

*Condensed consolidated interim financial report*  
**FIBREK INC.**

*Three and nine-months ended September 30, 2011*

(unaudited)

# **FIBREK INC.**

## **Table of contents**

---

Condensed consolidated interim statements of earnings.....	<b>1</b>
Condensed consolidated interim statements of comprehensive income .....	<b>2</b>
Condensed consolidated statements of financial position.....	<b>3</b>
Condensed consolidated interim statements of changes in equity .....	<b>4</b>
Condensed consolidated interim statements of cash flows .....	<b>5</b>
Notes to the condensed consolidated interim financial report .....	<b>6- 45</b>

# FIBREK INC.

## Condensed consolidated interim statements of earnings periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
<b>Sales</b>	<b>138,267</b>	132,177	<b>418,690</b>	425,085
Cost of products sold, including depreciation (Notes 5 and 19)	<b>120,476</b>	108,120	<b>356,851</b>	352,805
Delivery costs	<b>10,320</b>	9,695	<b>32,536</b>	31,391
Selling and administrative expenses (Note 19)	<b>3,681</b>	2,714	<b>11,204</b>	8,996
<b>Profit from operations</b>	<b>3,790</b>	11,648	<b>18,099</b>	31,893
Financial expenses (Note 17)	<b>2,361</b>	4,344	<b>8,860</b>	13,687
Financial income	<b>(11)</b>	(15)	<b>(180)</b>	(24)
Loss (gain) on financial instruments (Note 17)	<b>8</b>	(94)	<b>(3,549)</b>	3,231
Loss (gain) on disposal of property, plant and equipment	<b>9</b>	8	<b>86</b>	(5)
(Gain) loss on foreign currency translation (Note 17)	<b>(5,350)</b>	2,055	<b>(2,998)</b>	979
<b>Earnings before income taxes</b>	<b>6,773</b>	5,350	<b>15,880</b>	14,025
(Recovery of) provision for income taxes (Note 14)	-	(5)	<b>14</b>	(5)
<b>Net earnings</b>	<b>6,773</b>	5,355	<b>15,866</b>	14,030

### Per share information (Note 13)

	Earnings per share			
	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Basic	<b>0.05</b>	0.04	<b>0.12</b>	0.14
Diluted	<b>0.05</b>	0.04	<b>0.12</b>	0.10

The accompanying notes are an integral part of this condensed consolidated interim financial report.

## **FIBREK INC.**

### **Condensed consolidated interim statements of comprehensive income**

**periods ended September 30, 2011 and 2010**

**(in thousands of Canadian dollars)**

**(unaudited)**

	Three months ended September 30,		Nine months ended September 30,	
	<b>2011</b>	2010	<b>2011</b>	2010
	\$	\$	\$	\$
<b>Net earnings</b>	<b>6,773</b>	5,355	<b>15,866</b>	14,030
Other comprehensive gain (loss):				
Unrealized gain (loss) on translation of financial statements of foreign operations, net of tax effects of \$Nil, (2010- \$Nil)	<b>5,610</b>	(2,021)	<b>3,089</b>	(2,108)
Other comprehensive gain (loss)	<b>5,610</b>	(2,021)	<b>3,089</b>	(2,108)
<b>Comprehensive income</b>	<b>12,383</b>	3,334	<b>18,955</b>	11,922

The accompanying notes are an integral part of this condensed consolidated interim financial report.

# FIBREK INC.

## Condensed consolidated statements of financial position

as at September 30, 2011 and December 31, 2010

(in thousands of Canadian dollars)

(unaudited)

