



TIMBERWEST FOREST CORP.

THIRD QUARTER INTERIM REPORT
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2010

TSX:TWF:UN

WWW.TIMBERWEST.COM

Third Floor – 856 Homer Street
Vancouver, BC, Canada V6B 2W5

TIMBERWEST FOREST CORP.

TO OUR UNITHOLDERS,

Overview

TimberWest is pleased to report its third successive quarter of positive EBITDA, highlighting the improved financial performance of the Company. EBITDA for the quarter was \$2.4 million, which brings the YTD EBITDA to \$15.5 million. EBITDA for the first three quarters of 2009 totaled (\$6.2) million. The Company recorded a distributable cash loss in the quarter of (\$4.7) million. This brings the year to date distributable cash loss to (\$3.6) million, a meaningful improvement of \$20.9 million over the distributable cash loss of (\$24.5) million recorded during the comparable period in 2009. The latest quarter's financial results are particularly encouraging in light of a longer than normal suspension of summer harvesting activities due to extreme fire hazard conditions.

The primary driver of TimberWest's improving financial position is increasing sales to Asia. Strong economic growth in China and Korea, combined with a decline in Russian log supply, has created an unparalleled demand for fibre in Asia. To put this demand growth into context, the fibre deficit in China grew at a compound annual rate of just over 16% between 1997 and 2009. By the end of 2009, China's fibre deficit totaled 105 million m³, which was roughly equal to Canada's total reported harvest.

China and Korea have emerged as major new growth markets over the past three years. Year to date, export sales revenue into these two countries has more than tripled over the equivalent prior year period. With China's economy still growing, we see a further tightening of global fibre supply and a resulting sustainable demand for our products from this region. Increased access to the China market through reduced port restrictions early in the third quarter helped improve volumes and margins. In addition we have experienced dramatic growth into Japan in 2010. The year to date sales revenues into this country are almost twice as high as they were this time last year.

In contrast to Asia, U.S. log sales revenues remain at historically depressed levels. Residential housing starts in 2010 are not expected to surpass 625,000 units. Adding to this challenge is the significant inventory overhang created from the number of homes in the current and potential foreclosure process and continued high unemployment levels. Faced with these dynamics, we have actively reduced our exposure to this market. Year to date, log sales revenue into the U.S. represents only 4% of the Company's total, which has declined further from the 5.8% realized in the equivalent prior year period. In the peak 2005 period for U.S. log sales revenue, sales into that market represented 20% of the Company's total.

Domestic sales have increased with our increased production and purchase activity. Quarterly domestic sales revenues were \$19.8 million compared to \$10.9 million Q3, 2009.

TimberWest's market diversification program has strengthened its results and reduced its risk profile.

On October 15, 2010, the Company paid the April 15, 2009 deferred distribution in additional Stapled Units to unitholders. As the original deferral periods are coming due, the Company will now make quarterly distributions to unitholders by issuing additional Stapled Units.

Timberland Operational Results

Dry, hot weather conditions experienced during the third quarter required us to suspend harvesting activities for fire prevention purposes. While this form of closure is not unusual, the duration of the shutdown this past summer was longer than what we normally experience and resulted in low production levels. Despite the resultant negative impact on costs, we continued to record profits in our Timberland operations.

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Reduced production volumes in the quarter drove unit production costs and our cost of sales higher. Timberland cost of sales for the quarter averaged \$66 per m³, a \$3 per m³ increase in unit sales costs over Q2, 2010. Year to date timberland cost of sales of \$64 per m³ are a \$1 per m³ increase over the preceding quarter but \$10 per m³ less than what was recorded in the first three quarters of 2009. The improved cost performance in 2010 relates to the implementation of the sub-divided contractor model, reduced fixed costs, and the increased absorption of fixed costs associated with higher annual harvest volumes.

Harvest volumes on both private and public lands in Q3, 2010 were 486,108 and 1.8 million m³ on a year to date basis. At this rate of production we project that we will be below our long term economic harvest level (LTEHL) on our private lands for the year but we will have harvested the full annual allowable cut off our crown tenures.

Focusing sales on the Asian market with its higher sales realizations helped offset much lower North American prices. Combined sales realizations for all markets in the third quarter averaged \$75 per m³. This was a \$1 per m³ improvement over the second quarter and a meaningful \$6 per m³ improvement over Q3 2009. Sales realizations in Asian markets ranged from \$83 per m³ to \$95 per m³ during the quarter compared \$59 per m³ in the U.S.

Safety performance deteriorated slightly in the quarter with our Medical Incident Rating (MIR) increasing to 0.62. On a year to date basis the Company's MIR stands at 0.60 compared to a MIR of 0.44 for the same period last year. We will continue to work with our contractors to improve performance and with the goal of eliminating injuries altogether.

Couverdon

This summer proved to be a challenging period for land sales with very little activity in the Vancouver Island market overall. Gross revenues for Couverdon during the quarter were \$0.5 million, which brings our year to date total to \$11.5 million. The large acreage lot market, which comprises 100% of our currently available product, is a relatively thin market. Moreover, given the nature of the real estate business, sales are challenging to predict. We do however anticipate an improvement in real estate sales in the fourth quarter based on transactions currently underway.

We continue to work on planning and rezoning at many locations across our portfolio and are pleased with the progress we are making. The more significant work on our core development land will take a number of years to successfully complete. In the interim, we will continue to deliver large acreage lots and non-core land sales to the market that command a premium over timberland values.

Outlook

We will continue to look to Asia with its strong and growing demand to be our market focus, and may increase our 2011 private land harvest levels to further realize on the improved pricing from this region. While we see no near term improvement in the U.S. market, the growth in Asian demand for our product should sustain our recent financial performance, making us less reliant on a turnaround in the U.S. housing market. With our continued cost vigilance and in the absence of the production disruptions that occurred in the third quarter, we anticipate our production costs to return to their more normalized, lower levels. In addition, as noted above, we anticipate a fourth quarter improvement in real estate sales.

We remain bullish about the mid and long term prospects for our business. With the log shortage caused by the mountain pine beetle epidemic in western Canada, declining harvest levels in eastern Canada, reduced Russian log supply, growing demand for our products in Asia, and the eventual housing recovery in the U.S., the Company's future prospects are very strong. Log prices are expected to improve further in all of the markets TimberWest participates in as the U.S. housing industry recovers.

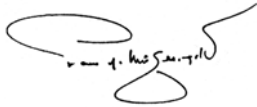
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We remain focused on creating value for unitholders by capturing the full potential of our land and timber resources and by remaining vigilant on minimizing costs throughout our supply chain. TimberWest has a premium species mix in its forest and enjoys a strategically important location that provides easy access to Pacific Rim markets.

We are a much leaner company today with 81 employees, compared to 1,200 ten years ago. In recent years we have moved to a lower cost contractor model for harvesting operations, reduced overhead costs, closed or sold unprofitable operations, refinanced the business, negotiated our way out of punitive fibre supply agreements, created Couverdon to unlock the value of our higher and better use lands, and diversified our end markets. We believe we are exceptionally well positioned for the future.

Thank you again to all of our unitholders for your ongoing support.

On behalf of the Board of Directors,

A handwritten signature in black ink, appearing to read "Paul McElligott". The signature is stylized with a large loop at the beginning and a long, sweeping tail that ends in a hook-like shape.

Paul McElligott
President and Chief Executive Officer
Vancouver, British Columbia
November 8, 2010

TIMBERWEST FOREST CORP.

MANAGEMENT'S DISCUSSION & ANALYSIS

For the three and nine months ended September, 2010 and 2009

Management's Discussion and Analysis supplements, but does not form part of, the unaudited interim consolidated financial statements of TimberWest Forest Corp. ("TimberWest" or the "Company") and the notes thereto for the third quarter of 2010 ("third quarter" or "Q3"). This discussion and analysis provides an overview of significant developments that have affected TimberWest's performance during the third quarter of 2010 relative to the third quarter of 2009, and that have affected the Company's financial position as at September 30, 2010, relative to December 31, 2009.

Factors that could affect future operations are also discussed. These factors may be affected by known and unknown risks and uncertainties that may cause the actual future results of the Company to be materially different than those expressed or implied in this discussion. These risks and uncertainties are described herein and in the Management's Discussion and Analysis contained in the Company's 2009 Annual Report.

TimberWest's unaudited interim consolidated financial statements and the accompanying notes included within this interim report include the accounts of TimberWest Forest Corp. and its subsidiaries. The unaudited interim consolidated financial statements and the accompanying notes are prepared in accordance with Canadian generally accepted accounting principles (GAAP) and are expressed in Canadian dollars.

This Management's Discussion and Analysis has been prepared based on information available as at November 8, 2010.

Additional information relating to TimberWest, including the Company's most recent Annual Information Form and other statutory reports, can be found on the System for Electronic Document Analysis and Retrieval (SEDAR) at <http://www.sedar.com>.

Forward Looking Statements

The statements which are not historical facts contained in this report are forward-looking statements that involve risks and uncertainties. TimberWest's actual results could differ materially from those expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to general economic conditions, variations in TimberWest's product prices and changes in commodity prices generally, changes in market conditions, variations in harvest levels, changes in log transportation costs, actions of competitors, interest rate and foreign currency fluctuations, regulatory, harvesting fee and trade policy changes and other actions by governmental authorities including real estate zoning approvals, the ability to implement business strategies and pursue business opportunities, labour relations, weather conditions, forest fires, insect infestation, disease and other natural phenomena and other risks and uncertainties described in TimberWest's public filings with securities regulatory authorities.

TIMBERWEST FOREST CORP.

