



KRUGER PRODUCTS L.P.

UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENT

**FOR THE 3-MONTH AND 6-MONTH PERIODS ENDED JUNE 25, 2017
AND JUNE 26, 2016**

Kruger Products L.P.

Unaudited Condensed Consolidated Statement of Financial Position

(tabular amounts are in thousands of Canadian dollars)

	June 25, 2017	December 31, 2016
	\$	\$
Assets		
Current assets		
Cash and cash equivalents	28,286	36,511
Trade and other receivables	107,667	123,095
Receivables from related parties (note 11)	273	185
Current portion of advances to partners (note 9)	3,678	5,465
Inventories	187,199	179,543
Income tax recoverable	666	423
Prepaid expenses	11,679	7,286
	<u>339,448</u>	<u>352,508</u>
Non-current assets		
Property, plant and equipment (note 6)	778,072	762,270
Other long-term assets	5,900	6,075
Goodwill	160,939	160,939
Intangible assets	14,781	15,270
Deferred income taxes	35,506	39,913
	<u>1,334,646</u>	<u>1,336,975</u>
Total assets		
Liabilities		
Current liabilities		
Bank indebtedness (note 14)	3,732	9,007
Trade and other payables	180,883	201,477
Payables to related parties (note 11)	3,756	3,606
Income tax payable	508	1,779
Distributions payable (notes 9 and 11)	10,259	10,148
Current portion of provisions (note 8)	1,487	1,885
Current portion of long-term debt (note 13)	8,754	8,859
	<u>209,379</u>	<u>236,761</u>
Non-current liabilities		
Long-term debt (note 13)	441,249	415,379
Provisions (note 8)	6,878	6,487
Pensions (note 7)	107,411	92,646
Post-retirement benefits (note 7)	60,629	57,162
	<u>825,546</u>	<u>808,435</u>
Liabilities to non-unitholders		
Current portion of Partnership units liability (note 9)	8,611	8,611
Long-term portion of Partnership units liability (note 9)	133,745	137,296
	<u>142,356</u>	<u>145,907</u>
Total Partnership units liability		
	<u>967,902</u>	<u>954,342</u>
Total liabilities		
Equity		
Partnership units (note 9)	346,334	336,576
Deficit	(65,094)	(42,792)
Accumulated other comprehensive income	85,504	88,849
	<u>366,744</u>	<u>382,633</u>
Total equity		
	<u>1,334,646</u>	<u>1,336,975</u>
Total equity and liabilities		
Subsequent events (note 9)		

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

Kruger Products L.P.
Unaudited Condensed Consolidated Statement of Comprehensive Loss
For the 3-month and 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars)

	3-month period ended June 25, 2017 \$	3-month period ended June 26, 2016 \$	6-month period ended June 25, 2017 \$	6-month period ended June 26, 2016 \$
Revenue (note 11)	314,388	295,757	603,659	575,447
Expenses				
Cost of sales (note 11)	267,077	249,878	511,331	490,525
Selling, general and administrative expenses (note 11)	22,520	21,986	45,741	43,638
Gain on sale of non-financial assets	(81)	-	(68)	-
Restructuring costs, net (note 8)	-	393	11	393
Operating income	24,872	23,500	46,644	40,891
Interest expense	10,757	10,921	21,021	22,135
Other (income) expense (note 5)	2,018	(291)	3,963	(1,120)
Income before income taxes	12,097	12,870	21,660	19,876
Income taxes (note 10)	2,150	834	4,764	1,450
Net income for the period	9,947	12,036	16,896	18,426
Other comprehensive loss				
Items that will not be reclassified to net income:				
Remeasurements of pensions	(12,656)	(27,120)	(15,223)	(43,889)
Remeasurements of post-retirement benefits	(2,317)	(1,755)	(3,201)	(1,634)
Items that may be subsequently reclassified to net income:				
Available-for-sale investment	-	-	-	(290)
Cumulative translation adjustment	(2,580)	(6,846)	(3,345)	(20,827)
Total other comprehensive loss for the period	(17,553)	(35,721)	(21,769)	(66,640)
Comprehensive loss for the period	(7,606)	(23,685)	(4,873)	(48,214)

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

Kruger Products L.P.

