close to Duncan and processes logs in the 5- to 30-inch range. The sawmill primarily cuts hemlock for the U.S. structural dimension market.

The Saltair, Nanaimo and Alberni Pacific sawmills have received authorization to stamp their lumber as having met the quality control requirements of the Japanese Agricultural Standard (“JAS”), indicating that the lumber meets rigorous Japanese structural grading rules.

Our remanufacturing facilities are also located on Vancouver Island on land we own. Our Chemainus value-added plant primarily dries and processes hemlock lumber into stock for doors, windows and moldings. Our Somass remanufacturing plant in Port Alberni processes cedar lumber into bevel-siding, board and panels for world markets. Our Mid Island and South Island remanufacturing plants primarily dry, trim and sort lumber for worldwide markets. We have a total of 50 kilns located at our remanufacturing plants and sawmills with an annual capacity of about 250 million board feet per year. As part of our sales and marketing strategy, we are reviewing the requirement to invest in future new kiln capacity.

In addition to lumber manufacturing at its own facilities, Western also operates a division known as “Custom Cut”. The Custom Cut operation focuses on converting logs to lumber on a custom basis to customer specifications. Unlike traditional lumber purchases, in which a customer will specify the volume of selected lumber products they wish to purchase, Custom Cut customers typically acquire all the lumber products which are cut from a defined volume of logs. Custom Cuts may be conducted at third-party manufacturing facilities in the Vancouver Lower Mainland using logs either harvested by Western or acquired on the open market. Alternatively, Custom Cuts may be conducted at Western’s facilities in situations where the customer specifications are compatible with mill capacities. Custom Cuts are routinely performed on Western’s major species and are the primary method of taking higher-value Yellow Cedar and Sitka Spruce lumber to market.

The current annual lumber production capacity and actual lumber production for each of our sawmills for each of the last three years are set out in the following table:

| Sawmills                           | Capacity <sup>(1)</sup><br>(MMfbm) | Year Ended December 31, |      |       |
|------------------------------------|------------------------------------|-------------------------|------|-------|
|                                    |                                    | 2008                    | 2007 | 2006  |
| Alberni Pacific <sup>(2)</sup>     | 225                                | 114                     | 94   | 100   |
| Chemainus <sup>(2)</sup>           | 130                                | 107                     | 85   | 78    |
| Cowichan Bay                       | 315                                | 139                     | 96   | 156   |
| Duke Point                         | 225                                | 51                      | 82   | 149   |
| Ladysmith <sup>(5)</sup>           | 170                                | 12                      | 109  | 142   |
| Nanaimo                            | 213                                | 72                      | 83   | 137   |
| New Westminster <sup>(2) (3)</sup> | n/a                                | 0                       | 7    | 99    |
| Saltair <sup>(4)</sup>             | 215                                | 98                      | 59   | 0     |
| Somass <sup>(2)</sup>              | 110                                | 62                      | 70   | 59    |
|                                    | 1,603                              | 655                     | 685  | 920   |
| Custom Cut                         | n/a                                | 113                     | 120  | 80    |
| Total <sup>(6)</sup>               | 1,603                              | 768                     | 805  | 1,000 |

(1) Based on three shifts and 250 operating days.

(2) Acquired in 2006 with the acquisition of Cascadia. Production is from May 1, 2006 to December 31, 2006.

(3) Operations at New Westminster were closed on February 7, 2007.

(4) Sawmilling operations at Saltair were indefinitely suspended on October 28, 2005 and resumed on February 12, 2007.

(5) Operations at Ladysmith were indefinitely suspended in May, 2008.

(6) The production in 2007 includes the impact of a three-month strike.

Our sawmills have a total annual production capacity of approximately one million volumetric units of wood chips. Residual chips from our manufacturing operations are being sold under long-term fibre supply agreements. We also trade log volumes with third parties to secure preferred fibre or for cost benefit. Wood residue produced by the sawmills, principally sawdust and bark, is either used as a fibre supply for pulp operations (some of the sawdust) or as hog fuel, which is sold to pulp mills.

The wood chip supply and usage for each of the last three years from our operations are set out in the following table (2006 figures include operations acquired on the acquisition of Cascadia commencing May 1, 2006):

|   | Year Ended December 31,   |      |      |
|---|---|------|------|
|   | 2008  | 2007 | 2006 |
| <i>(thousands of volumetric units)</i>      |   |      |      |
| Wood chips produced <sup>(1)(2)</sup> ..... | 513   | 455  | 607  |
| Wood chips purchased.....                   | 319   | 285  | 263  |
| Total wood chips consumed.....              | -   | -    | 41   |
| Total wood chips sold.....                  | 770   | 740  | 855  |
| (1)   | Production in 2007 includes the impact of a three-month strike.   |      |      |
| (2)   | Production in 2008 includes chips produced from whole-log chipping.   |      |      |
| (3)   | Wood chips purchased and sold in 2007 and 2006 restated to exclude chips sold with certain repurchase arrangements. |      |      |

### Sales, Marketing and Distribution

Western's lumber products are marketed by our sales and marketing division, which is based in Vancouver and has offices on Vancouver Island and in Japan, China and Australia. Lumber sales into the United States are primarily made directly to wholesale lumber distributors or major manufacturers. Our sales into the Japanese market are serviced both from our Vancouver sales office, where we sell directly to Japanese trading houses, and also through our Japanese sales offices, which sell to wholesale and manufacturing customers. Our European lumber sales are made through sales agencies.

In addition, the sales and marketing division liaises directly with the consumers of our lumber products. This allows us to react quickly to changes in market conditions and customer requirements and to achieve lower selling costs. Western adjusts sawmill processing programs in order to customize products to meet the specific requirements of our customers or changes in market conditions.

An increasing volume of our lumber products are sold kiln-dried, although a significant portion of our structural products are still sold green (neither kiln-dried nor air-dried). Sales to the U.S. market consist of a wide range of products from structural dimension lumber to high-grade western red cedar and hemlock that is used for more consumer-oriented products. We offer a comprehensive line of traditional components for the Japanese market and provide hemlock products with high structural values for this market which have been approved by Japanese government agencies. Our focus in Europe is kiln-dried, high-grade specialty products used predominantly in Germany, Italy and the United Kingdom. Western's business to China is focused on customers who produce components and finished wood products for re-export to Japan, Europe and the United States, as well as for a growing domestic market.

The distribution of the Company's sales by geographic area and by product line for each of the last three years is set out in the following table:

|   | Year Ended December 31, |                |                |
|---|-------------------------|----------------|----------------|
|   | 2008                    | 2007           | 2006           |
| <i>(millions of dollars)</i>                    |                         |                |                |
| <i>Sales by geographic area</i>                 |                         |                |                |
| Canada .....                                    | \$322.8                 | \$392.7        | \$345.4        |
| U.S. ....                                       | 178.3                   | 219.2          | 265.4          |
| Asia.....                                       | 220.2                   | 199.5          | 203.3          |
| Europe .....                                    | 65.8                    | 56.7           | 56.4           |
| Other.....                                      | 27.7                    | 22.4           | 26.4           |
|   | <u>\$814.8</u>          | <u>\$890.5</u> | <u>\$896.9</u> |
| <i>Sales by product line</i>                    |                         |                |                |
| Lumber .....                                    | \$623.9                 | \$650.1        | \$677.1        |
| Logs.....                                       | 133.6                   | 184.6          | 162.1          |
| Sawmill by-products .....                       | 57.3                    | 55.8           | 57.7           |
|   | <u>\$814.8</u>          | <u>\$890.5</u> | <u>\$896.9</u> |
| <i>Sales by product line by geographic area</i> |                         |                |                |
| <i>Lumber</i>                                   |                         |                |                |
| Canada .....                                    | \$134.3                 | \$152.3        | \$125.6        |
| U.S. ....                                       | 177.0                   | 219.2          | 265.4          |
| Asia .....                                      | 220.2                   | 199.5          | 203.3          |
| Europe.....                                     | 65.8                    | 56.7           | 56.4           |
| Other .....                                     | 26.6                    | 22.4           | 26.4           |
|   | <u>623.9</u>            | <u>650.1</u>   | <u>677.1</u>   |
| <i>Logs</i>                                     |                         |                |                |
| Canada.....                                     | 131.2                   | 184.6          | 162.1          |
| U.S. ....                                       | 1.3                     | -              | -              |
| Other .....                                     | 1.1                     | -              | -              |
|   | <u>133.6</u>            | <u>184.6</u>   | <u>162.1</u>   |
| <i>Sawmill by-products</i>                      |                         |                |                |
| Canada .....                                    | 57.3                    | 55.8           | 57.7           |
|   | <u>57.3</u>             | <u>55.8</u>    | <u>57.7</u>    |
| Total Sales.....                                | <u>\$814.8</u>          | <u>\$890.5</u> | <u>\$896.9</u> |

Lumber is delivered to customers by various means, including at times ocean-going vessel, barge, rail or truck. Western's location on the coast of British Columbia helps us compete in terms of ease of access to overseas markets.

In a normal operating year, there is some seasonality to our operations, with higher lumber sales activity in the second and third quarters as construction activity, particularly in the United States, has historically tended to be higher. Other export markets for the solid wood segment do not have such a pronounced seasonal pattern. Weather conditions such as storms, snow and ice in the winter and the threat of forest fires in the summer may cause logging activity, and consequently sales levels, to vary.

### Competition

To a great extent, lumber is a commodity and the market is cyclical. We compete on both a domestic and international level with a large number of forest products firms, ranging from very large integrated firms to smaller specialty companies. Western also competes indirectly with firms that manufacture substitutes for solid wood products, including non-wood and engineered wood products. The market for lumber is highly competitive and sensitive to cyclical changes in industry capacity and the economy, both domestically and internationally. Changes in the level of competition, industry capacity, foreign exchange rates and the global economy have a significant impact on our selling prices and overall profitability.

Our competitive position is influenced by the availability, quality and cost of fibre, energy and labour, and our plant efficiencies and productivity in relation to our competitors. Western is the largest timber tenure holder and

producer of lumber from the British Columbia Coastal Region. The diversity of species and high quality of wood enables the Company to produce products for a wide variety of final use, from dimension lumber for home construction to clear upper end lumber used for millwork such as door and window frames, along with timbers for various applications. Western is also the world's largest producer of Western Red Cedar. To a certain extent, the Company can use the flexibility of the variety of species and products to shift markets according to global wood market conditions, limiting or growing exposure to various markets and products within the constraints of the long-term balance of the various species in our timber supply.