1. Financial Highlights

Selected financial information

(in millions of dollars except where otherwise noted)	Three months ended		Nine months ended	
	September 30		September 30	
	2010	2009	2010	2009
Sales	\$ 65.9	\$ 37.5	\$ 205.5	\$ 105.9
Operating earnings (loss) from continuing operations	1.6	(2.2)	12.4	(9.9)
Operating earnings (loss) from continuing operations - % of sales	2%	(6)%	6%	(9)%
Net earnings (loss) from continuing operations	0.6	(25.9)	(7.0)	(63.7)
Net loss from continuing operations excluding unusual items ¹	(5.2)	(11.6)	(17.9)	(40.0)
Net earnings (loss)	0.6	(26.0)	(7.0)	(64.0)
Net loss excluding unusual items ¹	(5.2)	(11.7)	(17.9)	(40.3)
EBITDA from continuing operations ²	2.4	(0.4)	15.5	(5.9)
EBITDA ²	2.4	(0.5)	15.5	(6.2)
Distributable cash from continuing operations ²	(4.7)	(3.7)	(3.6)	(24.2)
Distributable cash ²	(4.7)	(3.8)	(3.6)	(24.5)
Per Stapled Units – basic and diluted				
Net earnings (loss) from continuing operations	0.01	(0.33)	(0.08)	(0.82)
Net loss from continuing operations excluding unusual items ¹	(0.05)	(0.15)	(0.21)	(0.52)
EBITDA from continuing operations ²	0.03	(0.01)	0.18	(0.08)
EBITDA ¹	0.03	(0.01)	0.18	(0.08)
Distributable cash from continuing operations ²	(0.05)	(0.05)	(0.04)	(0.31)
Distributable cash ²	(0.05)	(0.05)	(0.04)	(0.32)
Timberlands sales	65.4	29.6	194.0	91.1
Real estate sales	0.5	7.9	11.5	14.8
Stapled Units (thousands)				
At period-end	89,939	77,777	89,939	77,777
Basic weighted average	89,939	77,777	83,825	77,771
Diluted weighted average	90,298	78,074	84,309	77,923

1 Net loss from continuing operations excluding unusual items and net loss excluding unusual items are non-GAAP measures. Unusual items are defined as the following, net of their associated income tax impact: (i) gain on modification of Series A Subordinate Notes; (ii) accretion expense on the Series A Subordinate Notes; and (iii) change in fair value of financial instruments held for trading. These unusual items, net of their income tax impact, are quantified in the following table:

(in millions of dollars, except where otherwise noted)	Three months ended		Nine months ended	
	September 30		September 30	
	2010	2009	2010	2009
Accretion expense on Series A Subordinate Notes	\$ (1.9)	\$ (1.7)	\$ (5.4)	\$ (4.9)
Change in fair value of financial instruments held for trading	7.2	(13.1)	14.9	(24.7)
Total unusual items	5.3	(14.8)	9.5	(29.6)
Income tax recognized on unusual items	0.5	0.5	1.4	5.9
Total unusual items, net of income tax	\$ 5.8	\$ (14.3)	\$ 10.9	\$ (23.7)
Total unusual items per common share – basic and diluted (in dollars)	\$ 0.06	\$ (0.18)	\$ 0.13	\$ (0.30)

2 Distributable cash and earnings before interest, tax, depreciation and amortization (“EBITDA”) do not have a standardized meaning prescribed by Canadian generally accepted accounting principles and may not be comparable to similar measures presented by other companies. The Company’s calculation of EBITDA is provided on page 6 and distributable cash on page 7 of this report.

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Reconciliation of net earnings (loss) from continuing operations to EBITDA

(in millions of dollars)	Three months ended		Nine months ended	
	September 30	2009	September 30	2009
Net earnings (loss) from continuing operations	0.6	(25.9)	(7.0)	(63.7)
Add (deduct):				
Interest on Series A Subordinate Notes owned by unitholders	4.3	3.6	12.2	10.5
Interest on convertible debentures	3.6	3.4	10.7	8.5
Interest on long-term bank debt	2.0	2.5	6.9	7.2
Interest on short-term bank debt	-	-	-	0.5
Income tax recovery	(4.2)	(0.8)	(3.1)	(9.1)
Depreciation, depletion and amortization	1.0	1.2	3.2	3.0
Amortization of deferred financing costs	0.6	0.4	2.2	1.3
Change in fair value of financial instruments held for trading	(7.2)	13.1	(14.9)	24.7
Change in fair value of Stapled Unit option plan	(0.2)	0.4	(0.1)	0.8
Financing transaction costs	-	-	-	5.5
Accretion on Series A Subordinate Notes	1.9	1.7	5.4	4.9
EBITDA from continuing operations ¹	2.4	(0.4)	15.5	(5.9)
EBITDA from discontinued operations ^{1,2}	-	(0.1)	-	(0.3)
EBITDA ¹	2.4	(0.5)	15.5	(6.2)

1 EBITDA does not have a standardized meaning prescribed by Canadian generally accepted accounting principles and may not be comparable to similar measures presented by other companies. Management believes that the presentation of this measure will enhance an investor's understanding of the Company's operating performance.

2 The Company permanently closed its Elk Falls sawmill operations on May 9, 2008.

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2. Distributable Cash

Reconciliation of net earnings (loss) from continuing operations to distributable cash

(in millions of dollars)	Three months ended		Nine months ended	
	September 30		September 30	
	2010	2009	2010	2009
Net earnings (loss) from continuing operations	\$ 0.6	\$ (25.9)	\$ (7.0)	\$ (63.7)
Interest on Series A Subordinate Notes owned by unitholders	4.3	3.6	12.2	10.5
Earnings (loss) from continuing operations available for distribution	4.9	(22.3)	5.2	(53.2)
Accretion on Series A Subordinate Notes	1.9	1.7	5.4	4.9
Change in fair value of financial instruments held for trading	(7.2)	13.1	(14.9)	24.7
Future Income tax recovery	(4.2)	(0.8)	(2.6)	(9.1)
Loss from continuing operations available for distribution before accretion, changes in fair value of financial instruments held for trading, and provision for future income taxes	(4.6)	(8.3)	(6.9)	(32.7)
Add (deduct):				
Depreciation, depletion and amortization	1.6	1.6	5.4	4.3
Proceeds from sale of real estate	0.5	6.4	10.1	12.5
Gain on sale of real estate	(0.4)	(3.9)	(5.3)	(5.5)
Additions to property, plant and equipment	(2.2)	(0.3)	(3.7)	(0.7)
Financing transaction costs	-	-	(3.2)	(3.5)
Other non-cash items	0.4	0.8	-	1.4
	(0.1)	4.6	3.3	8.5
Distributable cash from continuing operations	(4.7)	(3.7)	(3.6)	(24.2)
Distributable cash from discontinued operations ¹	-	(0.1)	-	(0.3)
Distributable cash	\$ (4.7)	\$ (3.8)	\$ (3.6)	\$ (24.5)

1 The Company permanently closed its Elk Falls sawmill operations on May 9, 2008.

Calculation of distributable cash per Stapled Unit

Per Stapled Units – basic and diluted (in dollars)	Three months ended		Nine months ended	
	September 30		September 30	
	2010	2009	2010	2009
Loss from continuing operations available for distribution before accretion, changes in fair value of financial instruments held for trading, and provision for future income taxes	\$ (0.05)	\$ (0.11)	\$ (0.08)	\$ (0.42)
Distributable cash from continuing operations	(0.05)	(0.05)	(0.04)	(0.31)
Distributable cash from discontinued operations ¹	-	-	-	(0.01)
Distributable cash	(0.05)	(0.05)	(0.04)	(0.32)
Cash distributions paid	\$ -	\$ -	\$ -	\$ -

1 The Company permanently closed its Elk Falls sawmill operations on May 9, 2008.

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Reconciliation of operating cash flow from operations to distributable cash

(in millions of dollars)	Three months ended		Nine months ended	
	September 30		September 30	
	2010	2009	2010	2009
Cash provided by (used in) continuing operations	\$ (4.7)	\$ (11.0)	\$ (1.8)	\$ (30.3)
Add (deduct):				
Change in non-cash working capital	1.4	1.2	2.5	(2.6)
Interest on Series A Subordinate Notes owned by unitholders	4.3	3.6	12.2	10.5
Proceeds from sale of real estate	0.5	6.4	10.1	12.5
Additions to property, plant and equipment	(2.2)	(0.3)	(3.7)	(0.7)
Financing transaction costs	-	-	(3.2)	(3.5)
Change in deferred distribution payable	(4.3)	(3.6)	(12.2)	(10.5)
Convertible debenture interest paid in kind	-	-	(7.0)	-
Other non-cash items	0.3	-	(0.5)	0.4
	-	7.3	(1.8)	6.1
Distributable cash from continuing operations	(4.7)	(3.7)	(3.6)	(24.2)
Distributable cash from discontinued operations ¹	-	(0.1)	-	(0.3)
Distributable cash	\$ (4.7)	\$ (3.8)	\$ (3.6)	\$ (24.5)

1 The Company permanently closed its Elk Falls sawmill operations on May 9, 2008.

Distributable cash includes consolidated net earnings (loss), plus interest expensed on Series A Subordinate Notes owned by unitholders, plus non-cash items including income taxes, changes in fair values and accretion expense, plus depreciation, depletion and amortization, plus proceeds from the sale of property, plant and equipment net of their gain (loss) on sale, less additions to property, plant and equipment, less financing costs and, from time to time, adjustments for other items deemed appropriate by the Board of Directors.

Earnings from continuing operations available for distribution is comprised of consolidated net earnings (loss) from continuing operations plus interest expensed on Series A Subordinate Notes. The Series A Subordinate Notes are owned by the unitholders and interest thereon is paid to the unitholders, therefore, earnings from continuing operations available for distribution to unitholders reflects earnings before this interest charge.

Earnings from continuing operations available for distribution and distributable cash are measures that do not have a standardized meaning prescribed by Canadian GAAP and may not be comparable to similar measures presented by other companies. Management believes that the presentation of these measures will enhance an investor's understanding of the Company's operating performance. Reconciliations of net earnings (loss) and cash flow from continuing operations before changes in working capital, as determined in accordance with Canadian GAAP, and earnings from continuing operations available for distribution and distributable cash are provided in the preceding tables.