Unaudited Condensed Consolidated Statement of Changes in Equity

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

	Partnership units		Deficit \$	Accumulated other comprehensive income \$	Total equity \$
	#	\$			
As of January 1, 2016	54,840,093	318,012	(29,416)	99,805	388,401
Distributions payable (note 9)	-	-	(10,016)	-	(10,016)
Distributions paid (note 9)	-	-	(9,951)	-	(9,951)
Fair value adjustment (note 9)	-	30	(30)	-	-
Change in actuarial loss on pension	-	-	(43,889)	-	(43,889)
Change in actuarial loss on post-retirement benefits	-	-	(1,634)	-	(1,634)
Change in available-for-sale investment	-	-	-	(290)	(290)
Cumulative translation adjustment	-	-	-	(20,827)	(20,827)
Net income for the period	-	-	18,426	-	18,426
Issuance of partnership units (note 9)	802,067	8,979	-	-	8,979
As of June 26, 2016	55,642,160	327,021	(76,510)	78,688	329,199
As of January 1, 2017	56,376,788	336,576	(42,792)	88,849	382,633
Distributions payable (note 9)	-	-	(10,259)	-	(10,259)
Distributions paid (note 9)	-	-	(10,203)	-	(10,203)
Fair value adjustment (note 9)	-	312	(312)	-	-
Change in actuarial loss on pension	-	-	(15,223)	-	(15,223)
Change in actuarial loss on post-retirement benefits	-	-	(3,201)	-	(3,201)
Cumulative translation adjustment	-	-	-	(3,345)	(3,345)
Net income for the period	-	-	16,896	-	16,896
Issuance of partnership units (note 9)	618,379	9,446	-	-	9,446
As of June 25, 2017	56,995,167	346,334	(65,094)	85,504	366,744

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

Kruger Products L.P.

Unaudited Condensed Consolidated Statement of Cash Flows

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars)

	6-month period ended June 25, 2017 \$	6-month period ended June 26, 2016 \$
Cash flows from (used in) operating activities		
Net income for the period	16,896	18,426
Items not affecting cash		
Depreciation	24,064	21,768
Amortization	489	580
Gain on sale of property, plant and equipment	(2)	(3)
Change in amortized cost of Partnership units liability (note 5)	5,060	1,234
Gain on sale of investment (note 5)	-	(324)
Foreign exchange gain (note 5)	(1,097)	(2,030)
Interest expense	21,021	22,135
Pension and post-retirement benefits	5,026	5,318
Provisions (note 8)	338	799
Income taxes	4,764	1,450
Gain on sale of non-financial assets	(68)	-
Total items not affecting cash	59,595	50,927
Net change in non-cash working capital (note 15)	(31,089)	(4,462)
Contributions to pension and post-retirement benefit plans	(7,671)	(11,305)
Provisions paid	(450)	(1,118)
Income tax payments	(3,054)	(1,373)
Net cash from operating activities	34,227	51,095
Cash flows from (used in) investing activities		
Purchases of property, plant and equipment	(38,245)	(38,701)
Capitalized interest paid	(381)	-
Proceeds on sale of investment (note 5)	-	1,439
Government assistance received	2,949	1,209
Purchases of software	-	(71)
Proceeds on sale of property, plant and equipment	1,170	4
Net cash used in investing activities	(34,507)	(36,120)
Cash flows from (used in) financing activities		
Proceeds from long-term debt	26,770	791
Repayment of long-term debt	(501)	(7,510)
Payment of deferred financing fees	(12)	(335)
Interest paid on long-term debt	(11,111)	(9,756)
Distributions and advances paid, net (note 9)	(17,729)	(12,077)
Net cash used in financing activities	(2,583)	(28,887)
Effect of exchange rate changes on cash and cash equivalents held in foreign currency	(87)	(1,439)
Decrease in cash and cash equivalents during the period	(2,950)	(15,351)
Cash and cash equivalents - Beginning of period (note 14)	27,504	25,455
Cash and cash equivalents - End of period (note 14)	24,554	10,104

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

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

1 General information

Kruger Products L.P. (KPLP or the Partnership) is a limited partnership registered in the Province of Quebec, Canada whose partners are Kruger Inc. (ultimate parent), KPGP Inc. (KPGP), and KP Tissue Inc. (KPT). The Partnership manufactures, sells and distributes tissue products for household, industrial and commercial use. The Partnership has plants in New Westminster, British Columbia; Crabtree, Quebec; Sherbrooke, Quebec; Gatineau, Quebec; Scarborough and Trenton, Ontario and Memphis, Tennessee. The Partnership's headquarters are located in Mississauga, Ontario, Canada.

2 Basis of presentation

These unaudited condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) applicable to the preparation of interim financial statements, including International Accounting Standard (IAS) 34 - Interim Financial Reporting as issued by the International Accounting Standards Board (IASB), and with interpretations of the International Financial Reporting Committee which the Canadian Accounting Standards Board has approved for incorporation into Part 1 of the CPA Canada Handbook - Accounting. These unaudited condensed consolidated financial statements should be read in conjunction with the annual consolidated financial statements of the Partnership for the year ended December 31, 2016.

The 3-month period ended June 25, 2017 represents the 91 day period from March 27 to June 25, 2017 and the 3-month period ended June 26, 2016 represents the 91 day period from March 28 to June 26, 2016. The 6-month period ended June 25, 2017 represents the 176 day period from January 1 to June 25, 2017 and the 6-month period ended June 26, 2016 represents the 178 day period from January 1 to June 26, 2016.