	September 30, 2011	December 31, 2010
<b>Assets</b>		
Current assets		
Cash and cash equivalents (Notes 8 and 16)	6,812	16,421
Accounts receivable (Note 4)	70,806	68,424
Inventories (Note 5)	100,014	77,187
Prepaid expenses	3,869	3,097
Investment at fair value through profit or loss (Note 17)	33	5,544
	<b>181,534</b>	<b>170,673</b>
Deferred financing fees (Note 11)	1,461	1,716
Property, plant and equipment (Note 6)	369,719	382,609
Intangible assets (Note 7)	206	239
Other assets	704	663
	<b>553,624</b>	<b>555,900</b>
<b>Liabilities</b>		
Current liabilities		
Accounts payable and accrued liabilities	71,480	56,092
Landfill closure liability (Note 8)	273	160
Current portion of long-term debt (Note 11)	1,997	1,876
Convertible unsecured subordinated debentures (Note 12)	-	49,609
	<b>73,750</b>	<b>107,737</b>
Landfill closure liability (Note 8)	2,161	1,731
Employee benefits (Note 9)	26,135	28,361
Long-term debt (Note 11)	101,003	82,798
	<b>203,049</b>	<b>220,627</b>
<b>Equity</b>		
Shareholders' capital (Note 13)	696,537	696,537
Equity Component of Debentures	-	4,188
Reserves	(1,223)	(4,847)
Deficit	(344,739)	(360,605)
	<b>350,575</b>	<b>335,273</b>
	<b>553,624</b>	<b>555,900</b>

The accompanying notes are an integral part of this condensed consolidated interim financial report.

Approved by the Board and authorized for issue on November 2, 2011.

(Signed) Hubert T. Lacroix, Director

(Signed) François R. Roy, Director

# FIBREK INC.

## Condensed consolidated interim statements of changes in equity periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars) (unaudited)

	Nine months ended September 30, 2011					Total
	Shareholders' capital (Note 13)	Reserves		Equity component of Debentures	Deficit	
		Unrealized loss on translation	Contributed surplus			
	\$	\$	\$	\$	\$	\$
Balance, December 31, 2010	696,537	(5,124)	277	4,188	(360,605)	335,273
Other comprehensive gain	-	3,089	-	-	-	3,089
Share-based compensation (Note 15)	-	-	535	-	-	535
Redemption of debentures (Note 12)	-	-	-	(4,188)	-	(4,188)
Net earnings	-	-	-	-	15,866	15,866
<b>Balance, September 30, 2011</b>	<b>696,537</b>	<b>(2,035)</b>	<b>812</b>	<b>-</b>	<b>(344,739)</b>	<b>350,575</b>

	Nine months ended September 30, 2010					Total
	Shareholders' capital (Note 13)	Reserves		Equity component of Debentures	Deficit	
		Unrealized loss on translation	Contributed surplus			
	\$	\$	\$	\$	\$	\$
Balance, January 1, 2010	658,609	-	-	-	(372,202)	286,407
Other comprehensive loss	-	(2,108)	-	-	-	(2,108)
Share-based compensation (Note 15)	-	-	160	-	-	160
Conversion into a corporation	-	-	-	4,188	-	4,188
Issuance of shares	37,928	-	-	-	-	37,928
Net earnings	-	-	-	-	14,030	14,030
<b>Balance, September 30, 2010</b>	<b>696,537</b>	<b>(2,108)</b>	<b>160</b>	<b>4,188</b>	<b>(358,172)</b>	<b>340,605</b>

The accompanying notes are an integral part of this condensed consolidated interim financial report.

# FIBREK INC.

## Condensed consolidated interim statements of cash flows

periods ended September 30, 2011 and 2010

(in thousands of Canadian dollars)

(unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
<b>Operating activities</b>				
Net earnings	6,773	5,355	15,866	14,030
Adjustments for:				
Depreciation of property, plant and equipment	8,573	8,396	26,609	25,865
Amortization of intangible assets	11	32	33	68
Financial expenses (Note 17)	2,361	4,344	8,860	13,687
Unrealized (gain) loss on translation of monetary items denominated in foreign currency	(746)	308	(443)	212
Employee benefits	(1,482)	(699)	(2,226)	(875)
Share-based compensation	194	114	535	160
Changes in landfill closure liability (Note 8)	467	95	432	458
Loss (gain) on disposal of property, plant and equipment	9	8	86	(5)
Loss (gain) on financial instruments	8	(94)	(3,549)	3,231
Restricted cash (Note 8)	(1)	4	(1)	3
Changes in non-cash operating working capital items (Note 16)	(2,319)	2,367	(13,595)	(212)
	<b>13,848</b>	<b>20,230</b>	<b>32,607</b>	<b>56,622</b>
<b>Financing activities</b>				
Borrowings under ABL Credit Facility	12,674	10,427	62,393	10,427
Borrowings under the term loan plan, net of financing fees	-	75,691	-	75,691
Refinancing fees	-	(1,302)	-	(2,026)
Share issuance costs	-	38,394	-	37,928
Reimbursement of long-term debt (including the ABL Credit Facility)	(25,617)	(155,904)	(45,829)	(156,700)
Redemption of convertible debentures (Note 12)	-	-	(51,749)	-
Interest paid	(2,050)	(1,670)	(7,083)	(8,193)
	<b>(14,993)</b>	<b>(34,364)</b>	<b>(42,268)</b>	<b>(42,873)</b>
<b>Investing activities</b>				
Acquisitions of property, plant and equipment	597	(3,202)	(6,354)	(7,983)
Proceeds from disposal of property, plant and equipment	-	3	10	16
(Increase) decrease in other assets	(1)	176	(18)	197
Proceeds from disposal of financial instrument (Note 17)	-	-	6,307	-
	<b>596</b>	<b>(3,023)</b>	<b>(55)</b>	<b>(7,770)</b>
Effect of foreign exchange rate changes on cash and cash equivalents held in foreign currency	231	(388)	107	(92)
Cash and cash equivalents (outflow) inflow	(318)	(17,545)	(9,609)	5,887
Cash and cash equivalents, beginning of period	7,130	42,606	16,421	19,174
<b>Cash and cash equivalents, end of period (Note 16)</b>	<b>6,812</b>	<b>25,061</b>	<b>6,812</b>	<b>25,061</b>

Supplemental disclosure of cash flow information (Note 16).

The accompanying notes are an integral part of this condensed consolidated interim financial report.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 1. Description of the Company

FibreK Inc. is the successor to SFK Pulp Fund (the “Fund”) following the completion of the conversion of the Fund from an income trust structure to a corporate structure by way of the transfer of units held by unitholders of the Fund to Fibrek Inc., on the basis of one Common Share for each unit so transferred (the “Arrangement”). As a result of the Arrangement, the holders of units became the shareholders of Fibrek.

FibreK Inc. was incorporated on March 24, 2010 under the *Canadian Business Corporations Act* and did not carry on any active business prior to the Arrangement, other than executing the arrangement agreement pursuant to which the Arrangement was implemented on May 25, 2010. The registered office of Fibrek is located at 625 René-Lévesque Blvd. West, Suite 700, Montréal, Québec, H3B 1R2.

FibreK Inc. obtained the final order from the Québec Superior Court with respect to the plan of arrangement on May 25, 2010. Comparative figures presented in the condensed consolidated interim financial report of the Company include all amounts previously reported by the Fund. Reference to “Company”, “share”, “dividends” and “shareholders” means “Fund”, “unit”, “distributions” and “unitholders” for transactions that occurred before the conversion of the Fund into a corporation.

FibreK Inc., together with its subsidiaries (collectively the “Company”), is a producer and marketer of premium virgin and recycled kraft pulp. The Saint-Félicien (Québec) mill supplies northern bleached softwood kraft (“NBSK”) pulp to various sectors of the paper industry primarily in Canada, the United States and Europe for use in specialty products. The Fairmont (West Virginia) and Menominee (Michigan) mills manufacture air-dried market recycled bleached kraft (“RBK”) pulp and primarily supply manufacturers of uncoated freesheet, commercial and away-from-home tissue and coated paper in the United States.

