## MANAGEMENT'S RESPONSIBILITY

The information and representations in these consolidated financial statements are the responsibility of management and have been approved by the Board of Directors. The consolidated financial statements were prepared by management in accordance with International Financial Reporting Standards and, where necessary, reflect management's best estimates and judgments at this time. It is reasonably possible that circumstances may arise which cause actual results to differ. Management does not believe it is likely that any differences will be material.

Canfor Pulp Products Inc. maintains systems of internal accounting controls, policies and procedures to provide reasonable assurance as to the reliability of the financial records and the safeguarding of its assets.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board carries out these activities primarily through its Audit Committee.

The Audit Committee is comprised of three Directors who are not employees of the Company. The Committee meets periodically throughout the year with management, external auditors and internal auditors to review their respective responsibilities, results of the reviews of internal accounting controls, policies and procedures and financial reporting matters. The external and internal auditors meet separately with the Audit Committee.

The consolidated financial statements have been reviewed by the Audit Committee and approved by the Board of Directors. The consolidated financial statements have been audited by PricewaterhouseCoopers LLP, the external auditors, whose report follows.

February 4, 2015

| | |
|---|---|
| "*Don B. Kayne*" | "*Alan Nicholl*" |
| Don B. Kayne<br>Chief Executive Officer | Alan Nicholl<br>Chief Financial Officer |

## INDEPENDENT AUDITOR'S REPORT

### To the Shareholders of Canfor Pulp Products Inc.

We have audited the accompanying consolidated financial statements of Canfor Pulp Products Inc. and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2014 and December 31, 2013 and the consolidated statements of income, the consolidated statements of other comprehensive income (loss), the consolidated statements of changes in equity, and the consolidated statements of cash flows for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

### Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, 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.

### Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

### Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Canfor Pulp Products Inc. and its subsidiaries as at December 31, 2014 and December 31, 2013 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

*"PricewaterhouseCoopers LLP"*

Chartered Accountants
Vancouver, British Columbia
February 4, 2015

## Canfor Pulp Products Inc.
## Consolidated Balance Sheets

| (millions of Canadian dollars) | As at December 31, 2014 | As at December 31, 2013 |
|---|---|---|
| **ASSETS** | | |
| **Current assets** | | |
| Cash and cash equivalents | $ 76.8 | $ 13.5 |
| Accounts receivable - Trade | 60.7 | 71.0 |
| - Other | 10.0 | 10.3 |
| Inventories (Note 5) | 143.7 | 128.0 |
| Prepaid expenses and other assets | 11.2 | 7.2 |
| Total current assets | 302.4 | 230.0 |
| **Property, plant and equipment** (Note 6) | 524.1 | 528.1 |
| **Retirement benefit surplus** (Note 10) | - | 8.2 |
| **Other long-term assets** | 0.9 | 2.3 |
| **Total assets** | $ 827.4 | $ 768.6 |
| **LIABILITIES** | | |
| **Current liabilities** | | |
| Operating loans (Note 8) | $ - | $ 10.6 |
| Accounts payable and accrued liabilities (Note 7) | 123.2 | 118.4 |
| Total current liabilities | 123.2 | 129.0 |
| **Long-term debt** (Note 9) | 50.0 | 50.0 |
| **Retirement benefit obligations** (Note 10) | 94.9 | 75.8 |
| **Other long-term provisions** | 4.2 | 3.0 |
| **Deferred income taxes, net** (Note 14) | 65.5 | 72.8 |
| **Total liabilities** | $ 337.8 | $ 330.6 |
| **EQUITY** | | |
| Share capital (Note 12) | $ 522.1 | $ 523.4 |
| Retained earnings (deficit) | (32.5) | (85.4) |
| **Total equity** | $ 489.6 | $ 438.0 |
| **Total liabilities and equity** | $ 827.4 | $ 768.6 |

**Subsequent Events** (Note 21)

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

APPROVED BY THE BOARD

*"S.E. Bracken-Horrocks"*

Director, S.E. Bracken-Horrocks

*"M.J. Korenberg"*

Director, M.J. Korenberg

## Canfor Pulp Products Inc.
## Consolidated Statements of Income

| (millions of Canadian dollars, except per share data) | Year ended December 31, 2014 | 2013 |
|---|---|---|
| **Sales** | $ **980.5** | $ 886.8 |
| **Costs and expenses** | | |
| Manufacturing and product costs | **635.5** | 595.1 |
| Freight and other distribution costs | **129.1** | 123.3 |
| Amortization | **62.7** | 69.9 |
| Selling and administration costs | **27.8** | 24.0 |
| Restructuring and severance costs | **-** | 0.7 |
| | **855.1** | 813.0 |
| **Operating income** | **125.4** | 73.8 |
| Finance expense, net (Note 13) | **(5.5)** | (11.8) |
| Foreign exchange loss on long-term debt | **-** | (7.3) |
| Loss on derivative financial instruments (Note 20) | **(1.9)** | (0.1) |
| Other income, net | **2.0** | 5.2 |
| Net income before income taxes | **120.0** | 59.8 |
| Income tax expense (Note 14) | **(30.5)** | (18.0) |
| **Net income** | $ **89.5** | $ 41.8 |
| **Net income per common share:** (in Canadian dollars) | | |
| - Basic and diluted (Note 12) | $ **1.26** | $ 0.59 |

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

## Canfor Pulp Products Inc.
## Consolidated Statements of Other Comprehensive Income (Loss)

| (millions of Canadian dollars) | Year ended December 31, 2014 | 2013 |
|---|---|---|
| **Net income** | **$ 89.5** | $ 41.8 |
| **Other comprehensive income (loss)** | | |
| Items that will not be recycled through net income: | | |
| Defined benefit plan actuarial gains (losses) (Note 10) | **(25.8)** | 35.5 |
| Income tax recovery (expense) on defined benefit plan actuarial gains (losses) (Note 14) | **6.7** | (9.3) |
| Other comprehensive income (loss), net of tax | **(19.1)** | 26.2 |
| **Total comprehensive income** | **$ 70.4** | $ 68.0 |

## Consolidated Statements of Changes in Equity

| (millions of Canadian dollars) | Year ended December 31, 2014 | 2013 |
|---|---|---|
| **Share capital** | | |
| Balance at beginning of year | **$ 523.4** | $ 525.3 |
| Share purchases (Note 12) | **(1.3)** | (1.9) |
| Balance at end of year (Note 12) | **$ 522.1** | $ 523.4 |
| **Retained earnings (deficit)** | | |
| Balance at beginning of year | **$ (85.4)** | $ (138.7) |
| Net income | **89.5** | 41.8 |
| Defined benefit plan actuarial gains (losses), net of tax | **(19.1)** | 26.2 |
| Dividends declared | **(16.8)** | (14.2) |
| Share purchases (Note 12) | **(0.7)** | (0.5) |
| Balance at end of year | **$ (32.5)** | $ (85.4) |
| **Total equity** | **$ 489.6** | $ 438.0 |