These unaudited condensed consolidated financial statements were approved by the board of directors of KPGP on August 8, 2017.

3 Summary of significant accounting policies

The significant accounting policies that have been used in the preparation of these unaudited condensed consolidated financial statements are described in the annual consolidated financial statements of the Partnership for the year ended December 31, 2016 and have been applied to all periods presented except the following accounting policies, which were adopted effective January 1, 2017.

- (i) IAS 7, Statement of Cash Flows. In January 2016, the IASB issued an amendment to require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. Other than the aforementioned additional disclosures, which will be included in the annual consolidated financial statements, the application of the amendments to IAS 7 did not result in any changes to the presentation of the unaudited condensed consolidated statement of cash flows.
- (ii) IAS 12, Income Taxes – Deferred Tax. In February 2016, the IASB issued an amendment to clarify the requirements for recognizing deferred tax assets on unrealized losses. The amendment clarifies the accounting for deferred tax where an asset is measured at fair value and that fair value is below the asset's tax base. Certain other aspects of accounting for deferred tax assets are also clarified. The adoption of this standard had no impact on the unaudited condensed consolidated financial statements.
- (iii) In December 2016, the IASB issued an amendment clarifying the scope of IFRS 12, Disclosure of Interests in Other Entities. The amendment clarified that the disclosures requirement of IFRS 12 are applicable to interest in entities classified as held for sale, except for summarized financial information. The adoption of this standard had no impact on the unaudited condensed consolidated financial statements.

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

The impact of new standards, amendments to standards and interpretations that have been issued but not yet effective for financial periods beginning on or after January 1, 2018 and have not been early adopted have been discussed in the annual consolidated financial statements for the year ended December 31, 2016, except for the following:

- (i) IFRS 15, Revenue from Contracts with Customers, was issued by the IASB in May 2014. The standard specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with some informative, relevant disclosures. The standard supersedes IAS 18, Revenue, IAS 11, Construction Contracts, and a number of revenue-related interpretations. Application of the standard is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions being leases, financial instruments and insurance contracts. In September 2015, the IASB issued an amendment to defer the mandatory effective date to interim periods beginning on or after January 1, 2018, with early adoption permitted. In April 2016, the IASB issued an amendment to clarify the guidance on identifying performance obligations, licences of intellectual property and principal versus agent, and to provide additional practical expedients on transition. The amendment is effective for annual periods beginning on or after January 1, 2018. Management expects to adopt IFRS 15 using the modified retrospective approach.

Management is evaluating the estimated impact of the new standard on the consolidated financial statements. Additional details are expected to be disclosed before the adoption of IFRS 15.

- (ii) IFRS 9, Financial Instruments. In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments, bringing together the classification and measurement, impairment and hedge accounting phases of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement. The mandatory effective date of IFRS 9 would be annual periods beginning on or after January 1, 2018, with early adoption permitted.

Management is evaluating the estimated impact of the new standard on the consolidated financial statements. Additional details are expected to be disclosed before the adoption of IFRS 9.

- (iii) IFRS 16, Leases. In January 2016, the IASB issued IFRS 16, Leases which replaces the current guidance in IAS 17, Leases. IFRS 16 requires lessees to recognize a right-of-use asset and a lease liability reflecting future lease payments for virtually all lease contracts. IFRS 16 must be applied to an entity's first annual IFRS financial statements for periods beginning on or after January 1, 2019, with early adoption permitted. Management can elect to adopt IFRS 16 using either the full retrospective approach or the modified retrospective approach.

Management has performed a preliminary assessment of IFRS 16 adoption and expects a significant impact on the consolidated financial statements. The right-of-use asset and lease liability are expected to be material to the consolidated statement of financial position. There is expected to be a significant impact on the consolidated statement of income and Adjusted EBITDA, as IFRS 16 replaces operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. Significant changes to systems and processes are expected to be required, in order to collect the new data requirements.

Management is evaluating the potential implications on data systems, internal controls over financial reporting, information technology, business processes, and financing and compensation arrangements. Management is also evaluating the transition approach it will apply and whether it will use the optional exemptions or practical expedients under the standard. Additional details, including the transition approach, practical expedients elected and estimated quantitative impact on the consolidated financial statements, are expected to be disclosed before the adoption of IFRS 16.

- (iv) IFRIC 23, Uncertainty over income tax treatments. In June 2017, the IFRS Interpretation Committee issued an interpretation which clarifies how the recognition and measurement requirements of IAS 12 'Income

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

taxes', are applied where there is uncertainty over income tax treatments. The interpretation is effective for annual periods beginning on or after January 1, 2019. Management is evaluating the amended standard and has not yet determined the impact on the consolidated financial statements.