### 2. Summary of significant accounting policies

#### *Statement of compliance*

This condensed consolidated interim financial report has been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting* (“IAS 34”), using accounting policies consistent with International Financial Reporting Standards (“IFRS”) that are issued and expected to be effective as at December 31, 2011, the Company’s first annual IFRS reporting date. Prior to January 1, 2011, the interim and annual consolidated financial statements of the Company were prepared in accordance with Canadian generally accepted accounting principles (“GAAP”).

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Statement of compliance (continued)*

The adoption of IFRS resulted in changes to the accounting policies as compared with the most recent annual financial statements prepared under Canadian GAAP. The accounting policies set out below have been applied consistently to all periods presented. They also have been applied in the preparation of an opening IFRS statement of financial position as at January 1, 2010 (the "Transition Date"), as required by IFRS 1, First Time Adoption of International Financial Reporting Standards ("IFRS 1"). The impact of the transition from Canadian GAAP to IFRS is explained in Note 21.

The standards and interpretations within IFRS are subject to change and, accordingly, the accounting policies for the annual period that are relevant to this condensed consolidated interim financial report will be finalized only when the first annual IFRS financial statements are prepared for the year ending December 31, 2011.

The Company has elected to exceed the minimum requirements in order to present the Company's accounting policies in accordance with IFRS and the additional disclosures required under IFRS, which also highlight the changes from the Company's 2010 annual consolidated financial statements prepared in accordance with Canadian GAAP. In 2012 and beyond, the Company may not provide the same amount of disclosure in the Company's condensed consolidated interim financial reports under IFRS as the reader will be able to rely on the annual consolidated financial statements which will be prepared in accordance with IFRS.

#### *Basis of presentation*

This condensed consolidated interim financial report has been prepared on a historical cost basis, with the exception of financial instruments classified as fair value through profit or loss.

#### *Basis of consolidation*

This condensed consolidated interim financial report includes the accounts of the Company and its subsidiaries. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. All intercompany transactions, balances, income and expenses are eliminated in full on consolidation.

#### *Revenue recognition*

The Company's sales consist of NBSK and RBK pulp to various sectors of the paper industry primarily in Canada, the United States, and Europe. Sales are recognized after the Company has transferred the risks and rewards of ownership to the buyer and retains neither a continuing right to dispose of the goods, nor effective control of those goods; usually, this means that sales are recorded upon delivery of goods to customers in accordance with agreed terms of delivery.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Cash and cash equivalents*

Cash and cash equivalents in the statement of financial position comprise cash with financial institutions and on hand, and short term deposits with a maturity of three months or less, which are readily convertible into a known amount of cash. The Company's cash and cash equivalents are invested with major financial institutions in business accounts and bankers' acceptances that are available on demand by the Company for its programs.

#### *Inventories*

Pulp is measured at the lower of cost and net realizable value, with cost being determined using the weighted average cost method. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and any applicable variable selling costs.

Wood fibre, wastepaper, production and maintenance supplies and other raw materials are measured at cost determined using the weighted average cost method and are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost; otherwise, they would be valued at replacement cost.

The cost of inventories comprises all costs of purchase, costs of conversion, and other costs incurred in bringing the inventories to their present location and condition. The costs of purchase comprise the purchase price, import duties and non-recoverable taxes, transportation, handling and other costs directly attributable to the acquisition of finished goods, materials or services. The costs of conversion include direct material and labour costs, and a systematic allocation of fixed and variable overheads incurred in converting materials into finished goods.

#### *Property, plant and equipment*

Property, plant and equipment are recorded at cost, less accumulated depreciation and accumulated impairment losses.

The cost of property, plant and equipment consists of the purchase price net of grants, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Certain expenditures relating to replacement of components incurred during major maintenance are capitalized and amortized over the estimated benefit period of such expenditures.

