Domtar CORP
Form 10-K
February 22, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM TO
Commission File Number: 001-33164

Domtar Corporation

(Exact name of registrant as specified in its charter)

Delaware	20-5901152
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
234 Kingsley Park Drive	
Fort Mill, SC	29715
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (803) 802-7500

Securities registered pursuant to Section 12(b) of the Act: Common Stock, Par Value $0.01 Per Share; Common stock traded on the New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES NO

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. YES NO

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

Indicate by check mark whether the Registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit such files). YES NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Small reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES NO

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant, based on the closing price of the shares of common stock on The New York Stock Exchange on June 30, 2018, was $3,002,586,945.

The number of shares of Registrant's Common Stock outstanding as of February 16, 2019 was 62,923,743.

Portions of the Registrant's Proxy Statement relating to the Annual Meeting of Shareholders, scheduled to be held on May 8, 2019, are incorporated by reference into Part III of this Report.

DOMTAR CORPORATION

ANNUAL REPORT ON FORM 10-K

FOR THE YEAR ENDED DECEMBER 31, 2018

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PART I

ITEM 1. BUSINESS

GENERAL

We design, manufacture, market and distribute a wide variety of fiber-based products including communication papers, specialty and packaging papers and absorbent hygiene products. The foundation of our business is a network of wood fiber converting assets that produce paper grade, fluff and specialty pulp. More than 50% of our pulp production is consumed internally to manufacture paper and other consumer products, with the balance sold as market pulp. We are the largest integrated marketer of uncoated freesheet paper in North America serving a variety of customers, including merchants, retail outlets, stationers, printers, publishers, converters and end-users. We are also a marketer and producer of a broad line of incontinence care products as well as infant diapers. To learn more, visit www.domtar.com.

We operate the following business segments: Pulp and Paper and Personal Care. We had revenues of $5.5 billion in 2018, of which approximately 82% was from the Pulp and Paper segment and approximately 18% was from the Personal Care segment.

Throughout this Annual Report on Form 10-K, unless otherwise specified, “Domtar Corporation,” “the Company,” “Domtar,” “we,” “us” and “our” refer to Domtar Corporation, its subsidiaries, as well as its investments.

AVAILABILITY OF INFORMATION

In this Annual Report on Form 10-K, we incorporate by reference certain information contained in other documents filed with the Securities and Exchange Commission (“SEC”) and we refer you to such information. We file annual, quarterly and current reports and other information with the SEC. The SEC maintains a website at www.sec.gov that contains our quarterly and current reports, proxy and information statements, and other information we file electronically with the SEC. You may also access, free of charge, our reports filed with the SEC through our website. Reports filed or furnished to the SEC will be available through our website as soon as reasonably practicable after they are filed or furnished to the SEC. The information contained on or connected to our website, www.domtar.com, is not incorporated by reference into this Form 10-K and should in no way be construed as a part of this or any other report that we filed with or furnished to the SEC.

OUR CORPORATE STRUCTURE

At December 31, 2018, Domtar Corporation had a total of 62,914,569 shares of common stock issued and outstanding.

Our common stock is traded on the New York Stock Exchange and the Toronto Stock Exchange under the symbol “UFS”.

Information regarding our common stock is included in Item 8, Financial Statements and Supplementary Data under Note 20 “Shareholders’ Equity”.

OUR BUSINESS SEGMENTS

We have two reportable segments as described below, which also represent our two operating segments. Each reportable segment offers different products and services and requires different manufacturing processes, technology and/or marketing strategies. The following summary briefly describes the operations included in each of our reportable segments.

- Pulp and Paper: Our Pulp and Paper segment consists of the design, manufacturing, marketing and distribution of communication, specialty and packaging papers, as well as softwood, fluff and hardwood market pulp.
- Personal Care: Our Personal Care segment consists of the design, manufacturing, marketing and distribution of absorbent hygiene products.

Information regarding our reportable segments is included in Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations, as well as Item 8, Financial Statements and Supplementary Data under Note 23 “Segment Disclosures”. Geographic information is also included under Note 23 of the Financial Statements and Supplementary Data.

PULP AND PAPER

Our Manufacturing Operations

We produce approximately 4 million metric tons of softwood, fluff and hardwood pulp at 12 of our 13 mills (Port Huron being a non-integrated paper mill). More than 50% of our pulp is consumed internally to manufacture paper, with the balance being sold as market pulp. We also purchase limited papergrade pulp from third parties for specific grades and to optimize the logistics of our pulp capacity while reducing transportation costs.

We are the largest integrated manufacturer and marketer of uncoated freesheet paper in North America. We have nine integrated pulp and paper mills and one non-integrated paper mill (eight in the United States and two in Canada), with an annual paper production capacity of approximately 3 million tons of uncoated freesheet paper. Our paper manufacturing operations are supported by 13 converting and forms manufacturing operations (including a network of 10 plants located offsite from our paper making operations). Approximately 77% of our paper production capacity is in the United States and the remaining 23% is located in Canada.

We produce market pulp in excess of our internal requirements at our pulp and paper mills in Ashdown, Espanola, Hawesville, Windsor, Marlboro and Nekoosa. We also produce papergrade, fluff and specialty pulps at our three stand-alone pulp mills in Kamloops, Dryden and Plymouth. We can sell approximately 1.8 million metric tons of pulp per year depending on market conditions. Approximately 54% of our trade pulp production capacity is in the U.S., and the remaining 46% is located in Canada.

The table below lists our operating pulp and paper mills and their annual production capacity:

PRODUCTION FACILITY	Fiberline	Pulp Capacity	Saleable Paper [1]		
	# lines	('000 ADMT) [2]	# machines	Category [3]	('000 ST) [2]
Uncoated freesheet					
Ashdown, Arkansas	3	707	2	Communication	265
Windsor, Quebec	1	447	2	Communication	642
Hawesville, Kentucky	1	412	2	Communication	596
Kingsport, Tennessee	1	304	1	Communication	426
Marlboro, South Carolina	1	320	1	Specialty & Packaging	274
Johnsonburg, Pennsylvania	1	228	2	Communication	344
Nekoosa, Wisconsin	1	155	3	Specialty & Packaging	168
Rothschild, Wisconsin	1	65	1	Communication	131
Port Huron, Michigan	—	—	4	Specialty & Packaging	113
Espanola, Ontario	2	327	2	Specialty & Packaging	69
Total Uncoated freesheet	12	2,965	20		3,028
Pulp					
Kamloops, British Columbia	1	354	—		—
Dryden, Ontario	1	327	—		—
Plymouth, North Carolina	1	390	—		—
Total Pulp	3	1,071	—		—

Total	15	4,036	20	3,028
Total Trade Pulp [4]		1,789		

[1] Paper capacity is based on an operating schedule of 360 days and the production at the winder.
[2] ADMT refers to an air dry metric ton and ST refers to short ton.
[3] Represents the majority of the capacity at each of these facilities.
[4] Estimated third-party shipments dependent upon market conditions. This also includes shipments to our Personal Care segment.

Our Raw Materials

The manufacturing of pulp and paper requires wood fiber, chemicals and energy. We discuss these three major raw materials used in our manufacturing operations below.

Wood Fiber

United States pulp and paper mills

The fiber used by our pulp and paper mills in the United States is softwood and hardwood, both readily available in the market from multiple third-party sources. The mills obtain fiber from a variety of sources, depending on their location. These sources include a combination of supply contracts, wood lot management arrangements, advance stumpage purchases and spot market purchases.

Canadian pulp and paper mills

The fiber used at our Windsor pulp and paper mill is hardwood originating from a variety of sources, including purchases on the open market in Canada and the United States, contracts with Quebec wood producers' marketing boards, public land where we have wood supply allocations and from Domtar's private lands. The softwood and hardwood fiber for our Espanola pulp and paper mill and the softwood fiber for our Dryden pulp mill, are obtained from third parties, directly or indirectly from public lands and through designated wood supply allocations. The fiber used at our Kamloops pulp mill is all softwood, originating mostly from third-party sawmill operations in the southern-interior part of British Columbia.

Cutting rights on public lands related to our pulp and paper mills in Canada represent about 1.5 million cubic meters of softwood and 0.8 million cubic meters of hardwood per year. Access to harvesting of fiber on public lands in Ontario and Quebec is subject to licenses and review by the respective governmental authorities.

During 2018, the cost of wood fiber relating to our Pulp and Paper segment comprised approximately 20% of the total consolidated cost of sales.

Chemicals

We use various chemical compounds in our pulp and paper manufacturing operations that we purchase, primarily on a centralized basis, through contracts varying between one and ten years in length to ensure product availability. Most of the contracts have pricing that fluctuates based on prevailing market conditions. For pulp manufacturing, we use numerous chemicals including caustic soda, sodium chlorate, sulfuric acid, lime and peroxide. For paper manufacturing, we also use several chemical products including starch, precipitated calcium carbonate, optical brighteners, dyes and aluminum sulfate.

During 2018, the cost of chemicals relating to our Pulp and Paper segment comprised approximately 12% of the total consolidated cost of sales.

Energy

Our operations produce and consume substantial amounts of energy. Our primary energy sources include: biomass, natural gas and electricity. Approximately 72% of the total energy required to manufacture our products comes from renewable fuels such as bark and spent pulping liquor, generated as byproducts from our manufacturing processes. The remainder of the energy comes from smaller amounts of other fossil fuels and purchased steam procured under supply contracts. Under most of these contracts, suppliers are committed to provide quantities within pre-determined ranges that provide us with our needs for a particular type of fuel at a specific facility. Most of these contracts have pricing that fluctuate based on prevailing market conditions. Biomass and fossil fuels are consumed primarily to produce steam that is used in the manufacturing process and, to a lesser extent, to provide direct heat used in the chemical recovery process.

We own cogenerating assets at all of our integrated pulp and paper mills, as well as hydro assets at three locations: Espanola, Nekoosa and Rothschild. These generating assets produce approximately 72% of the electricity requirements of this business segment, with the balance supplied from local utilities. Electricity is primarily used to drive motors, pumps and other equipment, as well as provide lighting.

During 2018, net energy costs relating to our Pulp and Paper segment comprised approximately 5% of the total consolidated cost of sales.

Our Transportation

Transportation of raw materials, wood fiber, chemicals and pulp into our mills is mostly done by rail and trucks, although barges are used in certain circumstances. We rely strictly on third parties for the transportation of our pulp and paper products between our mills, converting operations, distribution centers and customers. Our paper products are shipped mostly by truck and logistics are managed centrally in collaboration with each location. Our pulp is either shipped by vessel, rail or truck depending on destination and customer preference. We work with all major railroads and approximately 350 trucking companies in the United States and Canada. Service agreements are typically negotiated on an annual basis. We pay diesel fuel surcharges which vary depending on the mode of transportation used, and the cost of diesel fuel.

During 2018, outbound transportation costs relating to our Pulp and Paper segment comprised approximately 11% of the total consolidated cost of sales.

Our Product Offering and Go-to-Market Strategy

Paper

Our uncoated freesheet papers are categorized into both communication papers and specialty and packaging papers. Communication papers are further categorized into business papers and commercial printing and publishing papers.

Our business papers include copy and electronic imaging papers, which are used with inkjet and laser printers, photocopiers and plain-paper fax machines, as well as computer papers, preprinted forms and digital papers. These products are primarily for office and home use. Business papers accounted for approximately 50% of our shipments of paper products in 2018.

Our commercial printing and publishing papers include uncoated freesheet papers, such as offset papers and opaques. These uncoated freesheet grades are used in sheet and roll fed offset presses across the spectrum of commercial printing end-uses, including digital printing. Our publishing papers include tradebook and lightweight uncoated papers used primarily in book publishing applications such as textbooks, dictionaries, catalogs, magazines, hard cover novels and financial documents. These products also include base papers that are converted into finished products, such as envelopes, tablets, business forms and data processing/computer forms. Commercial printing and publishing papers accounted for approximately 32% of our shipments of paper products in 2018.

Our specialty and packaging papers includes papers used for thermal printing, flexible packaging, food packaging, medical packaging, medical gowns and drapes, sandpaper backing, carbonless printing, labels and other papers used for coating and laminating applications. We also manufacture papers for industrial and specialty applications including carrier papers, treated papers, security papers and specialized printing and converting applications. These specialty and packaging papers accounted for approximately 18% of our shipments of paper products in 2018. These grades of papers require a certain amount of innovation and agility in the manufacturing system.

The chart below illustrates our main uncoated freesheet papers products and their applications:

Communication Papers					Specialty and Packaging Papers
Category	Business Papers		Commercial Printing and Publishing Papers		
Grade	Copy	Premium imaging	Offset	Opaques	Thermal papers
		Technology papers	Colors	Premium opaques	Food packaging
			Index	Lightweight	Bag stock
			Tag	Tradebook	Security papers
			Bristol		Imaging papers

					Label papers
					Medical disposables
Application	Photocopies	Presentations	Commercial printing	Stationery	Food & candy packaging
	Office documents	Reports	Direct mail	Brochures	Fast food takeout bag stock
	Presentations		Pamphlets	Annual reports	Check and security papers
			Brochures	Books	Surgical gowns
			Cards	Catalogs	
			Posters	Forms & Envelopes	

Our paper sales channels are aligned to efficiently bring a competitive and complete product offering to our varied customers. Our customer service personnel work closely with sales, marketing and production staff to provide service and support to merchants, converters, end-users, stationers, printers and retailers. We promote our products directly to end-users and others who influence paper purchasing decisions in order to enhance brand recognition and increase product demand. In addition, our sales representatives work closely with mill-based product development personnel and undertake joint marketing initiatives with customers in order to better understand their business needs and to support their future requirements.

We sell business papers primarily to paper stationers, merchants, office equipment manufacturers and retail outlets. We distribute uncoated commercial printing and publishing papers to end-users and commercial printers, mainly through paper merchants, as well as selling directly to converters. We sell our specialty and packaging papers mainly to converters, who apply a further production process such as coating, laminating, folding or waxing to our papers before selling them to a variety of specialized end-users.

The chart below illustrates our channels of distribution for our paper products:

Communication Papers							Specialty and Packaging Papers
Category	Business Papers			Commercial Printing and Publishing Papers			
Domtar sells to:	Retailers	Merchants	Office Equipment Manufacturers / Stationers	Merchants	Converters	End-Users	Converters
Customer sells to:	Printers / End-users	Printers / Retailers / End-users	Retailers / Stationers / End-users	Printers / Converters / End-users	Merchants / Retailers		End-users

Pulp

Our pulp products are comprised of softwood, fluff and hardwood kraft. These grades are sold to customers in over 40 countries worldwide. Our pulp is used in a variety of end products, such as diapers and personal hygiene products, bathroom and facial tissue, specialty and packaging papers, customers who make printing and writing grades, building products and electrical insulating papers.

We sell market pulp to customers in North America mainly through a North American sales force while sales to most overseas customers are made directly or through commission agents. We maintain pulp supplies at strategically located warehouses, which allow us to respond to customer orders on short notice.

Our Customers

Our ten largest customers represented approximately 44% of our Pulp and Paper segment sales or approximately 36% of our total sales in 2018. In 2018, Staples, a customer of our Pulp and Paper segment, represented approximately 10% of our total sales. The majority of our customers purchase products through individual purchase orders. In 2018, approximately 71% of our Pulp and Paper segment sales were in the United States, 11% were in Canada, and 18% were in other countries.

PERSONAL CARE

Our Operations

Our Personal Care business consists of the design, manufacturing, marketing and distribution of absorbent hygiene products, including adult incontinence and infant diaper products. We are one of the leading suppliers of adult incontinence products sold into North America and Europe, servicing institutional and consumer channels, marketed primarily under our Attends®, IncoPack®, Indasec® and Reassure® brands, in addition to our customers' brands.

We currently operate six manufacturing facilities, with each having the ability to produce multiple product categories. At our Jesup facility, we have research and development capabilities and production lines which manufacture high quality airlaid and ultrathin laminated absorbent cores and we also have research and development activities in our divisional headquarters in Raleigh, North Carolina. We operate in the United States and in Europe.

On November 1, 2018, we announced a margin improvement plan within our Personal Care segment. As part of this plan, we announced the permanent closure of our Waco, Texas, manufacturing and distribution facility, the relocation of certain of our manufacturing assets and a workforce reduction of 214 full time employees as well as certain temporary positions across the division. The Waco, Texas facility is expected to cease operations in the third quarter of 2019.

Our Industry Dynamics

Aging population

We compete in an industry with fundamental drivers for long-term growth. The worldwide aging population suggests that adult incontinence will become much more prevalent over the next several decades, as baby boomers enter their senior years and medical advances continue to extend the average lifespan. By the year 2030, approximately one billion people worldwide are estimated to be 65 years old or older, representing 12% of the projected total world population.

Increased healthcare spending

While we are expected to benefit from the overall increase in healthcare spending due to an aging population, the pressure to limit public spending on healthcare may impact overall consumption or the channels in which consumption occurs.

Infant products

We compete within the competitive store brand segment of infant diapers and training pants. Future demand growth based on birth rate and demographic trends is forecasted to be limited in North America and Europe. The importance of the category to key retailers is expected to remain strong given the purchasing power and strategic importance of the infant diaper shopper. Today, our business is focused on securing multiyear contracts with large retailers that control the majority of volume, leading to intense competition with other manufacturers in the industry.

We believe that our product assortment provides our customers with the complete bundle of products at a scale required to meet their national distribution requirements.

Our Raw Materials

The primary raw materials used in our manufacturing process are fluff pulp, nonwovens and super absorbent polymers. A significant portion of the fluff pulp used in our Personal Care business is supplied internally from our Pulp and Paper business. The majority of our nonwoven and super absorbent polymers are purchased centrally based on multiyear contracts with pricing that fluctuates with market conditions. Other raw materials used in our manufacturing process include polypropylene film, elastics and adhesives which are also purchased with multiyear contracts.

Our Product Offering and Go-to-Market Strategy

Our products, which include branded and private label briefs, protective underwear, underpads, pads and washcloths, as well as baby diapers, youth pants and infant training pants, are available in a variety of sizes, differing performance levels and product attributes. Our broad product portfolio covers most price points across each category.

We serve the healthcare, retail and direct-to-consumer channels. Through the utilization of our flexible production platform, manufacturing expertise and efficient supply chain management, we believe that we are able to provide a complete and high-quality line of products to customers across all channels, under our own brands or those of our customers. We maintain a direct sales organization in the United States and certain European countries.

Our Product Development

We currently offer a comprehensive, full suite of products, and we continue to focus on product development to improve products for our customers. We continue to explore materials, designs and processes that will allow us to manufacture products that absorb wetness more quickly, reduce skin dryness and improve containment.

OUR STRATEGIC INITIATIVES AND FINANCIAL PRIORITIES

As a leading fiber-based technology company, Domtar is focused on driving innovation, enhancing our operating platforms, and delivering high quality products. To further bolster our position and drive enhanced value for our stockholders, Domtar is focused on four key business objectives: (1) driving value in our Pulp and Paper business through strategic investment; (2) building on our core competencies in wood fiber to diversify and expand Domtar's footprint in growth markets and industries; (3) maintaining a balanced and disciplined approach to capital allocation that allows for investments in growth opportunities and rewards stockholders with capital returns; and (4) operating with a focus on environmental responsibility and sustainability. We are confident that the continued focus on these objectives will bolster the competitive position of our business and drive value for our stakeholders, including stockholders, customers and employees.

Driving value in the Pulp and Paper business. Domtar's Pulp and Paper business remains an important part of our growth plan, and we have strategies and operating priorities designed to maximize the value of the business. Our key priorities include: increasing productivity in our pulp business, pursuing new sources of paper consumption, pursuing asset repurposing opportunities and operating an optimal portfolio of strategic assets. We believe that execution on these priorities will enable Domtar to expand into complementary growth areas and protect its market position in Pulp and Paper.

Expanding into areas of growth and leveraging our fiber expertise. We are focused on optimizing and expanding our operations in markets with positive demand dynamics through investments for organic growth, the repurposing of assets and strategic acquisitions. Domtar has a history of proactively adapting to changing market conditions, and today, we are repositioning the Company towards areas of growth. We are well positioned to capitalize on new opportunities in the wood fiber market. The Company already has the financial resources, infrastructure, raw materials, technologies and expertise necessary to deliver new products. We believe that we have built a strong foundation for diversification and continue to make important, but disciplined, progress.

Maintaining a balanced and disciplined approach to capital allocation that allows for investments in growth opportunities and rewards stockholders with capital returns. We believe in a balanced and disciplined approach to capital allocation, and we are committed to deploying capital only to the areas that will achieve the best possible return for our stockholders. Domtar's free cash flow allows us to invest in growth opportunities and maintain a strong and flexible financial position for operating and strategic initiatives, while still returning capital to our stockholders. To continue generating free cash flow, we are focused on assigning our capital expenditures effectively and minimizing working capital requirements by reducing discretionary spending, reviewing procurement costs and pursuing the balance of production and inventory control.

Operating responsibly on behalf of all of Domtar's stakeholders. We try to make a positive difference every day by pursuing sustainable growth, valuing relationships, and responsibly managing our resources. We aim to care for our customers, end-users and stakeholders in the communities where we operate, all seeking assurances that resources are managed in a sustainable manner. We strive to provide these assurances by certifying our distribution and manufacturing operations and measuring our performance against internationally recognized benchmarks. Domtar is committed to the responsible use of forest resources across our operations, and we are enrolled in programs and initiatives to encourage landowners to pursue certification to improve their market access and increase their revenue opportunities. We believe that each of these initiatives also creates value for our stockholders and is part of our larger business strategy and commitment to environmental sustainability.

OUR COMPETITION

The markets in which our businesses operate are highly competitive with well-established domestic and foreign manufacturers.

In the paper business, our paper production does not rely on proprietary processes or formulas, except in highly specialized papers or customized products. In uncoated freesheet, we compete primarily on the basis of product quality, breadth of offering, service solutions and competitively priced paper products, which include an extensive offering of high quality Forest Stewardship Council ("FSC")-certified paper products. While we have a leading position in the North American uncoated freesheet market, we also compete with other paper grades, including coated freesheet, and with electronic transmission and document storage alternatives. As the use of these alternative products continues to grow, we continue to see a decrease in the overall demand for paper products. All of our pulp and paper manufacturing facilities are located in the United States or in Canada where we sell approximately 82% of our products. Domtar is the largest of the five manufacturers of uncoated freesheet papers in North America that represent approximately 80% of the total production capacity. On a global basis, there are hundreds of manufacturers that produce and sell uncoated freesheet paper. The level of competitive pressures from foreign producers in the North American market is highly dependent upon exchange rates, particularly the rate between the U.S. dollar and the Euro as well as the U.S. dollar and the Brazilian real.

The market pulp we sell is fluff, softwood or hardwood pulp. The pulp market is highly fragmented with many manufacturers competing worldwide. Competition is primarily on the basis of access to low-cost wood fiber, product quality and competitively priced pulp products. The fluff pulp we sell is used in absorbent products, incontinence products, diapers and feminine hygiene products. The softwood and hardwood pulp we sell is primarily slow growth northern bleached softwood and hardwood kraft, and we produce specialty engineered pulp grades with a pre-determined mix of wood species. Our softwood and hardwood pulps are sold to customers who make a variety of products for specialty paper, packaging, tissue and industrial applications, and customers who make printing and writing grades. We also seek product differentiation through the certification of our pulp mills to the FSC chain-of-custody standard and the procurement of FSC-certified virgin fiber. All of our market pulp production capacity is located in the United States or in Canada, and we sell approximately 58% of our pulp to other countries.

For the adult incontinence business, competition is primarily faced across four major product categories: protective underwear, pads, briefs and underpads, with customers served through the healthcare, retail (mass retailers, dollar stores, supermarkets, warehouse clubs), and direct to consumer channels. The retail channel in Europe is more fragmented than in North America, with a mix of larger chains and smaller players. Approximately 74% of institutional and homecare expenditures are reimbursed by governments in Western Europe.

For the infant diaper business, competition is primarily across three major product categories: diapers, training pants and youth pants with customers served through the retail (mass retailers, dollar stores, supermarkets, warehouse clubs) and direct to consumer channels. In North America, branded labels represent the majority of the infant market with the top two manufacturers supplying a significant portion of the branded demand. The remaining supply is represented by private label, and is split among the competition. In Europe, the top manufacturer supplies approximately 50% of the demand with branded labels, and the remainder is represented by private label. Products are marketed in multiple channels: mass retailers, dollar stores, supermarkets, warehouse clubs, internet and home health care.

In both the adult incontinence and infant diaper businesses, the principal methods and elements of competition remain brand recognition and loyalty, product innovation, quality and performance, price and marketing and distribution capabilities. Growing competitive market pressures in the healthcare and retail markets in recent years, including the entry of new competitors in the private label category, excess industry capacity and the pressure to limit public healthcare spending are resulting in lower than previously anticipated sales and operating margins.

OUR EMPLOYEES

We have approximately 10,000 employees, of which approximately 60% are employed in the United States, 28% in Canada and 12% in Europe. Approximately 44% of our employees are covered by collective bargaining agreements, generally on a facility-by-facility basis. Certain agreements will expire in 2019 and others will expire between 2020 and 2022.

OUR APPROACH TO SUSTAINABILITY

Domtar aims to deliver value to our customers, employees, shareholders and communities by viewing our business decisions within the larger context of sustainability. We take a long-term view on managing natural resources for the future. We strive to minimize waste and encourage recycling. We aim to have the highest standards for ethical conduct, for caring about the health and safety of each other, and for maintaining the environmental quality in the communities where we live and work. We value the partnerships we have formed with non-governmental organizations and believe they make us a better company. We focus on agility to respond to new opportunities, and we are committed to turning innovation into value creation. By embracing sustainability as our operating philosophy, we seek to internalize the fact that the choices we have and the impact of the decisions we make on our stakeholders are all interconnected. We believe that our business and the people and communities who depend on us are better served as we weave this focus on sustainability into the things we do.

Domtar executes this commitment to sustainability at every level and every location across the company. With the support of the Board of Directors, our Management Committee empowers senior managers from manufacturing, technology, finance, sales and marketing and corporate staff functions to regularly come together and establish key sustainability performance metrics, and to routinely assess and report on progress. We have a vice-president position to help lead this effort, allowing the company's organizational structure to better reflect the priority the company places on sustainable performance. We believe that weaving sustainability into our business better positions Domtar for the future.

OUR ENVIRONMENTAL COMPLIANCE

Our business is subject to a wide range of general and industry-specific laws and regulations in the United States and other countries where we have operations, relating to the protection of the environment, including those governing wood harvesting, air emissions, climate change, waste water discharges, storage, management and disposal of hazardous substances and wastes, contaminated sites, landfill operation and closure obligations and health and safety matters. Compliance with these laws and regulations is a significant factor in the operation of our business. We may encounter situations in which our operations fail to maintain full compliance with applicable environmental requirements, possibly leading to civil or criminal fines, penalties or enforcement actions, including those that could result in governmental or judicial orders that stop or interrupt our operations or require us to take corrective measures at substantial costs, such as the installation of additional pollution control equipment or other remedial actions.

Compliance with environmental laws and regulations involves capital expenditures as well as additional operating costs. Additional information regarding environmental matters is included in Item 8, Financial Statements and Supplementary Data under Note 21 "Commitments and Contingencies" and in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations under the section of Critical accounting estimates and policies, caption "Environmental matters and asset retirement obligations".

OUR INTELLECTUAL PROPERTY

Many of our brand name products are protected by registered trademarks. Our key trademarks include Cougar®, Lynx® Opaque Ultra, Husky® Opaque Offset, First Choice®, EarthChoice®, Attends®, NovaThin®, NovaZorb®, IncoPack®, Indasec®, Reassure® and Ariva®. These brand names and trademarks are important to our business. Our numerous trademarks have been registered in the United States and/or in other countries where our products are sold. The current registrations of these trademarks are effective for various periods of time. These trademarks may be renewed periodically, provided that we, as the registered owner, and/or licensee comply with all applicable renewal requirements, including the continued use of the trademarks in connection with similar goods.

We own U.S. and foreign patents and have several pending patent applications. Our management regards these patents and patent applications as important but does not consider any single patent or group of patents to be materially important to our business as a whole.

OUR EXECUTIVE OFFICERS ("MANAGEMENT COMMITTEE")

Name	Age	Position and Business Experience
John D. Williams	64	President and Chief Executive Officer of the Company since January 2009. He is also a member of the Board of Directors. Previously, Mr. Williams served as President of SCA Packaging Europe between 2005 and 2008. Prior to assuming his leadership position with SCA Packaging Europe, Mr. Williams held increasingly senior management and operational roles in the packaging business and related industries. Mr. Williams is Lead Independent Director of the Board of Directors of Owens Corning, the Chair of the advisory board of the Stern Center for Sustainable Business at New York University and the Non-Executive Chairman of Form Technologies, Inc., a privately-held leading global group of precision component manufacturers based in Charlotte, North Carolina.
Daniel Buron	55	Senior Vice-President and Chief Financial Officer of the Company since March 2007. Mr. Buron was previously Senior Vice-President and Chief Financial Officer of Domtar Inc. since May 2004. He joined Domtar Inc. in 1999. Prior to May 2004, he was Vice-President, Finance, Pulp and Paper sales division and, prior to September 2002, he was Vice-President and Controller. He has over 30 years of experience in finance. Mr. Buron is a Director of the McGill University Health Centre Foundation.
Michael D. Garcia	54	President, Pulp and Paper Division of the Company. Mr. Garcia joined Domtar in 2014. Prior to joining the Company, he was the chief executive officer at EVRAZ Highveld Steel & Vanadium Co., South Africa's second largest steel producer. Mr. Garcia has more than 25 years of international management experience in paper, steel, and aluminum manufacturing and marketing. He has broad global experience, including executive assignments in Asia and Africa. Mr. Garcia is a Director of the Federal Reserve Bank of Richmond, Charlotte Branch, and of the USO of North Carolina.
Michael Fagan	57	President, Personal Care Division of the Company. Mr. Fagan joined Domtar in 2011, following the acquisition of Attends Healthcare Products, Inc. Mr. Fagan has been with Attends since 1999, when he was hired as Senior Vice-President of Sales and Marketing. He was promoted to President and CEO in 2006. Prior to joining Attends, Mr. Fagan held a variety of sales development roles with Procter & Gamble, the previous owners of the Attends line of products.
Zygmunt Jablonski	65	Senior Vice-President and Chief Legal and Administrative Officer of the Company. Mr. Jablonski joined Domtar in 2008, after serving in various in-house counsel positions for major manufacturing and distribution companies in the paper industry for 13 years. From 1985 to 1994, he practiced law in Washington, DC.
Patrick Loulou	50	Senior Vice-President, Corporate Development since he joined the Company in March 2007. Previously, he held a number of positions in the telecommunications sector as well as in management consulting. His over 20 year career has spanned a number of areas and functions such as corporate strategy, M&A, operations, and business development.

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements relating to trends in, or representing management's beliefs about, Domtar Corporation's future growth, results of operations, performance and business prospects and opportunities. These forward-looking statements are generally denoted by the use of words such as "anticipate," "believe," "expect," "intend," "aim," "target," "plan," "continue," "estimate," "project," "may," "will," "should" a expressions. These statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements are necessarily based upon a number of estimates and assumptions that, while considered reasonable by management, are inherently subject to known and unknown risks and uncertainties and other factors that could cause actual results to differ materially from historical results or those anticipated. Accordingly, no assurances can be given that any of the events anticipated by the forward-looking statements will occur, or if any occur, what effect they will have on Domtar Corporation's results of operations or financial condition. These factors include, but are not limited to:

- continued decline in usage of fine paper products in our core North American market;
- our ability to implement our business diversification initiatives, including repurposing of assets and strategic acquisitions;
- product selling prices;
- raw material prices, including wood fiber, chemical and energy;
- conditions in the global capital and credit markets, and the economy generally, particularly in the U.S., Canada and Europe;
- performance of Domtar Corporation's manufacturing operations, including unexpected maintenance requirements;
- the level of competition from domestic and foreign producers;
- cyberattack or other security breaches;
- the effect of, or change in, forestry, land use, environmental and other governmental regulations and accounting regulations;
- the effect of weather and the risk of loss from fires, floods, windstorms, hurricanes and other natural disasters;
- transportation costs;
- the loss of current customers or the inability to obtain new customers;
- legal proceedings;
- changes in asset valuations, including impairment of property, plant and equipment, inventory, accounts receivable or other assets for impairment or other reasons;
- changes in currency exchange rates, particularly the relative value of the U.S. dollar to the Canadian dollar and European currencies;
- the effect of timing of retirements and changes in the market price of Domtar Corporation's common stock on charges for stock-based compensation;
- performance of pension fund investments and related derivatives, if any; and
- the other factors described under "Risk Factors," Item 1A.

You are cautioned not to unduly rely on such forward-looking statements, which speak only as of the date made, when evaluating the information presented in this Annual Report on Form 10-K. Unless specifically required by law, Domtar Corporation disclaims any obligation to update or revise these forward-looking statements to reflect new events or circumstances.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below in addition to the other information presented in this Annual Report on Form 10-K.

Conditions in the global political and economic environment, including the global capital and credit markets, can adversely affect the Company's business, results of operations and financial position.

A significant or prolonged downturn in the general economic environment may affect the Company's sales and profitability. The Company has exposure to counterparties with which it routinely executes transactions. Such counterparties include commercial banks, insurance companies and other financial institutions, some of which may be exposed to bankruptcy or liquidity risks. A bankruptcy or illiquidity event by one of its significant counterparties may materially and adversely affect the Company's access to capital, future business and results of operations. In addition, the Company's customers and suppliers may be adversely affected by severe economic conditions. This could result in reduced demand for its products or its inability to obtain necessary supplies at reasonable costs, or at all.

The Company may be negatively impacted by political issues or crisis in individual countries or regions, including sovereign risk related to a default by or deterioration in the credit worthiness of local governments. Any of these effects, and others the Company cannot anticipate, may have a negative effect and may adversely affect the Company's business.

Certain countries in Europe provide medicare coverage for adult incontinence products. The governments of these countries may decide to no longer reimburse part or all of the costs of adult incontinence products, and this may have a negative impact on the Company's operating results in the future.

The Company faces intense competition in its markets, and the failure to compete effectively could have a material adverse effect on its business and results of operations.

The Company competes with U.S., Canadian and European producers and, for many of its product lines with global producers, some of which may have greater financial resources and lower production costs than the Company. The principal basis for competition is selling price. The Company's ability to maintain satisfactory margins depends largely on its ability to control its costs. Our industries also are particularly sensitive to other factors including innovation, design, quality and service, with varying emphasis on these factors depending on the product line. The Company cannot provide assurance that it will compete effectively and maintain current levels of sales and profitability. If the Company cannot compete effectively, such failure could have a material adverse effect on its business and results of operations.

Failure to successfully implement the Company's business diversification initiatives could have a material adverse effect on its business, results of operations and financial position.

The Company is pursuing strategic initiatives that management considers important to our long-term success. The intent of these initiatives is to help grow the business and counteract the secular decline in our North American paper business. These initiatives may involve organic growth, select joint ventures and strategic acquisitions. The success of these initiatives will depend on, among other things, our ability to identify potential strategic initiatives, understand the key trends and principal drivers affecting those businesses and to execute the initiatives in a cost effective manner. There are significant risks involved with the execution of such initiatives, including significant business, economic and competitive uncertainties, many of which are outside the Company's control.

In addition, in the past we have converted paper mills to fluff pulp production facilities. If circumstances warrant, in the future we may again convert paper mills to produce pulp or other products. Conversions can be capital intensive and can involve the shutdown of a facility for an extended period of time, followed by an extended ramp-up and customer certification process. In addition, the success of a conversion depends upon demand over time for the new product relative to the previously produced paper products, as well as costs and other factors, and there can be no assurance that a conversion will be as successful as expected.