4 Critical accounting estimates and judgments

The preparation of these unaudited condensed consolidated financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities in the unaudited condensed consolidated financial statements and the disclosure of contingencies at the dates of the unaudited condensed consolidated statements of financial position, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The estimates and judgement applied by management that most significantly affect the unaudited condensed consolidated financial statements are the same as the ones that applied to the audited consolidated financial statements for the year ended December 31, 2016.

5 Other (income) expense

	3-month period ended June 25, 2017	3-month period ended June 26, 2016	6-month period ended June 25, 2017	6-month period ended June 26, 2016
	\$	\$	\$	\$
Foreign exchange gain	(513)	(291)	(1,097)	(2,030)
Change in amortized cost of Partnership units liability	2,531	-	5,060	1,234
Miscellaneous income	-	-	-	(324)
	<u>2,018</u>	<u>(291)</u>	<u>3,963</u>	<u>(1,120)</u>

During the 6-month period ended June 26, 2016, the available-for-sale investment was sold for proceeds of \$1.4 million. The sale resulted in a gain of \$0.3 million, which was reclassified from Accumulated other comprehensive income to Other income during the 6-month period ended June 26, 2016.

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

6 Property, plant and equipment

	Land \$	Buildings \$	Machinery and equipment \$	Assets under construction or development \$	Total \$
As of January 1, 2017					
Cost	38,130	185,150	1,085,265	36,977	1,345,522
Accumulated depreciation and impairments	-	(80,840)	(502,412)	-	(583,252)
Net book value as of January 1, 2017	38,130	104,310	582,853	36,977	762,270
Additions	-	-	62	44,483	44,545
Capitalized interest	-	-	-	413	413
Disposals	(59)	-	(41)	-	(100)
Government assistance	-	-	(2,386)	(563)	(2,949)
Transfers	-	661	18,671	(19,332)	-
Depreciation	-	(2,341)	(19,042)	-	(21,383)
Exchange differences	(18)	(697)	(4,003)	(6)	(4,724)
As of June 25, 2017	38,053	101,933	576,114	61,972	778,072
As of June 25, 2017					
Cost	38,053	184,965	1,095,369	61,972	1,380,359
Accumulated depreciation and impairment	-	(83,032)	(519,255)	-	(602,287)
Net book value as of June 25, 2017	38,053	101,933	576,114	61,972	778,072

7 Pensions and post-retirement benefits

The following were the significant assumptions for the defined benefit pension plans and other benefit plans:

Assumptions	Pensions		Post-retirement benefit plans	
	June 25, 2017 %	December 31, 2016 %	June 25, 2017 %	December 31, 2016 %
Discount rate - accrued benefit obligation	3.40	3.77	3.40	3.77
Rate of compensation increases	3.25 - 4.00	3.25 - 4.00		

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For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

The net benefit pension plan expense included the following components:

	Pensions		Post-retirement benefit plans	
	3-month period ended June 25, 2017	3-month period ended June 26, 2016	3-month period ended June 25, 2017	3-month period ended June 26, 2016
	\$	\$	\$	\$
Net benefit plan expense				
Current service cost	1,955	2,131	433	407
Interest cost	5,130	5,256	444	458
Expected return on plan assets	(4,347)	(4,495)	-	-
Administrative cost	125	121	-	-
	<u>2,863</u>	<u>3,013</u>	<u>877</u>	<u>865</u>

	Pensions		Post-retirement benefit plans	
	6-month period ended June 25, 2017	6-month period ended June 26, 2016	6-month period ended June 25, 2017	6-month period ended June 26, 2016
	\$	\$	\$	\$
Net benefit plan expense				
Current service cost	3,911	4,261	866	814
Interest cost	10,257	10,489	888	915
Expected return on plan assets	(8,692)	(8,998)	-	-
Administrative cost	249	243	-	-
	<u>5,725</u>	<u>5,995</u>	<u>1,754</u>	<u>1,729</u>

8 Provisions

	Environmental and asset retirement obligations	Long-term incentives	Restructuring	Total
	\$	\$	\$	\$
	(a)	(b)	(c)	
Provisions as of January 1, 2017	5,887	1,047	1,438	8,372
Current	-	447	1,438	1,885
Non-current	<u>5,887</u>	<u>600</u>	<u>-</u>	<u>6,487</u>
Provisions as of January 1, 2017	5,887	1,047	1,438	8,372
Additional provisions	-	327	11	338
Paid during the period	-	-	(450)	(450)
Interest accretion	105	-	-	105
Provisions as of June 25, 2017	<u>5,992</u>	<u>1,374</u>	<u>999</u>	<u>8,365</u>
Current	-	488	999	1,487
Non-current	<u>5,992</u>	<u>886</u>	<u>-</u>	<u>6,878</u>

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

(a) Environmental and asset retirement obligations

The Partnership has made a provision for the potential obligation under a land lease at one of its plant locations to demolish the building and restore the land at the end of the lease to its original condition. The current lease ends in 2028 but an extension is currently being negotiated. The estimated undiscounted amount to settle this obligation would be between \$9.0 million and \$11.7 million. The liability is estimated using a discounted cash flow with a discount rate of 3.635% (December 31, 2016 – 3.635%).

