

FORTRESS GLOBAL ENTERPRISES

(FORMERLY FORTRESS PAPER Ltd.)

FINANCIAL STATEMENTS

DECEMBER 31, 2018

TSX:FGE

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Independent auditor's report

To the Shareholders of Fortress Global Enterprises Inc.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Fortress Global Enterprises Inc. and its subsidiaries (together, the Company) as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Company's consolidated financial statements comprise:

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

Basis for opinion

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

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

Independence

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

PricewaterhouseCoopers LLP

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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.



Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis.

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

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

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

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

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

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

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

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

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



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

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

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



We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is John DeLucchi.

(signed) PricewaterhouseCoopers LLP

Chartered Professional Accountants

Vancouver, British Columbia
March 27, 2019

FORTRESS GLOBAL ENTERPRISES INC.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Canadian dollars, amounts in thousands)

	Note	December 31, 2018 \$	December 31, 2017 \$
ASSETS			
Current			
Cash and cash equivalents		12,608	40,877
Restricted cash	5	8,156	7,790
Trade accounts receivable	6	10,225	6,245
Other accounts receivable	7	5,706	7,441
Inventories	8	25,402	31,148
Financial instruments	9	–	176
Prepaid expenses		596	506
		62,693	94,183
Other long-term receivable	22	–	7,000
Intangible asset	10	2,404	–
Property, plant and equipment	12	281,216	293,524
Total assets		346,313	394,707
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities	13	35,142	50,241
Financial instruments	9	1,455	–
Current portion of long-term debt	14	14,225	14,516
		50,822	64,757
Long-term debt	14	195,116	194,719
Provisions and other long-term liabilities	16	538	9,929
Total liabilities		246,476	269,405
Shareholders' equity			
Share capital	17	177,196	174,704
Contributed surplus		24,959	24,315
Retained deficit		(135,246)	(103,066)
Accumulated other comprehensive income		32,928	29,349
Total shareholders' equity		99,837	125,302
Total liabilities and shareholders' equity		346,313	394,707
Commitments	22		
Subsequent events	27		

(See accompanying notes)

Approved by the Board of Directors:

“Anil Wirasekara”

Director

“Giovanni Iadeluca”

Chief Executive Officer

FORTRESS GLOBAL ENTERPRISES INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Canadian dollars, amounts in thousands, except share and per share data)

	Note	December 31, 2018 \$	December 31, 2017 \$
Sales		185,945	156,414
Costs and expenses			
Manufacturing and distribution costs		(152,263)	(140,560)
Amortization	12	(22,132)	(21,842)
Selling, general and administration		(21,255)	(19,537)
Stock-based compensation	18	(427)	(978)
Operating loss		(10,132)	(26,503)
Other income (expense)			
Finance expense	19	(22,703)	(15,989)
Finance income	19	4,405	2,856
Non-operating income		1,821	–
Gain on disposal of assets	12	–	680
Gain on financial instruments	9	(1,534)	962
Foreign exchange (loss) gain		(4,037)	5,003
Net loss from continuing operations before taxes		(32,180)	(32,991)
Income tax recovery	15	–	3
Net loss from continuing operations		(32,180)	(32,988)
Net loss from discontinued operations	11	–	(60,394)
Net loss		(32,180)	(93,382)
Net loss and diluted net loss per share from continuing operations		(2.17)	(2.31)
Net loss per share and diluted net loss per share		(2.17)	(6.54)
Weighted average number of shares outstanding			
Basic and diluted	20	14,795,924	14,283,747

(See accompanying notes)

FORTRESS GLOBAL ENTERPRISES INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Canadian dollars, amounts in thousands)

		December 31, 2018 \$	December 31, 2017 \$
	Note		
Net loss		(32,180)	(93,382)
Other comprehensive income			
Items that may be reclassified subsequently to net loss			
Exchange differences on translation of foreign operations		3,579	(1,540)
Items that will not be reclassified to net loss			
Employee future benefits (net of taxes of \$nil and \$nil)	11	–	7,291
Total other comprehensive income		3,579	5,751
Total comprehensive loss		(28,601)	(87,631)

(See accompanying notes)

FORTRESS GLOBAL ENTERPRISES INC.
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
(Canadian dollars, amounts in thousands)

	Note	December 31, 2018 \$	December 31, 2017 \$
Share capital	17		
Balance at beginning of period		174,704	175,445
Shares issued on business acquisition		2,400	–
Restricted share units vested		92	169
Exercise of stock options		–	371
Common share repurchase		–	(1,281)
Balance at end of period		177,196	174,704
Treasury shares			
Balance at beginning of period		–	(2,357)
Liability for treasury shares		–	2,357
Balance at end of period		–	–
Contributed surplus	18		
Balance at beginning of period		24,315	24,208
Stock-based compensation		736	647
Restricted share units vested		(92)	(169)
Exercise of stock options		–	(371)
Balance at end of period		24,959	24,315
Retained deficit			
Balance at beginning of period		(103,066)	(17,636)
Net loss		(32,180)	(93,382)
Employee future benefits	11	–	7,291
Common share repurchase	17	–	661
Balance at end of period		(135,246)	(103,066)
Accumulated other comprehensive income			
Balance at beginning of period		29,349	30,889
Translation adjustment on foreign operations		3,579	(1,540)
Balance at end of period		32,928	29,349
Total equity		99,837	125,302

(See accompanying notes)

FORTRESS GLOBAL ENTERPRISES INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Canadian dollars, amounts in thousands)

		December 31, 2018 \$	December 31, 2017 \$
	Note		
Cash flows from (used by) operating activities			
Net loss for the period		(32,180)	(93,382)
Adjustments:			
Gain on disposal of assets	12	–	(680)
Loss (gain) on financial instruments	9	1,631	(176)
Amortization	12	22,132	21,842
Unrealized foreign exchange loss (gain)		3,158	(3,990)
Finance expense, net	19	18,298	13,133
Stock-based compensation	18	390	978
Loss on sale of business	11	–	56,558
		13,429	(5,717)
Change in non-cash working capital items			
Accounts receivable		(3,022)	1,845
Inventories		5,746	(2,573)
Prepaid expenses		(90)	518
Accounts payable and accrued liabilities and other		(9,626)	22,129
Operating cash flows from discontinued operations	11	–	11,433
		6,437	27,635
Cash flows from (used by) financing activities			
Repayment of long-term debt		(5,990)	(2,468)
Repurchase of common shares	17	–	(621)
Convertible debt repurchase	14	–	(25,000)
Transaction costs incurred in convertible debt refinancing	14	(2,863)	–
Additions to long-term debt	14	–	41,745
Payment of long-term debt interest and financing fees	14	(9,927)	(10,243)
Financing cash flows used by discontinued operations	11	–	(92)
		(18,780)	3,321
Cash flows (used by) from investing activities			
Additions to property, plant and equipment	12	(22,463)	(32,009)
Cash acquired on acquisition	10	59	–
Net proceeds from disposal of assets	12	–	680
Finance income	19	329	231
Government grants received	21	6,126	8,475
Restricted cash	5	–	(5,421)
Proceeds from disposal of discontinued operation	11	–	27,168
Cash adjustments from disposal of discontinued operation	11	–	(4,906)
Investing cash flows from discontinued operations	11	–	(6,873)
		(15,949)	(12,655)
Increase (decrease) in cash position		(28,292)	18,301
Foreign exchange gain on cash and cash equivalents		23	444
Cash and cash equivalents, beginning of year		40,877	22,132
Cash and cash equivalents, end of period		12,608	40,877
Supplemental cash flow information	25		

(See accompanying notes)

1. NATURE OF OPERATIONS

Fortress Global Enterprises Inc. (formerly Fortress Paper Ltd.) (the “Company” or “Fortress”) was incorporated on May 30, 2006 under the laws of the Province of British Columbia. The address of the Company’s registered office is 157 Chadwick Court – 2nd floor, North Vancouver, British Columbia, Canada V7M 3K2. Up until December 20, 2017 Fortress operated internationally in two distinct business segments: dissolving pulp and security paper products. The Company operates its dissolving pulp business at the Fortress Specialty Cellulose mill located in Canada which also operates a cogeneration facility that produces renewable energy. On December 20, 2017, the Company sold its security paper products business that was located at the Landqart mill in Switzerland, where Fortress was a producer of banknote, passport, visa and other brand protection and security papers (Note 11). In March of 2018, the Company acquired S2G Biochemicals Inc. (Note 10) which has been included in the newly created Bioproducts Segment (Note 24).

