KRUGER PRODUCTS L.P.

AUDITED CONSOLIDATED FINANCIAL STATEMENT

FOR THE YEARS ENDED DECEMBER 31, 2018 AND DECEMBER 31, 2017

Kruger Products L.P
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Independent auditor's report

To the Unitholders of Kruger Products L.P.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Kruger Products L.P. and its subsidiaries, (together, the Partnership) as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Acccounting Standards Board (IFRS).

What we have audited
The Partnership's consolidated financial statements comprise:

- the consolidated statement of financial position as at December 31, 2018 and 2017;
- the consolidated statement of comprehensive income (loss) for the years then ended;
- the consolidated statement of changes in equity for the years then ended;
- the consolidated statement of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence
We are independent of the Partnership in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information. The other information obtained prior to the date of this auditor's report comprises the KP Tissue Inc. and Kruger Products L.P. Management's Discussion and Analysis of Results of Operations and Financial Position.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Partnership's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Partnership or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Partnership's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Partnership's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Partnership's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Partnership to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Partnership to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

(Signed) "PricewaterhouseCoopers LLP"

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Ontario
March 6, 2019

Kruger Products L.P.
Consolidated Statement of Financial Position

(tabular amounts are in thousands of Canadian dollars)

	December 31, 2018 $	December 31, 2017 $
Assets		
Current assets		
Cash and cash equivalents (note 25)	169,884	8,837
Trade and other receivables (note 6)	127,633	113,194
Receivables from related parties (note 16)	172	85
Current portion of advances to partners (note 14)	-	1,928
Inventories (note 7)	202,916	192,394
Income tax recoverable (note 15)	362	522
Prepaid expenses	6,904	8,007
	507,871	324,967
Non-current assets		
Advances to partners (note 14)	1,704	4,489
Property, plant and equipment (note 8)	786,022	761,610
Other long-term assets	10	6,331
Goodwill (note 9)	160,939	160,939
Intangible assets (note 9)	14,924	15,327
Deferred income taxes (note 15)	33,440	26,092
Total assets	1,504,910	1,299,755
Liabilities		
Current liabilities		
Bank indebtedness (note 25)	-	9,051
Trade and other payables (note 11)	238,856	190,698
Payables to related parties (note 16)	5,620	2,596
Income tax payable (note 15)	80	498
Distributions payable (notes 14 and 16)	10,723	10,382
Current portion of provisions (note 12)	292	333
Current portion of long-term debt (note 13)	13,939	190,947
	269,510	404,505
Non-current liabilities		
Long-term debt (note 13)	563,955	225,368
Provisions (note 12)	5,398	5,973
Pensions (note 10)	104,939	119,558
Post-retirement benefits (note 10)	54,051	60,457
Liabilities to non-unitholders	997,853	815,861
Current portion of Partnership units liability (note 14)	-	1,928
Long-term portion of Partnership units liability (note 14)	116,524	158,381
Total Partnership units liability	116,524	160,309
Total liabilities	1,114,377	976,170
Equity		
Partnership units (note 14)	376,274	356,240
Deficit	(78,780)	(99,742)
Accumulated other comprehensive income	93,039	67,087
Total equity	390,533	323,585
Total equity and liabilities	1,504,910	1,299,755

Commitments and contingencies (note 17)

Subsequent events (note 14)

Approved by the Board of Directors

/s/ James Hardy
Director

/s/ Michel Letellier
Director

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

Kruger Products L.P.
Consolidated Statement of Comprehensive Income (Loss)
For the years ended December 31, 2018 and December 31, 2017

(tabular amounts are in thousands of Canadian dollars)

	2018 $	2017 $
Revenue (notes 16 and 24)	1,370,432	1,280,014
Expenses		
Cost of sales (notes 16 and 18)	1,233,479	1,098,086
Selling, general and administrative expenses (notes 16 and 18)	87,655	90,076
Gain on sale of non-financial assets	(204)	(75)
Restructuring costs, net (note 12)	1	(180)
Operating income	49,501	92,107
Interest expense (note 13)	48,059	42,021
Other (income) expense (note 5)	(40,790)	21,990
Income (loss) before income taxes	42,232	28,096
Income taxes (note 15)	(3,174)	12,838
Net income for the year	45,406	15,258
Other comprehensive income (loss)		
Items that will not be reclassified to net income:		
Remeasurements of pensions	17,021	(27,563)
Remeasurements of post-retirement benefits	7,532	(2,763)
Items that may be subsequently reclassified to net income:		
Cumulative translation adjustment	25,952	(21,762)
Total other comprehensive income (loss) for the year	50,505	(52,088)
Comprehensive income (loss) for the year	95,911	(36,830)

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

Kruger Products L.P.
Consolidated Statement of Changes in Equity
For the years ended December 31, 2018 and December 31, 2017

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

	Partnership units		Deficit	Accumulated other comprehensive income	Total equity
	#	$	$	$	$
As of January 1, 2017	56,376,788	336,576	(42,792)	88,849	382,633
Distributions payable (note 14)	-	-	(10,382)	-	(10,382)
Distributions paid (note 14)	-	-	(30,786)	-	(30,786)
Fair value adjustment (note 14)	-	714	(714)	-	-
Change in actuarial loss on pension	-	-	(27,563)	-	(27,563)
Change in actuarial loss on post-retirement benefits	-	-	(2,763)	-	(2,763)
Cumulative translation adjustment	-	-	-	(21,762)	(21,762)
Net income for the year	-	-	15,258	-	15,258
Issuance of partnership units (note 14)	1,298,251	18,950	-	-	18,950
As of December 31, 2017	57,675,039	356,240	(99,742)	67,087	323,585
As of January 1, 2018	57,675,039	356,240	(99,742)	67,087	323,585
Change in accounting policy (note 3(*y*)(*i*))	-	-	(6,331)	-	(6,331)
Restated total equity as of January 1, 2018	57,675,039	356,240	(106,073)	67,087	317,254
Distributions payable (note 14)	-	-	(10,723)	-	(10,723)
Distributions paid (note 14)	-	-	(31,596)	-	(31,596)
Fair value adjustment (note 14)	-	347	(347)	-	-
Change in actuarial gain on pension	-	-	17,021	-	17,021
Change in actuarial gain on post-retirement benefits	-	-	7,532	-	7,532
Cumulative translation adjustment	-	-	-	25,952	25,952
Net income for the year	-	-	45,406	-	45,406
Issuance of partnership units (note 14)	1,896,360	19,687	-	-	19,687
As of December 31, 2018	59,571,399	376,274	(78,780)	93,039	390,533

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

Kruger Products L.P.
Consolidated Statement of Cash Flows
For the years ended December 31, 2018 and December 31, 2017

(tabular amounts are in thousands of Canadian dollars)

	2018 $	2017 $
Cash flows from (used in) operating activities		
Net income for the year	45,406	15,258
Items not affecting cash		
Depreciation	50,943	51,289
Amortization	1,426	1,092
Loss (gain) on sale of property, plant and equipment	622	(3)
Change in amortized cost of Partnership units liability (note 5)	(41,857)	23,013
Foreign exchange loss (gain) (note 5)	1,431	(1,387)
Change in fair value of derivatives (note 5)	(364)	364
Interest expense	48,059	42,021
Pension and post-retirement benefits (note 10)	12,954	10,111
Provisions (note 12)	(9)	278
Income taxes	(3,174)	12,838
Gain on sale of non-financial assets (note 8)	(204)	(75)
Total items not affecting cash	69,827	139,541
Net change in non-cash working capital (note 26)	26,968	(35,194)
Contributions to pension and post-retirement benefit plans (note 10)	(15,212)	(15,137)
Provisions paid (note 12)	(247)	(1,648)
Income tax payments	(2,478)	(3,592)
Net cash from operating activities	124,264	99,228
Cash flows from (used in) investing activities		
Purchases of property, plant and equipment	(33,647)	(68,127)
Purchases of property, plant and equipment related to the TAD2 Project	(26,638)	-
Capitalized interest paid	(184)	(497)
Government assistance received	19,226	4,646
Purchases of software	(1,023)	(1,149)
Proceeds on sale of property, plant and equipment	320	1,180
Net cash used in investing activities	(41,946)	(63,947)
Cash flows from (used in) financing activities (note 27)		
Proceeds from long-term debt	484,755	28,834
Repayment of long-term debt	(326,900)	(26,039)
Payment of deferred financing fees	(18,489)	(12)
Interest paid on long-term debt	(34,351)	(33,101)
Distributions and advances paid, net (note 14)	(19,506)	(31,547)
Net cash from (used in) financing activities	85,509	(61,865)
Effect of exchange rate changes on cash and cash equivalents held in foreign currency	2,271	(1,134)
Increase (decrease) in cash and cash equivalents during the year	170,098	(27,718)
Cash and cash equivalents - Beginning of year (note 25)	(214)	27,504
Cash and cash equivalents - End of year (note 25)	169,884	(214)

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

(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.

On August 16, 2018, the Partnership announced its plan for a capital investment of $575 million in the Brompton area of Sherbrooke, Quebec, for the construction of a new tissue plant featuring a new TAD paper machine (TAD2) along with related converting equipment and infrastructure (the TAD2 Project).

2 Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) 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 consolidated financial statements were approved by the board of directors of KPGP Inc. on March 6, 2019.

The Partnership consolidates all entities which it controls.

The principal subsidiaries of the Partnership are as follows:

K.T.G. (USA) Inc. (KTG)
Kruger Products (USA) Inc. (KP USA)
Grupo Tissue de Mexico S de RL de CV (GTM)
TAD Luxembourg S.A.R.L
TAD Canco Inc.
Kruger Products Real Estate Holdings Inc.
Kruger Products AFH GP. Inc.
Kruger Products AFH L.P.
Kruger Products Sherbrooke Inc. (KPSI)
KP TAD Holdco Inc.
TAD1 Canco I Inc.
TAD1 Canco II Inc.
TAD1 GP ULC
TAD2 GP ULC
TAD2 US LP
TAD1 US LP

3 Summary of significant accounting policies

The significant accounting policies used in the preparation of these consolidated financial statements were as follows:

(a) Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention, except for the derivative liabilities which are measured at fair value through profit or loss and accounting for pensions (note 3(*s*)).

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

The preparation of consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Partnership's accounting policies. The areas involving a higher degree of judgment or complexity or areas where assumptions and estimates are significant are disclosed in note 4.

(b) Consolidation

Subsidiaries are all those entities over which the Partnership has the power over the investee, is exposed or has rights to variable returns from its involvement with the investee and has the ability to affect these returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to the Partnership and de-consolidated from the date that control ceases. Intercompany transactions, balances and unrealized gains/losses on transactions between group companies are eliminated on consolidation.

The purchase method of accounting is used to account for the acquisition of subsidiaries that are not under common control. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the Partnership's share of the identifiable net assets acquired is recorded as goodwill.

(c) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer. The operating segments for the Partnership include Consumer, Away-From-Home (AFH) and Other.

(d) Foreign currency translation

(i) Functional and presentation currency

Items included in the consolidated financial statements of each entity of the Partnership are measured using the currency of the primary economic environment in which the entity operates (the functional currency). These consolidated financial statements are presented in Canadian dollars, which is the Partnership's functional currency.

The Partnership has determined that its foreign operations located in the United States (KTG and KP USA) and TAD Canco Inc., TAD Luxembourg S.A.R.L., TAD1 Canco I Inc., TAD1 GP ULC, TAD1 US LP and TAD1 Canco II Inc. have a functional currency of U.S. dollars. Mexico (GTM) has a functional currency of the Mexican peso. Consequently, revenue and expenses of these foreign operations are recorded using the rate of exchange in effect at the dates of the transactions and the translation of assets and liabilities use the rates of exchange in effect at the period-end date, with the resulting net unrealized gains and losses arising from the translation of these foreign operations included as part of the currency translation adjustment in other comprehensive income (loss).

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the rate of exchange in effect at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange prevailing at the date of the consolidated statement of financial position. Foreign exchange gains and losses arising from translating monetary foreign currency balances are included in selling, general and administrative (SG&A) expenses or other expenses.

(e) *Cash and cash equivalents*

The Partnership considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

(f) *Trade receivables*

Trade receivables are amounts due from customers from the sale of products or services rendered in the ordinary course of business. Trade receivables are classified as current assets if payment is due within one year or less. Trade receivables are recognized initially at fair value and subsequently measured at amortized cost, less provision for expected credit losses.

(g) *Inventories*

Inventories of raw materials and spare parts are valued at the lower of weighted average cost and net realizable value. Finished products and work-in-process are valued at the lower of standard cost and net realizable value and include the cost of raw materials, direct labour and manufacturing overhead expenses. Net realizable value is the estimated selling prices less applicable selling expenses and costs to complete. If the carrying value exceeds the net realizable value, a write-down is recognized.