Strategic acquisitions may expose the Company to additional risks. The Company may have to compete for acquisition targets and any acquisition it makes may fail to accomplish our strategic objectives or may not perform as expected. In addition, the costs of integrating an acquired business may exceed our estimates and may require significant time and attention from senior management. Accordingly, the Company cannot predict whether it will succeed in implementing these strategic initiatives. If it fails to successfully diversify our business, it may have a material adverse effect on the Company’s competitive position, financial condition and operating results.

The Company’s paper products are vulnerable to long-term declines in demand due to competing technologies or materials.

The Company’s paper business competes with electronic transmission and document storage alternatives, as well as with paper grades it does not produce, such as uncoated groundwood. As a result of such competition, the Company is experiencing ongoing decreasing demand for most of its existing paper products. As the use of these alternatives grows, demand for paper products is likely to decline further. Declines in demand for our paper products may adversely affect the Company’s business, results of operations and financial position.

The pulp and paper industry is highly cyclical. Fluctuations in the prices of and the demand for the Company’s pulp and paper products could result in lower sales volumes and smaller profit margins.

The pulp and paper industry is highly cyclical. Historically, economic and market shifts, fluctuations in capacity and changes in foreign currency exchange rates have created cyclical changes in prices, sales volume and margins for the Company’s pulp and paper products. The length and magnitude of industry cycles have varied over time and by product, but generally reflect changes in macroeconomic conditions and levels of industry capacity. Most of the Company’s paper products are commodities that are widely available from other producers. Because commodity products have few distinguishing qualities from producer to producer, competition for these products is based primarily on price, which is determined by supply relative to demand.

The overall levels of demand for the pulp and paper products that the Company manufactures and distributes, and consequently its sales and profitability, reflect fluctuations in levels of end-user demand, which depend in part on general macroeconomic conditions in North America and worldwide, the continuation of the current level of service and cost of postal services, as well as competition from electronic substitution. See “Conditions in the global political and economic environment, including the global capital and credit markets, can adversely affect the Company’s business, results of operations and financial position” and “The Company’s paper products are vulnerable to long-term declines in demand due to competing technologies or materials”.

Industry supply of pulp and paper products is also subject to fluctuation, as changing industry conditions can influence producers to idle or permanently close individual machines or entire mills. Such closures can result in significant cash and/or non-cash charges. In addition, to avoid substantial cash costs in connection with idling or closing a mill, some producers will choose to continue to operate at a loss, sometimes even a cash loss, which could prolong weak pricing environments due to oversupply. Oversupply can also result from producers introducing new capacity in response to favorable pricing trends.

Industry supply of pulp and paper products is also influenced by overseas production capacity, which has grown in recent years and is expected to continue to grow.

As a result, prices for all of the Company’s pulp and paper products are driven by many factors outside of its control, and the Company has little influence over the timing and extent of price changes, which are often volatile. Because market conditions beyond the Company’s control determine the prices for its commodity products, the price for any one or more of these products may fall below its cash production costs, requiring the Company to either incur cash losses on product sales or cease production at one or more of its pulp and paper manufacturing facilities. The Company continuously evaluates potential adjustments to its production capacity, which may include additional closures of machines or entire mills, and the Company could recognize significant cash and/or non-cash charges relating to any such closures in future periods. Refer to Item 8, Financial Statements and Supplementary Data under Note 15 “Closure and restructuring costs and liability” for more details. Therefore, the Company’s profitability with respect to these products depends on managing its cost structure, particularly wood fiber, chemical, transportation and energy costs, which represent the largest components of its operating costs and can fluctuate based upon factors beyond its control. If the prices or demand for its pulp and paper products decline, or if its wood fiber, chemical, transportation or energy costs increase, or both, this could adversely affect the Company's results of operations and financial position.

The Company is affected by changes in currency exchange rates.

The Company has manufacturing operations in the United States, Canada, Sweden and Spain. As a result, it is exposed to movements in foreign currency exchange rates in Canada and Europe. Moreover, certain assets and liabilities are denominated in currencies other than the U.S. dollar and are exposed to foreign currency movements. As a result, the Company's earnings are affected by increases or decreases in the value of the Canadian dollar and of other European currencies relative to the U.S. dollar. The Company's European subsidiaries are exposed to movements in foreign currency exchange rates on transactions denominated in a different currency than their Euro functional currency. Additionally, there has been, and may continue to be, volatility in currency exchange rates. The Company's risk management policy allows hedging a significant portion of its exposure to fluctuations in foreign currency exchange rates for periods up to three years. The Company may use foreign exchange derivative instruments to mitigate its exposure to fluctuations in foreign currency exchange rates. There can be no assurance that the Company will be protected against substantial foreign currency fluctuations. Currency exchange rates could adversely affect the Company’s results of operations and financial position.

The Company relies heavily on a small number of significant customers, including one customer that represented approximately 10% of the Company’s sales in 2018. A significant change in customer relationships or in customer demand for our products could materially adversely affect the Company’s business, financial condition or results of operations.

The Company heavily relies on a small number of significant customers. The Company’s largest customer, Staples, represented approximately 10% of the Company’s sales in 2018. A significant reduction in sales to any of the Company’s key customers could materially adversely affect the Company’s business, financial condition or results of operations, could result from such customers further diversifying their product sourcing, or experiencing financial difficulty or consolidating with each other.

The Company’s operations require substantial capital, and it may not have adequate capital resources to provide for all of its capital requirements.

The Company’s businesses are capital intensive and require ongoing capital expenditures in order to maintain its equipment, increase its operating efficiency and comply with environmental laws. In 2018, the Company’s total capital expenditures were $195 million.

If the Company’s available cash resources and cash generated from operations are not sufficient to fund its operating needs and capital expenditures, the Company would have to obtain additional funds from borrowings or other available sources or reduce or delay its capital expenditures. The Company may not be able to obtain additional funds on favorable terms, or at all. In addition, the Company’s debt service obligations will reduce its available cash flows. If the Company cannot maintain or upgrade its equipment as it requires or allocate funds to ensure environmental compliance, it could be required to curtail or cease some of its manufacturing operations, or it may become unable to manufacture products that compete effectively in one or more of its product lines.

The Company and its subsidiaries may incur substantially more debt. This could increase risks associated with its leverage.

The Company and its subsidiaries may incur substantial additional indebtedness in the future. Although the revolving credit facility contains restrictions on the incurrence of additional indebtedness, including secured indebtedness, these restrictions are subject to a number of qualifications and exceptions, and additional indebtedness incurred in compliance with these restrictions could be substantial. Refer to Item 8, Financial Statements and Supplementary Data under Note 18 “Long-term debt” for more details.

The Company’s ability to generate the significant amount of cash needed to pay interest and principal on the Company’s unsecured long-term notes and service its other debt and financial obligations and its ability to refinance all or a portion of its indebtedness or obtain additional financing depends on many factors beyond the Company’s control.

In 2018, the Company paid approximately $358 million in interest and principal payments. The Company’s ability to make payments on and refinance its debt, including the Company’s unsecured long-term notes and amounts borrowed under its revolving credit facility and term loan, if any, and other financial obligations and to fund its operations will depend on its ability to generate substantial operating cash flow. The Company’s cash flow generation will depend on its future performance, which will be subject to prevailing economic conditions and to financial, business and other factors, many of which are beyond its control.

The Company's business may not generate sufficient cash flow from operations and future borrowings may not be available to the Company under its revolving credit facility or otherwise in amounts sufficient to enable the Company to service its indebtedness, including the Company's unsecured long-term notes, and borrowings, if any, under its revolving credit facility and securitization or to fund its other liquidity needs. If the Company cannot service its debt, the Company will have to take actions such as reducing or delaying capital investments, selling assets, restructuring or refinancing its debt or seek additional equity capital. Any of these remedies may not be executed on commercially reasonable terms, or at all, and may impede the implementation of its business strategy. Furthermore, the revolving credit facility may restrict the Company from adopting any of these alternatives. Because of these and other factors that may be beyond its control, the Company may be unable to service its indebtedness.

The Company could incur substantial costs as a result of compliance with, violations of or liabilities under applicable environmental laws and regulations. It could also incur costs as a result of asbestos-related personal injury litigation.

The Company is subject to a wide range of general and industry-specific laws and regulations in the United States and other countries where we have operations, relating to the protection of the environment and natural resources, including those governing air emissions, greenhouse gases and climate change, wastewater discharges, harvesting, silvicultural activities, storage, management and disposal of hazardous substances and wastes, the cleanup of contaminated sites, landfill operation and closure obligations, forestry operations and endangered species habitat, and health and safety matters. In particular, the pulp and paper industry in the United States is subject to the United States Environmental Protection Agency's ("EPA") Cluster Rules.

The Company has incurred, and expects that it will continue to incur, significant capital, operating and other expenditures complying with applicable environmental laws and regulations as a result of remedial obligations. The Company incurred $68 million of operating expenses and $8 million of capital expenditures in connection with environmental compliance and remediation in 2018. As of December 31, 2018, the Company had a provision of $37 million for environmental expenditures, including certain asset retirement obligations (such as for landfill capping).

The Company could also incur substantial costs, such as civil or criminal fines, sanctions and enforcement actions (including orders limiting its operations or requiring corrective measures, installation of pollution control equipment or other remedial actions), cleanup and closure costs, and third-party claims for property damage and personal injury as a result of violations of, or liabilities under, environmental laws and regulations. The Company's ongoing efforts to identify potential environmental concerns that may be associated with its past and present properties may lead to future environmental investigations. Those efforts may result in the determination of additional environmental costs and liabilities which cannot be reasonably estimated at this time.

As the owner and operator of real estate, the Company may be liable under environmental laws for cleanup, closure and other damages resulting from the presence and release of hazardous substances, including asbestos, on or from its properties or operations, including properties that it no longer owns. The amount and timing of environmental expenditures is difficult to predict, and, in some cases, the Company's liability may be imposed without regard to contribution or to whether it knew of, or caused, the release of hazardous substances and may exceed forecasted amounts or the value of the property itself. The discovery of additional contamination or the imposition of additional cleanup obligations at the Company's or third-party sites may result in significant additional costs. Any material liability the Company incurs could adversely impact its financial condition or preclude it from making capital expenditures that would otherwise benefit its business.

In addition, the Company may be subject to asbestos-related personal injury litigation arising out of exposure to asbestos on or from its properties or operations, and may incur substantial costs as a result of any defense, settlement, or adverse judgment in such litigation. The Company may not have access to insurance proceeds to cover costs associated with asbestos-related personal injury litigation.

Enactment of new environmental laws or regulations or changes in existing laws or regulations (such as changes in climate change regulation), or interpretation thereof, might require significant expenditures. For additional information, refer to Item 8, Financial Statements and Supplementary Data under Note 21 "Commitments and Contingencies". The Company may be unable to generate funds or other sources of liquidity and capital to fund environmental liabilities or expenditures.

Failure to comply with applicable laws and regulations could have a material adverse effect on our business, financial results or condition.

In addition to environmental laws, the Company's business and operations are subject to a broad range of other laws and regulations in the United States and Canada as well as other jurisdictions in which the Company operates, including antitrust and competition laws, occupational health and safety laws, healthcare reimbursement laws, such as Medicare and Medicaid, and employment laws. Many of these laws and regulations are complex and subject to evolving and differing interpretation. If the Company is determined to have violated any such laws or regulations, whether inadvertently or willfully, it may be subject to civil and criminal penalties, including substantial fines, loss of authorizations to participate in or exclusion from government programs, claims for damages by third parties or fines or monetary penalties which may have a material adverse effect on the Company's financial position, results of operations or cash flows. For additional information, refer to Item 8, Financial Statements and Supplementary Data under Note 21 "Commitments and Contingencies" under the caption "Spanish Competition Investigation".

The Company's financial results could be affected by changes in U.S. and foreign tax laws or in the mix of our U.S. and foreign earnings, as well as adjustments to our estimates of uncertain tax issues or results from audits by U.S. or foreign tax authorities.

The Company is subject to U.S. and foreign tax laws and regulations. Tax laws, regulations, and administrative practices in various jurisdictions may be subject to significant change, with or without notice, due to economic, political and other conditions, and significant judgment is required in evaluating and estimating our provision and accruals for these taxes. Recently, international tax norms governing each country's jurisdiction to tax cross-border international trade have evolved partly due to the Base Erosion and Profit Shifting project led by the Organization for Economic Cooperation and Development and supported by the G20. Changes in these laws and regulations, or any change in the position of tax authorities regarding their application, administration or interpretation could adversely affect the Company's financial results. In addition, a number of countries are actively pursuing changes to their tax laws applicable to multinational corporations, such as the U.S. Tax Cuts and Jobs Acts ("U.S. Tax Reform"), enacted in 2017. Finally, foreign governments may enact tax laws in response to the U.S. Tax Reform that could result in further changes to global taxation and materially impact the Company's financial results.

The U.S. Tax Reform significantly changes how the U.S. taxes corporations. The U.S. Tax Reform requires complex computations to be performed that were not previously required under U.S. tax law, significant judgments to be made in interpretation of the provision of the U.S Tax Reform and significant estimates in calculations, and the preparation and analysis of information not previously relevant or regularly produced. The U.S. Treasury Department, the IRS, and other standard-setting bodies could interpret or issue guidance on how provisions of the U.S. Tax Reform will be applied or otherwise administered that is different from the Company's interpretation.

The Company's effective tax rates could be affected by changes in the mix of earnings in countries with differing statutory tax rates or changes in the valuation of deferred tax assets and liabilities. The Company is also subject to the examination of its tax returns and other matters by tax authorities and governmental bodies. The Company regularly assesses the likelihood of an adverse outcome resulting from these examinations to determine the adequacy of its provision for taxes and as of December 31, 2018, has a reserve for liabilities relating to uncertain tax positions of $32 million. Taxing authorities may disagree with the positions the Company has taken regarding the tax treatment or characterization of its transactions. If any tax authorities were successful in challenging the tax treatment or characterization of any of the Company's transactions, it could also adversely affect its financial results.

The Company's Pulp and Paper business may have difficulty obtaining wood fiber at favorable prices, or at all.

Wood fiber is the principal raw material used by the Company's Pulp and Paper business, comprising approximately 20% of the consolidated cost of sales in 2018. Wood fiber is a commodity, and prices historically have been impacted by a variety of factors. The primary source for wood fiber is timber. Environmental litigation and regulatory developments, alternative use for energy production and reduction in harvesting related to the housing market, have caused, and may cause in the future, significant reductions in the amount of timber available for commercial harvest in the United States and Canada. In addition, future domestic or foreign legislation and litigation concerning the use of timberlands, the protection of endangered species, the promotion of forest health and the response to and prevention of catastrophic wildfires could also affect timber supplies. Availability of harvested timber may be further limited by adverse weather, fire, insect infestation, disease, ice storms, wind storms, flooding and other natural and man-made causes, thereby reducing supply and increasing prices. Wood fiber pricing is subject to regional market influences, and the Company's cost of wood fiber may increase in particular regions due to market shifts in those regions. Any sustained increase in wood fiber prices would increase the Company's operating costs, and the Company may be unable to increase prices for its products in response to increased wood fiber costs due to additional factors affecting the demand or supply of these products.

The Company currently meets its wood fiber requirements by purchasing wood fiber from third parties and by harvesting timber pursuant to its forest licenses and forest management agreements. If the Company's cutting rights, pursuant to its forest licenses or forest management agreements are reduced, or any third-party supplier of wood fiber stops selling or is unable to sell wood fiber to the Company, its financial condition or results of operations could be materially and adversely affected.

An increase in the cost of the Company's purchased energy or other raw materials would lead to higher manufacturing costs, thereby reducing its margins.

The Company's operations consume substantial amounts of energy such as electricity, natural gas, fuel oil, coal and hog fuel. Energy prices, particularly for electricity, natural gas and fuel oil, have been volatile in recent years. As a result, fluctuations in energy prices will impact the Company’s manufacturing costs and contribute to earnings volatility. While the Company purchases substantial portions of its energy under supply contracts, most of these contracts are based on market pricing.

Other raw materials the Company uses include various chemical compounds, such as precipitated calcium carbonate, sodium chlorate, sulfuric acid, dyes, peroxide, methanol and aluminum sulfate, super absorbent polymers and nonwovens. The costs of these other raw materials have been volatile historically, and they are influenced by capacity utilization, energy prices and other factors beyond the Company’s control.

Due to the commodity nature of the Company’s products, the relationship between supply and demand for these products, rather than changes in the cost of raw materials or purchased energy, will determine the Company’s ability to increase prices. Consequently, the Company may be unable to pass on increases in its operating costs to its customers. Any sustained increase in raw material or energy prices without any corresponding increase in product pricing would reduce the Company’s operating margins and may have a material adverse effect on its business and results of operations.

The Company depends on third parties for transportation services.

The Company relies primarily on third parties for transportation of the products it manufactures and/or distributes, as well as delivery of its raw materials. In particular, a significant portion of the goods it manufactures and raw materials it uses are transported by railroad or trucks, which are highly regulated. If any of its third-party transportation providers were to fail to deliver the goods that the Company manufactures or distributes in a timely manner, the Company may be unable to sell those products at full value, or at all. Similarly, if any of these providers were to fail to deliver raw materials to the Company in a timely manner, it may be unable to manufacture its products in response to customer demand. In addition, if any of these third parties were to cease operations or cease doing business with the Company, it may be unable to replace them at reasonable cost. Any failure of a third-party transportation provider to deliver raw materials or finished products in a timely manner could harm the Company's reputation, negatively impact its customer relationships and may have a material adverse effect on its financial condition and results of operations.

The Company could experience disruptions in operations and/or increased labor costs due to labor disputes or restructuring activities.

Employees at 17 of the Company's facilities, representing approximately half of the Company's employees, are represented by unions through collective bargaining agreements generally negotiated on a facility-by-facility basis. In the future, the Company may not be able to negotiate acceptable new collective bargaining agreements, which could result in strikes or work stoppages or other labor disputes by affected workers. Renewal of collective bargaining agreements could also result in higher wages or benefits paid to union members. In addition, labor organizing activities could occur at any of the Company's facilities. Therefore, the Company could experience a disruption of its operations or higher ongoing labor costs, which could have a material adverse effect on its business and results of operations.

The Company continues to evaluate potential adjustments to its production capacity, which may include additional closures of machines or entire mills, and the Company could recognize significant cash and/or non-cash charges relating to any such closures in the future.

A material disruption at one or more of the Company's manufacturing facilities could prevent it from meeting customer demand, reduce its sales and/or negatively impact its results of operations.

Any of the Company's manufacturing facilities, or any of its machines within an otherwise operational facility, could cease operations unexpectedly due to a number of events, including:

- unscheduled maintenance outages;
- prolonged power failures;
- equipment failure;
- chemical spill or release;
- malfunction of a boiler;
- the effect of a drought or reduced rainfall on its water supply;
- labor difficulties;
- government regulations;
- disruptions in the transportation infrastructure, including roads, bridges, railroad tracks and tunnels;
- adverse weather, fires, floods, earthquakes, hurricanes or other catastrophes;
- cyberattack or other security breaches;
- terrorism or threats of terrorism; or
- other operational problems, including those resulting from the risks described in this section.

Events such as those listed above have resulted in operating losses in the past. Future events may cause shutdowns, which may result in additional downtime and/or cause additional damage to the Company's facilities. Any such downtime or facility damage could prevent the Company from meeting customer demand for its products and/or require it to make unplanned capital expenditures. If one or more of these machines or facilities were to incur significant downtime, it may have a material adverse effect on the Company's results of operations and financial position.

The efficiency of our operations could be adversely affected by disruptions to our Information Technology (IT) Services.

The Company's IT systems, some of which are dependent on services provided by third parties, serve an important role in the efficient operation of its business. The protection of customers, employees and company data is critical to the Company's business. This role includes ordering and managing materials from suppliers, managing its inventory, converting materials to finished products, facilitating order entry and fulfillment and processing of transactions, summarizing and reporting its financial results, facilitating internal and external communications, administering human resources functions, retaining certain personal information and providing other processes necessary to manage its business. The Company is exposed to the risk of cyber incidents in the normal course of business. Cyber incidents may be deliberate attacks for the theft of intellectual property or other sensitive information or may be the result of unintentional events. Like most companies, the Company's information technology systems may be vulnerable to interruption due to a variety of events beyond the Company's control, including, but not limited to, natural disasters, terrorist attacks, power and/or telecommunications failures, computer viruses, hackers and other security issues. The Company has technology security initiatives and disaster recovery plans in place to mitigate the Company's risk to these vulnerabilities, including protection of confidential or personal information, but these measures may not be adequate or implemented properly to ensure that the Company's operations are not disrupted. The Company's IT systems have been, and will likely continue to be, subject to computer viruses or other malicious codes, unauthorized access attempts, phishing and other cyber-incidents. The Company cannot guarantee that its security efforts will prevent breaches or breakdowns to its IT systems or those of its third party providers. Potential consequences of a material cyber incident, which could result in confidential or personal information being accessed, obtained, damaged or used by unauthorized or improper persons, include damage to the Company's reputation, litigation, inefficiencies or production downtimes and increased cyber security protection and remediation costs. Such consequences could have a negative impact on the Company's ability to meet customers' orders, resulting in a delay or decrease to its revenue and a reduction to its operating margins.

The Company could encounter difficulties restructuring operations or closing or disposing of facilities.

The Company is continuously seeking the most cost-effective means and structure to serve our customers and to respond to changes in our markets. Accordingly, from time to time, the Company has, and is likely to again close facilities, sell non-core assets and otherwise restructure operations in an effort to improve cost competitiveness and profitability. As a result, restructuring and divesture costs have been, and are expected to be, a recurring component of our operating costs, and may vary significantly from year to year depending on the scope of such activities. Divestures and restructuring may also result in significant financial charges for the impairment of assets, including intangible assets. For example, the Company expects that its 2019 results will include approximately $42 million of closure and restructuring costs related to its 2018 announced margin improvement plan at its Waco, Texas, Personal Care manufacturing and distribution facility. Furthermore, such activities may divert the attention of management, disrupt our ordinary operations, or result in a reduction in the volume of products produced and sold. There is no guarantee that any such activities will achieve its goal, and if the Company cannot successfully manage the associated risks, its financial condition and results of operations could be adversely affected.

The Company has liabilities with respect to its pension plans and the actual cost of its pension plan obligations could exceed current provisions. As of December 31, 2018, the Company's defined benefit plans had a surplus of $107 million on certain plans and a deficit of $88 million on others.

Since pension fund obligations are primarily long-term in nature, losses in pension fund investments, if any, would result in increased contributions by the Company, to be paid over 5 year or 10 year periods, depending upon the applicable legislation for funding pension deficits. Losses, if any, would also impact the Company's results over a longer period of time and immediately increase liabilities and reduce equity.

The Company’s future funding obligations for its defined benefit pension plans depend upon changes to the level of benefits provided by the plans, the future performance of assets set aside in trusts for these plans, the level of interest rates used to determine minimum funding levels, actuarial data and experience, and any changes in government laws and regulations. As of December 31, 2018, the Company’s defined benefit pension plans held assets with a fair value of $1,588 million.

The Company’s intellectual property rights are valuable, and any inability to protect them could reduce the value of its products and its brands.

The Company relies on patent, trademark and other intellectual property laws of the United States and other countries to protect its intellectual property rights. However, the Company may be unable to prevent third parties from using its intellectual property without its authorization, which may reduce any competitive advantage it has developed. If the Company had to litigate to protect these rights, any proceedings could be costly, and it may not prevail. The Company cannot guarantee that any United States or foreign patents, issued or pending, will provide it with any competitive advantage or will not be challenged by third parties. Additionally, the Company has obtained and applied for United States and foreign trademark registrations, and will continue to evaluate the registration of additional service marks and trademarks, as appropriate. The Company cannot guarantee that any of its pending patent or trademark applications will be approved by the applicable governmental authorities and, even if the applications are approved, third parties may seek to oppose or otherwise challenge these registrations. The failure to secure any pending patent or trademark applications may limit the Company’s ability to protect the intellectual property rights that these applications were intended to cover.

If the Company is unable to successfully retain and develop executive leadership and other key personnel, it may be unable to fully realize critical organizational strategies, goals and objectives.

The success of the Company is substantially dependent on the efforts and abilities of its key personnel, including its executive management team, to develop and implement its business strategies and manage its operations. The failure to retain key personnel or to develop successors with appropriate skills and experience for key positions in the Company could adversely affect the development and achievement of critical organizational strategies, goals and objectives. There can be no assurance that the Company will be able to retain or develop the key personnel it needs and the failure to do so may adversely affect its financial condition and results of operations.

The Company’s balance sheet includes a significant amount of intangible assets. The Company may be required to record a material charge to earnings due to impairment of intangible assets carried on its balance sheet.

As a result of business acquisitions in the past years, mostly in the Personal Care segment, the Company carries on its balance sheet intangible assets. As of December 31, 2018, the Company’s balance sheet included intangible assets of $597 million, of which $311 million related to intangible assets subject to amortization and $286 million related to indefinite-lived intangible assets. The Company performs annual evaluations or more frequently if indicators arise, for potential impairment of the carrying value of its intangible assets. Impairment assessments inherently involve management judgment as to the assumptions used to estimate fair value of the intangible asset being tested. Changes in assumptions or estimates can materially affect the determination of fair value. The major factors that influence the analysis of fair value are the Company's assessment of industry and market conditions, estimates for future revenue growth rates, royalty rates, economic indicators, tax rates and the discount rate associated with the asset being tested.

In connection with the Company's annual impairment testing performed in the fourth quarter of 2018, the Company performed a quantitative assessment for each indefinite-lived intangible asset (trade names and catalog rights) of the Personal Care segment. The tests indicated that the indefinite-lived intangible assets had fair values that exceeded their carrying amounts. Two Personal Care segment indefinite-lived intangible assets are considered to be at risk for future impairment given their respective fair values exceed their respective carrying values by 3% and 20% at the time the test was performed. As of December 31, 2018, the carrying value of these indefinite-lived intangible assets was $116 million and $39 million. If assumed revenue growth is not achieved in future periods and/or events occur that lead to a royalty rate decrease and/or there is an increase to the rate used to discount the estimated cash flows, there is the potential for partial or full impairment related to the indefinite-lived intangible assets. If the Company is required to impair all or a significant amount of the carrying value of related intangible assets, and consequently record a non-cash impairment charge, the Company’s net earnings could be materially and adversely affected.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

A description of our mills and related properties is included in Part I, Item I, Business, of this Annual Report on Form 10-K.

Production facilities

We own substantially all of our production facilities with the exception of some production facilities where a certain portion is subject to a lease in connection with an industrial development bond arrangement, or are leased with a third party or are fee-in-lieu-of-tax agreements, and lease substantially all of our sales offices, regional replenishment centers and warehouse facilities. We believe our properties are in good operating condition and are suitable and adequate for the operations for which they are used. We own substantially all of the equipment used in our facilities.

Forestlands

We manage approximately 5 million acres of forestlands that are directly licensed or owned by Domtar in Canada, through efficient management and the application of certified sustainable forest management practices. We also have access to fiber from an additional

24 million acres of public forestlands in Canada that are licensed and managed by third parties. We believe that these forestlands will provide a continuous supply of wood for future needs.

Listing of facilities and locations

Corporate Offices

Fort Mill, South Carolina

Montreal, Quebec

Pulp & Paper

Division Headquarters

Fort Mill, South Carolina

Uncoated Freesheet

Ashdown, Arkansas

Espanola, Ontario

Hawesville, Kentucky

Johnsonburg, Pennsylvania

Kingsport, Tennessee

Marlboro (Bennettsville), South Carolina

Nekoosa, Wisconsin

Port Huron, Michigan

Rothschild, Wisconsin

Windsor, Quebec

Pulp

Local Distribution Centers

Buffalo, New York

Cincinnati, Ohio

Cleveland, Ohio

Des Moines, Iowa

Houston, Texas

Kansas City, Kansas

Minneapolis, Minnesota

Nashville, Tennessee

Phoenix, Arizona

Plain City, Ohio

Richmond, Virginia

Salt Lake City, Utah

San Antonio, Texas

San Lorenzo, California

St. Louis, Missouri

Vancouver, Washington

Walton, Kentucky

Wayne, Michigan

Wisconsin Rapids, Wisconsin

Personal Care

Division Headquarters

Raleigh, North Carolina

Personal Care – Manufacturing and Distribution

NORTH AMERICA

Delaware, Ohio

Greenville, North Carolina

Jesup, Georgia

Waco, Texas (1)

EUROPE

Aneby, Sweden

Toledo, Spain

Personal Care –

Sales offices

Daytona Beach, Florida

Tuitjenhorn, The Netherlands

Olivette, Missouri

Dryden, Ontario

Kamloops, British Columbia

Plymouth, North Carolina

Chip Mills

Hawesville, Kentucky

Johnsonburg, Pennsylvania

Kingsport, Tennessee

Marlboro (Bennettsville), South Carolina

Converting and Distribution – Onsite

Ashdown, Arkansas

Rothschild, Wisconsin

Windsor, Quebec

Converting and Forms Manufacturing

Addison, Illinois

Brownsville, Tennessee

Dallas, Texas

DuBois, Pennsylvania

Griffin, Georgia

Owensboro, Kentucky

Ridgefields, Tennessee

Rock Hill, South Carolina

Regional Replenishment Centers – United States

Mira Loma, California

Jacksonville, Florida

Chicago, Illinois

Indianapolis, Indiana

Delran, New Jersey

Charlotte, North Carolina

Dallas, Texas

Seattle, Washington

Regional Replenishment Centers – Canada

Richmond, Quebec

Toronto, Ontario

Winnipeg, Manitoba

Representative Office – International

Hong Kong, China

Ariva – Canada

Ottawa, Ontario

Toronto, Ontario

Montreal, Quebec

Quebec City, Quebec

Halifax, Nova Scotia

Oslo, Norway

Linz, Austria

Madrid, Spain

Pusignan, France

Rheinfelden, Switzerland

Schwalbach am Taunus, Germany

Stockholm, Sweden

Texarkana, Arkansas

Wakefield, United Kingdom

Tatum, South Carolina	Mount Pearl, Newfoundland and Labrador
Washington Court House, Ohio	

[1]On November 1, 2018, we announced a margin improvement plan within our Personal Care segment, including the permanent closure of our Waco, Texas, manufacturing and distribution facility. The facility is expected to cease operations in the third quarter of 2019.

ITEM 3. LEGAL PROCEEDINGS

In the normal course of operations, the Company becomes involved in various legal actions mostly related to contract disputes, patent infringements, environmental and product warranty claims, and labor issues. The Company periodically reviews the status of these proceedings and assesses the likelihood of any adverse judgments or outcomes of these legal proceedings, as well as analyzes probable losses. Although the final outcome of any legal proceeding is subject to a number of variables and cannot be predicted with any degree of certainty, management currently believes that the ultimate outcome of current legal proceedings will not have a material adverse effect on the Company's long-term results of operations, cash flow or financial position. However, an adverse outcome in one or more of the significant legal proceedings could have a material adverse effect on the Company's results, financial condition or cash flow in a given quarter or year.

For a discussion of commitments, legal proceedings and related contingencies, refer to Item 8, Financial Statements and Supplementary Data under Note 21 "Commitments and Contingencies" for more details.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

MARKET INFORMATION

Domtar Corporation's common stock is traded on the New York Stock Exchange and the Toronto Stock Exchange under the symbol "UFS".

HOLDERS

At December 31, 2018, the number of shareholders of record (registered and non-registered) of Domtar Corporation common stock was approximately 21,215.

PERFORMANCE GRAPH

This graph compares the return on a $100 investment in the Company's common stock on December 31, 2013 with a $100 investment in an equally-weighted portfolio of a peer group[(1)], and a $100 investment in the S&P 400 MidCap Index. This graph assumes that returns are in local currencies and assumes quarterly reinvestment of dividends. The measurement dates are the last trading day of the period as shown.

(1) On May 18, 2007, the Human Resources Committee of the Board of Directors established performance measures as part of the Performance Conditioned Restricted Stock Units ("PCRSUs") Agreement including the achievement of a total shareholder return compared to a peer group.

The peer group includes: WestRock Company, Ontex Group NV, Glatfelter Corporation, International Paper Co., Kimberly-Clark Corporation, Neenah Paper, Inc., Packaging Corp. of America, Resolute Forest Products Inc., SCA, Sonoco Products Company, Stora Enso Oyj and UPM-Kymmene Corp.

ITEM 6. SELECTED FINANCIAL DATA

The following sets forth selected historical financial data of the Company for the periods and as of the dates indicated. The selected financial data as of and for the fiscal years then ended have been derived from the audited financial statements of Domtar Corporation.

The following table should be read in conjunction with Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations and Item 8, Financial Statements and Supplementary Data.

FIVE YEAR FINANCIAL SUMMARY	Year ended December 31, 2018	December 31, 2017	December 31, 2016	December 31, 2015	December 31, 2014
(In millions of dollars, except per share figures)					
Statement of Income Data:					
Sales[1]	$5,455	$ 5,148	$ 5,090	$ 5,257	$ 5,555
Closure and restructuring costs and impairment of property, plant and equipment and goodwill [2]	15	580	61	81	32
Depreciation and amortization	308	321	348	359	384
Operating income [2, 3]	386	(328)	208	276	376
Net (loss) earnings [4]	283	(258)	128	142	431
Net (loss) earnings per common share - basic	$4.50	$ (4.11)	$ 2.04	$ 2.24	$ 6.65
Net (loss) earnings per common share - diluted	$4.48	$ (4.11)	$ 2.04	$ 2.24	$ 6.64
Cash dividends paid per common share	$1.72	$ 1.66	$ 1.63	$ 1.58	$ 1.30
Balance Sheet Data:					
Cash and cash equivalents	$111	$ 139	$ 125	$ 126	$ 174
Property, plant and equipment, net	2,605	2,765	2,825	2,835	3,131
Total assets	4,925	5,212	5,680	5,654	6,175
Long-term debt due within one year	1	1	63	41	169
Long-term debt	853	1,129	1,218	1,210	1,171
Total shareholders' equity	2,538	2,483	2,676	2,652	2,890

[1] As a result of adopting the new accounting standard "Revenue from Contracts with Customers," we have revised our 2017, 2016, 2015 and 2014 previously reported Sales, which were as follows: $5,157 million, $5,098 million, $5,264 million and $5,563 million, respectively. Refer to Item 8, Financial Statement and Supplementary Data under Note 2 "Recent Accounting Pronouncements" for more details.

[2] In the fourth quarter of 2017, we recorded non-cash goodwill impairment charge associated with our Personal Care segment of $578 million. For additional information, refer to Item 8, Financial Statement and Supplementary Data under Note 4 "Impairment of Property, Plant and Equipment and Goodwill."

[3] As a result of adoption the new accounting guideline "Improving the Presentation of Net Periodic Cost and Net Periodic Postretirement Benefit Cost," we have revised our 2017, 2016, 2015 and 2014 previously reported Operating income (loss), which were as follows: $(317) million, $223 million, $288 million and $364 million, respectively.

Refer to Item 8, Financial Statement and Supplementary Data under Note 2 “Recent Accounting Pronouncements” for more details.

[4] In the fourth quarter of 2017, we recorded a net tax benefit of $140 million related to the U.S. Tax Reform of 2017, which is composed of a benefit of $186 million for the remeasurement of deferred tax assets and liabilities and a charge of $46 million for the repatriation tax. During 2018, we recorded an additional tax benefit of $13 million, $7 million related to adjustments to the repatriation tax and $6 million related to the revaluation of net deferred tax liabilities. Also, the net earnings for the fourth quarter of 2018 included a tax expense of $10 million related to the U.S. Tax Reform. For additional information, refer to Item 8, Financial Statement and Supplementary Data under Note 10 “Income Taxes.”

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with Domtar Corporation's audited consolidated financial statements and notes thereto included in Item 8, Financial Statements and Supplementary Data. Throughout this MD&A, unless otherwise specified, "Domtar Corporation," "the Company," "Domtar," "we," "us" and "our" refers to Domtar Corporation and its subsidiaries. Domtar Corporation's common stock is listed on the New York Stock Exchange and the Toronto Stock Exchange. Except where otherwise indicated, all financial information reflected herein is determined on the basis of accounting principles generally accepted in the United States.

