CANFOR PULP INCOME FUND

CANFOR PULP LIMITED PARTNERSHIP

Unaudited Interim Consolidated Financial Statements

For the three and nine months ended September 30, 2009

Canfor Pulp Income Fund
Consolidated Statements of Income, Comprehensive Income and Accumulated Earnings and Distributions

(thousands of dollars, except unit and per unit amounts, unaudited)	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Income				
Equity income (loss) in Canfor Pulp Limited Partnership	**$ 9,098**	$ 5,513	**$ (918)**	$ 36,226
Net income (loss) before future income taxes	**9,098**	5,513	**$ (918)**	$ 36,226
Future income taxes (recovery) (note 6)	**601**	305	**(3,081)**	2,336
Net income	**8,497**	5,208	**2,163**	33,890
Distributions declared (note 4)	**(1,065)**	(12,778)	**(4,260)**	(38,333)
Earnings in excess of distributions – surplus (deficit)	**$ 7,432**	$ (7,570)	**$ (2,097)**	$ (4,443)
Net income per unit, basic and diluted	**$ 0.24**	$ 0.15	**$ 0.06**	$ 0.95
Weighted average number of units	**35,493,505**	35,493,505	**35,493,505**	35,493,517

	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Net income for the period	**$ 8,497**	5,208	**2,163**	33,890
Equity interest in other comprehensive income (loss) of Canfor Pulp Limited Partnership	**14**	(104)	**(15)**	(284)
Comprehensive income	**$ 8,511**	$ 5,104	**$ 2,148**	$ 33,606

Accumulated Earnings and Distributions				
Balance, beginning of period – distributions in excess of earnings	**$ (82,392)**	$ (41,669)	**$ (72,863)**	$ (44,796)
Earnings in excess of distributions – surplus (deficit), current period	**$ 7,432**	$ (7,570)	**$ (2,097)**	$ (4,443)
Balance, end of period – Accumulated distributions in excess of earnings	**$ (74,960)**	$ (49,239)	**$ (74,960)**	$ (49,239)

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

Canfor Pulp Income Fund
Consolidated Statements of Cash Flows

(thousands of dollars, unaudited)	Three months ended **September 30, 2009**	Three months ended September 30, 2008	Nine months ended **September 30, 2009**	Nine months ended September 30, 2008
Cash generated from (used in)				
Operating activities				
Net income	**$ 8,497**	$ 5,208	**$ 2,163**	$ 33,890
Items not affecting cash:				
Equity (income) loss in Canfor Pulp Limited Partnership	**(9,098)**	(5,513)	**918**	(36,226)
Future income taxes (recovery)	**601**	305	**(3,081)**	2,336
Distributions received from Canfor Pulp Limited Partnership	**1,065**	12,778	**5,324**	38,333
	1,065	12,778	**5,324**	38,333
Financing activities				
Distributions paid to Unitholders	**$ (1,065)**	$ (12,778)	**$ (5,324)**	$ (38,333)
Beginning, change and ending balance in cash and cash equivalents	**$ -**	$ -	**$ -**	$ -

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

Canfor Pulp Income Fund
Consolidated Balance Sheets

(thousands of dollars, unaudited)		**As at September 30, 2009**		As at December 31, 2008
ASSETS				
Current assets				
Distributions receivable from Canfor Pulp Limited Partnership (notes 4,5)	$	**355**	$	1,420
Total current assets		**355**		1,420
Equity investment in Canfor Pulp Limited Partnership (note 3)		**261,081**		266,274
	$	**261,436**	$	267,694
LIABILITIES				
Current liabilities				
Distributions payable (note 4)	$	**355**	$	1,420
Total current liabilities		**355**		1,420
Future income taxes (note 6)		**36,628**		39,709
	$	**36,983**	$	41,129
UNITHOLDERS' EQUITY				
Unitholders' equity – 35,493,505 Fund units outstanding	$	**299,351**	$	299,351
Accumulated earnings and distributions		**(74,960)**		(72,863)
Accumulated other comprehensive income (note 7)		**62**		77
Total Unitholders' Equity		**224,453**		226,565
	$	**261,436**	$	267,694

Description of the fund and basis of presentation of financial statements (note 1).