### **Softwood Lumber Agreement**

Effective October 12, 2006 the Canadian and United States Governments implemented a softwood lumber agreement ("SLA") that replaced the United States imposed anti-dumping duty ("ADD") and countervailing duty ("CVD") regime with an export tax, payable to the Canadian Government. The SLA has a term of seven years and provides for an extension of two years and for early termination by either Government after two years. British Columbia's coastal region, the area in which the Company operates, elected to be subject to the new export tax only and not the quota alternative. The export tax rate varies according to the price of lumber based on the "Random Lengths Framing Lumber Composite Index" ("Index") and ranges from zero percent, when the Index is above US\$355 per thousand board feet, to 15%, when the Index is under US\$315 per thousand board feet. The export tax only applies to the first US\$500 per thousand board feet for any product sales. In addition, if the monthly volume of exports from the British Columbia coastal region exceeds a certain "Trigger Volume" as defined in the SLA, a "surge" mechanism will apply to retroactively increase the rate of the export tax for that month by 50% (for example, the 15% export tax rate would become 22.5% for that month). The export tax expensed by the Company was \$8.9 million for 2008 compared to \$15.7 million in 2007.

### **Environment, Health & Safety**

#### **Safety**

During the last three years the Company has embarked on a program to significantly reduce injuries and control losses relating to equipment, process and the environment. From 2005 our Medical Incident Rate ("MIR") has dropped approximately 58% to 2.49 per 100 employees per year at the end of 2008. Further, Western's Lost Time Incident Rate for 2008 was 1.8 for logging operations and 1.5 for sawmilling operations compared to the BC industry average of 5.8 and 3.1, respectively. Western has developed and adopted a corporate safety policy which reflects Western's values and expectations to ensure we meet all of our regulatory requirements under WorkSafeBC.

The Company performs or develops training, safety plans, follow-up on incidents, clear expectations for all employees, audits/inspections and contractor controls all of which are a key to our success. Western's Environment, Health and Safety representatives are also active in working with unions, WorkSafeBC and the BC Forest Safety Council to help shape programs, activities and regulations to ensure a safer workplace for all.

Other than Western's own employees in timberlands, approximately 200 contractor companies are utilized in timberlands operations to achieve the Company's overall AAC targets. Western expects these contractors to work to the same standards as Western's own operations. To this end, various programs have been developed to help support the contractors in their efforts to improve safety and performance; program development, training, inspection and access to Company safety materials and expertise. Western had also requested that all contractors obtain the BC Forest Safety Council's "Safe Company" certification by the end of 2008. This target was achieved. All of Western's own Company timberlands operations have also obtained such "Safe Company" certification.

#### **Environmental Policy**

We are committed to the protection of the environment and work with government, local communities, First Nations, environmental groups and other interested stakeholders to identify and address issues of environmental concern in all aspects of our business. Our operations are subject to a wide array of federal, provincial and local environmental legislation regulating water, land and air discharges and solid and hazardous waste management, disposal, transportation and remediation. To oversee and co-ordinate company-wide efforts for compliance with such legislation, we have established an Environmental, Health and Safety Committee of the Board of Directors and implemented a reporting system that is designed to monitor environmental compliance with regulatory requirements, identify environmental issues and communicate them to all levels of

management and operations. In conducting our operations, we attempt to minimize environmental impact through sound forestry and environmental management practices that meet or exceed government standards and adhere to an environmental policy based on the following:

- assessing and evaluating environmental risk on an ongoing basis in order to maintain meaningful environmental objectives and targets and effective operational controls;
- allocating sufficient resources to ensure continuing compliance with environmental responsibilities;
- meeting or surpassing all applicable legal requirements;
- establishing auditing and reporting procedures to monitor environmental performance, continually improve environmental practices and prevent pollution; and
- communicating this policy and our environmental performance to the public as well as our staff, employees and contractors.

### ***Environmental Management***

During 2008, Western's operations were in substantial compliance with environmental requirements, except for incidents which have not had, or are not expected to have, a material impact on the Company or its operations. We have a number of Environmental Management Systems for our timberlands and sawmills as follows:

*ISO 14001:* All of our timberlands and four of our manufacturing operations are registered to the International Organization for Standardization ("ISO") 14001 Environmental Management Systems standard. Through third party audits by the Quality Management Institute, as well as internal audits we confirm that we remain in conformance with the ISO 14001 standard. These audits provide important feedback to senior management to ensure that staff, employees and contractors conduct their activities in compliance with the legislation and regulations relevant to the forest products industry. Environmental Management Programs are another tool used to achieve adherence to our environmental policies.

*CSA Z809:* Seven of our timberlands operations are also certified to the Canadian Standards Association ("CSA") Z809 Sustainable Forest Management standard. These Operations have certified Program for the Endorsement of Forest Certification Chain of Custody systems in place to ensure that certified material can flow to our mills to produce certified product. An eighth Timberlands Operation was audited to the British Columbia Forest Stewardship Council Regional Standard and we expect registration in 2009.

Positioning our operations to address customer needs will drive future certification initiatives.

See "*Risk Factors – Environmental Regulation*" for additional information.

### **First Nations Relations**

Western is aware of over 50 First Nations or First Nation associations that claim to have interests in areas within our timber tenures. We have developed and continue to develop working relationships with many First Nations through timber harvesting, silviculture, planning and other capacity-building arrangements.

First Nations groups have made claims of rights and title to substantial portions of land in British Columbia, including areas where our timber tenures and operations are situated, creating uncertainty as to the status of competing property rights. Current Provincial Government policy requires that forest management and operating plans take into account and not unjustifiably infringe on aboriginal rights and title, proven or unproven, and provide for consultation with First Nations. This policy is reflected in the terms of our timber tenures, which provide that the Ministry of Forests may refuse to issue cutting permits in respect of a timber tenure if it is determined that the forestry operation would unjustifiably interfere with aboriginal rights and title. First Nations have, at times, sought to restrict the Provincial Government from granting or renewing forest tenures and other operating authorizations without full consultation or their consent if these decisions could affect lands claimed by them.

In addition, the Provincial Government is also negotiating Forest and Range Agreements with certain First Nations. These agreements are intended to provide partial interim accommodation of the economic component of aboriginal interests that may be impacted by certain forestry decisions until such time as those interests are

settled through the treaty process. To date, the Provincial Government has entered into agreements with over 100 First Nations throughout the Province, including First Nations whose traditional territories overlap some of our operating areas.

On December 12, 2007, the Province of BC and the Council of the Haida Nation entered into a Strategic Land Use Agreement (SLUA) regarding land use objectives and new Part 13 protected areas on the Queen Charlotte Islands that may impact Western's operations (see "*Forest Resources – Timber Available for Harvest*").

### Capital Expenditures

The following table summarizes capital expenditures for each of the last three years (2006 figures include expenditures incurred with respect to the Englewood Logging Division from March 17, 2006 and Cascadia from May 1, 2006):

|                              | Year Ended December 31 |                       |        |
|------------------------------|------------------------|-----------------------|--------|
|                              | 2008                   | 2007                  | 2006   |
| <i>(millions of dollars)</i> |                        |                       |        |
| Capital expenditures         | \$12.5 <sup>(1)</sup>  | \$26.5 <sup>(2)</sup> | \$37.5 |

(1) Capital expenditures in 2008 reflects Company actions to reduce capital programs in response to the economic downturn.

(2) Capital expenditures on roads in 2007 were impacted by a three-month strike, which lowered harvesting activities.

### Human Resources

As of December 31, 2008, Western employed 2,613 employees (of which 2,021 are hourly paid workers). The majority of hourly paid workers are represented by the United Steelworkers of America ("USW") Union under a three-year agreement, expiring June 14, 2010. The Pulp, Paper and Woodworkers of Canada ("PPWC") represents the remainder of the hourly workers and their collective agreement expires on June 14 2009. Western was a member of Forest Industrial Relations Limited ("FIR"), which represents certain forest products companies in the coastal region of the Province in their negotiations with the USW and certain other agreements. In the first quarter of 2008, Western formally withdrew as a member of FIR.

Typically, in our logging operations approximately 60% of the harvesting is performed by contractors. The majority of the contractors have replaceable contracts under the Timber Harvesting Contract and Subcontract Regulation (British Columbia). The substantial majority of the approximately 1,000 employees who work for the contractors harvesting our tenures are also represented by the USW.

### Research and Development

Silviculture and tree improvement research is conducted primarily by our employees at our Saanich Forestry Centre on Vancouver Island and from the Company's timberlands office in Campbell River. The Centre has seed orchards, a seedling nursery that supplies our requirements for most species of seedlings and a laboratory that provides technical support to maintain seed and seedling quality. The centre provides us with the ability to select and breed trees with superior growth and form that should improve the quality and quantity of timber produced over time.

The Company's logging and sawmilling operations also investigate new equipment and methods to improve operational efficiencies. We are a member of the Forest Engineering Research Institute of Canada ("FERIC"), now a division of FPInnovations, which conducts research into activities related to the harvesting and transportation of wood and the growing of trees. We are also members of Forintek, now also a division of FPInnovations, which conducts research into lumber manufacturing activities including lumber drying technology and a variety of lumber recovery improvement technologies, and provides support for marketing for new products such as treated lumber.

## **RISK FACTORS**

The following risks and uncertainties may have a material adverse effect on our operations:

### **Variable Operating Performance, Product Pricing and Demand Levels**

A key factor affecting Western's operating and financial performance is the price received for lumber, logs and other products. Prices for these products are highly cyclical and have fluctuated significantly in the past and may fluctuate significantly in the future. The markets for our products are also highly cyclical and are characterized by periods of excess product supply due to many factors, including:

- additions to industry capacity and production;
- periods of insufficient demand due to weak general economic activity or other causes including weather factors;
- customers experiencing reduced access to credit; and
- inventory de-stocking by customers.

Product demand is influenced to a significant degree by economic activity at the global level. Additionally, although costs may increase, customers may not accept related price increases for those products. We are not able to predict with certainty market conditions and prices for these products. Western's results of operations depend upon the prices we receive for lumber, logs and chips, and a deterioration in prices of, or demand for, these products could have a material adverse effect on our financial condition or results of operations. We cannot provide any assurance or prediction as to the timing and extent of any price changes. On an annualized basis and based on current operating metrics, we estimate that operating earnings would increase or decrease by approximately \$7 million for each incremental price increase or decrease, respectively, of \$10 per thousand board feet of lumber. Each incremental price swing greater than \$10 per thousand board feet of lumber is expected to have an impact on operating earnings of slightly less than \$7 million per increment due to the likely related change in stumpage fees.

Western's financial performance is also dependent on the rate at which production capacity is utilized. In times of challenging conditions in any of our major markets the Company maintains inventory control by aligning log supply and lumber production with anticipated sales volumes. When capacity utilization is reduced in response to weak demand for products, the cost per unit of production may increase and profitability decrease.