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The following tables present a quarterly comparison of distributable cash generated over the past five years, in total and on a per Stapled Unit basis:

	2010	2009	2008	2007	2006	2005
(in millions of dollars)						
First quarter	\$ (2.9)	\$ (15.3)	\$ (3.9)	\$ 26.9	\$ 31.5	\$ 23.9
Second quarter	4.0	(5.4)	(3.2)	13.6	35.5	15.4
Third quarter	(4.7)	(3.8)	(6.3)	(5.6)	9.3	(1.7)
Fourth quarter		(10.2)	(11.4)	55.4	27.5	29.7
	\$ (3.6)	\$ (34.7)	\$ (24.8)	\$ 90.3	\$ 103.8	\$ 67.3
Per Stapled Unit ¹ (in dollars)						
First quarter	\$ (0.04)	\$ (0.20)	\$ (0.05)	\$ 0.35	\$ 0.41	\$ 0.31
Second quarter	0.05	(0.07)	(0.04)	0.17	0.46	0.20
Third quarter	(0.05)	(0.05)	(0.08)	(0.07)	0.12	(0.02)
Fourth quarter		(0.13)	(0.15)	0.71	0.35	0.38
	\$ (0.04)	\$ (0.45)	\$ (0.32)	\$ 1.16	\$ 1.34	\$ 0.87

1 Per Stapled Unit amounts by quarter do not necessarily add to the total of the year and year-to-date due to changes in the weighted average number of Stapled Units outstanding during the year.

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3. Highlights and Significant Transactions

Deferred cash distributions on the Stapled Units

As announced in November, 2008, the January 15, 2009 distribution payment was deferred for 27 months pursuant to the terms of the Note Indenture and all 2009 distribution payments, payable at 2%, were deferred for 18 months. The Company has set the variable interest rate at 2% for 2010 and intends to defer cash distribution payments for the foreseeable future. As deferred distributions become payable, the Company intends to make payment in kind by the issuance of additional Stapled Units to unitholders.

The deferred distribution originally payable on April 15, 2009 but deferred for 18 months became payable on October 15, 2010 and was paid in kind by issuance of 885,447 Stapled Units. As the original deferral periods are coming due, the Company will now make quarterly distributions to unitholders by issuing additional Stapled Units.

The Company is currently reviewing the current Stapled Unit structure to determine its relevance for the business for the long term.

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4. Operating Highlights

Timberlands

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Log sales (in millions of dollars)				
Domestic	\$ 19.8	\$ 10.9	\$ 58.6	\$ 34.7
Export – Asia	32.9	14.7	99.7	46.0
Export – USA	2.7	0.7	6.7	4.9
	55.4	26.3	165.0	85.6
Freight and other	10.0	3.3	29.0	5.5
Total timberland sales	\$ 65.4	\$ 29.6	\$ 194.0	\$ 91.1
Log sales realizations (\$/m ³) - CAD				
Domestic	\$ 60	\$ 56	\$ 58	\$ 55
Export – Asia	90	86	89	94
Export – USA	59	45	60	60
Total log sales realizations - CAD	\$ 75	\$ 69	\$ 74	\$ 71
Log sales realizations (\$/m ³) – USD				
Domestic	\$ 57	\$ 51	\$ 56	\$ 47
Export – Asia	87	79	86	81
Export – USA	57	41	58	51
Total log sales realizations - USD	\$ 84	\$ 76	\$ 83	\$ 76
Log sales volume (thousand m ³)				
Domestic	333.2	194.8	1,002.8	627.8
Export – Asia	364.3	170.6	1,126.7	489.8
Export – USA	44.7	16.0	111.8	82.8
Total log sales volume	742.2	381.4	2,241.3	1,200.4
Log sales mix (thousand m ³)				
Fir	414.0	214.0	1,294.5	753.6
Hembal	255.4	127.2	731.2	308.9
Cedar	33.4	15.0	114.1	59.7
Other	39.4	25.2	101.5	78.2
Total log sales mix	742.2	381.4	2,241.3	1,200.4
Log production volume (thousand m ³)				
Public tenures	174.4	164.3	540.8	199.9
Private timberlands	311.7	169.3	1,277.8	708.4
Total production volume	486.1	333.6	1,818.6	908.3
Log production costs (\$/m ³)	\$ 67	\$ 78	\$ 63	\$ 75
Timberland cost of sales (\$/m ³)	66	77	64	74
Timberland operating margin (% of log sales)	11%	(14)%	12%	(6)%

Log sales revenues for the three months ended September 30, 2010 increased by 110% from the same quarter last year due to a 95% increase in the sales volumes and a \$6 per m³ increase in average log sales realizations. Log sales revenues for the nine months ended September 30, 2010 were up 93% from the same period last year due to an 87% increase in the sales volumes and a \$3 per m³ increase in average log sales realizations.

Log sales volumes increased in all markets for the quarter and year to date compared to the same periods in 2009. Volumes to Asia more than doubled from the same periods in 2009. Strong pricing in Asia helped to offset a stronger Canadian dollar during the third quarter of 2010 compared to the same quarter in 2009.

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Timberland sales include other sales of \$10.0 million and \$29.0 million for the three and nine months ended September 30, 2010, compared to \$3.3 million and \$5.5 million for the same periods in 2009. These sales in Q3, 2010 and the nine months ended September 30, 2010 include \$8.6 million and \$24.3 million, respectively, of shipping services to Asian customers. These include ocean freight and ship loading as a result of vessels TimberWest chartered to ship to Asian markets (Q3, 2009 - \$1.4 million and nine months ended September 30, 2009 - \$2.1 million). These other sales are offset by ocean freight and ship loading costs reported in cost of sales and result in no margin.

Unit logging production costs for the three and nine months ended September 30, 2010 improved by 14% and 16% over the respective periods in 2009. Lower unit costs are a result of higher production volumes over fixed costs as well as competitive contract rates on public and private land operations. These lower costs combined with higher revenues resulted in higher margins compared to the first three quarters of 2009.

Real estate

(in millions of dollars except where otherwise noted)	Three months ended		Nine months ended	
	September 30 2010	2009	September 30 2010	2009
Sales	\$ 0.5	\$ 7.9	\$ 11.5	\$ 14.8
Price per acre (\$/acre)	22,534	4,058	3,860	3,754

The Company's real estate division, Couverdon, sells higher and better use non-core landholdings, pursues entitlements on core development properties and markets these properties.

Deferred costs related to entitlement and planning activities were \$0.9 million and \$1.9 million, for the three and nine months ended September 30, 2010 respectively. Comparatively, deferred costs were \$0.2 million and \$0.4 million for the three and nine months ended September 30, 2009 respectively.

Real estate sales generally vary from year to year and quarter to quarter reflecting the variable nature and timing of real estate sales activity.

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5. Financial condition

The following table highlights the significant changes between the consolidated balance sheets as at September 30, 2010 and December 31, 2009:

(in millions of dollars)	September 30, 2010	December 31, 2009	Increase / (decrease)	
Cash and cash equivalents	\$ 3.6	\$ 1.8	\$ 1.8	The increase in cash is primarily the result of timing of cash receipts at period end. Refer to section 6 "Liquidity and capital resources" for greater detail.
Current assets, excluding cash and cash equivalents	45.4	37.6	7.8	The increase is primarily due to an increase in log inventory by \$1.3 million which reflects a 10% increase in inventory volumes; accounts receivable has increased by \$4.2 million; and prepaids and other assets increased by \$1.9 million.
Property, plant and equipment	1,208.7	1,213.0	(4.3)	The decrease is due to the sale of real estate properties and depreciation recorded in the period, partially offset by additions and capitalized development costs.
Other assets	11.4	12.0	(0.6)	The decrease in other assets is due to the amortization of the capitalized financing costs associated with the restructuring of the Company's credit facilities in 2009 offset in part with an increase in the fair value of the Company's financial instruments.
Current liabilities	61.7	27.2	34.5	The increase is primarily due to the reclassification of deferred distributions of \$30.5 million from long-term to current, as they become due within one year.
Revolving credit facilities	92.7	152.6	(59.9)	The decrease is primarily due to the reduction of the revolving facility with the net proceeds from the Stapled Unit issuance in May 2010.
Convertible debentures	202.3	207.8	(5.5)	The decrease is due to changes in fair value offset by the issuance of convertible debentures in 2010 as a result of paying \$7.0 million (face value) payments in kind. Refer to the note 11 in the notes to the unaudited interim consolidated financial statements. The face value of the convertible debentures is \$160.3 million at September 30, 2010.
Other long-term liabilities	221.3	241.5	(20.2)	The decrease is primarily due to the reclassification of deferred distributions of \$30.5 million from long-term to current offset by the increase in deferred distributions of \$12.2 million over December 31, 2009.
Series A Subordinate Notes owned by unitholders	309.6	247.1	62.5	The increase is primarily due to the \$60 million Stapled Unit issuance during the year and the recognition of accretion during the period.
Unitholders' Equity	\$ 381.5	\$ 388.0	\$ (6.5)	The decrease is due to the net loss for the period; offset in part by the increase in common shares issued as a result of the Stapled Unit issuance.

TIMBERWEST FOREST CORP.

6. Liquidity and capital resources

Selected financial information

(in millions of dollars except where otherwise noted)	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Cash provided by (used in):				
Operating activities from continuing operations	\$ (4.7)	\$ (11.0)	\$ (1.8)	\$ (30.3)
Financing activities	4.0	5.5	(2.6)	(8.6)
Investing activities	(1.7)	6.1	6.2	10.6
Cash used in discontinued operations	-	(0.5)	-	(1.4)
Increase (decrease) in cash and cash equivalents	\$ (2.4)	\$ 0.1	\$ 1.8	\$ (29.7)
Consolidated debt-to-total capitalization ratio ¹	9:91	15:85	9:91	15:85

1 The consolidated debt-to-total capitalization ratio does not have a standardized meaning prescribed by GAAP and may not be comparable to similar measures presented by other companies. Debt includes the senior debt held by a syndicate of banks. Management believes that the presentation of these measures will enhance an investor's understanding of the Company's operating performance.

The Company's primary cash requirements during the industry downturn are to fund operations, capital expenditures and interest payments on the Company's debt and convertible debt instruments. In the last two years, the Company took steps to improve its competitiveness by decreasing the number of employees to 81 at the end of 2009, restructuring its contractor arrangements, paying interest on the convertible debentures in kind for a period of one year, changing to a variable interest rate on the Series A Subordinate Notes, deferring interest payments on these notes for the foreseeable future, raising \$60.0 million through a public Stapled Unit offering in Q2, 2010, and diversifying its markets with a greater share of the sales mix going to Asia.