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

## Canfor Pulp Products Inc.
## Consolidated Statements of Cash Flows

| (millions of Canadian dollars) | Year ended December 31, 2014 | 2013 |
|---|---|---|
| **Cash generated from (used in):** | | |
| **Operating activities** | | |
| Net income | **$ 89.5** | $ 41.8 |
| Items not affecting cash: | | |
| Amortization | **62.7** | 69.9 |
| Income tax expense | **30.5** | 18.0 |
| Changes in mark-to-market value of derivative financial instruments | **0.8** | 0.2 |
| Employee future benefits | **4.6** | 5.1 |
| Net finance expense | **5.5** | 11.8 |
| Foreign exchange loss on long-term debt | **-** | 7.3 |
| Other, net | **4.2** | (2.8) |
| Defined benefit plan contributions | **(6.1)** | (10.1) |
| Income taxes paid, net | **(24.4)** | (0.4) |
| | **167.3** | 140.8 |
| Net change in non-cash working capital (Note 15) | **(13.9)** | 16.1 |
| | **153.4** | 156.9 |
| **Financing activities** | | |
| Change in operating bank loans | **(11.2)** | 10.6 |
| Proceeds from long-term debt (Note 9) | **-** | 50.0 |
| Repayment of long-term debt | **-** | (116.6) |
| Finance expenses paid | **(2.7)** | (9.1) |
| Dividends paid | **(16.8)** | (14.2) |
| Share purchases (Note 12) | **(2.0)** | (2.4) |
| Other, net | **-** | (0.1) |
| | **(32.7)** | (81.8) |
| **Investing activities** | | |
| Additions to property, plant and equipment, net | **(57.7)** | (61.2) |
| Other, net | **0.3** | 0.8 |
| | **(57.4)** | (60.4) |
| **Increase in cash and cash equivalents*** | **63.3** | 14.7 |
| Cash and cash equivalents at beginning of year* | **13.5** | (1.2) |
| **Cash and cash equivalents at end of year*** | **$ 76.8** | $ 13.5 |

*Cash and cash equivalents include cash on hand less unpresented cheques.

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

## 1. Reporting Entity

Canfor Pulp Products Inc. ("CPPI") is a company incorporated and domiciled in Canada and listed on The Toronto Stock Exchange. The address of the Company's registered office is 100-1700 West 75th Avenue, Vancouver, British Columbia, Canada, V6P 6G2. The consolidated financial statements of the Company as at and for the year ended December 31, 2014 comprise the Company and its subsidiaries (together referred to as "CPPI" or "the Company"). The Company's operations consist of two Northern Bleached Softwood Kraft ("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").

On December 27, 2013, the Canfor Pulp Limited Partnership was wound up and the net assets were transferred to Canfor Pulp Holding Inc., a wholly owned subsidiary of CPPI. Subsequent to the transfer, Canfor Pulp Holding Inc. was renamed Canfor Pulp Ltd. At December 31, 2014, Canfor Corporation ("Canfor") held a 50.5% interest in CPPI, an increase of 0.1% from December 31, 2013 as a result of share purchases in 2014 (Note 12).

## 2. Basis of Preparation

### *Statement of compliance*

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRSs" or "IFRS") as issued by the International Accounting Standards Board ("IASB").

The consolidated financial statements were authorized for issue by the Board of Directors on February 4, 2015.

### *Basis of measurement*

The consolidated financial statements have been prepared on the historical cost basis, except for the following material items:

- Financial instruments classified as fair value through profit and loss are measured at fair value;
- Asset retirement obligations are measured at the discounted value of expected future cash flows; and
- The retirement benefit surplus and obligation related to the defined benefit pension plans is the net of the accrued benefit obligation and the fair value of the plan assets.

### *Use of estimates and judgments*

The preparation of the consolidated financial statements in accordance with IFRSs requires management to make judgments, estimates and assumptions that effect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

The Company regularly reviews its estimates and assumptions; however, it is possible that circumstances may arise which cause actual results to differ from management estimates, and these differences could be material. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about the significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the applicable notes:

- Note 10 – Employee Future Benefits; and
- Note 11 – Asset Retirement Obligations.

## 3. Significant Accounting Policies

The following accounting policies have been applied to the financial information presented.

### *Basis of consolidation*

Subsidiaries are entities controlled by the Company. Control exists when CPPI is able to govern the financial and operating activities of those other entities to generate returns for the Company. Inter-company transactions, balances and unrealized gains and losses on transactions between different entities within the Company are eliminated.

### *Business Combinations*

Business combinations are accounted for using the acquisition method as at the acquisition date. CPPI measures goodwill at the acquisition date as the fair value of the consideration transferred including any non-controlling interest less the fair value of the identifiable assets acquired and liabilities assumed. When the excess is negative, a bargain purchase gain is recognized immediately in net income. Transaction costs in connection with business combinations are expensed as incurred.

### *Cash and cash equivalents*

Cash and cash equivalents include cash in bank accounts and highly liquid money market instruments with maturities of three months or less from the date of acquisition, and are valued at cost, which approximates market value. Cash is presented net of unpresented cheques. When the amount of unpresented cheques is greater than the amount of cash, the net amount is presented as cheques issued in excess of cash on hand. Interest is earned at variable rates dependent on amount, credit quality and term of the Company's deposits.

### *Financial instruments*

*Non-derivative financial instruments*

Non-derivative financial instruments comprise investments in equity securities, trade and other receivables, cash and cash equivalents, loans and advances, and trade and other payables. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through net income, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below:

Financial assets at fair value through net income - An instrument is classified at fair value through net income if it is held for trading or is designated as such upon initial recognition. Financial instruments at fair value through net income are measured at fair value, and changes therein are recognized in the statements of income, with attributable transaction costs being recognized in net income when incurred.

Available-for-sale financial assets - Available for sale financial assets are non-derivatives that are either designated in this category or not classified in any other categories.

Loans and receivables - Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These are measured at amortized cost using the effective interest method, less any impairment losses. The effective interest method is used to spread the total costs of or income from a financial instrument over the life of the instrument. Financial assets included within this category for CPPI are trade and other receivables, and cash and cash equivalents.

Other liabilities - All of CPPI's financial liabilities are measured at amortized cost using the effective interest method.

*Derivative financial instruments*

CPPI uses derivative financial instruments in the normal course of its operations as a means to manage its foreign exchange, interest rate, pulp price, and energy price risk. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

CPPI's derivative financial instruments are not designated as hedges for accounting purposes. Consequently, such derivatives for which hedge accounting is not applied are carried on the balance sheet at fair value, with changes in fair value (realized and unrealized) being recognized in the statements of income as 'Gain (loss) on derivative financial instruments'.

The fair value of the derivatives is determined with reference to period end market trading prices for derivatives with comparable characteristics.

### *Inventories*

Inventories include pulp, paper, wood chips, logs, and materials and supplies. These are measured at the lower of cost and net realizable value. The cost of inventories is based on the weighted average cost principle, and includes raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses.

### *Property, plant and equipment*

Items of property, plant and equipment, including expenditure on major overhauls, are measured at cost less accumulated amortization and impairment losses.

Cost includes expenditures which are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, borrowing costs (as applicable), and any other costs directly attributable to bringing assets to be used in the manner intended by management.

Expenditure on major overhauls, refits or repairs is capitalized where it enhances the life or performance of an asset above its originally assessed standard of performance. Certain expenditures relating to replacement of components incurred during major maintenance are capitalized and amortized over the estimated benefit period of such expenditures. The costs of the day-to-day servicing of property, plant and equipment are recognized in net income as incurred.

The cost of replacing a major component of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to CPPI and its cost can be measured reliably. The carrying amount of the replaced component is removed.