2. BASIS OF PRESENTATION

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) applicable to the preparation of financial statements as issued by the International Accounting Standards Board (“IASB”). The Company has consistently applied the same accounting policies throughout all years presented, except as discussed in notes 3 and 4. The Board of Directors approved these statements on March 26, 2019.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 3. The consolidated financial statements have been prepared on the historical cost basis with the exception of compound financial instruments, derivative financial instruments, and provisions which are discussed in Note 3.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The consolidated financial statements include the accounts of the Company and, from their respective dates of acquisition of control or formation, its wholly owned subsidiaries.

Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of each consolidated entity 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 presentation currency.

The financial statements of entities that have a functional currency other than Canadian dollars (“foreign operations”) are translated into Canadian dollars as follows: assets and liabilities – at the closing rate at the date of the statement of financial position, and income and expenses – using actual rates in place at the time of the transaction or an average rate if it is considered a reasonable approximation for the actual rate. All resulting exchange differences are recognized in other comprehensive income as cumulative translation adjustments.

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When the Company disposes of its entire interest in a foreign operation, or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in other comprehensive income related to the foreign operation are recognized in profit or loss. If the Company disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in other comprehensive income related to the subsidiary are reallocated between controlling and non-controlling interests.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in currencies other than an operation's functional currency are recognized in the statement of operations.

Consolidation

Subsidiaries are all entities (including structured entities) over which the Company has control. The Company controls an entity when the Company is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The following were the principal operating subsidiaries of the Company during 2017 and 2018:

	Jurisdiction	Functional Currency
Fortress Specialty Cellulose Inc.	Canada	Canadian dollar
Landqart AG (Note 11)	Switzerland	Swiss franc ("CHF")
Fortress Xylitol Inc. (Note 10)	Canada	Canadian dollar

Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are de-consolidated from the date that control ceases.

The Company applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Company. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. Acquisition-related costs are expensed as incurred.

Intercompany transactions, balances, income and expenses on transactions between companies are eliminated, with the exception of foreign exchange on intercompany loans for those for which repayment is expected. Profits and losses resulting from intercompany transactions that are recognised in assets are also eliminated. Accounting policies of subsidiaries are consistent with the policies adopted by the Company.

Cash and cash equivalents

The Company considers cash, cash in banks, and deposits with financial institutions with original maturities of three months or less from the date of acquisition and that can be liquidated without prior notice or penalty, to be cash or cash equivalents.

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Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

The financial instruments of the Company are comprised of cash and cash equivalents, trade and other receivables, other long-term receivable, accounts payable and accrued liabilities, long-term debt and derivative financial instruments.

Financial assets and liabilities are classified as either measured at amortized cost or fair value through net income or loss ("FVTPL") as follows:

- Amortized cost – measured at amortized cost using the effective interest method.
- FVTPL – measured at FVTPL if not classified as amortized cost with net gains and losses, including any interest, recognized through net income.

The Company's financial instruments are classified and measured as follows:

Financial Assets:	
Cash and cash equivalents	Amortized cost
Trade and other accounts receivable	Amortized cost
Other long-term receivable	Amortized cost
Foreign exchange forward contracts	FVTPL
Financial Liabilities:	
Accounts payable and accrued liabilities	Amortized cost
Long-term debt	Amortized cost

Government assistance

Government assistance related 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 assistance related to non-capital projects is recorded as a reduction of the related expenses.

Inventories

Inventories are valued at the lower of average cost and net realizable value. The cost of finished goods and work-in-progress comprises raw materials, direct labour, other direct costs and related production overheads including applicable amortization on property, plant and equipment. Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses. Supplies inventory is valued at the lower of average cost and replacement cost, which is an estimate of net realizable value.

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Intangible assets

The cost of intangible assets acquired in a business combination is the fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses.

Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually, or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated amortization and impairment charges.

No amortization is charged on major improvements or expansions until the asset is ready for its intended use. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company. Maintenance, repairs and minor replacements are expensed as incurred. The carrying amount of a replaced asset is derecognized when it is replaced.

The cost of major overhaul, repairs and replacement which increase the useful lives of existing property plant and equipment are capitalized and amortized over the period of benefit.

Property, plant and equipment are principally amortized on a straight-line basis over their estimated useful lives as follows:

Buildings	10-50 years
Manufacturing equipment	3-20 years

The Company allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant components and amortizes each such part separately. Residual values, methods of amortization and useful lives are reviewed at year end and adjusted if appropriate.

Impairment of long-lived assets

The Company reviews property, plant, and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). The recoverable amount is the higher of an asset's fair value less costs to dispose and value in use (being the present value of the expected future cash flows of the relevant asset or cash generating unit). An impairment loss is recognized in the statement of operations for the amount by which the asset's carrying amount exceeds its recoverable amount and is reviewed for possible reversal at each reporting date.

Borrowing costs

Borrowing costs attributable to the acquisition, construction or production of qualifying assets are added to

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the cost of those assets, until such time as the assets are substantially ready for their intended use. All other borrowing costs are recognized as interest expense in the statement of operations in the year in which they are incurred.

Compound financial instruments

Compound financial instruments issued by the Company comprise convertible notes that can be converted to share capital at the option of the holder and the number of shares to be issued does not vary with changes in their fair value.

The liability component of a compound financial instrument is recognized initially at the fair value of a similar liability that does not have an equity conversion option. The equity component is recognized initially at the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts.

Subsequent to initial recognition, the liability component of a compound financial instrument is measured at amortized cost using the effective interest method. The equity component of a compound financial instrument is not re-measured subsequent to initial recognition except on conversion or expiry.

Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of new common shares or options are shown in equity as a deduction, net of tax, from the proceeds. Any gains realized on repurchases of common shares are recognized directly to retained earnings.

Employee future benefits

Employees of entities included in these consolidated financial statements have entitlements under Company pension plans which are either defined contribution or defined benefit pension plans. Under a defined contribution plan an entity makes contributions to a separate entity and has no legal or constructive obligation to pay further amounts. Obligations for contributions are recognized as an employee benefit expense when they are earned.

For the Company's defined benefit pension plan the following policies have been adopted:

- The measurement date used for accounting purposes is December 31;
- The cost of pensions earned by employees is actuarially determined using the projected unit credit method pro-rated on service and management's estimate of expected plan investment performance, salary escalation and retirement ages of employees;
- The discount rate applied in arriving at the present value of the pension liability represents yields on high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the pension liability;
- For the purpose of calculating the expected return on plan assets, those assets are valued at fair value;

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- The related net pension liability recognized in the statement of financial position is the fair value of the plan assets less the present value of the defined benefit obligation at the statement of financial position date; and
- Actuarial gains and losses are recognized during the year in which they occur, in other comprehensive income (loss) and retained earnings, without recycling to the statement of operations in subsequent years.