The information contained on our website, www.domtar.com, is not incorporated by reference into this Form 10-K and should in no way be construed as a part of this or any other report that we file with or furnish to the SEC.

In accordance with industry practice, in this report, the term "ton" or the symbol "ST" refers to a short ton, an imperial unit of measurement equal to 0.9072 metric tons. The term "metric ton" or the symbol "ADMT" refers to an air dry metric ton. In this report, unless otherwise indicated, all dollar amounts are expressed in U.S. dollars, and the term "dollars" and the symbol "$" refer to U.S. dollars. In the following discussion, unless otherwise noted, references to increases or decreases in income and expense items, prices, contribution to net earnings (loss), and shipment volumes are based on the twelve-month periods ended December 31, 2018, 2017 and 2016. The twelve month periods are also referred to as 2018, 2017 and 2016. Reference to notes refers to footnotes to the consolidated financial statements and notes thereto included in Item 8, Financial Statements and Supplementary Data.

This MD&A is intended to provide investors with an understanding of our recent performance, financial condition and outlook. Topics discussed and analyzed include:

- Overview
- 2018 Highlights
- Outlook
- Consolidated Results of Operations and Segment Review
- Liquidity and Capital Resources
- Recent Accounting Pronouncements and Critical Accounting Estimates and Policies

OVERVIEW

We have two reportable segments as described below, which also represent our two operating segments. Each reportable segment offers different products and services and requires different manufacturing processes, technology and/or marketing strategies. The following summary briefly describes the operations included in each of our reportable segments.

Pulp and Paper: Our Pulp and Paper segment consists of the design, manufacturing, marketing and distribution of communication, specialty and packaging papers, as well as softwood, fluff and hardwood market pulp.

Personal Care: Our Personal Care segment consists of the design, manufacturing, marketing and distribution of absorbent hygiene products.

2018 HIGHLIGHTS

- Operating income and net earnings increased by 218% and 210%, respectively from 2017
-

Sales increased by 6% from 2017. Net average selling prices for pulp and paper were up while net average selling prices for personal care products were down from 2017. Our manufactured paper volumes were up while our pulp and personal care volumes were down when compared to 2017

- Recognition of a closure and restructuring charge and accelerated depreciation associated with an announced margin improvement plan within our Personal Care segment of $8 million and $7 million, respectively
- $554 million of cash flow from operating activities
- We paid $108 million in dividends

FINANCIAL HIGHLIGHTS	Twelve months ended December 31, 2018	December 31, 2017	December 31, 2016	Variance 2018 vs. 2017 $	%	Variance 2017 vs. 2016 $	%
(In millions of dollars, unless otherwise noted)							
Sales	$5,455	$ 5,148	$ 5,090	$ 307	6 %	$ 58	1 %
Operating (loss) income [1]	386	(328)	208	714	218 %	(536)	-258 %
Net (loss) earnings [2]	283	(258)	128	541	210 %	(386)	-302 %
Net (loss) earnings per common share (in dollars) [3]:							
Basic	$4.50	$ (4.11)	$ 2.04	$ 8.61		$ (6.15)	
Diluted	$4.48	$ (4.11)	$ 2.04	$ 8.59		$ (6.15)	

	At December 31, 2018	At December 31, 2017
Total assets	$ 4,925	$ 5,212
Total long-term debt, including current portion	$ 854	$ 1,130

[1] As a result of the margin improvement plan within our Personal Care segment announced in the fourth quarter of 2018, we recorded a closure and restructuring charge of $8 million and an accelerated depreciation of property, plant and equipment charge of $7 million. In the fourth quarter of 2017, we recorded non-cash goodwill impairment charge associated with our Personal Care segment of $578 million. See Item 8, Financial Statements and Supplementary Data under Note 15 “Closure and Restructuring Costs and Liability” and Note 4 “Impairment of Property, Plant and Equipment and Goodwill”, for more information.

[2] In the fourth quarter of 2017, we recorded a net tax benefit of $140 million related to the U.S. Tax Reform, which is composed of a benefit of $186 million for the remeasurement of deferred tax assets and liabilities and a charge of $46 million for the repatriation tax, and adjusted by $7 million in the third quarter of 2018. See Item 8, Financial Statements and Supplementary Data under Note 10 “Income Taxes” for more information.

[3] See Item 8, Financial Statements and Supplementary Data under Note 6 "Earnings (loss) per Common Share" for more information on the calculation of net earnings per common share.

OUTLOOK

In 2019, our paper shipments will increase as we respond to increased demand from our customers following the announced industry capacity closures while paper prices will continue to improve in the wake of the recently announced price increases across the majority of our paper grades. Softwood and fluff pulp markets will remain balanced through the year due to continued steady demand growth and limited announced new capacity. We anticipate costs, including freight, labor and raw materials, to marginally increase. Personal Care is expected to benefit from our margin improvement plan and new customer wins, partially offset by further raw material cost inflation.

CONSOLIDATED RESULTS OF OPERATIONS AND SEGMENT REVIEW

This section presents a discussion and analysis of our 2018, 2017 and 2016 sales, operating income (loss) and other information relevant to the understanding of our results of operations.

As a result of adopting the new accounting standard “Revenue from Contracts with Customers,” we have revised our segment disclosures to conform to the new guideline. In 2017 and 2016, previously reported Sales were as follows: $4,216 million for Pulp and Paper (2016 - $4,239 million), $1,005 million for Personal Care (2016 - $917 million), and $(64) million for Intersegment sales (2016 - $(58) million). As a result of adopting the new accounting guideline “Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost,” we have revised our 2017 and 2016 segment disclosures to conform to the new guideline. In 2017 and 2016, previously reported numbers for Operating income (loss) were as follows: $250 million for Pulp and Paper (2016 - $217 million), ($527) million for Personal Care (2016 - $57 million), and $(40) million for Corporate (2016 - $(51) million).

ANALYSIS OF NET SALES

By Business Segment	Twelve months ended December 31, 2018	December 31, 2017	December 31, 2016	Variance 2018 vs. 2017 $	%	Variance 2017 vs. 2016 $	%
Pulp and Paper	$4,523	$ 4,216	$ 4,239	307	7 %	(23)	-1 %
Personal Care	1,000	996	909	4	— %	87	10 %
Total for reportable segments	5,523	5,212	5,148	311	6 %	64	1 %
Intersegment sales	(68)	(64)	(58)	(4)		(6)	
Consolidated	5,455	5,148	5,090	307	6 %	58	1 %
Shipments							
Paper - manufactured (in thousands of ST)	2,971	2,891	3,021	80	3 %	(130)	-4 %
Communication Papers	2,446	2,401	2,522	45	2 %	(121)	-5 %
Specialty and Packaging papers	525	490	499	35	7 %	(9)	-2 %
Paper - sourced from third parties (in thousands of ST)	109	109	123	—	— %	(14)	-11 %
Paper - total (in thousands of ST)	3,080	3,000	3,144	80	3 %	(144)	-5 %
Pulp (in thousands of ADMT)	1,536	1,722	1,513	(186)	-11 %	209	14 %

ANALYSIS OF CHANGES IN SALES

	2018 vs. 2017 % Change in Net Sales due to Net Price	Volume / Mix	Currency	Total	2017 vs. 2016 % Change in Net Sales due to Net Price	Volume / Mix	Currency	Total
Pulp and Paper	8 %	-1 %	— %	7 %	— %	-1 %	— %	-1 %
Personal Care	-1 %	-1 %	2 %	— %	-1 %	11 % (a)	— %	10 %
Consolidated sales	7 %	-1 %	— %	6 %	— %	1 %	— %	1 %

(a) Includes sales of HDIS since October 1, 2016.

ANALYSIS OF OPERATING INCOME (LOSS)

By Business Segment	Twelve months ended December 31, 2018 (a)	December 31, 2017 (b)	December 31, 2016	2018 vs. 2017 Variance $	%	2017 vs. 2016 Variance $	%

Operating income (loss)							
Pulp and Paper	$ 438	$ 237	$ 201	201	85 %	36	18 %
Personal Care	$ (5)	$ (527)	$ 57	522	99 %	(584)	(1025)%
Corporate	$ (47)	$ (38)	$ (50)	(9)	-24 %	12	24 %
Consolidated operating income (loss)	$ 386	$ (328)	$ 208	714	218 %	(536)	(258)%

(a) Includes closure and restructuring charge and accelerated depreciation of property, plant and equipment associated with an announced margin improvement plan within our Personal Care segment of $8 million and $7 million, respectively.

(b) Includes non-cash goodwill impairment charge associated with our Personal Care segment of $578 million.

2018 VS. 2017

	$ Change in Segmented Operating Income (Loss) due to								
	Volume/ Mix	Net Price	Input Costs (a)	Operating Expenses (b)	Currency	Depreciation/ Impairment (c)	Restructuring (d)	Other Income/ Expense (e)	Total
Pulp and Paper	(1)	355	(69)	(94)	(9)	16	—	3	201
Personal Care	(2)	(5)	(25)	(11)	4	568	(6)	(1)	522
Corporate	—	—	—	7	—	—	—	(16)	(9)
Consolidated operating income (loss)	(3)	350	(94)	(98)	(5)	584	(6)	(14)	714

(a) Includes raw materials (such as fiber, chemicals, nonwovens and super absorbent polymers) and energy costs.
(b) Includes maintenance, freight costs, selling, general and administrative ("SG&A") expenses and other costs.
(c) In our Personal Care segment, in 2018, we recorded $7 million of non-cash impairment of property, plant and equipment compared to $578 million of non-cash impairment of goodwill recorded in 2017. Depreciation charges were lower by $13 million in 2018, excluding foreign currency impact.
(d)

2018 restructuring charges relate mostly to:	2017 restructuring charges relate mostly to:
-Inventory write-down ($4 million)	-Severance and termination costs ($2 million)
-Severance and termination costs ($3 million)	
-Other costs ($1 million)	

(e)

2018 operating expenses/income includes:	2017 operating expenses/income includes:
- Net gain on sale of property, plant and equipment ($4 million)	- Net gain on sale of property, plant and equipment ($13 million)
- Foreign exchange gain ($2 million)	- Reversal of contingent consideration ($2 million)
- Environmental provision ($5 million)	- Bad debt expense ($1 million)
- Bad debt expense ($2 million)	- Environmental provision ($3 million)
- Other income ($1 million)	- Foreign exchange loss ($1 million)
	- Other income ($4 million)

Commentary - 2018 vs. 2017

Interest Expense, net

We incurred $62 million of net interest expense in 2018 compared to net interest expense of $66 million in 2017. Interest expense decreased mainly due to the repayment at maturity of the 10.75% Notes due in June 2017 and was partially offset by an increase in interest rate on the Term Loan.

Income Taxes

We recorded an income tax expense of $57 million in 2018 compared to an income tax benefit of $125 million in 2017, which yielded an effective tax rate of 17% and 33% for 2018 and 2017, respectively.

During 2018, we recorded $19 million of tax credits, mainly research and experimentation credits, which significantly impacted our effective tax rate.

On December 22, 2017, the U.S. Tax Reform was signed into law. The U.S. Tax Reform significantly changed U.S. tax law for businesses by, among other things, lowering the maximum federal corporate income tax rate from 35% to

21% effective January 1, 2018, implementing a territorial tax system, and imposing a one-time deemed repatriation tax on accumulated foreign earnings. As a result of the U.S. Tax Reform, we recorded a net tax benefit of $140 million in the fourth quarter of 2017 when the legislation was enacted. This consisted of a provisional tax benefit of $186 million relating to the revaluation of our ending net deferred tax liabilities and a provisional expense of $46 million related to the deemed repatriation tax. Additionally, Staff Accounting Bulletin No. 118 (“SAB 118”) was issued to address the application in situations when a registrant did not have the necessary information available, prepared, or analyzed in reasonable detail to complete the accounting for certain income tax effects of the U.S. Tax Reform. The end of the measurement period for SAB 118 purposes was December 22, 2018. We have completed our analysis, including currently available legislative updates, and have recorded an additional tax benefit of $13 million for the year ended December 31, 2018. Of this benefit, $7 million related to adjustments to the deemed mandatory repatriation tax and $6 million related to the revaluation of the Company’s net deferred tax liabilities. Both of these amounts impacted the effective tax rate for 2018.

As a result of the deemed mandatory repatriation tax requirement of the U.S. Tax Reform, we have taxed our undistributed foreign earnings as of December 31, 2017, at reduced tax rates. After completing our evaluation of the U.S. Tax Reform’s impact on business operations, we have determined that we are no longer indefinitely reinvested in these undistributed foreign earnings as well as foreign earnings after December 31, 2017. Therefore, as of December 31, 2018, we have recorded a deferred tax liability of $10 million for foreign withholding tax and various state income taxes associated with future repatriation of these earnings. This $10 million of tax expense impacted the effective tax rate for 2018. We have not provided for deferred taxes on outside basis differences in our investments in foreign subsidiaries that are unrelated to unremitted earnings as we estimate that the deferred tax liability recorded in

2018 in combination with the repatriation tax amount covers all tax liabilities with foreign investments to date. We remain indefinitely reinvested in the outside basis differences of our foreign subsidiaries.

During 2017, we recorded a goodwill impairment charge of $578 million with minimal tax benefit which impacted the effective tax rate by $200 million. This was partially offset by a net tax benefit of $140 million related to the U.S. Tax Reform, which was composed of a benefit of $186 million for the remeasurement of deferred tax assets and liabilities and a charge of $46 million for the repatriation tax. The effective tax rate for 2017 was also significantly impacted by our foreign operations being taxed at lower statutory tax rates and by recording $24 million of current tax credits, mainly research and experimentation credits. We recorded a net valuation allowance increase of $3 million related to certain foreign loss carryforwards and a U.S. state credit, which impacted the effective tax rate for the year.

The U.S. Tax Reform also includes a base erosion provision for Global Intangible Low-Taxed Income (“GILTI”). Beginning in 2018, the GILTI provisions require us to include in our U.S. income tax return, earnings of foreign subsidiaries that are in excess of an allowable return on the tangible assets of the foreign subsidiaries. We are required to make an accounting policy election to either (1) treat taxes due related to GILTI as a current-period expense when incurred or (2) factor such amounts into the measurement of deferred taxes. We have elected to account for any taxes associated with GILTI in accordance with the current-period expense method.

2017 VS. 2016

	$ Change in Segmented Operating Income (Loss) due to								
	Volume/ Mix [a]	Net Price	Input Costs [b]	Operating Expenses [c]	Currency	Depreciation/ Impairment [d]	Restructuring [e]	Other Income/ Expense [f]	Total
Pulp and Paper	(17)	(2)	14	(73)	15	60	31	8	36
Personal Care	6	(11)	3	3	(4)	(579)	(1)	(1)	(584)
Corporate	—	—	—	2	(1)	—	—	11	12
Consolidated operating income (loss)	(11)	(13)	17	(68)	10	(519)	30	18	(536)

(a) Includes results of HDIS since October 1, 2016.

(b) Includes raw materials (such as fiber, chemicals, nonwovens and super absorbent polymers) and energy costs.

(c) Includes maintenance, freight costs, SG&A expenses and other costs.

(d) In 2017, we recorded $578 million of non-cash impairment of goodwill related to our Personal Care segment, compared to $29 million of accelerated depreciation recorded in 2016 related to the conversion of a paper machine to a high quality fluff pulp line at our Ashdown mill. Depreciation charges were lower by $30 million in 2017, excluding foreign exchange currency impact.

(e)

2017 restructuring charges related mostly to:	2016 restructuring charges related mostly to:
-Severance and termination costs ($2 million)	-Fluff pulp conversion outage ($26 million)
	-Severance and termination costs ($9 million)
	-Pension settlement and withdrawal liability ($3 million)

(f) 2017 operating expenses/income includes - Net gain on sale of property, plant and equipment ($13 million) - Reversal of contingent consideration ($2 million) - Bad debt expense ($1 million) - Environmental provision ($3 million) - Foreign exchange loss ($1 million) - Other income ($4 million)	2016 operating expenses/income includes:- Foreign exchange loss ($6 million)- Environmental provision ($2 million)- Other income ($4 million)

Commentary - 2017 vs. 2016

Interest Expense, net

We incurred $66 million of net interest expense in both 2017 and 2016. Interest expense increased due to a reduction in capitalized interest and an increase in interest expense related to the Term Loan Agreement. This increase was offset by the repayment at maturity of the 9.5% Notes due in August 2016 and of the maturity of the 10.75% Notes due in June 2017.

Income Taxes

We recorded an income tax benefit of $125 million in 2017 compared to a tax expense of $29 million in 2016, which yields an effective tax rate of 33% and 18% for 2017 and 2016, respectively.

During 2017, we recorded a goodwill impairment charge of $578 million with minimal tax benefit which impacted the effective tax rate by $200 million. This was partially offset by a net tax benefit of $140 million related to the U.S. Tax Reform, which is composed of a benefit of $186 million for the remeasurement of deferred tax assets and liabilities and a charge of $46 million for the repatriation tax. See “U.S. Tax Reform” below for more information. The effective tax rate for 2017 was also significantly impacted by our foreign operations being taxed at lower statutory tax rates and by recording $24 million of current tax credits, mainly research and experimentation credits.

During 2016, we recorded $18 million of tax credits, mainly research and experimentation credits, which significantly impacted the effective tax rate. The effective tax rate for 2016 was also significantly impacted by our foreign operations being taxed at lower statutory tax rates.

U.S. Tax Reform

The U.S. Tax Reform was signed into law on December 22, 2017. The U.S. Tax Reform significantly changed U.S. tax law for businesses by, among other things, lowering the maximum federal corporate income tax rate from 35% to 21% effective January 1, 2018, implementing a territorial tax system, and imposing a one-time deemed repatriation tax on accumulated foreign earnings. As a result of the corporate tax rate reduction, we revalued our ending net deferred tax liabilities, and recognized a provisional tax benefit of $186 million in our consolidated statement of earnings for the year ended December 31, 2017.

The U.S Tax Reform provided for a mandatory one-time deemed repatriation tax on our undistributed foreign earnings and profits. We recorded a provisional repatriation tax amount of $46 million, which we elected to pay over eight years, and which impacted the 2017 tax rate. While we made a reasonable estimate of the repatriation tax amount, we continued to analyze various factors, including the impact of foreign tax credits available to offset the tax. We continued to gather additional information and monitor for further interpretive guidance in order to finalize our calculations and complete our accounting for the repatriation tax liability.

Additionally, we continued to assess the impact of the U.S. Tax Reform with respect to our current strategy of reinvesting profits of foreign subsidiaries back into those foreign operations. As of December 31, 2017 we had not completed our analysis of the impacts of the U.S Tax Reform and how these changes would impact operational decisions around the utilization of cash residing in the foreign subsidiaries. As such, we had not recorded a tax liability amount for this item.

Valuation Allowances

In 2017, we recorded a net valuation allowance increase of $3 million related to certain foreign loss carryforwards and a U.S. state credit, which impacted the effective tax rate for the year. In 2016, we recorded a net valuation reversal of $1 million, related to foreign loss carryforwards, which impacted the effective tax rate for the year.

Commentary – Segment Review

Pulp and Paper Segment

2018 vs. 2017

Sales in our Pulp and Paper segment increased by $307 million, or 7%, when compared to sales in 2017. This increase in sales is mostly due to an increase in net average selling price for pulp and paper as well as an increase in our paper sales volume. This increase was partially offset by a decrease in our pulp sales volumes.

Operating income in our Pulp and Paper segment amounted to $438 million in 2018, an increase of $201 million, when compared to operating income of $237 million in 2017. Our results were positively impacted by:

- Higher average selling prices for pulp and paper ($355 million)
- Lower depreciation charges ($16 million) due to certain assets being fully depreciated
- Higher other income/expense ($3 million)

These increases were partially offset by:

- Higher operating expenses ($94 million) mostly due to higher freight as a result of a shortage of truck capacity in North America and higher maintenance costs due to timing of planned maintenance, as well as lower production
- Higher input costs ($69 million) mostly related to higher costs of chemical, fiber, and energy in part due to severe weather conditions as well as unfavorable market conditions
- Negative impact of our hedging program and a stronger Canadian dollar on our Canadian denominated expenses ($9 million)
- Lower volume and mix ($1 million) mostly related to lower volume of pulp, partially offset by higher volume of paper

2017 vs. 2016

Sales in 2017 in our Pulp and Paper segment decreased by $23 million, or 1%, when compared to sales in 2016. This decrease in sales is mostly due to a decrease in our paper sales volumes, partially offset by an increase in our pulp sales volumes. Our net average selling price for papers decreased while our net average selling price for pulp increased.

Operating income in our Pulp and Paper segment amounted to $237 in 2017, an increase of $36 million, when compared to operating income of $201 million in 2016. Our results were positively impacted by:

- Lower depreciation charges ($60 million) due to accelerated depreciation related to our 2014 decision to convert a paper machine at our Ashdown facility to a high quality fluff pulp line in 2016 and lower depreciation expenses due to certain assets being fully depreciated
- Lower restructuring costs mostly related to the conversion of a paper machine to a high quality fluff pulp line at our Ashdown mill and the closure of a pulp dryer and idling of related assets at our Plymouth mill related to our plan to optimize fluff pulp manufacturing, recorded in 2016 ($31 million)
- Lower input costs ($14 million) mostly related to lower fiber costs as a result of improved yields and better weather and lower energy costs mostly due to the favorable impact of a boiler conversion, partially offset by higher chemicals costs
- Positive impact of our hedging program, partially offset by a stronger Canadian dollar on our Canadian denominated expenses ($15 million)
- Higher other income/expense ($8 million)

These increases were partially offset by:

- Higher operating expenses ($73 million) mostly due to higher freight, compensation, warehousing and packaging costs as well as lower production
- Lower volume and mix ($17 million) mostly related to lower volume of paper, partially offset by higher volume of pulp
- Lower average selling prices for paper, partially offset by higher average selling prices for pulp ($2 million)

The markets in which our pulp and paper business operate are highly competitive with well-established domestic and foreign manufacturers. Most of our products are commodities that are widely available from other producers as well. Because commodity products have few distinguishing qualities from producer to producer, competition for these products is based primarily on price, which is determined by supply relative to demand. We also compete on the basis of product quality, breadth of offering and service solutions. Further, we compete against electronic transmission and document storage alternatives. As a result of such competition, we are experiencing ongoing decreasing demand for most of our existing paper products.

The pulp market is highly fragmented with many manufacturers competing worldwide. Competition is primarily on the basis of access to low-cost wood fiber, product quality and competitively priced pulp products.

Personal Care

2018 vs. 2017

Sales in 2018 in our Personal Care segment increased by $4 million, remaining relatively flat, when compared to sales in 2017. This increase in sales was driven by favorable foreign currency exchange, mostly due to a stronger Euro and favorable mix, partly offset by lower volume and selling prices.

Operating income increased by $522 million compared to 2017. Our results were positively impacted by:

- Lower depreciation/impairment charges ($568 million) mostly due to the non-cash impairment of goodwill recorded in 2017 of $578 million partially offset by a non-cash impairment of property, plant and equipment charge of $7 million recorded in 2018
- Favorable foreign exchange ($4 million), mostly due to a stronger Euro, net of our hedging program

These increases were partially offset by:

- Higher input costs ($25 million) mostly due to increasing raw materials pricing
- Higher operating expenses ($11 million) mostly due to higher manufacturing and freight costs
- Higher closure and restructuring charges ($6 million) mostly due to the charge recorded in the fourth quarter of 2018 for our margin improvement plan
- Unfavorable average net selling prices ($5 million)
- Lower volume and mix ($2 million)
- Unfavorable other income/expense ($1 million)

2017 vs. 2016

Sales in 2017 in our Personal Care segment increased by $87 million, or 10%, when compared to sales in 2016. This increase in sales was driven by higher sales volume and mix of 11%, mostly due to the acquisition of HDIS on October 1, 2016 and organic sales growth. This increase was partially offset by lower selling prices of 1% when compared to 2016.

Operating income decreased by $584 million compared to 2016. Our results were negatively impacted by:

- Higher depreciation/impairment charges ($579 million) mostly due to the non-cash impairment of goodwill recorded in 2017 of $578 million
- Unfavorable average net selling prices ($11 million)
- Unfavorable foreign exchange impact, net of our hedging program ($4 million)
- Higher restructuring charges ($1 million)
- Unfavorable other income/expense ($1 million)

These decreases were partially offset by the following:

- Higher volume and mix ($6 million)
- Lower input costs ($3 million) mostly due to a decrease in price of super absorbent polymers, fluff pulp and non-wovens
- Lower operating expenses ($3 million) mostly due to lower manufacturing costs, partially offset by higher salaries & wages

In our absorbent hygiene products business, we compete in an industry with fundamental drivers for long-term growth; however, competitive market pressures in the healthcare and retail markets grew significantly in recent years.

Although the impact of such pressures presents some uncertainties, we expect them to result in lower than previously anticipated sales and operating margins.

While we are expected to benefit from the overall increase in healthcare spending due to an aging population, the pressures to limit spending on healthcare may impact overall consumption or the channels in which consumption occurs. Additionally, excess industry capacity has increased pricing pressure in all markets and instigated a shift in the infant and adult private label retail space as competitors historically almost absent in our markets have increased their presence in such markets.

The principal methods and elements of competition remain brand recognition and loyalty, product innovation, quality and performance, price and marketing and distribution capabilities.

Margin Improvement Plan

On November 1, 2018, we announced a margin improvement plan within our Personal Care segment. As part of this plan, our Board of Directors approved the permanent closure of our Waco, Texas, manufacturing and distribution facility, the relocation of certain of our manufacturing assets and a workforce reduction across the division. The Waco, Texas facility is expected to cease operations in the third quarter of 2019.

The aggregate pre-tax earnings charge in connection with this margin improvement plan is estimated to be $57 million, which includes: a) an estimated $29 million in charges relating to accelerated depreciation of the carrying amounts of certain manufacturing equipment and the write-down of related spare parts; b) $10 million of estimated severance and related employee benefits; c) $11 million of estimated relocation and other costs; and d) $7 million of an estimated amount related to the future lease payments at the Waco facility, net of expected sublease revenues. We also expect to incur approximately $5 million of capital expenditures related to certain equipment installation costs.

Closure and restructuring costs are based on management's best estimates. Although we do not anticipate significant changes, actual costs may differ from these estimates due to subsequent business developments. As such, additional costs and further impairment charges may be required in future periods.

We recorded $7 million for the year ended December 31, 2018 of accelerated depreciation under Impairment of property, plant and equipment and goodwill on the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss). During the fourth quarter of 2018, we also recorded a $4 million write-down of inventory, $3 million of severance and termination costs, and $1 million of other costs under Closure and restructuring costs. The balance will be recognized through the third quarter of 2019.

STOCK-BASED COMPENSATION EXPENSE

Under the Omnibus Incentive Plan, we may award to key employees and non-employee directors, at the discretion of the Human Resources Committee of the Board of Directors, non-qualified stock options, incentive stock options, stock appreciation rights, restricted stock units, performance-conditioned restricted stock units, performance share units, deferred share units ("DSUs") and other stock-based awards. The non-employee directors only receive DSUs. We generally grant awards annually and use, when available, treasury stock to fulfill awards settled in common stock and options exercised.

For the year ended December 31, 2018, stock-based compensation expense recognized in our results of operations was $10 million (2017– $20 million; 2016 – $16 million) for all of the outstanding awards. Compensation costs not yet recognized amounted to $17 million (2017– $20 million; 2016– $17 million) and will be recognized over the remaining service period of approximately 26 months. The aggregate value of liability awards settled in 2018 was $8 million (2017 – $7 million; 2016 – $4 million). The total fair value of equity awards settled in 2018 was $6 million (2017 – $3 million), representing the fair value at the time of settlement. The fair value at the grant date for these settled equity awards was $7 million (2017 – $4 million). Compensation costs for performance awards are based on management's best estimate of the final performance measurement.

LIQUIDITY AND CAPITAL RESOURCES

Our principal cash requirements are for ongoing operating costs, pension contributions, working capital and capital expenditures, as well as principal and interest payments on our debt and income tax payments. We expect to fund our liquidity needs primarily with internally generated funds from our operations and, to the extent necessary, through borrowings under our contractually committed $700 million credit facility, of which $700 million is currently undrawn and available, or through our $150 million receivables securitization facility, of which $48 million is currently undrawn and available. Under adverse market conditions, there can be no assurance that these agreements would be available or sufficient. See “Capital Resources” below.

Our ability to make payments on the requirements mentioned above will depend on our ability to generate cash in the future, which is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. Our credit and receivable securitization facilities and debt indentures impose various restrictions and covenants on us that could limit our ability to respond to market conditions, to provide for unanticipated capital investments or to take advantage of business opportunities.

A portion of our cash is held outside the U.S. by foreign subsidiaries. The earnings of the foreign subsidiaries reflect full provision for local income taxes. The U.S. Tax Reform includes a mandatory one-time tax on accumulated earnings of foreign subsidiaries for which we recorded a provisional repatriation tax amount of $46 million in the fourth quarter of 2017 and adjusted by $7 million in the third quarter of 2018. After completing our evaluation of the U.S. Tax Reform’s impact on the business operations, we have determined that we are no longer indefinitely reinvested in these undistributed foreign earnings as well as foreign earnings after December 31, 2017. We remain indefinitely reinvested in the outside basis differences of our foreign subsidiaries.

Operating Activities

Our operating cash flow requirements are primarily for salaries and benefits, the purchase of raw materials, including fiber and energy, and other expenses such as income tax and property taxes.

Cash flows from operating activities totaled $554 million in 2018, a $105 million increase compared to cash flows from operating activities of $449 million in 2017. This increase in cash flows from operating activities is primarily due to an increase in profitability, partially offset by a decrease in cash flow from working capital elements in 2018 when compared to 2017. We made income tax payments, net of refunds, of $71 million in 2018 compared to income tax payments, net of refunds of $33 million in 2017. We paid $46 million of employer pension and other post-retirement contributions in excess of pension and other post-retirement expense in 2018, compared to $32 million in 2017.

Cash flows from operating activities totaled $449 million in 2017, a $16 million decrease compared to cash flows from operating activities of $465 million in 2016. This decrease in cash flows from operating activities is primarily due to a decrease in profitability, partially offset by a decrease in working capital requirements in 2017 when compared to 2016. We made income tax payments, net of refunds, of $33 million in 2017 compared to income tax payments, net of refunds, of $40 million in 2016. We paid $32 million of employer pension and other post-retirement contributions in excess of pension and other post-retirement expense in 2017, compared to $21 million in 2016.

Investing Activities

Cash flows used for investing activities in 2018 amounted to $196 million, a $25 million increase compared to cash flows used for investing activities of $171 million in 2017.

The use of cash in 2018 was attributable to additions to property, plant and equipment of $195 million. Also, in 2018, we made an additional investment of $4 million in our joint venture CelluForce (a company that develops and manufactures nanocrystalline cellulose, a recyclable and renewable nanomaterial) and a $2 million investment in Prisma Renewable Composites, LLC (a company focused on developing advanced materials from lignin and other natural resources). These uses of cash were partially offset by the proceeds from disposal of property, plant and equipment of $5 million.

Cash flows used for investing activities in 2017 amounted to $171 million, a $220 million decrease compared to cash flows used for investing activities of $391 million in 2016.

The use of cash in 2017 was attributable to additions to property, plant and equipment of $182 million as well as the earn-out payment related to the acquisition of Home Delivery Incontinent Supplies (“HDIS”) in the fourth quarter of 2017 for $8 million. This was partially offset by the proceeds from disposal of property, plant and equipment of $19 million.

The use of cash in 2016 was attributable to additions to property, plant and equipment of $347 million as well as the acquisition of HDIS in the fourth quarter of 2016 for $45 million. This was partially offset by the proceeds from disposal of property, plant and equipment of $1 million.

Our annual capital expenditures for 2019 are expected to be between $220 million and $240 million.

Financing Activities

Cash flows used for financing activities totaled $382 million in 2018 compared to cash flows used for financing activities of $274 million in 2017.

The use of cash in 2018 was primarily the result of the repayment of our term loan ($300 million) and dividend payments ($108 million), partially offset by the net proceeds of borrowings under our receivables securitization ($25 million).

Cash flows used for financing activities totaled $274 million in 2017 compared to cash flows used for financing activities of $73 million in 2016.

The use of cash in 2017 was primarily the result of dividend payments ($104 million), the net repayments of borrowings under our credit facilities (revolver and receivable securitization) ($95 million), repayment of unsecured note ($63 million) and a decrease in our bank indebtedness ($12 million).

The use of cash in 2016 was primarily the result of dividend payments ($102 million) and the repurchase of our common stock ($10 million). This was partially offset by the net proceeds from borrowings under our credit facilities (revolver and receivable securitization) ($30 million) and an increase in our bank indebtedness ($12 million).

Capital Resources

Net indebtedness, consisting of long-term debt, net of cash and cash equivalents, was $743 million as of December 31, 2018 compared to $991 million as of December 31, 2017.

Notes Maturity

Our 10.75% Notes, in aggregate principal amount of $63 million, matured on June 1, 2017.

Our 9.5% Notes, in aggregate principal amount of $39 million, matured on August 1, 2016.

Term Loan

In the fourth quarter of 2018, we repaid the $300 million unsecured Term Loan that had been entered into in 2015 by a wholly-owned subsidiary of Domtar with certain domestic banks.

Revolving Credit Facility

In August 2018, we amended and restated our unsecured revolving credit facility (the “Credit Agreement”) with certain domestic and foreign banks, extending the Credit Agreement’s maturity date from August 18, 2021 to August 22, 2023. The amount available under the Credit Agreement remains at $700 million.

Borrowings by the Company under the Credit Agreement are guaranteed by our significant domestic subsidiaries. Borrowings by foreign borrowers under the Credit Agreement are guaranteed by the Company, our significant domestic subsidiaries and certain of our significant foreign subsidiaries.

Borrowings under the Credit Agreement bear interest at LIBOR, EURIBOR, Canadian bankers' acceptance or prime rate, as applicable, plus a margin linked to our credit rating. In addition, we pay facility fees quarterly at rates dependent on our credit ratings.

The Credit Agreement contains customary covenants and events of default for transactions of this type, including two financial covenants: (i) an interest coverage ratio, as defined in the Credit Agreement, that must be maintained at a level of not less than 3 to 1 and (ii) a leverage ratio, as defined in the Credit Agreement, that must be maintained at a level of not greater than 3.75 to 1 (or 4.00 to 1 upon the occurrence of certain qualifying material acquisitions). At December 31, 2018, we were in compliance with these financial covenants, and had no borrowings (December 31, 2017 – nil). At December 31, 2018, we had no outstanding letters of credit (December 31, 2017 – nil), leaving $700 million unused and available under this facility.

Receivables Securitization

We have a $150 million receivables securitization facility that matures in November 2021, extended during 2018 from its previous maturity in March 2019.

At December 31, 2018, borrowings under the receivables securitization facility amounted to $50 million and we had $52 million of letters of credit under the program (December 31, 2017 – $25 million and $50 million, respectively).

The program contains certain termination events, which include, but are not limited to, matters related to receivable performance, certain defaults occurring under the Credit Agreement or our failure to repay or satisfy material obligations. At December 31, 2018, we had $48 million unused and available under this facility.

Common Stock

During 2018, we declared four quarterly dividends of $0.435 per share, to holders of our common stock. Dividends of $27 million, $28 million, $27 million and $27 million were paid on April 16, 2018, July 16, 2018, October 15, 2018 and January 15, 2019, respectively, to shareholders of record as of April 2, 2018, July 3, 2018, October 2, 2018 and January 2, 2019, respectively.

During 2017, we declared four quarterly dividends of $0.415 per share, to holders of our common stock. Dividends of $26 million were paid on April 17, 2017, July 17, 2017, October 16, 2017 and January 15, 2018, respectively, to shareholders of record as of April 3, 2017, July 3, 2017, October 2, 2017 and January 2, 2018, respectively.