Amortization is recognized in net income on a straight-line basis over the estimated useful lives of each component of an item of property, plant and equipment, as set out in the table below. Land is not amortized. The significant majority of CPPI's amortization expense for property, plant and equipment relates to manufacturing and product costs.

Amortization methods, useful lives and residual values are reviewed, and adjusted if appropriate, at each reporting date. The following rates have been applied to CPPI's capital assets:

| | |
|---|---|
| Buildings | 10 to 50 years |
| Pulp and paper machinery and equipment | 20 years |
| Mobile equipment | 4 years |
| Office furniture and equipment | 10 years |
| Major overhauls | 1 to 2 years |

### *Government assistance*

Government assistance relating to the acquisition of property, plant and equipment is recorded as a reduction of the cost of the asset to which it relates, with any amortization calculated on the net amount. Government grants related to income are recognized as income or a reimbursement of costs on a systematic basis over the periods necessary to match them with the related costs which they were intended to compensate.

### *Asset impairment*

CPPI's property, plant and equipment are reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognized in net income at the amount the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows that are largely independent of cash inflows from other assets or groups of assets (cash-generating units).

Non-financial assets, for which an impairment was recorded in a prior period are reviewed for possible reversal of the impairment at each reporting date. When an impairment loss is reversed, the increased carrying amount of the asset cannot exceed the carrying amount that would have been determined (net of amortization) had no impairment loss been recognized in prior years.

Financial assets are reviewed at each reporting date to determine whether there is evidence indicating they are impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative impact on estimated future cash flows from that asset. An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. All impairment losses are recognized in net income.

***Employee benefits***

*Defined contribution plans*

A defined contribution plan is a post-employment benefit plan under which an entity makes contributions to a separate entity and has no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognized as an employee benefit expense when they are earned.

For hourly employees covered by industry union defined contribution pension plans, the statements of income are charged with CPPI's contributions required under the collective agreements.

*Defined benefit plans*

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. CPPI, in participation with Canfor, has defined benefit plans that provide both pension and other retirement benefits to most of its salaried employees and certain hourly employees not covered by forest industry union plans. The Company also provides certain health care benefits and pension bridging benefits to eligible retired employees.

The surplus and obligation recognized in the balance sheet in respect of a defined benefit pension plan is the net of the accrued benefit obligation and the fair value of the plan assets. The accrued benefit obligation is calculated separately for each plan by estimating the amount of future benefit earned by employees in respect of their service in the current and prior periods; that benefit is discounted to determine its present value. The discount rate used to determine the present value of the obligation is the yield at the reporting date on high quality corporate bonds that have maturity dates approximating the terms of CPPI's obligations. The calculation is performed annually by a qualified actuary using the projected unit credit method and a measurement date of December 31. The pension surplus or obligation is adjusted on a quarterly basis for any material changes in underlying assumptions.

CPPI recognizes all actuarial gains and losses arising from defined benefit plans in other comprehensive income in the year in which they occur.

***Provisions***

CPPI recognizes a provision if, as a result of a past event, it has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. The provision recorded is management's best estimate of the expenditure required to settle the present obligation at the end of the reporting period. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The expense arising from the unwinding of the discount due to the passage of time is recorded as a finance cost. The main class of provision recognized by CPPI is as follows:

*Asset retirement obligations*

CPPI recognizes a liability for asset retirement obligations in the period in which they are incurred. The site restoration costs are capitalized as part of the cost of the related item of property, plant and equipment and amortized on a basis consistent with the expected useful life of the related asset. Asset retirement obligations are discounted at the risk-free rate in effect at the balance sheet date.

### *Revenue recognition*

CPPI's revenues are derived from the sale of pulp, paper, energy and commissions. Revenue is measured at the fair value of the consideration received or receivable net of applicable sales taxes, returns, rebates and discounts and after eliminating sales within the Company. Revenue is recognized when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible returns of the goods can be estimated reliably, there is no continuing management involvement with the goods, and the amounts of revenue can be measured reliably. Energy revenue is recognized when CPPI has met the terms and conditions under both the Electricity Purchase and Load Displacement Agreements.

Amounts charged to customers for shipping and handling are recognized as revenue, and shipping and handling costs incurred by CPPI are reported as a component of freight and other distribution costs.

### *Income taxes*

Income tax expense comprises current and deferred tax. Current and deferred tax are recognized in net income except to the extent that they relate to items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using the tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous periods.

CPPI recognizes deferred income tax in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is measured at tax rates expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred income tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Investment tax credits are credited to manufacturing and product costs in the period in which it becomes reasonably assured that the Company is entitled to them. Unused investment tax credits are recorded as other current or long-term assets in the Company's balance sheet, depending upon when the benefit is expected to be received.

### *Foreign currency translation*

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

The majority of CPPI sales are denominated in foreign currencies, principally the US dollar. Transactions in foreign currencies are translated to the functional currencies of the respective entities at exchange rates at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate on that date. Foreign currency differences arising on translation are recognized in net income.

The assets and liabilities of foreign operations are translated to the Canadian dollar at exchange rates at the reporting date. The income and expenses of foreign operations are translated to the Canadian dollar at exchange rates at the transaction dates. Foreign exchange differences are recognized in other comprehensive income.

### *Segment reporting*

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. Segment results reported to the chief operating decision-maker include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise interest bearing liabilities, head office expenses, and income tax assets and liabilities. Segment capital expenditure is the total cost incurred during the period to acquire property, plant and equipment.

## 4. Accounting Standards Issued and Not Applied

In July 2014, the IASB issued IFRS 9, *Financial Instruments*. The required adoption date for IFRS 9 is January 1, 2018 and the Company is in process of assessing the impact, if any, on the financial statements of this new standard.

In May 2014, the IASB issued IFRS 15, *Revenue from Contracts with Customers*, which will supersede IAS 18, *Revenue*, IAS 11, *Construction Contracts* and related interpretations. The new standard is effective for annual periods beginning on or after January 1, 2017. The Company is in the process of assessing the impact, if any, on the financial statements of this new standard.

## 5. Inventories

| (millions of Canadian dollars) | **As at December 31, 2014** | As at December 31, 2013 |
|---|---|---|
| Pulp | **$ 68.8** | $ 52.8 |
| Paper | **17.4** | 15.7 |
| Wood chips and logs | **12.1** | 14.1 |
| Materials and supplies | **45.4** | 45.4 |
| | **$ 143.7** | $ 128.0 |

In 2014, costs of raw materials, consumables and changes in finished products recognized as manufacturing and product costs amounted to $344.6 million (2013 - $321.8 million).