Operating

The increase in cash provided by continuing operating activities for Q3 and the nine months ended September 30, 2010 compared to the same periods last year is due to improved net earnings before non-cash expenses. No cash distributions were paid to unitholders in the nine months periods ended September 30, 2010 and 2009.

Financing Activities

During Q3, 2010, the Company increased its borrowings on its credit facilities by \$4.0 million. For the nine months ended September 30, 2010, the Company reduced its borrowings by \$59.9 million, received proceeds of \$60.0 million for the Stapled Unit bought deal issuance and received proceeds from the exercise of 148,181 Stapled Unit options of \$0.5 million. The transaction costs associated with the Stapled Unit bought deal were \$3.2 million.

As at November 8, 2010 the Company had 90,823,934 issued and outstanding Stapled Units and 2,916,917 granted and outstanding Stapled Unit option awards.

The Company has the option to pay the interest on the convertible debentures in kind in order to preserve liquidity. In Q3, 2010, interest was paid in cash to the holders of the convertible debentures and no additional convertible debentures were issued by the Company. For the nine months ended September 30, 2010 convertible debentures with a face value of \$7.0 million were issued as payment in kind for the January 15, 2010 and April 15, 2010 interest payments. The face value of the convertible debentures is \$160.3 million at September 30, 2010 on which interest accrues at 9%. Interest on the convertible debentures accrued and payable as at September 30, 2010 of \$3.6 million was paid in cash on October 15, 2010.

In the nine months ended September 30, 2009, the Company issued convertible debentures for cash proceeds of \$150.0 million, of which \$75.0 million was used to permanently pay down the credit facility, with the remainder

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reducing indebtedness under the revolving credit facility and to fund company operations. In 2009, the Company also completed a new three-year secured revolving credit refinancing arrangement with its syndicate of banks which resulted in the Company having access to \$220 million in this credit facility. No Stapled Unit options were exercised in the nine months ended September 30, 2009 and as a result no Stapled Units were issued.

In 2009, transaction costs associated with the refinancing were \$9.0 million; \$5.5 million was expensed against income as it relates to the convertible debentures, which have been designated as held for trading and \$3.5 million was deferred and capitalized on the balance sheet as these costs relate to debt refinancing held at amortized cost.

Cash and cash equivalents at the end of Q3, 2010 were \$3.6 million compared to \$1.8 million at December 31, 2009. The Company's consolidated debt-to-total capitalization ratio as at September 30, 2010 was 9:91 compared to 15:85 at December 31, 2009.

Investing Activities

The decrease in cash provided by investing activities in Q3, 2010 compared to Q3, 2009 and for the nine months ended September 30, 2010 compared to the nine months ended September 30, 2009 was due to increased spending on property, plant and equipment and reduced proceeds from the sale of property, plant and equipment, namely real estate.

Capital resources

The Company's capital resources at September 30, 2010 include amounts available under the revolving credit facility and the convertible debentures. Credit ratings for the Company have been confirmed by Dominion Bond Rating service at BBB in 2009.

Available capital resources and total liquidity at period-end is summarized in the following table:

(in millions of dollars)	2010	2010	2010	2009	2009
	Q3	Q2	Q1	Q4	Q3
Borrowing base					
Revolving credit facility (due February 11, 2012)	\$ 220.0	\$ 220.0	\$ 220.0	\$ 220.0	\$ 250.0
Convertible debentures, at face value (due February 11, 2014)	160.3	160.3	156.8	153.4	150.0
Total borrowing base	380.3	380.3	376.8	373.4	400.0
Letters of credit	14.5	14.5	16.4	16.4	16.4
Amount drawn, net	253.0	249.0	311.4	306.0	293.0
Available to be drawn	112.8	116.8	49.0	51.0	90.6
Cash on hand	3.6	6.0	4.0	1.8	1.1
Total liquidity	\$ 116.4	\$ 122.8	\$ 53.0	\$ 52.8	\$ 91.7

As of September 30, 2010, the Company had \$116.4 million of available liquidity, comprised of \$3.6 million of cash on hand and \$112.8 million available to be drawn on its \$220.0 million revolving credit facility. Compared to December 31, 2009 the Company's total liquidity increased by \$63.6 million, primarily due to the \$60.0 million Stapled Unit offering completed in the second quarter and improved timberland operating earnings.

TIMBERWEST FOREST CORP.**Debt**

At September 30, 2010, the total debt calculated for financial reporting purposes was \$295.0 million. The following table outlines the changes in the Company's long-term debt for the quarter ended September 30, 2010:

Issue (in millions of dollars)	June 30, 2010	Net increase (decrease)	September 30, 2010
Secured revolving credit facility of up to \$230.0 ¹ million due February 11, 2012 with interest based on Canadian or U.S. Prime rates + 5%, or Canadian BA rates + 6%	\$ 88.7	\$ 4.0	\$ 92.7
Convertible debentures with a face value of \$160.3 million as of September 30, 2010, due February 11, 2014	208.2	(5.9) ²	202.3
Total long-term debt	\$ 296.9	\$ (1.9)	\$ 295.0

1 The secured, revolving facility will increase from \$220.0 million to \$230.0 million beginning January 1, 2011 provided certain EBITDA levels are achieved, otherwise it will reduce to \$215.0 million of available capacity.

2 The convertible debentures are designated as held-for-trading for accounting purposes and as such are valued at fair value. The decrease in Q3, 2010 over Q2, 2010 is the result of a fair value adjustment of \$5.9 million.

Refer to the Company's unaudited interim consolidated financial statements for the three and nine months ended September 30, 2010, Note 10 for details related to covenant compliance. The Company is in compliance with its covenants.

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7. Summary of Quarterly Information

The following table presents selected unaudited quarterly financial information for each of the Company's last eight quarters. This data has been derived from the unaudited interim consolidated financial statements that have been prepared on the same basis as the 2009 annual audited consolidated financial statements. In the Company's opinion, the amounts include all normal recurring adjustments necessary for the fair presentation of such information. These financial results are not necessarily indicative of results for any future period and should not be relied upon to predict future performance.

The Company operates in a cyclical industry and it also experiences some seasonal fluctuations in quarterly results due to weather-related factors having an effect on harvesting operations. Earnings in the second half of the year generally trend lower as the result of fire season shutdowns and increased costs of harvesting at higher elevations.

Unaudited (in millions of dollars)	2010				2009			2008	
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4	
Sales	\$ 65.9	\$ 80.9	\$ 58.7	\$ 44.4	\$ 37.5	\$ 38.0	\$ 30.4	\$ 35.9	
Operating earnings (loss) from continuing operations	1.6	8.8	2.0	(3.1)	(2.2)	(4.6)	(3.1)	(8.6)	
Net earnings (loss) from continuing operations	0.6	17.1	(24.7)	8.3	(25.9)	(30.2)	(7.6)	312.3 ²	
Net earnings (loss) from discontinued operations	-	-	-	(0.1)	(0.1)	(0.1)	(0.1)	2.3	
Net earnings (loss)	0.6	17.1	(24.7)	8.2	(26.0)	(30.3)	(7.7)	314.6	
Earnings (loss) from continuing operations available for distribution ¹	4.9	21.3	(21.0)	12.0	(22.3)	(26.7)	(4.2)	330.1	
Earnings (loss) from continuing operations available for distribution before accretion, changes in fair value of financial instruments held for trading, gain on modification of Series A Subordinate Notes and provision for future income tax expense (recovery) ¹	(4.6)	2.4	(4.7)	(9.6)	(8.3)	(11.0)	(13.4)	(11.2)	
Distributable cash from continuing operations ¹	(4.7)	4.0	(2.9)	(10.1)	(3.7)	(5.3)	(15.2)	(11.4)	
Distributable cash from discontinued operations ¹	-	-	-	(0.1)	(0.1)	(0.1)	(0.1)	-	
Distributable cash ¹	(4.7)	4.0	(2.9)	(10.2)	(3.8)	(5.4)	(15.3)	(11.4)	
Distributions paid	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 21.0	

1 Earnings from continuing operations available for distribution and distributable cash are measures that do not have a standardized meaning prescribed by GAAP and may not be comparable to similar measures presented by other companies. Management believes that presentation of these measures will enhance an investor's understanding of the Company's operating performance.

2 The net earnings from continuing operations for Q4, 2008 includes a gain on the modification of the Series A Subordinate Notes of \$342.0 million, net of income taxes. Excluding this gain, the net loss from continuing operations is \$29.7 million.

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Unaudited	2010			2009			2008	
(in millions of dollars except per common share and per Stapled Unit amounts)	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Per common share¹ – basic								
Net earnings (loss) from continuing operations	\$ 0.01	\$ 0.20	\$ (0.32)	\$ 0.11	\$ (0.33)	\$ (0.39)	\$ (0.10)	\$ 4.02
Net earnings (loss) from discontinued operations	-	-	-	(0.01)	-	-	-	0.03
Net earnings (loss)	0.01	0.20	(0.32)	0.10	(0.33)	(0.39)	(0.10)	4.05
Per common share¹ – diluted								
Net earnings (loss) from continuing operations	\$ 0.01	\$ 0.14	\$ (0.32)	\$ 0.07	\$ (0.33)	\$ (0.39)	\$ (0.10)	\$ 4.02
Net earnings (loss) from discontinued operations	-	-	-	-	-	-	-	0.03
Net earnings (loss)	0.01	0.14	(0.32)	0.07	(0.33)	(0.39)	(0.10)	4.05
Per Stapled Unit¹ – basic								
Earnings (loss) from continuing operations available for distribution	\$ 0.05	\$ 0.25	\$ (0.27)	\$ 0.15	\$ (0.29)	\$ (0.34)	\$ (0.05)	\$ 4.24
Earnings (loss) from continuing operations available for distribution before accretion, changes in fair value of financial instruments held for trading, gain on modification of Series A Subordinate Notes and provision for future income tax expense (recovery)	(0.05)	0.03	(0.06)	(0.12)	(0.11)	(0.14)	(0.17)	(0.14)
Distributable cash from continuing operations ²	(0.05)	0.05	(0.04)	(0.13)	(0.05)	(0.07)	(0.20)	(0.15)
Distributable cash from discontinued operations ²	-	-	-	-	-	-	-	-
Distributable cash ²	(0.05)	0.05	(0.04)	(0.13)	(0.05)	(0.07)	(0.20)	(0.15)
Distributions paid	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 0.27
Per Stapled Unit¹ – diluted								
Earnings (loss) from continuing operations available for distribution	\$ 0.05	\$ 0.19	\$ (0.27)	\$ 0.15	\$ (0.29)	\$ (0.34)	\$ (0.05)	\$ 4.24
Earnings (loss) from continuing operations available for distribution before accretion, changes in fair value of financial instruments held for trading, gain on modification of Series A Subordinate Notes and provision for future income tax expense (recovery)	(0.05)	0.05	(0.06)	(0.12)	(0.11)	(0.14)	(0.17)	(0.14)
Distributable cash from continuing operations ²	(0.05)	0.06	(0.04)	(0.13)	(0.05)	(0.07)	(0.20)	(0.15)
Distributable cash from discontinued operations ²	-	-	-	-	-	-	-	-
Distributable cash ²	(0.05)	0.06	(0.04)	(0.13)	(0.05)	(0.07)	(0.20)	(0.15)
Distributions paid	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 0.27