From time to time and in accordance with market influences, the Company will reduce production with temporary logging and/or sawmilling curtailments. In extreme cases, such curtailments may become permanent closures. When Western undertakes significant market related curtailments of sawmills, the volume of chips produced is reduced and accordingly there is greater risk that the Company may not meet minimum contractual obligations under chip supply agreements without incurring additional cost. The Company did not deliver the minimum volume of chips required under one of its chip supply agreements for the three year period ending December 31, 2008. The Company is in discussions with the customer on potential remedies or damages due, if any. The customer has ninety days from January 30, 2009 to accomplish one available remedy which is to act on its security over the Company's Englewood Logging Division, comprising a tree farm license with an allowable annual cut of 826,000 cubic metres, 6,800 hectares of private timberlands and other capital improvements and equipment. At this time the Company is unable to quantify the extent of additional cost, if any, or whether the customer will act on its security.

### **International Business and Risks of Exchange Rate Fluctuations**

Western's products are sold in international markets. Economic conditions in those markets, especially the United States, Japan and China, the strength of the housing markets in the United States and Japan, fluctuations in foreign exchange rates and international sensitivity to interest rates, can all have a significant effect on our financial condition and results of operations. In general, our sales are subject to the risks of international business, including:

- fluctuations in foreign currencies;

- changes in the economic strength of the countries in which we conduct business;
- trade disputes;
- changes in regulatory requirements;
- tariffs and other barriers;
- quotas, duties, taxes and other charges or restrictions upon exportation;
- transportation costs and the availability of carriers of any kind including those by land or sea; and
- strikes or labour disputes in the transportation industry or related dock or container service industries.

Depending on product mix, destination and exchange rates, between 40% and 50% of our total product sales are denominated in US dollars and between 10% and 13% in Japanese Yen, while most operating costs and expenses are incurred in Canadian dollars, with small portions in US dollars and Japanese Yen. The Company's functional currency is the Canadian dollar and results of operations are reported in Canadian dollars. Significant variations in relative currency values, particularly significant changes in the value of the Canadian dollar relative to the US dollar, have had, and in the future could have, a material impact on our operating earnings and cash flows. We estimate that an increase or decrease of 1% in the value of the Canadian dollar compared to the US dollar and Japanese Yen would decrease or increase, respectively, operating earnings by approximately \$4.0 million to \$5.0 million dollars annually.

The Softwood Lumber Agreement with the United States was implemented on October 12, 2006. The agreement has a term of seven years, extendable for up to two years, and may be terminated after 18 months by either the Canadian or United States government with not less than six months' notice. We are unable to predict whether the agreement will be terminated prior to expiration or the consequences upon termination, should it occur. In addition, the agreement provides that if the monthly volume of exports from the British Columbia coastal region exceeds a certain "Trigger Volume" as defined in the agreement, a "surge" mechanism will apply to increase the rate of the export tax for that month by 50% (for example, a 15% export tax rate would become 22.5% for that month). The surge mechanism can be triggered by any or all companies in the region over-shipping, causing total exports to exceed the trigger volume. We are unable to predict if or when the surge mechanism will apply to any of our future lumber shipments into the United States.

### **Employees and Labour Relations**

The majority of the hourly paid employees at our manufacturing facilities and timber harvesting operations are unionized. Our current collective agreements expire at various dates from June 2009 through to May 2012. The union contract representing the majority of our employees, the Coast Master Agreement with the USW, expires on June 14, 2010. Should the Company be unable to negotiate an acceptable contract at the time the existing collective agreements expire with any of the unions, a strike or work stoppage could occur. Furthermore, a negotiated settlement could result in unplanned increases in wages or benefits payable to union members. Therefore, a strike or other work stoppage could involve significant disruption of operations and/or a material adverse impact on our financial condition or results of operations.

In addition, the Company relies on certain third parties, such as logging contractors, stevedores or major railways, whose workforces are unionized, to provide us with services needed to operate our business. If those workers engage in strike or other work stoppages, our operations could be disrupted.

### **Long-Term Competition**

The markets for our products are highly competitive on a domestic and international level, with a large number of major companies competing in each market. Many of our competitors have both substantially greater financial resources and less debt than Western. Some of these competitors are not subject to fluctuations in the relative value of the Canadian dollar to the same extent as Western. We also compete indirectly with firms that manufacture substitutes for solid wood products, including non-wood and engineered wood products. While the principal basis for competition is price, we also compete to a lesser extent on the basis of quality and customer service. Changes in the level of competition, industry capacity and the global economy have had, and are expected to continue to have, a significant impact on the selling prices and overall profitability of the Company.

Our competitive position will be influenced by factors including the availability, quality and cost of fibre, energy and labour, and plant efficiencies and productivity in relation to our competitors. Our competitive position could be affected by fluctuations in the value of the Canadian dollar relative to the US dollar and/or the Japanese Yen, and by the export tax on softwood lumber shipments to the United States.

### **Forest Resource Risk and Natural Catastrophes**

Our timber tenures are subject to the risks associated with standing forests, in particular, forest fires, wind storms, insect infestations and disease. Procedures and controls are in place to manage such risk through prevention and early detection. Most of the timber that we harvest comes from Crown tenures and insurance coverage is maintained only for loss of logs due to fire and other occurrences following harvesting. However, this coverage does not extend to standing timber, and there is no assurance that this coverage would be adequate to provide protection against all eventualities, including natural catastrophes. Western has entered into a cost-sharing agreement with the Crown for our private timberlands to reduce individual incident costs of mobilizing helicopters and aerial water tankers in the event of a fire on those lands.

In addition, our operations may be adversely affected by severe weather including wind, snow and rain that may result in our operations being unable to harvest or transport logs to our manufacturing facilities for extended periods of time. Although we anticipate and factor in a certain period of down-time due to weather, extended periods of severe or unusual weather may adversely impact our financial results due to higher costs and missed sales opportunities arising from fibre shortages or the deterioration of logs remaining on the ground or in the water for extended periods of time.

The majority of our business operations are located on the British Columbia coast, which is geologically active and considered to be at risk from earthquakes.

Climate change over time is predicted to lead to changes in the frequency of storm events as well as their severity. We also expect to see changes in the occurrence of wildfires and forest pest outbreaks. Long-term climatic models are predicting that the optimum ranges of many species, including those of our major tree species, will shift over time. We are unable to predict the impact of all of these factors on our tenures or on forest practices.

While the Company maintains insurance coverage to the extent deemed prudent, we cannot predict that all potential insurable risks have been foreseen or that adequate coverage is maintained against known risks.

### **Impact of Mountain Pine Beetle Infestation**

The west-central interior of British Columbia has been, and continues to be, seriously damaged by North America's largest recorded mountain pine beetle infestation. Western does not operate in the affected area and the lodgepole pine, the species most at risk from the infestation, is not a key source of timber in the coastal forests. This natural disaster is causing widespread mortality of lodgepole pine. Increases in harvest levels have resulted in higher lumber production volumes and therefore more supply in the marketplace, potentially decreasing prices, primarily in the structural dimension market in the United States. There is growing evidence that, as the dead trees decay, they become more difficult and costly to manufacture into lumber and that the quality of the residual wood chips may diminish. The mountain pine beetle has crossed into Alberta, and timber harvesting of lodgepole and jackpine in Alberta will likely see an increase in allowable annual cut ("AAC") to promote salvage before decay, potentially adding to downward price pressures as the supply may increase. The Company is unable to predict when and if the mountain pine beetle infestation will be halted or its impact on future lumber, chip and log prices.

### **Pulp and Paper Market Variability**

The selling price in Canadian dollars of our residual wood chips is tied by formula to the net pulp realizations in US dollars obtained by our wood chip customers. Fluctuations in pulp prices and foreign currencies will accordingly impact the selling price of our residual wood chips. The price and demand for the pulp and other logs sold to pulp and paper companies is also dependent on the market conditions for pulp and paper. If contraction in the coastal pulp and paper industry were to occur, we may need to find alternative customers for our sawmill residual chips and pulp logs.

## **Liquidity and Capital Resources**

Western has incurred net losses through the six quarters ended December 31, 2008, which has significantly impacted available liquidity. The business may continue to require substantial expenditures, and we cannot be certain that we will achieve or sustain profitability from operating activities in the future. The Rights Offering of \$50 million that closed in January 2009 provides additional liquidity to fund operations in the near term, and the Company intends to sell non-core assets to reduce outstanding debt. However, if we continue to be impacted by adverse market conditions and incur losses and make no further significant asset sales, we may need additional financing to fund continued operations and service existing debt obligations, including \$53.5 million of long term debt becoming due in September 2009. We have taken action, and are continuing to take action, to improve our cash flow, including rationalizing our operations to reduce costs, focusing sales and production efforts on margin-generating activities, identifying opportunities to increase productivity and reduce unit costs, and managing maintenance and corporate expenditures. Although we believe our actions should result in improved cash flow, there can be no assurance that we will be successful or that market forces or competition will not work to offset our actions. In the event we are not successful, the Company may consequently be in violation of certain of its loan covenants, which could result in its debt becoming immediately due and payable or in it not being able to access funds under its revolving credit facility.

## **Dependency on Fibre Obtained from Government Timber Tenures**

Currently, substantially all of the timberlands in which we operate are owned by the Province and administered by the Ministry of Forests and Range. The *Forest Act* (British Columbia) ("Forest Act") empowers the Ministry of Forests and Range to grant timber tenures, including Tree Farm Licences ("TFL"), Forest Licences ("FL"), and Timber Licences ("TL"), to producers. The Provincial Chief Forester must conduct a review of AAC for each Timber Supply Area and each TFL in the Province on a periodic basis, which is usually once every five years. This review is then used to determine the AAC for licences issued by the Province under the Forest Act. Many factors affect the AAC such as timber inventory, the amount of operable forest land, growth estimates of young forests, regulation changes and environmental and social changes. Such assessments have in the past resulted and may in the future result in reductions or increases to the AAC attributable to licences held by British Columbia forest companies (without compensation), including the licences that we hold. In addition, our AAC can be temporarily reduced (without compensation for the first four years) in areas where logging has been suspended under Part 13 of the Forest Act pending further consideration in land use planning. Land use planning and new harvesting regulations can constrain access to timber and new parks can permanently remove land from the timber harvesting land base. There can be no assurance that the amounts of such future reductions on our licences, if any, will not be material or the amounts of compensation, if any, for such reductions will be fair and adequate.

## **Forest Policy Changes in British Columbia**

In 2003 and 2004, the Province implemented the most significant legislative reforms in the British Columbia forest industry in over 40 years. The most controversial aspect of these legislative reforms involved the Province taking back approximately 20% of the AAC from major licence holders, including Western, and providing monetary compensation. There can be no assurance that the Province will not implement further policy changes, or that any such changes will not have a material adverse effect on our operations or our financial condition.