## 6. Property, Plant and Equipment

| (millions of Canadian dollars) | Land and improvements | Buildings, machinery and equipment | Asset retirement - landfill | Construction in Progress | Major Overhauls | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| Balance at January 1, 2013 | $ 5.4 | $ 1,421.5 | $ 2.1 | $ 16.0 | $ 42.5 | $ 1,487.5 |
| Additions[1] | - | - | - | 67.6 | - | 67.6 |
| Disposals | - | (8.2) | - | - | (33.4) | (41.6) |
| Transfers | - | 44.7 | - | (68.1) | 23.4 | - |
| Balance at December 31, 2013 | $ 5.4 | $ 1,458.0 | $ 2.1 | $ 15.5 | $ 32.5 | $ 1,513.5 |
| Additions[1] | - | - | - | 59.3 | - | 59.3 |
| Disposals | - | (3.6) | - | - | (7.1) | (10.7) |
| Transfers | - | 26.3 | - | (35.4) | 9.1 | - |
| Balance at December 31, 2014 | $ 5.4 | $ 1,480.7 | $ 2.1 | $ 39.4 | $ 34.5 | $ 1,562.1 |
| **Amortization** | | | | | | |
| Balance at January 1, 2013 | $ - | $ (932.5) | $ (0.9) | $ - | $ (23.3) | $ (956.7) |
| Amortization for the year | - | (48.9) | (0.1) | - | (20.9) | (69.9) |
| Disposals | - | 7.9 | - | - | 33.3 | 41.2 |
| Balance at December 31, 2013 | $ - | $ (973.5) | $ (1.0) | $ - | $ (10.9) | $ (985.4) |
| Amortization for the year | - | (47.7) | - | - | (15.0) | (62.7) |
| Disposals | - | 3.0 | - | - | 7.1 | 10.1 |
| Balance at December 31, 2014 | $ - | $ (1,018.2) | $ (1.0) | - | $ (18.8) | (1,038.0) |
| **Carrying amounts** | | | | | | |
| At January 1, 2013 | $ 5.4 | $ 489.0 | $ 1.2 | $ 16.0 | $ 19.2 | $ 530.8 |
| At December 31, 2013 | $ 5.4 | $ 484.5 | $ 1.1 | $ 15.5 | $ 21.6 | $ 528.1 |
| **At December 31, 2014** | **$ 5.4** | **$ 462.5** | **$ 1.1** | **$ 39.4** | **$ 15.7** | **$ 524.1** |

[1] Net of capital expenditures financed by government grants.

## 7. Accounts Payable and Accrued Liabilities

| (millions of Canadian dollars) | | **As at December 31, 2014** | | As at December 31, 2013 |
|---|---|---|---|---|
| Trade payables and accrued liabilities | **$** | **59.6** | $ | 58.0 |
| Accrued payroll and related liabilities | | **29.9** | | 30.0 |
| Income tax payable | | **13.7** | | 8.7 |
| Other | | **20.0** | | 21.7 |
| | **$** | **123.2** | $ | 118.4 |

## 8. Operating Loans

| (millions of Canadian dollars) | | **As at December 31, 2014** | | As at December 31, 2013 |
|---|---|---|---|---|
| Available Operating Loans: | | | | |
| Operating loan facility | **$** | **110.0** | $ | 110.0 |
| Facility for letters of credit related to energy agreements | | **20.0** | | 20.0 |
| Total operating loans | | **130.0** | | 130.0 |
| Drawn | | **-** | | (10.6) |
| Energy letters of credit | | **(12.2)** | | (12.2) |
| Total available operating loans | **$** | **117.8** | $ | 107.2 |

The terms of the Company's operating loan facility include interest payable at floating rates that vary depending on the ratio of net debt to total capitalization and is based on the lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin. The facility has certain financial covenants that stipulate maximum net debt to total capitalization ratios and minimum net worth amounts based on shareholders' equity. The maturity date of this facility is January 31, 2018.

The Company has a separate facility with a maturity date of June 30, 2015 to cover energy-related letters of credit. At December 31, 2014, $9.4 million of energy-related letters of credit were covered under this facility with the balance of $2.8 million covered under the Company's general operating loan facility.

As at December 31, 2014, the Company was in compliance with all covenants relating to its operating loans.

## 9. Long-Term Debt

On November 5, 2013, CPPI completed a $50.0 million unsecured non-revolving term debt financing, which is repayable on November 5, 2018 with no penalty for early repayment. The interest rate on the new term debt is based on the lenders' Canadian prime rate or bankers acceptance rate in the year of payment. On November 29, 2013, CPPI repaid its $116.6 million (US$110.0 million) 6.41% term debt.

As at December 31, 2014, the Company was in compliance with all covenants relating to the long-term debt.

### *Fair value of total long-term debt*

At December 31, 2014, the fair value of the Company's long-term debt approximates its amortized cost of $50.0 million (2013 - $50.0 million).

## 10. Employee Future Benefits

The Company, in participation with Canfor, has several funded and unfunded defined benefit plans, as well as defined contribution plans, that provide pension, other retirement and post-employment benefits to substantially all salaried employees and certain hourly employees. The defined benefit plans are based on years of service and final average salary. CPPI's other post-retirement benefit plans are non-contributory and include a range of health care and other benefits. Total cash payments for employee future benefits for 2014 were $14.1 million (2013 – $17.8 million), consisting of cash contributed by CPPI to its funded pension plans, cash payments directly to beneficiaries for its unfunded other benefit plans, and cash contributed to its defined contribution plans.

### ***Defined benefit plans***

CPPI measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year.

CPPI has one registered defined benefit plan for which an actuarial valuation is performed every three years. The plan underwent an actuarial valuation for funding purposes as of December 31, 2013. The next actuarial valuation for funding purposes is currently scheduled for December 31, 2016.

Information about CPPI's defined benefit plans, in aggregate, is as follows:

**Fair Market Value of Plan Assets**

| | **2014** | | 2013 | |
|---|---|---|---|---|
| (millions of Canadian dollars) | **Pension Benefit Plans** | **Other Benefit Plans** | Pension Benefit Plans | Other Benefit Plans |
| Beginning of year | **$ 105.1** | **$ -** | $ 87.3 | $ - |
| Interest income on plan assets | **4.5** | **-** | 3.9 | - |
| Return on plan assets greater than discount rate | **3.9** | **-** | 8.5 | - |
| Reallocation of assets in proportion to obligations | **(3.9)** | **-** | - | - |
| CPPI contributions | **4.6** | **1.5** | 8.3 | 1.6 |
| Employee contributions | **0.1** | **-** | 0.2 | - |
| Benefit payments | **(5.1)** | **(1.5)** | (3.0) | (1.6) |
| Administrative expenses | **(0.3)** | **-** | (0.1) | - |
| End of year | **$ 108.9** | **$ -** | $ 105.1 | $ - |

| Plan assets consist of the following: | **As at December 31, 2014** | As at December 31, 2013 |
|---|---|---|
| | Percentage of Plan Assets | |
| Asset category | | |
| Equity securities | **16%** | 60% |
| Debt securities | **83%** | 35% |
| Cash and cash equivalents | **1%** | 5% |
| | **100%** | 100% |

**Accrued Benefit Obligations**

| | **2014** | | 2013 | |
|---|---|---|---|---|
| (millions of Canadian dollars) | **Pension Benefit Plans** | **Other Benefit Plans** | Pension Benefit Plans | Other Benefit Plans |
| Beginning of year | **$ 107.6** | **$ 64.1** | $ 110.3 | $ 79.9 |
| Current service cost | **3.2** | **1.6** | 3.2 | 2.0 |
| Interest cost | **4.5** | **3.0** | 4.6 | 3.4 |
| Employee contributions | **0.1** | **-** | 0.2 | - |
| Benefit payments | **(5.1)** | **(1.5)** | (3.0) | (1.6) |
| Actuarial loss (gain) | **15.6** | **10.0** | (7.7) | (19.3) |
| Other | **-** | **(0.3)** | - | (0.3) |
| End of year | **$ 125.9** | **$ 76.9** | $ 107.6 | $ 64.1 |

Of the defined benefit plan obligation of $125.9 million (2013 - $107.6 million), $115.2 million (2013 - $98.6 million) relates to plans that are wholly or partly funded, $10.7 million (2013 - $9.0 million) relates to plans that are wholly unfunded. At December 31, 2014 the total obligation for the other benefit plans of $76.9 million (2013 - $64.1 million) is unfunded.