Provisions

Provisions for cleanup of landfill sites, uncertain tax positions and legal claims, where applicable, are recognized as liabilities when the Company has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting year, and are discounted to present value where the effect is material.

Income taxes

Income taxes comprise current and deferred taxes. Income tax is recognized in the statement of operations except to the extent that it relates to items recognized directly in other comprehensive income (loss) or equity, in which case the income tax is recognized directly in other comprehensive income (loss) or equity, respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted, or substantively enacted, at the end of the reporting year in the countries where the Company and its subsidiaries operate and generate taxable income. The Company periodically evaluates the position taken and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred tax is recognized, using the liability method, in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the statement of financial position date and are expected to apply when the deferred tax asset or liability is settled. Deferred tax assets are recognized to the extent that it is probable that the assets can be recovered.

Deferred income tax is provided for taxable temporary differences associated with investments in subsidiaries except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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

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Earnings (loss) per share

Basic earnings (loss) per share are computed using the weighted average number of common shares outstanding during the year. Diluted earnings per share amounts are calculated giving effect to the potential dilution that would occur if securities or other contracts to issue common shares were exercised or converted to common shares using the treasury stock method. The treasury stock method assumes that proceeds received from the exercise of stock options and warrants are used to repurchase common shares at the prevailing market rate. Diluted earnings per share for convertible debt, using the if converted method, assumes the debt has been converted at the beginning of the period or, if later, the date of the issue of the convertible debt.

Stock-based compensation

The Company grants stock options and other share-based awards to certain employees. Each tranche in an award is considered a separate award with its own vesting year and grant date fair value. The fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. The value of stock options granted to directors and officers is recorded as stock-based compensation and credited to contributed surplus over the relevant vesting period. Any consideration received on the exercise of stock options is credited to share capital and the appropriate original fair value is reallocated from contributed surplus to share capital.

Performance options and share awards based on certain conditions are recognized when it is considered likely that the performance condition will be achieved.

Revenue and related cost recognition

The Company recognizes revenue from dissolving pulp sales when a customer obtains control over the product. For the majority of dissolving pulp sales, control is obtained by the customer when the product is loaded on a common carrier at the mill. The remainder is recognized when the product is either delivered to the customer or when it is loaded on an ocean carrier. Sales are reported net of discount, allowances and freight. The Company does not have any multiple element revenue arrangements.

Prior to January 1, 2018, the Company recognized revenue from product sales when persuasive evidence of an arrangement existed, the sales price was fixed or could be measured reliably, title of ownership and risk of loss had passed to the customer and collectability was reasonably assured. Sales were reported net of discounts and allowances. Amounts charged to customers for shipping and handling were recognized as revenue. Shipping and handling costs incurred by the Company were included in cost of products sold. The Company did not have any multiple element revenue arrangements.

The Company reports the sale of energy as revenue upon generation at its cogeneration facility.

Development costs

Expenditure incurred in the development of products or enhancements to existing product ranges is capitalized as an intangible asset only when the future economic benefits expected to arise are deemed probable and the costs can be reliably measured. Development costs not meeting these criteria are expensed in the statement of operations as incurred. Capitalized development costs are amortized on a straight-line basis over their estimated useful economic lives once the product or enhancement is available for use. Product research costs are expensed as incurred.

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Leases

The Company leases certain property, plant and equipment. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the statement of operations on a straight-line basis over the term of the lease.

Leases of property, plant and equipment where the Company has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Each lease payment is allocated between the liability and finance charges. The corresponding rental obligations, net of finance charges, are included in provisions and other long term liabilities. The interest element of the finance cost is charged to the statement of operations over the lease year so as to produce a constant periodic rate of interest on the remaining balance of the liability for each year. The property, plant and equipment acquired under finance leases are amortized over the shorter of the useful life of the asset and the lease term.

Estimates

The preparation of the consolidated financial statements in accordance with IFRS 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 estimates are reviewed and in any future periods affected.

Information about 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 3, 12 – Property, plant and equipment;
- Note 9 – Financial instruments;
- Note 10 – Intangible assets; and
- Note 16 – Provisions and other long term liabilities.

Segmented reporting

Operating segments are reported in a manner consistent with the internal reporting provided to management and the Board of Directors. The Company's operations are managed and reported internally on a divisional basis that reflects the different characteristics of each business. These divisions have been disclosed as reportable segments because they are the components that management and the Board of Directors monitors regularly in making decisions about operating matters such as allocating resources to businesses and assessing performance.

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4. NEW ACCOUNTING PRONOUNCEMENTS

Adoption of new accounting standards

IFRS 15 - Revenue from Contracts with Customers

Effective January 1, 2018, the Company adopted IFRS 15 – Revenue from Contracts with Customers. The standard supersedes IAS 18 - Revenue, IAS 11 - Construction Contracts, and related interpretations. This standard addresses revenue recognition and establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. IFRS 15 requires that revenue is recognised at the transaction price when certain contractual obligations are met. Any variable consideration elements of the price should be recognised when it is highly probable that there will be no reversal of that revenue.

The Company elected to apply IFRS 15 using a modified retrospective approach; however, the adoption of IFRS 15 resulted in no changes to classification or measurement on the financial statements of the Company, as the timing of revenue recognition was unchanged.

Revenue in the prior year comparative period was recognized in accordance with IAS 18 – Revenue.

IFRS 9 – Financial Instruments - Classification and Measurement

Effective January 1, 2018, the Company adopted IFRS 9 - Financial Instruments. IFRS 9 supersedes IAS 39 Financial Instruments: Recognition and Measurement. The standard makes changes to the previous guidance on the classification and measurement of financial assets and liabilities and introduces an expected credit loss model for the impairment of financial assets. The standard also has new requirements on the application of hedge accounting.

The table below outlines the original measurement categories under IAS 39 and the new measurement categories under IFRS 9 for each class of the Company's financial instruments at January 1, 2018:

	New Classification under IFRS 9	Original Classification under IAS 39
Financial Assets:		
Cash and cash equivalents	Amortized cost	Loans and receivables
Trade and other accounts receivable	Amortized cost	Loans and receivables
Foreign exchange forward contracts	FVTPL	FVTPL
Financial Liabilities:		
Accounts payable and accrued liabilities	Amortized cost	Other liabilities
Long-term debt	Amortized cost	Other liabilities

The Company applied the IFRS 9 retrospectively; however, the adoption of IFRS 9 did not require any adjustments to the classification or measurement of the Company's financial assets and financial liabilities. The Company applied the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables. The adoption of the new expected credit loss model under IFRS 9 had only a negligible impact on the carrying amount of the Company's financial assets on the transition date. Any gain or losses on modifications of existing debt have always immediately been recorded through the profit and loss in accordance with IFRS 9.

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Accounting standards issued and not applied

IFRS 16 – Leases

In January 2016, the IASB issued IFRS 16 - Leases, which requires, among other things, lessees to recognize leases traditionally recorded as operating leases in the same manner as a financing lease. This standard establishes a single, on-balance sheet accounting model for all leases which will result in the recognition of a right-of-use asset and a lease obligation. The nature of expenses related to those leases will change as IFRS 16 replaces the straight-line operating lease expense, currently reported under cost of products sold on our consolidated statements of earnings, with a depreciation charge for the right-of-use asset and an interest expense on the lease liability which will be reported under finance expense. Although the depreciation charge is typically even, the interest expense reduces over the life of the lease as lease payments are made. This results in a reduction in total expense as an individual lease matures.