1 Per common share and per Stapled Unit amounts presented for each quarter have been determined based on the weighted average number of common shares or weighted average number of Stapled Units outstanding during the quarter. Per common share and per Stapled Unit amounts by quarter do not necessarily add to the total of the year due to changes in the weighted average number of common shares and Stapled Units outstanding during the year.

2 Distributable cash does not have a standardized meaning prescribed by Canadian GAAP and may not be comparable to similar measures presented by other companies. Management believes that the presentation of this measure will enhance an investor's understanding of the Company's operating performance.

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8. Impact of accounting pronouncements affecting future periods

On February 13, 2008, the Canadian Accounting Standards Board (“AcSB”) confirmed the use of International Financial Reporting Standards (“IFRS”) to commence in 2011 for publicly accountable profit-oriented enterprises. IFRS will replace Canada’s Generally Accepted Accounting Principles (“GAAP”) and the official changeover date is for interim and annual financial statements relating to fiscal periods beginning on or after January 1, 2011.

IFRS are premised on a conceptual framework similar to GAAP, however, significant differences exist in certain matters of recognition, measurement and disclosure. TimberWest will adopt IFRS according to requirements outlined by the AcSB, and is in the process of preparing for the adoption of IFRS on January 1, 2011.

The Company’s IFRS conversion project began in 2008 and it has established a formal project governance structure which includes the audit committee, senior management and a steering committee. A detailed review of the impact of IFRS on the Company’s financial statements is ongoing. A qualified external advisor has been engaged by the Company to assist in the IFRS conversion project. The audit committee is updated on a quarterly basis and training is provided as necessary. The project is progressing according to plan.

The Company’s IFRS conversion project consists of four phases: raise awareness; assessment; design; and implementation. The Company expects the transition to IFRS to impact accounting, financial reporting, internal control over financial reporting, taxes, information systems and processes.

The Company has identified areas that are expected to be impacted by the conversion to IFRS. These areas include the Company’s private timberlands, higher and better use lands, impairment of assets, provisions, and employee future benefits. The Company has engaged qualified external valuers to perform valuations of the Company’s private timberlands and HBU properties. These valuations are well underway and will assist in determining the Company’s opening balance sheet at January 1, 2010. The Company continues to assess the financial reporting impact of IFRS on these areas and will make IFRS accounting policy choices throughout 2010. The Company will complete an internal control financial reporting assessment once final policy decisions have been made.

Identification of impacts on business activities is ongoing. Adoption of IFRS is not expected to have any material impact on the Company’s contracts. The adoption of IFRS is not expected to materially affect the current bank debt covenants as the covenants will continue to be calculated based on current GAAP.

A review of the current information systems was performed and the Company does not expect IFRS to have a significant impact on these systems in the near future. The current information system in place for financial reporting allows for the Company to capture financial information under GAAP and IFRS. The Company will continue to monitor its systems requirements as the transition to IFRS progresses.

As the Company continues to evaluate the impact of adoption on its processes and accounting policies it will provide updated disclosure where appropriate.

9. Disclosure controls and internal control over financial reporting

During the quarter ended September 30, 2010, there was no change in the Company’s internal control over financial reporting that has materially affected, or is reasonably likely to materially affect the Company’s internal control over financial reporting.

TIMBERWEST FOREST CORP.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

Unaudited (in millions of dollars, except per share amounts)	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Sales	\$ 65.9	\$ 37.5	\$ 205.5	\$ 105.9
Operating costs and expenses:				
Cost of sales	61.0	35.8	181.7	104.4
Selling, administrative and other	2.3	2.7	8.2	8.4
Depreciation, depletion and amortization	1.0	1.2	3.2	3.0
	64.3	39.7	193.1	115.8
Operating earnings (loss) from continuing operations	1.6	(2.2)	12.4	(9.9)
Interest expense:				
Series A Subordinate Notes owned by unitholders	6.2	5.3	17.6	15.4
Convertible debentures	3.6	3.4	10.7	8.5
Long-term bank debt	2.0	2.5	6.9	7.2
Short-term bank debt	-	-	-	0.5
	11.8	11.2	35.2	31.6
Financing transaction costs	-	-	-	5.5
Amortization of deferred financing costs	0.6	0.4	2.2	1.3
Loss (gain) on change in fair value of financial instruments held for trading (notes 9, 11 and 16)	(7.2)	13.1	(14.9)	24.7
Other expense (income)	-	(0.2)	-	(0.2)
	5.2	24.5	22.5	62.9
Loss before income taxes from continuing operations	(3.6)	(26.7)	(10.1)	(72.8)
Income tax recovery (note 5)	(4.2)	(0.8)	(3.1)	(9.1)
Net earnings (loss) and comprehensive earnings (loss) from continuing operations	0.6	(25.9)	(7.0)	(63.7)
Net loss and comprehensive loss from discontinued operations (note 4)	-	(0.1)	-	(0.3)
Net earnings (loss) and comprehensive earnings (loss)	\$ 0.6	\$ (26.0)	\$ (7.0)	\$ (64.0)
Basic and diluted earnings (loss) from continuing operations per share (note 6)	0.01	(0.33)	(0.08)	(0.82)
Basic and diluted earnings (loss) per share (note 6)	0.01	(0.33)	(0.08)	(0.82)

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS (DEFICIT)

Unaudited (in millions of dollars)	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Retained earnings, beginning of period	\$ 187.4	\$ 212.8	\$ 195.0	\$ 250.8
Net earnings (loss) and comprehensive earnings (loss) for the period	0.6	(26.0)	(7.0)	(64.0)
Retained earnings, end of period	\$ 188.0	\$ 186.8	\$ 188.0	\$ 186.8

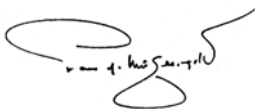
See accompanying notes to the unaudited interim consolidated financial statements.

TIMBERWEST FOREST CORP.**CONSOLIDATED BALANCE SHEETS**

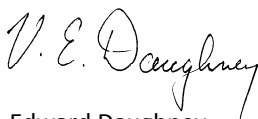
	September 30, 2010	December 31, 2009
(in millions of dollars)	Unaudited	
Assets		
Current assets:		
Cash	\$ 3.6	\$ 1.8
Accounts receivable	10.0	5.8
Inventories (note 7)	28.5	27.2
Prepaid expenses and other current assets	4.9	3.0
Future income taxes	2.0	1.6
	49.0	39.4
Property, plant and equipment (note 8)	1,208.7	1,213.0
Other assets (note 9)	11.4	12.0
	\$ 1,269.1	\$ 1,264.4
Liabilities and Unitholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 27.9	\$ 23.9
Deferred distribution payable (note 13)	33.8	3.3
Discontinued operations	-	0.2
	61.7	27.4
Revolving credit facilities (note 10)	92.7	152.6
Convertible debentures (note 11)	202.3	207.8
Long-term silviculture liability	3.3	3.0
Employee future benefits (note 12)	37.5	37.1
Deferred distribution payable (note 13)	10.5	28.8
Stapled Unit option plan (note 15)	1.1	1.5
Future income taxes	168.9	171.1
	578.0	629.3
Series A Subordinate Notes owned by unitholders (note 14)	309.6	247.1
	887.6	876.4
Unitholders' equity		
Share capital, consisting of common shares (note 14)	191.5	191.0
Contributed surplus	2.0	2.0
Retained earnings	188.0	195.0
	381.5	388.0
	\$ 1,269.1	\$ 1,264.4

See accompanying notes to the unaudited interim consolidated financial statements.