**Reconciliation of Funded Status of Benefit Plans to Amounts Recorded in the Financial Statements**

| (millions of Canadian dollars) | December 31, 2014 Pension Benefit Plans | December 31, 2014 Other Benefit Plans | December 31, 2013 Pension Benefit Plans | December 31, 2013 Other Benefit Plans |
|---|---|---|---|---|
| Fair market value of plans assets | **$ 108.9** | **$ -** | $ 105.1 | $ - |
| Accrued benefit obligations | **(125.9)** | **(76.9)** | (107.6) | (64.1) |
| Funded status of plans – deficit | **$ (17.0)** | **$ (76.9)** | $ (2.5) | $ (64.1) |
| Other pension plans | **(1.0)** | **-** | (1.0) | - |
| Total accrued liability, net | **$ (18.0)** | **$ (76.9)** | $ (3.5) | $ (64.1) |

The net accrued benefit liability is included in CPPI's balance sheet as follows

| (millions of Canadian dollars) | December 31, 2014 Pension Benefit Plans | December 31, 2014 Other Benefit Plans | December 31, 2013 Pension Benefit Plans | December 31, 2013 Other Benefit Plans |
|---|---|---|---|---|
| Retirement benefit surplus | **$ -** | **$ -** | $ 8.2 | $ - |
| Retirement benefit obligations | **(18.0)** | **(76.9)** | (11.7) | (64.1) |
| Total accrued benefit liability, net | **$ (18.0)** | **$ (76.9)** | $ (3.5) | $ (64.1) |

### Components of pension cost

The following table shows the before tax impact on net income and other comprehensive income of the Company's pension and other defined benefit plans:

| (millions of Canadian dollars) | 2014 Pension Benefit Plans | 2014 Other Benefit Plans | 2013 Pension Benefit Plans | 2013 Other Benefit Plans |
|---|---|---|---|---|
| **Recognized in net income** | | | | |
| Current service cost | **$ 3.2** | **$ 1.6** | $ 3.2 | $ 2.0 |
| Administration expense | **0.1** | **-** | 0.1 | - |
| Interest cost | **-** | **3.0** | 0.7 | 3.4 |
| Other | **-** | **(0.3)** | 0.2 | (0.3) |
| Total included in net income | **$ 3.3** | **$ 4.3** | $ 4.2 | $ 5.1 |
| **Recognized in other comprehensive income** | | | | |
| Actuarial (gain) – experience | **$ (2.0)** | **$ (0.2)** | $ (0.2) | $ (11.8) |
| Actuarial loss – demographic | **3.3** | **2.0** | 2.8 | 0.4 |
| Actuarial loss (gain) – financial assumptions | **14.3** | **8.2** | (10.3) | (7.9) |
| Return on plan assets (greater) than discount rate | **(3.9)** | **-** | (8.5) | - |
| Administrative greater than expected | **0.2** | **-** | - | - |
| Reallocation of assets in proportion to obligations | **3.9** | **-** | - | - |
| Total included in other comprehensive income | **$ 15.8** | **$ 10.0** | $ (16.2) | $ (19.3) |

### Significant assumptions

The actuarial assumptions used in measuring CPPI's benefit plan provisions and benefit costs are as follows:

| | **December 31, 2014** | | December 31, 2013 | |
|---|---|---|---|---|
| | **Pension Benefit Plans** | **Other Benefit Plans** | Pension Benefit Plans | Other Benefit Plans |
| Discount rate | **3.90%** | **3.90%** | 4.80% | 4.90% |
| Rate of compensation increases | **3.00%** | **n/a** | 3.00% | n/a |
| Future salary increases | **2.50%** | **n/a** | 3.00% | n/a |
| Initial medical cost trend rate | **n/a** | **7.00%** | n/a | 7.00% |
| Ultimate medical cost trend rate | **n/a** | **4.50%** | n/a | 4.50% |
| Year ultimate rate is reached | **n/a** | **2021** | n/a | 2021 |

In addition to the significant assumptions listed in the table above, the average life expectancy of a 65 year old at December 31, 2014 is between 20.8 years and 24.0 years (2013 – 19.8 years and 23.0 years). As at December 31, 2014, the weighted average duration of the defined benefit plan obligation is 12.4 years (2013 – 11.4 years). The weighted average duration of the other benefit plans is 13.9 years (2013 – 13.7 years).

### Sensitivity analysis

Assumed discount rates and medical cost trend rates have a significant effect on the accrued benefit obligation. A one percentage point change in these assumptions would have the following effects on the accrued benefit obligation for 2014:

| (millions of Canadian dollars) | 1% Increase | 1% Decrease |
|---|---|---|
| Pension benefit plans | | |
| Discount rate | $ (15.8) | $ 17.8 |
| Other benefit plans | | |
| Discount rate | $ (10.6) | $ 13.4 |
| Initial medical cost trend rate | $ 9.5 | $ (8.0) |

As at December 31, 2014, CPPI estimated that it will make contribution payments of $3.4 million to its defined benefit plans in 2015 based on the last actuarial valuation for funding purposes.

#### *Defined contribution and other plans*

The total expense recognized in 2014 for CPPI's defined contribution plans was $1.3 million (2013 - $1.2 million).

CPPI contributes to a pulp industry pension plan providing pension benefits. This plan is accounted for as defined contribution plan. Contributions to this plan, not included in the expense for defined contribution plan above, amounted to $6.7 million in 2014 (2013 - $6.7 million).

#### *Other*

CPPI's total employee benefits expense includes salaries and wages, future employee benefits and terminations as applicable. The total benefits expense in 2014 was $146.2 million (2013 - $142.0 million).

### 11. Asset Retirement Obligations

The following table provides a reconciliation of the asset retirement obligations as at December 31, 2014 and 2013:

| (millions of Canadian dollars) | **2014** | 2013 |
|---|---|---|
| Asset retirement obligations at beginning of year | **$ 2.7** | $ 3.3 |
| Accretion expense | **0.1** | 0.1 |
| Changes in estimates | **0.7** | (0.7) |
| Asset retirement obligations at end of year | **$ 3.5** | $ 2.7 |

CPPI's asset retirement obligations represent estimated undiscounted future payments of $7.2 million to remediate landfills at the operations at the end of their useful lives. The payments are expected to occur at periods ranging from 4 to 37 years and have been discounted at risk-free rates ranging from 1.4% to 2.4% (2013 – 1.9% to 3.2%). The $0.7 million changes in estimates associated with the asset retirement obligation principally reflects a lower discount rate used in valuation of the obligation.

CPPI has certain assets that have indeterminable retirement dates and, therefore, there is an indeterminate settlement date for the related asset retirement obligations. As a result, no asset retirement obligations are recorded for these assets. These assets include wastewater and effluent ponds that will have to be drained once the related operating facility is closed and storage sites for which removal of chemicals, fuels and other related materials will be required once the related operating facility is closed. When the retirement dates of these assets become determinable and an estimate can be made, an asset retirement obligation will be recorded.