IFRS 16 allows two exemptions for short-term and low-value leases for which the payments will be recognized as an expense, typically on a straight-line basis over the lease term.

The Company will apply IFRS 16 initially on January 1, 2019, using the modified retrospective approach. Under this method, the right-of-use asset is recognized at the date of the initial application at an amount equal to the lease liability, using the company's incremental borrowing rate. Comparative figures are not restated.

The Company has completed an assessment of the potential impact on our consolidated financial statements and has determined that IFRS 16 will not have a significant impact on our consolidated financial statements.

IFRIC 23 – Uncertainty over Income Tax Treatments

This interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 – Income Taxes when there is uncertainty over income tax treatments. This interpretation is effective for annual reporting periods beginning on or after January 1, 2019. The Company is currently evaluating the impact from the adoption of this interpretation.

There are no other standards or amendments or interpretations to existing standards issued but not yet effective which are expected to have a material impact on our consolidated financial statements.

5. RESTRICTED CASH

	Note	December 31, 2018 \$	December 31, 2017 \$
Debt service reserve fund	14(b)	3,669	3,624
Funds held in escrow from business disposal	11	4,467	4,146
Other		20	20
		8,156	7,790

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6. TRADE ACCOUNTS RECEIVABLE

	December 31, 2018 \$	December 31, 2017 \$
Trade accounts receivable	10,225	6,245

During the year ended December 31, 2018, the Company had minimal expected credit losses (Note 26).

7. OTHER ACCOUNTS RECEIVABLE

	Note	December 31, 2018 \$	December 31, 2017 \$
Refundable sales tax		3,813	5,138
Government grants	21	1,016	1,790
Other		877	513
Other accounts receivable		5,706	7,441

8. INVENTORIES

	December 31, 2018 \$	December 31, 2017 \$
Raw materials and supplies	18,047	27,162
Work in progress	459	617
Finished goods	6,896	3,369
Inventory	25,402	31,148

The cost of raw materials, purchased materials and change in inventory recognized as expenses included in cost of products sold amounted to \$95,833 (2017: \$84,164).

The inventory write-down to record finished goods inventory at the lower of cost and net realizable value at December 31, 2018 was \$249 (2017: \$598).

The carrying amount of inventories pledged as security amounted to \$25,402 (2017: \$31,148).

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9. FINANCIAL INSTRUMENTS

The Company's cash and cash equivalents, restricted cash, trade accounts receivable, other accounts receivable, other long-term receivable, accounts payable and accrued liabilities, and long term debt are measured at amortized cost subsequent to initial measurement. Marketable securities and derivative financial instruments are measured at fair value through profit and loss in accordance with IFRS 9, *Financial Instruments: Classification and Measurement* and IFRS 13, *Fair Value Measurement*, which requires the classification of financial instruments within a hierarchy that prioritizes the inputs to fair value measurement. The Company uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates.

The three levels of the fair value hierarchy are:

Level 1 – Quoted prices (unadjusted) 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 unobservable for the asset or liability.

The following table summarizes the Company's financial instruments measured at fair value at December 31, 2018 and December 31, 2017, and shows the level within the fair value hierarchy in which they have been classified:

	Fair Value Hierarchy Level	December 31, 2018 \$	December 31, 2017 \$
Derivative financial instruments – FVTPL	Level 2	(1,455)	176
Total financial instruments		(1,455)	176

The following table summarizes the (loss) gain on financial instruments for the years ended December 31, 2018 and December 31, 2017:

	December 31, 2018 \$	December 31, 2017 \$
US dollar collars and variable rate forwards	(1,534)	962
Gain on financial instruments	(1,534)	962

The Company had the following foreign exchange derivatives at December 31, 2018 and December 31, 2017:

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	December 31, 2018		December 31, 2017	
	Notional Amount US dollars	Exchange Rates protection/ topside, per dollar	Notional Amount US dollars	Exchange Rates protection/ topside, per dollar
US dollar variable rate forwards				
0-12 Months	37,500	1.31/1.37	11,000	1.26/1.32

10. BUSINESS ACQUISITION

On March 26, 2018, the Company acquired all of the issued and outstanding common shares of S2G Biochemicals Inc. ("S2G"), a chemical engineering and technology company, for the purchase price of \$2,400 paid through the issuance of 666,652 (Note 17) common shares of the Company. The purchase price was calculated using the closing share price of the Company's common shares on the date of acquisition. Through a newly formed subsidiary, the Company intends to commission the construction of a demonstration plant to produce xylitol at its Fortress Specialty Cellulose Mill.

The recognition of assets acquired and liabilities assumed is based upon estimated fair values at the date of acquisition. Fair values are estimated using market information where applicable; however, directly comparable information is not always readily available so significant estimates and judgments are used.

The Company has recorded an intangible asset for the proprietary process technologies and license, know-how and expertise acquired. Management has determined that the intangible asset is indefinite-lived as it is not currently available-for-use and further activities are necessary before economic benefits will result. The acquisition has been accounted for as follows:

	Note	March 26, 2018 \$
Assets acquired at fair values		
Cash		59
Restricted cash		11
Prepaid expenses		17
Intangible assets		2,404
		2,491
Liabilities acquired at fair values		
Accounts payable and accrued liabilities		91
Net assets acquired at fair values		2,400
Consideration paid		2,400

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11. DISPOSAL OF BUSINESS

On December 20, 2017, the Company sold all of the shares of its wholly owned subsidiaries Landqart AG (the “Landqart mill”) and Landqart Management and Services AG which represents the entire security paper products segment of the Company, for an aggregate purchase price of 21,500 CHF.

Based on the book values of the net assets disposed of, the related sales proceeds, and the effect of foreign exchange, the loss on disposal of the Landqart Mill is \$56,558, as summarized below.

	December 20, 2017 \$
Book value of net assets disposed of	80,067
Sale proceeds	
Cash	27,694
Less: directly attributable costs	(526)
Total net proceeds	27,168
Loss on disposal before cumulative translation adjustment	52,899
Cumulative translation adjustment	3,659
Loss on disposal	56,558

With the sale of the Landqart mill, the Company no longer holds a defined benefit pension plan. The results for the period ended December 31, 2017 have been reclassified in the statement of operations as discontinued operations. The results of the discontinued operations are as follows:

	December 31, 2017 \$
Sales from discontinued operations	132,535
Costs and expenses from discontinued operations	(136,371)
Net loss before income taxes and loss on disposal	(3,836)
Income taxes	–
Loss on disposal	(56,558)
Net loss from discontinued operations	(60,394)
Basic and diluted net loss per share	(4.23)

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12. PROPERTY, PLANT AND EQUIPMENT

	2018				
	Land	Building	Equipment	Work in Progress	Total
	\$	\$	\$	\$	\$
At December 31, 2017					
Cost	1,196	134,371	260,335	7,847	403,749
Accumulated amortization	–	(29,537)	(80,688)	–	(110,225)
Net book value	1,196	104,834	179,647	7,847	293,524
Year ended December 31, 2018					
Additions	–	–	4,493	5,331	9,824
Transfers	–	838	8,653	(9,491)	–
Amortization	–	(4,034)	(18,098)	–	(22,132)
Net book value	1,196	101,638	174,695	3,687	281,216
At December 31, 2018					
Cost	1,196	135,209	273,481	3,687	413,573
Accumulated amortization	–	(33,571)	(98,786)	–	(132,357)
Net book value	1,196	101,638	174,695	3,687	281,216
	2017				
	Land	Building	Equipment	Work in Progress	Total
	\$	\$	\$	\$	\$
At December 31, 2016					
Cost	1,442	135,631	342,104	10,089	489,266
Accumulated amortization	–	(26,048)	(117,929)	–	(143,977)
Net book value	1,442	109,583	224,175	10,089	345,289
Year ended December 31, 2017					
Additions	–	–	7,787	27,527	35,314
Disposals	–	–	(362)	–	(362)
Transfers	–	3,317	25,161	(28,478)	–
Amortization	–	(4,197)	(25,957)	–	(30,154)
Disposal of business (Note 11)	(242)	(3,880)	(50,448)	(1,043)	(55,613)
Exchange differences	(4)	11	(709)	(248)	(950)
Net book value	1,196	104,834	179,647	7,847	293,524
At December 31, 2017					
Cost	1,196	134,371	260,335	7,847	403,749
Accumulated amortization	–	(29,537)	(80,688)	–	(110,225)
Net book value	1,196	104,834	179,647	7,847	293,524

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Property, plant and equipment pledged as security for loans and mortgages amounted to \$281,216 (2017: \$293,524) (Note 14).