On behalf of the Board of Directors:



Paul J. McElligott
Director



V. Edward Daughney
Director

TIMBERWEST FOREST CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited (in millions of dollars)	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Cash provided by (used in):				
Operating activities:				
Net earnings (loss) from continuing operations	\$ 0.6	\$ (25.9)	\$ (7.0)	\$ (63.7)
Items not involving cash:				
Depreciation, depletion and amortization	1.6	1.6	5.4	4.3
Accretion on Series A Subordinate Notes	1.9	1.7	5.4	4.9
Gain on sale of property, plant and equipment	(0.4)	(3.9)	(5.3)	(5.5)
Future income tax recovery	(4.2)	(0.8)	(2.6)	(9.1)
Change in deferred distribution payable	4.3	3.6	12.2	10.5
Change in fair value of financial instruments held for trading	(7.2)	13.1	(14.9)	24.7
Convertible debenture interest paid in kind	-	-	7.0	-
Other non-cash items	0.1	0.8	0.5	1.0
	(3.3)	(9.8)	0.7	(32.9)
Changes in non-cash working capital:				
Accounts receivable	(1.8)	(3.1)	(4.2)	(3.1)
Inventories	7.3	1.5	(1.3)	9.0
Prepaid expenses and other working capital	1.3	(1.2)	(1.9)	(0.8)
Accounts payable and accrued liabilities	(8.2)	1.6	4.9	(2.5)
	(1.4)	(1.2)	(2.5)	2.6
	(4.7)	(11.0)	(1.8)	(30.3)
Financing activities:				
Issuance of Stapled Units:				
Series A Subordinate Notes	-	-	60.0	-
Share capital	-	-	0.5	-
	-	-	60.5	-
Convertible debentures	-	-	-	150.0
Revolving credit facilities	4.0	5.5	(59.9)	(46.8)
Term credit facilities	-	-	-	(108.3)
Financing transaction costs	-	-	(3.2)	(3.5)
	4.0	5.5	(2.6)	(8.6)
Investing activities:				
Proceeds from sale of property, plant and equipment	0.5	6.4	10.1	12.5
Additions to property, plant and equipment	(2.2)	(0.3)	(3.7)	(0.7)
Other assets	-	-	(0.2)	(1.2)
	(1.7)	6.1	6.2	10.6
Cash provided by (used in) continuing operations	(2.4)	0.6	1.8	(28.3)
Cash provided by (used in) discontinued operations (note 4)	-	(0.5)	-	(1.4)
Increase (decrease) in cash and cash equivalents	(2.4)	0.1	1.8	(29.7)
Cash and cash equivalents, beginning of period	6.0	1.0	1.8	30.8
Cash and cash equivalents, end of period	\$ 3.6	\$ 1.1	\$ 3.6	\$ 1.1
Supplemental information:				
Interest on the convertible debentures paid in cash	\$ 3.6	\$ 3.4	\$ 3.6	\$ 5.2
Other interest paid	\$ 2.1	\$ 2.5	\$ 6.7	\$ 8.7
Financing costs paid	\$ -	\$ -	\$ 3.2	\$ 9.0

See accompanying notes to the unaudited interim consolidated financial statements.

TIMBERWEST FOREST CORP.**CONSOLIDATED BUSINESS SEGMENTS**

Unaudited (in millions of dollars)	Three months ended September 30, 2010			
	Timberlands	Real Estate	Other	Total
Sales	\$ 65.4	\$ 0.5	\$ -	\$ 65.9
Operating earnings (loss)	6.1	(0.3)	(4.2)	1.6
Total assets	986.0	261.6	21.5	1,269.1
Additions to property, plant and equipment	0.3	1.2	0.7	2.2

Unaudited (in millions of dollars)	Three months ended September 30, 2009			
	Timberlands	Real Estate	Other	Total
Sales	\$ 29.6	\$ 7.9	\$ -	\$ 37.5
Operating earnings (loss)	(3.5)	4.5	(3.2)	(2.2)
Total assets	978.3	263.9	14.2	1,256.4
Additions to property, plant and equipment	-	0.2	0.1	0.3

Unaudited (in millions of dollars)	Nine months ended September 30, 2010			
	Timberlands	Real Estate	Other	Total
Sales	\$ 194.0	\$ 11.5	\$ -	\$ 205.5
Operating earnings (loss)	20.4	3.6	(11.6)	12.4
Total assets	986.0	261.6	21.5	1,269.1
Additions to property, plant and equipment	0.8	2.2	0.7	3.7

Unaudited (in millions of dollars)	Nine months ended September 30, 2009			
	Timberlands	Real Estate	Other	Total
Sales	\$ 91.1	\$ 14.8	\$ -	\$ 105.9
Operating earnings (loss)	(5.0)	5.0	(9.9)	(9.9)
Total assets	978.3	263.9	14.2	1,256.4
Additions to property, plant and equipment	0.2	0.4	0.1	0.7

In 2009, the Company commenced reporting its operating results on a segmented basis in order to disclose the results of its two significant operating segments, timberlands and real estate. Prior to 2009, the Company operated in one operating segment, timberlands, and any real estate sales were incidental to the timberland operations. Effective January 1, 2009, the Company has formed a real estate division and the activities of this division are managed separately from the timberlands operation. Sales and operating earnings reflect the income and expenses of each segment. Private land identified as having a higher and better use is reported as real estate assets at its carrying value. All other assets have been reported under the segment in which they are managed. The 'other' segment reflects those costs and assets that are allocated for general corporate purposes.

TIMBERWEST FOREST CORP.

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

For the three and nine months ended September 30, 2010 and 2009

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

1. Significant accounting policies

The accompanying unaudited interim consolidated financial statements include the accounts of TimberWest Forest Corp. and its subsidiaries ("the Company"), have been prepared in accordance with Canadian Generally Accepted Accounting Principles and are expressed in Canadian dollars. Not all disclosures required by Canadian Generally Accepted Accounting Principles ("GAAP") for annual financial statements are presented and, accordingly, these interim consolidated financial statements should be read in conjunction with the Company's most recent annual consolidated financial statements. These interim consolidated financial statements follow the same accounting policies and methods of application used in the Company's audited annual consolidated financial statements of December 31, 2009.

2. Going concern

At September 30, 2010, the Company had total liquidity available of \$116.4 million, a decrease of \$6.4 million from June 30, 2010. Based on the Company's current liquidity position and forecasted cash requirements over the remainder of 2010 and fiscal 2011, the Company does not foresee any going concern issues in the near term.

In the long term, the Company's ability to continue as a going concern will be dependent on the economic factors affecting the Company's core businesses – timberland operations and real estate. In addition, the Company's revolving credit facility will come due on February 11, 2012. Although the Company is confident in the ability of its operations and assets in the long term, the Company recognizes the economic outlook for the forest products industry mid term will be affected by economic, competitive and other factors, many of which are beyond the Company's control.

3. Segmented information

Commencing in 2009, the Company identified two reporting segments:

Timberlands - The timberland division maximizes value by harvesting logs in a cost-effective manner consistent with sound safety, environmental and sustainable forestry practices and selling these products to targeted customers in both the domestic and higher value export markets.

Real Estate – Couverdon, the real estate division of TimberWest, is mandated to realize value from land that has a higher and better use than timberlands.

The segments are managed separately. During the first quarter of 2009, the Company branded its real estate division "Couverdon Real Estate."

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

4. Discontinued operations

On May 9, 2008, the Elk Falls sawmill and planer mill in Campbell River, B.C. was permanently closed including the associated shipping operations at Stuart Channel Wharves located in Crofton, B.C. Subsequent to the closure, TimberWest disposed of all the sawmill assets and dismantled the sawmill. Ongoing costs such as property taxes continue to be expensed as incurred. The Company is assessing alternatives for the former sawmill site.

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Sales	\$ -	\$ -	\$ -	\$ -
Loss before income taxes	\$ -	\$ (0.1)	\$ -	\$ (0.3)
Net loss	\$ -	\$ (0.1)	\$ -	\$ (0.3)

Sales from the logging operations to the sawmill operations have been recorded at fair value in accordance with the Company's internal policies. There were no inter-divisional sales for the three and nine months ended September 30, 2010 (2009 - nil).

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Cash flow from operating activities	\$ -	\$ (0.5)	\$ -	\$ (1.4)
Cash flow from financing activities	-	-	-	-
Cash flow from investing activities	-	-	-	-
Cash provided by operations	\$ -	\$ (0.5)	\$ -	\$ (1.4)

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

5. Income taxes

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Current income tax recovery	\$ -	\$ -	\$ (0.5)	\$ -
Future income tax expense (recovery)	(4.2)	(0.8)	(2.6)	(9.1)
	\$ (4.2)	\$ (0.8)	\$ (3.1)	\$ (9.1)

In the third quarter of 2010, the Company recorded a future income tax recovery of \$4.2 million primarily due to a change in estimated non-capital loss carryforwards as a result of recent income tax filings.

In the first quarter of 2009, British Columbia provincial tax legislation was substantively enacted, resulting in the reduction of the provincial corporate tax rate to 10.5% for the year ending December 31, 2010 and 10% thereafter. This tax rate change resulted in a future income tax recovery of \$6.2 million and is included in the future income tax recovery for the nine months ended September 30, 2009.

6. Earnings (loss) per share

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Net earnings (loss) from continuing operations	\$ 0.6	\$ (25.9)	\$ (7.0)	\$ (63.7)
Net earnings (loss)	0.6	(26.0)	(7.0)	(64.0)
Basic weighted average number of common shares	89,938,487	77,776,574	83,824,954	77,770,620
Incremental common shares from potential exercise of options	359,864	297,447	484,297	152,320
Diluted weighted average number of common shares	90,298,351	78,074,021	84,309,251	77,922,940
Basic and diluted net earnings (loss) from continuing operations per common share	0.01	(0.33)	(0.08)	(0.82)
Basic and diluted net earnings (loss) from discontinued operations per common share	-	-	-	-
Basic and diluted net earnings (loss) per common share	0.01	(0.33)	(0.08)	(0.82)

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

7. Inventories

	September 30, 2010	December 31, 2009
Logs	\$ 28.5	\$ 27.2

The \$1.3 million increase in log inventory from December 31, 2009 is primarily due to increased logging production.

For the three months ended September 30, 2010, the write-down associated with accounting for log inventories at net realizable value increased by \$0.2 million at September 30, 2010 over June 30, 2010, which was expensed to cost of sales for the period (Q3, 2009 - \$0.2 million decrease to the write-down to log inventory, which was offset against cost of sales for the period).

For the nine months ended September 30, 2010, the write-down associated with accounting for log inventories at net realizable value was reduced by \$0.4 million at September 30, 2010 over December 31, 2009, which was offset against cost of sales for the period (2009 - \$0.6 million decrease to the write-down to log inventory, which was offset against cost of sales for the period).

8. Property, plant and equipment

Property, plant and equipment at September 30, 2010, includes private lands with a carrying value of \$1,163.0 million (December 31, 2009 - \$1,165.9 million). This amount includes a valuation increase adjustment of \$372.2 million resulting from the adoption of Section 3465 – Income Taxes of the CICA Handbook, which was mandatory for fiscal years ending on or after January 1, 2000.

9. Other assets

	September 30, 2010	December 31, 2009
Deferred financing costs	\$ 3.2	\$ 5.4
Financial instruments	7.3	5.9
Other	0.9	0.7
	\$ 11.4	\$ 12.0

Financial instruments of \$7.3 million include the value of two embedded derivatives as outlined below.