(h) *Borrowing costs*

Borrowing costs attributable to the acquisition, construction or production of qualifying assets are added to the cost of these assets, until such time as the assets are substantially ready for their intended use. All other borrowing costs are recognized as interest expense in the consolidated statement of comprehensive income (loss) in the period in which they are incurred.

(i) *Property, plant and equipment*

Property, plant and equipment are stated at cost, less accumulated depreciation, investment tax credits, U.S. State tax credits, government assistance and accumulated impairment loss. Cost includes expenditures that are directly attributable to the acquisition of the asset and an estimate of the asset retirement obligation. The Partnership allocates the amount initially recognized to an item of property, plant and equipment to its segregated parts and depreciates each of these segregated parts separately. The Partnership also capitalizes interest costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of the asset. Subsequent costs are included in the asset's carrying value or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Partnership and the cost can be reliably measured. The carrying amount of a replaced asset is derecognized when replaced. Residual values, method of depreciation and useful lives of property, plant and equipment are reviewed annually and adjusted if appropriate.

Depreciation of property, plant and equipment is generally calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives as follows:

Buildings	20 to 40 years
Machinery and equipment	5 to 40 years

Assets under construction or development are depreciated from the date the asset is ready for productive use. Land is not depreciated.

Repairs and maintenance costs are charged to the consolidated statement of comprehensive income (loss) during the period in which they are incurred.

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included in SG&A expenses.

(j) Goodwill

Goodwill arises on the acquisition of subsidiaries and represents the excess of the consideration transferred over the Partnership's interest in fair value of the net identifiable assets, liabilities and contingent liabilities of the acquiree. Goodwill is carried at cost less accumulated impairment losses.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash-generating units (CGUs), or groups of CGUs, that is expected to benefit from the synergies of the combination. Each CGU or group of CGUs to which the goodwill is allocated represents the lowest level within the Partnership at which the goodwill is monitored for internal management purposes.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of the CGU is compared to the recoverable amount, which is the higher of the value in use and the fair value less costs to sell. Any goodwill impairment is recognized immediately as an expense and is not subsequently reversed.

(k) Intangible assets

(i) Trademarks

Separately acquired trademarks have indefinite useful lives and are carried at cost. The trademarks have indefinite useful lives as the trademarks can be renewed infinitely without substantial cost. Management believes the trademarks are very well established in the marketplace and will continue to provide benefits indefinitely into the future.

(ii) Software and licences

Costs to purchase non-integral software and licences are capitalized and included as part of intangible assets on the consolidated statement of financial position. Costs associated with maintaining software programs are recognized as an expense as incurred.

Software and licence costs recognized as assets are amortized over their estimated useful lives, which represent management's view of the expected period over which the Partnership will receive benefits from the software and licences. The useful life of software and licences is five years.

(l) Impairment of non-financial assets

The carrying values of non-financial assets with finite lives, such as property, plant and equipment and intangible assets with finite useful lives are assessed for impairment whenever events or changes in circumstances indicate their carrying amounts may not be recoverable. Non-financial assets that are not amortized are subject to an annual impairment test. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use (which is the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows. Non-financial assets other than goodwill that have suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

(m) Related party transactions

Related party transactions that are in the normal course of operations and have commercial substance are made under competitive terms and conditions or in accordance with the agreements with the related party.

(n) Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the consolidated statement of comprehensive income (loss) on a straight-line basis over the period of the lease.

(o) Provisions

Provisions include environmental and asset retirement obligations, long-term incentives and restructuring. A provision is recognized when the Partnership has a legal or constructive obligation as a result of a past event and it is probable that settlement of the obligation will require a financial payment or cause a financial loss and a reliable estimate can be made of the amount of the obligation.

If some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement is recorded in the consolidated statement of financial position as a separate asset, but only if it is virtually certain that the reimbursement will be received.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

(p) Government assistance, investment tax credits and U.S. State tax credits

Government assistance, investment tax credits, and U.S. State tax credits are accounted for using the cost reduction method, whereby such amounts are deducted from the expenditures or assets to which they relate when there is reasonable assurance that the assistance or credit will be received and where the Partnership will comply with the conditions attached to the assistance.

(q) Revenue recognition

For the year ended December 31, 2018:

The Partnership recognizes revenue when control of the products has transferred, being when the products are delivered to, and accepted by, the customer (based on shipping terms).

Revenue is measured based on the price specified in the sales contract and is net of discounts, rebates and allowances. Reductions to revenue for expected and actual payments to customers for rebates and allowances are based on actual expenses incurred during the period, on estimates of what is due to customers for estimated credits earned during the period and any adjustments for credits based on actual activity. Revenue is only recognized to the extent that it is highly probable that a significant reversal will not occur. As all of the Partnership's sales contracts have a term of less than one year, the Partnership has elected to use the practical expedient and therefore not capitalize closing contract costs or disclose unfulfilled performance obligations. A contract liability is recognized for expected discounts, rebates and allowances payable to customers in relation to sales made in the reporting period. The contract liability is included in trade and other payables.

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

For the year ended December 31, 2017:

The Partnership recognizes revenue when it is probable that the economic benefits will flow to the Partnership, the significant risks and benefits of ownership are transferred (based on shipping terms), the price is fixed or determinable and collection of the resulting receivable is reasonably assured.

Revenue is measured based on the price specified in the sales contract and is net of discounts, rebates and allowances. Reductions to revenue for expected and actual payments to customers for rebates and allowances are based on actual expenses incurred during the period, on estimates of what is due to customers for estimated credits earned during the period and any adjustments for credits based on actual activity.

(r) Cost of sales and SG&A expenses

Cost of sales includes cost of finished goods sold, freight, warehousing, handling costs, and inventory write-downs. Marketing, selling, and general and administrative expenses are included in SG&A expenses.

(s) Pensions and post-retirement benefits

The Partnership accrues its obligation under employee benefit plans and the related costs, net of plan assets. The Partnership has the following policies:

- The costs of pensions under defined benefit plans and post-retirement benefits are actuarially determined using the projected unit credit method and management's best estimate of expected plan investment performance for funded plans, salary escalation, retirement ages of employees and expected health-care costs. Actuarial valuations for defined benefit plans and post-retirement benefits are completed annually. The discount rate applied in arriving at the present value of the pension liability represents the yield on high quality corporate bonds denominated in the currency in which the benefits are to be paid and having terms to maturity approximating the terms of the related pension liability.

- Pension assets are valued at fair value.

- Past-service costs from plan amendments are recognized immediately to the extent the benefits are vested in net income (loss) and are otherwise amortized on a straight-line basis over the average period until the benefits become vested.

- The actuarial gains or losses are recognized in full in the period in which they occur in other comprehensive income (loss) without recycling to the income statement in subsequent periods. Amounts recognized in other comprehensive income (loss) are recognized immediately in retained earnings (deficit).

- The pension expense is split into two components: (i) current service costs and past-service costs have been recognized in cost of sales and SG&A expenses; and (ii) the interest cost on the benefit obligation offset by the expected return on plan assets is recorded within interest expense on the consolidated statement of comprehensive income (loss).

- The Partnership also participates in a multi-employer pension plan and defined contribution pension plans. The costs of the multi-employer pension plan and defined contribution pension plans are charged to expense as the contributions become payable.

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

(t) Income taxes

The tax expense for the year comprises current and deferred tax. Tax is recognized in net income (loss), except to the extent that it relates to items recognized in other comprehensive income (loss) or directly in equity. In this case, the tax is also recognized in other comprehensive income (loss) or directly in equity, respectively.

The Partnership is not a tax paying entity. The income from the Partnership flows to the partners, Kruger Inc., KPGP and KPT. Accordingly no provision for income taxes has been made for the Partnership's income. The U.S. entities, KP USA and KTG are subject to tax on the basis of the tax laws enacted in the U.S. where the entities operate and generate taxable income. The remaining entities, TAD Canco Inc., GTM, TAD Luxembourg S.A.R.L., KP TAD Holdco Inc., TAD1 Canco I Inc., TAD1 Canco II Inc., TAD1 GP ULC, TAD2 GP ULC, and KPSI are subject to tax on the basis of the laws enacted in Canada, Mexico and Luxembourg.

Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. The Partnership establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Current tax is the expected tax payable on the taxable income for the year at closing tax rates enacted or substantively enacted at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognized if they arise from the initial recognition of goodwill, or from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates and laws that have been enacted or substantively enacted by the consolidated statement of financial position dates and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. Deferred income tax assets and liabilities are presented as non-current.

(u) Financial instruments

Financial assets and liabilities are recognized when the Partnership becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Partnership has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognized when the obligation specified in the contract is discharged, cancelled or expired.

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

(i) *Investments and other financial assets*

For the year ended December 31, 2018, the Partnership accounted for its investments and other financial assets as follows:

Classification

Beginning January 1, 2018, the Partnership classifies its financial assets in the following measurement categories, as disclosed in note 21:

- those to be measured subsequently at fair value (either through other comprehensive income (OCI), or through profit or loss), and
- those to be measured at amortized cost

The classification depends on the Partnership's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether the Partnership has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The Partnership reclassifies debt investments only when its business model for managing those assets changes.

Measurement

At initial recognition, the Partnership measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Debt instruments

Subsequent measurement of debt instruments depends on the Partnership's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Partnership classifies its debt instruments:

- *Amortized cost:* Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. Interest income from these financial assets is included in interest income using the effective interest rate method. Any gain or loss arising on derecognition is recognized directly in profit or loss. Impairment losses are included in SG&A expenses.
- *FVOCI:* Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from the deficit to profit or loss and recognized in other income (expense). Interest income from these

financial assets is included in interest income using the effective interest rate method. Foreign exchange gains and losses are presented in SG&A expenses in the consolidated statement of comprehensive income (loss).

- *FVPL:* Assets that do not meet the criteria for amortized cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognized in profit or loss and presented net within other income (expense) in the period in which it arises.

Equity instruments

The Partnership subsequently measures all equity investments at fair value. Where the Partnership's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognized in profit or loss as other income when the Partnership's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognized in other income (expense) in the consolidated statement of comprehensive income (loss) as applicable. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

Impairment

Beginning January 1, 2018, the Partnership assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortized cost and FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

For trade receivables, the Partnership applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

(ii) *Investments and other financial assets*

For the year ended December 31, 2017, the Partnership accounted for its investments and other financial assets as follows:

At initial recognition, the Partnership classifies its financial instruments in the following categories:

(i) *Financial assets and liabilities at fair value through profit or loss:* A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the consolidated statement of comprehensive income (loss) in SG&A expenses. Financial assets and liabilities at fair value through profit or loss are classified as current, except for the portion expected to be realized or paid beyond 12 months of the dates of the consolidated statement of financial position, which are classified as non-current.

(ii) *Financial assets and liabilities at fair value through other comprehensive income or loss:* A financial asset or liability is classified in this category if acquired for the purpose of holding the investment for a long-term period. The financial instruments classified in this category would include the available-for-sale investment.

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the consolidated statement of comprehensive income (loss) in SG&A expenses. Gains and losses arising from changes in fair value of the available-for-sale investment are presented in the other comprehensive income (loss) in the period in which they arise. Financial assets and liabilities at fair value through other comprehensive income (loss) or loss are classified as current, except for the portion expected to be realized or paid beyond 12 months of the dates of the consolidated statement of financial position, which are classified as non-current.

(iii) *Loans and receivables*: Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables include cash and cash equivalents, trade and other receivables, mortgage receivable, receivables from related parties and advances to partners. Loans and receivables are initially recognized at the amount expected to be received, less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment. Loans and receivables are classified as current, except for the portion expected to be realized beyond 12 months of the dates of the consolidated statement of financial position, which are classified as non-current.

(iii) Financial liabilities at amortized cost

Financial liabilities at amortized cost include bank indebtedness, trade payables, accrued expenses, contract liabilities, payables to related parties, distributions payable, long-term debt and the Partnership units liability. Payables are initially recognized at the amount required to be paid less, when material, a discount to reduce the payables to fair value. Subsequently, bank indebtedness, payables to related parties, distributions payable, trade payables, accrued expenses and contract liabilities are measured at amortized cost using the effective interest method. Long-term debt is recognized initially at fair value, net of any transaction costs incurred and subsequently at amortized cost using the effective interest method. The Partnership units liability is recognized initially at fair value and subsequently at amortized cost. Amortized cost is estimated based on the expected tax distributions to be paid as required by the partnership agreement using a discount rate that reflects current market assessments of the time value of money and the rates specific to the obligation, and a terminal value as the obligation will continue indefinitely.

Financial liabilities are classified as current liabilities if payment is due within 12 months. Otherwise, they are presented as non-current liabilities.

(v) Fair value hierarchy

The Partnership categorizes its financial assets and liabilities measured at fair value into one of three different levels depending on the inputs used in the measurement.