During the year ended December 31, 2018, the Company sold non-core assets at the Fortress Specialty Cellulose mill for \$nil (2017: \$680). The carrying amount of the assets sold was \$nil (2017: \$nil), with a resulting net gain of \$nil (2017: \$680).

Impairment of property, plant and equipment

In accordance with the Company's accounting policy, each asset or cash generating unit is evaluated at each reporting date to determine whether there are any indicators of impairment. If any such indication exists, a formal estimate of recoverable amount is performed and an impairment loss is recognized to the extent that the carrying amount exceeds the recoverable amount. The recoverable amount has been determined by the Company as the value in use.

The determination of value in use requires management to make estimates and assumptions about expected production and sales volumes, prices, operating costs, capital expenditures, and appropriate discount rates for future cash flows. The estimate and assumptions are subject to risk and uncertainty, and as such there is the possibility that changes in circumstances will alter these projections, which may impact the recoverable amount of the assets. In such circumstances, some or all of the carrying value of the assets may be further impaired or the impairment charge reduced with the impact recorded in the statement of operations.

As at December 31, 2018, the Company's market capitalization was lower than the carrying amount of its net assets. Management of the Company determined that this constituted an impairment indicator and completed an impairment assessment of the Fortress Specialty Cellulose mill.

An impairment assessment model for the Fortress Specialty Cellulose mill included the following assumptions:

- Operating costs based on historical costs incurred and estimated forecasts.
- Production volumes based on expected production compared to industry normal utilization rates.
- Efficiencies and production increases from future planned capital projects were not included.
- Dissolving pulp pricing based on externally available pricing forecasts.
- Discount rates reflecting the risks involved.

Key sensitivities for inputs in the impairment assessment model for the Fortress Specialty Cellulose mill, assuming all other variables are held constant, are as follows:

- For each 1% change in the price of dissolving pulp, the calculated fair value of the cash generating unit changes by approximately \$18,440.
- For each \$0.01 change in the Canadian dollar when compared to the United States dollar, the calculated fair value of the cash generating unit changes by approximately \$22,544.
- For each 1% change in the discount rate, the calculated fair value of the cash generating unit changes by approximately \$46,870.

Management's impairment evaluation did not result in the identification of an impairment loss at the Fortress Specialty Cellulose mill as at December 31, 2018.

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13. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

		December 31, 2018 \$	December 31, 2017 \$
	Note		
Trade payable and accrued liabilities		25,477	45,254
Accrued payroll and related liabilities		4,748	2,555
Customer prepayments		4,055	1,437
Landfill and environmental remediation	16	862	995
		35,142	50,241

14. LONG-TERM DEBT

		December 31, 2018 \$	December 31, 2017 \$
	Note		
Credit facilities with lenders			
\$103,879 (2017: \$99,469), interest at 5%, maturing 2026, secured by the assets of the Fortress Specialty Cellulose mill, maturing December 2026	14(a)	117,413	111,469
\$34,675 (2017: \$37,532) interest and fees at 6.5%, maturing 2031, secured by certain assets of the Fortress Specialty Cellulose mill	14(b)	33,598	36,303
US\$nil (2017: \$2,497) interest at LIBOR plus 5.75%, secured by certain inventory of the Fortress Specialty Cellulose mill	14(c)	–	3,133
Unsecured convertible debentures			
\$62,100 (2017: \$62,100) principal, interest at 9.75%, maturing December 2021	14(d)	58,330	58,330
		209,341	209,235
Less: current portion		(14,225)	(14,516)
Long-term debt		195,116	194,719
		December 31, 2018 \$	December 31, 2017 \$
Principal value of debt		200,654	202,233
Adjustments for unamortized borrowing costs, amounts allocated to equity for convertible debentures, and expected contingent payments		8,687	7,002
Net amount recorded in liabilities		209,341	209,235

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Principal repayments as at December 31, 2018 are required as follows:

	(\$ 000's)
2019	14,225
2020	14,225
2021	76,325
2022	14,225
2023	14,225
Thereafter	67,429
	200,654

Although there can be no assurances, the Company believes that current cash, cash generated from operations, cashflow derived from improved inventory and cash management, alternative financing arrangements, and other cash generating initiatives, should be sufficient to meet its debt service, capital expenditure and short term working capital requirements. The Company's future operating performance and its ability to service its debt and pay other indebtedness will be subject to future economic conditions and the operating financial success of the Company's business, including achieving planned levels of production and other factors which may not be within the Company's control, such as the receipt of necessary permits, changes in market prices for its dissolving pulp and raw material costs.

At December 31, 2018, the fair value of the long-term debt, measured at its amortized cost of \$209,341 was \$198,206. The fair value was determined based on prevailing market rates for long-term debt with similar characteristics and risk profile.

Borrowings under the above agreements require maintenance of subsidiary specific minimum working capital ratios, maximum long-term debt to adjusted net worth ratios, and certain non-financial covenants. The Company has been in compliance with all covenants for all periods presented.

At December 31, 2018, the Company's current portion of long term debt, accounts payable and accrued liabilities totaled \$49,367, all of which fall due for payment within one year of the statement of financial position date. If necessary, the Company has the ability to repay principal amounts outstanding, subject to receiving requisite approvals, of the \$62,100 of convertible debentures due in 2021, in common shares of the Company.

- (a) During the twelve months ended December 31, 2018, the Company entered into an amendment with a lender to which three quarterly principal payments payable in 2018 totaling \$8,523 have been deferred, without penalty or interest accruing on such amounts. Quarterly payments of \$2,842 will resume on March 31, 2019 (Note 27). This amendment resulted in a reduction in the current portion of long-term debt and an increase in long-term debt by the amount of the principal deferred. Twelve monthly interest payments for the period January 1, 2018 to December 31, 2018, totaling \$4,411 (Note 19) will be accruing on the outstanding principal amount and such accrued interest will not bear interest during this period. Commencing on March 31, 2019, the same quarterly principal payments will resume with a lump sum payment due on maturity. The amendment was subject to a condition to be satisfied by the end of August 2018, which the Company has fulfilled. The Company recorded a gain of \$4,075 in finance income in relation to the amendment.
- (b) During the year ended December 31, 2017, the Company entered into an agreement with a new lender for a

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\$40,000 secured loan. The loan matures in 14 years from the advance date of February 2, 2017, and is repayable in monthly payments of principal and interest over the term. The loan accrues interest at a rate of 6% per annum plus an account maintenance fee of 0.5% per annum. Security for the loan includes a charge against the cogeneration assets of the Dissolving Pulp segment and guarantees from Fortress Specialty Cellulose and Fortress Global Enterprises. The Company was required to set up a debt service reserve fund consisting of nine months of principal and interest payments. The Company has recorded \$3,669 in restricted cash in relation to the fund. In connection with the loan, which is held by a wholly owned subsidiary, a distribution test must be met for the cash held by the subsidiary to be available within the group. There are no restrictions on the cash for use within the subsidiary. As at December 31, 2018, the cash and cash equivalents balance of the subsidiary was \$4,298.