On February 19, 2019, our Board of Directors approved a quarterly dividend of $0.435 per share, to be paid to holders of our common stock. This dividend is to be paid on April 15, 2019 to shareholders of record on April 2, 2019.

OFF BALANCE SHEET ARRANGEMENTS

In the normal course of business, we finance certain of our activities off balance sheet through operating leases.

GUARANTEES

Indemnifications

In the normal course of business, we offer indemnifications relating to the sale of our businesses and real estate. In general, these indemnifications may relate to claims from past business operations, the failure to abide by covenants and the breach of representations and warranties included in sales agreements. Typically, such representations and warranties relate to taxation, environmental, product and employee matters. The terms of these indemnification agreements are generally for an unlimited period of time. At December 31, 2018, we were unable to estimate the potential maximum liabilities for these types of indemnification guarantees as the amounts are contingent upon the outcome of future events, the nature and likelihood of which cannot be reasonably estimated at this time. Accordingly, no provision has been recorded. These indemnifications have not yielded significant expenses in the past.

Pension Plans

We have indemnified and held harmless the trustees of our pension funds, and the respective officers, directors, employees and agents of such trustees, from any and all costs and expenses arising out of the performance of their obligations under the relevant trust agreements, including in respect of their reliance on authorized instructions from us or for failing to act in the absence of authorized instructions. These indemnifications survive the termination of such agreements. At December 31, 2018, we have not recorded a liability associated with these indemnifications, as we do not expect to make any payments pertaining to these indemnifications.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

In the normal course of business, we enter into certain contractual obligations and commercial commitments. The following tables provide our obligations and commitments at December 31, 2018:

CONTRACT TYPE (in millions of dollars)	2019	2020	2021	2022	2023	THEREAFTER	TOTAL
Long-term debt (excluding interest)	—	—	50	300	—	$ 500	$ 850
Capital leases (including interest)	2	2	2	1	1	7	15
Operating leases	26	21	17	12	10	17	103
Long-term income taxes payable (1)	3	3	3	3	6	18	36
Total obligations	$ 31	$ 26	$ 72	$ 316	$ 17	$ 542	1,004

COMMITMENT TYPE (in millions of dollars)	2019	2020	2021	2022	2023	THEREAFTER	TOTAL
Other commercial commitments (2)	$ 84	$ 13	$ 3	1	—	2	$ 103

(1) In connection with the U.S. Tax Reform, we have remaining liabilities of $36 million in repatriation tax to pay through 2025. See Note 10 "Income Taxes" for additional information on the U.S. Tax Reform.

(2) Includes commitments to purchase property, plant and equipment, roundwood, wood chips, gas and certain chemicals. Purchase orders in the normal course of business are excluded.

In addition, we expect to contribute a minimum total amount of $12 million to the pension plans in 2019 and a minimum total amount of $5 million in 2019 to the other post-retirement benefits plans.

For 2019 and the foreseeable future, we expect cash flows from operations and from our various sources of financing to be sufficient to meet our contractual obligations and commercial commitments.

RECENT ACCOUNTING PRONOUNCEMENTS

Refer to Item 8, Financial Statements and Supplementary Data under Note 2 “Recent Accounting Pronouncements”.

CRITICAL ACCOUNTING ESTIMATES AND POLICIES

Our principal accounting policies are described in Item 8, Financial Statements and Supplementary Data under Note 1 “Summary of Significant Accounting Policies”. Notes referenced in this section are included in Item 8, Financial Statements and Supplementary Data.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates, assumptions and choices amongst acceptable accounting methods that affect our reported results of operations and financial position. Critical accounting estimates pertain to matters that contain a significant level of management estimates about future events, encompass the most complex and subjective judgments and are subject to a fair degree of measurement uncertainty. On an ongoing basis, management reviews its estimates, including those related to environmental matters and asset retirement obligations, impairment and useful lives of long-lived assets, closure and restructuring costs, intangible assets impairment, pension and other post-retirement benefit plans, income taxes and contingencies related to legal claims. These critical accounting estimates and policies have been reviewed with the Audit Committee of our Board of Directors. We believe these accounting policies, and others as set forth in Note 1 “Summary of Significant Accounting Policies”, should be reviewed as they are essential to understanding our results of operations, cash flows and financial condition. Actual results could differ from those estimates.

Environmental Matters and Asset Retirement Obligations

We maintain provisions for estimated environmental costs when remedial efforts are probable and can be reasonably estimated. Environmental provisions relate mainly to air emissions, effluent treatment, silvicultural activities and site remediation (together referred to as “environmental matters”). The environmental cost estimates reflect assumptions and judgments as to probable nature, magnitude and timing of required investigation, remediation and monitoring activities, as well as contribution by other responsible parties.

The most significant environmental provision is related to the Seaspan action. The provision estimates are based on an awarded contract to implement the remediation plan approved by the relevant government authorities. Additional information regarding Seaspan and other environmental matters is available in Note 21 “Commitments and Contingencies”.

While we believe that we have determined the costs for environmental matters likely to be incurred, based on known information, our ongoing efforts to identify potential environmental concerns that may be associated with the properties may lead to future environmental investigations. These efforts may result in the determination of additional environmental costs and liabilities, which cannot be reasonably estimated at this time. In addition, environmental laws and regulations and interpretation by regulatory authorities could change which could result in significant changes to our estimates. For further details on “Climate change regulation” and other environmental matters refer to Note 21 “Commitments and Contingencies”.

Asset retirement obligations are mainly associated with landfill operation and closure and bark pile management. We recognize asset retirement obligations, at fair value, in the period in which we incur a legal obligation associated with the retirement of an asset. The fair value is based on the expected cash flow approach, in which multiple cash flow scenarios that reflect a range of possible outcomes are considered. Probabilities are applied to each of the cash flow scenarios to arrive at an expected cash flow. The estimated cash flows are then discounted using a credit adjusted risk-free interest rate in combination with business-specific and other relevant risks to discount the cash flow. The rates used vary between 4.7% and 12.0%.

Cash flow estimates incorporate assumptions that marketplace participants would use in their estimates of fair value, whenever that information is available without undue cost and effort. If unavailable, assumptions are based on internal experts, third-party engineers' studies and historical experience in remediation work. As at December 31, 2018, we had an asset retirement obligation provision of $12 million for 11 locations (2017 – $15 million).

As at December 31, 2018, we had a provision of $37 million for environmental matters and other asset retirement obligations (2017 – $44 million). Certain of these amounts have been discounted due to more certainty of the timing of expenditures using the credit adjusted risk-free interest rate for the corresponding period until the settlement date. The rates used vary, based on the prevailing rate at the moment of recognition of the liability and on its settlement period. Additional costs, not known or identified, could be incurred for remediation efforts. Based on policies and procedures in place to monitor environmental exposure, management believes that such additional remediation costs would not have a material adverse effect on our financial position, result of operations or cash flows.

Impairment of Property Plant and Equipment and Definite-Lived Intangible Assets

Property, plant and equipment and definite-lived intangible assets are reviewed for impairment upon the occurrence of events or changes in circumstances indicating that, at the lowest level of determinable cash flows, the carrying value of the assets may not be recoverable. Step I of the impairment test assesses if the carrying value of the assets exceeds their estimated undiscounted future cash flows in order to assess if the property, plant and equipment and definite-lived intangible assets are impaired. In the event the estimated undiscounted future cash flows are lower than the net book value of the assets, a Step II impairment test must be carried out to determine the impairment charge. In Step II, the assets are written down to their estimated fair values. Given that there is generally no readily available quoted value for our property, plant and equipment and definite-lived intangible assets, we determine fair value of our assets based on the present value of estimated future cash flows expected from their use and eventual disposition, and by using the liquidation or salvage value in the case of idled assets. The fair value estimate in Step II is based on the undiscounted cash flows used in Step I.

Estimates of undiscounted future cash flows used to test the recoverability of the property, plant and equipment and definite-lived intangible assets includes key assumptions related to selling prices, inflation-adjusted cost projections, forecasted exchange rates (when applicable) and estimated useful life. Changes in our assumptions and estimates may affect our forecasts and may lead to an outcome where impairment charges would be required. In addition, actual results may vary from our forecasts, and such variations may be material and unfavorable, thereby triggering the need for future impairment tests where our conclusions may differ in reflection of prevailing market conditions.

Useful Lives

On a regular basis, we review the estimated useful lives of our property, plant and equipment and our definite-lived intangible assets. Assessing the reasonableness of the estimated useful lives of property, plant and equipment and definite-lived intangible assets requires judgment and is based on currently available information. Changes in circumstances such as technological advances, changes to our business strategy, changes to our capital strategy or changes in regulation can result in useful lives differing from our estimates. Revisions to the estimated useful lives of property, plant and equipment and definite-lived intangible assets constitute a change in accounting estimate and are dealt with prospectively by amending depreciation and amortization rates.

A change in the remaining estimated useful life of a group of assets, or their estimated net salvage value, will affect the depreciation or amortization rate used to depreciate or amortize the group of assets and thus affect depreciation or amortization expense as reported in our results of operations. In 2018, we recorded depreciation and amortization expense of $308 million compared to $321 million and $348 million in 2017 and 2016, respectively. At December 31, 2018, we had property, plant and equipment with a net book value of $2,605 million (2017 – $2,765 million) and definite-lived intangible assets, net of amortization, of $311 million (2017 – $337 million).

In the fourth quarter of 2018, we announced the permanently closure of our Waco, Texas Personal Care manufacturing and distribution facility, the relocation of certain of our manufacturing assets and a workforce reduction across the division. As a result, we recognized $7 million of accelerated depreciation in 2018.

In the fourth quarter of 2014, we announced the conversion of a paper machine at our Ashdown, Arkansas facility to a high quality fluff pulp line. As a result, we recognized $29 million of accelerated depreciation in 2016.

Closure and Restructuring Costs

Closure and restructuring costs are recognized as liabilities in the period when they are incurred and are measured at their fair value. For such recognition to occur, management, with the appropriate level of authority, must have approved and committed to a firm plan and appropriate communication to those affected must have occurred. These provisions may require an estimation of costs such as severance and termination benefits, pension and related curtailments, environmental remediation and may also include expenses related to demolition and outplacement. Actions taken may also require an evaluation of any remaining assets to determine required impairments, if any, and a review of estimated remaining useful lives which may lead to accelerated depreciation expense.

Estimates of cash flows and fair value relating to closures and restructuring require judgment. Closure and restructuring liabilities are based on management's best estimates of future events at December 31, 2018. Although we do not anticipate significant changes, actual costs may differ from these estimates due to subsequent business developments. As such, additional costs and further impairment charges may be required in future periods.

In 2018, in connection with our announced plan to permanently close our Waco, Texas Personal Care manufacturing and distribution facility, we recognized a $4 million write-down of inventory, $3 million of severance and termination costs, and $1 million of other costs under Closure and restructuring costs.

During 2018, there were no other costs related to previous and ongoing closures and restructuring (severance and termination costs of $2 million and $3 million in 2017 and 2016, respectively, and pension settlement costs of nil and $1 million in 2017 and 2016, respectively).

In 2016, in connection with our plan to optimize fluff pulp manufacturing at the Plymouth, North Carolina mill, we recognized $5 million of severance and termination costs.

In 2016, due to the conversion of the paper machine at our Ashdown, Arkansas mill, we recognized $26 million of costs related to the fluff pulp conversion outage. In 2016, as a result of a revision in our estimated withdrawal liability for U.S. multiemployer plans, we recorded a credit to earnings of $4 million in Closure and restructuring costs on the Consolidated Statement of Earnings and Comprehensive Income (Loss).

Additional information can be found under Note 15 “Closure and Restructuring Costs and Liability”.

Indefinite-lived intangible assets impairment assessment

Indefinite-lived intangible assets consist of trade names ($238 million) and catalog rights ($38 million) following the business acquisitions in the Personal Care segment and license rights ($6 million) and water rights ($4 million) in our Pulp and Paper segment.

We test indefinite-lived intangible assets at the asset level. Indefinite-lived intangible assets are not amortized and are evaluated at the beginning of the fourth quarter of every year or more frequently whenever indicators of potential impairment exist.

In performing the quantitative assessment, fair value of the indefinite-lived intangible assets is derived using an income approach. Under this approach, we estimate the fair value of indefinite-lived intangible assets based on the present value of estimated future cash flows (mainly a relief from royalty model). Considerable management judgment is necessary to estimate future cash flows used to measure the fair value. Key estimates supporting the cash flow projections include, but are not limited to, management's assessment of industry and market conditions as well as its estimates of revenue growth rates, royalty rates, economic indicators and tax rates. Financial forecasts are consistent with our operating plans and are prepared for each indefinite-lived intangible asset quantitative assessment.

The discount rate assumption used is based on the weighted-average cost of capital adjusted for business-specific and other relevant risks. If the carrying amounts of the indefinite-lived intangible assets exceed their fair value, an impairment loss is recognized in an amount equal to that excess.

In connection with the Company's annual impairment testing performed in the fourth quarter of 2018, we performed a quantitative assessment for each indefinite-lived intangible asset (trade names and catalog rights) of the Personal Care segment. The tests indicate that the indefinite-lived intangible assets have fair values that exceed their carrying amounts. Two Personal Care segment indefinite-lived intangible assets are considered to be at risk for future impairment given their respective fair values exceed their respective carrying values by 3% and 20% at the time the test was performed. As of December 31, 2018, the carrying value of these indefinite-lived intangible assets was $116 million and $39 million.

Variations in our assumptions and estimates, particularly in the expected growth rates and royalty rates embedded in our cash flow projections, and the discount rate could have a significant impact on fair value. Specifically, regarding the indefinite-lived intangible asset noted above with carrying value of $116 million and a fair value that exceeded the carrying value by 3%, a 0.5% decrease in expected growth rates, a 0.25% decrease in royalty rate or a 0.70% increase in the discount rate would have the effect of making the fair value to be equal to the carrying value. A significant reduction in the estimated fair values could result in significant non-cash impairment charges in the future.

Pension Plans and Other Post-Retirement Benefit Plans

We have several defined contribution plans and multiemployer plans. The pension expense under these plans is equal to our contribution. Defined contribution pension expense was $50 million for the year ended December 31, 2018 (2017– $39 million and 2016 – $40 million).

We sponsor both contributory and non-contributory U.S. and non-U.S. defined benefit pension plans. We also sponsor a number of other post-retirement benefit plans for eligible U.S. and non-U.S. employees; the plans are unfunded and include life insurance programs and medical and dental benefits. In addition, we provide supplemental unfunded defined benefit pension plans and supplemental unfunded defined contribution pension plans to certain senior management employees.

We account for pensions and other post-retirement benefits in accordance with Compensation-Retirement Benefits Topic of the Financial Accounting Standards Board-Accounting Standards Committee which requires employers to recognize the overfunded or underfunded status of defined benefit pension plans as an asset or liability in its Consolidated Balance Sheets. Pension and other post-retirement benefit charges require assumptions in order to estimate the projected and accumulated benefit obligations. These assumptions require considerable management judgment and include:

- Expected long-term rate of return on plan assets – used to estimate the growth and expected return on assets
- Discount rate – used to determine interest costs and the net present value of our obligations
- Rate of compensation increase – used to calculate the impact of future increases on our obligations
- Health care cost trends – used to calculate the impact of future health care costs on our obligations
- Employee related factors, such as mortality rates, turnover, retirement age and disabilities – used to determine the extent of our obligations

Changes in these assumptions result in actuarial gains or losses, which are amortized over the expected average remaining service life of the active employee group covered by the plans, only to the extent that the unrecognized net actuarial gains and losses are in excess of 10% of the greater of the projected benefit obligation and the market value of assets, over the average remaining service period of approximately nine years of the active employee group covered by the pension plans, and 13 years of the active employee group covered by the other post-retirement benefits plans.

An expected rate of return on plan assets of 5.2% was considered appropriate by management for the determination of pension expense for 2018. Effective January 1, 2019, we will use 5.2% as the expected return on plan assets, which reflects the current view of long-term investment returns. The overall expected long-term rate of return on plan assets is based on management's best estimate of the long-term returns of the major asset classes (cash and cash equivalents, equities and bonds) weighted by the actual allocation of assets at the measurement date, net of expenses. This rate includes an equity risk premium over government bond returns for equity investments and a value-added premium for the contribution to returns from active management. The sources used to determine management's best estimate of long-term returns are numerous and include country specific bond yields, which may be derived from the market using local bond indices or by analysis of the local bond market, and country-specific inflation and investment market expectations derived from market data and analysts' or governments' expectations, as applicable.

We set our discount rate assumption annually to reflect the rates available on high-quality, fixed income debt instruments, with a duration that is expected to match the timing and amount of expected benefit payments. High-quality debt instruments are corporate bonds with a rating of AA or better. The discount rates at December 31, 2018 for pension plans were estimated at 3.8% for the projected benefit obligation and 3.5% for the net periodic benefit cost for 2018 and for post-retirement benefit plans were estimated at 3.8% for the projected benefit obligation and 3.5% for the net periodic benefit cost for 2018.

We used a full yield curve approach to estimate the current service and interest cost components of net periodic benefit cost for Canadian pension plans and U.S. funded pension plans. The estimate of these components is made by applying the specific spot rates along the yield curve used in the determination of the benefit obligation to the relevant projected cash flows. We used this approach to provide a more precise measurement of current service and interest cost components by improving the correlation between projected benefit cash flows to the corresponding spot yield curve rates.

The rate of compensation increase is another significant assumption in the actuarial model for pension (set at 2.7% for the projected benefit obligation and 2.8% for the net periodic benefit cost) and for post-retirement benefit plans (set at 2.8% for the projected benefit obligation and 2.7% for the net periodic benefit cost) and is determined based upon our long-term plans for such increases.

For employee related factors, mortality rate tables tailored to our industry were used and the other factors reflect our historical experience and management's best estimate regarding future expectations.

For measurement purposes, a 4.4% weighted average annual rate of increase in the per capita cost of covered health care benefits was assumed for 2018. The rate was assumed to decrease gradually to 3.5% by 2033 and remain at that level thereafter.

The following table provides a sensitivity analysis of the key weighted average economic assumptions used in measuring the projected pension benefit obligation, the accrued other post-retirement benefit obligation and related net periodic benefit cost for 2018. The sensitivity analysis should be used with caution as it is hypothetical and changes in each key assumption may not be linear. The sensitivities in each key variable have been calculated independently of each other.

PENSION AND OTHER POST-RETIREMENT BENEFIT PLANS	Pension		Other Post-Retirement Benefit	
	Projected Benefit Obligation	Net Periodic Benefit Cost	Projected Benefit Obligation	Net Periodic Benefit Cost
(In millions of dollars)				
Expected rate of return on assets				
Impact of:				
1% increase	N/A	(16)	N/A	N/A
1% decrease	N/A	17	N/A	N/A
Discount rate				
Impact of:				
1% increase	(170)	(5)	(7)	-
1% decrease	207	20	8	-
Assumed overall health care cost trend				
Impact of:				
1% increase	N/A	N/A	3	-
1% decrease	N/A	N/A	(3)	-

Our pension plan funding policy is to contribute annually the amount required to provide for benefits earned in the year and to fund solvency deficiencies, funding shortfalls and past service obligations over periods not exceeding those permitted by the applicable regulatory authorities. Past service obligations primarily arise from improvements to plan benefits. The other post-retirement benefit plans are not funded and contributions are made annually to cover benefit payments. We expect to contribute a minimum total amount of $12 million in 2019 compared to $57 million in 2018 (2017– $47 million; 2016 – $31 million) to the pension plans. We expect to contribute a minimum total amount of $5 million in 2019 compared to $4 million in 2018 to the other post-retirement benefit plans (2017– $3 million; 2016– $5 million).

Benefit obligations and fair values of plan assets as of December 31, 2018 for our pension and post-retirement plans were are follows:

	December 31, 2018		December 31, 2017	
	Pension plans $	Other post-retirement benefit plans $	Pension plans $	Other post-retirement benefit plans $
Projected benefit obligation at end of year	(1,569)	(62)	(1,764)	(76)
Fair value of assets at end of year	1,588	—	1,765	—
Funded status	19	(62)	1	(76)

For additional details on our pension plans and other post-retirement benefit plans, refer to Note 7 “Pension Plans and Other Post-Retirement Benefit Plans”.

Income Taxes

We use the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined according to differences between the carrying amounts and tax bases of the assets and liabilities. The change in the net deferred tax asset or liability is included in earnings. Deferred tax assets and liabilities are measured using enacted tax rates and laws expected to apply in the years in which assets and liabilities are expected to be recovered or settled. Deferred tax assets and liabilities are classified as non-current items on the Consolidated Balance Sheets. For these years, a projection of taxable income and an assumption of the ultimate recovery or settlement period for temporary differences are required. The projection of future taxable income is based on management's best estimate and may vary from actual taxable income.

On a quarterly basis, we assess the need to establish a valuation allowance for deferred tax assets and, if it is deemed more likely than not that our deferred tax assets will not be realized based on these taxable income projections, a valuation allowance is recorded. In general, "realization" refers to the incremental benefit achieved through the reduction in future taxes payable or an increase in future taxes refundable from the deferred tax assets. Evaluating the need for an amount of a valuation allowance for deferred tax assets often requires significant judgment. All available evidence, both positive and negative, should be considered to determine whether, based on the weight of that evidence, a valuation allowance is needed.

In our evaluation process, we give the most weight to historical income or losses. After evaluating all available positive and negative evidence, although realization is not assured, we determined that it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets, with the exception of certain state credits and losses for which a valuation allowance of $6 million exists at December 31, 2018, and certain foreign loss carryforwards for which a valuation allowance of $10 million exists at December 31, 2018. Of this amount, ($8) million favorably impacted tax expense and the effective tax rate for 2018 (2017 – $3 million; 2016 – ($1) million).

Our deferred tax assets are mainly composed of temporary differences related to various accruals, accounting provisions, pension and post-retirement benefit liabilities, net operating loss carryforwards, and available tax credits. Our deferred tax liabilities are mainly composed of temporary differences pertaining to property, plant and equipment, intangible assets, and other items. Estimating the ultimate settlement period requires judgment. The reversal of timing differences is expected at enacted tax rates, which could change due to changes in income tax laws or the introduction of tax changes through the presentation of annual budgets by different governments. As a result, a change in the timing and the income tax rate at which the components will reverse could materially affect deferred tax expense in our future results of operations.

In addition, U.S. and foreign tax rules and regulations are subject to interpretation and require judgment that may be challenged by taxation authorities. To the best of our knowledge, we have adequately provided for our future tax consequences based upon current facts and circumstances and current tax law. In accordance with Income Taxes Topic of FASB ASC 740, we evaluate new tax positions that result in a tax benefit to us and determine the amount of tax benefits that can be recognized. The remaining unrecognized tax benefits are evaluated on a quarterly basis to determine if changes in recognition or classification are necessary. Significant changes in the amount of unrecognized tax benefits expected within the next 12 months are disclosed quarterly. Future recognition of unrecognized tax benefits would impact the effective tax rate in the period the benefits are recognized. At December 31, 2018, we had gross unrecognized tax benefits of $32 million (2017 – $37 million). These amounts represent the gross amount of exposure in individual jurisdictions and do not reflect any additional benefits expected to be realized if such positions were sustained, such as federal deduction that could be realized if an unrecognized state deduction was not sustained. As of December 31, 2018, we believe it is reasonably possible that up to $6 million of our unrecognized tax benefits may be recognized in 2019, which could significantly impact the effective tax rate. However, the amount and timing of the recognition of these benefits is subject to some uncertainty. In addition, a number of countries are actively pursuing changes to their tax laws applicable to corporation multinationals, such as the U.S. Tax Reform, enacted in 2017. Finally, foreign governments may enact tax laws in response to the U.S. Tax Reform that could result in further changes to global taxation and materially impact our financial results.

We operate in multiple jurisdictions with complex tax policy and regulatory environments. U.S. and foreign tax rules and regulations are subject to interpretation and require judgment that may be challenged by taxation authorities. The U.S. Tax Reform significantly changes how the U.S. taxes corporations. The U.S. Tax Reform requires complex computations to be performed that were not previously required in U.S. tax law, significant judgments to be made in interpretation of the provision of the U.S Tax Reform and significant estimates in calculations, and the preparation and analysis of information not previously relevant or regularly produced. The U.S. Treasury Department, the IRS, and other standard-setting bodies could interpret or issue guidance on how provisions of the U.S. Tax Reform will be applied or otherwise administered that is different from our interpretation.

Tax audits by their nature are often complex and can require several years to resolve. We have a number of audits in process in various jurisdictions. Although the resolution of these tax positions is uncertain, based on currently available information, we believe that we have adequately provided for our future tax consequences based upon current facts and circumstances and current tax law, and we believe that the ultimate outcomes will not have a material adverse effect on our financial position, results of operations or cash flows. For further details refer to Note 10 “Income

Taxes".

Contingencies related to legal claims

As discussed in Item 1A Risk Factors, under the risk "Failure to comply with applicable laws and regulations could have a material adverse effect on our business, financial results or condition" and in Note 21 "Commitments and Contingencies", the Company is subject to various legal proceedings and claims that arise in the ordinary course of business. The Company records a liability when it is probable that a loss has been incurred, and the amount is reasonably estimable. The most likely cost to be incurred is accrued based on an evaluation of the then available facts with respect to each matter. When no amount within a range of estimates is more likely, the minimum is accrued. There is significant judgment required in both the probability determination and as to whether an exposure can be reasonably estimated. For further details on "Contingencies" and legal claims refer to Note 21 "Commitments and Contingencies".

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Our operating income can be impacted by the following sensitivities:

SENSITIVITY ANALYSIS
(In millions of dollars, unless otherwise noted)

Each $10/unit change in the selling price of the following products[1]:	
Papers	
Business Papers	$ 15
Commercial Print & Publishing Papers	10
Specialty & Packaging Papers	5
Pulp - net position	
Softwood	$ 10
Fluff	7
Hardwood	1
Foreign exchange, excluding depreciation and amortization	
(US $0.01 change in relative value to the Canadian dollar before hedging)	9
(US $0.01 change in relative value to the EURO before hedging)	2
Energy [2]	
Natural gas: $0.25/MMBtu change in price before hedging	7

[1] Based on estimated 2019 capacity (ST or ADMT).
[2] Based on estimated 2019 consumption levels. The allocation between energy sources may vary during the year in order to take advantage of market conditions.

Note that we may, from time to time, hedge part of our foreign exchange, and energy positions, which may therefore impact the above sensitivities.

In the normal course of business, we are exposed to certain financial risks. We do not use derivative instruments for speculative purposes; although all derivative instruments purchased to minimize risk may not qualify for hedge accounting.

CREDIT RISK

We are exposed to credit risk on the accounts receivables from our customers. In order to reduce this risk, we review new customers' credit history before granting credit and conduct regular reviews of existing customers' credit performance. As of December 31, 2018, one of our Pulp and Paper segment customers located in the United States represented 10% or $67 million (2017– 12% or $83 million) of our receivables.

We are exposed to credit risk in the event of non-performance by counterparties to our financial instruments. We attempt to minimize this exposure by entering into contracts with counterparties that are believed to be of high credit quality. Collateral or other security to support financial instruments subject to credit risk is usually not obtained. The credit standing of counterparties is regularly monitored.

INTEREST RATE RISK

We are exposed to interest rate risk arising from fluctuations in interest rates on our cash and cash equivalents, bank indebtedness, revolving credit facility, securitization, term loan and long-term debt. Our objective in managing exposure to interest rate changes is to minimize the impact of interest rate changes on earnings and cash flows and to lower our overall borrowing costs. We may manage this interest rate exposure through the use of derivative instruments such as interest rate swap contracts, whereby we agree to exchange the difference between fixed and variable interest amounts calculated by reference to an agreed upon notional principal amount.

COST RISK

We are exposed to price volatility for raw materials and energy used in our manufacturing process. We manage our exposure to cost risk primarily through the use of supplier contracts. We purchase natural gas at the prevailing market price at the time of delivery. To reduce the impact on cash flow and earnings due to pricing volatility, we may utilize derivatives to fix the price of forecasted natural gas purchases. The changes in the fair value on qualifying instruments are included in Accumulated other comprehensive loss to the extent effective, and reclassified into Cost of sales in the period during which the hedged transaction affects earnings. Current contracts are used to hedge a portion of forecasted purchases over the next 42 months.

FOREIGN CURRENCY RISK

Cash flow hedges

We have manufacturing operations in the United States, Canada and Europe. As a result, we are exposed to movements in foreign currency exchange rates in Canada and Europe. Moreover, certain assets and liabilities are denominated in currencies other than the U.S. dollar and are exposed to foreign currency movements. Accordingly, our earnings are affected by increases or decreases in the value of the Canadian dollar and European currencies. Our European subsidiaries are also exposed to movements in foreign currency exchange rates on transactions denominated in a currency other than their Euro functional currency. Our risk management policy allows us to hedge a significant portion of the exposure to fluctuations in foreign currency exchange rates for periods up to three years. We may use derivative financial instruments (currency options and foreign exchange forward contracts) to mitigate our exposure to fluctuations in foreign currency exchange rates.

Derivatives are currently used to hedge forecasted purchases in Canadian dollars by our Canadian subsidiary over the next 24 months. A small amount of derivatives has also been used to hedge a portion of the expected non-Euro foreign exchange cash flow of the Company’s European subsidiaries into Euros for the next 2 months. Such derivatives are designated as cash flow hedges. The changes in the fair value on qualifying instruments are included in Accumulated other comprehensive loss to the extent effective, and reclassified into Sales or Cost of sales in the period during which the hedged transaction affects earnings.

The foreign exchange derivative contracts were fully effective as of December 31, 2018. There were no amounts reflected in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) for the year ended December 31, 2018 resulting from hedge ineffectiveness (2017 and 2016 - nil).

PART II

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Management's Reports to Shareholders of Domtar Corporation

Management's Report on Financial Statements and Practices

The accompanying Consolidated Financial Statements of Domtar Corporation and its subsidiaries (the "Company") were prepared by management. The statements were prepared in accordance with accounting principles generally accepted in the United States of America and include amounts that are based on management's best judgments and estimates. Management is responsible for the completeness, accuracy and objectivity of the financial statements. The other financial information included in the annual report is consistent with that in the financial statements.

Management has established and maintains a system of internal accounting and other controls for the Company and its subsidiaries. This system and its established accounting procedures and related controls are designed to provide reasonable assurance that assets are safeguarded, that the books and records properly reflect all transactions, that policies and procedures are implemented by qualified personnel, and that published financial statements are properly prepared and fairly presented. The Company's system of internal control is supported by written policies and procedures, contains self-monitoring mechanisms, and is audited by the internal audit function. Appropriate actions are taken by management to correct deficiencies as they are identified.

Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. In order to evaluate the effectiveness of internal control over financial reporting, management has conducted an assessment, including testing, using the criteria established in 2013 Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). The Company's system of internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. The Company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on the assessment, management has concluded that the Company maintained effective internal control over financial reporting as of December 31, 2018, based on criteria in Internal Control – Integrated Framework issued in 2013 by the COSO.

The effectiveness of the Company’s internal control over financial reporting as of December 31, 2018 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report, which is included herein.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of Domtar Corporation:

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Domtar Corporation and its subsidiaries (the “Company”) as of December 31, 2018 and December 31, 2017, and the related consolidated statements of earnings (loss) and comprehensive income (loss), shareholders’ equity and cash flows for each of the three years in the period ended December 31, 2018, including the related notes and financial statement schedule listed in the index appearing under Item 15(a)(2) (collectively referred to as the “consolidated financial statements”). We also have audited the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and December 31, 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the COSO.

Change in Accounting Principle

As discussed in Note 2 to the consolidated financial statements, the Company changed the manner in which it accounts for revenues from contracts with customers in 2018.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on the Company’s consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

Charlotte, North Carolina

February 22, 2019

We have served as the Company's auditor since 2007.