- Level 1 - fair value based on unadjusted quoted prices for identical assets and liabilities in active markets that are accessible at the measurement date;
- Level 2 - valuations determined using directly or indirectly observable inputs other than quoted prices included within Level 1. Derivative instruments in this category are valued using models or other industry standard valuation techniques derived from observable market inputs; and
- Level 3 - valuations based on inputs that are less observable, unavailable or where the observable data does not support a significant portion of the instrument's fair value.

(w) Derivative financial instruments

From time to time the Partnership uses derivative financial instruments to manage foreign currency risk and interest rate risk. Foreign exchange swaps and foreign exchange forwards are used from time to time to manage U.S. dollar borrowings. Interest rate swaps are used to fix the interest rate under certain long-term debt obligations. As these derivatives do not qualify for hedge accounting, the changes in their fair value are recorded in the consolidated statement of comprehensive income (loss) in Other (income) expense. The derivative liabilities are recorded in the consolidated statement of financial position in Trade and other payables.

(x) Dividend reinvestment plan

Pursuant to the Dividend Re-investment Plan (DRIP), the Partnership is required to issue Partnership units in lieu of cash distributions at the option of the Partners. Upon settlement of the DRIP, the difference between the distributions declared and the fair value of the units issued is charged to retained earnings (deficit).

(y) Accounting standards implemented for the year ended December 31, 2018

(i) IFRS 15, Revenue from Contracts with Customers, specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with some informative, relevant disclosures. The Partnership adopted the standard on January 1, 2018 using the modified retrospective approach. The adoption of this standard had no significant impact on the consolidated financial statements. The application of IFRS 15 resulted in a change in the revenue recognition related to dispensers and related revenue. A transitional adjustment of $6.3 million, to reduce the balance related to the dispensers recorded in Other long-term assets at December 31, 2017, was recognized in the deficit on the date of initial application, January 1, 2018. Refer to the consolidated statement of changes in equity for the restated total equity as of January 1, 2018.

(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 adoption of this standard had no significant impact on the consolidated financial statements.

(iii) IFRS 2, Share-based Payments. In June 2016, the IASB issued an amendment to address (i) certain issues related to the accounting for cash settled awards, and (ii) the accounting for equity settled awards that include a "net settlement" feature in respect of employee withholding taxes. The adoption of this standard had no impact on the consolidated financial statements.

(iv) IFRIC 22, Foreign Currency Transactions and Advance Consideration. In November 2016, the IFRS Interpretation Committee issued an interpretation on how to determine the date of the transaction when applying the standard on foreign currency transactions, IAS 21. The interpretation applies where an entity either pays or receives consideration in advance for foreign currency-denominated contracts. The adoption of this standard had no significant impact on the consolidated financial statements.

(v) IAS 40, Investment Property. In December 2016, the IASB issued an amendment to clarify when assets are transferred to, or from, investment properties. The amendment clarified that to transfer to, or from, investment properties there must be a change in use. This change must be supported by evidence. A change in intention, in isolation, is not enough to support a transfer. The adoption of this standard had no impact on the consolidated financial statements.

(z) Accounting standards issued but not yet applied

The following revised standards and amendments are effective for annual periods beginning on or after January 1, 2019, with earlier application permitted where indicated. Management continues to assess the impact of these standards and amendments and has not yet determined whether it will early adopt them, except as noted below.

(i) 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 has performed an assessment of IFRS 16 adoption and expects a significant impact on the consolidated financial statements.

As at December 31, 2018, the Partnership had non-cancellable operating lease commitments of $91.7 million (note 17). Of these commitments, approximately $0.3 million relate to low value leases, which will be recognized on a straight-line basis as expense in the consolidated statement of comprehensive income (loss).

The Partnership expects to recognize, on January 1, 2019, a right-of-use asset of approximately $94 million to $100 million and a lease liability of approximately $115 million to $120 million for the remaining lease commitments (after adjustments for prepayments and accrued lease payments recognized as at December 31, 2018). Overall net assets are expected to decrease by approximately $20 million.

The Partnership does not expect a significant impact on consolidated net income or cash flow for 2018 as a result of adopting the new standard. Adjusted EBITDA is expected to increase by approximately $15 million to $18 million, as the operating lease payments were included in Adjusted EBITDA in prior reporting periods, while the amortization of the right-of-use assets and interest on the lease liabilities are excluded from this measure in future reporting periods.

Management has configured data systems and information technology to accommodate the requirements of IFRS 16 adoption. Internal controls over financial reporting and business processes impacted by the new standard have been modified and implemented accordingly. The implications on financing and compensation arrangements have also been evaluated and no significant impact is expected. Estimates noted above are subject to change as management completes its review and testing of the implementation of the new standard and systems. Management has elected to adopt IFRS 16 using the full retrospective approach, and has elected not to implement the practical expedients available under the standard.

(ii) IAS 19, Employee Benefits. In February 2018, the IASB issued an amendment in connection with defined benefit plans and accounting for plan amendments, settlements or curtailments. The mandatory effective date would be annual periods beginning on or after January 1, 2019, with early adoption permitted. The amended standard is not expected to have an impact on the consolidated financial statements.

(iii) IAS 28, Interests in Associates and Joint Ventures. In February 2018, the IASB issued an amendment to clarify that an entity applies IFRS 9, including its impairment requirements, to long term interests in an associate or joint venture to which the equity method is not applied. The mandatory effective date would be annual periods beginning on or after January 1, 2019, with early adoption permitted. The amended standard is not expected to have an impact on the consolidated financial statements.

(iv) IAS 1 and IAS 8, Definition of Material. In October 2018, the IASB issued amendments to the definition of material in IAS 1 and IAS 8 and provide guidance to improve consistency in the application of the concept whenever it is used. The mandatory effective date would be annual periods beginning on or after January 1, 2020, with early adoption permitted. The amended standards are not expected to have an impact on the consolidated financial statements.

(v) IFRS 3, Definition of a Business. In October 2018, the IASB issued an amendment that revises the definition of a business. The amendment aims to resolve the difficulties that arise when an entity determines whether it has acquired a business or a group of assets. The mandatory effective date would be annual periods beginning on or after January 1, 2020, with early adoption permitted. Management is evaluating the standard and has not yet determined the impact on its consolidated financial statements.

4 Critical accounting estimates and judgments

The preparation of these 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 consolidated financial statements and the disclosure of contingencies at the dates of the consolidated statements of financial position, and the reported amounts of revenues and expenses during the reporting period. On a regular basis and with the information available, management reviews its estimates, including those related to pensions and post-retirement obligations, the Partnership units liability, impairment tests and income taxes. Actual results could differ from those estimates. When adjustments become necessary, they are reported in earnings in the period in which they occur. The following are the estimates and judgments applied by management that most significantly affect the Partnership's consolidated financial statements.

Pensions and post-retirement benefit obligations

The present value of the pension and post-retirement obligations is dependent on actuarial calculations, which include a number of assumptions. These assumptions include the discount rate, which is used to calculate the present value of the estimated future cash outflows that will be required to meet the pension obligations. In determining the discount rate to use, the Partnership considers market yields of high quality corporate bonds denominated in Canadian dollars that have terms to maturity approximating the terms of the pension liability.

Other key assumptions for pension obligations are based in part on current market conditions. Additional information is disclosed in note 10.

Partnership units

On December 13, 2012, in connection with the issuance of Partnership units to KPT, the Limited Partnership Agreement was amended to require KPLP, subject to compliance with contractual obligations and applicable law, to make distributions to its partners in such amounts as would enable KPT to discharge its obligation to pay federal and provincial income taxes (the Tax Distribution). Each partner is entitled to its share of the Tax Distribution made in respect of any given year. KPLP determined that it was appropriate to reclassify a portion of its equity to Partnership units liability, since the Tax Distribution represents a contractual obligation to deliver cash and, as such, meets the definition of a financial liability for accounting purposes under IFRS. As of December 31, 2018, $116.5 million was recorded as a liability in respect of this obligation (December 31, 2017 - $160.3 million).

The liability is based on management's best estimate of the net present value of expected future Tax Distributions, which are made on a pro rata basis based on taxes payable by KPT, which results from KPT's taxable income from its partnership interest in KPLP. KPLP updates the net present value of the liability annually and records any resulting change in other income (expense). The net present value of the liability is based on a number of assumptions including estimates of taxable income and tax rates, as well as discount rates, growth rates, forecasted Adjusted EBITDA, future commodity prices and foreign exchange rates. Taxable income can differ significantly from accounting income as a result of both timing and permanent tax differences based on enacted tax legislation and therefore changes in the Partnership units obligation are not necessarily indicative of a change in the expected future profitability of KPLP.

As of December 31, 2018, $116.5 million was recorded as a liability in respect of this obligation (December 31, 2017 - $160.3 million). As of December 31, 2018, the valuation utilized a discount rate and terminal growth rate of 10.75% and 2.0% (December 31, 2017 – 11.75% and 2.0%), respectively. An increase/decrease in the discount rate by 0.5% would result in a decrease/increase in the Partnership units liability of approximately $7.7 million and $8.8 million, respectively. The discount rate reflects the risks associated with the business, which operates primarily in Canada.

The Partnership units liability was adjusted during the year ended December 31, 2018 to reflect the current year advances of $1.7 million made to the partners required to allow KPT to make tax installment payments. The gain of $41.9 million recorded during the year ended December 31, 2018 (2017 – loss of $23.0 million) related to the change in amortized cost of Partnership units liability represents the adjustment made as a result of the reassessment performed as of December 31, 2018. The change in the discount rate resulted in an increase in the liability of $14.6 million, while the changes in other assumptions resulted in a decrease to the liability of $56.5 million. The decrease resulted primarily from the current level of pulp and freight prices and the unfavourable foreign exchange fluctuations.

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

Impairment tests

The Partnership performs an annual impairment test for goodwill and indefinite lived trademarks. As of December 31, 2018, no impairments were identified as a result of these tests. The Partnership is executing a new marketing plan in support of the indefinite lived trademarks. Recoverable amounts are determined based on management's best estimate of value in use. The estimates of value in use are based on the present value of forecasted future cash flows. Additional assumptions include estimates of the discount rate, forecasted Adjusted EBITDA, growth rates, and foreign exchange rates.

Income taxes

The Partnership computes its income taxes in each jurisdiction in which its subsidiaries operate. Estimation of income taxes includes evaluating the recoverability of the deferred tax assets and the income taxes recoverable based on an assessment of the ability to use the underlying tax deductions and credits against future taxable income. The assessment requires an estimate of future taxable income compared to the net operating loss carry forwards and U.S. State tax credits. To the extent estimates differ from the final tax return, earnings would be affected in a subsequent period. During the year ended December 31, 2018, the Partnership assessed its ability to utilize the U.S. State tax credits. As a result of this assessment, a reversal of $1.2 million (December 31, 2017 – $2.8 million) of the U.S. State tax credits was recorded in the consolidated statement of comprehensive income (loss).

5 Other (income) expense

	2018	2017
	$	$
Foreign exchange loss (gain)	1,431	(1,387)
Change in amortized cost of Partnership units liability	(41,857)	23,013
Change in fair value of derivatives	(364)	364
	(40,790)	21,990

6 Trade and other receivables

	December 31, 2018	December 31, 2017
	$	$
Trade receivables	104,160	102,803
Other receivables	23,775	10,685
Employee loans	20	9
Less: Allowance for expected credit losses	(322)	(303)
	127,633	113,194

The Partnership sells eligible trade receivables owing by certain key customers through a factoring arrangement with the Bank of Nova Scotia, with a facility limit of $50 million. As eligible trade receivables are sold, the Partnership removes the factored receivables from the Consolidated Statement of Financial Position, recognizes the proceeds received as consideration for the transfer and records a loss on factoring, which is included in interest expense in the Consolidated Statement of Comprehensive Income (Loss). Cash flows from the factoring arrangement are presented as operating activities in the Consolidated Statement of Cash Flows. Additional information is disclosed in note 21.

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

7 Inventories

	December 31, 2018	December 31, 2017
	$	$
Finished products	92,350	88,639
Work-in-process	30,385	30,201
Raw materials and supplies	42,659	38,944
Spare parts	37,522	34,610
	202,916	192,394

Total inventories recognized as cost of sales during the year ended December 31, 2018 were $1,050.9 million (2017 – $933.3 million). The Partnership wrote-off inventories during the year ended December 31, 2018 totalling $3.7 million (2017 - $2.3 million). Inventory provisions as of December 31, 2018 were $7.6 million (December 31, 2017 - $6.6 million).