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

Approved by the Trustees

"Stan Bracken-Horrocks" *"Charles Jago"*

Stan Bracken-Horrocks Charles Jago

Canfor Pulp Income Fund

Notes to the Unaudited Interim Consolidated Financial Statements as at September 30, 2009

1. Description of the Fund and Basis of Presentation of Financial Statements

Canfor Pulp Income Fund (the Fund) is an unincorporated open-ended trust established under the laws of Ontario on April 21, 2006, pursuant to the Fund Declaration. The principal head office of the Fund is located at 1700 West 75th Avenue, Vancouver, BC, Canada. The Fund has been established to acquire and hold, through a wholly owned trust, the Canfor Pulp Trust (the Trust), investments in the Limited Partnership Units of the Canfor Pulp Limited Partnership (the Partnership), and such other investments as the Trustees of the Fund may determine. The general partner of the Partnership is Canfor Pulp Holding Inc. (the General Partner) and each partner holds an ownership interest in the General Partner equal to its Partnership interest.

Each unitholder participates pro-rata in any distributions from the Fund.

The Fund is entirely dependent on distributions from the Partnership to make its own distributions.

2. Significant Accounting Policies

These unaudited interim consolidated financial statements do not include all of the disclosures required by Canadian generally accepted accounting principles for annual financial statements and, accordingly, should be read in conjunction with the audited consolidated financial statements and notes included in the Fund's 2008 Annual Report available at www.canforpulp.com or www.sedar.com. These unaudited interim consolidated financial statements follow the same accounting policies and methods of computation as used in the 2008 audited consolidated financial statements.

3. Equity Investment in Canfor Pulp Limited Partnership

The Fund's equity investment in the Partnership is as follows:

(thousands of dollars, unaudited)	**Nine months ended September 30, 2009**	Year ended December 31, 2008
Balance, beginning of period	**266,274**	291,458
Equity interest in income (loss) of the Partnership	**(918)**	23,280
Equity interest in other comprehensive loss of the Partnership	**(15)**	(193)
Distributions from the Partnership	**(4,260)**	(48,271)
Balance, end of period	**261,081**	266,274

4. Distributions

The Fund declared distributions during the first nine months of 2009 as follows:

(thousands of dollars, except per unit amounts, unaudited)

Record Date	**Payable Date**	**Amount per Fund Unit $**	**Amount $**
January 30, 2009	February 13, 2009	0.04	1,420
February 27, 2009	March 13, 2009	0.01	355
March 31, 2009	April 15, 2009	0.01	355
April 30, 2009	May 15, 2009	0.01	355
May 29, 2009	June 15, 2009	0.01	355
June 30, 2009	July 15, 2009	0.01	355
July 31, 2009	August 14, 2009	0.01	355
August 31, 2009	September 15, 2009	0.01	355
September 30, 2009	October 15, 2009	0.01	355
		0.12	4,260

The Fund's monthly distributions are based on the Partnership's monthly distributions.

Monthly cash distributions from the Partnership are based on the Partnership's cash flow and are not directly equal to the Fund's pro-rata share of the Partnership's income under the equity method.

5. Related Party Transactions

All accounting, treasury, legal and administrative functions for the Fund are performed on its behalf, without charge, by the Partnership pursuant to a support agreement. Distributions earned from the Partnership for the three months ended September 30, 2009 were $1.1 million of which $0.7 million was received, with the balance of $0.4 million receivable on September 30, 2009.

6. Future Income Taxes

The following table reconciles the income tax expense calculated using statutory tax rates to the actual income tax expense.

(thousands of dollars, unaudited)	**Nine months ended September 30, 2009**	Year ended December 31, 2008
Expected income tax expense at statutory tax rate of nil (2008 – nil)	**-**	-
Future income taxes (recovery) on temporary differences	**(3,081)**	3,076
	(3,081)	3,076

The temporary differences based on the Fund's 49.8% ownership of the Partnership are as follows:

(thousands of dollars, unaudited)	**September 30, 2009**	December 31, 2008
Future income tax liability:		
Equity investment in the Partnership	**43,476**	44,453
Expected reversal of temporary differences prior to 2011	**(6,848)**	(4,744)
	36,628	39,709

In 2009 a future income tax recovery of $3.7 million was recorded as a result of a change in legislation impacting future taxation rates for Specified Investment Flow Through Trusts.

The future income tax liability is based on a current estimate of the balance at the beginning of 2011. The balance relates to the Fund's 49.8% ownership in the Partnership and is based on temporary differences between the accounting and tax basis of the Partnership's assets and liabilities expected to reverse after January 1, 2011.

7. Accumulated Other Comprehensive Income

(thousands of dollars, unaudited)	**Nine months ended September 30, 2009**	Year ended December 31, 2008
Balance, beginning of period	**77**	270
Other comprehensive loss	**(15)**	(193)
Balance, end of period	**62**	77

8. Financial Instruments

The Fund's financial instruments consist of distributions receivable from the Partnership and distributions payable to unitholders. Distributions receivable are classified as loans and receivables, and are measured at amortized cost. Distributions payable are classified as other liabilities and are measured at amortized cost. The carrying values of these financial instruments approximate their fair values due to the relatively short period to maturity of these instruments.