## **First Nations Land Claims**

First Nations groups have made claims of rights and title to substantial portions of land in British Columbia, including areas where our timber tenures and operations are situated, creating uncertainty as to the status of competing property rights and of legislation and Crown decisions that adversely affect such asserted rights and title. The Supreme Court of Canada has held that aboriginal groups may have a spectrum of constitutionally recognized and affirmed aboriginal rights and title in lands that have been traditionally used or occupied by their ancestors; however, such rights or title are not absolute and may be infringed by government in furtherance of a valid legislative objective, including forestry, subject to meeting a justification test. The effect on any particular lands will not be determinable until the nature of historical use, occupancy and rights in any particular piece of property have been clarified. The Supreme Court of Canada has also held that even before claims of rights and title are proven, the Crown has a legal duty to consult with First Nations, which can become a duty to seek possible accommodations, when the Crown has knowledge, real or constructive, of the potential existence of an aboriginal right or title and contemplates conduct that might adversely impact it. During the period before

asserted claims are proven, the Crown is required to consult in good faith with the intention of substantially addressing First Nation concerns, but First Nations agreement is not required in these consultations.

First Nations are seeking compensation from governments (and in some instances from forest tenure holders) with respect to these claims, and the effect of these claims on timber tenure rights, including our timber tenures, cannot be estimated at this time. The Federal and Provincial Governments have been seeking to negotiate settlements with aboriginal groups throughout British Columbia in order to resolve these claims. Any settlements that may result from these negotiations may involve a combination of cash, land, resources, grants of conditional rights of resource co-management or rights to gather food or resources on public lands, and some rights of self-government. The effect of such a settlement on our timber tenures or the amounts of compensation that we would receive for any taking from those tenures as a result of this process, if any, cannot be estimated at this time.

Current Provincial Government policy requires that forest management and operating plans take into account and not unreasonably infringe on aboriginal rights and title, proven or unproven, and provide for consultation with First Nations. This policy is reflected in the terms of our timber tenures, which provide that the Ministry of Forests may refuse to issue cutting permits in respect of a timber tenure if it is determined that the forestry operation would unreasonably interfere with aboriginal rights and title. First Nations have, at times, sought to restrict the Provincial Government from granting or replacing forest tenures and other operating authorizations or from approving forest management plans on Crown lands without full consultation and accommodation or their consent if these decisions could affect lands claimed by them. There can be no assurance that denial of required approvals for, or changes to the terms of our timber tenures, other operating authorizations or forest management plans as a consequence of such consultation or action will not have an adverse effect on our financial condition or results of operations.

The issues surrounding aboriginal title and rights are not likely to be resolved by the Federal Government or Provincial Government in the near future. In the interim period, the Ministry of Forests and Range initiated its Forest and Range Agreements program with a view to addressing an economic component of the Crown's legal obligations on an interim basis. This program provides revenue sharing and short-term forest tenure opportunities for First Nations who enter into agreements with the Provincial Government. The Ministry of Forests and Range has stated it intends to provide approximately 8% of the Province's total Crown AAC to First Nations under this program or otherwise, using the AAC taken from other licensees under the *Forestry Revitalization Act* (British Columbia). The re-allocation of tenure to First Nations is in progress and the continuity of the timber supply from these short-term tenures is uncertain.

In 2007 the British Columbia Supreme Court released a judgment in an aboriginal rights and title claim made by the Tsilhqot'in Nation and Chief Roger William regarding lands and forests in the Interior of British Columbia (the "William decision"). In the William decision, the court made a declaration of certain aboriginal rights in the claimed territory but declined, on procedural grounds, to make the declaration of aboriginal title that had been sought by the Tsilhqot'in Nation. The court offered the opinion that aboriginal title exists within and outside the claimed area and found that the present provisions of the Forest Act do not apply to areas that meet the test for aboriginal title and that the jurisdiction to legislate in respect of the granting of rights to harvest timber on such lands lies with the federal government. In the court's view, prior to a finding of aboriginal title there is a presumption that non-private forest lands are Crown lands for the purposes of the Forest Act and provincial legislative provisions apply, even where aboriginal title and other rights are alleged to exist, in which case the Crown's duty to consult First Nations is engaged. In the court's view, if that duty of consultation is properly discharged, it gives adequate protection to alleged aboriginal interests. If there is a later declaration of rights or title there is a serious risk that, without proper consultation and accommodation, such rights may be infringed. In the court's view, those persons whose aboriginal rights or title have been so compromised as a result of government action will have their remedy in damages. The legal principles enunciated in the William decision, if confirmed on an appeal or applied in subsequent decisions on aboriginal title, could ultimately have a negative impact on all of Western's Crown timber tenures or its financial condition, but the extent of any such impact is uncertain at present.

An unfavourable result in any of the First Nations litigation in which the Company is a party or which involves assets of the Company could have a material adverse effect on our financial condition or results of operations. See also "Legal proceedings".

## **Stumpage Fees**

Stumpage is the fee that the Province charges forest companies to harvest timber from Crown land in British Columbia. In January 2004, the Provincial Government announced the move to a more open and competitive market pricing system for timber and logs for the coastal region. Previously, the amount of stumpage paid for each cubic metre of wood harvested from the coastal region was based on a target rate set by the Province. Since February 29, 2004, stumpage for the coastal region is being set using the Coast Market Pricing System, which uses the results from British Columbia Timber Sales auctions to predict the value of Crown timber harvested under long-term tenures. There can be no assurance that future changes to the stumpage system or the Province's administrative policy will not have a material impact on stumpage fees payable and consequently affect our financial condition and results of operations.

## **Safety**

Western is subject to workplace safety laws and regulations. Failure to comply with these laws and regulations can result in monetary penalties and work stoppages. The laws and regulations change over time and may involve new methodologies and additional costs necessary to bring the Company into compliance.

## **Environmental Regulation**

We are subject to extensive environmental laws and regulations. These laws and regulations impose stringent standards on our operations and impose liability to remedy problems for which we are legally responsible regarding, among other things:

- air emissions;
- land and water discharges;
- operations or activities affecting watercourses or the natural environment;
- operations or activities affecting species at risk;
- use and handling of hazardous materials;
- use, handling, and disposal of waste; and
- remediation of environmental contamination.

We may incur substantial costs to comply with current or future requirements, to respond to orders or directions made, to remedy or to compensate others for the cost to remedy problems for which we are legally responsible or to comply with new environmental laws that may be adopted from time to time. In addition, we may discover currently unknown environmental problems or conditions affecting our operations or activities or for which we are otherwise legally responsible. Western has closed certain operations and although we have engaged specialists to advise us of environmental problems and conditions, normal site clean-up may identify additional problems or conditions. Any such event could have a material adverse effect on our financial condition and results of operations.

## **Regulatory Risks**

Our forestry and sawmill operations are subject to extensive federal, provincial, state, municipal and other local laws and regulations, including those governing forestry, exports, taxes, labour standards, occupational health, safety, waste disposal, building structures/systems, environmental protection and remediation, protection of endangered and protected species and land use and expropriation. Under certain laws and regulations, we are also required to obtain permits, licences and other authorizations to conduct our operations, which permits, licences and authorizations may impose additional conditions that must be satisfied. Although we budget for expenditures to maintain compliance with such laws and permits, there can be no assurance that these laws and regulations or government policy will not change in the future in a manner that could have an adverse effect on our financial condition or results of operations or the manner in which we operate. Nor can there be any assurance that administrative interpretation of existing laws and regulation will not change or more stringent enforcement of existing laws will not occur, in response to changes in the political or social environment in which we operate or otherwise, in a manner that could have an adverse effect on our financial condition or results of operations or the manner in which we operate.

## **Legal Proceedings**

In January 2008 the Ditidaht First Nation commenced litigation in the B.C. Supreme Court against the Province of British Columbia, Canada, certain other First Nations and two forestry companies, including the Company, seeking amongst other things declarations of aboriginal title and rights in areas of Vancouver Island that include areas covered by timber tenures held by the Company and declarations that provincial forestry legislation and the Company's timber tenures are of no force or effect on the claimed aboriginal title lands. This proceeding is in the early stages and no trial date has been set.

In April 2008 the Kwakiutl First Nation commenced litigation in the B.C. Supreme Court against the Province of British Columbia, Western and the Federal Government of Canada seeking, amongst other things, orders to set aside the Province's decision to remove Western's private lands from a TFL and the Province's approval of the Company's Forest Stewardship Plan on the Crown lands within their area of interest, based on alleged infringements of their treaty rights and unextinguished aboriginal title and rights. This proceeding is in the early stages and no trial date has been set.

In 2005 the Hupacasath First Nation obtained an order of the B.C. Supreme Court requiring the Province of British Columbia to consult with them regarding certain Crown decisions, including a 2004 decision of the Minister of Forests and Range to remove private lands from TFL 44, a TFL subsequently acquired by the Company. In the third quarter of 2008 the Court ordered that a mediator be appointed to address appropriate accommodation for the effects of the Minister's 2004 private land decision upon the asserted aboriginal rights of the Hupacasath First Nation on their claimed territory, both with respect to the private lands that are now outside the TFL and the Crown lands that remain within the Company's TFL. The scope of this mediation is to include, among other things, consideration of possible accommodation from resources on the Crown lands remaining in the TFL now held by the Company.

The Company is currently unable to predict the outcome of these First Nation legal proceedings on Western's ongoing operations or on any sale of its non-core assets and private forestry lands.

In addition, Western is subject to routine litigation incidental to our business, the outcome of which we do not anticipate will have a material adverse affect on our financial condition and results of operations.

## **Reliance on Directors, Management and Other Key Personnel**

Western relies upon the experience and expertise of our personnel. No assurance can be given that we will be able to retain our current personnel and attract additional personnel as necessary for the development and operation of our business. Loss of or failure to attract and retain key personnel could have a material adverse effect on Western's business.

## **Change of Control of Western**

Tricap Management Limited, which is related to Brookfield Asset Management, currently holds 49% of the outstanding Common Shares of Western and its additional equity interest in Western through Non-Voting Shares. If a change of control of Western were to occur, there could be significant adverse consequences to Western. If it is determined that there has been an acquisition of control for Canadian tax purposes we may lose the benefit of historical tax losses of subsidiaries that were incurred by our predecessor in its operations, which may limit our ability to shelter future operating income from tax. In addition, if Tricap Management or any person were to acquire sufficient Common Shares to constitute a change or acquisition of control of Western, and the British Columbia Minister of Forests and Range (the "Minister of Forests") were to be satisfied the change or acquisition of control unduly restricted competition in standing timber, log or wood chip markets, the Minister of Forests and Range could make a determination to cancel all or a part of our Forest Act (British Columbia) tenures. If this were to occur, we may have to obtain the fibre to run the combined business facilities from external sources, perhaps at a higher cost. A significant increase in our costs could have a material adverse effect on the financial condition and results of operations of the combined business.

## **Certain Voting Rights of the Non-Voting Shares**

The holders of Non-Voting Shares are generally not entitled to vote at meetings of our shareholders. They are, however, entitled to one vote per share on any vote relating to our liquidation, dissolution or winding-up, or the sale, lease or exchange of all or substantially all of our property and as otherwise provided by law or any amendment that would add, change or remove attributes of the Non-Voting Shares or any class of share

adversely affecting the Non-Voting Shares either separately or in relation to the Common Shares. As such, holders of Non-Voting Shares will be able to vote on, and potentially affect the outcome of, certain transactions, such as our liquidation or winding-up or the sale of substantially all of our assets.