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

8 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 impairment	-	(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	-	-	63	74,892	74,955
Capitalized interest	-	204	551	-	755
Disposals	(61)	-	(41)	-	(102)
Government assistance	-	-	(4,646)	-	(4,646)
Transfers	-	15,187	77,349	(92,536)	-
Depreciation	-	(4,911)	(40,719)	-	(45,630)
Exchange differences	(101)	(3,855)	(21,972)	(64)	(25,992)
As of December 31, 2017	37,968	110,935	593,438	19,269	761,610
As of December 31, 2017					
Cost	37,968	195,832	1,127,282	19,269	1,380,351
Accumulated depreciation and impairment	-	(84,897)	(533,844)	-	(618,741)
Net book value as of December 31, 2017	37,968	110,935	593,438	19,269	761,610
Additions	-	-	-	58,887	58,887
Capitalized interest	-	-	-	794	794
Disposals	(116)	(1)	(621)	-	(738)
Government assistance	-	-	(1,182)	(18,044)	(19,226)
Transfers	28	2	24,286	(24,316)	-
Depreciation	-	(5,073)	(41,270)	-	(46,343)
Exchange differences	126	4,621	26,130	161	31,038
As of December 31, 2018	38,006	110,484	600,781	36,751	786,022
As of December 31, 2018					
Cost	38,006	201,684	1,183,635	36,751	1,460,076
Accumulated depreciation and impairment	-	(91,200)	(582,854)	-	(674,054)
Net book value as of December 31, 2018	38,006	110,484	600,781	36,751	786,022

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

9 Goodwill and intangible assets

	Trademarks $	Software $	Total $
As of January 1, 2017			
Cost	11,825	7,953	19,778
Accumulated amortization	-	(4,508)	(4,508)
Net book value as of January 1, 2017	11,825	3,445	15,270
Additions	-	1,149	1,149
Amortization	-	(1,092)	(1,092)
Net book value as of December 31, 2017	11,825	3,502	15,327
As of January 1, 2018			
Cost	11,825	9,102	20,927
Accumulated amortization	-	(5,600)	(5,600)
Net book value as of January 1, 2018	11,825	3,502	15,327
Additions	-	1,023	1,023
Amortization	-	(1,426)	(1,426)
Net book value as of December 31, 2018	11,825	3,099	14,924
As of December 31, 2018			
Cost	11,825	10,125	21,950
Accumulated amortization	-	(7,026)	(7,026)
Net book value as of December 31, 2018	11,825	3,099	14,924

The carrying value of goodwill as of December 31, 2018 was $160.9 million (December 31, 2017 - $160.9 million).

Impairment tests

The Partnership performs an annual impairment test for goodwill and indefinite lived trademarks. As of December 31, 2018 and December 31, 2017, no impairments were identified. Goodwill of $152.0 million is allocated to the Canada Consumer CGU and $8.9 million is allocated to the AFH CGU. The recoverable amount of the CGU is determined based on management's best estimate of value in use. The estimates of value in use were based on the present value of the forecasted future cash flows expected to be derived from the CGUs. Based on the sensitivity analysis, no reasonable change in assumptions would result in an impairment.

10 Pensions and post-retirement benefits

The Partnership sponsors a number of defined benefit and defined contribution pension plans, with participation available to substantially all of its employees. Length of service and individual earnings determine the pension and post-retirement benefits for all members of the Partnership plans.

The Partnership has five registered defined benefit pension plans with a final average salary component, four of which are registered in the province of Quebec and one of which is registered in the province of Ontario. The pension obligation, net of plan assets for these five plans of $83.8 million as of December 31, 2018 (December 31, 2017 -

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

$96.5 million) is included in Pensions on the consolidated statement of financial position. The solvency deficiency of the defined benefit plan for the Crabtree members is supported by a letter of credit in the amount of $3.6 million (December 31, 2017 - $4.6 million).

The Partnership has a Supplementary Retirement Plan (SRP) for designated employees. The accrued benefit liability, net of plan assets related to the SRP of $14.4 million as of December 31, 2018 (December 31, 2017 - $15.1 million) is included in Pensions on the consolidated statement of financial position, and is supported by irrevocable letters of credit in the amount of $17.3 million (December 31, 2017 - $21.0 million).

The Partnership also sponsors a Term Annuity Arrangement for the Western Manufacturing Division, which provides hourly employees with a bridging supplement commencing at age 61 and payable up to but not including age 65. The Term Annuity Arrangement is unfunded and the pension obligation of $6.8 million as of December 31, 2018 (December 31, 2017 - $8.0 million) is included in Pensions on the consolidated statement of financial position.

The Partnership's hourly employees at the Western Manufacturing Division are members of an industry multi-employer pension plan to which the Partnership contributes monies. During the year ended December 31, 2018, the Partnership contributed and expensed $2.8 million (2017 - $2.8 million) related to this defined benefit plan. Sufficient information regarding the Partnership's share of the defined benefit obligation is not available and accordingly the Partnership accounts for the multi-employer plan as a defined contribution plan.

The Partnership sponsors a defined contribution plan which covers substantially all of its salaried employees. During the year ended December 31, 2018, the Partnership recorded an expense of $2.5 million (2017 - $2.6 million) related to this plan.

KTG sponsors a defined contribution plan that covers substantially all of its employees. During the year ended December 31, 2018, the Partnership recorded an expense of $0.6 million (2017 - $0.6 million) related to this plan.

The Partnership provides certain health and other similar benefits for qualifying retirees (post-retirement benefit plans). These plans are not funded.

The measurement date of the employee future benefit plans is December 31 of each year.

By their design, the defined benefit pension plans and the post-retirement benefits plan exposes the Partnership to the typical risks faced by such plans such as investment performance (pension plans only), changes to the discount rate used to value the obligations, longevity of plan members and future inflation. Pension and benefit risk is managed by regular monitoring of the plans, applicable regulations and other factors that could impact the expenses and cash flows of the Partnership. As of December 31, 2017, the aggregate solvency deficit of the defined benefit plans was $100.4 million (December 31, 2016 - $105.2 million). The next actuarial valuations are required as of December 31, 2020. The funding obligations are dependent on a number of factors, including the assumptions used in the most recent actuarial valuation. Actual contributions that are determined on the basis of future valuation reports may vary significantly from the predictions.

The cumulative actuarial losses recognized in the deficit as of December 31, 2018 and December 31, 2017 were as follows:

	December 31, 2018 $	December 31, 2017 $
Pensions	106,214	123,235
Post-retirement benefits	12,779	20,311
Total	118,993	143,546

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

Information about the Partnership's defined benefit pension plans and post-retirement benefit plans was as follows:

	Pensions		Post-retirement benefit plans	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
	$	$	$	$
Change in defined benefit obligation:				
As of January 1	694,923	654,745	60,457	57,162
Current service cost	10,365	7,780	2,072	1,732
Interest cost	21,343	20,511	1,841	1,776
Employee contributions	3,797	3,484	-	-
Benefits paid	(35,122)	(34,301)	(2,787)	(2,976)
Remeasurements:				
Losses (gains) from changes in experience	953	792	(5,204)	(4,959)
Losses (gains) from changes in economic assumptions	(29,120)	41,912	(2,328)	3,725
Losses (gains) from changes in demographic assumptions	1,326	-	-	3,997
As of December 31	668,465	694,923	54,051	60,457
Change in plan assets at fair value:				
As of January 1	575,365	562,099	-	-
Expected return on plan assets	17,398	17,380	-	-
Remeasurements:				
(Losses) gains on plan assets	(9,820)	15,141	-	-
Administrative costs	(517)	(599)	-	-
Employer contributions	12,425	12,161	2,787	2,976
Employee contributions	3,797	3,484	-	-
Benefits paid	(35,122)	(34,301)	(2,787)	(2,976)
As of December 31	563,526	575,365	-	-
Accrued benefit liability				
Funded status - deficit	104,939	119,558	54,051	60,457

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

Plan assets, which are funding the Partnership's defined benefit plans, are comprised as follows:

	December 31, 2018	December 31, 2017
	%	%
Fixed income	34.7	38.8
Public equities	29.3	31.2
Hedge funds	21.3	17.8
Private equity	7.3	5.7
Real assets	7.4	6.5
Total	100.0	100.0
Quoted on an active market	64.0	70.0
Unquoted	36.0	30.0
	100.0	100.0

The following were the significant assumptions for the defined benefit pension plans and other benefit plans as of December 31:

	Pensions		Post-retirement benefit plans	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
	%	%	%	%
Assumptions				
Discount rate - accrued benefit obligation	3.65	3.36	3.65	3.36
Rate of compensation increases	3.25 - 4.00	3.25 - 4.00		

Except for the discount rate, the assumptions represent management's best estimates. The discount rate was based on the yield of high quality Canadian corporate fixed income investments with cash flows that match expected benefit payments.

Pensions

Expected fees payable by the plan were deducted from the expected rate of return of plan assets.

The effect of a 1% reduction in the discount rate, a 1% increase in the rate of compensation and one-year change in the life expectancy rate were:

	Discount rate		Rate of compensation		Life expectancy	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
	$	$	$	$	$	$
Increase in Pension obligation	102,835	113,176	7,092	10,297	15,966	18,229

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

Post-retirement benefit plan

For measurement purposes, the trend factor for all health-care expenses, excluding medication, was assumed to be 3.0%. The trend factor for medication was assumed to be 4.85% the first year, with an annual 0.05% reduction for 17 years, and 4.0% thereafter.

The sensitivity analysis presented was performed by changing each assumption individually. If an actual change were to occur, it is likely that certain of these assumptions would correlate, which would create a combined impact.

The effect of a 1% increase in the health care cost trend rate, a 1% reduction in the discount rate and a one-year change in the life expectancy rate were:

	Health care		Discount rate		Life expectancy	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
	$	$	$	$	$	$
Increase in Post-retirement benefit obligation	7,248	7,067	10,014	10,819	1,372	1,581

Contributions to the defined benefit pension plans for the year ending December 31, 2019 are expected to be $17.5 million.

The net benefit pension plan expense included the following components:

	Pensions		Post-retirement benefit plans	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
	$	$	$	$
Net benefit plan expense				
Current service cost	10,365	7,780	2,072	1,732
Interest cost	21,343	20,511	1,841	1,776
Expected return on plan assets	(17,398)	(17,380)	-	-
Administrative cost	517	599	-	-
	14,827	11,510	3,913	3,508

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

The following amounts are recognized in other comprehensive income (loss):

	Pensions		Post-retirement benefit plans	
	2018	**2017**	**2018**	**2017**
	$	**$**	**$**	**$**
Gains (losses) from changes in experience	(953)	(792)	5,204	4,959
Gains (losses) from changes in economic assumptions	29,120	(41,912)	2,328	(3,725)
Losses from changes in demographic assumptions	(1,326)	-	-	(3,997)
Gains (losses) on plan assets	(9,820)	15,141	-	-
	17,021	(27,563)	7,532	(2,763)

11 Trade and other payables

	December 31, 2018	December 31, 2017
	$	**$**
Trade payables	136,650	104,558
Accrued expenses	59,207	47,283
Contract liabilities	42,999	38,493
Derivative liabilities	-	364
	238,856	190,698

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

12 Provisions

	Environmental and asset retirement obligations **$** (a)	**Long-term incentives and DSU's** **$** (b)	**Restructuring** **$** (c)	**Total** **$**
Provisions as of January 1, 2017	5,887	1,047	1,438	8,372
Additional provisions	(911)	458	(180)	(633)
Paid during the year	-	(443)	(1,205)	(1,648)
Interest accretion	215	-	-	215
Provisions as of December 31, 2017	5,191	1,062	53	6,306
Current	-	280	53	333
Non-current	5,191	782	-	5,973
Provisions as of January 1, 2018	5,191	1,062	53	6,306
Additional provisions	(575)	(10)	1	(584)
Paid during the year	-	(193)	(54)	(247)
Interest accretion	215	-	-	215
Provisions as of December 31, 2018	4,831	859	-	5,690
Current	-	292	-	292
Non-current	4,831	567	-	5,398

(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 $8.0 million and $10.5 million. The liability is estimated using a discounted cash flow with a discount rate of 5.135% (December 31, 2017 – 4.165%).

(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.

The Partnership has adopted a policy that requires that each director own a minimum of 5,000 common shares and/or share equivalents in the form of deferred share units (DSUs) of KPT. A deferred share unit plan (Plan) has been adopted which allows independent directors to receive all or part of their director retainer fees in the form of DSUs. The Plan allows for the issuance of additional units as dividend equivalents when KPT declares and issues a dividend to shareholders. Upon the individual ceasing to be a director, the DSUs will be paid out in cash. As of December 31, 2018, DSUs of $0.05 million were recorded (December 31, 2017 – nil).