DOMTAR CORPORATION

CONSOLIDATED STATEMENTS OF EARNINGS (LOSS) AND COMPREHENSIVE INCOME (LOSS)

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Sales	5,455	5,148	5,090
Operating expenses			
Cost of sales, excluding depreciation and amortization	4,303	4,145	4,051
Depreciation and amortization	308	321	348
Selling, general and administrative	443	444	418
Impairment of property, plant and equipment and goodwill (NOTE 4)	7	578	29
Closure and restructuring costs (NOTE 15)	8	2	32
Other operating (income) loss, net (NOTE 8)	—	(14)	4
	5,069	5,476	4,882
Operating income (loss)	386	(328)	208
Interest expense, net (NOTE 9)	62	66	66
Non-service components of net periodic benefit cost (NOTE 7)	(18)	(11)	(15)
Earnings (loss) before income taxes and equity loss	342	(383)	157
Income tax expense (benefit) (NOTE 10)	57	(125)	29
Equity loss, net of taxes	2	—	—
Net earnings (loss)	283	(258)	128
Per common share (in dollars) (NOTE 6)			
Net earnings (loss)			
Basic	4.50	(4.11)	2.04
Diluted	4.48	(4.11)	2.04
Weighted average number of common shares outstanding (millions)			
Basic	62.9	62.7	62.6
Diluted	63.1	62.7	62.7
Cash dividends per common share	1.72	1.66	1.63
Net earnings (loss)	283	(258)	128
Other comprehensive (loss) income:			
Net derivative (losses) gains on cash flow hedges			
Net (losses) gains arising during the period, net of tax $10 (2017 – $(5); 2016 – $(15))	(30)	6	27
Less: Reclassification adjustment for (gains) losses included in net earnings (loss), net of tax of $1 (2017 – $5; 2016 – $(10))	(2)	(9)	14
Foreign currency translation adjustments	(91)	146	(7)
Change in unrecognized (losses) gains and prior service	(8)	20	(32)

cost related to pension and post-retirement benefit plans, net of tax of $3 (2017 – $(5); 2016 – $12)			
Other comprehensive (loss) income	(131)	163	2
Comprehensive income (loss)	152	(95)	130

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

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DOMTAR CORPORATION

CONSOLIDATED BALANCE SHEETS

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

	At December 31, 2018 $	December 31, 2017 $
Assets		
Current assets		
Cash and cash equivalents	111	139
Receivables, less allowances of $6 and $7	670	704
Inventories (NOTE 11)	762	757
Prepaid expenses	24	33
Income and other taxes receivable	22	24
Total current assets	1,589	1,657
Property, plant and equipment, net (NOTE 12)	2,605	2,765
Intangible assets, net (NOTE 13)	597	633
Other assets (NOTE 14)	134	157
Total assets	4,925	5,212
Liabilities and shareholders' equity		
Current liabilities		
Trade and other payables (NOTE 16)	757	716
Income and other taxes payable	25	24
Long-term debt due within one year (NOTE 18)	1	1
Total current liabilities	783	741
Long-term debt (NOTE 18)	853	1,129
Deferred income taxes and other (NOTE 10)	476	491
Other liabilities and deferred credits (NOTE 19)	275	368
Commitments and contingencies (NOTE 21)		
Shareholders' equity (NOTE 20)		
Common stock $0.01 par value; authorized 2,000,000,000 shares; issued 65,001,104 and 65,001,104 shares	1	1
Treasury stock $0.01 par value; 2,086,535 and 2,305,419 shares	—	—
Additional paid-in capital	1,981	1,969
Retained earnings	1,023	849
Accumulated other comprehensive loss	(467)	(336)
Total shareholders' equity	2,538	2,483
Total liabilities and shareholders' equity	4,925	5,212

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

DOMTAR CORPORATION

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

	Issued and outstanding common shares (millions of shares)	Common stock, at par $	Additional paid-in capital $	Retained earnings $	Accumulated other comprehensive loss $	Total shareholders' equity $
Balance at December 31, 2015	62.8	1	1,966	1,186	(501)	2,652
Stock-based compensation, net of tax	0.1	—	7	—	—	7
Net earnings	—	—	—	128	—	128
Net derivative gains on cash flow hedges:						
Net gains arising during the period, net of tax of $(15)	—	—	—	—	27	27
Less: Reclassification adjustments for losses included in net earnings, net of tax of $(10)	—	—	—	—	14	14
Foreign currency translation adjustments	—	—	—	—	(7)	(7)
Change in unrecognized losses and prior service cost related to pension and post-retirement benefit plans, net of tax of $12	—	—	—	—	(32)	(32)
Stock repurchase	(0.3)	—	(10)	—	—	(10)
Cash dividends declared	—	—	—	(103)	—	(103)
Balance at December 31, 2016	62.6	1	1,963	1,211	(499)	2,676
Stock-based compensation, net of tax	0.1	—	6	—	—	6
Net loss	—	—	—	(258)	—	(258)

Net derivative losses on cash flow hedges:						
Net gains arising during the period, net of tax of $(5)	—	—	—	—	6	6
Less: Reclassification adjustments for gains included in net loss, net of tax of $5	—	—	—	—	(9)	(9)
Foreign currency translation adjustments	—	—	—	—	146	146
Change in unrecognized gains and prior service cost related to pension and post-retirement benefit plans, net of tax of $(5)	—	—	—	—	20	20
Cash dividends declared	—	—	—	(104)	—	(104)
Balance at December 31, 2017	62.7	1	1,969	849	(336)	2,483
Stock-based compensation, net of tax	0.2	—	12	—	—	12
Net earnings	—	—	—	283	—	283
Net derivative losses on cash flow hedges:						
Net losses arising during the period, net of tax of $10	—	—	—	—	(30)	(30)
Less: Reclassification adjustments for gains included in net earnings, net of tax of $1	—	—	—	—	(2)	(2)
Foreign currency translation adjustments	—	—	—	—	(91)	(91)
Change in unrecognized losses and prior service cost related to pension and post-retirement benefit plans, net of tax of $3	—	—	—	—	(8)	(8)
Cash dividends declared	—	—	—	(109)	—	(109)
Balance at December 31, 2018	62.9	1	1,981	1,023	(467)	2,538

The accompanying notes are an integral part of the consolidated financial statements

DOMTAR CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN MILLIONS OF DOLLARS)

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Operating activities			
Net earnings (loss)	283	(258)	128
Adjustments to reconcile net earnings (loss) to cash flows from operating activities			
Depreciation and amortization	308	321	348
Deferred income taxes and tax uncertainties (NOTE 10)	13	(207)	9
Impairment of property, plant and equipment and goodwill (NOTE 4)	7	578	29
Net gains on disposals of property, plant and equipment	(4)	(13)	—
Stock-based compensation expense	8	6	7
Equity loss, net	2	—	—
Other	(1)	2	(2)
Changes in assets and liabilities, excluding the effect of sale and acquisition of businesses			
Receivables	18	(72)	18
Inventories	(24)	21	14
Prepaid expenses	2	5	5
Trade and other payables	24	35	(51)
Income and other taxes	(32)	12	(18)
Difference between employer pension and other post-retirement contributions and pension and other post-retirement expense	(46)	(32)	(21)
Other assets and other liabilities	(4)	51	(1)
Cash flows from operating activities	554	449	465
Investing activities			
Additions to property, plant and equipment	(195)	(182)	(347)
Proceeds from disposals of property, plant and equipment and sale of business	5	19	1
Acquisition of businesses, net of cash acquired (NOTE 3)	—	(8)	(46)
Other	(6)	—	1
Cash flows used for investing activities	(196)	(171)	(391)
Financing activities			
Dividend payments	(108)	(104)	(102)
Stock repurchase	—	—	(10)

Net change in bank indebtedness	—	(12)	12
Change in revolving credit facility	—	(50)	—
Proceeds from receivables securitization facility	85	45	140
Repayments of receivables securitization facility	(60)	(90)	(70)
Repayments of long-term debt	(301)	(64)	(40)
Other	2	1	(3)
Cash flows used for financing activities	(382)	(274)	(73)
Net (decrease) increase in cash and cash equivalents	(24)	4	1
Impact of foreign exchange on cash	(4)	10	(2)
Cash and cash equivalents at beginning of year	139	125	126
Cash and cash equivalents at end of year	111	139	125
Supplemental cash flow information			
Net cash payments for:			
Interest	57	58	64
Income taxes	71	33	40

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

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

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DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS

Domtar designs, manufactures, markets and distributes a wide variety of fiber-based products including communication papers, specialty and packaging papers and absorbent hygiene products. The foundation of its business is a network of wood fiber converting assets that produce paper grade, fluff and specialty pulp. The majority of this pulp production is consumed internally to manufacture paper and other consumer products with the balance sold as market pulp. Domtar is the largest integrated marketer of uncoated freesheet paper in North America serving a variety of customers, including merchants, retail outlets, stationers, printers, publishers, converters and end-users. Domtar also designs, manufactures, markets and distributes a broad line of absorbent hygiene products, as well as infant diapers.

BASIS OF PRESENTATION

The Company’s consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America which requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the year, the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements. On an ongoing basis, management reviews the estimates and assumptions, including but not limited to those related to environmental matters and asset retirement obligations, impairment and useful lives of long-lived assets, closure and restructuring costs, pension and other post-retirement benefit plans, income taxes, business combinations and contingencies, based on currently available information. Actual results could differ from those estimates.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Domtar and its controlled subsidiaries. Intercompany transactions have been eliminated on consolidation. The equity method of accounting is used for investments in affiliates over which the Company has significant influence but does not have effective control.

TRANSLATION OF FOREIGN CURRENCIES

The Company determines its international subsidiaries’ functional currency by reviewing the currencies in which their respective operating activities occur. The Company translates assets and liabilities of its non-U.S. dollar functional currency subsidiaries into U.S. dollars using the rate in effect at the balance sheet date and revenues and expenses are translated at the average exchange rates during the year. Foreign currency translation gains and losses are included in Shareholders' equity as a component of Accumulated other comprehensive loss in the accompanying Consolidated Balance Sheets.

Monetary assets and liabilities denominated in a currency that is different from a reporting entity's functional currency must first be remeasured from the applicable currency to the legal entity's functional currency. The effect of this remeasurement process is recognized in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) and is partially offset by the Company's hedging program (refer to Note 22 "Derivatives and hedging activities and fair value measurement").

At December 31, 2018, the accumulated translation adjustment accounts amounted to $(223) million (2017 – $(132) million).

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

REVENUE RECOGNITION

The Company’s revenue is generated from the sale of finished goods to customers. Revenue is recognized at a single point in time when the performance obligation is satisfied which occurs when the control over the goods is transferred to customers. For shipping and handling activities performed after customers obtain control of the goods, the Company elected to account for these activities as fulfillment activities rather than assessing such activities as separate performance obligations. Accordingly, the sale of goods to customers represents a single performance obligation to which the entire transaction price is allocated.

The point in time when the control of goods is transferred to customers is largely dependent on delivery terms. Revenue is recorded at the time of shipment for delivery terms designated free on board (“f.o.b.”) shipping point. For sales transactions designated f.o.b. destination, revenue is recorded when the product is delivered to the customer’s delivery site.

Revenue is measured as the amount of consideration the Company expects to receive in exchange for goods transferred to customers. Revenue is recognized net of variable consideration in the form of rebates, discounts and other commercial incentives extended to customers. Variable consideration is recognized using the most likely amounts which are based on an analysis of historical experience and current period expectations. The Company includes estimated amounts of variable consideration in revenue to the extent that it is probable that there will not be a significant reversal of recognized revenue when the uncertainty related to that variable consideration is resolved.

For all the Company’s contracts, customer payments are due in less than one year. Accordingly, the Company does not adjust the amount of revenue recognized for the effects of a significant financing component.

Sales taxes, and other similar taxes, collected from customers are excluded from revenue.

SHIPPING AND HANDLING COSTS

The Company classifies shipping and handling costs as a component of Cost of sales in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).

CLOSURE AND RESTRUCTURING COSTS

Closure and restructuring costs are recognized as liabilities in the period when they are incurred and are measured at their fair value. For such recognition to occur, management, with the appropriate level of authority, must have approved and committed to a firm plan and appropriate communication to those affected must have occurred. These provisions may require an estimation of costs such as severance and termination benefits, pension and related curtailments, environmental remediation and may also include expenses related to demolition and outplacement. Actions taken may also require an evaluation of any remaining assets to determine required impairments, if any, and a review of estimated remaining useful lives which may lead to accelerated depreciation expense.

Estimates of cash flows and fair value relating to closures and restructurings require judgment. Closure and restructuring liabilities are based on management's best estimates of future events at December 31, 2018. Although the Company does not anticipate significant changes, the actual costs may differ from these estimates due to subsequent developments such as the results of environmental studies, the ability to find a buyer for assets set to be dismantled and demolished and other business developments. As such, additional costs and further working capital adjustments may be required in future periods.

INCOME TAXES

Domtar uses the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined according to differences between the carrying amounts and tax bases of the assets and liabilities. The Company records its worldwide tax provision based on the respective tax rules and regulations for the jurisdictions in which it operates. The change in the net deferred tax asset or liability is included in Income tax expense (benefit) or in Other comprehensive (loss) income in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss). Deferred tax assets and liabilities are measured using enacted tax rates and laws expected to apply in the years in which the assets and liabilities are expected to be recovered or settled. Uncertain tax positions are recorded based upon the Company's evaluation of whether it is "more likely than not" (a probability level of more than 50%) that, based upon its technical merits, the tax position will be sustained upon examination by the taxing authorities.

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Company establishes a valuation allowance for deferred tax assets when it is more likely than not that they will not be realized. In general, “realization” refers to the incremental benefit achieved through the reduction in future taxes payable or an increase in future taxes refundable from the deferred tax assets. Deferred tax assets and liabilities are classified as non-current items on the Consolidated Balance Sheets.

The Company recognizes interest and penalties related to income tax matters as a component of Income tax expense (benefit) in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).

If and when incurred, the Company accounts for any taxes associated with Global Intangible Low-Taxed Income (“GILTI”) as a period cost.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash and short-term investments with original maturities of less than three months and are presented at cost which approximates fair value.

RECEIVABLES

Receivables are recorded net of a provision for doubtful accounts that is based on expected collectability. The securitization of receivables is accounted for as secured borrowings. Accordingly, financing expenses related to the securitization of receivables are recognized in earnings as a component of Interest expense, net in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).

INVENTORIES

Inventories are stated at the lower of cost or net realizable value. Cost includes labor, materials and production overhead. The last-in, first-out (“LIFO”) method is used to account for certain domestic raw materials, in process and finished goods inventories. LIFO inventories were $227 million and $236 million at December 31, 2018 and 2017, respectively. The balance of domestic raw material inventories, all materials and supplies inventories and all foreign inventories are recorded at either the first-in, first-out (“FIFO”) or average cost methods. Had the inventories for which the LIFO method is used been valued under the FIFO method, the amounts at which product inventories are stated would have been $61 million and $54 million greater at December 31, 2018 and 2017, respectively.

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost less accumulated depreciation including asset impairments. Costs for repair and maintenance activities are expensed as incurred under the direct expense method of accounting. Interest costs are capitalized for significant capital projects. For timberlands, the amortization is calculated using the unit of production method. For all other assets, depreciation is calculated using the straight-line method over the estimated useful lives of the assets. Buildings and improvements are depreciated over periods of 10 to 40 years and machinery and equipment over periods of 3 to 20 years. No depreciation is recorded on assets under construction.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are reviewed for impairment upon the occurrence of events or changes in circumstances indicating that the carrying value of the assets may not be recoverable, by comparing the net book value of the asset group to their estimated undiscounted future cash flows expected from their use and eventual disposition. Impaired assets are recorded at estimated fair value, determined principally by using the present value of estimated future cash flows expected from their use and eventual disposition (refer to Note 4 “Impairment of property, plant and equipment and goodwill”).

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

INTANGIBLE ASSETS AND GOODWILL

Indefinite-lived intangible assets are not amortized and are evaluated for impairment individually at the beginning of the fourth quarter of every year, or more frequently whenever indicators of potential impairment exist. The Company has the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of indefinite-lived intangible assets are less than their carrying amounts. The qualitative assessment follows the same process as the one performed for goodwill, as described below. If a qualitative assessment is performed and after assessing the qualitative factors, the Company determines that it is more likely than not that the fair value of the indefinite-lived intangible assets are less than their carrying amounts, then a quantitative impairment test is required. The Company can also elect to proceed directly to the quantitative test. The quantitative impairment test consists of comparing the fair value of the indefinite-lived intangible assets determined using a variety of methodologies to their carrying amount. If the carrying amounts of the indefinite-lived intangible assets exceed their fair value, an impairment loss is recognized in an amount equal to that excess.

Indefinite-lived intangible assets include trade names related to Attends®, IncoPack®, Indasec® and Reassure®, catalog rights related to Laboratorios Indas S.A.U., license rights related to Xerox and water rights. The Company reviews its indefinite-lived intangible assets each reporting period to determine whether events and circumstances continue to support indefinite useful lives.

Definite-lived intangible assets are stated at cost less amortization and are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Definite-lived intangible assets include water rights, customer relationships, technology, non-compete agreements as well as license rights, which are being amortized using the straight-line method over their respective estimated useful lives. Any potential impairment for definite-lived intangible assets will be calculated in the same manner as disclosed under impairment of property, plant and equipment.

Amortization is based on the following useful lives:

	Useful life
Water rights	40 years
Customer relationships	10 to 40 years
Technology	7 to 20 years
Non-Compete agreements	9 years

Licence rights	12 years

Goodwill is not amortized; instead it is evaluated for impairment at the beginning of the fourth quarter of every year or more frequently whenever indicators of potential impairment exist. A significant amount of judgment is involved in determining if an indicator of impairment has occurred. Such indicators may include deterioration in general economic conditions, negative developments in equity and credit markets, adverse changes in the markets in which an entity operates, increases in input costs that have a negative effect on earnings and cash flows, or a trend of negative or declining cash flows over multiple periods, among others.

The Company performs its goodwill impairment test at the reporting unit level.

In reviewing goodwill for impairment, the Company has the option to first assess qualitative factors to determine whether it is more likely than not (greater than 50%) that the fair value of a reporting unit is less than its carrying amount including goodwill. In performing the qualitative assessment, the Company may identify the relevant drivers of fair value of a reporting unit and the relevant events and circumstances that may have an impact on those drivers of fair value and assesses their impact on the fair value of the reporting unit. To carry out the qualitative assessment, the Company considers elements such as the results of recent fair value assessments, macroeconomic conditions, industry and market considerations, cost factors, overall financial performance, specific events affecting the Company and the business. The identification and impact assessment of events and circumstances on the fair value involves significant judgment and assumptions. If, a qualitative assessment is performed and after assessing the totality of events or circumstances, the Company determines that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill, then it performs the quantitative goodwill impairment test. The Company can also elect to bypass the qualitative assessment and proceed directly to the quantitative goodwill impairment test.

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The quantitative goodwill impairment test is performed by comparing the fair value of the reporting unit with its carrying value including goodwill and recognizing an impairment charge for the amount by which the carrying value exceeds the fair value. The impairment charge is limited to the total amount of goodwill allocated to the reporting unit.

Significant judgment is required to estimate the fair value of a reporting unit. The Company uses an income approach to determine the fair value of a reporting unit. Under the income approach, the Company estimates the fair value of a reporting unit based on the present value of estimated future cash flows. Key estimates supporting the cash flow projections include, but are not limited to, management's assessment of industry and market conditions as well as its estimates of revenue growth rates and profit margins, economic indicators, tax rates and capital expenditures. Assumptions used in the impairment evaluations are consistent with internal projections and operating plans. Analysis of the sensitivities of the fair value estimate to changes in assumptions are also performed. Unanticipated market and macroeconomic events and circumstances may occur and could affect the accuracy and validity of management assumptions and estimates.

OTHER ASSETS

Other assets are recorded at cost.

DEBT ISSUANCE COSTS

Debt issuance costs are presented in the Consolidated Balance Sheets as a deduction from the carrying value of long-term debt. Debt issuance costs associated with revolving credit arrangements are presented in Other assets in the Consolidated Balance Sheets. Debt issuance costs are amortized using the effective rate method over the term of the related debt and included in Interest expense, net in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).

ENVIRONMENTAL COSTS AND ASSET RETIREMENT OBLIGATIONS

Environmental expenditures for effluent treatment, air emission, silvicultural activities and site remediation (together referred to as environmental matters) are expensed or capitalized depending on their future economic benefit. In the normal course of business, Domtar incurs certain operating costs for environmental matters that are expensed as incurred. Expenditures for property, plant and equipment that prevent future environmental impacts are capitalized and amortized on a straight-line basis over 10 to 40 years. Provisions for environmental matters are recorded when remediation efforts are probable and can be reasonably estimated. Provisions for environmental matters are generally not discounted, due to uncertainty with respect to timing of expenditures.

Asset retirement obligations are mainly associated with landfill operation and closure, dredging of settling ponds and bark pile management and are recognized, at fair value, in the period in which Domtar incurs a legal obligation associated with the retirement of an asset. Conditional asset retirement obligations are recognized, at fair value, when the fair value of the liability can be reasonably estimated or on a probability-weighted discounted cash flow estimate. The associated costs are capitalized as part of the carrying value of the related asset and depreciated over its remaining useful life. The liability is accreted using the credit adjusted risk-free interest rate used to discount the cash flow.

STOCK-BASED COMPENSATION AND OTHER STOCK-BASED PAYMENTS

Domtar recognizes the cost (net of estimated forfeitures) of employee services received in exchange for awards of equity instruments over the requisite service period, based on their grant date fair value for awards accounted for as equity and based on the quoted market value at the end of each reporting period for awards accounted for as liability. The Company awards are accounted for as compensation expense in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) and presented in Additional paid-in capital on the Consolidated Balance Sheets for equity type awards and presented in Other liabilities and deferred credits on the Consolidated Balance Sheets for liability type awards.

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Company's awards may be subject to market, performance and/or service conditions. Any consideration paid by plan participants on the exercise of stock options or the purchase of shares is credited to Additional paid-in capital in the Consolidated Balance Sheets. The par value included in the Additional paid-in capital component of stock-based compensation is transferred to Common stock upon the issuance of shares of common stock.

Stock options subject to service conditions vest pro rata on the first three anniversaries of the grant and have a seven-year term. Service and performance-based awards vest on the third anniversary of the grant. The performance-based awards have an additional feature where the ultimate number of units that vest will be determined by the Company's performance results or shareholder return in relation to a predetermined target over the vesting period. Deferred Share Units vest immediately at the grant date and are remeasured at the end of each reporting period, until settlement, using the quoted market value.

Under the amended and restated Domtar Corporation 2007 Omnibus Incentive Plan ("Omnibus Plan"), a maximum of 1,246,036 shares are reserved for issuance in connection with awards to be granted.

DERIVATIVE INSTRUMENTS

Derivative instruments are utilized by Domtar as part of the overall strategy to manage exposure to fluctuations in foreign currency, interest rate and commodity price on certain purchases. As a matter of policy, derivatives are not used for trading or speculative purposes. All derivatives are recorded at fair value either as assets or liabilities. When derivative instruments have been designated within a hedge relationship and are highly effective in offsetting the identified risk characteristics of specific financial assets and liabilities or group of financial assets and liabilities, hedge accounting is applied. In a fair value hedge, changes in fair value of derivatives are recognized in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss). The change in fair value of the hedged item attributable to the hedged risk is also recorded in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) by way of a corresponding adjustment of the carrying amount of the hedged item recognized in the Consolidated Balance Sheets. In a cash flow hedge, changes in fair value of derivative instruments are recorded in Other comprehensive (loss) income. These amounts are reclassified in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) in the periods in which results are affected by the cash flows of the hedged item within the same line item. Any hedge ineffectiveness is recorded in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) when incurred.

PENSION PLANS

Domtar's plans include funded and unfunded defined benefit and defined contribution pension plans. Domtar recognizes the overfunded or underfunded status of defined benefit and underfunded defined contribution pension plans as an asset or liability in the Consolidated Balance Sheets. The net periodic benefit cost includes the following:

- The cost of pension benefits provided in exchange for employees' services rendered during the period,
- The interest cost of pension obligations,
- The expected long-term return on pension fund assets based on a market value of pension fund assets,
- Gains or losses on settlements and curtailments,
- The straight-line amortization of past service costs and plan amendments over the average remaining service period of approximately nine years of the active employee group covered by the plans, and
- The amortization of cumulative net actuarial gains and losses in excess of 10% of the greater of the projected benefit obligation and the market value of assets over the average remaining service period of approximately nine years of the active employee group covered by the plans.

The defined benefit plan obligations are determined in accordance with the projected unit credit actuarial cost method.

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

OTHER POST-RETIREMENT BENEFIT PLANS

The Company recognizes the unfunded status of other post-retirement benefit plans (other than multiemployer plans) as a liability in the Consolidated Balance Sheets. These benefits, which are funded by Domtar as they become due, include life insurance programs, medical and dental benefits and short-term and long-term disability programs. The Company amortizes the cumulative net actuarial gains and losses in excess of 10% of the greater of the projected benefit obligation and the market value of assets over the average remaining service period of approximately 13 years of the active employee group covered by the plans.

GUARANTEES

A guarantee is a contract or an indemnification agreement that contingently requires Domtar to make payments to the other party of the contract or agreement, based on changes in an underlying item that is related to an asset, a liability or an equity security of the other party or on a third party's failure to perform under an obligating agreement. It could also be an indirect guarantee of the indebtedness of another party, even though the payment to the other party may not be based on changes in an underlying item that is related to an asset, a liability or an equity security of the other party. Guarantees, when applicable, are accounted for at fair value.

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 2.

RECENT ACCOUNTING PRONOUNCEMENTS

ACCOUNTING CHANGES IMPLEMENTED

REVENUE FROM CONTRACTS WITH CUSTOMERS

In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers”. The core principal of this guidance is that an entity should recognize revenue, to depict the transfer of promised goods or services to customers, in an amount that reflects the consideration for which the entity is entitled to, in exchange for those goods and services. This new guidance supersedes the revenue recognition requirements found in topic 605.

On January 1, 2018, the Company adopted the standard using the full retrospective method which resulted in a reclassification in the Company’s Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss) for the years ended December 31, 2017 and 2016. The previously reported amounts for Sales and Selling, general and administrative expenses were decreased by $9 million and $8 million, respectively, in relation to the reclassification of certain payments made to customers classified as a reduction of Sales under the new standard. These reclassifications are exclusively contained within the Company’s Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss) and do not have a cumulative effect on retained earnings or other components of equity or net assets in the Company’s Consolidated Balance Sheet as of January 1, 2017.

No practical expedients were used in the transition to the new standard as they were not applicable.

RETIREMENT BENEFITS

In March 2017, the FASB issued ASU 2017-07, “Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost”, which requires an entity to present the service cost component of the net periodic benefit cost with other employee compensation costs in operating income. Only the service cost components are eligible for capitalization in assets. The other components of the net periodic benefit cost (i.e. interest expense, expected return on plan assets, amortization of actuarial gains or losses and amortization of prior year service costs) are presented outside of any subtotal of operating income.

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

On January 1, 2018, the Company adopted the guidance of this accounting standard update which resulted in a reclassification in the Company's Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss) for the years ended December 31, 2017 and 2016. The previously reported amounts of Cost of sales were increased by $14 million and $16 million, respectively, Selling, general and administrative expenses were decreased by $3 million and $1 million, respectively, both with a corresponding impact in Non-service components of net periodic benefit cost. The Company utilized a practical expedient included in the accounting standard update which allowed the Company to use amounts previously disclosed in its pension plans and other post-retirement benefits plans note for the prior periods as the estimation basis for applying the required retrospective presentation requirements. In addition, these required retrospective reclassifications resulted in adjustments to the previously reported Operating income (loss) within the Company's reportable operating segment disclosures for the years ended December 31, 2017 and 2016.

	Year ended December 31, 2017			
	As Reported (Unaudited)	Impact of ASU 2014-09	Impact of ASU 2017-07	As Adjusted
	$	$	$	$
Sales	5,157	(9)	—	5,148
Operating expenses				
Cost of sales, excluding depreciation and amortization	4,131	—	14	4,145
Depreciation and amortization	321	—	—	321
Selling, general and administrative	456	(9)	(3)	444
Impairment of goodwill	578	—	—	578
Closure and restructuring costs	2	—	—	2
Other operating income, net	(14)	—	—	(14)
	5,474	(9)	11	5,476
Operating loss	(317)	—	(11)	(328)

Interest expense, net	66	—	—	66
Non-service components of net periodic benefit cost	—	—	(11)	(11)
Loss before income taxes	(383)	—	—	(383)
Income tax benefit	(125)	—	—	(125)
Net loss	(258)	—	—	(258)

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DOMTAR CORPORATION

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NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

	Year ended December 31, 2016			
	As Reported (Unaudited)	Impact of ASU 2014-09	Impact of ASU 2017-07	As Adjusted
	$	$	$	$
Sales	5,098	(8)	—	5,090
Operating expenses				
Cost of sales, excluding depreciation and amortization	4,035	—	16	4,051
Depreciation and amortization	348	—	—	348
Selling, general and administrative	427	(8)	(1)	418
Impairment of property, plant and equipment	29	—	—	29
Closure and restructuring costs	32	—	—	32
Other operating loss, net	4	—	—	4
	4,875	(8)	15	4,882
Operating income (loss)	223	—	(15)	208
Interest expense, net	66	—	—	66
Non-service components of net periodic benefit cost	—	—	(15)	(15)
Earnings before income taxes	157	—	—	157
Income tax expense	29	—	—	29
Net earnings	128	—	—	128

FINANCIAL INSTRUMENTS

In January 2016, the FASB issued ASU 2016-01, “Recognition and Measurement of Financial Assets and Financial Liabilities”, which amends the guidance on the classification and measurement of financial instruments. Although the ASU retains many current requirements, it significantly revises an entity’s accounting related to the classification and measurement of investments in equity securities and the presentation of certain fair value changes for financial liabilities measured at fair value. The ASU also amends certain disclosure requirements associated with the fair value of financial instruments.

The Company adopted the new guidance on January 1, 2018 with no impact on the consolidated financial statements.

DERIVATIVES AND HEDGING

In March 2016, the FASB issued ASU 2016-05, "Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships", which clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument in an existing hedging relationship would not, in and of itself, be considered a termination of the derivative instrument or a change in a critical term of the hedging relationship. As long as all other hedge accounting criteria in ASC 815 are met, a hedging relationship in which the hedging derivative instrument is novated would not be discontinued or require redesignation. This clarification applies to both cash flow and fair value hedging relationships.

The Company adopted the new guidance on January 1, 2018 with no impact on the consolidated financial statements.

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NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

CLASSIFICATION OF CASH FLOWS

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows", which amends ASC 230 to add or clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows. The new guidance is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows.

The Company adopted the new guidance on January 1, 2018 with no impact on the consolidated financial statements.

DERIVATIVES AND HEDGING

In August 2017, the FASB issued ASU 2017-12, "Targeted Improvements to Accounting for Hedging Activities", which amends the hedge accounting recognition and presentation requirements in ASC 815. The objectives of the ASU are to (1) improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities by better aligning the entity's financial reporting for hedging relationships with those risk management activities and (2) reduce the complexity of and simplify the application of hedge accounting by preparers.

The Company early adopted the new guidance on January 1, 2018 with no impact on the consolidated financial statements.

FUTURE ACCOUNTING CHANGES

LEASES

In February 2016, the FASB issued ASU 2016-02, "Leases", which requires lessees to recognize right-of-use assets and lease liabilities for all of their operating leases while continuing to recognize expenses in the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss) in a manner similar to current accounting standard. Under the standard, disclosures are required to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases.

As a lessee, Domtar's various leases under the existing accounting standard are classified as operating leases that are not recorded on the Consolidated Balance Sheets but are recorded in the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss) as the lease expense is recognized on a straight-line basis over the lease term. With the adoption of the new standard, the Company is required to record substantially all operating leases on the Consolidated Balance Sheets as right-of-use assets and lease liabilities. The operating lease expense will continue to be recognized on a straight-line basis over the lease term. The accounting for finance leases will remain substantially unchanged.

The Company elected to apply the new leases standard as of January 1, 2019. Upon adoption, no cumulative-effect adjustments to the retained earnings were required. At January 1, 2019, the amounts of the operating lease right-of-use assets and lease liabilities were $81 million and $90 million, respectively. The adoption of the standard will not have an impact on the Company’s Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).

For all comparative periods presented in the Consolidated financial statements prior to the adoption of the new leases standard, the Company will continue to report operating leases under Topic 840 “Leases” and provide the related required disclosures.

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NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

IMPLEMENTATION COSTS FOR CLOUD COMPUTING ARRANGEMENTS

In August 2018, the FASB issued ASU 2018-15 "Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract". Under the guidance, implementation costs for cloud computing arrangements ("CCA") should be evaluated for capitalization using the same approach as implementation costs associated with internal-use software and expensed over the term of the hosting arrangement. The ASU also provides the following guidance on presentation and disclosure:

- Capitalized implementation costs should be presented in the same line item on the balance sheet as amounts prepaid for the hosted CCA service, if any (generally as an "other asset").
- The amortization of capitalized implementation costs should be presented in the same statement of earnings line item as the fees associated with the hosted CCA service. Accordingly, the amortization of capitalized implementation costs should not be included with depreciation or amortization expense related to property, plant, and equipment or intangible assets.
- Cash flows related to capitalized implementation costs should be presented as operating activities, consistent with the presentation of cash flows for the fees related to the hosted CCA service.
- Entities are required to disclose the nature of the hosting arrangements that are service contracts and significant judgments made when applying the guidance. Additionally, companies are required to provide quantitative disclosures, including amounts capitalized, amortized, and impaired.

This ASU is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period. The amendments in this ASU should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption.

While the Company is still evaluating the impact of adopting the new standard, it does not expect this new guidance to have a material impact on the consolidated financial statements.

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NOTE 3.

ACQUISITION OF BUSINESSES

Acquisition of Home Delivery Incontinent Supplies Co.

On October 1, 2016, Domtar completed the acquisition of 100% of the outstanding shares of Home Delivery Incontinent Supplies Co. ("HDIS"). HDIS is a leading national direct-to-consumer provider of adult incontinence and related products. Based in Olivette, Missouri, HDIS provides customers with high-quality products and a personalized service for all of their incontinence needs. HDIS operates a distribution center in Olivette, Missouri, as well as two retail locations, in Texarkana, Arkansas and Daytona Beach, Florida and has approximately 240 employees. The results of HDIS's operations are included in the Personal Care reportable segment starting on October 1, 2016. The purchase price was $52 million, net of cash acquired of $3 million and included a potential earn-out payment of up to $10 million to be settled after the first anniversary of the acquisition. The final amount of the earn-out was $8 million and was paid in the last quarter of 2017.

The total purchase price was allocated to tangible and intangible assets acquired and liabilities assumed based on the Company's estimates of their fair value, which were based on information available at that time.

The table below illustrates the purchase price allocation:

Fair value of net assets acquired at the date of acquisition		
Receivables		$4
Inventory		4
Property, plant and equipment		1
Intangible assets		
Customer relationships (1)	21	
Trade names (2)	13	
		34
Goodwill		17
Deferred income tax assets		2
Total assets		62

Less: Liabilities	
Trade and other payables	10
Total liabilities	10
Fair value of net assets acquired at the date of acquisition	52

(1) The useful life of the Customer relationships acquired is estimated at 10 years (as of the date of acquisition).
(2) Indefinite useful life.

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NOTE 4.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT AND GOODWILL

IMPAIRMENT OF GOODWILL

In 2017, the Company performed its annual goodwill impairment testing at October 1. At that date, total goodwill amounting to $578 million resided in the Personal Care reporting unit. Management proceeded directly to the quantitative impairment test for the Personal Care reporting unit. The estimated fair value, determined by the present value of estimated future cash flows was lower than the reporting unit's carrying value and as such the Company recognized a non-cash impairment charge of $578 million, representing the entire amount of goodwill related to the Personal Care reporting unit.

Growing competitive market pressures in the healthcare and retail markets throughout 2017, including the entry of new competitors in the private label category, excess industry capacity and the pressure to limit healthcare spending by governmental agencies, resulted in lower than previously anticipated sales and operating margin. In light of this weakened market outlook, the Company's business forecast was not sufficient to derive a fair value able to support the carrying value of the goodwill associated with the Personal Care reporting unit, leading to the impairment of goodwill.

In 2016, the Company performed its annual goodwill impairment tests at October 1 and determined that the estimated fair value of the Personal Care reporting unit exceeded its carrying value. As a result, no impairment charges were recorded during 2016.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT

The Company reviews property, plant and equipment for impairment upon the occurrence of events or changes in circumstances indicating that, at the lowest level of determinable cash flows, the carrying value of the asset group may not be recoverable.

Estimates of undiscounted future cash flows used to test the recoverability of the asset group includes key assumptions related to selling prices, inflation-adjusted cost projections, forecasted exchange rates when applicable and the estimated useful life of the asset group.

Waco, Texas personal care manufacturing and distribution facility – Permanent closure

In the fourth quarter of 2018, the Company announced a margin improvement plan within the Personal Care Division. As part of this plan, the Board of Directors approved the permanent closure of its Waco, Texas Personal Care manufacturing and distribution facility. As a result, in 2018 the Company recognized $7 million of accelerated depreciation in Impairment of property, plant and equipment and goodwill on the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss).

Ashdown, Arkansas pulp and paper mill – Conversion of a paper machine

In 2016, as a result of a previously announced conversion of a paper machine at Ashdown, Arkansas pulp and paper mill to a high quality fluff pulp line, the Company recognized $29 million of accelerated depreciation in Impairment of property, plant and equipment and goodwill on the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss).

DOMTAR CORPORATION

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NOTE 5.

STOCK-BASED COMPENSATION

OMNIBUS PLAN

Under the Omnibus Plan, the Company may award to key employees and non-employee directors, at the discretion of the Human Resources Committee of the Board of Directors, non-qualified stock options, incentive stock options, stock appreciation rights, restricted stock units, performance-conditioned restricted stock units, performance share units, deferred share units ("DSUs") and other stock-based awards. The non-employee directors only receive DSUs. The Company generally grants awards annually and uses, when available, treasury stock to fulfill awards settled in common stock and option exercises.

PERFORMANCE SHARE UNITS ("PSUs")

PSUs are granted to Management Committee and non-Management Committee members. These awards will be settled in shares for Management Committee members and in cash for non-Management Committee members, based on market conditions and/or performance and service conditions. These awards have an additional feature where the ultimate number of units that vest will be determined by the Company's performance results or shareholder return in relation to a predetermined target over the vesting period. No awards vest when the minimum thresholds are not achieved. The performance measurement date will vary depending on the specific award. These awards will cliff vest at various dates up to February 20, 2021.

PSUs	Number of units	Weighted average grant date fair value $
Vested and non-vested at December 31, 2015	426,079	46.00
Granted	295,504	32.38
Forfeited	(28,523)	39.81
Cancelled	(101,124)	51.27
Vested and settled	(74,655)	35.97
Vested and non-vested at December 31, 2016	517,281	38.98
Granted	256,078	39.04
Forfeited	(24,581)	37.59

Cancelled	(75,710)	38.78
Vested and settled	(50,600)	54.95
Vested and non-vested at December 31, 2017	622,468	37.78
Granted	238,537	41.39
Forfeited	(36,932)	38.09
Issued	52,563	41.05
Vested and settled	(154,178)	44.22
Vested and non-vested at December 31, 2018	722,458	37.82

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NOTE 5. STOCK-BASED COMPENSATION (CONTINUED)

The fair value of PSUs granted in 2018, 2017 and 2016 was estimated at the grant date using the Monte Carlo simulation methodology. The Monte Carlo simulation creates artificial futures by generating numerous sample paths of potential outcomes. The following assumptions were used in calculating the fair value of the units granted:

	2018	2017	2016
Dividend yield	3.800 %	4.130 %	4.740 %
Expected volatility 1 year	22 %	28 %	24 %
Expected volatility 3 years	26 %	28 %	30 %
Risk-free interest rate December 31, 2016	—	—	1.057 %
Risk-free interest rate December 31, 2017	—	1.614 %	0.860 %
Risk-free interest rate December 31, 2018	2.233 %	1.606 %	0.900 %
Risk-free interest rate December 31, 2019	2.461 %	1.751 %	—
Risk-free interest rate December 31, 2020	2.607 %	—	—

At December 31, 2018, of the total vested and non-vested PSUs, 352,241 are expected to be settled in shares and 370,217 will be settled in cash.