It is possible that changes in future conditions could require a material change in the recognized amount of the asset retirement obligations. The asset retirement obligations balance is included in other long-term provisions on the balance sheet.

## 12. Share Capital

### *Authorized*

Unlimited number of common shares, no par value

### *Issued and Fully Paid*

| | **2014** | | | 2013 | | |
|---|---|---|---|---|---|---|
| (millions of Canadian dollars, except number of shares) | **Number of Shares** | | **Amount** | Number of Shares | | Amount |
| Common shares at beginning of year | **71,007,341** | **$** | **523.4** | 71,269,790 | $ | 525.3 |
| Shares purchased | **(177,518)** | | **(1.3)** | (262,449) | | (1.9) |
| Common shares at end of year | **70,829,823** | **$** | **522.1** | 71,007,341 | $ | 523.4 |

The holders of common shares are entitled to vote at all meetings of shareholders of the Company and are entitled to receive dividends when declared.

Basic net income per share is calculated by dividing the net income available to common shareholders by the weighted average number of common shares outstanding during the period. The weighted average number of common shares outstanding for 2014 was 70,949,525 (2013 – 71,149,822), and reflected shares purchased under the Company's Normal Course Issuer Bid (see below).

### *Normal Course Issuer Bid*

On March 5, 2014, the Company renewed its normal course issuer bid whereby it can purchase for cancellation up to 3,550,367 common shares or approximately 5% of its issued and outstanding common shares as of February 28, 2014. The renewed normal course issuer bid is set to expire on March 4, 2015. In 2014, CPPI purchased 177,518 common shares for $2.0 million (an average price of $11.27 per common share), of which $1.3 million was charged to share capital and $0.7 million was charged to retained earnings. As a result of the share purchases in 2014, Canfor's interest in CPPI increased from 50.4% at December 31, 2013 to 50.5% at December 31, 2014.

In 2013, under a previous normal course issuer bid, CPPI purchased 262,449 common shares for $2.4 million (an average price of $9.14 per common share), of which $1.9 million was charged to share capital and $0.5 million was charged to retained earnings.

## 13. Finance Expense, Net

| (millions of Canadian dollars) | | **2014** | | 2013 |
|---|---|---|---|---|
| Finance expense | **$** | **(5.8)** | $ | (12.2) |
| Less: Interest income | | **0.3** | | 0.4 |
| Finance expense, net | **$** | **(5.5)** | $ | (11.8) |

For the year ended December 31, 2014, finance expense, net related substantially to interest expense on term debt and net interest expense on retirement benefit obligations. Included in finance expense, net in 2014 was $3.0 million related to retirement benefit obligations (2013 - $4.1 million) and $1.4 million related to term debt (2013 - $6.6 million).

## 14. Income Taxes

The components of income tax expense are as follows:

| (millions of Canadian dollars) | 2014 | 2013 |
|---|---|---|
| Current | **$ (31.0)** | $ (14.4) |
| Deferred | **0.5** | (3.6) |
| Income tax expense | **$ (30.5)** | $ (18.0) |

The reconciliation of income taxes calculated at the statutory rate to the actual income tax provision is as follows:

| (millions of Canadian dollars) | 2014 | 2013 |
|---|---|---|
| Income tax expense at statutory rate 2014 – 26.0% (2013 - 25.75%)[2] | **$ (31.2)** | $ (15.4) |
| Add (deduct): | | |
| Permanent difference from capital gains and other non-deductible items | **(0.1)** | (1.0) |
| Entities with different income tax rates and other tax adjustments | **0.8** | 0.8 |
| Change in substantively enacted tax rate[2] | **-** | (2.4) |
| Income tax expense | **$ (30.5)** | $ (18.0) |

[2]Effective April 1, 2013, the British Columbia Provincial Government increased the corporate tax rate from 10% to 11%.

In addition to the amounts recorded to net income, a tax recovery of $6.7 million was recorded to other comprehensive income for the year ended December 31, 2014 (2013 - $9.3 million expense) in relation to actuarial gains/losses on defined benefit employee compensation plans.

The tax effects of the significant components of temporary differences that give rise to deferred income tax assets and liabilities are as follows:

| (millions of Canadian dollars) | As at December 31, 2014 | As at December 31, 2013 |
|---|---|---|
| Deferred income tax assets | | |
| Loss carry forwards | **$ -** | $ 5.6 |
| Retirement benefit obligations | **24.6** | 17.4 |
| Other | **1.8** | 1.3 |
| | **$ 26.4** | $ 24.3 |
| Deferred income tax liabilities | | |
| Depreciable capital assets | **$ (91.9)** | $ (96.6) |
| Other | **-** | (0.5) |
| | **(91.9)** | (97.1) |
| Total deferred income taxes, net | **$ (65.5)** | $ (72.8) |

Of the amounts included in the table, $0.6 million of the deferred tax assets are forecast to be recovered within twelve months of the balance sheet date (2013 - $5.9 million deferred tax asset).

## 15. Net Change in Non-Cash Working Capital

| (millions of Canadian dollars) | 2014 | 2013 |
|---|---|---|
| Accounts receivable | **$ 11.5** | $ (0.3) |
| Inventories | **(15.6)** | 6.1 |
| Prepaid expenses and other assets | **(5.6)** | 2.7 |
| Accounts payable and accrued liabilities | **(4.2)** | 7.6 |
| Net decrease (increase) in non-cash working capital | **$ (13.9)** | $ 16.1 |

## 16. Related Party Transactions

In 2014, the Company depended on Canfor to provide approximately 59% (2013 - 61%) of its fibre supply as well as to provide certain key business and administrative services as described below. As a result, of these relationships, the Company considers its operations to be dependent on its ongoing relationship with Canfor. The pricing under the Company's Fibre Supply Agreement with Canfor was renewed effective November 1, 2013. The current pricing under the agreement expires September 1, 2016 and may be amended as necessary to ensure that it is reflective of market conditions.

CPPI undertakes transactions with various related entities. These transactions are in the normal course of business and are generally on similar terms as those accorded to unrelated third parties, except where noted otherwise.

The Company purchased wood chips, logs and hog fuel from Canfor sawmills in the amount of $147.5 million in 2014 (2013 - $126.1 million).

Canfor provides certain business and administrative services to CPPI under a services agreement. The total value of the services provided by Canfor in 2014 was $10.6 million (2013 - $8.7 million). These amounts are included in manufacturing and product costs and selling and administration costs.

CPPI provides certain business and administrative services to Canfor under an incidental services agreement. Total value of the services provided to Canfor in 2014 was $2.8 million (2013 - $2.5 million). These amounts are included as a cost recovery in manufacturing and product costs and selling and administration costs.

The Company markets bleached chemi-thermo mechanical pulp ("BCTMP") production from Canfor's Taylor Pulp Mill ("Taylor") for which it earned commissions totaling $1.8 million in 2014 (2013 - $2.0 million), included in sales. The Company did not purchase BCTMP from Taylor for resale in 2014 (2013 – $0.2 million). The Company sold NBSK pulp to Taylor for packaging use totaling $3.4 million in 2014 (2013 – $3.0 million). Subsequent to the purchase of the Taylor Pulp Mill on January 30, 2015 (Note 21b), the Taylor Pulp Mill became a division of CPPI and these transactions became internal.