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

13 Long-term debt

	Maturity	December 31, 2018 $	December 31, 2017 $
Senior Credit Facility [(a)]	2023	109,008	181,055
Notes [(b)]	2025	121,887	-
AgCredit Agreement [(c)]	2036	190,191	-
IQ Debenture [(d)]	2028	87,566	-
Quebec PM Loan [(e)]	2026	31,985	34,581
Nordea2 Credit Facility [(f)]	2029	24,832	-
Nordea Credit Facility [(g)]	2019	8,960	16,405
Ontario Loan [(h)]	2026	3,465	2,513
Caisse Facility	2018	-	181,761
		577,894	416,315
Less: Current portion of long-term debt		13,939	190,947
		563,955	225,368

[(a) - (h)] All amounts are net of deferred financing fees

a) Senior Credit Agreement

The Partnership is a party to a sixth amended and restated credit agreement dated as of April 24, 2018 entered into by the Partnership, as borrower, the lenders party thereto and National Bank of Canada, as administrative agent, as amended by a first supplemental credit agreement dated November 19, 2018 (the Senior Credit Agreement) pursuant to which a senior secured revolving credit facility in a maximum amount of $200 million (reduced from $300 million) with a $75 million accordion feature (the Senior Credit Facility) is made available to the Partnership. The maturity date of the Senior Credit Facility is April 24, 2023. The Senior Credit Facility is to be used by the Partnership to finance general corporate purposes and the ongoing working capital requirements of the Restricted Credit Parties (as defined below), and to finance the cash portion of any permitted acquisition or any investment by any such Restricted Credit Party (as defined below).

The Senior Credit Agreement is guaranteed by each Restricted Credit Party. Under the Senior Credit Agreement, “Restricted Credit Parties” means the Partnership, KPGP, Kruger Products Real Estate Holdings Inc., GTM, KP USA, Kruger Products AFH G.P. Inc. and Kruger Products AFH L.P. and their respective subsidiaries involved in the tissue business but excluding the Unrestricted Credit Parties (which include TAD Canco Inc. TAD Luxembourg S.A.R.L., KTG, KPSI, KP TAD Holdco Inc., TAD2 GP ULC, TAD2 US LP, TAD1 Canco I Inc., TAD1 GP ULC, TAD1 US LP and TAD1 Canco II Inc.) and the Non-Material Credit Parties (as such terms are defined in the Senior Credit Agreement). All Restricted Credit Parties granted first ranking security interests and hypothecs over all of their assets, present and future, movable and immovable, corporeal and incorporeal, to secure the obligations under the Senior Credit Agreement including a pledge of 100% of the stock or ownership interest in all credit parties owned by the Partnership and the Restricted Credit Parties.

Borrowings under the Senior Credit Facility bear interest at a base rate of Canadian Prime Rate, U.S. Base Rate, LIBOR, Banker’s Acceptance Stamping Fees or LC Fees, plus a margin varying between 0.20% and 2.875% depending on the ratio of total net funded debt to EBITDA (as defined in the Senior Credit Agreement) and the type of advance. Stand-By Fees are also payable on the available portion of the Senior Credit Facility at a rate varying between 0.24% and 0.575% depending on the Restricted Credit Parties’ ratio of total net funded debt to EBITDA (as defined in the Senior Credit Agreement).

The Partnership may voluntarily cancel or reduce the Senior Credit Facility, in whole or in part, subject to minimum amounts and notice period, with customary restrictions on prepayment of Banker's Acceptances, Libor Loans and liabilities under Letters of Credit (in each case, as defined in the Senior Credit Agreement).

The Senior Credit Agreement contains customary affirmative covenants, including, but not limited to, delivery of financial and other information to the administrative agent, delivery of notice to the administrative agent upon the occurrence of certain material events, preservation of existence and authorizations, maintenance of insurance, compliance with laws, payment of taxes and other claims, limitation of transactions with affiliates and maintenance of security.

The Senior Credit Agreement requires the Restricted Credit Parties to comply with certain financial covenants, including, but not limited to, the maintenance of (i) a ratio of total net funded debt to EBITDA not greater than 4.25 to 1.00, (ii) a ratio of senior secured net funded debt to EBITDA not greater than 3.00 to 1.00, and (iii) an interest coverage ratio of at least 3.00 to 1.00. The financial covenants are calculated on an Adjusted Consolidated Basis (as defined in the Senior Credit Agreement) such that the Unrestricted Credit Parties are accounted for as investments but not consolidated. As such, indebtedness under the AgCredit Agreement and the Unrestricted Subsidiaries' EBITDA are not included in such calculations.

The Senior Credit Agreement contains customary negative covenants of the Partnership, including, but not limited to, (i) restrictions on the ability of the Partnership and the Restricted Credit Parties to, subject to certain exceptions, grant liens, incur indebtedness, merge or consolidate, amend, restate or otherwise modify the Limited Partnership Agreement, make investments and loans, grant guarantees, make acquisitions, declare, set apart and pay distributions (which does not apply to the Tax Distribution (as defined below) to KPT), reduce capital, sell or otherwise dispose of assets, incur capital expenditures or materially change their business, and (ii) restrictions on the indebtedness of TAD Canco Inc., TAD Luxembourg S.A.R.L and KTG and the amendment of the TAD financing documents.

The Senior Credit Agreement contains customary events of default, including, but not limited to, non-payment, misrepresentation, breach of covenants, cross-default and cross-acceleration to other debt above a certain threshold, cross defaults to the Nordea Credit Facility (as defined below) and the Caisse Facility (as defined below), insolvency, change of control of the Partnership or Kruger and enforcement proceedings.

The Senior Credit Facility is guaranteed by each Restricted Credit Party. the Partnership and each Restricted Credit Party granted first ranking security interests and hypothecs over their current and future tangible and intangible assets (subject to permitted liens) to secure the obligations under the Senior Credit Facility, including a pledge of all capital stock or ownership interest in all subsidiaries owned by the Partnership and the Restricted Credit Parties. The guarantees and security are granted on a pari passu basis in favour of the lenders and the administrative agent under the Senior Credit Agreement and the lenders and the administrative agent under the Nordea Credit Agreement (as defined below).

b) Indenture

On April 24, 2018, the Partnership issued $125 million aggregate principal amount of 6.0% senior unsecured notes due April 24, 2025 (the Notes) by way of private placement in Canada in accordance with applicable Canadian prospectus and registration exemptions. The Notes were issued pursuant to a trust indenture entered into as of April 24, 2018 between the Partnership, the Guarantors and Computershare Trust Company of Canada (the Indenture). Interest on the Notes accrues at 6.0% per year and is payable semi-annually on April 24 and October 24 of each year.

Under the Notes, "Restricted Subsidiaries" means any subsidiary of the Partnership that is not an Unrestricted Subsidiary as defined in the Indenture (which Unrestricted Subsidiaries include TAD Canco, TAD Luxembourg, KTG and Non-Material Subsidiaries as defined in the Indenture).

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

The Notes are senior unsecured obligations of the Partnership. The Notes rank senior in right of payment to all existing and future subordinated indebtedness of the Partnership and equal in right of payment to all indebtedness of the Partnership that is not subordinated in right of payment to the Notes other than any indebtedness that ranks senior to the Notes by operation of law. The Notes will be effectively subordinated to all existing and future secured indebtedness of the issuer, to the extent of the assets securing such indebtedness.

Proceeds from the offering were $125.0 million, which were used to reduce the outstanding balance under the Senior Credit Facility and to pay transactions costs associated with the offering.

The Notes are unconditionally guaranteed, jointly and severally, by all existing and future Restricted Subsidiaries (the Guarantors). The guarantees are senior unsecured obligations of each of the Guarantors and will rank senior in right of payment to all existing and future subordinated indebtedness of the Guarantors and equal in right of payment to all indebtedness of such Guarantor that is not subordinated in right of payment to their guarantee, other than indebtedness that ranks senior to the guarantees by operation of law.

At any time prior to April 24, 2021, the Partnership may redeem up to 35.0% of the aggregate principal amount of the Notes at a redemption price of 106% of the principal amount of the Notes to be redeemed, plus accrued and unpaid interest to the date of redemption, with the net proceeds received by KPLP from certain equity offerings after the issue date.

At any time prior to April 24, 2021, the Partnership may redeem the Notes, at a redemption price equal to the greater of (a) the Applicable Premium (as defined in the Indenture) and (b) 101% of the aggregate principal amount of the Notes redeemed, plus, in each case, accrued and unpaid interest, if any, to the applicable redemption date.

On or after April 24, 2021, the Partnership may redeem all or part of the Notes at the following redemption prices, plus accrued and unpaid interest to the applicable redemption date, if redeemed during the 12-month period commencing April 24 of the year set forth below:

Year	Percentage
2021	104.5%
2022	103.0%
2023	101.5%
2024 and thereafter	100.0%

Upon the occurrence of a Change of Control of the Partnership (as defined in the Indenture), the Partnership will be required to offer to repurchase all or any part of each holders Notes for a payment in cash equal to 101% of the aggregate principal amount of Notes repurchased, plus accrued and unpaid interest thereon to the purchase date.

The Indenture contains certain restrictive covenants of the Partnership, including, but not limited to, limitations on making certain restricted payments by the Partnership or its Restricted Subsidiaries, restrictions on incurring certain indebtedness by the Partnership or its Restricted Subsidiaries, restrictions on incurring certain liens by the Partnership or its Restricted Subsidiaries, restrictions on transactions with affiliates, limitations on engaging in any line of business other than the businesses in which the Partnership and the Restricted Subsidiaries were engaged on the date of issuance of the Notes, and any business reasonably related, incidental, complementary or ancillary thereto, limitations on creating any contractual restrictions on the ability of the Partnership or its Restricted Subsidiaries to take certain actions, such as the payment of dividends or making of distributions, restrictions on consolidating, amalgamating or merging into any other person and restrictions on selling, transferring, assigning, leasing, conveying or otherwise disposing of all or substantially all of the property of the Partnership and the Restricted Subsidiaries taken as a whole.

The Indenture contains customary events of default such as non-payment, liquidation of assets, change of control, non-payment or acceleration of any indebtedness in an aggregate amount exceeding $25 million, insolvency and enforcement proceedings.

c) AgCredit Agreement

Subsidiaries of the Partnership are party to a credit agreement dated as of November 19, 2018 entered into by, among others, KTG, TAD 1 US LP, TAD2 US LP and KPSI, as borrowers, each guarantor from time to time party thereto, as guarantors, each lender from time to time party thereto, as lenders, American AgCredit, FLCA, as administrative agent and National Bank of Canada, as Canadian administrative agent (AgCredit Agreement) pursuant to which the following credit facilities were made available: (i) US $188 million term loan facility repayable by December 31, 2036 by quarterly principal instalment payments commencing on March 31, 2026 and bearing interest at a fixed rate based on the farm credit system cost of funds plus an applicable margin set at the time of each tranche draw, (ii) $111 million term loan repayable by December 31, 2025 by quarterly principal instalment payments commencing on March 31, 2022 and bearing interest at a floating interest rate based on CDOR plus an applicable margin, (iii) revolving loans of U.S. $10 million and $12.5 million for five years with floating interest rates and a renewal option (the facility detailed in items (i) to (iii), collectively the TAD2 Project Facility), and (iv) U.S. $147 million term loan repayable by December 31, 2036 by quarterly principal instalment payments commencing on March 31, 2022 and bearing interest at a 7.3% maximum fixed interest rate and repayable after a three-year lock-out period (the KTG Facility).

Interest expense on the AgCredit Agreement is recorded based on an effective interest rate of 7.1%.

The purpose of the TAD2 Project Facility is to partially finance the TAD2 Project. The purpose of the KTG Facility is to repay existing indebtedness of KTG and TAD Canco Inc.

The TAD2 Project Facility and KTG Facility are each guaranteed by each of the borrowers and guarantors. All Borrowers and Guarantors are granted first ranking security interests over all of their assets, present and future, movable and immovable, corporeal and incorporeal, to secure the obligations under the AgCredit Agreement.

The Borrowers may voluntarily cancel or reduce the revolving loans, in whole or in part, without premiums or penalty. The Borrowers shall have the right at any time to voluntarily prepay the entire amount or any amount outstanding of the term loans subject to minimum amounts and notice period. Prepayment shall be accompanied by the payment of all accrued and unpaid interest with respect to fixed rate advances. If all or any portion of the outstanding balance of a term loan is prepaid prepayment premiums may apply.

The AgCredit Agreement contains customary affirmative covenants, including, but not limited to, delivery of financial and other information to the administrative agent, delivery of notice to the administrative agent upon the occurrence of certain material events, preservation of existence and authorizations, maintenance of insurance, compliance with laws, payment of taxes and other claims, limitation of transactions with affiliates and maintenance of security.

The AgCredit Agreement contains customary events of default such as non-payment, misrepresentation, breach of covenants and change of control.

As of December 31, 2018, U.S.$147.0 million has been drawn on the KTG Facility and no amounts have been drawn on the TAD2 Project Facility. As of December 31, 2018, unamortized deferred financing fees were $10.3 million (December 31, 2017 – nil).

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

d) IQ Debenture

On November 19, 2018, KPSI issued a 10-year convertible debenture in favour of Investissement Québec (IQ) in the principal amount of $105 million (the IQ Debenture). The IQ Debenture is being used to partially finance the TAD2 Project.

Borrowings under the IQ Debenture bear interest at a fixed capitalized interest rate of 3%.