RESTRICTED STOCK UNITS (“RSUs”)

RSUs are granted to Management Committee and non-Management Committee members. These awards will be settled in shares for Management Committee members and in cash for non-Management Committee members, upon completing service conditions. The awards cliff vest after a service period of approximately three years. Additionally, the RSUs are credited with dividend equivalents in the form of additional RSUs when cash dividends are paid on the Company’s stock. The grant date fair value of RSUs is equal to the market value of the Company’s stock on the date the awards are granted.

RSUs	Number of units	Weighted average grant date fair value $

Non-vested at December 31, 2015	346,966	44.21
Granted/issued	196,786	34.04
Forfeited	(17,884)	39.69
Vested and settled	(107,198)	39.12
Non-vested at December 31, 2016	418,670	40.90
Granted/issued	182,937	39.83
Forfeited	(19,194)	37.97
Vested and settled	(121,750)	48.72
Non-vested at December 31, 2017	460,663	38.56
Granted/issued	157,502	44.04
Forfeited	(27,251)	39.91
Vested and settled	(135,323)	42.54
Non-vested at December 31, 2018	455,591	39.16

At December 31, 2018, of the total non-vested RSUs, 189,079 are expected to be settled in shares and 266,512 will be settled in cash.

DEFERRED SHARE UNITS

DSUs are granted to the Company's Directors. The DSUs granted to the Directors vest immediately on the grant date. The DSUs are credited with dividend equivalents in the form of additional DSUs when cash dividends are paid on the Company's stock. For

DOMTAR CORPORATION

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NOTE 5. STOCK-BASED COMPENSATION (CONTINUED)

Directors' DSUs, the Company will deliver at the option of the holder either one share of common stock or the cash equivalent of the fair market value on settlement of each outstanding DSU (including dividend equivalents accumulated) upon termination of service. Directors who attained the share ownership requirements may elect to receive the equity component of their annual retainer in DSUs that may be settled in either cash or stock one year after the grant date. The grant date fair value of DSU awards is equal to the market value of the Company's stock on the date the awards are granted.

Management Committee members may elect to defer awards earned under another program into DSUs. In 2018, no vested awards were deferred to DSUs (2017 – nil; 2016 – nil).

DSUs	Number of units	Weighted average grant date fair value $
Vested at December 31, 2015	289,460	28.20
Granted/issued	46,737	37.43
Settled	(15,123)	39.60
Vested at December 31, 2016	321,074	29.01
Granted/issued	36,215	40.68
Settled	(85,055)	32.27
Vested at December 31, 2017	272,234	29.55
Granted/issued	31,691	44.64
Settled	(9,752)	40.95
Vested at December 31, 2018	294,173	30.79

NON-QUALIFIED & PERFORMANCE STOCK OPTIONS

Stock options are granted to Management Committee and non-Management Committee members. The stock options vest at various dates up to February 20, 2021 subject to service conditions for non-qualified stock options. The options expire at various dates no later than seven years from the date of grant.

The fair value of the stock options granted in 2018, 2017 and 2016 was estimated at the grant date using a Black-Scholes based option pricing model or an option pricing model that incorporated the market conditions when applicable. The following assumptions were used in calculating the fair value of the options granted:

	2018		2017		2016	
Dividend yield	3.27	%	3.48	%	3.78	%
Expected volatility	29	%	28	%	30	%
Risk-free interest rate	2.62	%	1.86	%	1.17	%
Expected life	4.5 years		4.5 years		4.5 years	
Strike price	$43.66		$39.81		$33.78	

The grant date fair value of the non-qualified options granted in 2018 was $8.65 (2017 – $7.05; 2016 – $5.95).

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NOTE 5. STOCK-BASED COMPENSATION (CONTINUED)

OPTIONS (including Performance options)	Number of options	Weighted average exercise price $	Weighted average remaining life (in years)	Aggregate intrinsic value (in millions) $
Outstanding at December 31, 2015	451,302	46.48	4.8	0.1
Granted	114,723	33.78	6.2	—
Exercised	(37,296)	41.11	—	—
Forfeited/expired	(6,502)	20.89	—	—
Outstanding at December 31, 2016	522,227	44.39	4.5	0.7
Options exercisable at December 31, 2016	286,011	46.50	3.9	0.1
Outstanding at December 31, 2016	522,227	44.39	4.5	0.7
Granted	106,268	39.81	6.2	—
Exercised	(65,430)	36.33	—	—
Outstanding at December 31, 2017	563,065	44.46	4.1	3.6
Options exercisable at December 31, 2017	359,960	48.02	3.2	1.3
Outstanding at December 31, 2017	563,065	44.46	4.1	3.6
Granted	104,086	43.66	6.2	—
Exercised	(147,397)	39.42	—	—
Forfeited/expired	(6,102)	50.05	—	—
Outstanding at December 31, 2018	513,652	45.68	3.6	0.1
Options exercisable at December 31, 2018	303,055	49.15	2.3	—

The total intrinsic value of options exercised in 2018 was $1 million (2017 – nil; 2016 – nil). Based on the Company's closing year-end stock price of $35.13 (2017 – $49.52; 2016 – $39.03), the aggregate intrinsic value of options outstanding and options exercisable is nil.

For the year ended December 31, 2018, stock-based compensation expense recognized in the Company's results of operations was $10 million (2017 – $20 million; 2016 – $16 million) for all of the outstanding awards. Compensation costs not yet recognized amounted to $17 million (2017 – $20 million; 2016 – $17 million) and will be recognized over the remaining service period of approximately 26 months. The aggregate value of liability awards settled in 2018 was $8 million (2017 – $7 million; 2016 – $4 million). The total fair value of equity awards settled in 2018 was $6 million (2017 – $3 million), representing the fair value at the time of settlement. The fair value at the grant date for these settled equity awards was $7 million (2017 – $4 million). Compensation costs for performance awards are based on management's best estimate of the final performance measurement.

CLAWBACK FOR FINANCIAL REPORTING MISCONDUCT

If a participant in the Omnibus Plan knowingly or grossly negligently engages in financial reporting misconduct, then all awards and gains from the exercise of options in the 12 months prior to the date the misleading financial statements were issued as well as any awards that vested based on the misleading financial statements will be disgorged to the Company. In addition, the Company may cancel or reduce, or require a participant to forfeit and disgorge to the Company or reimburse the Company for, any awards granted or vested, and bonus granted or paid, and any gains earned or accrued, due to the exercise, vesting or settlement of awards or sale of any common stock, to the extent permitted or required by, or pursuant to any Company policy implemented as required by applicable law, regulation or stock exchange rule as may from time to time be in effect.

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NOTE 6.

EARNINGS (LOSS) PER COMMON SHARE

The calculation of basic earnings (loss) per common share is based on the weighted average number of Domtar common shares outstanding during the year. The calculation for diluted earnings (loss) per common share recognizes the effect of all potential dilutive common securities.

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

	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
Net earnings (loss)	$ 283	$ (258)	$ 128
Weighted average number of common shares outstanding (millions)	62.9	62.7	62.6
Effect of dilutive securities (millions)	0.2	—	0.1
Weighted average number of diluted common shares outstanding (millions)	63.1	62.7	62.7
Basic net earnings (loss) per common share (in dollars)	$ 4.50	$ (4.11)	$ 2.04
Diluted net earnings (loss) per common share (in dollars)	$ 4.48	$ (4.11)	$ 2.04

The following table provides the securities that could potentially dilute basic earnings (loss) per common share in the future, but were not included in the computation of diluted earnings (loss) per common share because to do so would have been anti-dilutive:

	December 31, 2018	December 31, 2017	December 31, 2016
Options	227,221	312,893	410,978

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NOTE 7.

PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS

DEFINED CONTRIBUTION PLANS

The Company has several defined contribution plans and multiemployer plans. The pension expense under these plans is equal to the Company's contribution. For the year ended December 31, 2018, the related pension expense was $50 million (2017 – $39 million; 2016 – $40 million).

DEFINED BENEFIT PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS

The Company sponsors both contributory and non-contributory U.S. and non-U.S. defined benefit pension plans. Non-unionized employees in Canada joining the Company after January 1, 1998 participate in a defined contribution pension plan. Salaried employees in the U.S. joining the Company after January 1, 2008 participate in a defined contribution pension plan. Unionized and non-union hourly employees in the U.S. that are not grandfathered under the existing defined benefit pension plans, participate in a defined contribution pension plan for future service. The Company also sponsors a number of other post-retirement benefit plans for eligible U.S. and non-U.S. employees; the plans are unfunded and include life insurance programs and medical and dental benefits. The Company also provides supplemental unfunded defined benefit pension plans and supplemental unfunded defined contribution pension plans to certain senior management employees.

Related pension and other post-retirement plan expenses and the corresponding obligations are actuarially determined using management's most probable assumptions.

The Company's pension plan funding policy is to contribute annually the amount required to provide for benefits earned in the year and to fund solvency deficiencies, funding shortfalls and past service obligations over periods not exceeding those permitted by the applicable regulatory authorities. Past service obligations primarily arise from improvements to plan benefits. The other post-retirement benefit plans are not funded and contributions are made annually to cover benefit payments.

The Company expects to contribute a minimum total amount of $12 million in 2019 compared to $57 million in 2018 (2017 – $47 million; 2016 – $31 million) to the pension plans. The Company expects to contribute a minimum total amount of $5 million in 2019 compared to $4 million in 2018 (2017 – $3 million; 2016 – $5 million) to the other post-retirement benefit plans.

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

CHANGE IN PROJECTED BENEFIT OBLIGATION

The following table represents the change in the projected benefit obligation as of December 31, 2018 and December 31, 2017, the measurement date for each year:

	December 31, 2018		December 31, 2017	
	Pension plans $	Other post-retirement benefit plans $	Pension plans $	Other post-retirement benefit plans $
Projected benefit obligation at beginning of year	1,764	76	1,584	90
Service cost for the year	34	1	30	2
Interest expense	53	2	52	4
Plan participants' contributions	6	—	6	—
Actuarial (gain) loss	(80)	(8)	95	(17)
Plan amendments	—	—	1	(5)
Benefits paid	(101)	—	(85)	—
Direct benefit payments	(3)	(4)	(3)	(3)
Settlement	—	—	(2)	—
Effect of foreign currency exchange rate change	(104)	(5)	86	5
Projected benefit obligation at end of year	1,569	62	1,764	76

CHANGE IN FAIR VALUE OF ASSETS

The following table represents the change in the fair value of assets, as of December 31, 2018 and December 31, 2017, reflecting the actual return on plan assets, the contributions and the benefits paid for each year:

	December 31, 2018	December 31, 2017

	Pension plans $	Pension plans $
Fair value of assets at beginning of year	1,765	1,546
Actual return on plan assets	(27)	166
Employer contributions	57	47
Plan participants' contributions	6	6
Benefits paid	(104)	(88)
Settlement	—	(2)
Effect of foreign currency exchange rate change	(109)	90
Fair value of assets at end of year	1,588	1,765

INVESTMENT POLICIES AND STRATEGIES OF THE PLAN ASSETS

The assets of the pension plans are held by a number of independent trustees and are accounted for separately in the Company's pension funds. The investment strategy for the assets in the pension plans is to maintain a diversified portfolio of assets, invested in a prudent manner to maintain the security of funds while maximizing returns within the guidelines provided in the investment policy. Diversification of the pension plans' holdings is maintained in order to reduce the pension plans' annual return variability, reduce market and credit exposure to any single asset and to any single component of the capital markets, reduce exposure to unexpected inflation, enhance the long-term risk-adjusted return potential of the pension plans and reduce funding risk.

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

Over the long-term, the performance of the pension plans is primarily determined by the long-term asset mix decisions. To manage the long-term risk of not having sufficient funds to match the obligations of the pension plans, the Company conducts asset/liability studies. These studies lead to the recommendation and adoption of a long-term asset mix target that sets the expected rate of return and reduces the risk of adverse consequences to the plans from increases in liabilities and decreases in assets. In identifying the asset mix target that would best meet the investment objectives, consideration is given to various factors, including (a) each plan's characteristics, (b) the duration of each plan's liabilities, (c) the solvency and going concern financial position of each plan and their sensitivity to changes in interest rates and inflation, and (d) the long-term return and risk expectations for key asset classes.

The investments of each plan can be done directly through cash investments in equities or bonds or indirectly through derivatives or pooled funds. The use of derivatives must be in accordance with an approved mandate and cannot be used for speculative purposes.

The Company's pension funds are not permitted to directly own any of the Company's shares or debt instruments.

The following table shows the allocation of the plan assets, based on the fair value of the assets held and the target allocation for 2018:

	Target allocation	Percentage of plan assets at December 31, 2018		Percentage of plan assets at December 31, 2017	
Fixed income					
Cash and cash equivalents	0% – 9%	2	%	2	%
Bonds	46% – 56%	52	%	52	%
Insurance contracts	5%	5	%	5	%
Equity					
Canadian Equity	3% – 10%	6	%	6	%
U.S. Equity	8% – 18%	13	%	13	%
International Equity	17% – 27%	22	%	22	%
Total [1]		100	%	100	%

(1) Approximately 77% of the pension plans' assets relate to Canadian plans and 23% relate to U.S. plans.

RECONCILIATION OF FUNDED STATUS TO AMOUNTS RECOGNIZED IN THE CONSOLIDATED BALANCE SHEETS

The following table presents the difference between the fair value of assets and the actuarially determined projected benefit obligation. This difference is also referred to as either the deficit or surplus, as the case may be, or the funded status of the plans. The table further reconciles the amount of the surplus or deficit (funded status) to the net amount recognized in the Consolidated Balance Sheets.

	December 31, 2018		December 31, 2017	
	Pension plans $	Other post-retirement benefit plans $	Pension plans $	Other post-retirement benefit plans $
Projected benefit obligation at end of year	(1,569)	(62)	(1,764)	(76)
Fair value of assets at end of year	1,588	—	1,765	—
Funded status	19	(62)	1	(76)

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

The funded status includes $49 million of projected benefit obligation ($54 million at December 31, 2017) related to supplemental unfunded defined benefit and defined contribution plans.

	December 31, 2018		December 31, 2017	
	Pension plans $	Other post-retirement benefit plans $	Pension plans $	Other post-retirement benefit plans $
Trade and other payables (Note 16)	—	(5)	—	(5)
Other liabilities and deferred credits (Note 19)	(88)	(57)	(130)	(71)
Other assets (Note 14)	107	—	131	—
Net amount recognized in the Consolidated Balance Sheets	19	(62)	1	(76)

The following table presents the pre-tax amounts included in Other comprehensive (loss) income:

	Year ended December 31, 2018		Year ended December 31, 2017		Year ended December 31, 2016	
	Pension plans $	Other post-retirement benefit plans $	Pension plans $	Other post-retirement benefit plans $	Pension plans $	Other post-retirement benefit plans $
Prior service (cost) credit	—	—	(1)	5	—	—
Amortization of prior year service cost	5	—	5	—	5	—
Net (loss) gain	(31)	8	(10)	17	(53)	(2)
Amortization of net actuarial loss (gain)	8	(1)	9	—	6	—
Net amount recognized in other comprehensive	(18)	7	3	22	(42)	(2)

(loss) income (pre-tax)

An estimated loss of $15 million for pension plans and gain of $2 million for other post-retirement benefit plans will be amortized from Accumulated other comprehensive loss into net periodic benefit cost in 2019.

At December 31, 2018, the projected benefit obligation and the fair value of defined benefit plan assets with a projected benefit obligation in excess of fair value of plan assets were $731 million and $643 million, respectively (2017 – $811 million and $680 million, respectively).

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

Components of net periodic benefit cost for pension plans	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Service cost for the year	34	30	32
Interest expense	53	52	50
Expected return on plan assets	(85)	(81)	(80)
Amortization of net actuarial loss	8	9	5
Settlement loss	—	—	1
Amortization of prior year service cost	5	5	5
Net periodic benefit cost	15	15	13

Components of net periodic benefit cost for other post-retirement benefit plans	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Service cost for the year	1	2	2
Interest expense	2	4	4
Amortization of net actuarial gain	(1)	—	—
Net periodic benefit cost	2	6	6

WEIGHTED-AVERAGE ASSUMPTIONS

The Company used the following key assumptions to measure the projected benefit obligation and the net periodic benefit cost. These assumptions are long-term, which is consistent with the nature of employee future benefits.

Pension plans	December 31, 2018	December 31, 2017	December 31, 2016
Projected benefit obligation			
Discount rate	3.8 %	3.5 %	3.8 %

Rate of compensation increase	2.7	%	2.7	%	2.7	%
Net periodic benefit cost						
Discount rate	3.5	%	3.9	%	4.1	%
Rate of compensation increase	2.8	%	2.8	%	2.8	%
Expected long-term rate of return on plan assets	5.2	%	5.3	%	5.3	%

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

The Company used a full yield curve approach to estimate the current service and interest cost components of net periodic benefit cost for Canadian pension plans and U.S. funded pension plans. The estimate of these components is made by applying the specific spot rates along the yield curve used in the determination of the benefit obligation to the relevant projected cash flows.

For the U.S. unfunded pension plan and other post-retirement benefits, given materiality, the current service and interest cost components were estimated using a single weighted-average discount rate derived from the yield curve for each unfunded pension plan or based on each post-retirement plans' projected cash flows. The discount rate for U.S. unfunded plans of 4.2% is obtained by incorporating the plans' expected cash flows in the Mercer Yield Curve.

For Canadian plans, short-term yields to maturity are derived from actual AA rated corporate bond yield data. For longer terms, extrapolated data is used. The extrapolated data are created by adding a term-based spread over long provincial bond yields. For U.S. funded plans, the rates are taken from the Mercer Yield Curve which is based on bonds rated AA by Moody's or Standard & Poor's, excluding callable bonds, bonds of less than a minimum issue size, and certain other bonds. The universe of bonds also includes private placement (traded in reliance on Rule 144A and which are at least two years from issuance), make whole, and foreign corporation (denominated in U.S. dollars) bonds.

Effective January 1, 2019, the Company will use 5.2% (2018 – 5.2%; 2017 – 5.3%) as the expected return on plan assets, which reflects the current view of long-term investment returns. The overall expected long-term rate of return on plan assets is based on management's best estimate of the long-term returns of the major asset classes (cash and cash equivalents, equities, and bonds) weighted by the actual allocation of assets at the measurement date, net of expenses. This rate includes an equity risk premium over government bond returns for equity investments and a value-added premium for the contribution to returns from active management. The sources used to determine management's best estimate of long-term returns are numerous and include country specific bond yields, which may be derived from the market using local bond indices or by analysis of the local bond market, and country-specific inflation and investment market expectations derived from market data and analysts' or governments' expectations, as applicable.

Other post-retirement benefit plans	December 31, 2018		December 31, 2017		December 31, 2016	
Projected benefit obligation						
Discount rate	3.8	%	3.5	%	3.9	%
Rate of compensation increase	2.8	%	2.8	%	2.8	%

Net periodic benefit cost			
Discount rate	3.5 %	3.8 %	4.1 %
Rate of compensation increase	2.7 %	2.8 %	2.8 %

For measurement purposes, a 4.4% weighted average annual rate of increase in the per capita cost of covered health care benefits was assumed for 2018. The rate was assumed to decrease gradually to 3.5% by 2033 and remain at that level thereafter. An increase or decrease of 1% of this rate would have the following impact:

	Increase of 1%	Decrease of 1%
	$	$
Impact on net periodic benefit cost for other post-retirement benefit plans	—	—
Impact on projected benefit obligation	3	(3)

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

FAIR VALUE MEASUREMENT

Fair Value Measurements and Disclosures Topic of FASB ASC 820 establishes a fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value into three levels. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is available and significant to the fair value measurement.

Level 1	Quoted prices in active markets for identical assets or liabilities.
Level 2	Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
Level 3	Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the assets or liabilities.

The following table presents the fair value of the plan assets at December 31, 2018, by asset category:

	Fair Value Measurements at December 31, 2018			
Asset Category	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	$	$	$	$
Cash and short-term investments	68	68	—	—
Canadian provincial government bonds	493	492	1	—
Canadian corporate debt securities	123	100	23	—
U.S. corporate debt securities	37	37	—	—
International corporate debt securities	9	9	—	—
Bond fund (1 & 2)	156	—	156	—
Canadian equities (3)	94	94	—	—
U.S. equities (4)	91	91	—	—
International equities (5)	233	233	—	—
U.S. stock index funds (2 & 6)	200	—	200	—

Insurance contracts [7]	84	—	—	84
Total	1,588	1,124	380	84

[1] This category represents a U.S. actively managed bond fund that is benchmarked to the Barclays Capital Long-term Government/Credit index.

[2] The fair value of these plan assets are classified as Level 2 (inputs that are observable, directly or indirectly) as they are measured based on quoted prices in active markets and can be redeemed at the measurement date or in the near term.

[3] This category represents an active segregated large capitalization Canadian equity portfolio with the ability to purchase small and medium capitalized companies and the Canadian equity portion of an active segregated global equity portfolio.

[4] This category represents U.S. equities held within an active segregated global equity portfolio and an active international equity portfolio.

[5] This category represents an active segregated non-North American multi-capitalization equity portfolio and the non-North American portion of an active segregated global equity portfolio.

[6] This category represents two equity index funds, not actively managed, that track the Russell 3000 index.

[7] This category includes: 1) two group annuity contracts totaling $75 million purchased through an insurance company that are held in the pension plans' name as an asset within the pension plans. These insurance contracts cover pension entitlements associated with specific groups of retired members of the pension plans and 2) $9 million of insurance contracts with a minimum guarantee rate.

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

The following table presents the fair value of the plan assets at December 31, 2017, by asset category:

	Fair Value Measurements at December 31, 2017			
Asset Category	Total $	Quoted Prices in Active Markets for Identical Assets (Level 1) $	Significant Observable Inputs (Level 2) $	Significant Unobservable Inputs (Level 3) $
Cash and short-term investments	79	79	—	—
Asset backed notes	1	—	—	1
Canadian provincial government bonds	566	565	1	—
Canadian corporate debt securities	139	117	22	—
U.S. corporate debt securities	43	43	—	—
International corporate debt securities	2	2	—	—
Bond fund (1 & 2)	152	—	152	—
Canadian equities (3)	111	111	—	—
U.S. equities (4)	103	103	—	—
International equities (5)	252	252	—	—
U.S. stock index funds (2 & 6)	224	—	224	—
Insurance contracts (7)	94	—	—	94
Derivative contracts (8)	(1)	—	(1)	—
Total	1,765	1,272	398	95

(1) This category represents a U.S. actively managed bond fund that is benchmarked to the Barclays Capital Long-term Government/Credit index.

(2) The fair value of these plan assets are classified as Level 2 (inputs that are observable, directly or indirectly) as they are measured based on quoted prices in active markets and can be redeemed at the measurement date or in the near term.

(3) This category represents an active segregated large capitalization Canadian equity portfolio with the ability to purchase small and medium capitalized companies and the Canadian equity portion of an active segregated global equity portfolio.

(4) This category represents U.S. equities held within an active segregated global equity portfolio and an active international equity portfolio.

(5) This category represents an active segregated non-North American multi-capitalization equity portfolio and the non-North American portion of an active segregated global equity portfolio.

(6) This category represents equity two equity index funds, not actively managed, that track the Russell 3000 index.

(7) This category includes: 1) two group annuity contracts totaling $85 million purchased through an insurance company that are held in the pension plans' name as an asset within the pension plans. These insurance contracts cover pension entitlements associated with specific groups of retired members of the pension plans and 2) $9 million of insurance contracts with a minimum guarantee rate.

(8) The fair value of the derivative contracts are classified as Level 2 (inputs that are observable, directly or indirectly) as they are measured using long-term bond indices.

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NOTE 7. PENSION PLANS AND OTHER POST-RETIREMENT BENEFIT PLANS (CONTINUED)

The following table presents changes during the period for Level 3 fair value measurements of plan assets:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)		
	Insurance contracts $	Other $	TOTAL $
Balance at December 31, 2016	84	3	87
Settlements	(5)	(2)	(7)
Return on plan assets	9	—	9
Effect of foreign currency exchange rate change	6	—	6
Balance at December 31, 2017	94	1	95
Settlements	(5)	(1)	(6)
Return on plan assets	2	—	2
Effect of foreign currency exchange rate change	(7)	—	(7)
Balance at December 31, 2018	84	—	84

ESTIMATED FUTURE BENEFIT PAYMENTS FROM THE PLANS

Estimated future benefit payments from the plans for the next 10 years at December 31, 2018 are as follows:

.	Pension plans $	Other post-retirement benefit plans $

2019	103	5
2020	102	5
2021	103	4
2022	103	4
2023	104	4
2024 – 2028	517	21

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NOTE 8.

OTHER OPERATING (INCOME) LOSS, NET

Other operating (income) loss, net is an aggregate of both recurring and occasional loss or income items and, as a result, can fluctuate from year to year. The Company's other operating (income) loss, net includes the following:

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Net gain on sale of property, plant and equipment	(4)	(13)	—
Reversal of contingent consideration	—	(2)	—
Bad debt expense	2	1	—
Environmental provision	5	3	2
Foreign exchange (gain) loss	(2)	1	6
Other	(1)	(4)	(4)
Other operating (income) loss, net	—	(14)	4

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NOTE 9.

INTEREST EXPENSE, NET

The following table presents the components of interest expense, net:

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Interest on long-term debt [1]	56	59	59
Interest on receivables securitization	1	2	2
Interest on withdrawal liabilities for multiemployer plans	2	3	3
Amortization of debt issuance costs and other	3	2	2
	62	66	66

[1] The Company capitalized $1 million of interest expense in 2018 (2017 – $1 million; 2016 – $5 million).

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NOTE 10.

INCOME TAXES

The Company's earnings (loss) before income taxes by taxing jurisdiction were:

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
U.S. earnings (loss)	216	(209)	69
Foreign earnings (loss)	126	(174)	88
Earnings (loss) before income taxes	342	(383)	157

Provisions for income taxes include the following:

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
U.S. Federal and State:			
Current	32	73	10
Deferred	(6)	(208)	1
Foreign:			
Current	12	9	10
Deferred	19	1	8
Income tax expense (benefit)	57	(125)	29

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NOTE 10. INCOME TAXES (CONTINUED)

The Company's provision for income taxes differs from the amounts computed by applying the statutory income tax rate of 21% (35% for December 31, 2017 and December 31, 2016) to earnings (loss) before income taxes due to the following:

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
U.S. federal statutory income tax	72	(134)	55
Reconciling Items:			
State and local income taxes, net of federal income tax benefit	8	2	3
Foreign income tax rate differential	1	(16)	(14)
Tax credits and special deductions	(19)	(24)	(18)
Goodwill impairment	—	200	—
Tax rate changes	(9)	(188)	—
Deemed mandatory repatriation tax	(7)	46	—
Uncertain tax positions	(4)	(6)	2
U.S. manufacturing deduction	—	(4)	(2)
Deferred taxes on foreign earnings	10	—	—
Net operating loss cancellation	9	—	—
Valuation allowance on deferred tax assets	(8)	3	(1)
Other	4	(4)	4
Income tax expense (benefit)	57	(125)	29

During 2018, the Company recorded $19 million of tax credits, mainly research and experimentation credits, which significantly impacted the effective tax rate. The effective tax rate was also impacted by the cancellation of $9 million, after-tax, of net operating losses in a foreign jurisdiction. This was offset by the reversal of $9 million of valuation allowance on these same net operating losses. Additionally, a valuation allowance of $1 million was recorded on new operating losses in 2018 for a net benefit pertaining to valuation allowance movements of $8 million.

On December 22, 2017, the U.S. Tax Reform was signed into law. The U.S. Tax Reform significantly changed U.S. tax law for businesses by, among other things, lowering the maximum federal corporate income tax rate from 35% to 21% effective January 1, 2018, implementing a territorial tax system, and imposing a one-time deemed repatriation tax on accumulated foreign earnings. As a result of the U.S. Tax Reform, the Company recorded a net tax benefit of $140 million in the fourth quarter of 2017 when the legislation was enacted. This consisted of a provisional tax benefit of $186 million relating to the revaluation of the Company's ending net deferred tax liabilities and a provisional expense of $46 million related to the deemed repatriation tax. Additionally, Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address the application in situations when a registrant does not have the necessary information available, prepared, or analyzed in reasonable detail to complete the accounting for certain income tax effects of the U.S. Tax Reform. December 22, 2018 marked the end of the measurement period for purposes of SAB 118. As such, the Company completed its analysis, including currently available legislative updates, and recorded an additional tax benefit of $13 million for the year ended December 31, 2018. Of this benefit, $7 million related to adjustments to the deemed mandatory repatriation tax and $6 million related to the revaluation of the Company's net deferred tax liabilities. The $6 million benefit for the revaluation of the net deferred tax liabilities is included in the "Tax rate changes" above, along with $3 million of additional tax benefits relating to 2018 law changes in Sweden and various U.S. states.

As a result of the deemed mandatory repatriation tax requirement of the U.S. Tax Reform, the Company has taxed its undistributed foreign earnings as of December 31, 2017, at reduced tax rates. After completing its evaluation of the U.S. Tax Reform's impact on its business operations, the Company has determined that it is no longer indefinitely reinvested in these undistributed foreign earnings as well as foreign earnings after December 31, 2017. As such, as of December 31, 2018, the Company has recorded a deferred tax liability of $10 million for foreign withholding tax and various state income taxes associated with future repatriation of these earnings. This $10 million tax expense impacted the effective tax rate for 2018.

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NOTE 10. INCOME TAXES (CONTINUED)

During 2017, the Company recorded a goodwill impairment of $578 million with minimal tax benefit which impacted the effective tax rate by $200 million. The effective tax rate for 2017 was also significantly impacted by the Company's foreign operations being taxed at lower statutory tax rates and by the Company recording $24 million of current tax credits, mainly research and experimentation credits.

On December 22, 2017, the U.S. Tax Reform was signed into law. The U.S. Tax Reform significantly changed U.S. tax law for businesses by, among other things, lowering the maximum federal corporate income tax rate from 35% to 21% effective January 1, 2018, implementing a territorial tax system, and imposing a one-time deemed repatriation tax on accumulated foreign earnings. As a result of the corporate tax rate reduction, the Company revalued its ending net deferred tax liabilities, and recognized a provisional tax benefit of $186 million in the Company's Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss) for the year ended December 31, 2017. This, combined with a $2 million tax benefit from other changes in law in certain U.S. states earlier in the year, had a significant impact on the effective tax rate for 2017.

On December 22, 2017, the SEC staff issued SAB 118 to address the application in situations when a registrant does not have the necessary information available, prepared, or analyzed in reasonable detail to complete the accounting for certain income tax effects of the U.S. Tax Reform. SAB 118 provides guidance which allows companies to use a measurement period, similar to that used in business combinations, to account for the impacts of the U.S. Tax Reform. The U.S. Tax Reform provides for a mandatory one-time deemed repatriation tax on the Company's undistributed foreign earnings and profits. The Company recorded a provisional repatriation tax amount of $46 million, which it will elect to pay over eight years, and which impacted the 2017 tax rate.

During 2016, the Company recorded $18 million of tax credits, mainly research and experimentation credits, which significantly impacted the effective tax rate. The effective tax rate for 2016 was also significantly impacted by the Company's foreign operations being taxed at lower statutory tax rates.

Deferred tax assets and liabilities are based on tax rates that are expected to be in effect in future periods when deferred items are expected to reverse. Changes in tax rates or tax laws affect the expected future benefit or expense. The effect of such changes that occurred during each of the last three fiscal years is included in "Tax rate changes" disclosed under the effective income tax rate reconciliation shown above.

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NOTE 10. INCOME TAXES (CONTINUED)

DEFERRED TAX ASSETS AND LIABILITIES

The tax effects of significant temporary differences representing deferred tax assets and liabilities at December 31, 2018 and December 31, 2017 are comprised of the following:

	December 31, 2018 $	December 31, 2017 $
Accounting provisions	38	36
Net operating loss carryforwards and other deductions	36	43
Pension and other employee future benefit plans	22	31
Inventory	10	10
Tax credits	21	36
Gross deferred tax assets	127	156
Valuation allowance	(16)	(25)
Net deferred tax assets	111	131
Property, plant and equipment	(422)	(436)
Intangible assets	(122)	(131)
Other	(10)	(16)
Total deferred tax liabilities	(554)	(583)
Net deferred tax liabilities	(443)	(452)
Included in:		
Other assets (Note 14)	1	2
Deferred income taxes and other	(444)	(454)
Total	(443)	(452)

At December 31, 2018, the Company had less than $1 million of federal net operating loss carryforwards remaining which expire in 2032. These U.S. federal net operating losses are subject to annual limitations under Section 382 of the Internal Revenue Code of 1986, as amended (the "Code"), that can vary from year to year. The Company also has other foreign net operating losses and deduction limitations of $176 million, all except $3 million of which may be carried forward indefinitely. In 2027, a small amount of the $3 million of foreign net operating losses will begin to expire.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during periods in which temporary differences become deductible.

The Company evaluates the realization of deferred tax assets on a quarterly basis. Evaluating the need for an amount of a valuation allowance for deferred tax assets often requires significant judgment. All available evidence, both positive and negative, is considered when determining whether, based on the weight of that evidence, a valuation allowance is needed. Specifically, the Company evaluated the following items:

- Historical income / (losses) – particularly the most recent three-year period
- Reversals of future taxable temporary differences
- Projected future income / (losses)
- Tax planning strategies
- Divestitures

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NOTE 10. INCOME TAXES (CONTINUED)

Management believes that it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets, with the exception of certain state credits for which a valuation allowance of $6 million exists at December 31, 2018, and certain foreign loss carryforwards for which a valuation allowance of $10 million exists at December 31, 2018. Of this amount, $(8) million favorably impacted tax expense and the effective tax rate for 2018 (2017 – $3 million; 2016 – $(1) million).

As of December 31, 2018, the Company has recorded a deferred tax liability of $10 million for foreign withholding tax and various state income taxes associated with the repatriation of earnings subject to the repatriation tax as well as future repatriation of its unremitted foreign earnings. The Company has not provided for deferred taxes on outside basis differences in its investments in its foreign subsidiaries that are unrelated to unremitted earnings as it estimates that the deferred tax liability recorded in 2018, in combination with the repatriation tax amount, covers all tax liabilities with foreign investments to date.

The U.S. Tax Reform also includes a base erosion provision for GILTI. Beginning in 2018, the GILTI provisions require the Company to include in its U.S. income tax return, earnings of foreign subsidiaries that are in excess of an allowable return on the tangible assets of the foreign subsidiaries. The Company is required to make an accounting policy election to either (1) treat taxes due related to GILTI as a current period expense when incurred or (2) factor such amounts into the measurement of deferred taxes. The Company has elected to account for any taxes associated with GILTI as a period cost.

ACCOUNTING FOR UNCERTAINTY IN INCOME TAXES

At December 31, 2018, the Company had gross unrecognized tax benefits of approximately $32 million ($37 million and $43 million for 2017 and 2016, respectively). If recognized in 2019, these tax benefits would impact the effective tax rate. These amounts represent the gross amount of exposure in individual jurisdictions and do not reflect any additional benefits expected to be realized if such positions were sustained, such as federal deduction that could be realized if an unrecognized state deduction was not sustained.