The Fund is exposed to certain risks related to the nature of its investment in the Partnership and the structure of the Fund, as well as the underlying risks related to the business of the Partnership. The Fund relies on the objectives, policies and processes of the Partnership for managing these risks.

9. Segmented Information

The Fund operates in one industry segment, namely investing in pulp and paper producing assets in one geographic region, Canada.

Canfor Pulp Limited Partnership

Consolidated Statements of Income (Loss), Comprehensive Income (Loss) and Partners' Equity

(millions of dollars, except units and per unit amounts, unaudited)	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Revenue				
Sales	**$ 202.0**	$ 215.4	**$ 593.3**	$ 639.4
Business interruption insurance	**-**	3.5	**3.2**	18.2
	202.0	218.9	**596.5**	657.6
Costs and expenses				
Manufacturing and product costs	**140.3**	143.6	**452.4**	451.5
Freight and other distribution costs	**30.6**	29.8	**91.5**	82.3
Amortization	**12.6**	13.2	**36.8**	36.8
Selling and administration costs	**6.1**	5.7	**18.2**	18.2
Settlement of asset retirement obligation	**-**	(0.9)	**-**	(0.9)
	189.6	191.4	**598.9**	587.9
Operating income (loss)	**12.4**	27.5	**(2.4)**	69.7
Interest expense, net	**(2.8)**	(2.1)	**(7.9)**	(5.5)
Foreign exchange gain (loss) on long-term debt	**9.9**	(5.2)	**16.7**	(7.9)
Gain (loss) on derivative financial instruments (note 12)	**3.4**	(12.7)	**(2.0)**	2.2
Foreign exchange (loss) gain on working capital	**(4.6)**	3.8	**(6.2)**	6.1
Net property damage insurance gain	**-**	-	**0.2**	8.5
Other expense	**-**	(0.2)	**(0.2)**	(0.3)
	5.9	(16.4)	**0.6**	3.1
Net income (loss)	**18.3**	11.1	**(1.8)**	72.8
Other comprehensive loss				
Adjustment for derivatives (note 15)	**-**	(0.2)	**(0.1)**	(0.5)
Comprehensive income (loss)	**$ 18.3**	$ 10.9	**$ (1.9)**	$ 72.3
Net income (loss) per Partnership unit (in dollars) (note 11)				
Basic and diluted	**$ 0.26**	$ 0.15	**$ (0.02)**	$ 1.02
Weighted average Partnership units outstanding	**71,270,025**	71,270,025	**71,270,025**	71,270,025
Partners' Equity				
Balance, beginning of period	**$ 507.8**	$ 595.0	**$ 534.4**	$ 584.9
Net income (loss)	**18.3**	11.1	**(1.8)**	72.8
Distributions declared to partners (note 14)	**(2.2)**	(25.7)	**(8.6)**	(77.0)
Other comprehensive loss (note 15)	**-**	(0.2)	**(0.1)**	(0.5)
Balance, end of period	**$ 523.9**	$ 580.2	**$ 523.9**	$ 580.2

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

Canfor Pulp Limited Partnership
Consolidated Statements of Cash Flows

(millions of dollars, unaudited)	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Cash and cash equivalents generated from (used in)				
Operating activities				
Net income (loss)	**$ 18.3**	$ 11.1	**$ (1.8)**	$ 72.8
Items not affecting cash:				
Amortization	**12.6**	13.2	**36.8**	36.8
Foreign exchange (gain) loss on long-term debt	**(9.9)**	5.2	**(16.7)**	7.9
Reduction (increase) in value of outstanding derivative financial instruments (note 12)	**(4.0)**	12.7	**(1.2)**	(2.2)
Employee future benefits	**1.5**	2.0	**3.7**	6.1
Loss on disposal of fixed assets	**-**	0.7	**-**	1.2
Settlement of asset retirement obligation	**-**	(0.9)	**-**	(0.9)
Change in long-term maintenance provision	**0.8**	3.4	**2.3**	8.3
Net property damage insurance gain	**-**	-	**(0.2)**	(8.5)
Other	**0.5**	0.1	**0.5**	0.4
Asset retirement obligation expenditures	**-**	(0.3)	**-**	(1.2)
Salary pension plan contribution	**(0.5)**	(0.5)	**(1.9)**	(1.4)
Long-term maintenance expenditure	**(0.8)**	(0.2)	**(3.4)**	(7.2)
Cash flow from operations before working capital changes	**18.5**	46.5	**18.1**	112.1
Changes in non-cash working capital (note 13)	**30.6**	(19.8)	**75.6**	(28.9)
	49.1	26.7	**93.7**	83.2
Financing activities				
Distributions paid to partners	**(2.2)**	(25.7)	**(10.7)**	(77.0)
Operating loan (repayment) draw (note 8)	**(15.1)**	(0.8)	**(25.2)**	4.2
	(17.3)	(26.5)	**(35.9)**	(72.8)
Investing activities				
Property, plant and equipment, net (note 13)	**(6.2)**	(8.6)	**(14.4)**	(27.0)
Net insurance proceeds	**-**	-	**0.1**	8.0
	(6.2)	(8.6)	**(14.3)**	(19.0)
Increase (decrease) in cash and cash equivalents	**25.6**	(8.4)	**43.5**	(8.6)
Cash and cash equivalents, beginning of period	**18.3**	2.4	**0.4**	2.6
Cash and cash equivalents, end of period	**$ 43.9**	$ (6.0)	**$ 43.9**	$ (6.0)