- (c) During the year ended December 31, 2017, the Company entered into a credit agreement with a private arm's length lender for a secured revolving credit facility in the principal amount of up to US\$5,000 as determined by the balance of certain eligible inventory. The loan will mature on December 30, 2020 and will accrue interest at a rate of LIBOR plus 5.75% per annum. The loan is secured by certain inventory located at the Fortress Specialty Cellulose mill.
- (d) During the year ended December 31, 2018, the Company amended its convertible debentures in the principal amount of \$62,100 due in 2019. The Company extended the maturity date of the debentures from December 31, 2019 to December 31, 2021 and increased the interest rate on the debentures from 7.0% to 9.75% per annum, effective January 1, 2019. The Company accounted for the amendments as a modification to the existing debentures which resulted in a loss of \$898 in the year ended December 31, 2018, and an additional \$1,708 in interest per annum beginning in 2019.

15. INCOME TAXES

The analysis of deferred tax assets and deferred tax liabilities is as follows:

	December 31, 2018 \$	December 31, 2017 \$
Deferred tax assets:		
Deferred tax asset to be recovered after more than 12 months	37,518	44,466
Deferred tax asset to be recovered within 12 months	2,605	3,107
	40,123	47,573
Deferred tax liabilities:		
Deferred tax liability to be reversed after more than 12 months	(37,518)	(44,466)
Deferred tax liability to be reversed within 12 months	(2,605)	(3,107)
	(40,123)	(47,573)
Deferred net tax liability	–	–

The movement in deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

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	December 31, 2018 \$	December 31, 2017 \$
Deferred tax assets		
Tax credits	4,659	4,659
Tax loss carryforwards	21,127	30,521
Other	14,337	12,393
	40,123	47,573
Deferred tax liabilities		
Property, plant and equipment	(31,293)	(38,778)
Long-term debt	(1,019)	(1,065)
Other	(7,811)	(7,730)
	(40,123)	(47,573)
Deferred net tax liability	–	–

Deferred income tax assets are recognized for tax loss carry-forwards and other tax credits to the extent that the realization of the related tax benefit through future taxable profits is probable. The Company did not recognize deferred tax assets of \$71,855 in 2018 (2017: \$60,874). Tax loss carry-forwards consist of approximately \$367,226 which expire beginning in 2028 through 2038.

The components of income tax (recovery) expense for operations are as follows:

	Year Ended December 31, 2018 \$	Year Ended December 31, 2017 \$
Current	–	(3)
Deferred	–	–
	–	(3)

Included in income tax (recovery) expense is income tax expense (recovery) related to discontinued operations of \$nil for 2018 (2017: \$nil).

The reconciliation of income taxes calculated at the statutory rate of 27% (2017: 27%) to the actual income tax provision is as follows:

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	Year Ended December 31, 2018 \$	Year Ended December 31, 2017 \$
Net loss before taxes	(32,180)	(93,385)
Income tax recovery at statutory rates	(8,689)	(25,214)
Stock-based compensation and other non-deductible expenses	557	278
Rate differentials between foreign jurisdictions, capital gains and future tax rates	682	(128)
Undistributed earnings of subsidiary	–	3,038
Change in deferred tax assets not recognized	7,450	22,023
Income tax (recovery) expense	–	(3)

16. PROVISIONS AND OTHER LONG-TERM LIABILITIES

	Note	December 31, 2018 \$	December 31, 2017 \$
Provisions			
Landfills		1,197	1,235
		1,197	1,235
Long-term liabilities			
Employment agreement obligation	23	–	2,689
Guarantee	22	–	7,000
Other long-term liabilities		203	–
		1,400	10,924
Less: current portion included in accounts payable and accrued liabilities	13	(862)	(995)
Total provisions and other long-term liabilities		538	9,929

Landfills

The Company has costs associated with containment and ongoing maintenance relating to landfill sites in Canada. These costs are measured at fair value, which approximates the cost a third party would incur in performing the tasks associated with the landfill sites. These obligations represent estimated undiscounted future payments of \$1,197 to remediate the landfills at the end of their useful lives.

The following table reflects changes in the provision for the landfill related provisions:

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	December 31, 2018 \$	December 31, 2017 \$
Opening balance	1,235	393
Estimated costs of capping landfills	320	842
Landfill maintenance payments	(358)	–
Balance at end of year	1,197	1,235
Less: current portion included in accounts payable	(862)	(995)
Long-term landfill related provisions	335	240

17. SHARE CAPITAL

Authorized

Unlimited number of common shares without par value
Unlimited number of preferred shares with par value \$1,000

Issued and fully paid — common shares

	Number of Shares	Share Capital \$
Balance, December 31, 2016	14,286,092	175,445
Restricted share units vested	66,074	169
Exercise of stock options	1,915	371
Repurchase of common shares	(104,468)	(1,281)
Balance, December 31, 2017	14,249,613	174,704
Shares issued on business acquisition	666,652	2,400
Restricted share units vested	33,630	92
Balance, December 31, 2018	14,949,895	177,196

Repurchase of common shares

During the year ended December 31, 2017, the Company repurchased and cancelled 104,468 common shares for \$621 through a normal course issuer bid which has since expired.

18. STOCK-BASED COMPENSATION

During 2016, the Company adopted a stock incentive plan. The exercise price of options granted under the stock option plan shall be as determined by the Board of Directors when such options are granted, subject to any limitations imposed by any relevant stock exchange or regulatory authority.

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At the Company's annual general meeting held April 21, 2016, shareholders approved a long-term incentive plan which provides for the grant of restricted share units, performance share units and deferred share units to key employees and directors of the Company.

The aggregate number of shares issuable under the long-term incentive plan and stock incentive plan in respect of awards, together with shares reserved for issuance under all of the Company's other security-based compensation arrangements, shall not exceed ten percent of the Company's issued and outstanding shares.

Stock Options

During the year ended December 31, 2018, the Company granted 21,403 (2017: 305,658) stock options to employees of the Company. The Company valued the options using the Black Scholes pricing model which requires the input of highly subjective assumptions including the expected volatility. Expected volatility is based on the Company's stock performance. Changes in assumptions can affect the fair value estimate, and, therefore, does not necessarily provide a reliable measure of the fair value of the Company's stock options. Assumptions used in the pricing model are as follows:

	2018
Risk-free interest rate	1.97%
Expected life of options	5 years
Annualized volatility	64.4%
Weighted average fair value	1.93
Dividend rate	Nil

Stock option transactions and the number of stock options outstanding are summarized as follows:

	Number of Options	Weighted Average Exercise Price \$
Balance, December 31, 2016	590,725	10.51
Granted	305,658	6.55
Expired	(103,575)	8.00
Cancelled	(169,800)	8.00
Exercised	(117,350)	8.00
Balance, December 31, 2017	505,658	10.05
Granted	21,403	3.50
Balance, December 31, 2018	527,061	9.79

The following table summarizes stock options outstanding as at December 31, 2018:

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Exercise Price	Number Outstanding as at December 31, 2018	Weighted Average Remaining Life of Outstanding Options (Years)	Number Exercisable as at December 31, 2018	Weighted Average Remaining Life of Exercisable Options (Years)
\$				
15.41	200,000	3.66	200,000	3.66
5.10	20,000	3.64	6,666	3.64
8.20	84,150	3.22	-	-
6.00	201,508	3.37	-	-
3.50	21,403	4.21	-	-
	527,061	3.50	206,666	3.66

The following table summarizes stock options outstanding as at December 31, 2017:

Exercise Price	Number Outstanding as at December 31, 2017	Weighted Average Remaining Life of Outstanding Options (Years)	Number Exercisable as at December 31, 2017	Weighted Average Remaining Life of Exercisable Options (Years)
\$				
15.41	200,000	4.66	200,000	4.66
5.10	20,000	4.64	-	-
8.20	84,150	4.22	-	-
6.00	201,508	4.37	-	-
	505,658	4.47	200,000	4.66

Deferred Share Unit Awards

A deferred share unit ("DSU") is a right granted to a non-employee director to receive one common share of the Company, from treasury, on a deferred basis. The value of the DSUs, when redeemed, is equal to the market value of the shares on the redemption date, including the value of dividends paid on the Company's common shares, if any, as if they had been reinvested in additional DSUs on each payment date. The DSUs may only be redeemed upon a director's retirement from the Company. The Company recognizes the expense at the time of grant.