	December 31, 2018	December 31, 2017	December 31, 2016
	$	$	$
Balance at beginning of year	37	43	41
Additions based on tax positions related to current year	3	3	3

Additions for tax positions of prior years	4	4	3
Reductions for tax positions of prior years	—	—	(2)
Reductions related to settlements with taxing authorities	—	(1)	—
Expirations of statutes of limitations	(12)	(13)	(3)
Interest	1	1	1
Foreign exchange impact	(1)	—	—
Balance at end of year	32	37	43

The Company recorded $1 million of accrued interest associated with unrecognized tax benefits for the period ending December 31, 2018 ($1 million and $1 million for 2017 and 2016, respectively). The Company recognizes accrued interest and penalties, if any, related to unrecognized tax benefits as a component of tax expense. The Company believes it is reasonably possible that up to $6 million of its unrecognized tax benefits may be recognized by December 31, 2019, which could significantly impact the effective tax rate. However, the amount and timing of the recognition of these benefits is subject to some uncertainty.

The major jurisdictions where the Company and its subsidiaries will file tax returns for 2018, in addition to filing one consolidated U.S. federal income tax return, are Canada, Sweden and Spain. The Company and its subsidiaries will also file returns in various other countries in Europe and Asia as well as various U.S. states and Canadian provinces. At December 31, 2018, the Company's subsidiaries are subject to foreign federal income tax examinations for the tax years 2008 through 2017, with federal years prior to 2015 being closed from a cash tax liability standpoint in the U.S., but the loss carryforwards can be adjusted in any open year where the loss has been utilized. The Company does not anticipate that adjustments stemming from these audits would result in a significant change to the results of its operations and financial condition.

DOMTAR CORPORATION

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NOTE 11.

INVENTORIES

The following table presents the components of inventories:

	December 31, 2018	December 31, 2017
	$	$
Work in process and finished goods	410	399
Raw materials	126	135
Operating and maintenance supplies	226	223
	762	757

DOMTAR CORPORATION

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NOTE 12.

PROPERTY, PLANT AND EQUIPMENT

The following table presents the components of property, plant and equipment:

	Range of useful lives (in years)	December 31, 2018	December 31, 2017
		$	$
Machinery and equipment	3 – 20	7,655	7,674
Buildings and improvements	10 – 40	1,043	1,059
Timberlands	(1)	193	207
Assets under construction	—	131	104
		9,022	9,044
Less: Accumulated depreciation		(6,417)	(6,279)
		2,605	2,765

(1) Amortization is calculated using the unit of production method.

Depreciation expense related to property, plant and equipment for the year ended December 31, 2018 was $289 million (2017 – $302 million; 2016 – $329 million).

DOMTAR CORPORATION

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NOTE 13.

INTANGIBLE ASSETS

The following table presents the components of intangible assets:

	Estimated useful lives (in years)	December 31, 2018			December 31, 2017		
		Gross carrying amount	Accumulated amortization	Net	Gross carrying amount	Accumulated amortization	Net
Definite-lived intangible assets subject to amortization		$	$	$	$	$	$
Water rights	40	3	(1)	2	3	(1)	2
Customer relationships	10 – 40	384	(94)	290	392	(79)	313
Technology	7 – 20	8	(4)	4	8	(4)	4
Non-Compete	9	1	(1)	—	1	(1)	—
License rights	12	28	(13)	15	29	(11)	18
		424	(113)	311	433	(96)	337
Indefinite-lived intangible assets not subject to amortization							
Water rights		4	—	4	4	—	4
Trade names		238	—	238	245	—	245
License rights		6	—	6	6	—	6
Catalog rights		38	—	38	41	—	41
Total		710	(113)	597	729	(96)	633

Amortization expense related to intangible assets for the year ended December 31, 2018 was $19 million ($19 million in 2017 and 2016, respectively).

Amortization expense for the next five years related to intangible assets is expected to be as follows:

	2019 $	2020 $	2021 $	2022 $	2023 $
Amortization expense related to intangible assets	21	21	21	21	20

The Company performed its annual impairment test on its indefinite-lived intangible assets at October 1, 2018, 2017 and 2016, using a quantitative approach, except for the license rights and water rights, where the Company used a qualitative approach, and determined that the estimated fair values of its indefinite-lived intangible assets exceeded their carrying amounts. No impairment charge was recorded for indefinite-lived intangible assets during 2018, 2017 or 2016.

DOMTAR CORPORATION

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NOTE 14.

OTHER ASSETS

The following table presents the components of other assets:

	December 31, 2018 $	December 31, 2017 $
Pension asset - defined benefit pension plans (Note 7)	107	131
Investment tax credits receivable	5	7
Unamortized debt issuance costs	4	4
Deferred income tax assets (Note 10)	1	2
Derivative financial instruments (Note 22)	—	5
Investments and advances	6	—
Other	11	8
	134	157

DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 15.

CLOSURE AND RESTRUCTURING COSTS AND LIABILITY

In the fourth quarter of 2016, as a result of a revision in the Company's estimated withdrawal liability for U.S. multiemployer plans, the Company recorded a credit of $4 million in Closure and restructuring costs on the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss). At December 31, 2018, the total provision for the withdrawal liabilities was $47 million.

Waco, Texas facility

On November 1, 2018, the Company announced a margin improvement within the Personal Care Division. As part of this plan, the Board of Directors approved the permanent closure of its Waco, Texas Personal Care manufacturing and distribution facility, the relocation of certain of its manufacturing assets and a workforce reduction across the division. The Waco, Texas facility is expected to cease operations in the third quarter of 2019.

The Company recorded $7 million for the year ended December 31, 2018 of accelerated depreciation under Impairment of property, plant and equipment and goodwill on the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss). During the fourth quarter of 2018, the Company also recorded a $4 million write-down of inventory, $3 million of severance and termination costs, and $1 million of other costs under Closure and restructuring costs.

Plymouth, North Carolina mill

On September 23, 2016, the Company announced a plan to optimize fluff pulp manufacturing at the Plymouth, North Carolina mill. The restructuring, which was completed in 2018, included the permanent closure of a pulp dryer and idling of assets, in addition to a workforce reduction of approximately 100 positions. The streamlining process also right-sized the mill to an annualized production target of approximately 380,000 metric tons of fluff pulp. The Company recorded $5 million of severance and termination costs under Closure and restructuring costs during the third quarter of 2016.

Ashdown, Arkansas mill

On December 10, 2014, the Company announced a project to convert a paper machine at its Ashdown, Arkansas mill to a high quality fluff pulp line used in absorbent applications such as baby diapers, feminine hygiene and adult incontinence products. The Company also invested in a pulp bale line that will provide flexibility to manufacture papergrade softwood pulp, contingent on market conditions. The conversion work commenced during the second quarter of 2016 and the production of bale softwood pulp began in the third quarter of 2016. The project resulted in the permanent reduction of 364,000 short tons of annual uncoated freesheet production capacity on March 31, 2016.

The Company recorded $29 million for the year ended December 31, 2016, of accelerated depreciation under Impairment of property, plant and equipment and goodwill on the Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss). During 2016, the Company also recorded $26 million of costs related to the fluff pulp conversion outage and $1 million of severance and termination costs under Closure and restructuring costs.

Other costs

During 2018, there were no other costs related to previous and ongoing closures and restructuring (severance and termination costs of $2 million and $3 million in 2017 and 2016, respectively, and pension settlement costs of nil and $1 million in 2017 and 2016, respectively).

DOMTAR CORPORATION

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NOTE 15. CLOSURE AND RESTRUCTURING COSTS AND LIABILITY (CONTINUED)

The following tables provide the components of closure and restructuring costs by segment:

	Year ended December 31, 2018		
	Paper	Pulp and Personal Care	Total
	$	$	$
Severance and termination costs	—	3	3
Inventory write-down	—	4	4
Other	—	1	1
Closure and restructuring costs	—	8	8

	Year ended December 31, 2017		
	Paper	Pulp and Personal Care	Total
	$	$	$
Severance and termination costs	—	2	2
Closure and restructuring costs	—	2	2

	Year Ended December 31, 2016		
	Paper	Pulp and Personal Care	Total
	$	$	$

Severance and termination costs	8	1	9
Pension settlement and withdrawal liability	(3)	—	(3)
Fluff pulp conversion outage	26	—	26
Closure and restructuring costs	31	1	32

The following table provides the activity in the closure and restructuring liability:

	December 31, 2018 $	December 31, 2017 $
Balance at beginning of year	7	7
Additions	4	2
Payments	(5)	(2)
Balance at end of year	6	7

The $6 million provision is comprised of $5 million of severance and termination costs, of which $3 million and $2 million relate to the Pulp and Paper segment and Personal Care segment, respectively, and $1 million of other costs which relate to the Personal Care segment.

Closure and restructuring costs are based on management's best estimates at December 31, 2018. Actual costs may differ from these estimates due to subsequent developments such as the results of environmental studies, the ability to find a buyer for assets set to be dismantled and demolished and other business developments. As such, additional costs and further impairment charges may be required in future periods.

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NOTE 16.

TRADE AND OTHER PAYABLES

The following table presents the components of trade and other payables:

	December 31, 2018 $	December 31, 2017 $
Trade payables	404	382
Payroll-related accruals	173	164
Accrued interest	16	16
Payables on capital projects	21	11
Rebate accruals	64	72
Liability - pension and other post-retirement benefit plans (Note 7)	5	5
Liability - multiemployer plan withdrawal	2	2
Provision for environment and other asset retirement obligations (Note 21)	10	13
Closure and restructuring costs liability (Note 15)	6	7
Derivative financial instruments (Note 22)	21	7
Dividends payable (Note 20)	27	26
Stock-based compensation - liability awards (Note 22)	6	6
Other	2	5
	757	716

DOMTAR CORPORATION

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NOTE 17.

CHANGES IN ACCUMULATED OTHER COMPREHENSIVE LOSS BY COMPONENT

The following table presents the changes in Accumulated other comprehensive loss by component[1] for the period ended December 31, 2018 and 2017.

	Net derivative gains (losses) on cash flow hedges	Pension items[2]	Post-retirement benefit items[2]	Foreign currency items	Total
	$	$	$	$	$
Balance at December 31, 2016	11	(221)	(11)	(278)	(499)
Natural gas swap contracts	(5)	N/A	N/A	N/A	(5)
Currency options	11	N/A	N/A	N/A	11
Net (gain) loss	N/A	(6)	17	N/A	11
Foreign currency items	N/A	N/A	N/A	146	146
Other comprehensive income (loss) before reclassifications	6	(6)	17	146	163
Amounts reclassified from Accumulated other comprehensive loss	(9)	9	—	—	—
Net current period other comprehensive (loss) income	(3)	3	17	146	163
Balance at December 31, 2017	8	(218)	6	(132)	(336)
Natural gas swap contracts	1	N/A	N/A	N/A	1
Currency options	(12)	N/A	N/A	N/A	(12)
Foreign exchange forward contracts	(19)	N/A	N/A	N/A	(19)
Net (gain) loss	N/A	(23)	6	N/A	(17)
Foreign currency items	N/A	N/A	N/A	(91)	(91)
Other comprehensive (loss) income before	(30)	(23)	6	(91)	(138)

reclassifications					
Amounts reclassified from Accumulated other comprehensive loss	(2)	10	(1)	—	7
Net current period other comprehensive (loss) income	(32)	(13)	5	(91)	(131)
Balance at December 31, 2018	(24)	(231)	11	(223)	(467)

(1) All amounts are after tax. Amounts in parentheses indicate losses.
(2) The projected benefit obligation is actuarially determined on an annual basis as of December 31.

DOMTAR CORPORATION

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NOTE 17. CHANGES IN ACCUMULATED OTHER COMPREHENSIVE LOSS BY COMPONENT (CONTINUED)

The following table presents reclassifications out of Accumulated other comprehensive loss:

Details about Accumulated other comprehensive loss components	Amount reclassified from Accumulated other comprehensive loss[1]		
	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
	$	$	$
Net derivative (losses) gains on cash flow hedge			
Natural gas swap contracts [2]	(2)	—	12
Currency options and forwards [2]	(1)	(14)	12
Total before tax	(3)	(14)	24
Tax benefit (expense)	1	5	(10)
Net of tax	(2)	(9)	14
Amortization of defined benefit pension items			
Amortization of net actuarial loss [3]	8	9	6
Amortization of prior year service cost [3]	5	5	5
Total before tax	13	14	11
Tax expense	(3)	(5)	(4)
Net of tax	10	9	7
Amortization of other post-retirement benefit items			
Amortization of net actuarial gain [3]	(1)	—	—
Total before tax	(1)	—	—
Tax expense	—	—	—
Net of tax	(1)	—	—

(1) Amounts in parentheses indicate losses.
(2) These amounts are included in Cost of sales in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).
(3) These amounts are included in the computation of net periodic benefit cost (see Note 7 "Pension Plans and Other Post-Retirement Benefit Plans" for more details).

DOMTAR CORPORATION

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NOTE 18.

LONG-TERM DEBT

	Maturity	Par Amount $	Currency	December 31, 2018 $	December 31, 2017 $
Unsecured notes					
4.4% Notes	2022	300	US	300	300
6.25% Notes	2042	250	US	249	249
6.75% Notes	2044	250	US	249	249
Revolving Credit Facility	2023	—	US	—	—
Term Loan	2025	300	US	—	300
Securitization	2021	50	US	50	25
Capital lease obligations and other	2019 - 2032			11	14
				859	1,137
Less: Unamortized debt issuance costs				5	7
Less: Due within one year				1	1
				853	1,129

Principal long-term debt repayments, including capital lease obligations, in each of the next five years will amount to:

	Long-term debt $	Capital leases and other $
2019	—	2
2020	—	2

2021	50	2
2022	300	1
2023	—	1
Thereafter	500	7
	850	15
Less: Amounts representing interest	—	4
Total payments	850	11

UNSECURED NOTES

The Company’s 10.75% Notes, in the aggregate principal amount of $63 million, matured on June 1, 2017.

The Company’s 9.5% Notes, in the aggregate principal amount of $39 million, matured on August 1, 2016.

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NOTE 18. LONG-TERM DEBT (CONTINUED)

REVOLVING CREDIT FACILITY

In August 2018, the Company amended and restated its $700 million unsecured revolving credit facility (the "Credit Agreement") with certain domestic and foreign banks. The amendment extended the Credit Agreement's maturity date from August 18, 2021 to August 22, 2023. The maturity date of the facility may be extended by one year and the lender commitments may be increased by up to $400 million, subject to lender approval and customary requirements.

Borrowings by the Company under the Credit Agreement are guaranteed by its significant domestic subsidiaries. Borrowings by certain foreign subsidiaries under the Credit Agreement are guaranteed by the Company, the Company's significant domestic subsidiaries and certain of the Company's significant foreign subsidiaries.

Borrowings under the Credit Agreement bear interest at LIBOR, EURIBOR, Canadian bankers' acceptance or prime rate, as applicable, plus a margin linked to the Company's credit rating. In addition, the Company pays facility fees quarterly at rates dependent on the Company's credit ratings.

The Credit Agreement contains customary covenants and events of default for transactions of this type, including two financial covenants: (i) an interest coverage ratio, as defined in the Credit Agreement, that must be maintained at a level of not less than 3 to 1 and (ii) a leverage ratio, as defined in the Credit Agreement, that must be maintained at a level of not greater than 3.75 to 1 (or 4.00 to 1 upon the occurrence of certain qualifying material acquisitions). At December 31, 2018, the Company was in compliance with these financial covenants, and there were no borrowings (December 31, 2017 – nil).

TERM LOAN

In the third quarter of 2015, a wholly-owned subsidiary of Domtar borrowed $300 million under an unsecured 10 year Term Loan Agreement with certain domestic banks.

In the fourth quarter of 2018, the Term Loan was fully repaid.

RECEIVABLES SECURITIZATION

The Company has a $150 million receivables securitization facility. This facility was amended in November 2018 to extend the maturity date from March 2019 to November 2021. This facility provides additional liquidity to the Company to fund its operations or issue letters of credit. The costs under the program vary based on changes in interest rates and amounts utilized.

Sales of receivables under this program are accounted for as secured borrowings. The program consists of the ongoing sale of most of the receivables of its domestic subsidiaries to a bankruptcy remote consolidated subsidiary which, in turn, transfers a senior beneficial interest in them to a special purpose entity managed by a financial institution for multiple sellers of receivables to support borrowings or the issue of letters of credit by the Company.

The program contains certain termination events, which include, but are not limited to, matters related to receivable performance, certain defaults occurring under the Credit Agreement, or the failure by Domtar to satisfy material obligations.

At December 31, 2018, $50 million was borrowed and $52 million of letters of credit were outstanding under this facility (2017 – $25 million and $50 million, respectively).

In 2018, a net charge of $1 million (2017 – $2 million; 2016 – $2 million) resulted from the program described above and was included in Interest expense, net in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss).

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NOTE 19.

OTHER LIABILITIES AND DEFERRED CREDITS

The following table presents the components of other liabilities and deferred credits:

.	December 31, 2018 $	December 31, 2017 $
Liability - other post-retirement benefit plans (Note 7)	57	71
Pension liability - defined benefit pension plans (Note 7)	88	130
Pension liability - multiemployer plan withdrawal	45	47
Long-term income taxes payable	9	42
Provision for environmental and asset retirement obligations (Note 21)	27	31
Stock-based compensation - liability awards (Note 22)	14	20
Derivative financial instruments (Note 22)	16	5
Other	19	22
	275	368

ASSET RETIREMENT OBLIGATIONS

The asset retirement obligations are principally linked to landfill capping obligations and demolition of certain abandoned buildings. At December 31, 2018, Domtar estimated the net present value of its asset retirement obligations to be $12 million (2017 – $15 million); the present value is based on probability weighted undiscounted cash outflows of $59 million (2017 – $58 million). The majority of the asset retirement obligations are estimated to be settled prior to December 31, 2058. Domtar’s credit adjusted risk-free rates were used to calculate the net present value of the asset retirement obligations. The rates used vary between 4.7% and 12.0%, based on the prevailing rate at the moment of recognition of the liability and on its settlement period.

The following table reconciles Domtar’s asset retirement obligations:

	December 31, 2018 $	December 31, 2017 $
Asset retirement obligations, beginning of year	15	14
Asset retirement obligation payments	(3)	—
Accretion expense	1	1
Effect of foreign currency exchange rate change	(1)	—
Asset retirement obligations, end of year	12	15

DOMTAR CORPORATION

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NOTE 20.

SHAREHOLDERS' EQUITY

During 2018, the Company declared four quarterly dividends of $0.435 per share, to holders of the Company's common stock. Dividends of $27 million, $28 million, $27 million and $27 million were paid on April 16, 2018, July 16, 2018, October 15, 2018 and January 15, 2019, respectively, to shareholders of record as of April 2, 2018, July 3, 2018, October 2, 2018 and January 2, 2019, respectively.

During 2017, the Company declared four quarterly dividends of $0.415 per share, to holders of the Company's common stock. Dividends of $26 million were paid on April 17, 2017, July 17, 2017, October 16, 2017 and January 15, 2018, respectively, to shareholders of record as of April 3, 2017, July 3, 2017, October 2, 2017 and January 2, 2018, respectively.

On February 19, 2019, the Company's Board of Directors approved a quarterly dividend of $0.435 per share, to be paid to holders of the Company's common stock. This dividend is to be paid on April 15, 2019 to shareholders of record on April 2, 2019.

STOCK REPURCHASE PROGRAM

The Company's Board of Directors has authorized a stock repurchase program ("the Program") of up to $1.3 billion. Under the Program, the Company is authorized to repurchase, from time to time, shares of its outstanding common stock on the open market or in privately negotiated transactions. The timing and amount of stock repurchases will depend on a variety of factors, including the market conditions as well as corporate and regulatory considerations. The Program may be suspended, modified or discontinued at any time, and the Company has no obligation to repurchase any amount of its common stock under the Program. The Program has no set expiration date. The Company repurchases its common stock in part to reduce the dilutive effects of stock options and awards, and to improve shareholders' returns.

The Company makes open market purchases of its common stock using general corporate funds. Additionally, the Company may enter into structured stock repurchase agreements with large financial institutions using general corporate funds in order to lower the average cost to acquire shares. The agreements would require the Company to make up-front payments to the counterparty financial institutions, which would result in either the receipt of stock at the beginning of the term of the agreements followed by a share adjustment at the maturity of the agreements, or the receipt of either stock or cash at the maturity of the agreements, depending upon the price of the stock.

During 2018 and 2017, there were no shares repurchased under the Program.

Since the inception of the Program, the Company repurchased 24,853,827 shares at an average price of $39.33 for a total cost of $977 million. All shares repurchased are recorded as Treasury stock on the Consolidated Balance Sheets under the par value method at $0.01 per share.

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NOTE 20. SHAREHOLDERS' EQUITY (CONTINUED)

The authorized stated capital consists of the following:

PREFERRED SHARES

The Company is authorized to issue 20 million preferred shares, par value $0.01 per share. The Board of Directors of the Company will determine the voting powers (if any) of the shares, and the preferences and relative, participating, optional or other special rights, if any, and any qualifications, limitations or restrictions thereof, of the shares at the time of issuance. No preferred shares were outstanding at December 31, 2018 or December 31, 2017.

COMMON STOCK

The Company is authorized to issue two billion shares of common stock, par value $0.01 per share. Holders of the Company's common stock are entitled to one vote per share.

The changes in the number of outstanding common stock and their aggregate stated value during the years ended December 31, 2018 and December 31, 2017, were as follows:

Common stock	December 31, 2018 Number of shares	$	December 31, 2017 Number of shares	$
Balance at beginning of year	62,695,685	1	62,588,837	1
Shares issued				
Treasury stock	218,884	—	106,848	—
Balance at end of year	62,914,569	1	62,695,685	1

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DOMTAR CORPORATION

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NOTE 21.

COMMITMENTS AND CONTINGENCIES

ENVIRONMENTAL MATTERS

The Company is subject to environmental laws and regulations enacted by federal, provincial, state and local authorities. The Company may also incur substantial costs in relation to enforcement actions (including orders requiring corrective measures, installation of pollution control equipment or other remedial actions) as a result of violations of, or liabilities under, environmental laws and regulations applicable to its past and present properties. The Company's ongoing efforts to identify potential environmental concerns that may be associated with such properties may result in additional environmental costs and liabilities which cannot be reasonably estimated at this time.

In 2018, the Company's operating expenses for environmental matters amounted to $68 million (2017 – $67 million; 2016 – $65 million).

The Company made capital expenditures for environmental matters of $8 million in 2018 (2017– $2 million; 2016 – $4 million).

In connection with contamination of a site bordering Burrard Inlet in North Vancouver, on February 16, 2010, the government of British Columbia issued a Remediation Order to Seaspan International Ltd. and the Company, in order to define and implement an action plan to address soil, sediment and groundwater issues. Construction began in January 2017 and is expected to be completed in 2019. The Company previously recorded an environmental reserve to address its estimated exposure. The possible cost in excess of the reserve is not considered to be material for this matter.

The following table reflects changes in the reserve for environmental remediation and asset retirement obligations:

	December 31, 2018 $	December 31, 2017 $
Balance at beginning of year	44	50
Additions and other changes	4	4
Environmental spending	(9)	(12)
Effect of foreign currency exchange rate change	(2)	2

Balance at end of year [1]	37	44

[1] At December 31, 2018, $10 million is shown in Trade and other payables (see Note 16) and $27 million is shown in Other liabilities and deferred credits (see Note 19).

At December 31, 2018, anticipated undiscounted payments in each of the next five years are as follows:

	2019 $	2020 $	2021 $	2022 $	2023 $	Thereafter $	Total $
Environmental provision and asset retirement obligations	10	1	2	2	2	67	84

The U.S. Environmental Protection Agency (the "EPA") and/or various state agencies have notified the Company that it may be a potentially responsible party under the Comprehensive Environmental Response Compensation and Liability Act, commonly known as "Superfund," and similar state laws with respect to other hazardous waste sites as to which no proceedings have been instituted against the Company. The Company continues to take remedial action under its Care and Control Program at its former wood preserving sites, and at a number of former operating sites due to possible soil, sediment or groundwater contamination.

DOMTAR CORPORATION

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NOTE 21. COMMITMENTS AND CONTINGENCIES (CONTINUED)

Climate change regulation

Various national and local laws and regulations relating to climate change have been established or are emerging in jurisdictions where the Company currently has, or may have in the future, manufacturing facilities or investments.

The EPA Clean Power Plan regulation is being litigated and has been stayed. The EPA has proposed to repeal and replace the Clean Power Plan. The proposed replacement rule, entitled the "Affordable Clean Energy" ("ACE") rule, was published on August 31, 2018, and the EPA plans to finalize the rule in the first part of 2019. Regardless of the outcome for the Clean Power Plan and ACE, the Company does not expect to be disproportionately affected compared with other pulp and paper producers located in the states where the Company operates.

The province of Quebec has a greenhouse gases ("GHG") cap-and-trade system with reduction targets. British Columbia has a carbon tax that applies to the purchase of fossil fuels within the province. The Company does not expect its facilities to be disproportionately affected by these measures compared with other pulp and paper producers located in these jurisdictions.

In October 2018, the Government of Canada proposed to establish a federal carbon pricing system in provinces that do not already impose a cost on carbon emissions. This system is expected to become effective in 2019. The Government of Canada is seeking to impose a carbon pricing program for regulating GHG emissions in Ontario, where there is not currently a provincial program. This effort may result in the determination of additional environmental costs which cannot be reasonably estimated at this time.

CONTINGENCIES

In the normal course of operations, the Company becomes involved in various legal actions mostly related to contract disputes, patent infringements, environmental and product warranty claims, and labor issues. While the final outcome with respect to actions outstanding or pending at December 31, 2018, cannot be predicted with certainty, it is management's opinion that their resolution will not have a material adverse effect on the Company's financial position, results of operations or cash flows.

Spanish Competition Investigation

On October 15, 2015, the Competition Directorate of Spain's National Commission of Markets and Competition ("CNMC") filed a Statement of Objections against a number of industry participants alleging the existence of a series of agreements between manufacturers, distributors and pharmacists to fix prices and to allocate margins for heavy adult incontinence products within the pharmacy channel in Spain during the period from December 1996 through January 2014. Among the parties named in the Statement of Objections was Indas, which the Company acquired in January 2014, and two of its affiliates.

On January 4, 2016, the Competition Directorate issued a proposed decision confirming the allegations of the Statement of Objections. The proposed decision recommended the imposition of fines on the parties without recommending the amount of any fines. The Company recorded a €0.2 million ($0.2 million) provision in the fourth quarter of 2015 in Other operating (income) loss, net.

On May 26, 2016, the CNMC rendered its final decision, which declared that a number of manufacturers of heavy adult incontinence products, the sector association and certain individuals participated in price fixing during the period from December 1996 through January 2014. Indas and one of its subsidiaries were fined a total of €13.5 million ($14.9 million) for their participation. A provision was recorded in the second quarter of 2016 in the amount of €13.3 million ($14.7 million) in Other operating (income) loss, net.

The sellers of Indas made representations and warranties to the Company in the purchase agreement regarding, among other things, Indas' and its subsidiary's compliance with competition laws. The liability retained by the sellers was backed by a retained purchase price of €3 million ($3.3 million) and bank guarantees of €9 million ($9.9 million).

On June 27, 2016, in light of the CNMC decision, the sellers, in terms of their indemnity obligations, agreed to the appropriation by the Company of the retained purchase price and the release of the bank guarantees. Accordingly, a recovery of €12 million ($13.2 million) was recorded in the second quarter of 2016 and included in Other operating (income) loss, net.

In July 2016, the fines were paid and Indas and two of its affiliates named in the final decision appealed the decision to the Spanish courts.

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NOTE 21. COMMITMENTS AND CONTINGENCIES (CONTINUED)

The Company purchased limited insurance coverage with respect to the purchase agreement, and is seeking to recover the remaining €1.5 million ($1.7 million) under the insurance policy. Any recovery from the insurers would be recorded in the period when the proceeds are received.

LEASE AND OTHER COMMERCIAL COMMITMENTS

The Company has entered into operating leases for property, plant and equipment. The Company also has commitments to purchase property, plant and equipment, roundwood, wood chips, gas and certain chemicals. Purchase orders in the normal course of business are excluded from the table below. Any amounts for which the Company is liable under purchase orders are reflected in the Consolidated Balance Sheets as Trade and other payables. Minimum future payments under these operating leases and other commercial commitments, determined at December 31, 2018, were as follows:

	2019	2020	2021	2022	2023	Thereafter	Total
	$	$	$	$	$	$	$
Operating leases	26	21	17	12	10	17	103
Other commercial commitments	84	13	3	1	—	2	103

Total operating lease expense amounted to $29 million in 2018 (2017 – $31 million; 2016 – $28 million).

INDEMNIFICATIONS

In the normal course of business, the Company offers indemnifications relating to the sale of its businesses and real estate. In general, these indemnifications may relate to claims from past business operations, the failure to abide by covenants and the breach of representations and warranties included in the sales agreements. Typically, such representations and warranties relate to taxation, environmental, product and employee matters. The terms of these indemnification agreements are generally for an unlimited period of time. At December 31, 2018, the Company is unable to estimate the potential maximum liabilities for these types of indemnification guarantees as the amounts are contingent upon the outcome of future events, the nature and likelihood of which cannot be reasonably estimated at this time. Accordingly, no provision has been recorded. These indemnifications have not yielded a significant expense in the past.

Pension Plans

The Company has indemnified and held harmless the trustees of its pension funds, and the respective officers, directors, employees and agents of such trustees, from any and all costs and expenses arising out of the performance of their obligations under the relevant trust agreements, including in respect of their reliance on authorized instructions from the Company or for failing to act in the absence of authorized instructions. These indemnifications survive the termination of such agreements. At December 31, 2018 the Company has not recorded a liability associated with these indemnifications, as it does not expect to make any payments pertaining to these indemnifications.

DOMTAR CORPORATION

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NOTE 22.

DERIVATIVES AND HEDGING ACTIVITIES AND FAIR VALUE MEASUREMENT

HEDGING PROGRAMS

The Company is exposed to market risk, such as changes in currency exchange rates, commodity prices and interest rates. To the extent the Company decides to manage the volatility related to these exposures, the Company may enter into various financial derivatives that are accounted for under the derivatives and hedging guidance. These transactions are governed by the Company's hedging policies which provide direction on acceptable hedging activities, including instrument type and acceptable counterparty exposure.

Upon inception, the Company formally documents the relationship between hedging instruments and hedged items. At inception and quarterly thereafter, the Company formally assesses whether the financial instruments used in hedging transactions are effective at offsetting changes in either the cash flow or the fair value of the underlying exposures. The ineffective portion of the qualifying instrument is immediately recognized to earnings. The amount of ineffectiveness recognized was immaterial for all years presented. The Company does not hold derivative financial instruments for trading purposes.

CREDIT RISK

The Company is exposed to credit risk on accounts receivables from its customers. In order to reduce this risk, the Company reviews new customers' credit history before granting credit and conducts regular reviews of existing customers' credit performance. As of December 31, 2018, one of Domtar's Pulp and Paper segment customers located in the U.S. represented 10% or $67 million (2017 – 12% or $83 million) of the Company's receivables.

The Company is exposed to credit risk in the event of non-performance by counterparties to its financial instruments. The Company attempts to minimize this exposure by entering into contracts with counterparties that are believed to be of high credit quality. Collateral or other security to support financial instruments subject to credit risk is usually not obtained. The credit standing of counterparties is regularly monitored.

INTEREST RATE RISK

The Company is exposed to interest rate risk arising from fluctuations in interest rates on its cash and cash equivalents, bank indebtedness, revolving credit facility and securitization, term loan and long-term debt. The Company's objective in managing exposure to interest rate changes is to minimize the impact of interest rate changes on earnings and cash flows and to lower its overall borrowing costs. The Company may manage this interest rate exposure through the use of derivative instruments such as interest rate swap contracts, whereby it agrees to exchange the difference between fixed and variable interest amounts calculated by reference to an agreed upon notional principal amount.

DOMTAR CORPORATION

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NOTE 22. DERIVATIVES AND HEDGING ACTIVITIES AND FAIR VALUE MEASUREMENT (CONTINUED)

COST RISK

Cash flow hedges:

The Company is exposed to price volatility for raw materials and energy used in its manufacturing process. The Company manages its exposure to cost risk primarily through the use of supplier contracts. The Company purchases natural gas at the prevailing market price at the time of delivery. To reduce the impact on cash flow and earnings due to pricing volatility, the Company may utilize derivatives to fix the price of forecasted natural gas purchases. The changes in the fair value on qualifying instruments are included in Accumulated other comprehensive loss to the extent effective, and reclassified into Cost of sales in the period during which the hedged transaction affects earnings. Current contracts are used to hedge a portion of forecasted purchases over the next 42 months.

The following table presents the volumes under derivative financial instruments for natural gas contracts outstanding as of December 31, 2018 to hedge forecasted purchases:

Commodity	Notional contractual quantity under derivative contracts MMBTU[1]	Notional contractual value under derivative contracts (in millions of dollars)	Percentage of forecasted purchases under derivative contracts
Natural gas			
2019	11,430,000	$ 34	41%
2020	8,880,000	$ 27	32%
2021	3,920,000	$ 12	14%
2022	2,070,000	$ 6	7%

(1) MMBTU: Millions of British thermal units

The natural gas derivative contracts were fully effective as of December 31, 2018. There were no amounts reflected in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) for the year ended December 31, 2018 resulting from hedge ineffectiveness (2017 and 2016 – nil).

FOREIGN CURRENCY RISK

Cash flow hedges:

The Company has manufacturing operations in the United States, Canada and Europe. As a result, it is exposed to movements in foreign currency exchange rates in Canada and Europe. Moreover, certain assets and liabilities are denominated in currencies other than the U.S. dollar and are exposed to foreign currency movements. Accordingly, the Company's earnings are affected by increases or decreases in the value of the Canadian dollar and European currencies. The Company's European subsidiaries are also exposed to movements in foreign currency exchange rates on transactions denominated in a currency other than their Euro functional currency. The Company's risk management policy allows it to hedge a significant portion of its exposure to fluctuations in foreign currency exchange rates for periods up to three years. The Company may use derivative financial instruments (currency options and foreign exchange forward contracts) to mitigate its exposure to fluctuations in foreign currency exchange rates.

Derivatives are used to hedge forecasted purchases in Canadian dollars by the Company's Canadian subsidiary over the next 24 months. Derivatives are also currently used to hedge a portion of forecasted non-Euro cash flows of its European subsidiaries for the next 2 months. Such derivatives are designated as cash flow hedges. The changes in the fair value on qualifying instruments are included in Accumulated other comprehensive loss to the extent effective, and reclassified into Sales or Cost of sales in the period during which the hedged transaction affects earnings.

DOMTAR CORPORATION

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NOTE 22. DERIVATIVES AND HEDGING ACTIVITIES AND FAIR VALUE MEASUREMENT (CONTINUED)

The following table presents the currency values under significant currency positions pursuant to currency derivatives outstanding as of December 31, 2018 to hedge forecasted purchases and sales:

Currency exposure hedged	Business Segment	Year of maturity	Notional contractual value	Percentage of forecasted net exposures under contracts	Average Protection rate	Average Obligation rate
CAD/USD	Pulp and Paper	2019	699 CAD	78%	1 USD = 1.2873	1 USD = 1.3168
CAD/USD	Pulp and Paper	2020	324 CAD	36%	1 USD = 1.2937	1 USD = 1.2937

The foreign exchange derivative contracts were fully effective as of December 31, 2018. There were no amounts reflected in the Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss) for the year ended December 31, 2018 resulting from hedge ineffectiveness (2017 and 2016 – nil).

FAIR VALUE MEASUREMENT

The accounting standards for fair value measurements and disclosures, establishes a fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value into three levels. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is available and significant to the fair value measurement.

Level 1	Quoted prices in active markets for identical assets or liabilities.
Level 2	Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
Level 3	Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

DOMTAR CORPORATION

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NOTE 22. DERIVATIVES AND HEDGING ACTIVITIES AND FAIR VALUE MEASUREMENT (CONTINUED)

The following tables present information about the Company's financial assets and financial liabilities measured at fair value on a recurring basis (except Long-term debt, see (b) below) at December 31, 2018 and December 31, 2017, in accordance with the accounting standards for fair value measurements and disclosures and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value.