(b) Long-term incentives

Long-term incentives include the Executive Long-Term Incentive Plan (LTIP) for the Partnership. The LTIP uses performance share units and results are based primarily on Adjusted EBITDA return on capital employed using a three year average, along with other components. The LTIP is paid in cash in May of the year following the three year period it is earned. The compensation expense is recognized over the same three year period.

(c) Restructuring

During the first quarter of 2014, the Partnership undertook a review of corporate overhead costs and identified a number of cost reduction opportunities. As of June 25, 2017, there was a remaining provision of \$0.6 million.

In response to market cost pressures, in the first half of 2015, senior management undertook a comprehensive review of its cost structure and identified a number of cost reduction opportunities. As of June 25, 2017, there was a remaining provision of \$0.4 million.

9 Distributions and Partnership units liability

	Partnership units liability
	\$
As of January 1, 2017	145,907
Change in amortized cost of Partnership units liability (note 5)	5,060
Tax Distributions	(8,611)
As of June 25, 2017	<u>142,356</u>

The Partnership unit distributions paid, the portion of the distribution reinvested by the partners, the additional Partnership units issued at the unit price, and the gross proceeds were as follows:

Distribution Payment Date	6-month period ended June 25, 2017			
	Partnership unit distributions	Unit price	Issuance of Partnership units	Gross proceeds
	\$	\$	#	\$
January 16, 2017	10,148	15.25	309,196	4,715
April 17, 2017	10,203	15.30	309,183	4,731
	<u>20,351</u>		<u>618,379</u>	<u>9,446</u>

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

<u>Distribution Payment Date</u>	6-month period ended June 26, 2016			
	Partnership unit distributions	Unit price	Issuance of Partnership units	Gross proceeds
	\$	\$	#	\$
January 15, 2016	9,871	10.29	442,929	4,558
April 15, 2016	9,951	12.31	359,138	4,421
	<u>19,822</u>		<u>802,067</u>	<u>8,979</u>

On July 17, 2017, the Partnership paid a distribution of \$10.3 million to partners. Pursuant to the Partnership's Distribution Reinvestment Plan (DRIP), a portion of the distribution was reinvested by the partners, resulting in the Partnership issuing 357,887 Partnership units at a price of \$13.23. During the 6-month period ended June 25, 2017, a fair value adjustment of \$0.3 million was recorded to reflect the market value of the Partnership units issued.

Subsequent to June 25, 2017, the Partnership declared a distribution of \$10.3 million, payable on October 16, 2017.

The Partnership paid Partnership unit distributions, Tax Distributions and advances to its related parties as follows:

	6-month period ended June 25, 2017			
	Tax Distributions	Advances	Partnership unit distributions	Total
	\$	\$	\$	\$
Paid to Kruger Inc. ^(a)	2,665	3,082	8,535	14,282
Paid to KPGP	-	-	2	2
Paid to KPT ^(b)	481	596	2,368	3,445
Total paid	<u>3,146</u>	<u>3,678</u>	<u>10,905</u>	<u>17,729</u>

	6-month period ended June 26, 2016		
	Advances	Partnership unit distributions	Total
	\$	\$	\$
Paid to Kruger Inc. ^(a)	1,029	8,293	9,322
Paid to KPGP	-	2	2
Paid to KPT ^(b)	205	2,548	2,753
Total paid	<u>1,234</u>	<u>10,843</u>	<u>12,077</u>

(a) During the 6-month periods ended June 25, 2017 and June 26, 2016, Partnership unit distributions were paid to Kruger Inc. net of the DRIP reinvestment. During the 6-month period ended June 25, 2017, Kruger Inc.'s DRIP reinvestment was \$8.5 million (6-month period ended June 26, 2016 - \$8.3 million).

(b) During the 6-month periods ended June 25, 2017 and June 26, 2016, Partnership unit distributions were paid to KPT net of the DRIP reinvestment. During the 6-month period ended June 25, 2017, KPT's DRIP reinvestment was \$0.9 million (6-month period ended June 26, 2016 - \$0.7 million).

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For the 6-month periods ended June 25, 2017 and June 26, 2016

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

Tax Distributions

On February 28, 2017, the Partnership declared a Tax Distribution of \$8.6 million, of which \$1.4 million was used to settle the advances to KPT and pay the final tax instalment on behalf of KPT. The remaining \$7.2 million was used to settle Kruger Inc.'s and KPGP's respective advances, with the balance paid to Kruger Inc. and KPGP.