***These risks should be considered in the context of our business, which is described under “Development of the Business” and “Business of the Company”.***

## **DIVIDENDS**

The payment of dividends on the Company’s Common Shares and Non-Voting Shares is at the discretion of the Board and depends on our financial condition, the need to finance capital expenditures, financial covenants in credit agreements and other factors the Board may wish to consider. No dividends have been paid by the Company on the Common Shares or the Non-Voting Shares.

Financing facilities currently in place contain covenants restricting certain payments, including the payment of dividends on Common Shares and Non-Voting Shares. The facilities provide, among other things, that any subsidiary may declare or pay dividends or otherwise make distributions in cash to the parent company or a guarantor existing under the facilities.

## **CAPITAL STRUCTURE**

### **Share Capital**

Western’s authorized capital consists of an unlimited number of Common Shares, an unlimited number of Non-Voting Shares, and an unlimited number of Preferred Shares. As of the date hereof, 128,625,600 Common Shares, 338,945,860 Non-Voting Shares and no Preferred Shares are issued and outstanding.

### **Common and Non-Voting Shares**

The Common Shares entitle the holders thereof to one vote per share. The Non-Voting Shares do not entitle the holders thereof to any votes at meetings of our shareholders (or to receive notice of or attend such meetings), subject to the condition that the Non-Voting Shares will entitle the holders thereof to one vote per share on any vote relating to our liquidation, dissolution or winding-up, or the sale, lease or exchange of all or substantially all of our property and as otherwise provided by law or any amendment that would add, change or remove attributes of the Non-Voting Shares or of any class of share adversely affecting the Non-Voting Shares either separately or in relation to the Common Shares.

The holders of Common Shares and Non-Voting Shares participate equally with each other in respect of the payment of dividends, including the amount per share of the dividend.

The Common Shares and Non-Voting Shares rank equally with each other in respect of the return of capital in the event of the liquidation, dissolution or other distribution of our assets for the purpose of winding up our affairs.

If either the Common Shares or Non-Voting Shares are subdivided, consolidated, reclassified or otherwise changed, appropriate adjustments would be made at the same time to the rights attaching to the shares of the other class to ensure the preservation of the rights of each class in relation to those of the other.

Western may convert the Non-Voting Shares into Common Shares on a one-for-one basis, in whole or in part, at any time in our sole discretion, provided that our Board of Directors is at that time of the opinion that to do so would not have a material adverse effect on the Company’s business, financial condition or business prospects. The Board has the right to select the Non-Voting Shares to be converted on a *pro rata* basis, by lot or in such other manner as it considers appropriate.

The Non-Voting Shares and Common Shares shall be treated identically by us in the event of an issuer bid by the Company. In the event that a take-over bid is made for our Common Shares that is not made on the same economic terms on a per-share basis to holders of Non-Voting Shares, Western will convert the outstanding Non-Voting Shares into Common Shares in order to enable them to participate in the take-over bid on the same terms as if the Non-Voting Shares had been converted into Common Shares before the take-over bid for the Common Shares was made.

Except as described above, the Common Shares and the Non-Voting Shares have the same rights, are equal in all respects and will be treated by us as if they were shares of one class only.

Western has entered into a registration rights agreement (the "Registration Rights Agreement") with Tricap dated March 20, 2007 providing holders of the Non-Voting Shares with "demand" and "piggy-back" registration rights, which will enable the holders to require us to file a prospectus (in respect of a "demand" registration) or enable the holders to participate in an offering made by us (in the case of a "piggy-back" registration) and otherwise assist with a public offering of Non-Voting Shares or, subject to the Exchange Limitation, Common Shares for which the Non-Voting Shares may be exchanged, subject to certain limitations. These registration rights may not be exercised until May 1, 2009, the third anniversary of the closing date of the Acquisition. The registration rights will only be exercisable in circumstances where, if the Non-Voting Shares that have been requested to be registered were exchanged for Common Shares, the Exchange Limitation would not apply, and our Board has not caused those Non-Voting Shares to be exchanged for Common Shares. Western has agreed to use best efforts to cause the shares subject to a registration request to be listed on the TSX, provided that, for greater certainty, we will not be required to issue additional Non-Voting Shares in order to secure such a listing. In the event of a "piggy-back" registration, our financing requirements would take priority. Any expenses of such a "demand" or "piggy-back" registration shall be borne by us (other than underwriting fees or other selling expenses, which shall be borne proportionately between us and the selling holders on the basis of the proportional shares of the aggregate proceeds of the offering).

### ***Preferred Shares***

The Preferred Shares may, at any time or from time to time, be issued in one or more series, and the directors may, by resolution, fix the number of Preferred Shares in, and determine the designation, rights, privileges, restrictions and conditions attaching to the Preferred Shares of each series. Before issuing Preferred Shares of a series, the directors must file with the Director of the CBCA articles of amendment. Preferred Shares of each series rank on a parity with the Preferred Shares of every other series with respect to priority in the payment of dividends and in the distribution of our assets in the event of our liquidation, dissolution or winding-up or any other distribution of our assets among shareholders for the purpose of winding-up our affairs.

If Preferred Shares were outstanding, the holders of such shares would be entitled to priority over the Common Shares and the Non-Voting Shares with respect to the payment of dividends and the distribution of our assets on a liquidation, dissolution or winding-up or other distribution of our assets for the purpose of winding-up our affairs. The Preferred Shares of each series may be given such other preferences not inconsistent with the above over the Common Shares and the Non-Voting Shares as may be determined in the case of each series authorized to be issued.

Except as otherwise required by law, the holders of the Preferred Shares are not entitled to receive notice of or to attend or to vote at any meeting of shareholders of Western.

### **Class C Warrants**

Western has outstanding 569,373 Tranche 1 Class C Warrants, 854,146 Tranche 2 Class C Warrants and 1,423,743 Tranche 3 Class C Warrants, issued as of July 28, 2004 under the Class C Warrant Indenture entered into in connection with the implementation of the Plan. In accordance with the terms of the Class C Warrant Indenture, following the completion of the Rights Offering to all shareholders, effective January 26, 2009 the Class C Warrants were re-priced so that each Class C Warrant now entitles the holder to purchase one Common Share (subject to certain adjustments) at the following exercise prices: \$14.11 (previously \$14.72) for Tranche 1 Class C Warrants, \$22.56 (previously \$23.54) for Tranche 2 Class C Warrants, and \$29.32 (previously \$30.60) for Tranche 3 Class C Warrants.

The Class C Warrants are non-transferable and have a five-year term that expires on July 27, 2009, subject to early termination provisions. Western is entitled to give a 30-day notice of termination with respect to any tranche of Class C Warrants if, during a 20-day trading period ending prior to the fifth business day prior to the date of such notice, the Common Shares trade at a weighted average price per share that is more than 125% of the exercise price of such tranche. In addition, the Class C Warrants will expire upon any amalgamation or similar business combination that results in the shareholders of Western owning less than 80% of the issued and outstanding equity shares of the continuing entity.

## MARKET FOR SECURITIES

### Trading Price and Volume

As of the date hereof the Common Shares are listed and posted for trading on the Toronto Stock Exchange under the symbol "WEF". The following sets out the price range and volumes traded on the Toronto Stock Exchange on a monthly basis for each month of the most recently completed financial year:

| Month          | High   | Low    | Volume    |
|----------------|--------|--------|-----------|
| January 2008   | \$1.70 | \$1.34 | 89,625    |
| February 2008  | \$1.65 | \$1.40 | 55,002    |
| March 2008     | \$1.65 | \$1.12 | 158,906   |
| April 2008     | \$1.35 | \$1.10 | 343,886   |
| May 2008       | \$1.35 | \$1.10 | 173,466   |
| June 2008      | \$1.20 | \$0.85 | 362,462   |
| July 2008      | \$0.96 | \$0.67 | 90,439    |
| August 2008    | \$0.95 | \$0.75 | 98,390    |
| September 2008 | \$1.00 | \$0.65 | 374,049   |
| October 2008   | \$0.82 | \$0.50 | 241,854   |
| November 2008  | \$0.74 | \$0.35 | 223,043   |
| December 2008  | \$0.38 | \$0.10 | 1,078,788 |

### Prior Sales

On January 22, 2009, pursuant to a final prospectus dated December 10, 2008 the Company issued 8,783,241 Common Shares and 254,374,654 Non-Voting Shares at a price of \$0.19 per share.

## DIRECTORS AND OFFICERS

Western's articles provide that the Board is to consist of a minimum of three directors and a maximum of 15 directors. Western currently has eight directors.

At each annual meeting of shareholders of Western, the entire Board of Directors retires and directors are elected for the next term. Each director serves until the close of the next annual meeting or until his successor is elected or appointed, unless his office is earlier vacated in accordance with our articles or with the provisions of the CBCA. Not less than 25% of the members of our Board of Directors are required to be resident Canadians, in accordance with the CBCA. Western's officers serve at the discretion of the Board.

The table below set forth the names, provinces of residence and positions with Western of the directors of Western as of the date hereof, and the principal occupation of each of them during the past five years.