Cash and cash equivalents include cash on hand and highly liquid investments with an original maturity date of 90 days or less net of outstanding cheques.

Supplementary cash flow information (note 13).

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

Canfor Pulp Limited Partnership
Consolidated Balance Sheets

(millions of dollars, unaudited)	**As at September 30, 2009**	As at December 31, 2008
ASSETS		
Current assets		
Cash and cash equivalents	**$ 43.9**	$ 0.4
Accounts receivable (note 10)		
Trade	**102.2**	77.0
Insurance	**-**	7.4
Other	**4.5**	7.5
Inventories (note 3)	**140.0**	176.7
Prepaid expenses and other assets	**13.5**	16.5
Total current assets	**304.1**	285.5
Property, plant and equipment (note 4)	**544.3**	570.2
Other long-term assets (note 5)	**13.5**	13.2
	$ 861.9	$ 868.9
LIABILITIES		
Current liabilities		
Operating loan (note 8)	**$ -**	$ 25.2
Accounts payable and accrued liabilities (note 10)	**166.9**	121.6
Distributions payable (note 14)	**0.7**	2.8
Total current liabilities	**167.6**	149.6
Long-term debt (note 8)	**117.9**	134.7
Long-term liabilities (note 9)	**52.5**	50.2
	$ 338.0	$ 334.5
PARTNERS' EQUITY – 14,254,005 Class A Limited Partnership Units and 57,016,020 Class B Limited Partnership Units (note 1)	**523.9**	534.4
	$ 861.9	$ 868.9

Description of the Partnership and basis of presentation of financial statements (note 1).
Contingency (note 13)
Subsequent event (note 17)
The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Approved on behalf of Canfor Pulp Limited Partnership by its
General Partner, Canfor Pulp Holding Inc.,

"Stan Bracken-Horrocks"

Stan Bracken-Horrocks
Director

"Paul Richards"

Paul Richards
Director

Canfor Pulp Limited Partnership

Notes to the Unaudited Interim Consolidated Financial Statements as at September 30, 2009

1. Business Description and Basis of Presentation

Canfor Pulp Limited Partnership (the Partnership) is a limited partnership formed on April 21, 2006, under the laws of Manitoba, to acquire and carry on the NBSK pulp and paper business of Canadian Forest Products Ltd. a subsidiary of Canfor Corporation (collectively Canfor). The business consists of two NBSK pulp mills and one NBSK pulp and paper mill located in Prince George, British Columbia and a marketing group based in Vancouver, British Columbia (the Pulp Business).

At September 30, 2009, Canfor owned 50.2% and Canfor Pulp Income Fund (the Fund) indirectly owned 49.8% of the issued and outstanding units of the Partnership.

The general partner of the Partnership is Canfor Pulp Holding Inc. (the General Partner), which holds an interest of 0.001% of the Partnership.

These unaudited interim consolidated financial statements are those of the Partnership and do not include the assets, liabilities, revenues and expenses of its partners. The Partnership, other than its incorporated subsidiaries, is not subject to income taxes as its income is allocated for tax purposes to its partners. Accordingly, no recognition has been made for income taxes related to Partnership income in these financial statements. The tax attributes of the Partnership's net assets flow directly to the partners.

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

Economic Dependence

The Partnership depends on Canfor to provide approximately 62% (2008 Year – 64%) of its fibre supply as well as to provide certain key business and administrative services as described in the Fund's 2008 Annual Report available at www.canforpulp.com or www.sedar.com. As a result of these relationships the Partnership considers its operations to be dependent on its ongoing relationship with Canfor.