During the 6-month period ended June 25, 2017, pursuant to the Tax Distribution as defined in the Partnership Agreement, the Partnership made advances to its partners of \$3.7 million, of which \$0.6 million was used to pay the monthly tax instalment on behalf of KPT and the remaining was advanced to Kruger Inc. and KPGP. The advances are non-interest bearing and non-recourse in nature and will be settled when the Tax Distribution is declared annually.

10 Income taxes

The Partnership is not a tax paying entity for the 6-month periods ended June 25, 2017 and June 26, 2016. The income from the Partnership flows to the partners, Kruger Inc., KPGP, and KPT. However, the Partnership's subsidiaries Kruger Products (USA) Inc., K.T.G. (USA) Inc., TAD Canco Inc., Grupo Tissue de Mexico S de RL de CV and TAD Luxembourg S.A.R.L. are corporate entities and, therefore, are subject to tax.

Income tax expense (recovery) was recognized based on management's best estimate of the weighted average annual income tax rate expected for the full financial year. The estimated weighted average annual income tax rate for the 6-month period ended June 25, 2017 was 22.0% (6-month period ended June 26, 2016 – 7.3%).

The components of income taxes were as follows:

	3-month period ended June 25, 2017	3-month period ended June 26, 2016	6-month period ended June 25, 2017	6-month period ended June 26, 2016
	\$	\$	\$	\$
Current tax expense	735	468	1,320	1,342
Deferred tax expense	1,415	366	3,444	108
	<u>2,150</u>	<u>834</u>	<u>4,764</u>	<u>1,450</u>

11 Related party transactions

The Partnership makes sales to and acquires goods and services from Kruger Inc. and its subsidiary companies (related parties) in the normal course of business. These transactions are measured at the exchange amount, which is the amount agreed on by the related parties, and are non-interest bearing.

Sales of goods to Kruger Inc. for the 6-month period ended June 25, 2017 were \$0.7 million (6-month period ended June 26, 2016 - \$0.4 million). Goods are sold based on the price lists in force and terms that would be available to third parties.

Purchases of goods and services from Kruger Inc. for the 6-month period ended June 25, 2017 were \$17.9 million (6-month period ended June 26, 2016 - \$16.2 million). Purchases of goods and services from subsidiaries of Kruger Inc. for the 6-month period ended June 25, 2017 were \$4.1 million (6-month period ended June 26, 2016 - \$4.3 million). Goods are purchased from Kruger Inc. and related parties under normal commercial terms and conditions. These purchases of goods and services are included within cost of sales and selling, general and administrative expenses in the unaudited condensed consolidated statement of comprehensive income (loss). During the 6-month period ended June 25, 2017, management fees of \$2.1 million (6-month period ended June 26, 2016 - \$2.1 million) were paid to Kruger Inc. for management services provided to the Partnership.

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Balances due to and from related parties were as follows:

	June 25, 2017 \$	December 31, 2016 \$
Receivables from Kruger Inc.	2	171
Receivables from subsidiaries of Kruger Inc.	-	14
Receivables from KPT	271	-
	<u>273</u>	<u>185</u>
	June 25, 2017 \$	December 31, 2016 \$
Payables to Kruger Inc.	3,025	2,646
Payables to subsidiaries of Kruger Inc.	731	534
Payables to KPT	-	426
	<u>3,756</u>	<u>3,606</u>

The receivables from and payables to related parties are based on commercial terms agreed on between the parties, unsecured and non-interest bearing. There were no provisions related to the receivables from related parties as of June 25, 2017 and December 31, 2016. There were no loans outstanding with related parties as of June 25, 2017 and December 31, 2016.

The Partnership had declared distributions which are payable to its related parties as follows:

	June 25, 2017 \$	December 31, 2016 \$
Distribution payable to Kruger Inc.	8,611	8,511
Distribution payable to KPGP	1	1
Distribution payable to KPT	1,647	1,636
Total distribution payable	<u>10,259</u>	<u>10,148</u>

12 Segment information

Reportable segments

Management has determined the operating segments based on the reports reviewed by the Chief Executive Officer who is considered to be the Chief Operating Decision Maker. The Partnership operates in three industry segments: Consumer, Away From Home (AFH) and Other.

(a) Consumer

This segment operates using the Partnership's manufacturing facilities in Canada (New Westminster, British Columbia; Crabtree, Quebec; Sherbrooke, Quebec; Gatineau, Quebec) and in the United States (Memphis, Tennessee). The Consumer segment includes sales of branded tissue products such as Cashmere™, Purex™, White Swan™, Scotties™, Sponge Towels™ and White Cloud™ and private label tissue products.