At December 31, the following amounts were included in the balance sheet of the Company:

| (millions of Canadian dollars) | **As at December 31, 2014** | As at December 31, 2013 |
|---|---|---|
| **Balance Sheet** | | |
| Included in accounts payable and accrued liabilities: | | |
| Canfor | **$ 18.0** | $ 18.9 |
| Included in trade and other accounts receivable: | | |
| Products marketed for Canfor | **$ 1.7** | $ 9.0 |

### *Key Management Personnel*

Key management includes members of the Board of Directors and the Senior Executive management team. The compensation expense for key management for services is as follows:

| (millions of Canadian dollars) | **2014** | 2013 |
|---|---|---|
| Short-term benefits | **$ 3.4** | $ 3.9 |
| Post-employment benefits | **0.2** | 0.3 |
| | **$ 3.6** | $ 4.2 |

Short-term benefits for most members of the Board of Directors include an annual retainer as well as attendance fees.

### *Other Related Parties*

During the year, CPPI made contributions to certain post-employment benefit plans for the benefit of CPPI employees. Note 10 Employee Future Benefits contains further details.

Subsequent to year end CPPI completed the purchase of Canfor's Taylor Pulp Mill. Note 21 Subsequent Events contains further details.

## 17. Segment Information

The Company has two reportable segments which operate as separate business units and represent separate product lines.

Sales between pulp and paper segments are accounted for at prices that approximate fair value. These include sales of slush pulp from the pulp segment to the paper segment.

Information regarding the operations of each reportable segment is included in the table below. The accounting policies of the reportable segments are the same as described in Note 3.

The Company's interest-bearing liabilities are not considered to be segment liabilities but rather are managed centrally by the treasury function. Other liabilities are not split by segment for the purposes of allocating resources and assessing performance.

| (millions of Canadian dollars) | | Pulp | Paper | Unallocated | Elimination Adjustment | | Total |
|---|---|---|---|---|---|---|---|
| **Year ended December 31, 2014** | | | | | | | |
| **Sales to external customers** | **$** | **816.4** | **162.8** | **1.3** | **-** | **$** | **980.5** |
| **Sales to other segments** | **$** | **93.8** | **-** | **-** | **(93.8)** | **$** | **-** |
| **Operating income (loss)** | **$** | **115.0** | **22.0** | **(11.6)** | **-** | **$** | **125.4** |
| **Amortization** | **$** | **59.2** | **3.4** | **0.1** | **-** | **$** | **62.7** |
| **Capital expenditures[3]** | **$** | **56.2** | **1.1** | **0.4** | **-** | **$** | **57.7** |
| **Identifiable assets** | **$** | **677.9** | **57.6** | **91.9** | **-** | **$** | **827.4** |
| Year ended December 31, 2013 | | | | | | | |
| Sales to external customers | $ | 738.4 | 147.1 | 1.3 | - | $ | 886.8 |
| Sales to other segments | $ | 76.2 | - | - | (76.2) | $ | - |
| Operating income (loss) | $ | 63.2 | 22.7 | (12.1) | - | $ | 73.8 |
| Amortization | $ | 66.1 | 3.7 | 0.1 | - | $ | 69.9 |
| Capital expenditures[3] | $ | 60.1 | 0.9 | 0.2 | - | $ | 61.2 |
| Identifiable assets | $ | 674.9 | 56.7 | 37.0 | - | $ | 768.6 |

[3] Capital expenditures represent cash paid for capital assets during the period and include capital expenditures financed by government grants.

### Geographic information

CPPI's products are marketed worldwide, with sales made to customers in a number of different countries. In presenting information on the basis of geographical location, revenue is based on the geographical location of customers.

| (millions of Canadian dollars) | | **2014** | | 2013 |
|---|---|---|---|---|
| Sales by location of customer | | | | |
| Canada | **$** | **54.8** | $ | 41.3 |
| United States | | **301.0** | | 238.3 |
| Europe | | **86.3** | | 106.9 |
| Asia | | **492.5** | | 464.5 |
| Other | | **45.9** | | 35.8 |
| | **$** | **980.5** | $ | 886.8 |

## 18. Commitments

At the end of the year, CPPI had contractual commitments for the construction of capital assets for $0.6 million (2013 - $4.0 million). These commitments are expected to be settled over the following year.

CPPI has committed to operating leases for property, plant and equipment. As at December 31, 2014 and 2013, the future minimum lease payments under these operating leases were as follows:

| (millions of Canadian dollars) | | **As at December 31, 2014** | | As at December 31, 2013 |
|---|---|---|---|---|
| Within one year | **$** | **0.8** | $ | 1.7 |
| Between one and five years | | **0.3** | | 1.0 |
| Total | **$** | **1.1** | $ | 2.7 |

During the year ended December 31, 2014, $2.9 million (2013 - $2.9 million) was recognized as an expense in the income statement in respect to operating leases.

In addition to the above commitments, the Company has operational agreements with minimum usage requirements. No issues were identified with meeting these obligations.

*Energy Agreements*

The Company has entered into three separate energy agreements with a BC energy company and electricity transmission provider (the "Energy Agreements") for all three of the Company's mills, with commencement dates ranging from 2006 through 2015. These agreements are for the commitment of electrical load displacement and the sale of incremental power from the Company's pulp and paper mills. These Energy Agreements include incentive grants from the BC energy company for capital investments to increase electrical generation capacity, and also call for performance guarantees to ensure minimum required amounts of electricity are generated, with penalty clauses if they are not met. As part of these commitments, the Company has entered into standby letters of credit for these guarantees. The standby letters of credit have variable expiry dates, depending on the capital invested and the length of the Energy Agreement involved. As at December 31, 2014 CPPI had posted $12.2 million of standby letters of credit (2013 - $12.2 million) under these agreements, and had no repayment obligations under the terms of any of these agreements.

## 19. Financial Risk and Capital Management

### *Financial Risk Management*

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

The CPPI Risk Management Committee manages risk in accordance with a Board approved Risk Management Controls Policy. The policy sets out the responsibilities, reporting and counter party credit and communication requirements associated with all of the Company's risk management activity. Responsibility for overall philosophy, direction and approval is that of the Board of Directors.

*Credit risk:*

Credit risk is the risk of financial loss to CPPI if a counterparty to a financial instrument fails to meet its contractual obligations.

Financial instruments that are subject to credit risk include cash and cash equivalents and accounts receivable. Cash and cash equivalents includes cash held through major Canadian and international financial institutions as well as temporary investments with an original maturity date of three months or less. The cash and cash equivalents balance at December 31, 2014 is $76.8 million (2013 – $13.5 million).

CPPI utilizes credit insurance to manage the risk associated with trade receivables. As at December 31, 2014, approximately 81% (2013 - 87%) of the outstanding trade receivables are covered under credit insurance. In addition, CPPI requires letters of credit on certain export trade receivables and regularly discounts these letters of credit without recourse. CPPI recognizes the sale of the letters of credit on the settlement date, and accordingly reduces the related trade accounts receivable balance. CPPI's trade receivable balance at December 31, 2014 was $60.7 million (2013 - $71.0 million). At December 31, 2014, approximately 98% (2013 – 96%) of the trade accounts receivable balance was within CPPI's established credit terms.

*Liquidity risk:*

Liquidity risk is the risk that CPPI will be unable to meet its financial obligations as they come due. The Company manages liquidity risk through regular cash-flow forecasting in conjunction with an adequate committed operating loan facility.