The Company has the option to defer the distributions payable to its unitholders for a period of up to 18 months in length while the distribution rate is set at 2% (note 14). This option constitutes an embedded derivative and is measured at its fair value. As the Company has elected to defer distributions for the immediate future, the value of this option is \$6.6 million (2009 - \$5.2 million).

The embedded derivative arising from the option to extend the maturity of the Series A Subordinate Notes for a further 10-year period from 2038 to 2048 is measured at its fair value of \$0.7 million (2009 - \$0.7 million).

Changes in the fair value of these embedded derivatives from one period to the next are recognized in the statement of operations and comprehensive income (loss) in the period (note 16).

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

10. Credit facilities

The Company's credit facilities are as follows:

	September 30, 2010	December 31, 2009
Secured revolving credit facility of up to \$230.0 million due February 11, 2012 with interest based on Canadian or U.S. Prime rates + 5%, or Canadian BA rates + 6%	\$ 92.7	\$ 152.6

Under the secured revolving credit facility, funds are available to the Company in Canadian and US dollars by way of adjusted Canadian bankers' acceptances plus 6%, or Canadian or U.S. prime rates plus 5% loans and letters of credit. This facility has been underwritten by a syndicate of banks and is due on February 11, 2012.

The facility includes financial covenants to maintain:

- a waiver of the minimum EBITDA tests for both 2010 and 2011, with the maximum availability under the line set at \$220 million for 2010 and \$215 million for 2011. So long as the Company generates minimum EBITDA of \$325,000 per quarter on a cumulative basis in 2011, then the maximum availability under the line will be increased to \$230 million for 2011;
- consolidated tangible net worth at the end of each quarter in excess of \$700 million;
- consolidated debt is less than 40% of capitalization;
- consolidated debt is less than 40% of the market value of the Company's private timberlands and higher use properties; and
- a permanent repayment provision which specifies that once cumulative real estate proceeds exceed \$50 million, 50% of additional proceeds will be applied to permanently reduce the facility size. The remaining 50% can be used by the Company to improve its liquidity. Current cumulative real estate proceeds are \$34.9 million.

The complete terms of the revolving credit agreement and amendment are filed on SEDAR.

Bank EBITDA calculations include proceeds of real estate sales and other items. At September 30, 2010 the Company is in compliance with the terms of its credit facility.

Transaction costs related to this financing have been deferred and capitalized on the balance sheet as they relate to debt refinancing held at amortized cost. The unamortized balance of these costs at September 30, 2010 was \$3.2 million. Amortization of deferred financing costs relating to the credit facility recognized on the consolidated statements of operation and comprehensive income for the three months and nine months ended September 30, 2010 was \$0.6 million and \$2.2 million, respectively (2009 - \$0.4 million and \$1.3 million, respectively).

On April 27, 2010, the Company completed an amendment to the bank loan agreement with its syndicate of banks. The amendment removes the requirement that the Company pay interest on its convertible debentures by issuing additional convertible debentures in lieu of cash. In connection with the amendment, the Company cannot make cash distributions on the Stapled Units unless its available cash exceeds, in the applicable year, the following thresholds: \$90 million in 2010; \$75 million in 2011; and \$75 million in 2012.

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

11. Convertible debentures

Details as to the Company's convertible debentures are as follows:

	Face Value	Fair Value
Balance, December 31, 2008	\$ -	\$ -
Nine months ended, September 30, 2009		
Change in value as a result of:		
Initial convertible debentures issuance, February 11, 2009	150.0	150.0
Change in fair value		22.8
Balance, September 30, 2009	\$ 150.0	\$ 172.8
Balance, December 31, 2009	\$ 153.4	\$ 207.8
Nine months ended, September 30, 2010		
Change in value as a result of:		
Interest paid in kind through issuance of convertible debentures	7.0	9.5
Conversions	(0.1)	(0.1)
Change in fair value		(14.9)
Balance, September 30, 2010	\$ 160.3	\$ 202.3

The convertible debentures mature on February 11, 2014 and are convertible into Stapled Units at \$3.50. The convertible debentures pay interest quarterly at 9% with the first interest payment made on April 15, 2009.

The Company has elected to designate this obligation as 'held-for-trading' and it is to be revalued at fair value at each reporting date. Changes in fair value from one period to the next are recognized in the statement of operations and comprehensive income (loss) in the period. For the three and nine months ended September 30, 2010 the change in fair value was a gain of \$5.9 million, and 14.9 million, respectively (Q3, 2009 – loss of \$12.1 million, and 22.8 million, respectively) (note 16). To determine the fair value of the convertible debentures management relies on the current trading price of the securities in the market. The key reason that the fair value has decreased is because of a lower Stapled Unit trading price of \$4.00 at September 30, 2010 compared to the Stapled Unit trading price of \$4.34 at December 31, 2009. Transaction costs of \$5.5 million were incurred and expensed to the statement of operations in 2009.

For the three months ended September 30, 2010, the Company paid the July 15, 2010 interest of \$3.6 million in cash (Q3, 2009 - \$3.4 million in cash). For the nine months ended September 30, 2010 the Company paid interest in kind by issuing additional convertible debentures with a face value of \$7.0 million and a fair value of \$9.5 million, for the January 15 and April 15, 2010 convertible debenture interest payments. For the nine months ended September 30, 2009, the Company paid \$5.2 million in cash for the April 15 and July 15 interest payments.

For the three and nine months ended September 30, 2010 the Company recorded interest expense on the convertible debentures of \$3.6 million and \$10.7 million respectively (2009 - \$3.4 million and \$8.5 million). The interest obligation outstanding at September 30, 2010 was paid in cash on October 15, 2010.

There were no conversions during the three months ended September 30, 2010 (Q3, 2009 – no conversions). Conversions during the nine months ended September 30, 2010, were \$0.1 million at face value with 13,674 Stapled Units being issued upon conversion (2009 – debentures with a face value of \$38,500 were converted into 11,134 Stapled Units).

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

12. Employee future benefits

	September 30, 2010	December 31, 2009
Pension benefits	\$ 9.5	\$ 9.6
Non-pension benefits	28.0	27.5
	\$ 37.5	\$ 37.1

The Company, through its subsidiaries, maintains pension plans that include defined benefit and defined contribution segments available to all salaried employees and a small number of hourly retirees not covered by union pension plans. For the three months ended September 30, 2010, the Company recorded an expense of \$0.5 million for pension benefit costs (2009 – \$0.4 million) and made cash payments of \$0.4 million to fund current service costs (2009 – \$0.3 million). For the nine months ended September 30, 2010, the Company recorded an expense of \$1.3 million for pension benefit costs (2009 – \$1.2 million) and made cash payments of \$1.2 million to fund current service costs (2009 – \$1.2 million).

The Company also provides non-pension benefits consisting of group life insurance and medical benefits to eligible retired employees, which the Company funds on an as-incurred basis. For the three months ended September 30, 2010, the Company recorded an expense of \$0.7 million for non-pension benefit costs (2009 – \$0.6 million) and made cash payments of \$0.2 million to fund current benefit costs (2009 – \$0.2 million). For the nine months ended September 30, 2010, the Company recorded an expense of \$1.9 million for non-pension benefit costs (2009 – \$1.9 million) and made cash payments of \$1.5 million to fund current benefit costs (2009 – \$1.4 million).

13. Deferred distribution payable

	Rate	Due Date	Face Value	September 30, 2010	December 31, 2009
October 15, 2010 distribution	2%	April 15, 2012	\$ 4.0	\$ 3.6	\$ -
July 15, 2010 distribution	2%	January 15, 2012	4.0	3.7	-
April 15, 2010 distribution	2%	October 15, 2011	3.5	3.2	-
January 15, 2010 distribution	2%	July 15, 2011	3.5	3.3	3.1
October 15, 2009 distribution	2%	April 15, 2011	3.5	3.4	3.2
July 15, 2009 distribution	2%	January 15, 2011	3.5	3.4	3.3
April 15, 2009 distribution	2%	October 15, 2010	3.5	3.5	3.3
January 15, 2009 distribution	12%	April 15, 2011	21.0	20.2	19.2
			\$ 46.5	\$ 44.3	\$ 32.1
Less current portion			(35.0)	(33.8)	(3.3)
			\$ 11.5	\$ 10.5	\$ 28.8

The Company can defer distributions on its Series A Subordinate Notes after December 31, 2008 for up to 18 months while the distribution rate is set at 2% (note 14) and defer the January 15, 2009 distribution for up to 27 months. As a result of these deferrals, the deferred distribution payable is accounted for at its fair value and the obligation is revalued at each reporting date.

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

For the three and nine months ended September 30, 2010 and 2009

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14. Stapled units

	Number	Series A Subordinate Notes	Stapled Unit Components			Total Share Capital	Total Stapled Units
			Preferred Shares	Common Shares	Issue Costs		
Nine months ended September 30, 2009:							
Balance, December 31, 2008	77,765,440	\$ 240.4	\$ 190.1	\$ 31.4	\$ (30.5)	\$ 191.0	\$ 431.4
Issuance of Stapled Units on conversion of debentures	11,134	0.1	-	-	-	-	0.1
Accretion on Series A Subordinate Notes	-	4.9	-	-	-	-	4.9
Conversion of preferred shares into common shares	-	-	(190.1)	190.1	-	-	-
Balance, September 30, 2009	77,776,574	\$ 245.4	\$ -	\$ 221.5	\$ (30.5)	\$ 191.0	\$ 436.4
Nine months ended September 30, 2010:							
Balance, December 31, 2009	77,776,632	\$ 247.1	\$ -	\$ 221.5	\$ (30.5)	\$ 191.0	\$ 438.1
Issuance of Stapled Units on public equity offering	12,000,000	56.3	-	0.5	-	0.5	56.8
Issuance of Stapled Units on conversion of debentures	13,674	0.1	-	-	-	-	0.1
Issuance of Stapled Units on exercise of options	148,181	0.7	-	-	-	-	0.7
Accretion on Series A Subordinate Notes	-	5.4	-	-	-	-	5.4
Balance, September 30, 2010	89,938,487	\$ 309.6	\$ -	\$ 222.0	\$ (30.5)	\$ 191.5	\$ 501.1

The Company issues equity by way of Stapled Units, each Stapled Unit consisting of approximately \$8.98 face amount of Series A Subordinate Notes and one common share. The securities comprising a Stapled Unit trade together as Stapled Units and cannot be transferred except with each other as part of a Stapled Unit until the date of maturity of the Series A Subordinate Notes or the payment of the principal amount of the Series A Subordinate Notes following an event of default and expiration of a remedies blockage period.