| <b><u>Name and Province and Country of Residence</u></b>       | <b><u>Principal Occupation</u></b>   | <b><u>Director Since</u></b> |
|--|--|------------------------------|
| JAMES ARTHURS <sup>(1)(2)(3)</sup> .....<br>B.C., Canada       | Senior Vice President, North American Operations, Integrated Paving Concepts Inc. , a manufacturer of equipment, tooling and high technology coatings for the decorative asphalt industry. From 2002 through 2004, Managing Director, Operations, for The Jim Pattison Group. January 2002 to May 2002, Senior Vice President and Chief Information Officer for Alderwoods Group, Inc. (emergent company of the former Loewen Group) and from May 2000 to January 2002, he was with the Loewen Group. The Loewen Group was the subject of CCAA proceedings in Canada and Chapter 11 proceedings in the U.S. from June 1, 1999 to December 31, 2001.  | July 27, 2004                |
| LEE DONEY <sup>(2)(3)</sup> .....<br>B.C., Canada              | Vice Chairman of the Board since November 4, 2008. Independent consultant. Director on the Community Living Board of the British Columbia government and the Chairman of the Board of Columbia Power Corporation. Deputy Minister of Skills and Development and Labour of the British Columbia government from June 2001 until his retirement in April 2004.   | July 27, 2004                |
| DOMINIC GAMMIERO <sup>(2)</sup> .....<br>Ontario, Canada       | President and Chief Executive Officer of Western from November 4, 2008. Chairman of Fraser Papers Inc. since 2007. From 2004 until 2006, President and Chief Executive Officer of Fraser Papers Inc. and from 1999 to 2004, President and Chief Executive Officer of Norbord Inc.  | June 16, 2006                |
| ROBERT HARDING, FCA <sup>(3)(4)</sup> .....<br>Ontario, Canada | Chairman of Brookfield Asset Management Inc.   | June 16, 2006                |
| JOHN MACINTYRE, CA <sup>(1)</sup> .....<br>Ontario, Canada     | Chairman of the Board of Western since July 27, 2004. Partner in Birch Hill Equity Partners Inc. (a successor to TD Capital's private equity fund). From 2002 to 2004, he was an independent financial advisor.  | July 27, 2004                |
| CYRUS MADON, CA <sup>(3)(4)</sup> .....<br>Ontario, Canada     | Managing Partner, Tricap Partners Ltd. for Brookfield Asset Management Inc.  | June 16, 2006                |
| PIERRE MCNEIL <sup>(2)</sup> .....<br>Ontario, Canada          | Senior Vice President, Tricap Partners Ltd. and the President and CEO of Concert Industries Corp. From July 2004 to December 2006, Senior Vice President with Fraser Papers Inc. From October 2001 until July 2004 site director for Norbord Inc.'s manufacturing operations in Cowie, Scotland.   | December 20, 2007            |
| JOHN B. NEWMAN <sup>(1)(3)(4)</sup> .....<br>Ontario, Canada   | Chairman and CEO of Multibanc Financial Holdings Limited, a private investment vehicle located in Toronto. Chairman of Dale-Parizeau LM Inc., Morris & Mackenzie Inc. and the AGF Family of Mutual Funds Trusts and Corporations. Chairman of Simmons Canada Inc. until its sale on November 30, 2006, and of Multi-Fund Management Inc. until its sale on June 30, 2006. Director or member of the Independent Review Committee of certain closed-end funds administered by Scotia Capital Inc., TD Securities Inc. and BMO Nesbitt Burns Inc. Independent director of FT Capital Inc. until his resignation on December 17, 2002. FT Capital Inc. was operating under an agreed moratorium on its principal and interest payments on its subordinated debentures prior to Mr. Newman becoming one of its independent directors. Prior to Mr. Newman's resignation, FT Capital Inc. was subject to a number of cease trade orders issued in 2001 and 2002 by various securities regulatory authorities in Canada for failure to file financial statements while its principal shareholder B.C. Pacific Capital Corporation considered restructuring options with Brascan Financial Corporation. Those cease trade orders were subsequently terminated after FT Capital Inc. filed the requisite financial statements. | July 27, 2004                |

- 
- (1) Member of the Audit Committee.
  - (2) Member of the Environmental, Health and Safety Committee.
  - (3) Member of the Nominating and Corporate Governance Committee.
  - (4) Member of the Management Resources and Compensation Committee.

Messrs. Gammiero, Harding, Madon and McNeil (collectively, the “Tricap Directors”) are officers and/or directors of Brookfield and/or its subsidiaries or related entities. Mr. Gammiero is also the Chief Executive Officer of Western. Brookfield has a number of relationships with the Corporation as described under “The Company” and “Interest of Management and Others in Material Transactions.” The Board considers that these relationships with Brookfield affiliates are not an interest or a business or other relationship that could, or could reasonably be perceived to, interfere materially with the Tricap Directors’ ability to act with a view to the best interests of the Corporation, other than interests and relationships arising from shareholding. The Board also considers that four director nominees (which constitutes 50% of the eight directors) fairly reflects the relative investment of Brookfield (through Tricap) and other shareholders in the Corporation.

The transactions with Brookfield described herein were approved, as required by the Canada Business Corporations Act and applicable securities laws, by the independent directors who are not Tricap Directors.

### ***Executive Officers***

The table below set forth the names, provinces of residence and positions with Western of the executive officers of Western as of the date hereof, and the principal occupation of each of them during the past five years (other than the CEO, whose information is set forth above).

#### **Name and Province and**

#### **Country of Residence**

#### **Position with Western and Principal Occupation**

TREVOR BONIFACE  
B.C., Canada

**Vice President, Timberlands** since January 2005 and prior to that Regional Manager for the Nootka region since July 2004. Regional Manager for the Nootka region for Doman since 1998. Mr. Boniface has a Bachelor of Science Degree in Forestry (Harvesting Option) and is also a Registered Professional Forester (British Columbia).

NORM FACEY  
B.C., Canada

**Vice President, Manufacturing** since August of 2007. Previously, Vice President of Operations at Catalyst Paper. Mr. Facey holds a Bachelor of Applied Science from the University of British Columbia and is a Registered Professional Engineer.

DOMINIC GAMMIERO  
Ontario, Canada

**President, Chief Executive Officer and Director**

MURRAY JOHNSTON  
B.C., Canada

**Vice President, Chief Financial Officer, and Corporate Secretary** since December 2007. Previously Vice President and Chief Financial Officer of Wipak Ltd., since 1999. Mr. Johnston is a Chartered Accountant.

DUNCAN KERR  
B.C., Canada

**Senior Vice President and Chief Operating Officer** since August 2005. Previously, senior project manager with RLG International. Mr. Kerr has a Bachelor of Engineering from McGill University.

JENS NILAUSEN  
B.C., Canada

**Vice President, Sales and Marketing** since September 12, 2005. Previously Sales Manager for our Export Division since July 2004 and prior to that with Doman since June of 1998 in the same position. Mr. Nilausen has a Bachelor of Arts Degree in Business Administration from the Copenhagen Business School, a Diploma of Business Management from the University of British Columbia, and attended the European Institute of Business Administration in France (Young Manager’s Program).

NEIL STEVENS  
B.C., Canada

**Vice President, Fibre Optimization** since June 2006. From 1994 to 2006, he held various positions with Weyerhaeuser in Softwood Lumber and in Canadian Forestlands, conducting work primarily in Alberta, Saskatchewan and Ontario. Prior to that Mr. Stevens was employed in forestry consulting in Alberta, as Manager and Senior Consultant. Mr. Stevens has a Bachelor and a Master of Science degree in Forestry from the University of Alberta and is a non-resident member of the College of Alberta Professional Foresters.

### ***Shareholdings of Directors and Executive Officers***

As at the date hereof, except as described herein, none of our Common Shares are beneficially owned, directly or indirectly, and no direction or control over any of our shares is exercised by any of the directors and executive officers of Western. As of the date hereof, Tricap Management Limited (as manager for Tricap) has the right to control or direct 63,026,544 Common Shares (49% of the issued and outstanding Common Shares) and 338,945,860 Non-Voting Shares (100% of the issued and outstanding Non-Voting Shares). Mr. MacIntyre is a member of the independent advisory board of Tricap. Of the shares beneficially owned by the co-investors in Tricap, 441 Common Shares are beneficially owned by Mr. McIntyre. However, as disclosed above, Tricap

Management has the right to control or direct those shares, including the right to vote or dispose of them. Mr. Arthurs, Mr. Doney, Mr. MacIntyre and Mr. Johnston beneficially own 11,436, 5,000, 441 and 22,873 Common Shares, respectively. Together, these 39,750 shares represent less than one percent of the Company's outstanding Common Shares.

### **AUDIT COMMITTEE**

The Audit Committee was established to assist the Board in fulfilling its oversight responsibilities regarding:

- (a) the accuracy and completeness of our financial statements;
- (b) our internal control and financial reporting systems;
- (c) the selection and activities of our external auditor;
- (d) risk management; and
- (e) our compliance with legal and regulatory requirements.

The committee is responsible for the oversight of financial reporting and disclosure, annual and quarterly review of financial statements, and the related management's discussion and analysis and earnings release, and oversight of internal controls and disclosure procedures. The committee also recommends the appointment of our external auditors, reviews the annual audit plan and auditor compensation, approves non-audit services provided by the external auditor, reviews hiring policies regarding former staff and auditors and reviews the adequacy of our risk management policies and procedures.

The Audit Committee has adopted a charter that reflects these and other responsibilities. The charter as most recently approved by the Board of Directors is attached as an appendix to this Annual Information Form.

### **Composition of and Education and Experience of Members of the Audit Committee**

The Audit Committee is comprised of three directors being, as of February 25, 2009, John MacIntyre – Chairman, James Arthurs and John B. Newman. The Board of Directors has determined that all three members of the Audit Committee are independent and financially literate under the standards established by Canadian securities regulatory authorities in Multilateral Instrument 52-110-Audit Committees. During 2008, the Audit Committee met 10 times.

### **Relevant Education and Experience**

**John MacIntyre, CA – Chairman** – Mr. MacIntyre is a Chartered Accountant, a Chartered Business Valuator and a graduate of Queen's University. He has extensive experience with accounting, finance and audit committee functions. He is a partner in Birch Hill Equity Partners Inc. (a successor to TD Capital's private equity fund). Mr. MacIntyre has been a director of several public and private corporations, and is currently a member of the advisory boards of TD Capital Private Equity Investors, TD Capital Ventures and Tricap Restructuring Fund.

**James Arthurs** – Mr. Arthurs is Senior Vice President, North American Operations, Integrated Paving Concepts Inc., a manufacturer of equipment, tooling and high technology coatings for the decorative asphalt industry. In addition to his current occupation, he has held several other positions requiring a high degree of financial acumen including Managing Director, Operations, for The Jim Pattison Group and Senior Vice President and Chief Information Officer for the Alderwoods Group, Inc. Mr. Arthurs holds a Bachelor of Science Degree in Computer Science from the University of Calgary.

**John B. Newman** – Mr. Newman has extensive financial and audit committee experience. He is currently the Chairman and CEO of Multibanc Financial Holdings Limited, a private investment vehicle located in Toronto. He is also Chairman of Dale-Parizeau LM Inc., Morris & Mackenzie Inc. and the AGF Family of Mutual Funds Trusts and Corporations and was formerly the Chairman of Simmons Canada Inc., First Place Tower Inc. and Multi-Fund Management Inc. Until his retirement in 1990 Mr. Newman was the Deputy Chairman of Prudential Securities (Canada).

### Pre-Approval Policies and Procedures of Non-Audit Services

The Audit Committee has adopted a policy that requires, in accordance with applicable law, its pre-approval of all non-audit services to be provided by the Company's auditors. The Audit Committee has adopted the following pre-approval policies:

- (a) Annually, the Audit Committee will review a list of audit, audit-related, tax and other non-audit services and recommend pre-approval of these services.
- (b) All additional requests to engage our auditor for other services will be addressed on a case-by-case specific engagement basis. Except as otherwise permitted by applicable law, the engagement may only commence upon approval by the Audit Committee.