The IQ Debenture is redeemable on a monthly basis commencing 36 months from the date of issuance, which payments KPSI undertakes to cause KPLP or Kruger Inc. to make, failing which IQ will have a conversion right on terms of conversion that would provide IQ with a 48% equity interest in KPSI if the entirety of the debenture was so converted.

Pursuant to a repayment agreement (the Repayment Agreement) between Kruger Inc., the Partnership, KPSI, and IQ, the Partnership has at its discretion, a priority right to make any required monthly redemption payment to IQ. The party that makes the redemption payment will receive common shares of KPSI as consideration of such payment. Pursuant to the Repayment Agreement, if Kruger Inc. makes all of the redemption payments, it will hold approximately 48% of KPSI.

The IQ Debenture contains covenants including, but not limited to, providing proof of the existence of binding commitments with respect to each source of debt financing for the TAD2 Project and the delivery of financial statements and other information.

The IQ Debenture contains customary events of default such as failure to convert, misrepresentation and breach of covenants.

The Partnership has recorded the IQ debenture at its fair value of $87.6 million at the date of issuance. The fair value was estimated by discounting the cash flows using a discount rate of 6.0%. The difference between the proceeds received of $105.0 million and the fair value has been recorded as government assistance and netted against the purchases of the property, plant and equipment for the TAD2 Project.

As of December 31, 2018, unamortized deferred financing fees were $0.6 million (December 31, 2017 – nil).

e) Quebec PM Loan Agreement

The Partnership is a party to a loan agreement dated as of August 9, 2016 entered into by the Partnership, as borrower, and IQ as lender (the Quebec PM Loan Agreement) pursuant to which a secured non-revolving loan in a maximum amount of $39.5 million (the Quebec PM Loan) is made available to the Partnership. The Quebec PM Loan is being used to partially finance the acquisition and relocation of a paper machine to be installed at the Crabtree facility (PM Project). The Quebec PM Loan Agreement matures ten years after the first loan disbursement, which occurred on September 6, 2016.

Borrowings under the Quebec PM Loan bear interest at a fixed interest rate of 2.5% per annum for a period of seven years from the date of the first loan disbursement. The interest rate thereafter increases to a fixed rate of 3.5% per annum until the eighth anniversary of the first loan disbursement, a fixed rate of 4.5% per annum until the ninth anniversary of the first loan disbursement, and a fixed rate of 5.5% per annum thereafter. Monthly interest payments commence the month following the first loan disbursement.

The Quebec PM Loan has a moratorium on repayment of the principal for the initial 24 months following the date of the first loan disbursement, after which the principal is to be repaid in 96 monthly consecutive payments.

The monthly repayments are reduced, in the reverse order of maturity, by repayments to Investissement Quebec corresponding to the Partnership's receipt of Government of Quebec electricity tariff rebates.

The Quebec PM Loan Agreement contains covenants including, but not limited to, delivery of financial and other information to IQ, the preservation of existence, maintenance of insurance and maintenance of operations. The Quebec PM Loan Agreement also contains restrictions on the disposition of assets, incurrence of indebtedness and granting of liens, change of control and changes in the PM Project.

The Quebec PM Loan Agreement contains customary events of default such as non-performance, non-payment, misrepresentation, breach of covenants, cross-default to the Nordea Credit Facility (as defined below) and the Senior Credit Facility, insolvency and enforcement proceedings.

The Quebec PM Loan is secured by the acquired paper machine and the portion of the property on which the paper machine is installed. The security is second ranking immediately after the security granted in favour of the Senior Credit Facility.

f) Nordea2 Credit Agreement

The Partnership is party to a credit agreement dated as of November 2, 2018 entered into by the Partnership, as borrower, the lender party thereto and Nordea Bank Abp Filial I Sverige, as administrative agent, as amended by an amendment letter dated November 19, 2018 (the Nordea2 Credit Agreement) pursuant to which a senior secured non-revolving loan facility in a maximum amount of U.S. $48.8 million (the Nordea2 Credit Facility) was made available to the Partnership. The Nordea2 Credit Facility is to be used to partially finance the TAD2 Project and the fees of the Swedish Export Credits Guarantee Board (EKN) in connection with its guarantee of the Nordea2 Credit Facility. The Nordea2 Credit Facility matures on August 31, 2029.

Borrowings under the Nordea2 Credit Facility bear interest at a fixed interest rate of 3.74% per annum, comprised of a Swedish state reported interest rate, risk premium and administrative margin.

The Nordea2 Credit Facility is repayable in 17 equal consecutive semi-annual installments of principal together with interest commencing at the latest on August 28, 2021. Prepayments are allowed subject to a make-whole payment on account of interest losses.

The covenants, financial covenants and negative covenants provided by the Partnership under the Senior Credit Agreement are incorporated and made part of the Nordea2 Credit Agreement. See Senior Credit Agreement above. The Nordea2 Credit Agreement contains restrictions on amendments to the Senior Credit Agreement and related security and other documents.

The Nordea2 Credit Agreement contains customary events of default such as non-payment, misrepresentation and breach of covenants and also provides for a cross-default to the Senior Credit Agreement and a default related to the termination or loss of the EKN guarantee.

The Nordea2 Credit Agreement provides for pari passu security and guarantees on the assets and undertaking of the Partnership and each Restricted Credit Party, the relationship between the lender and administrative agent under the Nordea Credit Agreement, the Nordea2 Credit Agreement and the administrative agent and the lenders under the Senior Credit Agreement being governed by a collateral agency and security sharing agreement.

As of December 31, 2018, unamortized deferred financing fees were $3.7 million (December 31, 2017 – nil).

g) Nordea Credit Agreement

The Partnership is a party to a fourth amended and restated credit agreement (the Nordea Credit Agreement) dated as of April 24, 2018 entered into by the Partnership, as borrower, the lender party thereto and Nordea Bank Abp Filial I Sverige (as successor of Nordea Bank A.B. (publ)), as administrative agent, as amended by an amendment letter dated November 19, 2018 (the Nordea Credit Agreement) pursuant to which a senior secured non-revolving loan facility in a maximum amount of U.S. $46.2 million (the Nordea Credit Facility) was made available to the Partnership. The Nordea Credit Facility was used to pay up to 85% of the equity investment of the Partnership in the Memphis TAD Machine and the fees of the Swedish Export Credits Guarantee Board (EKN) in connection with its guarantee of the Nordea Credit Facility. The Nordea Credit Facility matures on December 30, 2019.

Borrowings under the Nordea Credit Facility bear interest at a fixed interest rate of approximately 3% per annum, comprised of a Swedish state reported interest rate, risk premium and administrative margin.

The Nordea Credit Facility is repayable in 14 equal consecutive semi-annual installments of principal together with interest commencing on June 28, 2013. Prepayments are allowed subject to a make-whole payment on account of interest losses.

The covenants, financial covenants and negative covenants provided by the Partnership under the Senior Credit Agreement are incorporated and made part of the Nordea Credit Agreement. See Senior Credit Agreement above. The Nordea Credit Agreement contains restrictions on amendments to the Senior Credit Agreement and related security and other documents.

The Nordea Credit Agreement contains customary events of default such as non-payment, misrepresentation and breach of covenants and also provides for a cross-default to the Senior Credit Agreement and a default related to the termination or loss of the EKN guarantee.

The Nordea Credit Agreement provides for pari passu security and guarantees on the assets and undertaking of the Partnership and each Restricted Credit Party, the relationship between the lender and administrative agent under the Nordea Credit Agreement, the Nordea2 Credit Agreement and the administrative agent and the lenders under the Senior Credit Agreement being governed by a collateral agency and security sharing agreement.

h) Ontario Loan Agreement

The Partnership is a party to a conditional loan agreement dated as of July 1, 2015 entered into by the Partnership, as borrower, and the Government of Ontario as lender (the Ontario Loan Agreement) pursuant to which a secured non-revolving loan in a maximum amount of $10.0 million (the Ontario Loan) is made available to the Partnership. The Ontario Loan is being used to partially finance the expansion project at the Trenton facility. The Ontario Loan Agreement matures ten years after the first loan disbursement, which occurred on February 24, 2016.

Borrowings under the Ontario Loan bear interest, up to a maximum rate of 4.4% per annum for a period of ten years from the date of the first loan disbursement. A portion of the loan interest is forgivable, subject to prescribed conditions.

The Ontario Loan has a moratorium on repayment of the principal for the initial five years following the date of the first loan disbursement, after which the principal is to be repaid in five equal annual payments. A portion of the loan principal is forgivable, subject to prescribed conditions, up to a maximum forgivable portion of $5.0 million.

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

The Ontario Loan Agreement contains covenants including, but not limited to, delivery of financial and other information to the Government of Ontario, the preservation of existence, maintenance of insurance, compliance with laws, payment of taxes, completion of project and limitations on project procurement. The Ontario Loan Agreement also contains restrictions on the disposition of assets and changing the nature of the business and an undertaking to comply with the negative covenants in the Senior Credit Agreement.

The Ontario Loan Agreement contains customary events of default such as non-performance, non-payment, misrepresentation, breach of covenants and abandonment of the project and also provides for a cross-default to the Senior Credit Agreement.

The Ontario Loan is secured by the assets acquired for the expansion project at the Trenton facility.

The aggregate future principal repayments required on long-term debt are as follows:

	$
Less than 1 year	13,635
Between 1 and 5 years	214,029
More than 5 years	390,246
	617,910

Interest expense reflected on the consolidated statement of comprehensive income (loss) was as follows:

	2018	2017
	$	$
Interest expense on long-term debt	42,058	36,899
Interest accretion on provisions and other liabilities	215	215
Pension and post-retirement benefits, net	5,786	4,907
	48,059	42,021

14 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)	23,013
Tax Distributions	(8,611)
As of December 31, 2017	160,309
As of January 1, 2018	160,309
Change in amortized cost of Partnership units liability (note 5)	(41,857)
Tax Distributions	(1,928)
As of December 31, 2018	116,524

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

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:

				2018
Distribution Payment Date	**Partnership unit distributions** $	**Unit price** $	**Issuance of Partnership units** #	**Gross proceeds** $
January 15, 2018	10,382	13.50	361,174	4,876
April 16, 2018	10,447	10.70	457,788	4,898
July 16, 2018	10,529	9.72	506,143	4,920
October 15, 2018	10,620	8.74	571,255	4,993
	41,978		1,896,360	19,687

				2017
Distribution Payment Date	**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
July 17, 2017	10,259	13.23	357,887	4,735
October 16, 2017	10,324	14.81	321,985	4,769
	40,934		1,298,251	18,950

On January 15, 2019, the Partnership paid a distribution of $10.7 million to the 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 875,273 Partnership units at a price of $8.36. During the year ended December 31, 2018, a fair value adjustment of $0.3 million was recorded to reflect the market value of the Partnership units issued.

Subsequent to Deceember 31, 2018, the Partnership declared a distribution of $10.9 million, payable on April 15, 2019.

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

				2018
	Advances received $	**Advances paid** $	**Partnership unit distibutions** $	**Total** $
Paid to (received from) Kruger Inc. [(a)]	(3,759)	1,436	17,648	15,325
Paid to KPGP	-	-	3	3
Paid to (received from) KPT [(b)]	(736)	274	4,640	4,178
Total paid (received)	(4,495)	1,710	22,291	19,506

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

				2017
	Tax Distributions $	**Advances paid** $	**Partnership unit distibutions** $	**Total** $
Paid to Kruger Inc. [(a)]	2,665	5,377	17,175	25,217
Paid to KPGP	-	-	3	3
Paid to KPT [(b)]	481	1,040	4,806	6,327
Total paid	3,146	6,417	21,984	31,547

(a) During the years ended December 31, 2018 and December 31, 2017, Partnership unit distributions were paid to Kruger Inc. net of the DRIP reinvestment. During the year ended December 31, 2018, Kruger Inc.'s DRIP reinvestment was $17.6 million (2017 - $17.2 million).

(b) During the years ended December 31, 2018 and December 31, 2017, Partnership unit distributions were paid to KPT net of the DRIP reinvestment. During the year ended December 31, 2018, KPT's DRIP reinvestment was $2.0 million (2017 - $1.8 million).

Tax Distributions

On February 28, 2018, the Partnership declared a Tax Distribution of $1.9 million, of which $0.3 million was used to partially settle the advance to KPT recorded during the year ended December 31, 2017, and $1.6 million was used to partially settle the advances to Kruger Inc. and KPGP recorded during the year ended December 31, 2017. The excess advances over the Tax Distributions in the amount of $4.5 million were repaid by KPT in the amount of $0.7 million, and by Kruger Inc. and KPGP in the amount of $3.8 million.