2. Significant Accounting Policies

These unaudited interim consolidated financial statements do not include all of the note disclosures required by Canadian generally accepted accounting principles for annual financial statements. The Partnership's accounting policies are as disclosed in the annual consolidated financial statements of the Partnership included in the Fund's 2008 Annual Report available at www.canforpulp.com or www.sedar.com. These unaudited interim consolidated financial statements follow the same accounting policies and methods of computation as used in the 2008 audited consolidated financial statements.

3. Inventories

(millions of dollars, unaudited)	**September 30, 2009**	December 31, 2008
Pulp	**59.2**	86.7
Paper	**15.5**	20.6
Wood chips	**21.9**	23.3
Processing materials and supplies	**43.4**	46.1
	140.0	176.7

4. Property, Plant and Equipment

(millions of dollars, unaudited)	**September 30, 2009**		
	Cost	Accumulated amortization	Net
Land and improvements	**5.4**	**-**	**5.4**
Asset retirement - Landfill	**2.3**	**0.8**	**1.5**
Buildings, machinery and equipment	**1,321.8**	**793.5**	**528.3**
Construction in progress	**9.1**	**-**	**9.1**
	1,338.6	**794.3**	**544.3**

(millions of dollars, unaudited)	December 31, 2008		
	Cost	Accumulated amortization	Net
Land and improvements	5.4	-	5.4
Asset retirement - Landfill	2.3	0.8	1.5
Buildings, machinery and equipment	1,318.6	757.7	560.9
Construction in progress	2.4	-	2.4
	1,328.7	758.5	570.2

5. Other Long-term Assets

(millions of dollars, unaudited)	**September 30, 2009**	December 31, 2008
Pension benefit plan	**11.4**	11.7
Maintenance shutdown costs	**1.9**	0.9
Other	**0.2**	0.6
	13.5	13.2

6. Employee Future Benefits

The Partnership, in participation with Canfor, has funded and unfunded defined benefit plans, as well as a defined contribution plan, that provide pension, other retirement and post-employment benefits to substantially all salaried employees and for its hourly employees covered under collective agreements. The defined benefit plans are based on years of service and final average salary. The post-employment benefit plans are non-contributory and include a range of health care and other benefits.

Total employee future benefit expenses were as follows:

(millions of dollars, unaudited)	**Three months ended**		**Nine months ended**	
	September 30, 2009	September 30, 2008	**September 30, 2009**	September 30, 2008
Pension plans	**1.2**	0.9	**3.7**	2.8
Other employee future benefit plans	**0.9**	1.5	**2.6**	4.5
Contributions to forest industry union plans	**1.7**	1.7	**5.0**	5.1
	3.8	4.1	**11.3**	12.4

7. Asset Retirement Obligations

(millions of dollars, unaudited)	**September 30, 2009**	December 31, 2008
Balance beginning of period	**2.8**	11.3
Accretion expense	**0.1**	0.4
Current expenditures	**-**	(1.2)
Gain on settlement	**-**	(0.9)
Change in estimate	**-**	(6.8)
Balance end of period	**2.9**	2.8

8. Credit Facilities and Long-term Debt

At the end of the current quarter, the Partnership had cash and cash equivalents of $43.9 million. On September 30, 2009 the Partnership completed a new $40 million bank credit facility with a maturity date of November 30, 2011. In addition, the Partnership has arranged a $25 million letter of credit facility, subject to completion of legal documentation. This replaced the Partnership's previous operating credit facility of $75 million which was scheduled to mature on November 30, 2009. On September 30, 2009, utilization of the new facility consisted of $16.5 million of standby letters of credit issued to B.C. Hydro. The general terms and conditions of the new financing are similar to the previous bank credit facility, with interest and other costs at prevailing market rates. The leverage ratio and interest coverage ratio remain consistent with the financial covenants under the long-term Note agreement, which agreement was unchanged and not affected by the new bank financing.

At September 30, 2009 the Partnership has outstanding long-term debt of $117.9 million (US$110.0 million) in the form of unsecured US dollar private placement notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013.

The agreements covering the new financing facility and the long-term Notes contain financial covenants including four quarter trailing maximum allowable debt to EBITDA leverage ratio of 3.25 and minimum required EBITDA to interest coverage ratio of 2.5. The Partnership remained in compliance with all covenants at September 30, 2009.

The fair value of long-term debt at September 30, 2009 was $123.7 million (US$115.4 million).