On December 19, 2008 the holders of the Stapled Units approved a series of note amendments that came into effect on December 31, 2008. The note amendments are as follows: (i) the rate of interest on the Series A Subordinate Notes payable was changed from a fixed 12% per annum to a variable rate between 2% and 12% per annum to be set from time to time based on the Company's distributable cash; (ii) the period over which the Company can defer payments of interest on the notes was reduced from 27 months to 18 months, and the Company may only exercise this deferral right in respect of interest payments for periods where the applicable interest rate on the subordinate notes is 2%; and (iii) replaces the Company's right to elect to pay interest on the subordinate notes by delivering common shares or preferred shares of the Company with the right to elect to pay interest on the notes by delivering Stapled Units.

TIMBERWEST FOREST CORP.

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

For the three and nine months ended September 30, 2010 and 2009

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

14. Stapled units (continued)

Each Series A Subordinate Note has been issued with a face amount of \$8.978806569, entitling the holder to an interest payment per unit of between \$0.179576131 and \$1.077456788 per annum (2-12%). The Series A Subordinate Notes are unsecured and subordinate to all credit facilities (see note 10) and convertible debentures (note 11). The principal amount of the Series A Subordinate Notes plus accrued and unpaid interest thereon are due on August 31, 2038, unless such date is extended by the Company at the time of the issuance of additional subordinate notes to a date not later than the earlier of: (i) the date of maturity of such additional subordinate notes; and (ii) August 31, 2048, and will be payable by cash or, at the option of the Company, by delivery of common shares to the Subordinate Note Trustee for the benefit of the holders of the subordinate notes.

The revalued Series A Subordinate Notes are measured by the Company under Canadian GAAP at amortized cost under CICA Section 3855 'Financial Instruments.' As such, the balance of the Series A Subordinate Notes will be accreted using the effective interest rate method to face value of \$807.5 million on maturity. For the three and nine months ending September 30, 2010, accretion recognized in the statement of operations was \$1.9 million and \$5.4 million, respectively (2009 - \$1.7 million and \$4.9 million, respectively).

On May 7, 2009 the Company's preferred shares were converted into common shares and consolidated in order to simplify TimberWest's capital structure and eliminate administrative burdens and related expenses associated with maintaining the preferred shares. Each TimberWest Stapled Unit contains one Series A Subordinate Note and one common share. The conversion and consolidation was approved by the unitholders on May 6, 2009 and were approved by the Toronto Stock Exchange ("TSX").

On May 18, 2010 the Company successfully raised \$60.0 million through a public Stapled Unit offering. The public offering was 12,000,000 Stapled Units at a price of \$5.00 per Stapled Unit for gross proceeds of \$60 million. As part of this issuance, transaction costs of \$3.2 million were deferred and offset against the Series A Subordinate Notes and are being amortized using the effective rate method over the life of the Series A Subordinate Notes until maturity.

The option to defer interest distributions to the holders of the Stapled Units for up to 18 months is an embedded derivative under Canadian GAAP and is revalued at each reporting date. As at September 30, 2010 the fair value of this option is \$6.6 million (December 31, 2009 - \$5.2 million) and is accounted for as Other Assets (note 9).

The option to extend the maturity date on the Series A Subordinate Notes from August 31, 2038 to August 31, 2048 is an embedded derivative under Canadian GAAP and is revalued at each reporting date. As at September 30, 2010 the fair value of this option is \$0.7 million (December 31, 2009 - \$0.7 million) and is accounted for as Other Assets (note 9).

During the three and nine months ending September 30, 2010, the Company issued nil and 13,674 Stapled Units on the conversion of the Company's convertible debentures (note 11) (2009 - nil and 11,134). In Q3, 2010, no Stapled Units were issued on the exercise of Stapled Unit options (Q3, 2009 - no options exercised), while for the nine months ended September 30, 2010, 148,181 Stapled Units were issued on the exercise of Stapled Unit options (note 15) (2009 - no options exercised).

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

15. Stapled Unit option plan

Under the Company's Stapled Unit Option Plan, the Company may grant options for the purchase of Stapled Units to directors, officers or employees who are in active service or employment of the Company or of any of its subsidiaries. During the quarter ended September 30, 2010, no Stapled Unit options were granted (Q3, 2009 – 22,500 Stapled Unit options were granted at an average exercise price of \$3.71). During the nine months ended September 30, 2010, 880,047 Stapled Unit options were granted at an average exercise price of \$5.21 (2009 – 1,719,327 Stapled Unit options were granted at an average exercise price of \$3.01 during the first nine months of the year).

The option to acquire a Stapled Unit effectively provides the option holder with an option on the Series A Subordinated Note component and an option on the equity component of the Stapled Unit. An option to acquire a debt instrument is accounted for under the intrinsic value method whereby the compensation cost is determined each period based on the fair value of the debt instrument compared to the exercise price of the option to acquire the debt instrument. The fair value of the equity component is based on the fair value of the option as determined using an option pricing model. Historically, the Company has determined that the intrinsic value of the option to acquire the Series A Subordinate Notes has not been material and the fair value of the option has been recorded in equity as contributed surplus based on the fair value as determined by the Black Scholes option pricing model.

With the recent changes to the Series A Subordinate Note terms, including modifying the interest rate to a variable rate from 2% to 12% which is ultimately based on distributable cash levels, and the current market value of the Stapled Unit, which is below the face value of the Series A Subordinate Note, the Company has determined that the value of the Stapled Unit option is now in the debt component and that the equity option value is immaterial. As a result, the accounting for the options issued in the period has been done using the intrinsic value method.

On this basis, no compensation cost was recognized in 2010 for the 880,047 Stapled Unit options granted between January 1, 2010 and September 30, 2010, based on an intrinsic value method of accounting.

Compensation cost previously recognized for the 1,434,599 Stapled Unit options granted during 2009 and outstanding as at September 30, 2010 was reversed by \$0.2 million during Q3, 2010 as a result of the intrinsic value method of accounting, with a corresponding debit to the Stapled Unit option plan liability (Q3, 2009 – the company recognized compensation expense of \$0.4 million, with a corresponding credit to the Stapled Unit option plan liability). For the nine months ended September 30, 2010 the compensation cost previously recognized for these same options was reversed by \$0.1 million, with a corresponding debit to the Stapled Unit option plan liability (2009 – the Company recognized compensation expense of \$0.8 million, with a corresponding credit to the Stapled Unit option plan liability).

Under the Company's Distribution Equivalent Plan, the Company awards Stapled Unit option holders an amount equal to actual distributions paid on the Company's Stapled Units. Awards granted under the Distribution Equivalent Plan vest under the same terms that apply to the corresponding options and can only be exercised at the time of exercise of the corresponding options.

Awards are accrued on a basis equal to actual distributions paid on the Company's issued and outstanding Stapled Units and are charged to earnings as the underlying Stapled Unit options vest. For the three and nine months ended September 30, 2010, no amount was accrued as no distributions were paid (2009 – no amount was accrued as no distributions were paid). For the three and nine months ended September 30, 2010 no amount has been amortized against earnings (2009 – nil and \$0.1 million, respectively).

TIMBERWEST FOREST CORP.**NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS****For the three and nine months ended September 30, 2010 and 2009**

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

15. Stapled Unit option plan (continued)

During the three months ended September 30, 2010, no Stapled Unit options were exercised, 40,000 Stapled Unit options were cancelled with an average exercise price of \$4.67, and no Stapled Unit options expired (Q3, 2009 – no Stapled Unit options were exercised, no Stapled Unit options were cancelled and no Stapled Unit options expired).

During the nine months ended September 30, 2010, 148,181 Stapled Unit options were exercised, with an average exercise price of \$3.01, 40,000 Stapled Unit options were cancelled with an average exercise price of \$4.67, and 312,694 Stapled Unit options with an average exercise price of \$14.88 expired (2009 – no Stapled Unit options were exercised, 47,500 Stapled Unit options with an average exercise price of \$12.72 were cancelled and 223,103 Stapled Unit options with an average exercise price of \$13.08 expired).

16. Financial instruments**Accounting for financial instruments**

These interim consolidated financial statements follow the same accounting policies and methods of application used in the Company's audited annual consolidated financial statements of December 31, 2009 with one exception.

The public convertible debentures are now considered to trade in an active market and accordingly, fair value is measured based on level 1 inputs, as the trading activity is now considered active. The fair value of the private convertible debentures continues to be measured based on level 2 inputs, as there is no active market for trading.

Details as to the changes in fair value of financial instruments held for trading as recognized in the statement of operations and comprehensive income (loss) are as follows:

	Three months ended		Nine months ended	
	September 30		September 30	
(in millions of dollars)	2010	2009	2010	2009
Change in fair value of:				
Convertible debentures	(5.9)	12.1	(14.9)	22.8
Interest payable in kind on convertible debentures	-	0.5	1.4	0.5
Embedded derivatives within the Series A Subordinate Notes	(1.3)	0.5	(1.4)	1.4
Change in fair value of financial instruments held for trading	(7.2)	13.1	(14.9)	24.7

17. Comparative figures

Certain comparative figures have been reclassified to conform to the current year presentation.

About TimberWest

TimberWest Forest Corp. is uniquely positioned as western Canada's largest private timber and land management company. The Company owns in fee simple approximately 320,000 hectares or 791,000 acres of private land and is in the business of selling timber products and real estate.

Investor Relations Contact

Robert Allen
Vice President Finance and
Chief Financial Officer
Telephone: 604-654-4600
Facsimile: 604-654-4571
Email: invest@timberwest.com

Stapled Units of TimberWest Forest Corp. are traded on the Toronto Stock Exchange under the symbol: TWF.UN



TimberWest Forest Corp.
Third Floor, 856 Homer Street
Vancouver, BC V6B 2W5
Telephone: 604-654-4600
Facsimile: 604-654-4571
www.timberwest.com