DSU transactions and the number of DSUs outstanding are summarized as follows:

	Number of DSUs	Expense Recognized \$
Balance, December 31, 2016	243,795	6,524
Granted	32,717	214
Balance, December 31, 2017	276,512	6,738
Granted	119,367	360
Balance, December 31, 2018	395,879	7,098

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Restricted Share Unit Awards

A restricted share unit ("RSU") is a right granted to a key employee to receive one common share of the Company, from treasury, on a time vested basis. The fair value of restricted share awards is determined based upon the number of shares granted and the quoted price of the Company's stock on the date of grant. Restricted shares generally vest over three to five years.

RSU transactions and the number of RSUs outstanding are summarized as follows:

	Number of RSUs
Balance, December 31, 2016	160,761
Granted	8,711
Vested	(66,074)
Cancelled	(26,114)
Balance, December 31, 2017	77,284
Granted	65,542
Vested	(33,630)
Cancelled	(9,108)
Balance, December 31, 2018	100,088

19. FINANCE INCOME AND EXPENSE

	Note	December 31, 2018 \$	December 31, 2017 \$
Finance expense:			
Long-term debt interest		6,817	8,884
Capitalised interest	14(a)	4,411	-
Accretion and other		10,577	7,105
Convertible debt amendment	14(d)	898	-
Total finance expense		22,703	15,989
Finance income:			
Debt amendment	14(a)	(4,075)	(2,624)
Interest on short-term bank deposits and long-term receivable		(330)	(232)
Net finance expense		18,298	13,133

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20. EARNINGS PER SHARE

a) Basic

Basic loss per share, is calculated by dividing the net loss from continuing operations attributable to equity holders of the Company by the weighted average number of common shares outstanding during the year.

	2018	2017
Net loss from continuing operations	(32,180)	(32,988)
Weighted average number of common shares outstanding	14,795,924	14,283,747

b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of common shares outstanding to assume conversion of all dilutive potential common shares. The Company has five categories of dilutive potential common shares: convertible debt, stock options, warrants, RSUs and DSUs. The convertible debt is assumed to have been converted into common shares, and the net income is adjusted to eliminate the interest expense less the tax effect. For the stock options, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding stock options. The number of shares calculated reduces the number of shares that would have been issued assuming the exercise of the share options. RSUs and DSUs are assumed to be converted as of the grant date.

A total of 2,951,885 (2017: 2,969,810) instruments, which include convertible debt, stock options, restricted share units and deferred share units have not been included in the calculation for diluted loss per share as they are antidilutive. These could potentially dilute basic earnings per share in the future.

21. GOVERNMENT GRANTS

During the year ended December 31, 2018, the Company received \$6,126 (2017: \$8,475) and recorded a receivable for \$1,016 (2017: \$1,790) as at December 31, 2018 in non-repayable government grant contributions from the governments of Canada and Québec. The grants received have reduced additions to property, plant and equipment.

22. COMMITMENTS

During the year ended December 31, 2018, the Company was released from a guarantee previously provided on a secured note receivable that was transferred to a lender in 2017 as early repayment of a portion of the principal amount outstanding. As a result, the Company recorded a decrease of \$7,000 to both other accounts receivable and provisions and other long-term liabilities.

As at December 31, 2018, the Company has issued guaranteed letters of credit of \$1,070 relating to the continued delivery of power at our cogeneration facility and \$400 relating to suppliers. The Company has a performance security guarantee of up to \$2,500 million for derivative financial instruments.

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As at December 31 2018, the Company has committed to purchase \$76 in property, plant, and equipment.

Operating lease commitments for land, buildings, equipment, storage, and offices over the next five years and thereafter are as follows:

	\$
2019	758
2020	447
2021	–
2022	–
2023	–
Thereafter	–
	1,205

23. RELATED PARTIES

The remuneration of directors and other key management personnel was as follows:

	December 31, 2018 \$	December 31, 2017 \$
Salaries and other short-term employee benefits	2,922	3,486
Share-based awards	600	1,153
Total	3,522	4,639

As at December 31, 2018, the Company has accrued \$2,000 (2016: \$2,689) under an employment agreement for certain executive management.

As at December 31, 2018, in addition to the amounts related to certain executive management, there was \$284 in amounts owing to directors and other key management personnel included in accounts payable and accrued liabilities (2017: \$315).

24. SEGMENTED INFORMATION

The segmentation of the Company's manufacturing operations is based on a number of factors, including production and economic characteristics. Up until December 20, 2017, the Landqart mill produced security papers and products. Fortress Specialty Cellulose produces dissolving pulp products. S2G is developing a demonstration plant for the production of xylitol at the Fortress Specialty Cellulose mill and has been included in the Bioproducts segment.

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Year ended December 31, 2018				
	Bioproducts	Pulp	Corporate	Fortress Global Consolidated
	\$	\$	\$	\$
Sales	–	185,945	–	185,945
Operating loss	(1,734)	(2,653)	(5,745)	(10,132)
Amortization ¹	–	(22,132)	–	(22,132)
Stock-based compensation ¹	–	–	427	427
Capital expenditures	–	9,824	–	9,824
Total assets	2,634	335,509	8,170	346,313

Sales by geographic area	%
Asia	88.5
Canada ²	11.5
Total	100.0

¹Stock-based compensation and amortization are included in operating loss.

²Canadian sales are from the cogeneration facility.

Year ended December 31, 2017					
	Pulp	Corporate	Continuing Operations	Discontinued Operations (Security)	Fortress Global Consolidated
	\$	\$	\$	\$	\$
Sales	156,414	–	156,414	132,535	288,949
Operating loss	(18,836)	(7,667)	(26,503)	(7,042)	(33,545)
Amortization ¹	(21,842)	–	(21,842)	(8,312)	30,154)
Stock-based compensation ¹	–	(978)	(978)	–	(978)
Capital expenditures	25,738	–	25,738	9,578	35,316
Total assets	356,969	37,738	394,707	–	394,707

Sales by geographic area	%	%	%
Europe	–	21.1	9.7
Asia	87.5	78.1	83.2
Canada ²	12.5	–	6.7
Other	–	0.8	0.4
Total	100.0	100.0	100.0

¹Stock-based compensation and amortization are included in operating loss.

²Canadian sales are from the cogeneration facility.