9. Long-term Liabilities

(millions of dollars, unaudited)	**September 30, 2009**	December 31, 2008
Accrued pension obligations	**5.7**	5.9
Post-employment benefits	**42.6**	40.8
Derivative financial instruments (note 12)	**1.3**	0.7
Asset retirement obligations (note 7)	**2.9**	2.8
	52.5	50.2

10. Related Party Transactions

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2008 audited consolidated financial statements and are based on agreed upon amounts between the parties, and are summarized below:

(millions of dollars, unaudited)	Three months ended **September 30, 2009**	Three months ended September 30, 2008	Nine months ended **September 30, 2009**	Nine months ended September 30, 2008
Transactions				
Canfor	**33.8**	34.0	**89.1**	111.0
Howe Sound LP – commission	**0.7**	0.7	**1.9**	2.1
Howe Sound LP – sale of wood chips	**-**	0.1	**0.1**	0.5
Lakeland Mills Ltd. and Winton Global Lumber Ltd. – purchase of wood chips	**0.9**	1.1	**2.7**	5.1

	September 30, 2009	December 31, 2008
Balance Sheet		
Included in accounts payable and accrued liabilities:		
Canfor	**63.2**	27.4
Howe Sound LP	**37.0**	20.4
Lakeland Mills Ltd. and Winton Global Lumber Ltd.	**0.3**	0.2
Included in trade accounts receivable:		
Product marketed for Canfor	**19.7**	9.9
Product marketed for Howe Sound LP	**21.1**	16.9

Transactions and payables to Canfor include purchases of wood chips, pulp and administrative services.

11. Net Income (loss) per Partnership Unit

Basic net income (loss) per Partnership unit is based on the weighted average number of Limited Partnership units outstanding during the period. All outstanding Partnership units were issued on July 1, 2006, and there was no change in the number of outstanding Partnership units during the quarter.

12. Financial Instruments

Classification of Financial Instruments

The Partnership has classified its cash and cash equivalents as held-for-trading. Accounts receivable are classified as loans and receivables and are measured at amortized cost. Accounts payable and accrued liabilities, distributions payable, operating loan and long-term debt, including interest payable, are classified as other liabilities, all of which are measured at amortized cost. Derivative instruments are recorded in the balance sheet at fair value. The Partnership has no derivatives embedded in its financial or non-financial contracts that are not closely related to the host contract.

Financial Risk Management

The Partnership is exposed to a number of risks as a result of holding financial instruments. These risks include credit risk, liquidity risk and market risk.

Risk management is carried out by the risk management committee under a "Risk Management Controls Policy". The policy sets out the responsibilities, reporting and counter party credit and communication requirements associated with all Partnership risk management activity. Responsibility for overall philosophy, direction and approval is that of the Board of Directors.

I. Credit risk:

Credit risk is the risk of financial loss to the Partnership if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Financial instruments that potentially subject the Partnership to credit risk include cash and cash equivalents, accounts receivable and derivatives.

In order to mitigate the risk of financial loss, cash on deposit is held with major Canadian and international financial institutions. The cash and cash equivalents balance at September 30, 2009 was $43.9 million. The Partnership does not believe there is any significant credit risk associated with cash on deposit held in major Canadian and international financial institutions.

The Partnership utilizes a combination of credit insurance and self-insurance to manage the risk associated with trade receivables. Approximately 74% of the outstanding trade receivables are covered under credit insurance. In addition, the Partnership requires letters of credit on certain export trade receivables and periodically discounts these letters of credit without recourse. The Partnership recognizes the sale of the letters of credit at the settlement date, and accordingly reduces the related trade account receivable balance. At September 30, 2009, the Partnership had reduced the trade accounts receivable balance by $33.2 million due to discounting of letters of credit. The Partnership's trade receivable balance at September 30, 2009 was $102.2 million. The Partnership believes that its approach to managing credit risk associated with the collection of outstanding trade accounts receivable is appropriate in the current credit market.

The Partnership does not believe that there is any significant counter party credit risk in respect of outstanding derivatives.

II. Liquidity risk:

Liquidity risk is the risk that the Partnership will be unable to meet its financial obligations as they fall due. The Partnership manages liquidity risk through management of its capital structure in conjunction with cash flow forecasting including anticipated investing and financing activities, and use of the new revolving credit facility to meet short-term working capital requirements. On September 30, 2009 the Partnership completed a new $40 million bank credit facility with a maturity date of November 30, 2011. In addition, the Partnership has arranged a $25 million letter of credit facility, subject to completion of legal documentation.

The Partnership also actively reviews on an ongoing basis, the level of distributions, capital expenditures and timing of scheduled major maintenance outages and may adjust these amounts periodically to ensure adequate cash is available. In addition, the Partnership discounts letters of credit on outstanding trade receivables to manage liquidity risk. At September 30, 2009, the impact of discounting of letters of credit accelerated cash collection and reduced the trade accounts receivable balance by $33.2 million. The Partnership believes it will be able to meet all financial obligations as they come due.