At December 31, 2014, CPPI had no amounts drawn (2013 – $10.6 million) on its operating loans and accounts payable and accrued liabilities of $123.2 million (2013 - $118.4 million), all of which are due within twelve months of the balance sheet date.

*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, foreign currency, commodity and energy prices.

*(i) Interest rate risk:*

CPPI is exposed to interest rate risk through its current financial assets and financial obligations bearing variable interest rates.

CPPI utilizes interest rate swaps to reduce its exposure to financial obligations bearing variable interest rates. At December 31, 2014, CPPI had $35.0 million in fixed interest rate swaps (2013 – $105.0 million) with interest rates ranging from 2.32% to 2.34%, maturing in 2015.

*(ii) Currency risk:*

CPPI is exposed to foreign exchange risk primarily related to the US dollar, as CPPI 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 Company holds financial assets and liabilities in US dollars. These primarily include US dollar bank accounts, investments and trade accounts.

An increase (decrease) in the value of the Canadian dollar by US$0.01 would result in a pre-tax: (i) loss (gain) of approximately $0.6 million in relation to working capital balances denominated in US dollars at year end (including cash, accounts receivable and accounts payable).

A portion of the currency risk associated with US dollar denominated sales is naturally offset by US dollar denominated expenses. A portion of the remaining exposure is covered by foreign exchange collar contracts that effectively limit the minimum and maximum Canadian dollar recovery related to the sale of those US dollars.

CPPI had the following foreign exchange derivatives at December 31, 2014 and 2013:

| | **As at December 31, 2014** | | As at December 31, 2013 | |
|---|---|---|---|---|
| | **Notional Amount** | **Exchange Rates** | Notional Amount | Exchange Rates |
| **US Dollar Collars** | (millions of US dollars) | (protection/topside, per dollar) | (millions of US dollars) | (protection/topside, per dollar) |
| *0-12 months* | **$ 104.0** | **$1.11 / $1.22** | $ 90.0 | $ 1.04 / $1.11 |

*(iii) Commodity price risk:*

CPPI's financial performance is dependent on the selling price of its products and the purchase price of raw material inputs. Consequently, CPPI 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, CPPI is subject to reduced revenues and margins, which adversely impact profitability.

From time to time, CPPI enters into futures contracts on commodity exchanges for pulp. Under the Price Risk Management Controls Policy up to 5% of pulp sales may be sold in this way.

CPPI had the following pulp futures contracts at December 31, 2014 and 2013:

| | **As at December 31, 2014** | | As at December 31, 2013 | |
|---|---|---|---|---|
| | **Notional Amount** | **Average Rate** | Notional Amount | Average Rate |
| **Pulp** | (tonnes) | (US dollars per tonne) | (tonnes) | (US dollars per tonne) |
| Future Sales Contracts | | | | |
| *0-12 months* | **-** | **$ -** | 12,000 | $945.00 |

*(iv) Energy price risk:*

CPPI is exposed to energy price risk relating to purchases of natural gas and diesel oil for use in its operations.

The exposure is hedged up to 100% through the use of floating to fixed swap contracts or option contracts with maturity dates up to a maximum of eighteen months. In the case of diesel, CPPI uses Western Texas Intermediate oil ("WTI") contracts to hedge its exposure.

As at December 31, 2014, the Company had 102 thousand barrels of WTI oil collars outstanding, which will be settled in 2015, with weighted average protection of $58.14 per barrel and topside of $77.35 per barrel. As at December 31, 2013, the Company had no WTI oil collars outstanding.

***Capital management***

CPPI's objectives when managing capital are to maintain a strong balance sheet and a globally competitive cost structure, that ensure adequate liquidity to maintain and develop the business through the commodity price cycle.

CPPI's capital is comprised of net debt and shareholders' equity:

| (millions of Canadian dollars) | | **As at December 31, 2014** | | As at December 31, 2013 |
|---|---|---|---|---|
| Total debt (including operating loans) | **$** | **50.0** | $ | 60.6 |
| Less: Cash and cash equivalents | | **76.8** | | 13.5 |
| Net debt (cash) | **$** | **(26.8)** | $ | 47.1 |
| Total equity | | **489.6** | | 438.0 |
| | **$** | **462.8** | $ | 485.1 |

The Company has certain financial covenants in its debt obligations that stipulate maximum net debt to total capitalization ratios and minimum net worth amounts based on total shareholders' equity. The net debt to total capitalization is calculated by dividing total debt less cash and cash equivalents, by shareholders' equity plus total debt less cash and cash equivalents.

CPPI's strategy is to ensure it remains in compliance with all of its existing debt covenants, so as to ensure continuous access to capital. CPPI was in compliance with all its debt covenants for the years ended December 31, 2014 and 2013.

There were no changes in the Company's approach to capital management in the year. Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

## 20. Financial Instruments

*Classification and measurement of financial instruments*

CPPI's cash and cash equivalents, accounts receivable, loans and advances, operating loans, accounts payable and accrued liabilities, and long-term debt are measured at amortized cost subsequent to initial recognition.

Derivative instruments are measured at fair value. IFRS 13, *Fair Value Measurement,* requires classification of these items within a hierarchy that prioritizes the inputs to fair value measurement.

The three levels of the fair value hierarchy are:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 – Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly;

Level 3 – Inputs that are not based on observable market data.

*Derivative financial instruments*

The Company uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, pulp prices, energy costs and interest rates. At December 31, 2014, the fair value of derivative financial instruments was a net liability of $1.0 million (2013 – net liability of $0.1 million). The fair value of these financial instruments was determined based on prevailing market rates for instruments with similar characteristics.

The following table summarizes the gain (loss) on derivative financial instruments for the years ended December 31, 2014 and 2013:

| (millions of Canadian dollars) | | **2014** | | 2013 |
|---|---|---|---|---|
| Foreign exchange collars | **$** | **(0.3)** | $ | 0.1 |
| Energy derivatives | | **(0.7)** | | 0.1 |
| Interest rate swaps | | **(0.1)** | | (0.2) |
| Pulp futures | | **(0.8)** | | (0.1) |
| Loss on derivative financial instruments | **$** | **(1.9)** | $ | (0.1) |

These financial instruments are classified as held for trading and as level 2 in the fair value hierarchy. There were no financial instrument transfers between fair value hierarchy levels during 2014 or 2013.

## 21. Subsequent Events

### *(a) Dividends*

On February 4, 2015, the Board of Directors declared a quarterly dividend of $0.0625 per share, payable on February 24, 2015, to shareholders of record on February 17, 2015.

### *(b) Purchase of Taylor Pulp Mill*

On January 30, 2015, CPPI completed the purchase of the BCTMP Taylor Pulp Mill from Canfor for cash proceeds of approximately $15.0 million including working capital. The transaction also includes a long-term fibre supply agreement under which Canfor will supply fibre to the Taylor Pulp Mill at prices that approximate fair market value. In addition to the cash proceeds, Canfor may also receive contingent consideration over a 3 year period, starting January 31, 2015, based on the Taylor Pulp Mill's annual adjusted operating income before amortization. On the acquisition date the fair value of the contingent consideration was approximately $1.8 million. CPPI recognized long-term assets acquired net of liabilities assumed of approximately $2.8 million and net working capital of approximately $14.0 million. The acquisition has been accounted for in accordance with IFRS 3 *Business Combinations.*