Pursuant to the Tax Distribution as defined in the Partnership Agreement, the Partnership would typically declare a Tax Distribution on February 28, 2019, related to taxes owing resulting from the taxable income of KPT for the year ended December 31, 2018. However, KPT incurred a loss for tax purposes for the year ended December 31, 2018 and as a result no Tax Distribution was declared on February 28, 2019. The excess advances over the Tax Distribution in the amount of $1.7 million, of which $0.3 million was used to pay the monthly tax instalment on behalf of KPT and the remaining was advanced to Kruger Inc. and KPGP, are repayable by the partners and due to the Partnership on or before March 31, 2020. The advances are non-interest bearing and non-recourse in nature and will be settled when the Tax Distribution is declared annually.

15 Income taxes

The Partnership is not a tax paying entity for the years ended December 31, 2018 and December 31, 2017. The income (loss) from the Partnership flows to the partners, Kruger Inc., KPGP, and KPT. However, the Partnership's subsidiaries KP USA, KTG, TAD Canco Inc., GTM, TAD Luxembourg S.A.R.L, KP TAD Holdco Inc., TAD1 Canco I Inc., TAD1 Canco II Inc., TAD1 GP ULC, TAD2 GP ULC, and KPSI are corporate entities and, therefore, are subject to tax.

The consolidated income tax recovery for the Partnership of $3.2 million for the year ended December 31, 2018 (2017 – income tax expense of $12.8) related to KP USA, KTG, TAD Luxembourg S.A.R.L and GTM.

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

The components of income taxes were as follows:

	2018	2017
	$	$
Current tax expense	2,220	2,346
Deferred tax expense (recovery)	(5,394)	10,492
	(3,174)	12,838

Details of the provision for income taxes and the reconciliation of the consolidated Canadian federal and provincial statutory income tax rates to the effective tax rate on earnings were as follows:

	2018		2017	
	$	%	$	%
Combined federal and provincial income tax rates after manufacturing and processing credits	11,149	26.4	7,361	26.2
Income tax in partners' hands	(15,771)	(37.3)	(4,917)	(17.5)
Difference in statutory income tax rate of foreign operations	(121)	(0.3)	906	3.2
U.S. State tax credits not recognized	1,210	2.9	2,756	9.8
Change in U.S. tax rates	-	-	6,205	22.1
Permanent and other	359	0.8	527	1.9
	(3,174)	(7.5)	12,838	45.7

Components of the deferred income tax asset (liability) were as follows:

	December 31, 2018	December 31, 2017
	$	$
Property, plant and equipment	(63,398)	(53,509)
Net operating losses	69,311	56,340
Long term debt and deferred financing charges	10,899	7,208
Inventory and accrued liabilities	2,963	2,238
U.S. State tax credits	11,218	11,978
Other	2,447	1,837
	33,440	26,092

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

The analysis of the deferred tax assets and (liabilities) was as follows:

	December 31, 2018	December 31, 2017
	$	$
Deferred tax asset to be recovered within 12 months	2,963	2,238
Deferred tax asset to be recovered after 12 months	30,477	23,854
	33,440	26,092

In addition to the above, the Partnership has deferred tax assets of $43.1 million related to net operating loss carry-forwards and $9.7 million related to U.S. State tax credits which have not been recognized in the consolidated financial statements.

The Partnership had the following net operating loss carry-forwards available as of December 31, 2018:

	U.S. Federal		U.S. State		Canada	
	$	Expiry date	$	Expiry date	$	Expiry date
	-		2,053	2019	-	
	-		450	2020	-	
	-		6,418	2021	-	
	-		143	2022	-	
	-		225	2023	-	
2003	6	2023	60	2026	-	
2004	5,477	2024	5,633	2027	-	
2005	28	2025	62,374	2028	-	
2006	6,047	2026	66,133	2029	-	
2009	1,663	2029	39,359	2030	-	
2011	652	2031	32,083	2031	1,255	2031
2012	2,889	2032	14,616	2032	11,624	2032
2013	60,892	2033	25,971	2033	24,007	2033
2014	66,972	2034	1,210	2034	25,226	2034
2015	38,872	2035	1,138	2035	24,397	2035
2016	31,470	2036	905	2036	26,238	2036
2017	17,577	2037	416	2037	25,952	2037
2018	32,412		657	2038	24,850	2038
	264,957		259,844		163,549	

The Partnership had the following U.S. State tax credits available for carry-forward as of December 31, 2018:

	U.S. State	
	$	Expiry date
2012	1,151	2027
2013	14,174	2028
2014	1,850	2029
2015	1,725	2030
2016	1,970	2031
	20,870	

These credits are available to reduce future Tennessee excise tax and franchise tax otherwise payable by its subsidiary, KTG.

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

16 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 year ended December 31, 2018 were $0.5 million (2017 - $1.0 million). Sales of goods to subsidiaries of Kruger Inc. for the year ended December 31, 2018 were $0.2 million (2017 – $0.2 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 year ended December 31, 2018 were $7.3 million (2017 - $7.3 million). Purchases of goods and services from subsidiaries of Kruger Inc. for the year ended December 31, 2018 were $34.5 million (2017 - $39.3 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 consolidated statement of comprehensive income (loss). During the year ended December 31, 2018, management fees of $4.3 million (2017 - $4.3 million) were paid to Kruger Inc. for management services provided to the Partnership.

Balances due to and from related parties were as follows:

	December 31, 2018 $	December 31, 2017 $
Receivables from Kruger Inc.	157	33
Receivables from subsidiaries of Kruger Inc.	15	-
Receivables from KPT	-	52
	172	85
Payables to Kruger Inc.	2,785	999
Payables to subsidiaries of Kruger Inc.	2,566	1,597
Payables to KPT	269	-
	5,620	2,596

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 December 31, 2018 and December 31, 2017. There were no loans outstanding with related parties as of December 31, 2018 and December 31, 2017.

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

	December 31, 2018 $	December 31, 2017 $
Distribution payable to Kruger Inc.	9,028	8,723
Distribution payable to KPGP	1	1
Distribution payable to KPT	1,694	1,658
Total distribution payable	10,723	10,382

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

17 Commitments and contingencies

Non-cancellable operating lease commitments related to land, buildings, vehicles and other machinery and equipment were as follows:

	December 31, 2018 $	December 31, 2017 $
Less than 1 year	20,289	14,631
Between 1 and 5 years	49,169	41,127
More than 5 years	22,264	32,866
	91,722	88,624

Operating lease expense recognized in the consolidated statement of comprehensive income (loss) during the year ended December 31, 2018 was $18.6 million (2017 - $15.1 million).

As of December 31, 2018, the Partnership had commitments under service contracts of $5.5 million for 2019, $3.6 million for 2020, and $0.6 million for 2021 and beyond.

From time to time, the Partnership is involved in various litigation matters arising in the ordinary course of its business. The Partnership has no reason to believe the disposition of any such current matter could reasonably be expected to have a material adverse impact on the Partnership's financial position, results of operations or its ability to carry on any of its business activities.

As of December 31, 2018, the Partnership had irrevocable letters of credit outstanding of $21.3 million (December 31, 2017 - $25.9 million), which included letters of credit for the pension plans disclosed in note 10.

As of December 31, 2018, the Partnership had foreign exchange swaps outstanding of nil (December 31, 2017 – $31.5 million) and foreign exchange forwards outstanding of nil (December 31, 2017 – $19.0 million).

18 Expense by nature

	2018 $	2017 $
Materials and production costs	697,720	590,481
Salaries, wages and other employee benefit expenses	289,031	280,134
Energy costs	60,370	59,832
Depreciation and amortization	52,369	52,381
Freight and warehousing	170,580	151,349
Marketing, selling and administrative expenses	51,064	53,985
	1,321,134	1,188,162

Classified in the consolidated statement of comprehensive income (loss) were:

	2018	2017
	$	$
Cost of sales	1,233,479	1,098,086
SG&A expenses	87,655	90,076
	1,321,134	1,188,162

19 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, 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.

(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 and sales of recycled fibre primarily to its parent company. It also includes certain corporate costs.

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, (x) change in fair value of derivatives, and (xi) 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 respective 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.

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

	Consumer $	AFH $	Other $	2018 Total $
Revenue from external customers	1,124,553	231,087	14,792	1,370,432
Segment Adjusted EBITDA	119,643	(12,844)	(4,510)	102,289
Depreciation and amortization				52,369
Interest expense				48,059
Change in amortized cost of Partnership units liability				(41,857)
Change in fair value of derivatives				(364)
Loss on sale of property, plant and equipment				622
Gain on sale of non-financial assets				(204)
Restructuring costs, net				1
Foreign exchange loss				1,431
Income before income taxes				42,232
Income taxes				(3,174)
Net income				45,406

	Consumer $	AFH $	Other $	2017 Total $
Revenue from external customers	1,040,428	233,321	6,265	1,280,014
Segment Adjusted EBITDA	138,158	6,235	(163)	144,230
Depreciation and amortization				52,381
Interest expense				42,021
Change in amortized cost of Partnership units liability				23,013
Change in fair value of derivatives				364
Gain on sale of property, plant and equipment				(3)
Gain on sale of non-financial assets				(75)
Restructuring costs, net				(180)
Foreign exchange gain				(1,387)
Income before income taxes				28,096
Income taxes				12,838
Net income				15,258

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.

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

				2018
	Canada	**US**	**Mexico**	**Total**
	$	**$**	**$**	**$**
Revenue	803,565	479,364	87,503	1,370,432
Property, plant and equipment	405,741	380,258	23	786,022
Goodwill	160,939	-	-	160,939
Intangible assets	14,924	-	-	14,924

				2017
	Canada	**US**	**Mexico**	**Total**
	$	**$**	**$**	**$**
Revenue	774,587	452,837	52,590	1,280,014
Property, plant and equipment	397,133	364,435	42	761,610
Goodwill	160,939	-	-	160,939
Intangible assets	15,327	-	-	15,327

20 Compensation of key management

	2018	**2017**
	$	**$**
Compensation awarded to key management included:		
Salaries and other employee benefits	5,886	5,802
Post-employment benefits	815	538
	6,701	6,340

Key management includes the Partnership's senior executives.

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

21 Financial instruments

Classification of financial instruments

As of December 31, 2018, the classification of the financial instruments, as well as their carrying amounts and fair values, was as follows:

	Classification	Carrying amount $	Fair Value $
Cash and cash equivalents	financial assets at amortized cost	169,884	169,884
Trade and other receivables	financial assets at amortized cost	127,633	127,633
Receivables from related parties	financial assets at amortized cost	172	172
Advances to partners	financial assets at amortized cost	1,704	1,704
Embedded derivative	embedded derivative at fair value through profit and loss	10	10
Trade payables	financial liabilities at amortized cost	(136,650)	(136,650)
Accrued expenses	financial liabilities at amortized cost	(59,207)	(59,207)
Contract liabilities	financial liabilities at amortized cost	(42,999)	(42,999)
Payables to related parties	financial liabilities at amortized cost	(5,620)	(5,620)
Distributions payable	financial liabilities at amortized cost	(10,723)	(10,723)
Long-term debt	financial liabilities at amortized cost	(577,894)	(597,220)
Partnership units liability	financial liabilities at amortized cost	(116,524)	(116,524)

The following table details the fair value hierarchy of financial instruments by level as of December 31, 2018:

	Level 1 $	Level 2 $	Level 3 $	Total $
Embedded derivative	-	10	-	10
Long-term debt	-	(597,220)	-	(597,220)
Partnership units liability	-	-	(116,524)	(116,524)

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

As of December 31, 2017, the classification of the financial instruments, as well as their carrying amounts and fair values, was as follows:

	Classification	Carrying amount $	Fair Value $
Cash and cash equivalents	loans and receviables at amortized cost	8,837	8,837
Trade and other receivables	loans and receviables at amortized cost	113,194	113,194
Receivables from related parties	loans and receviables at amortized cost	85	85
Advances to partners	loans and receviables at amortized cost	6,417	6,417
Bank indebtedness	financial liabilities at amortized cost	(9,051)	(9,051)
Trade payables	financial liabilities at amortized cost	(104,558)	(104,558)
Accrued expenses	financial liabilities at amortized cost	(47,283)	(47,283)
Contract liabilities	financial liabilities at amortized cost	(38,493)	(38,493)
Derivative liabilities	financial liabilities at fair value through profit and loss	(364)	(364)
Payables to related parties	financial liabilities at amortized cost	(2,596)	(2,596)
Distributions payable	financial liabilities at amortized cost	(10,382)	(10,382)
Long-term debt	financial liabilities at amortized cost	(416,315)	(419,940)
Partnership units liability	financial liabilities at amortized cost	(160,309)	(160,309)

The following table details the fair value hierarchy of financial instruments by level as of December 31, 2017:

	Level 1 $	Level 2 $	Level 3 $	Total $
Derivative liabilities	-	(364)	-	(364)
Long-term debt	-	(419,940)	-	(419,940)
Partnership units liability	-	-	(160,309)	(160,309)

Fair value

Cash and cash equivalents, trade and other receivables, receivables from related parties, advances to partners, bank indebtedness, trade payables, accrued expenses, contract liabilities, 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 December 31, 2018, the fair values of the Senior Credit Facility, the Notes, the AgCredit Agreement, the Nordea2 Credit Facility, the Nordea Credit Facility and the Caisse Facility were $110.2 million, $125.0 million, $200.4 million, $28.6 million, $9.0 million and nil (December 31, 2017 – $182.0 million, nil, nil, nil $16.6 million and $183.9 million), respectively, which approximates the current principal amount outstanding as the interest rate approximates current market interest rates. As of December 31, 2018, the fair values of the IQ Debenture, the Quebec PM Loan and the Ontario Loan were $87.6 million, $33.0 million and $3.4 million (December 31, 2017 – nil, $34.9 million and $2.5 million), respectively, which are recorded on discounted future cash flows using market rates of 6.0%, 4.4% and 4.4% accordingly, net of the government grant recorded on the below-market rate of interest.