Fair Value of financial instruments at:	December 31, 2018 $	Quoted prices in active markets for identical assets (Level 1) $	Significant observable inputs (Level 2) $	Significant unobservable inputs (Level 3) $		Balance sheet classification
Derivatives designated as hedging instruments:						
Asset derivatives						
Currency derivatives	1	—	1	—	(a)	Prepaid expenses
Natural gas swap contracts	1	—	1	—	(a)	Prepaid expenses
Total Assets	2	—	2	—		
Liabilities derivatives						
Currency derivatives	19	—	19	—	(a)	Trade and other payables
Natural gas swap contracts	2	—	2	—	(a)	Trade and other payables
Currency derivatives	11	—	11	—	(a)	Other liabilities and deferred credits
Natural gas swap contracts	5	—	5	—	(a)	Other liabilities and deferred credits
Total Liabilities	37	—	37	—		

Other Instruments:						
Stock-based compensation - liability awards	6	6	—	—		Trade and other payables
Stock-based compensation - liability awards	14	14	—	—		Other liabilities and deferred credits
Long-term debt	858	—	858	—	(b)	Long-term debt

The net cumulative loss recorded in Accumulated other comprehensive loss relating to natural gas contracts is $6 million at December 31, 2018, of which a loss of $1 million will be recognized in Cost of sales upon maturity of the derivatives over the next 12 months at the then prevailing values, which may be different from those at December 31, 2018.

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NOTE 22. DERIVATIVES AND HEDGING ACTIVITIES AND FAIR VALUE MEASUREMENT (CONTINUED)

The net cumulative loss recorded in Accumulated other comprehensive loss relating to currency options and forwards hedging forecasted purchases is $29 million at December 31, 2018, of which a loss of $18 million will be recognized in Cost of sales or Sales upon maturity of the derivatives over the next 12 months at the then prevailing values, which may be different from those at December 31, 2018.

Fair Value of financial instruments at:	December 31, 2017 $	Quoted prices in active markets for identical assets (Level 1) $	Significant observable inputs (Level 2) $	Significant unobservable inputs (Level 3) $		Balance sheet classification
Derivatives designated as hedging instruments:						
Asset derivatives						
Currency derivatives	16	—	16	—	(a)	Prepaid expenses
Currency derivatives	4	—	4	—	(a)	Other assets
Natural gas swap contracts	1	—	1	—	(a)	Other assets
Total Assets	21	—	21	—		
Liabilities derivatives						
Currency derivatives	5	—	5	—	(a)	Trade and other payables
Natural gas swap contracts	2	—	2	—	(a)	Trade and other payables
Natural gas swap contracts	5	—	5	—	(a)	Other liabilities and deferred credits
Total Liabilities	12	—	12	—		
Other Instruments:						
Stock-based compensation -	6	6	—	—		Trade and other payables

liability awards						
Stock-based compensation - liability awards	20	20	—	—		Other liabilities and deferred credits
Long-term debt	1,216	—	1,216	—	(b)	Long-term debt

(a) Fair value of the Company's derivatives is classified under Level 2 (inputs that are observable; directly or indirectly) as it is measured as follows:

- For currency derivatives: Fair value is measured using techniques derived from the Black-Scholes pricing model. Interest rates, forward market rates and volatility are used as inputs for such valuation techniques.
- For natural gas contracts: Fair value is measured using the discounted difference between contractual rates and quoted market future rates.

(b) Fair value of the Company's long-term debt is measured by comparison to market prices of its debt. The Company's long-term debt is not carried at fair value on the Consolidated Balance Sheets at December 31, 2018 and December 31, 2017. However, fair value disclosure is required. The carrying value of the Company's long-term debt is $854 million and $1,130 million at December 31, 2018 and December 31, 2017, respectively.

Due to their short-term maturity, the carrying amounts of cash and cash equivalents, receivables, bank indebtedness, trade and other payables and income and other taxes approximate their fair values.

DOMTAR CORPORATION

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NOTE 23.

SEGMENT DISCLOSURES

The Company's two reportable segments described below also represent its two operating segments. Each reportable segment offers different products and services and requires different manufacturing processes, technology and/or marketing strategies. The following summary briefly describes the operations included in each of the Company's reportable segments:

- Pulp and Paper – consists of the design, manufacturing, marketing and distribution of communication, specialty and packaging papers, as well as softwood, fluff and hardwood market pulp.
- Personal Care – consists of the design, manufacturing, marketing and distribution of absorbent hygiene products.

The accounting policies of the reportable segments are the same as those described in Note 1. The Company evaluates segment performance based on operating income. Transfer prices between segments are based on market prices. Certain Corporate general and administrative costs are allocated to the segments. Corporate costs that are not related to segment activities, as well as the mark-to-market impact on stock based compensation awards, are presented on the Corporate line. The Company does not allocate interest expense and income taxes to the segments. Segment assets are those directly used in segment operations.

The Company attributes sales to customers in different geographical areas on the basis of the location of the customer.

Long-lived assets consist of property, plant and equipment, intangible assets and goodwill used in the generation of sales in the different geographical areas.

DOMTAR CORPORATION

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NOTE 23. SEGMENT DISCLOSURES (CONTINUED)

An analysis and reconciliation of the Company's business segment information to the respective information in the financial statements is as follows:

SEGMENT DATA	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Sales [1]			
Pulp and Paper	4,523	4,216	4,239
Personal Care	1,000	996	909
Total for reportable segments	5,523	5,212	5,148
Intersegment sales	(68)	(64)	(58)
Consolidated sales [2]	5,455	5,148	5,090
Sales by product group			
Communication papers	2,548	2,382	2,571
Specialty and packaging papers	710	651	680
Market pulp	1,197	1,119	930
Absorbent hygiene products	1,000	996	909
Consolidated sales [2]	5,455	5,148	5,090
Depreciation and amortization			
Pulp and Paper	238	254	284
Personal Care	70	67	64
Total for reportable segments	308	321	348
Impairment of property, plant and equipment and goodwill - Personal Care	7	578	—
Impairment of property, plant and equipment - Pulp and Paper	—	—	29
Consolidated depreciation and amortization and impairment of property, plant and equipment and goodwill	315	899	377
Operating income (loss) [3]			
Pulp and Paper	438	237	201
Personal Care	(5)	(527)	57

Corporate	(47)	(38)	(50)
Consolidated operating income (loss)	386	(328)	208
Interest expense, net	62	66	66
Non-service components of net periodic benefit cost	(18)	(11)	(15)
Earnings (loss) before income taxes and equity loss	342	(383)	157
Income tax expense (benefit)	57	(125)	29
Equity loss, net of taxes	2	—	—
Net earnings (loss)	283	(258)	128

(1) As a result of adopting ASU 2014-09 "Revenue from Contracts with Customers," the Company has revised its 2017 and 2016 segment disclosures to conform to the new guideline. (Previously reported numbers for Sales for the years ended December 31, 2017 and 2016 were as follows: Pulp and Paper: $4,216 million and $4,239 million, respectively; Personal Care: $1,005 million and $917 million, respectively; Intersegment sales: $(64) million and $(58) million, respectively.)

(2) In 2018 and 2017, Staples, one of the Company's largest customers in the Pulp and Paper segment, represented approximately 10% (2017 – 10%) of the total sales.

(3) As a result of adopting ASU 2017-07 "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost," the Company has revised its 2017 and 2016 segment disclosures to conform to the new guideline. (Previously reported numbers for Operating income (loss) for the years ended December 31, 2017 and 2016 were as follows:

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NOTE 23. SEGMENT DISCLOSURES (CONTINUED)

Pulp and Paper: $250 million and $217 million, respectively; Personal Care: $(527) million and $57 million, respectively; Corporate: $(40) million and $(51) million, respectively.)

	December 31, 2018 $	December 31, 2017 $
Segment assets		
Pulp and Paper	3,475	3,649
Personal Care	1,331	1,406
Total for reportable segments	4,806	5,055
Corporate	119	157
Consolidated assets	4,925	5,212

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $
Additions to property, plant and equipment			
Pulp and Paper	164	128	287
Personal Care	37	48	55
Total for reportable segments	201	176	342
Corporate	2	4	4
Consolidated additions to property, plant and equipment	203	180	346
Add: Change in payables on capital projects	(8)	2	1
Consolidated additions to property, plant and equipment per Consolidated Statements of Cash Flows	195	182	347

	Year ended December 31, 2018 $	Year ended December 31, 2017 $	Year ended December 31, 2016 $

Geographic information			
Sales			
United States	3,669	3,486	3,571
Canada	480	474	493
Europe	682	610	597
Asia	489	444	351
Other foreign countries	135	134	78
	5,455	5,148	5,090

	December 31, 2018 $	December 31, 2017 $
Long-lived assets		
United States	2,056	2,136
Canada	604	677
Europe	542	585
	3,202	3,398

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NOTE 24.

SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION

The following information is presented as required under Rule 3-10 of Regulation S-X, in connection with the Company's issuance of debt securities that are fully and unconditionally guaranteed by Domtar's significant 100% owned domestic subsidiaries, including Domtar Paper Company, LLC, Domtar Industries LLC (and subsidiaries, excluding Domtar Funding LLC), Domtar A.W. LLC, Attends Healthcare Products Inc., EAM Corporation, Associated Hygienic Products LLC and Home Delivery Incontinent Supplies Co., ("Guarantor Subsidiaries"), on a joint and several basis. The Guaranteed Debt is not guaranteed by certain of Domtar's foreign and non-significant domestic subsidiaries, all 100% owned, (collectively the "Non-Guarantor Subsidiaries"). A subsidiary's guarantee may be released in certain customary circumstances, such as if the subsidiary is sold or sells all of its assets, if the subsidiary's guarantee of the Credit Agreement is terminated or released and if the requirements for legal defeasance to discharge the indenture have been satisfied.

The following supplemental condensed consolidating financial information sets forth, on an unconsolidated basis, the Balance Sheets at December 31, 2018 and 2017 and the Statements of Earnings (Loss) and Comprehensive Income (Loss) and Cash Flows for the years ended December 31, 2018, 2017 and 2016 for Domtar Corporation (the "Parent"), and on a combined basis for the Guarantor Subsidiaries and, on a combined basis, the Non-Guarantor Subsidiaries. The supplemental condensed consolidating financial information reflects the investments of the Parent in the Guarantor Subsidiaries, as well as the investments of the Guarantor Subsidiaries in the Non-Guarantor Subsidiaries, using the equity method.

CONDENSED CONSOLIDATING STATEMENT OF EARNINGS AND COMPREHENSIVE INCOME	Year ended December 31, 2018				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Sales	—	4,411	2,226	(1,182)	5,455
Operating expenses					
Cost of sales, excluding depreciation and amortization	—	3,782	1,703	(1,182)	4,303

Depreciation and amortization	—	216	92	—	308
Selling, general and administrative	11	108	324	—	443
Impairment of property, plant and equipment	—	7	—	—	7
Closure and restructuring costs	—	6	2	—	8
Other operating (income) loss, net	—	(1)	1	—	—
	11	4,118	2,122	(1,182)	5,069
Operating (loss) income	(11)	293	104	—	386
Interest expense (income), net	62	91	(91)	—	62
Non-service components of net periodic benefit cost	—	1	(19)	—	(18)
(Loss) earnings before income taxes and equity loss	(73)	201	214	—	342
Income tax (benefit) expense	(20)	30	47	—	57
Equity loss, net of taxes	—	1	1	—	2
Share in earnings of equity accounted investees	336	166	—	(502)	—
Net earnings	283	336	166	(502)	283
Other comprehensive loss	(131)	(133)	(110)	243	(131)
Comprehensive income	152	203	56	(259)	152

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NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING STATEMENT OF LOSS AND COMPREHENSIVE INCOME (LOSS)	Year ended December 31, 2017				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Sales	—	4,243	2,053	(1,148)	5,148
Operating expenses					
Cost of sales, excluding depreciation and amortization	—	3,688	1,605	(1,148)	4,145
Depreciation and amortization	—	233	88	—	321
Selling, general and administrative	9	142	293	—	444
Impairment of goodwill	—	313	265	—	578
Closure and restructuring costs	—	2	—	—	2
Other operating loss (income), net	—	1	(15)	—	(14)
	9	4,379	2,236	(1,148)	5,476
Operating loss	(9)	(136)	(183)	—	(328)
Interest expense (income), net	63	86	(83)	—	66
Non-service components of net periodic benefit cost	—	1	(12)	—	(11)
Loss before income taxes	(72)	(223)	(88)	—	(383)
Income tax expense (benefit)	9	(179)	45	—	(125)
Share in earnings of equity accounted investees	(177)	(133)	—	310	—
Net loss	(258)	(177)	(133)	310	(258)
Other comprehensive income	163	175	170	(345)	163
Comprehensive (loss) income	(95)	(2)	37	(35)	(95)

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DOMTAR CORPORATION

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NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING STATEMENT OF EARNINGS AND COMPREHENSIVE INCOME	Year ended December 31, 2016				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Sales	—	4,203	2,032	(1,145)	5,090
Operating expenses					
Cost of sales, excluding depreciation and amortization	—	3,638	1,558	(1,145)	4,051
Depreciation and amortization	—	256	92	—	348
Selling, general and administrative	17	93	308	—	418
Impairment of property, plant and equipment	—	29	—	—	29
Closure and restructuring costs	—	31	1	—	32
Other operating loss (income), net	1	(1)	4	—	4
	18	4,046	1,963	(1,145)	4,882
Operating (loss) income	(18)	157	69	—	208
Interest expense (income), net	65	50	(49)	—	66
Non-service components of net periodic benefit cost	—	—	(15)	—	(15)
(Loss) earnings before income taxes	(83)	107	133	—	157
Income tax (benefit) expense	(43)	36	36	—	29
Share in earnings of equity accounted investees	168	97	—	(265)	—
Net earnings	128	168	97	(265)	128
Other comprehensive income (loss)	2	(12)	(35)	47	2
Comprehensive income	130	156	62	(218)	130

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DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING BALANCE SHEET	December 31, 2018				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Assets					
Current assets					
Cash and cash equivalents	—	—	111	—	111
Receivables	—	344	326	—	670
Inventories	—	525	237	—	762
Prepaid expenses	6	12	6	—	24
Income and other taxes receivable	1	3	18	—	22
Intercompany accounts	498	194	35	(727)	—
Total current assets	505	1,078	733	(727)	1,589
Property, plant and equipment, net	—	1,802	803	—	2,605
Intangible assets, net	—	256	341	—	597
Investments in affiliates	3,645	2,611	—	(6,256)	—
Intercompany long-term advances	5	1	1,569	(1,575)	—
Other assets	18	26	104	(14)	134
Total assets	4,173	5,774	3,550	(8,572)	4,925
Liabilities and shareholders' equity					
Current liabilities					
Trade and other payables	52	464	241	—	757
Intercompany accounts	125	264	338	(727)	—
Income and other taxes payable	1	12	12	—	25
Long-term debt due within one year	—	—	1	—	1
Total current liabilities	178	740	592	(727)	783
Long-term debt	793	—	60	—	853
Intercompany long-term loans	636	938	1	(1,575)	—
Deferred income taxes and other	—	335	155	(14)	476
Other liabilities and deferred credits	28	116	131	—	275

Shareholders' equity	2,538	3,645	2,611	(6,256)	2,538
Total liabilities and shareholders' equity	4,173	5,774	3,550	(8,572)	4,925

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DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING BALANCE SHEET	December 31, 2017				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Assets					
Current assets					
Cash and cash equivalents	3	14	122	—	139
Receivables	—	402	302	—	704
Inventories	—	522	235	—	757
Prepaid expenses	5	22	6	—	33
Income and other taxes receivable	7	1	16	—	24
Intercompany accounts	380	314	45	(739)	—
Total current assets	395	1,275	726	(739)	1,657
Property, plant and equipment, net	—	1,870	895	—	2,765
Intangible assets, net	—	268	365	—	633
Investments in affiliates	3,892	2,609	—	(6,501)	—
Intercompany long-term advances	6	81	1,513	(1,600)	—
Other assets	22	24	129	(18)	157
Total assets	4,315	6,127	3,628	(8,858)	5,212
Liabilities and shareholders' equity					
Current liabilities					
Trade and other payables	55	424	237	—	716
Intercompany accounts	244	63	432	(739)	—
Income and other taxes payable	1	14	9	—	24
Long-term debt due within one year	—	—	1	—	1
Total current liabilities	300	501	679	(739)	741
Long-term debt	792	300	37	—	1,129
Intercompany long-term loans	674	925	1	(1,600)	—
Deferred income taxes and other	—	356	153	(18)	491
Other liabilities and deferred credits	66	153	149	—	368

Shareholders' equity	2,483	3,892	2,609	(6,501)	2,483
Total liabilities and shareholders' equity	4,315	6,127	3,628	(8,858)	5,212

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DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS	Year ended December 31, 2018				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Operating activities					
Net earnings	283	336	166	(502)	283
Changes in operating and intercompany assets and liabilities and non-cash items, included in net earnings	(557)	434	(108)	502	271
Cash flows (used for) provided from operating activities	(274)	770	58	—	554
Investing activities					
Additions to property, plant and equipment	—	(142)	(53)	—	(195)
Proceeds from disposals of property, plant and equipment	—	1	4	—	5
Other	—	(2)	(4)	—	(6)
Cash flows used for investing activities	—	(143)	(53)	—	(196)
Financing activities					
Dividend payments	(108)	—	—	—	(108)
Proceeds from receivables securitization facilities	—	—	85	—	85
Repayments of receivables securitization facilities	—	—	(60)	—	(60)
Repayments of long-term debt	—	(300)	(1)	—	(301)
Increase in long-term advances to related parties	—	(341)	(36)	377	—
Decrease in long-term advances to related parties	377	—	—	(377)	—
Other	2	—	—	—	2
Cash flows provided from (used for) financing	271	(641)	(12)	—	(382)

activities					
Net decrease in cash and cash equivalents	(3)	(14)	(7)	—	(24)
Impact of foreign exchange on cash	—	—	(4)	—	(4)
Cash and cash equivalents at beginning of year	3	14	122	—	139
Cash and cash equivalents at end of year	—	—	111	—	111

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DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS	Year ended December 31, 2017				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Operating activities					
Net loss	(258)	(177)	(133)	310	(258)
Changes in operating and intercompany assets and liabilities and non-cash items, included in net loss	287	259	471	(310)	707
Cash flows provided from operating activities	29	82	338	—	449
Investing activities					
Additions to property, plant and equipment	—	(99)	(83)	—	(182)
Proceeds from disposals of property, plant and equipment	—	—	19	—	19
Acquisition of business, net of cash acquired	—	—	(8)	—	(8)
Cash flows used for investing activities	—	(99)	(72)	—	(171)
Financing activities					
Dividend payments	(104)	—	—	—	(104)
Net change in bank indebtedness	—	(12)	—	—	(12)
Change in revolving credit facility	(50)	—	—	—	(50)
Proceeds from receivables securitization facilities	—	—	45	—	45
Repayments of receivables securitization facilities	—	—	(90)	—	(90)
Repayments of long-term debt	(63)	—	(1)	—	(64)
Increase in long-term advances to related parties	—	—	(202)	202	—
Decrease in long-term advances to related parties	173	29	—	(202)	—
Other	1	—	—	—	1

Cash flows (used for) provided from financing activities	(43)	17	(248)	—	(274)
Net (decrease) increase in cash and cash equivalents	(14)	—	18	—	4
Impact of foreign exchange on cash	—	—	10	—	10
Cash and cash equivalents at beginning of year	17	14	94	—	125
Cash and cash equivalents at end of year	3	14	122	—	139

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DOMTAR CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2018

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

NOTE. 24 SUPPLEMENTAL GUARANTOR FINANCIAL INFORMATION (CONTINUED)

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS	Year ended December 31, 2016				
	Parent $	Guarantor Subsidiaries $	Non-Guarantor Subsidiaries $	Consolidating Adjustments $	Consolidated $
Operating activities					
Net earnings	128	168	97	(265)	128
Changes in operating and intercompany assets and liabilities and non-cash items, included in net earnings	(4,280)	4,149	203	265	337
Cash flows (used for) provided from operating activities	(4,152)	4,317	300	—	465
Investing activities					
Additions to property, plant and equipment	—	(265)	(82)	—	(347)
Proceeds from disposals of property, plant and equipment and sale of business	—	—	1	—	1
Acquisition of businesses, net of cash acquired	—	(1)	(45)		(46)
Other	—	—	1	—	1
Cash flows used for investing activities	—	(266)	(125)	—	(391)
Financing activities					
Dividend payments	(102)	—	—	—	(102)
Stock repurchase	(10)	—	—	—	(10)
Net change in bank indebtedness	—	12	—	—	12
Proceeds from receivables securitization facilities	—	—	140	—	140
Repayments of receivables securitization facilities	—	—	(70)	—	(70)
Repayments of long-term debt	(38)	(1)	(1)	—	(40)
Increase in long-term advances to related parties	—	(4,050)	(223)	4,273	—

Decrease in long-term advances to related parties	4,273	—	—	(4,273)	—
Other	(3)	—	—	—	(3)
Cash flows provided from (used for) financing activities	4,120	(4,039)	(154)	—	(73)
Net (decrease) increase in cash and cash equivalents	(32)	12	21	—	1
Impact of foreign exchange on cash	—	—	(2)	—	(2)
Cash and cash equivalents at beginning of year	49	2	75	—	126
Cash and cash equivalents at end of year	17	14	94	—	125

Domtar Corporation

Interim Financial Results (Unaudited)

(In millions of dollars, unless otherwise noted)

2018	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter		Year
Sales	$ 1,345		$ 1,353		$ 1,367		$ 1,390		$ 5,455
Operating income	77	(a)	62	(b)	114		133	(d)	386
Earnings before income taxes and equity loss	65		51		103		123		342
Net earnings	54		43		99	(c)	87	(e)	283
Basic net earnings per common share	0.86		0.68		1.57		1.38		4.50
Diluted net earnings per common share	0.86		0.68		1.57		1.38		4.48

2017	1st Quarter	2nd Quarter	3rd Quarter		4th Quarter		Year
Sales	$ 1,302	$ 1,221	$ 1,290		$ 1,335		$ 5,148
Operating income (loss)	38	62	85	(f)	(513)	(g)	(328)
Earnings (loss) before income taxes and equity loss	25	47	73		(528)		(383)
Net earnings (loss)	20	38	70		(386)	(h)	(258)
Basic net earnings (loss) per common share	0.32	0.61	1.12		(6.16)		(4.11)
Diluted net earnings (loss) per common share	0.32	0.61	1.11		(6.16)		(4.11)

(a) The operating income for the first Quarter of 2018 included a gain on disposal of property, plant and equipment of $1 million related to our Pulp and Paper segment.

The Company also recorded a litigation settlement of $2 million related to our Corporate segment.

(b) The operating income for the second Quarter of 2018 included a gain on disposal of property, plant and equipment of $3 million related to our Pulp and Paper segment.

(c) The net earnings for the third Quarter of 2018 included a tax benefit of $7 million related to the U.S. Tax Reform.

(d) The operating income for the fourth Quarter of 2018 included closure and restructuring costs of $8 million and accelerated depreciation of $7 million, both related to our Personal Care segment.

(e) The net earnings for the fourth Quarter of 2018 included a tax expense of $10 million related to the U.S. Tax Reform.

(f) The operating income for the third Quarter of 2017 included the partial reversal of contingent consideration provision of $2 million related to our Corporate segment.

The Company also recorded a gain on disposal of property, plant and equipment of $4 million related to our Pulp and Paper segment.

(g) The operating loss for the fourth Quarter of 2017 included a goodwill impairment charge of $578 million and closure and restructuring costs of $2 million, both associated with our Personal Care segment.

The Company also recorded a gain on disposal of property, plant and equipment of $9 million related to our Corporate segment.

(h) The net loss for the fourth Quarter of 2017 included a net tax benefit of $140 million related to the U.S. Tax Reform, which is composed of a benefit of $186 million for the remeasurement of deferred tax assets and liabilities and a charge of $46 million for the repatriation tax.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

The Company has nothing to report under this item.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to provide reasonable assurance that information required to be disclosed in our reports under the Securities and Exchange Act of 1934, as amended ("Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. As of December 31, 2018, an evaluation was performed by members of management, at the direction and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Exchange Act). Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as at December 31, 2018, our disclosure controls and procedures were effective.

Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. In order to evaluate the effectiveness of internal control over financial reporting, management has conducted an assessment, including testing, using the criteria established in the 2013 Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's system of internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. The Company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on its assessment, management has concluded that the Company maintained effective internal control over financial reporting as of December 31, 2018, based on criteria established in the 2013 Internal Control – Integrated Framework issued by the COSO.

The effectiveness of the Company's internal control over financial reporting as at December 31, 2018 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report, which is included under Item 8, Financial Statements and Supplementary Data.

Change in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that have materially affected or are reasonably likely to materially affect our internal control over financial reporting during the fourth quarter ended December 31, 2018.

ITEM 9B. OTHER INFORMATION

The Company has nothing to report under this item.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information included under the captions “Governance of the Corporation”, “Election of Directors” and “Section 16(a) Beneficial Ownership Reporting Compliance” in our Proxy Statement for the 2019 Annual Meeting of Stockholders, to be filed on or about March 31, 2019, is incorporated herein by reference.

Information regarding our executive officers is presented in Item 1, Business, under the caption “Our Executive Officers”.

ITEM 11. EXECUTIVE COMPENSATION

The information appearing under the caption “Compensation Discussion and Analysis”, “Executive Compensation” and “Director Compensation” in our Proxy Statement for the 2019 Annual Meeting of Stockholders, to be filed on or about March 31, 2019, is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information appearing under the caption “Security Ownership of Certain Beneficial Owners, Directors and Officers” in our Proxy Statement for the 2019 Annual Meeting of Stockholders, to be filed on or about March 31, 2019, is incorporated herein by reference.

The following table sets forth the number of shares of our stock reserved for issuance under our equity compensation plans as of December 31, 2018:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (#) (a)		Weighted average exercise price of outstanding options, warrants and rights ($) (b)		Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a) (#) (c)	
Equity compensation plans approved by security holders	1,698,973	(1)	$ 45.68	(2)	1,246,036	(3)
Equity compensation plans not approved by security holders	N/A		N/A		N/A	

Total	1,698,973	$ 45.68	1,246,036

(1) Represents the total number of shares associated with options, restricted stock units ("RSUs"), performance share units ("PSUs"), deferred share units ("DSUs") and dividends equivalent units ("DEUs") outstanding as of December 31, 2018 that may or will be settled in equity. This number assumes that PSUs will vest at the "maximum" performance level, and that any performance requirements applicable to options will be satisfied.

(2) Represents the weighted average exercise price of options disclosed in column (a).

(3) Represents the number of shares remaining available for issuance in settlement of future awards under the Omnibus Incentive Plan.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information appearing under the captions "Governance of the Corporation – Board Independence and Other Determinations" in our Proxy Statement for the 2019 Annual Meeting of Stockholders is incorporated herein by reference.

ITEM 14. PRINCIPLE ACCOUNTANT FEES AND SERVICES

The information appearing under the caption "Ratification of Appointment of Independent Registered Public Accounting Firm" and "Independent Registered Public Accounting Firm Fees" in our Proxy Statement for the 2019 Annual Meeting of Stockholders is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) 1. Financial Statements – See Item 8, Financial Statements and Supplementary Data.
2. Schedule II – Valuation and Qualifying Accounts

All other schedules are omitted as the information required is either included elsewhere in the consolidated financial statements in Item 8, Financial Statements and Supplementary Data – or is not applicable.

3. Exhibits:

		Incorporated by reference to:		
Exhibit Number	Exhibit Description	Form	Exhibit	Filing Date
3.1	Amended and Restated Certificate of Incorporation	10-Q	3.1	08/08/2008
3.2	Certificate of Amendment of the Amended and Restated Certificate of Incorporation	8-K	3.1	06/08/2009
3.3	Amended and Restated By-Laws	8-K	3.1	02/24/2016
4.1	Form of Indenture between Domtar Corp. and the Bank of New York, as trustee, relating to Domtar Corp.'s (i) 7.125% Notes due 2015, (ii) 5.375% Notes due 2013, (iii) 7.875% Notes due 2011, (iv) 9.5% Notes due 2016 to be issued as part of a debt exchange	S-4	4.1	10/16/2007
4.2	Supplemental Indenture, dated February 15, 2008, among Domtar Corp., Domtar Paper Company LLC, The Bank of New York, as Trustee, and the new subsidiary guarantors as parties thereto, relating to the guarantee by the new subsidiary guarantors of the obligations under the Indenture	8-K	4.1	02/21/2008
4.3	Supplemental Indenture, dated September 7, 2011, among Domtar Corporation, Attends Healthcare Products Inc., and The Bank of New York Mellon (formerly the Bank of New York), as trustee, relating to the guarantee by Attends Healthcare Products Inc. of the obligations under the Indenture	10-Q	4.1	11/04/2011
4.4	Supplemental Indenture, dated as of March 16, 2012, among Domtar Corporation, the subsidiary guarantors party thereto, and The Bank of New York Mellon (formerly known as The Bank of New York), as trustee, providing for Domtar Corporation's 4.40% Notes due 2022	8-K	4.1	03/16/2012
4.5		S-3	4.8	08/20/2012

	Supplemental Indenture, dated May 21, 2012, among Domtar Corporation, EAM Corporation, and The Bank of New York Mellon, as trustee, relating to EAM Corporation's guarantee of the obligations under the Indenture			
4.6	Supplemental Indenture, dated as of August 23, 2012, among Domtar Corporation, the subsidiary guarantors party thereto, and The Bank of New York Mellon (formerly the Bank of New York), as trustee, providing for Domtar Corporation's 6.25% Notes due 2042	8-K	4.1	08/23/2012
4.7	Supplemental Indenture, dated as of July 31, 2013, among Domtar Corporation, Associated Hygienic Products LLC, and The Bank of New York Mellon (formerly the Bank of New York), as trustee, relating to the guarantee by Associated Hygienic Products LLC of the obligations under the Indenture	S-3ASR	4.10	10/01/2013
4.8	Supplemental Indenture, dated as of November 26, 2013, among Domtar Corporation, the subsidiary guarantors party thereto, and The Bank of New York Mellon (formerly the Bank of New York), as trustee, providing for Domtar Corporation's 6.75% Notes due 2044	8-K	4.1	11/26/2013

Exhibit Number	Exhibit Description	Incorporated by reference to: Form	Exhibit	Filing Date
4.9	Supplemental Indenture, dated as of January 23, 2017, among Home Delivery Incontinent Supplies Co, Domtar Corporation and The Bank of New York Mellon, as trustee, relating to Home Delivery Incontinent Supplies Co's guarantee of the obligations under the Indenture	10-Q	4.1	05/05/2017
10.1*	Domtar Corporation Executive Deferred Share Unit Plan (applicable to members of the Management Committee of Domtar Inc. prior to March 7, 2007)	10-K	10.29	02/27/2009
10.2*	Domtar Corporation Deferred Share Unit Plan for Outside Directors (for former directors of Domtar Inc.)	10-K	10.30	02/27/2009
10.3*	Director Deferred Stock Unit Agreement	8-K	10.1	05/24/2007
10.4*	Non-Qualified Stock Option Agreement			
10.5*	Restricted Stock Unit Agreement			
10.6*	Performance Share Unit Agreement			
10.7*	Severance Program for Management Committee Members	10-K	10.7	02/24/2017
10.8*	Amended and Restated DB SERP for Management Committee Members of Domtar	10-Q	10.1	08/04/2017
10.9*	Amended and Restated DC SERP for Designated Executives of Domtar			
10.10*	Form of Indemnification Agreement for members of Pension Administration Committee of Domtar Corporation	10-K	10.50	02/27/2009
10.11	Amended and Restated Domtar Corporation 2007 Omnibus Incentive Plan	DEF 14A	Annex B	03/31/2017
10.12	Domtar Corporation Annual Incentive Plan for members of the Management Committee	DEF 14A	Annex A	03/31/2017
10.13*	Employment agreement of Mr. Michael Fagan	10-K	10.48	02/28/2013
10.14*		10-Q	10.3	08/04/2017

	Amended and Restated Supplementary Pension Plan for Designated Managers of Domtar Inc.			
10.15*	Amended and Restated Employment Agreement of Mr. John D. Williams	10-Q	10.1	08/02/2013
10.16*	Amended and Restated DC SERP for Designated Executives of Domtar Personal Care			
10.17*	Employment agreement of Mr. Michael D. Garcia	10-Q	10.1	08/01/2014
10.18	Second Amended and Restated Credit Agreement dated as of August 18, 2016, among the Company, Domtar Inc, Domtar Pulp and Paper General Partnership, Laboratorios Indas, S.A.U., and Attends Healthcare AB, Bank of Montreal, Goldman Sachs Bank USA, Royal Bank of Canada and Wells Fargo Bank, N.A., as co-documentation agents, The Bank of Nova Scotia and Bank of America, N.A., as syndication agents and JP Morgan Chase Bank, N.A., as administrative agent.	10-Q	10.1	11/03/2016

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Exhibit Number	Exhibit Description	Incorporated by reference to: Form	Exhibit	Filing Date
21	Subsidiaries of Domtar Corporation			
23	Consent of Independent Registered Public Accounting Firm			
24.1	Powers of Attorney (included in signature page)			
31.1	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002			
31.2	Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002			
32.1	Certification of the Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002			
32.2	Certification of the Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002			
101.INS	XBRL Instance Document			
101.SCH	XBRL Taxonomy Extension Schema			
101.CAL	XBRL Taxonomy Extension Calculation Linkbase			
101.DEF	XBRL Taxonomy Extension Definition Linkbase			
101.LAB	XBRL Taxonomy Extension Label Linkbase			
101.PRE	XBRL Extension Presentation Linkbase			

* Indicates management contract or compensatory arrangement

FINANCIAL STATEMENT SCHEDULE

(IN MILLIONS OF DOLLARS, UNLESS OTHERWISE NOTED)

SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS

For the three years ended:

	Balance at beginnings of year $	Charged to income $	(Deductions) from / Additions to reserve $	Balance at end of year $
Allowances deducted from related asset accounts:				
Doubtful accounts - Accounts receivable				
2018	7	2	(3)	6
2017	7	1	(1)	7
2016	6	—	1	7

	Balance at beginnings of year $	Charged to income $	Deductions from reserve $	Balance at end of year $
Valuation Allowance on Deferred Tax Assets				
2018	25	(8)	(1)	16
2017	22	3	—	25
2016	23	(1)	—	22

ITEM 16. FORM 10-K SUMMARY

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized in the City of Fort Mill, South Carolina, United States, on February 22, 2019

DOMTAR CORPORATION

by	/s/ John D. Williams
Name:	John D. Williams
Title:	President and Chief Executive Officer

We, the undersigned directors and officers of Domtar Corporation, hereby severally constitute Zygmunt Jablonski and Razvan L. Theodoru, and each of them singly, our true and lawful attorneys with full power to them and each of them to sign for us, in our names in the capacities indicated below, any and all amendments to this Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ John D. Williams John D. Williams	President and Chief Executive Officer (Principal Executive Officer) and Director	February 22, 2019
/s/ Daniel Buron Daniel Buron	Senior Vice-President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	February 22, 2019
/s/Giannella Alvarez Giannella Alvarez	Director	February 22, 2019
/s/ Robert E. Apple Robert E. Apple	Director	February 22, 2019
/s/ David J. Illingworth David J. Illingworth	Director	February 22, 2019
/s/ Brian M. Levitt	Director	

Brian M. Levitt		February 22, 2019
/s/ David G. Maffucci David G. Maffucci	Director	February 22, 2019
/s/ Pamela B. Strobel Pamela B. Strobel	Director	February 22, 2019
/s/ Denis Turcotte Denis Turcotte	Director	February 22, 2019
/s/ Mary A. Winston Mary A. Winston	Director	February 22, 2019