At September 30, 2009, the Partnership accounts payable and accrued liabilities totalled $166.9 million, all of which fall due for payment within one year of the balance sheet date. The Partnership's distributions payable at September 30, 2009 totalled $0.7 million, which fall due for payment on October 15, 2009.

III. Market risk:

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in interest rates and foreign currency.

a. Interest rate risk:

The Partnership is exposed to interest rate risk though its financial assets and financial obligations bearing variable interest rates and through its operating lease obligations. The Partnership's cash and cash equivalents include term deposits with an original maturity date of 90 days or less.

Fluctuations in the market interest rates are not expected to have a material impact on the Partnership's results of operations due to the short-term nature of the respective financial assets and obligations and the fixed interest rate on long-term debt.

The Partnership currently does not use derivative instruments to reduce its exposure to interest rate risk.

b. Currency risk:

The Partnership is exposed to foreign exchange risk. The Partnership's products are sold globally with prices primarily denominated in US dollars or linked to prices quoted in US dollars with certain expenditures transacted in US dollars. In addition, the Partnership holds financial assets and liabilities in US dollars. These primarily include US dollar bank accounts and investments, trade accounts receivable and long-term debt.

The Partnership enters into US dollar forward sales contracts to reduce exposure to fluctuations in US exchange rates on US dollar denominated accounts receivable and accounts payable balances.

c. Commodity price risk:

The Partnership's financial performance is dependant on the selling price of its products and the purchase price of raw material inputs. Consequently, the Partnership is exposed to changes in commodity prices for pulp and paper, as well as changes in fibre, freight, chemical and natural gas prices. The markets for pulp and paper are cyclical and are influenced by a variety of factors. These factors include periods of excess supply due to industry capacity additions, periods of decreased demand due to weak global economic activity, inventory destocking by customers and fluctuations in currency exchange rates. During periods of low prices, the Partnership is subject to reduced revenues and margins, which adversely impact profitability.

The Partnership may periodically use derivative instruments to mitigate commodity price risk. For the quarter ended September 30, 2009 the Partnership used derivative instruments to reduce exposure to natural gas prices.

Derivative Instruments

Periodically, the Partnership uses a variety of derivative instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, pulp and natural gas prices.

For the third quarter of 2009 the Partnership recorded a gain on derivative financial instruments of $3.4 million (third quarter 2008 – loss of $12.7 million) relating to the settlement of maturing contracts during the quarter, and the revaluation to market of outstanding contracts at the end of the quarter, for natural gas swaps and foreign exchange hedging contracts.

The Partnership recorded losses of $2.5 million during the third quarter of 2009 (third quarter 2008 – gain of $0.8 million) relating to settlement of maturing natural gas contracts as a charge to non-operating income. At September 30, 2009 the Partnership had outstanding commodity swaps hedging future natural gas purchases of 2.1 million gigajoules extending to October, 2011. At September 30, 2009 the loss of $4.3 million (December 31, 2008 – $3.2 million) on these outstanding commodity swaps was recorded as a liability in accounts payable and accrued liabilities and in long-term liabilities.

The Partnership recorded a gain of $1.9 million during the third quarter of 2009 (third quarter 2008 – nil) on settlement of maturing US dollar forward sales contracts as a charge to non-operating income. At September 30, 2009 the Partnership had outstanding US dollar forward sales contracts of $57.0 million extending to December, 2009. At September 30, 2009 the gain of $1.0 million (December 31, 2008 – $1.3 million) on these outstanding US dollar forward sales contracts was recorded as an asset in other accounts receivable.

13. Supplementary Cash Flow Information

(millions of dollars, unaudited)	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Changes in non-cash working capital				
Accounts receivable – trade and other	**11.2**	16.8	**(21.1)**	21.6
Insurance receivable	**-**	(3.7)	**7.3**	(8.8)
Inventories	**(6.0)**	(17.4)	**36.8**	(33.7)
Prepaid expenses and other assets	**(0.3)**	(1.6)	**3.0**	(7.7)
Accounts payable and accrued liabilities	**25.7**	(13.9)	**49.6**	(0.3)
	30.6	(19.8)	**75.6**	(28.9)
Capital expenditures				
Capital expenditures – cash	**6.2**	8.6	**14.4**	27.0
Less property damage insurance proceeds	**-**	(5.7)	**-**	(5.7)
Net capital expenditures – cash	**6.2**	2.9	**14.4**	21.3
Capital expenditures – net accruals	**0.9**	2.8	**(3.4)**	(2.8)
	7.1	5.7	**11.0**	18.5
Net interest paid	**0.5**	0.2	**5.3**	3.7

A payment to BC Hydro totaling $4.3 million is included in capital expenditures – cash, in the third quarter of 2009. This represents a payment to reduce the Partnership's obligation for power production from the cogeneration project at the Prince George Pulp and Paper Mill. The obligation to produce power for the remainder of the term of the agreement, extending to August 2020, is reduced to 338 GWh per year from 390 GWh effective September 15, 2009.