Management has estimated the fair value of the embedded derivative using a probability-weighted interest rate pricing method. The valuation methodology used is categorized as a Level 2 methodology.

The fair value of the derivative liabilities was based on foreign exchange rates and interest rates in the active market. The change in the fair value of the derivative liabilities based on foreign exchange rates was $0.4 million gain during the year ended December 31, 2018 (2017 – $0.4 million loss), which was recorded in the consolidated statement of comprehensive income (loss) in Other expense. The valuation methodology used was categorized as a Level 2 methodology. The change in the fair value of the derivative liabilities based on interest rates was $0.2 million loss during the year ended December 31, 2018 (2017 – nil), which was recorded in the consolidated statement of comprehensive income (loss) in Interest expense. The valuation methodology used was categorized as a Level 2 methodology.

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. Additional information is disclosed in note 4.

Objectives and policies relating to financial risk management

The Partnership's activities result in exposure to a variety of financial risks, including risks related to credit, currency, liquidity and interest rate risks.

Credit risk

Credit risk is the risk of an unexpected loss if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Partnership's financial instruments exposed to credit risk include cash and cash equivalents, trade and other receivables, receivables from related parties and advances to partners. The Partnership places its cash and cash equivalents with financial institutions of high creditworthiness.

The Partnership sells its products to a variety of customers under certain credit terms and therefore is exposed to credit risks. Normal trade receivables are due in 30 days from the invoice date and amounts in excess of 90 days past the invoice date are considered delinquent. The Partnership routinely assesses the financial strength of its customers and mitigates against identified exposure primarily by lowering credit limits with high risk accounts. The customers of the Partnership are well established companies and accordingly, the Partnership has experienced limited financial loss with respect to credit risk. As a result, the Partnership believes its exposure to credit risk is limited.

On November 16, 2018, the Partnership entered into a factoring arrangement with the Bank of Nova Scotia, pursuant to a Receivables Purchase Agreement. As a result, the Partnership sells to the Bank of Nova Scotia eligible trade receivables owing by certain key customers with a facility limit of $50 million. Eligible trade receivables are sold on a non-recourse basis. The Partnership receives 95% of customer invoices sold net of a dilution factor. The dilution factor is an estimate of rebates accrued for each customer in respect of the customer invoice. The Partnership is restricted from selling or pledging these trade receivables. The factoring arrangement bears interest at a floating interest rate based on CDOR plus applicable margin. The Partnership is committed to a two year term, renewable for additional one year periods. As eligible trade receivables are sold, the Partnership removes the factored receivables from the Consolidated Statement of Financial Position, recognizes the proceeds received as consideration for the transfer and records a loss on factoring, which is included in interest expense in the Consolidated Statement of Comprehensive Income (Loss). Cash flows from the factoring arrangement are presented as operating activities in the Consolidated Statement of Cash Flows. During the year ended December 31, 2018, the gross amount of eligible trade receivables sold to the Bank of Nova Scotia was $141.9 million. The Partnership sold 95% of these trade receivables, net of a dilution factor, for $87.1 million. As of December 31, 2018, the trade receivables sold and uncollected amounted to $30.9 million.

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

	December 31, 2018	December 31, 2017
	$	$
Trade receivables	104,160	102,803
Less: Allowance for expected credit losses	(322)	(303)
Total trade receivables, net	103,838	102,500
Trade receivables, net		
0 to 60 days	100,284	101,546
61 to 90 days	2,466	728
Over 90 days	1,410	529
Less: Allowance for expected credit losses	(322)	(303)
	103,838	102,500

Currency risk

Currency risk is the risk the Partnership's earnings may fluctuate due to changes in Canadian to U.S. dollar exchange rates.

The Partnership sells certain of its products in U.S. dollars at prevailing U.S. dollar prices. A majority of the currency exposure is naturally offset by U.S. dollar expenses and the U.S. dollar denominated debt.

From time to time, the Partnership uses derivative financial instruments to manage foreign currency risk. Foreign exchange swaps and foreign exchange forwards are used to manage U.S. dollar borrowings. As of December 31, 2018, the Partnership had foreign exchange swaps outstanding of nil (December 31, 2017 – $31.5 million) and foreign exchange forwards outstanding of nil (December 31, 2017 – $19.0 million).

As of December 31, 2018, the Partnership had net liabilities denominated in U.S. dollars of $16.0 million (December 31, 2017 - $23.2 million). Assuming the Canadian dollar strengthened (weakened) by 5% against the U.S. dollar, with all other variables held constant, the hypothetical result on income before income taxes for the year ended December 31, 2018 would have been an increase/decrease of $0.8 million (2017 - $1.2 million).

Liquidity risk

The purpose of liquidity risk management is to maintain sufficient cash and cash equivalents and to ensure the Partnership has sufficient authorized credit facilities to finance operations. The Partnership had unused lines of credit available of $68.5 million as of December 31, 2018 (December 31, 2017 - $83.0 million). The Partnership prepares projections to ensure it has sufficient funds to fulfill its obligations. The Partnership monitors the covenants on its credit facilities in the normal course of business. Refinancing risks are minimized by ensuring the Senior Credit Facility will not mature for two years. The ability to pay its obligations relies on the Partnership collecting its trade receivables in a timely manner and by maintaining sufficient cash and cash equivalents in excess of anticipated needs. The Partnership's trade and other payables of $238.9 million (December 31, 2017 - $190.7 million) are all due for payment within 12 months of the dates of the consolidated statement of financial position.

The Partnership is required to operate within certain quarterly financial covenants. To allow for greater operating flexibility and the impact of continuing high pulp prices and foreign exchange fluctuations, the Partnership is currently engaged in discussions to obtain an amendment under the Senior Credit Facility to increase the ratio of total net funded debt to EBITDA and senior secured net funded debt to EBITDA covenants during the year ended December 31, 2019. In the event the Partnership is not able to obtain the amendment it is seeking, management believes it would be in a position to adjust cash inflows and outflows to manage within the existing covenants.

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

The Partnership's contractual obligations in respect of its financial instruments comprise the following:

			December 31, 2018
	Less than 1 year	1 to 5 years	Greater than 5 years
	$	$	$
Long-term debt [(a)]	41,920	342,411	493,744
Trade and other payables	238,856		
Payables to related parties	5,620		
Distributions payable	10,723		

(a) Long-term debt includes principal repayments and an estimate of interest based on current interest rates.

			December 31, 2017
	Less than 1 year	1 to 5 years	Greater than 5 years
	$	$	$
Long-term debt [(a)]	215,546	233,285	14,064
Trade and other payables	190,698		
Payables to related parties	2,596		
Distributions payable	10,382		

(a) Long-term debt includes principal repayments and an estimate of interest based on current interest rates.

The above table excludes the Partnership units liability. Payments on the Partnership units liability are made upon the declaration of the Tax Distribution, which for 2018 was nil (2017 - $1.9 million) and paid the following February. The Partnership units liability is estimated based on expected future Tax Distributions and is an obligation that will continue into perpetuity (note 4).

Interest rate risk

The Partnership holds interest rate swaps, contracted to fix the interest rate on a notional amount of $100.0 million at December 31, 2018 (December 31, 2017 – nil). The interest rate swaps are maturing during the 3-month period ended March 2020.

As of December 31, 2018, the Partnership had variable rate debts of $109.0 million (December 31, 2017 - $181.1). These loans bear interest at a base rate of Canadian prime rate, U.S. base rate, banker's acceptance rates or LIBOR, plus a margin varying between 0.20% and 2.875%. A 1% increase/decrease in the market rate of interest would result in a decrease/increase in income before income taxes of $1.1 million for the year ended December 31, 2018 (2017 - $1.8 million).

22 Capital management

The Partnership's policy is to maintain a sufficient capital base in order to maintain a strong statement of financial position and otherwise meet financial tests for the credit facilities.

Capital comprises net debt (long-term debt and bank indebtedness, less cash and cash equivalents) and equity (including the Partnership units classified as a liability). The Partnership monitors externally imposed debt covenants as established pursuant to its credit facility agreements. The requirements include a quarterly debt to EBITDA ratio and EBITDA to interest expense coverage ratio (as defined in the Senior Credit Agreement).

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

23 Environmental costs

The Partnership is subject to extensive regulation by various federal and provincial agencies concerning compliance with environmental control statutes and regulations. These regulations impose limitations on the discharge of materials into the environment and require the Partnership to operate in compliance with the conditions of permits and other governmental authorizations. Future environmental expenditures will depend on the emergence of new regulations and technological developments.

24 Economic dependence

The Partnership manufactures, distributes and sells a wide range of disposable tissue paper and related products primarily in Canada and the U.S. As of December 31, 2018, the Partnership had two major customers which represented 33.6% (2017 – 30.8%) of total revenues, and of these customers, one represented 21.5% (2017 – 19.2%) of the total revenues.

A portion of the trade receivables for these two customers are subject to a factoring arrangement with the Bank of Nova Scotia. The Partnership sells eligible accounts receivable owing by certain key customers through the factoring arrangement up to a facility limit of $50.0 million. As a result, credit risk is partially mitigated.

25 Cash and cash equivalents

	December 31, 2018 $	December 31, 2017 $
Cash and cash equivalents	169,884	8,837
Bank indebtedness	-	(9,051)
Cash and cash equivalents in the consolidated statement of cash flows	169,884	(214)

26 Non-cash working capital

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

	2018 $	2017 $
Decrease (increase) in trade and other receivables	(6,373)	1,217
Decrease (increase) in receivables from related parties	(87)	100
Increase in inventories	(11,049)	(22,650)
Decrease (increase) in prepaid expenses	957	(1,334)
Increase in other long-term assets	-	(256)
Decrease in income taxes	785	987
Increase (decrease) in trade and other payables	39,711	(12,248)
Increase (decrease) in payables to related parties	3,024	(1,010)
	26,968	(35,194)

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

27 Cash flows from (used in) financing activities

The change in financing activities on the unaudited condensed consolidated statement of cash flows comprised the following:

	Advances to partners $	Prepaid interest $	Accrued interest $	Distributions payable $	Long-term debt $	Partnership units $	Total $
As of January 1, 2017	(5,465)	(1,149)	755	10,148	424,238	336,576	765,103
Proceeds from long-term debt	-	-	-	-	28,834	-	28,834
Repayment of long-term debt	-	-	-	-	(26,039)	-	(26,039)
Payment of deferred financing fees	-	-	-	-	(12)	-	(12)
Interest paid on long-term debt	-	(6,519)	(26,582)	-	-	-	(33,101)
Distributions and advances paid, net	(9,563)	-	-	(40,934)	-	18,950	(31,547)
Interest expense on long-term debt	-	7,045	26,949	-	2,905	-	36,899
Foreign exchange	-	-	(311)	-	(13,611)	-	(13,922)
Distributions declared	-	-	-	41,168	-	-	41,168
Tax Distributions declared	8,611	-	-	-	-	-	8,611
Fair value adjustment	-	-	-	-	-	714	714
As of December 31, 2017	(6,417)	(623)	811	10,382	416,315	356,240	776,708
As of January 1, 2018	(6,417)	(623)	811	10,382	416,315	356,240	776,708
Proceeds from long-term debt	-	-	-	-	484,755	-	484,755
Repayment of long-term debt	-	-	-	-	(326,900)	-	(326,900)
Payment of deferred financing fees	-	-	-	-	(18,489)	-	(18,489)
Interest paid on long-term debt	-	(6,100)	(27,321)	-	(930)	-	(34,351)
Distributions and advances (paid) received, net	2,785	-	-	(41,978)	-	19,687	(19,506)
Interest expense on long-term debt	-	6,315	29,521	-	6,222	-	42,058
Foreign exchange	-	-	(659)	-	16,921	-	16,262
Distributions declared	-	-	-	42,319	-	-	42,319
Tax Distributions declared	1,928	-	-	-	-	-	1,928
Fair value adjustment	-	-	-	-	-	347	347
As of December 31, 2018	(1,704)	(408)	2,352	10,723	577,894	376,274	965,131