### External Auditor Service Fees

The aggregate fees billed for professional services rendered by our auditors, KPMG LLP to us for the years ended December 31, 2008 and 2007 are as follows:

|                               | Fees Paid          |                    |
|-------------------------------|--------------------|--------------------|
|                               | 2008               | 2007               |
| Audit services                | \$745,000          | \$860,000          |
| Audit-related services        | 202,000            | 623,000            |
| Taxation services             | 134,000            | 149,000            |
| Other non-audit services      | -                  | -                  |
| <b>Total for all services</b> | <b>\$1,081,000</b> | <b>\$1,632,000</b> |

**Description of Services:**

Audit services include the audit of the annual financial statements of the Corporation and its subsidiaries and the review of the Corporation's unaudited interim financial statements.

Audit-related services include audits of the Corporation's pension plans, accounting advice relating to new or complex accounting standards, supplemental audit and review procedures conducted during the course of the year and the auditor's involvement with offering and continuous disclosure documents.

Taxation services consist of tax compliance services and tax planning and structuring.

### LEGAL PROCEEDINGS

In addition to the legal proceedings referred to elsewhere in this Annual Information Form, in the normal course of business, Western is subject to a number of claims and legal actions that may be made by customers, suppliers, logging contractors and others in respect of which either provision has been made or for which no material liability is expected. Where we are not able to determine the outcome of these disputes, no amounts have been accrued in our financial statements.

Other than as disclosed elsewhere herein, we are not aware of any material legal proceedings to which we are a party or to which our property is subject, nor are we aware that any such proceedings are contemplated.

## INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS

Except as otherwise disclosed herein, we are not aware of any material interest, direct or indirect, of any director or executive officer of the Company, any person or company that is the direct or indirect beneficial owner of, or who exercises control or direction over, more than 10% of the voting rights attached to the Common Shares, or any associate or affiliate of any of the foregoing, in any transaction within the three most recently completed financial years or during the current financial year that has materially affected or will materially affect us. The transactions comprise:

- The Company has certain arrangements with entities related to Brookfield Asset Management Inc. ("BAM") to provide financing, acquire and sell logs, lease certain facilities, provide access to roads and other areas, and acquire services including insurance, all in the normal course and at market rates or at cost. During the year ended December 31, 2008 the Company incurred costs of \$28.8 million (2007 - \$42.8 million; 2006 - \$43.2 million) and charged entities related to BAM \$0.8 million (2007 - \$6.8 million; 2006 - \$8.5 million) in connection with these arrangements.
- On January 22, 2009 the Company closed a Rights Offering pursuant to a final prospectus dated December 10, 2008 to all shareholders raising \$50.0 million before issue expenses. See *"Development of the Business - Significant Developments Since January 2006"*.
- In December, 2008 BAM, an affiliate of Tricap Management, agreed to provide credit support to the Corporation by way of a letter of credit for \$15.0 million (the "Letter of Credit") in favour of one of the Corporation's lenders. Western will reimburse BAM in connection with the provision of the Letter of Credit for BAM's costs with an incremental return component. The letter of credit was withdrawn following the closing of the Rights Offering.
- On May 1, 2006, the Company acquired Cascadia Forest Products Ltd. from a wholly-owned subsidiary of BAM for cash consideration of \$202.2 million. See *"Development of the Business - Significant Developments Since January 2006"*.
- Also on May 1, 2006 Western raised \$295 million before issue expenses on the closing of an offering of rights to acquire subscription receipts exchangeable for Common Shares (the "2006 Rights Offering"). See *"Development of the Business - Significant Developments Since January 2006"*.
- On March 10, 2006, Western entered into a senior secured credit agreement with BBLF (the "BBLF Credit Agreement") pursuant to which BBLF provided Western with new senior secured credit facilities (the "BBLF Facilities") in the form of a US\$187.5 million term loan facility (the "U.S. Facility"), and a \$90 million term loan facility (the "Canadian Facility"). The proceeds of the BBLF Facilities were used to redeem Western's US\$221 million 15% Secured Bonds, together with all accrued interest. The US Facility had a term of 48 months maturing on March 10, 2010 and the Canadian Facility has a term of 12 months, which was extended for one additional 12-month period to mature on March 10, 2008 on payment of a fee of 2% of the balance outstanding. Interest on the US Facility was originally payable at a rate equal to the one-month London Interbank Offered Rate plus 8.15% but was subsequently reduced. Interest on the Canadian Facility was calculated at a rate equal to the CIBC Prime bank rate plus 5.25%. During 2006 US\$4.2 million was paid down against the US debt upon completion of the equity rights offering. A further US\$88.0 million was paid down in the fourth quarter of 2006 upon receipt of the softwood lumber duty refund. In March 2007 Western renegotiated the terms of the US facility reducing the interest rate to the one-month London Interbank Offered Rate plus 3.00% and repaid a further US\$21.8 million of the debt then outstanding. The remaining balance of the BBLF Facilities was repaid on March 14, 2008 from the proceeds of new term debt.

## TRANSFER AGENTS AND REGISTRARS

The registrar and transfer agent for our Common Shares is Computershare Investor Services Inc. at its principal office in Vancouver located at 3<sup>rd</sup> Floor, 510 Burrard Street, Vancouver, British Columbia, V6C 3B9 and 11<sup>th</sup> Floor, 100 University Avenue, Toronto, Ontario, M5J 2Y1.

The registrar and transfer agent for our Class C Warrants is Computershare Trust Company of Canada at its principal offices located at 3<sup>rd</sup> Floor, 510 Burrard Street, Vancouver, British Columbia, V6C 3B9.

The register of transfers for our:

- (a) Common Shares is located at our Transfer Agent's principal offices in Vancouver, British Columbia and Toronto, Ontario; and
- (b) Class C Warrants is located at the Class C Warrant Trustee's principal offices in Vancouver, British Columbia and Toronto, Ontario.

## MATERIAL CONTRACTS

Except for contracts entered into in the ordinary course of business or as otherwise disclosed herein, Western has not entered into any other material contracts within the most recently completed financial year or before the most recently completed financial year (but after January 1, 2002) and still in effect.

The material contracts disclosed herein are:

- Long-term fibre supply agreement as further described under "*Development of the Business — Significant Developments Since January, 2006.*"

## INTEREST OF EXPERTS

Our auditors, KPMG LLP, have prepared the audit report attached to our audited financial statements for our most recent year-end. KPMG LLP has confirmed that it is independent with respect to the Company within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of British Columbia as of February 11, 2009.

## ADDITIONAL INFORMATION

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of our securities, and securities authorized for issuance under equity compensation plans, will be contained in our management information circular for our annual meeting of shareholders expected to be held in May 2009. Additional financial information is provided in our audited financial statements and accompanying management's discussion and analysis for our most recent year-end. Additional information relating to Western is available on SEDAR at [www.sedar.com](http://www.sedar.com) under the Company name.

## GLOSSARY OF CERTAIN TERMS

Certain terms used herein are defined below.

|                                |  |
|--------------------------------|--|
| “AAC” .....                    | Allowable annual cut — the volume of timber which the holder of a tree farm licence or forest licence may harvest under the licence in any given year as determined by the Ministry of Forests.  |
| “annual cut” .....             | The volume of timber which the holder of a timber licence expects to harvest annually from that timber licence.  |
| “BAM” .....                    | Brookfield Asset Management Inc.   |
| “BBLF” .....                   | Brookfield Bridge Lending Fund Inc.  |
| “BBLF Facilities” .....        | The US Facility and the Canadian Facility, collectively, described under “Capital and Debt Structure – Senior Secured Facilities”.   |
| “board feet” .....             | The plural of board foot; a board foot is calculated by multiplying 1” x 12” x 12” = 1 foot board measure gross count. Lumber is then finished (planed/sanded) to a smaller size and sold based on the original gross count. The difference between gross size and net size is approximately 7%. |
| “Canadian GAAP” .....          | Canadian generally accepted accounting principles.   |
| “CBCA” .....                   | <i>Canada Business Corporations Act</i> , as amended.  |
| “CIBC Prime”                   | Canadian Imperial Bank of Commerce prime lending rate  |
| “CIT” .....                    | CIT Business Credit Canada Inc.  |
| “Exchange Limitation” .....    | Means the requirement that no holder or group of holders should beneficially own, or exercise control or direction over, 50% or more of the Common Shares,.  |
| “forest licence” or “FL” ..... | A licence granted by the Ministry of Forests which entitles the holder to cut a specific volume of timber on government lands.   |
| “FR Act” .....                 | <i>Forestry Revitalization Act</i> (British Columbia).   |
| “green” .....                  | A term used to describe lumber that is not kiln-dried or air-dried.  |
| “hectare” .....                | An area 100 metres by 100 metres, equal to 2.47 acres.   |
| “hog fuel” .....               | Wood residue produced by a sawmill or a log merchandiser.  |
| “ISO” .....                    | International Standards Organization.  |
| “m <sup>3</sup> ” .....        | A cubic metre.   |
| “Ministry of Forests” .....    | The Ministry of Forests and Range of British Columbia.   |
| “MMfbm” .....                  | One million board feet measure (see “board feet”).   |
| “Part 13” .....                | Part 13 of the Forest Act, under which the Province of B.C. may suspend cutting authorities or plans in identified areas in the public interest for a period of time specified in regulations. Also known as “Designated” or “Protected” areas.  |

|                                      |   |
|--------------------------------------|---|
| “replaceable contract” .....         | Replaceable contract under the Forest Act. An “evergreen” timber harvesting contract that is entered into between a holder of a replaceable licence and a contractor, whereby the contractor is obligated to perform one or more defined phases of timber harvesting within the licence and, if satisfactorily performed, the licence holder is obligated, prior to the expiry of the term of the contract, to offer the contractor a replacement contract on substantially the same terms and conditions as the contract being replaced. |
| “SPF 2x4 lumber” .....               | 2” x 4” kiln-dried random lengths of spruce, pine and fir lumber, which is a North American commodity grade of standard and better dimensional lumber.  |
| “sustained yield” .....              | The yield that a forest can produce continuously (i.e. in perpetuity) at a given intensity of management without impairment of the land’s productivity, with the intent that there will be a balance between timber growth and harvesting on a sustainable basis.   |
| “timber licence” or “TL” .....       | A licence granted by the Ministry of Forests which entitles the holder to harvest the area over a specified period.   |
| “timber supply areas” or “TSA” ..... | The areas of Provincial Government timberland which are not designated as TFLs.   |
| “tonne” .....                        | A metric tonne — 1,000 kilograms or 2,204.6 pounds.   |
| “tree farm licence” or “TFL” .....   | A TFL is a replaceable timber tenure that requires the licensee to manage a specified area of timberland on a sustained yield basis. TFLs are granted for 25-year terms and, subject to satisfactory performance of its obligations under the TFL agreement by the licensee, are replaced by the Minister of Forests every five to 10 years with a new TFL with a 25-year term.   |
| “Tricap” .....                       | Tricap Management Limited.  |
| “TSX” .....                          | Toronto Stock Exchange  |
| “volumetric unit” .....              | Equals 200 cubic feet of wood chips.  |
| “wood chips” .....                   | Small pieces of wood used to make pulp. The wood chips are produced either from wood-waste in a sawmill or a log merchandiser or from pulp wood cut specifically for this purpose. Wood chips are generally uniform in size and are larger and coarser than sawdust.  |

**APPENDIX**  
**WESTERN FOREST PRODUCTS INC.**  
**AUDIT COMMITTEE CHARTER**

**1. Purpose**

The Board of Directors (the "Board") of Western Forest Products Inc. (the "Corporation") has established an Audit Committee (the "Committee") to assist the Board in fulfilling its oversight responsibilities regarding:

- (a) the accuracy and completeness of the Corporation's financial statements;
- (b) the internal control and financial reporting systems of the Corporation;
- (c) the selection and activities of the Corporation's external auditor;
- (d) risk management;
- (e) the Corporation's compliance with legal and regulatory requirements, and
- (f) any additional duties set out in this Charter or otherwise delegated to the Committee by the Board.