(b) AFH

This segment operates using the Partnership's manufacturing facilities in Canada. The AFH business sells tissue products primarily through distributors to businesses involved in property management, health care, food service, manufacturing and lodging and also to public facilities.

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(c) Other

This segment includes sales of parent rolls by the Partnership to other tissue manufacturing companies primarily in the United States and also in Canada. It also includes sales of recycled fibre primarily to its parent company.

Segment operating income is the earnings (loss) for each such segment before (i) interest expense, (ii) income taxes, (iii) depreciation, (iv) amortization, (v) impairment (gain on sale) of non-financial assets, (vi) loss (gain) on disposal of property, plant and equipment, (vii) foreign exchange loss (gain), (viii) costs related to restructuring activities, (ix) changes in amortized cost of Partnership units liability, and (x) one-time costs due to pension revaluations related to past service. “Consumer Segment Adjusted EBITDA”, “AFH Segment Adjusted EBITDA” and “Other Segment Adjusted EBITDA” means in each case the Segment operating income for the referring reportable segment of KPLP.

The Partnership’s assets, operations and employees are located primarily in Canada and the United States. The same long-term assets of the Partnership are used for the Consumer, AFH and Other segments. Accordingly, assets cannot be allocated to these segments.

	3-month period ended June 25, 2017			
	Consumer	AFH	Other	Total
	\$	\$	\$	\$
Revenue from external customers	252,152	59,919	2,317	314,388
Segment Adjusted EBITDA	34,902	2,333	121	37,356
Depreciation and amortization				12,565
Interest expense				10,757
Change in amortized cost of Partnership units liability				2,531
Gain on sale of non-financial assets				(81)
Foreign exchange gain				(513)
Income before income taxes				12,097
Income taxes				2,150
Net income				9,947

	3-month period ended June 26, 2016			
	Consumer	AFH	Other	Total
	\$	\$	\$	\$
Revenue from external customers	231,924	59,051	4,782	295,757
Segment Adjusted EBITDA	33,719	1,775	372	35,866
Depreciation and amortization				11,977
Interest expense				10,921
Gain on sale of property, plant and equipment				(4)
Restructuring costs				393
Foreign exchange gain				(291)
Income before income taxes				12,870
Income taxes				834
Net income				12,036

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	6-month period ended June 25, 2017			
	Consumer	AFH	Other	Total
	\$	\$	\$	\$
Revenue from external customers	491,079	108,593	3,987	603,659
Segment Adjusted EBITDA	67,874	2,988	276	71,138
Depreciation and amortization				24,553
Interest expense				21,021
Change in amortized cost of Partnership units liability				5,060
Gain on sale of property, plant and equipment				(2)
Gain on sale of non-financial assets				(68)
Restructuring costs				11
Foreign exchange gain				(1,097)
Income before income taxes				21,660
Income taxes				4,764
Net income				16,896

	6-month period ended June 26, 2016			
	Consumer	AFH	Other	Total
	\$	\$	\$	\$
Revenue from external customers	460,076	108,102	7,269	575,447
Segment Adjusted EBITDA	61,526	1,805	622	63,953
Depreciation and amortization				22,348
Interest expense				22,135
Change in amortized cost of Partnership units liability				1,234
Gain on sale of property, plant and equipment				(3)
Restructuring costs				393
Foreign exchange gain				(2,030)
Income before income taxes				19,876
Income taxes				1,450
Net income				18,426

Geographic segments

The Partnership operates in Canada, the United States and Mexico. Revenue and assets were allocated to geographic segment based on the location of the customer and long-term assets, respectively.

	3-month period ended June 25, 2017	3-month period ended June 26, 2016	6-month period ended June 25, 2017	6-month period ended June 26, 2016
Revenue	\$	\$	\$	\$
Canada	187,783	180,263	361,660	344,035
US	114,904	102,617	219,553	206,403
Mexico	11,701	12,877	22,446	25,009
	314,388	295,757	603,659	575,447

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	June 25, 2017			
	Canada	US	Mexico	Total
	\$	\$	\$	\$
Property, plant and equipment	387,451	390,559	62	778,072
Goodwill	160,939	-	-	160,939
Intangible assets	14,781	-	-	14,781

	December 31, 2016			
	Canada	US	Mexico	Total
	\$	\$	\$	\$
Property, plant and equipment	357,689	404,581	-	762,270
Goodwill	160,939	-	-	160,939
Intangible assets	15,270	-	-	15,270

13 Financial instruments

Classification of financial instruments

As of June 25, 2017, the classification of the financial instruments, as well as their carrying amounts and fair values, was as follows:

	Classification	Measurement	Carrying amount	Fair Value
			\$	\$
Cash and cash equivalents	loans and receivables	amortized cost	28,286	28,286
Trade and other receivables	loans and receivables	amortized cost	107,667	107,667
Receivables from related parties	loans and receivables	amortized cost	273	273
Advances to partners	loans and receivables	amortized cost	3,678	3,678
Bank indebtedness	financial liabilities	amortized cost	(3,732)	(3,732)
Trade and other payables	financial liabilities	amortized cost	(180,883)	(180,883)
Payables to related parties	financial liabilities	amortized cost	(3,756)	(3,756)
Distributions payable	financial liabilities	amortized cost	(10,259)	(10,259)
Long-term debt	financial liabilities	amortized cost	(450,003)	(454,817)
Partnership units liability	financial liabilities	amortized cost	(142,356)	(142,356)

The following table details the fair value hierarchy of financial instruments by level as of June 25, 2017:

	Level 1	Level 2	Level 3	Total
	\$	\$	\$	\$
Long-term debt	-	(454,817)	-	(454,817)
Partnership units liability	-	-	(142,356)	(142,356)

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As of December 31, 2016, the classification of the financial instruments, as well as their carrying amounts and fair values, was as follows:

	Classification	Measurement	Carrying amount	Fair Value
			\$	\$
Cash and cash equivalents	loans and receivables	amortized cost	36,511	36,511
Trade and other receivables	loans and receivables	amortized cost	123,095	123,095
Receivables from related parties	loans and receivables	amortized cost	185	185
Advances to partners	loans and receivables	amortized cost	5,465	5,465
Mortgage receivable	loans and receivables	amortized cost	1,000	1,000
Bank indebtedness	financial liabilities	amortized cost	(9,007)	(9,007)
Trade and other payables	financial liabilities	amortized cost	(201,477)	(201,477)
Payables to related parties	financial liabilities	amortized cost	(3,606)	(3,606)
Distributions payable	financial liabilities	amortized cost	(10,148)	(10,148)
Long-term debt	financial liabilities	amortized cost	(424,238)	(431,041)
Partnership units liability	financial liabilities	amortized cost	(145,907)	(145,907)

The following table details the fair value hierarchy of financial instruments by level as of December 31, 2016:

	Level 1	Level 2	Level 3	Total
	\$	\$	\$	\$
Mortgage receivable	-	-	1,000	1,000
Long-term debt	-	(431,041)	-	(431,041)
Partnership units liability	-	-	(145,907)	(145,907)

Fair value

Cash and cash equivalents, trade and other receivables, receivables from related parties, advances to partners, mortgage receivable, bank indebtedness, trade and other payables, payables to related parties and distributions payable are short-term financial instruments whose fair value approximates the carrying amount, given they will mature in the near future. As of June 25, 2017, the fair values of the Credit Facility, the Nordea Facility and the Caisse Facility were \$214.0 million, \$26.3 million and \$194.5 million (December 31, 2016 – \$198.0 million, \$26.6 million and \$196.8 million), respectively, which approximates the current principal amount outstanding as the interest rate approximates current market interest rates. As of June 25, 2017, the fair values of the Quebec PM Loan and the Ontario Loan were \$17.6 million and \$2.4 million (December 31, 2016 – \$8.8 million and \$0.8 million), respectively, which are recorded on discounted future cash flows using a market rate of 4.4%, net of the government grant recorded on the below-market rate of interest.

Fair value of the Partnership units liability

The Partnership units liability is classified as a financial liability at amortized cost. Management has estimated the fair value of the Partnership units liability using a discounted cash flow model. Significant assumptions include the income tax obligation, discount rate and an industry capitalization rate. There were no significant changes in the assumptions during the 6-month period ended June 25, 2017.

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14 Cash and cash equivalents

	June 25, 2017	December 31, 2016
	<u>\$</u>	<u>\$</u>
Cash and cash equivalents	28,286	36,511
Bank indebtedness	<u>(3,732)</u>	<u>(9,007)</u>
Cash and cash equivalents in the consolidated statement of cash flows	<u><u>24,554</u></u>	<u><u>27,504</u></u>

15 Non-cash working capital

The change in non-cash working capital on the unaudited condensed consolidated statement of cash flows comprised the following:

	6-month period ended June 25, 2017	6-month period ended June 26, 2016
	<u>\$</u>	<u>\$</u>
Decrease (increase) in trade and other receivables	14,761	(4,832)
Decrease (Increase) in receivables from related parties	(88)	24
Increase in inventories	(11,126)	(4,214)
Increase in prepaid expenses	(3,683)	(1,297)
Decrease (increase) in other long-term assets	175	(137)
Decrease (increase) in income taxes	805	(849)
Increase (decrease) in trade and other payables	(32,083)	5,534
Increase in payables to related parties	<u>150</u>	<u>1,309</u>
	<u><u>(31,089)</u></u>	<u><u>(4,462)</u></u>