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	December 31, 2018 \$	December 31, 2017 \$
Property, plant and equipment by location		
Canada	281,216	293,524
Intangible asset by location		
Canada	2,404	–

25. SUPPLEMENTAL CASH FLOW INFORMATION

Changes in Liabilities arising from Financing Activities

	January 1, 2018 \$	Cash flows	Interest + Accretion	Non-cash changes Change in cash flow	Business disposal	Foreign Exchange	December 31, 2018 \$
Long-term debt	150,905	(8,344)	12,525	(4,075)	–	–	151,011
Convertible debt	58,330	(4,347)	6,313	(1,966)	–	–	58,330
	209,235	(12,691)	18,838	(6,041)	–	–	209,341

	January 1, 2017 \$	Cash flows	Interest + Accretion	Non-cash changes Change in cash flow	Business disposal	Foreign Exchange	December 31, 2017 \$
Long-term debt	116,434	35,432	7,745	(2,555)	(5,985)	(166)	150,905
Convertible debt	81,346	(29,514)	6,498	–	–	–	58,330
	197,780	5,918	14,243	(2,555)	(5,985)	(166)	209,235

Non Cash Financing and Investing Activities

During the year ended December 31, 2018, the Company issued 666,652 common shares as consideration in a business acquisition (Note 10).

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26. FINANCIAL RISK MANAGEMENT

a. Financial risk factors

The Company's activities expose it to a variety of financial risks: credit risk, liquidity risk and market risk.

Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk is managed on a Company basis, except for credit risk relating to accounts receivable balances. Each local entity is responsible for managing and analyzing the credit risk for each of their new clients before standard payment and delivery terms and conditions are offered. Credit risk arises from cash and cash equivalents, and deposits with banks and financial institutions, as well as credit exposures to customers.

Cash and cash equivalents include cash on deposit and cash equivalents with an original maturity date of 90 days or less. 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 December 31, 2018 was \$12,608 (2017: \$40,877).

The Company utilizes credit insurance to manage the risk associated with trade receivables. Approximately all of the outstanding trade receivables are covered under credit insurance or backed by letters of credit. The majority of the balance is with large and financially sound customers. The Company sells all pulp through a third party agent that takes ownership of the inventory before it is delivered to the final customer. Accounts receivable aged greater than 90 days are \$nil of which \$nil is provided for as potentially impaired. The Company's trade receivable balance at December 31, 2018 was \$10,225 (2017: \$6,245). At December 31, 2018, approximately, all of the trade accounts receivable balance was within the Company's established credit terms.

Liquidity Risk

Liquidity risk is the risk that the Company will be unable to meet its financial obligations as they fall due. Cash flow forecasting is performed in the operating entities of the Company and aggregated by Company finance. Company finance monitors rolling forecasts of the Company's liquidity requirements to ensure it has sufficient cash to meet operational needs while not breaching borrowing limits or covenants. The Company manages liquidity risk through management of its capital structure in conjunction with cash flow forecasting including anticipated investing and financing activities. The Company manages liquidity risk through ongoing review of accounts receivable balances and the management of its cash and debt positions.

At December 31, 2018, the Company's current portion of long term debt, accounts payable and accrued liabilities totaled \$49,367 (2017: \$64,757), all of which fall due for payment within one year of the statement of financial position date. If necessary, the Company has the ability to pay the interest and repay principal amounts outstanding, subject to receiving requisite approvals, of the \$62,100 of convertible debentures due in 2021, in common shares of the Company.

Although there can be no assurances, Fortress believes that current cash, cash generated from operations, and cash from the sale of non-core assets, and other strategic initiatives, should be sufficient to meet its debt service, capital expenditure and short term working capital requirements for the next year. Fortress' future operating performance and its ability to service its debt and pay other indebtedness of Fortress will be subject to future economic conditions and the financial success of Fortress' business and other factors, many

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of which are not within Fortress' control, including changes in market prices for its dissolving pulp and raw material costs.

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.

Currency risk:

The Company is exposed to foreign exchange risk primarily in United States dollars ("USD"). The Company's products are sold globally with prices denominated primarily in United States dollars. The majority of the Company's expenditures are denominated in Canadian dollars. The Company holds derivative financial instruments to help mitigate currency risk for USD (Note 9).

An increase in the value of the Canadian dollar by \$0.01 when compared to the USD would result in a pre-tax loss of approximately \$26 in relation to working capital balances held by Canadian entities denominated in USD at December 31, 2018 (including cash, accounts receivable, and accounts payable).

Sensitivity analysis:

The Company has completed a sensitivity analysis to estimate the impact on operating income for the year that a change in foreign exchange rates or interest rates during the year ended December 31, 2018 would have had.

This sensitivity analysis includes the following assumptions:

- Changes in individual foreign exchange rates do not cause foreign exchange in other countries to alter
- Changes in market interest rates do not cause a change in foreign exchange rates

The results of the foreign exchange sensitivity analysis on operations can be seen in the following table:

	Decrease in operating income \$
Change in Canadian dollar exchange rate	
Strengthening of 1% compared to USD foreign exchange rate	1,614

The above results arise due to the impact of foreign currency fluctuations on operations for transactions denominated in USD. Fortress will continue to monitor and evaluate the future use of exchange contracts to limit exposure to exchange fluctuations.

Changes in market interest rates would have no significant impact on operating income.

Limitations of sensitivity analysis

The financial position of the Company may vary at the time that a change in the factors occurs, causing the impact on the Company's results to differ from that shown above.

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Commodity risk:

The Company's financial performance is dependent on the selling price of its products and the purchase of raw material inputs. Therefore, the Company is exposed to changes in commodity prices for dissolving pulp, as well as changes in fibre, chemical and energy prices. The market for dissolving pulp is cyclical and can be impacted by a variety of factors, including but not limited to excess supply due to industry capacity, periods of decreased demand due to weak global economic activity and fluctuations in currency exchange rates. A reduction in pricing can result in reduced revenue and margins, which adversely impact the Company's financial results.

b. Capital management

The Company's objectives when managing capital are to safeguard its assets and maintain a globally competitive cost structure while looking for growth opportunities to provide returns to its shareholders. In addition, the Company works with all relevant stakeholders to ensure the safety of its operations and employees, and remain in compliance with all environmental regulations.

The Company continuously monitors and assesses its financial performance in order to ensure that its net debt levels are prudent taking into account the anticipated direction of the business cycle. The Company continuously monitors the public and private debt markets and the public equity markets in order to assure that its capital structure is appropriately balanced. The Company can be materially influenced by changes in the relative value of the Canadian dollar and American dollar.

The Company's capital comprises net debt and shareholders' equity:

	December 31, 2018 \$	December 31, 2017 \$
Cash and cash equivalents	12,608	40,877
Less total debt	209,341	209,235
Net debt	(196,733)	(168,358)
Shareholders' equity	99,837	125,302

The Company has certain financial covenants stipulating maximum long-term debt to adjusted net worth ratios and minimum working capital ratios. Debt obligations are held by various entities within the Company with individual debt agreements specifying the entities within the Company that are to be included in the covenant calculations.

The Company's strategy is to ensure it remains in compliance with all of its existing debt covenants in order to ensure continuous access to capital. Management reviews past results and forecasts to monitor their compliance. The Company was in compliance with all externally imposed capital requirements for the years ended December 31, 2018 and December 31, 2017.

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27. SUBSEQUENT EVENTS

Subsequent to the year ended December 31, 2018, the Company entered into an amendment with a lender to which the quarterly principal payment due March 31, 2019, totaling \$2,841 will be due on maturity of the loan in December 2026. The interest payable from January 1, 2019 to March 31, 2019, totaling \$1,341, will be capitalized and added to the outstanding balance of the loan. The next principal and interest payment will be due on June 30, 2019, and interest and principal will be payable on a quarterly basis thereafter.