14. Distributions

The Partnership declared distributions in the first nine months of 2009 as follows:

(millions of dollars, except per unit amounts, unaudited)

Record Date	Payable Date	Amount per Partnership Unit $	Amount $
January 30, 2009	February 13, 2009	0.04	**2.9**
February 27, 2009	March 13, 2009	0.01	**0.7**
March 31, 2009	April 15, 2009	0.01	**0.7**
April 30, 2009	May 15, 2009	0.01	**0.7**
May 29, 2009	June 15, 2009	0.01	**0.7**
June 30, 2009	July 15, 2009	0.01	**0.7**
July 31, 2009	August 14, 2009	0.01	**0.8**
August 31, 2009	September 15, 2009	0.01	**0.7**
September 30, 2009	October 15, 2009	0.01	**0.7**
		0.12	**8.6**

15. Accumulated Other Comprehensive Income

(millions of dollars, unaudited)	Nine months ended September 30, 2009	Year ended December 31, 2008
Balance, beginning of period	**0.1**	0.5
Adjustment for exchange translation	**(0.1)**	0.2
Adjustment for derivatives recorded in other comprehensive income	**-**	(0.6)
Balance, end of period	**-**	0.1

Since the inception of the Partnership, the total of the cumulative comprehensive income, less cumulative distributions is as follows:

(millions of dollars, unaudited)	**September 30, 2009**
Cumulative comprehensive income	**261.5**
Cumulative distributions	**(325.1)**
	(63.6)
Partners' capital – at July 1, 2006	**587.5**
Partners' equity, end of period	**523.9**

16. Segmented Information [a]

(millions of dollars, unaudited)	Pulp	Paper	Unallocated Costs	Total
Three months ended September 30, 2009				
Sales to external customers [b]	**170.1**	**31.9**	**-**	**202.0**
Sales of pulp to paper segment [c]	**16.2**	**(16.2)**	**-**	**-**
Operating income (loss)	**11.6**	**3.2**	**(2.4)**	**12.4**
Amortization	**11.7**	**0.8**	**0.1**	**12.6**
Capital expenditures, net	**7.1**	**-**	**-**	**7.1**
Three months ended September 30, 2008				
Sales to external customers [b]	181.7	33.7	-	215.4
Sales of pulp to paper segment [c]	21.1	(21.1)	-	-
Operating income (loss)	26.8	3.7	(3.0)	27.5
Amortization	12.2	1.0	-	13.2
Capital expenditures, net	11.2	-	0.2	11.4
Nine months ended September 30, 2009				
Sales to external customers [b]	**503.1**	**90.2**	**-**	**593.3**
Sales of pulp to paper segment [c]	**42.8**	**(42.8)**	**-**	**-**
Operating income (loss)	**(6.2)**	**10.5**	**(6.7)**	**(2.4)**
Amortization	**34.1**	**2.5**	**0.2**	**36.8**
Capital expenditures, net	**10.9**	**-**	**0.1**	**11.0**
Identifiable assets	**735.0**	**65.0**	**61.9**	**861.9**
Nine months ended September 30, 2008				
Sales to external customers [b]	536.1	103.3	-	639.4
Sales of pulp to paper segment [c]	61.4	(61.4)	-	-
Operating income (loss)	72.9	6.9	(10.1)	69.7
Amortization	33.8	2.9	0.1	36.8
Capital expenditures, net	23.5	0.4	0.3	24.2
Identifiable assets	831.8	71.9	17.1	920.8

(a) Operations are presented by product lines. Operations are considered to be in one geographic area since all production facilities are in Canada. Substantially all sales are exported outside Canada, with sales to the United States representing 36% (Year 2008 – 43%).

(b) Sales to the largest customer represented approximately 8% of pulp segment sales (Year 2008 – 22%).

(c) Sales of slush pulp to the paper segment are accounted for at approximate market value. The sales are transacted as a cost transfer and are not reflected in Pulp sales.

17. Subsequent event

On October 9, 2009 the Canadian federal government announced the allocation of credits from the billion dollar Pulp and Paper Green Transformation Program (the Program). The Partnership has been allocated $122.2 million from the Program announced by the Canadian government on June 17, 2009. The Program is designed as a reimbursement of funds to be spent on qualifying energy and environmental capital projects. Credits may be used until the program end date of March 31, 2012.