**2. Members**

Committee members, including the Committee Chair, shall be appointed annually by the Board based on recommendations of the Nominating and Corporate Governance Committee and shall consist of at least three members of the Board who meet the independence requirements of Multilateral Instrument 52-110 - Audit Committees.

All members of the Committee shall be financially literate. While the Board shall determine the definition of and criteria for financial literacy, this shall, at a minimum, include the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the Corporation's financial statements.

**3. Duties**

The Committee shall have the following duties:

- (a) Financial Reporting and Disclosure
  - (i) *Audited Annual Financial Statements*: Review the audited annual financial statements as prepared by management in conjunction with the external auditors, related management discussion and analysis ("MD&A") and earnings press releases for submission to Board for approval.
  - (ii) *Quarterly Review*: Review the unaudited quarterly financial statements, the related MD&A and earnings press releases for submission to the Board for approval.
  - (iii) *Significant Accounting Practices and Disclosure Issues*: Review with management and the external auditor, significant accounting practices employed by the Corporation and disclosure issues, including complex or unusual transactions, judgmental areas such reserves or estimates, significant changes to accounting principles, and alternative treatments under Canadian GAAP for material transactions. This review process shall be undertaken in order to have reasonable assurance that the financial statements are complete, do not contain any misrepresentations, and present fairly the Corporation's financial position and the results of its operations in accordance with Canadian GAAP.

- (iv) *Compliance*: Confirm through discussions with management and auditors whether Canadian GAAP and all applicable laws or regulations related to financial reporting and disclosure have been considered and obtain confirmations from management that Canadian GAAP and all such applicable laws have been complied with.
  - (v) *Legal Events*: Review any actual or anticipated litigation or other events, including tax assessments, which could have a material current or future affect on the Corporation's financial statements, and the manner in which these have been disclosed in the financial statements.
  - (vi) *Off-Balance Sheet Transactions*: Discuss with management the effect of any off-balance sheet transactions, arrangements, obligations and other relationships with unconsolidated entities or other persons that may have a material current or future affect on the Corporation's financial condition, changes in financial condition, results of operations, liquidity, capital expenditures, capital resources, or significant components or revenues and expenses.
  - (vii) *Disclosure Procedures*: Satisfy itself that adequate procedures are in place for the review of the Corporation's public disclosure of financial information extracted from the Corporation's financial statements and periodically assess the adequacy of those procedures.
- (b) Oversight of Internal Controls
- (i) *Review and Assessment*: Review the adequacy and effectiveness of the Corporation's system of internal control and management information systems through discussions with management and the external auditor.
  - (ii) *Oversight*: Oversee system of internal control, by:
    - Consulting with the external auditor regarding the adequacy of the Corporation's internal controls;
    - Monitoring policies and procedures for internal accounting, financial control and management information, electronic data control and computer security;
    - Obtaining from management adequate assurances that all statutory payments and withholdings have been made; and
    - Taking other actions as considered necessary.
  - (iii) *Fraud*: Oversee investigations of alleged fraud and illegality relating to the Corporation's finances and any resulting actions.
  - (iv) *Complaint*: Establish procedures for the receipt, retention and treatment of complaints received by the Corporation regarding accounting, internal accounting controls or auditing matters, the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters, and for the protection from retaliation of those who report such complaints in good faith.
- (c) External Audit
- (i) *Appointment or Replacement*: Recommend the appointment or replacement of the external auditor to the Board, who will consider the recommendation prior to submitting the nomination to the shareholders for their approval.
  - (ii) *Compensation*: Review with management, and make recommendations to the Board, regarding the compensation of the external auditor. In making a recommendation with respect to compensation, the Committee shall consider the number and nature of reports issued by the external auditor, the quality of internal controls, the size, complexity and financial condition of the Corporation, and the extent of other support provided by the Corporation to the external auditor.

- (iii) *Reporting Relationships*: The external auditor will report directly to the Committee.
- (iv) *Performance*: Review with management the terms of the external auditor's engagement, accountability, experience, qualifications and performance. Evaluate the performance of the external auditor.
- (v) *Transition*: Review management's plans for an orderly transition to a new external auditor, if required.
- (vi) *Audit Plan*: Review the audit plan and scope of the external audit with the external auditor and management, and consider the nature and scope of the planned audit procedures.
- (vii) *Audit Plan Changes*: Discuss with the external auditor any significant changes required in the approach or scope of their audit plan, management's handling of any proposed adjustments identified by the external auditor, and any actions or inactions by management that limited or restricted the scope of their work.
- (viii) *Review of Results*: Review, independently from management and without management present, the results of the annual external audit, the audit report thereon and the auditor's review of the related MD&A, and discuss with the external auditor the quality (not just the acceptability) of accounting principles used, any alternative treatments of financial information that have been discussed with management, the ramifications of their use and the auditor's preferred treatment, and any other material communications with management.
- (ix) *Disagreements with Management*: Resolve any disagreements between management and the external auditor regarding financial reporting.
- (x) *Material Written Communications*: Review all other material written communications between the external auditor and management, including the post-audit management letter containing the recommendations of the external auditor, management's response and, subsequently, follow up identified weaknesses.
- (xi) *Interim Financial Statements*: Engage the external auditor to review all internal financial statements and review the results of the auditor's review of the interim financial statements and the auditor's review of the related MD&A independent of and without management present.
- (xii) *Other Audit Matters*: Review any other matters related to the external audit that are to be communicated to the Committee under generally accepted auditing standards or that relate to the external auditor.
- (xiii) *Meeting with External Auditor*: Meet with the external auditor independently from management and without management present (1) at least annually to discuss and review specific issues; and (2) as appropriate with respect to any significant matters that the auditor may wish to bring to the Committee for its consideration.
- (xiv) *Correspondence*: Review with management and the external auditor any correspondence with regulators or governmental agencies, employee complaints or published reports that raise material issues regarding the Corporation's financial statements or accounting policies.
- (xv) *Independence*: At least annually, and before the external auditor issues its report on the annual financial statements, review and confirm the independence of the external auditor through discussions with the auditor on their relationship with the Corporation, including details of all non-audit services provided. Consider the safeguards implemented by the external auditor to minimize any threats to their independence, and take action to eliminate all factors that might impair, or be perceived to impair, the independence of the external auditor. Consider the number of years the lead audit partner has been assigned to the Corporation, and consider whether it is appropriate to

recommend to the Board a policy of rotating the lead audit partner more frequently than every five years, as is required under the rules of the Canadian Public Accountability Board.

- (xvi) *Non-Audit/Audit Services*: Pre-approve, in accordance with applicable law, any non-audit services to be provided to the Corporation by the external auditor, with reference to compatibility of the service with the external auditor's independence.
- (xvii) *Hiring Policies*: Review and approve the Corporation's hiring policies regarding partners, employees and former partners and employees of the present and former external auditor.

(d) **Risk Management**

Review and assess the adequacy of the Corporation's risk management policies and procedures with respect to the Corporation's principal business risks. Review and assess the adequacy of the implementation of appropriate systems to mitigate and manage the risks, and report regularly to the Board. Review the Corporation's insurance program.

(e) **Regulatory Compliance**

Review with management the Corporation's relationship with regulators and the timeliness and accuracy of Corporation filings with regulatory authorities.

(f) **Related Party Transactions**

Review with management all related party transactions and the development of policies and procedures related to those transactions.

(g) **Board Relationship and Reporting**

- (i) *Adequacy of Charter*: Review and assess the adequacy of the Committee Charter annually and submit such amendments as the Committee proposes to the Board.
- (ii) *Disclosure*: Oversee appropriate disclosure of the Committee's Charter, and other information required to be disclosed by applicable legislation, in the Corporation's Annual Information Form and all other applicable disclosure documents, including any management information circular distributed in connection with the solicitation of proxies from the Corporation's security holders.
- (iii) *Reporting*: Report regularly to the Board on Committee activities, issues and related recommendations.

4. **Chair**

The Board will in each year appoint the Chair of the Committee. The Chair shall be financially literate. In the Chair's absence, or if the position is vacant, the Committee may select another member as Chair. The Chair will have the right to exercise all powers of the Committee between meetings but will attempt to involve all other members as appropriate prior to the exercise of any powers and will, in any event, advise all other members of any decisions made or powers exercised.

5. **Meetings**

The Committee shall meet at the request of its Chair, but in any event it will meet at least four times a year. Notices calling meetings shall be sent to all Committee members. The external auditor or any member of the Committee may call a meeting of the Committee. The Chair of the Committee shall develop and set the Committee's agenda, in consultation with the other members of the Committee. Each member of the Committee is free to suggest the inclusion of items on the agenda. The agenda and information concerning the business to be conducted at each Committee meeting shall be distributed to the members of the Committee in advance of each meeting to permit meaningful review.

6. **Quorum**

A majority of members of the Committee, present in person, by teleconference, or by videoconference will constitute a quorum.

7. **Removal and Vacancy**

A member may resign from the Committee, and may be removed and replaced at any time by the Board, and will automatically cease to be a member as soon as the member ceases to be a director. The Board will fill vacancies in the Committee by appointment from among the directors of the Board in accordance with Section 2 of this Charter. Subject to quorum requirements, if a vacancy exists on the Committee, the remaining members will exercise all its powers.

8. **Experts and Advisors**

In order to carry out its duties, the Committee may retain or appoint, at the Corporation's expense, such independent counsel and other experts and advisors as it deems necessary. The Committee shall provide notice to the Nominating and Corporate Governance Committee of its actions in this regard.

9. **Access**

The Committee may have access to and direct contact with any employee, contractor, supplier, customer or other person that is engaged in any business relationship with the Corporation to confirm information or to investigate any matter within the mandate of the Committee.

10. **Secretary and Minutes**

The Chair of the Committee shall appoint a secretary for each meeting to keep minutes of such meeting. The minutes of the Committee will be in writing and duly entered into the books of the Corporation. The minutes of the Committee will be circulated to all members of the Board.

Dated as of May 6, 2005