Depreciation is based on cost less residual value, over the estimated useful lives, and provided for using the following methods and rates over the estimated useful lives of the assets:

Land	Not amortized	indefinite life
Buildings and related components	Straight-line	10 to 40 years
Warehouse under finance lease	Straight-line	over the lease term
Equipment:		
Processing equipment	Straight-line	5 to 20 years
Mobile equipment	Declining balance	30%
Furniture and fixtures	Straight-line	20 years
Computers	Straight-line	3 to 10 years
Roads, lots and other	Straight-line	20 years
Major maintenance	Straight-line	1 to 4 years
Construction in progress	Not amortized	-

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Property, plant and equipment (continued)*

Additions to property, plant and equipment are amortized from the date they are available for use. Expenditures incurred to replace a component of an item of property, plant and equipment, including those associated with major inspections, are capitalized.

Assets subject to finance leases are recorded in the financial statements under the same category as if they were directly owned by the Company and amortized over the shorter of their estimated useful life or the lease term.

The depreciation method, residual values, and useful lives of property, plant and equipment are reviewed annually and any change in estimate is applied prospectively.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in the statement of earnings.

#### *Borrowing costs*

The Company capitalizes borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, until the qualifying assets are ready for their intended use. All other borrowing costs are expensed as incurred.

Qualifying assets are those that necessarily take a substantial period of time to get ready for use or sale. Borrowing costs include the costs related to specific or general borrowed funds, funds which relate to borrowings that could have been avoided had the asset not been acquired, constructed or produced.

#### *Intangible assets*

Intangible assets represent application softwares and are recorded at cost. These assets are recognized at cost less accumulated depreciation and accumulated impairment losses. Depreciation is provided for using the straight-line method over their useful life of 3 to 10 years. Additions to intangible assets are amortized from the date they are available for use.

The depreciation method and useful life is reviewed annually and any change in estimate is applied prospectively.

#### *Leases*

Leases are classified as either finance or operating leases. Finance leases are those that substantially transfer the benefits and risks of ownership of an asset to the lessee. All leases other than finance leases are operating leases.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Leases (continued)*

Assets held under finance leases are recognized as assets of the Company at the lower of the fair value at the inception of the lease or the present value of the minimum lease payments. The corresponding liability is recognized as a finance lease obligation. Lease payments are apportioned between financial expenses and reduction of the lease obligation to achieve a constant rate of interest on the remaining liability. Financial expenses are charged to the statement of earnings, unless they are directly attributable to qualifying assets, in which case they are capitalized.

Total payments under operating leases are expensed on a straight-line basis over the term of the relevant lease. Incentives received upon entry into an operating lease are recognized straight-line over the lease term.

#### *Impairment of assets*

At each financial position reporting date, the carrying amounts of the Company's assets are reviewed to determine whether there is any indication that those assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated to determine the extent of the impairment, if any.

The recoverable amount is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted at a rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in the statement of earnings.

For an asset that does not generate independent cash inflows, the review for indications of impairment and determination of recoverable amount are performed for the cash generating unit to which the asset belongs. A cash generating unit is the smallest identifiable group of assets that generates independent cash inflows.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, to the extent the increased carrying amount does not exceed what the carrying amount would be, had no impairment loss been previously recognized. A reversal of an impairment loss is recognized immediately in the statement of earnings.

#### *Financial instruments*

The Company recognizes financial assets and financial liabilities when the Company becomes a party to a contract. Financial assets and financial liabilities, with the exception of financial assets and financial liabilities classified at fair value through profit or loss, are measured at fair value plus transaction costs on initial recognition.

Measurement in subsequent periods depends on the classification of the financial instrument.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Financial instruments (continued)*

##### *i) Financial assets at fair value through profit or loss (FVTPL)*

Financial assets are classified as FVTPL when acquired principally for the purpose of trading, if so designated by management (fair value option), or if they are derivative assets that are not part of an effective and designated hedging relationship. Financial assets classified as FVTPL are measured at fair value on initial recognition, with subsequent changes recognized in the statement of earnings, and transaction costs are expensed when incurred.

The Company's financial assets classified as FVTPL include cash and cash equivalents, investment at FVTPL and derivative instruments that are not part of an effective and designated hedging relationship. The Company does not currently apply hedge accounting to any of its derivative instruments.

##### *ii) Financial liabilities at FVTPL*

Financial liabilities are classified as FVTPL if they are designated as such by management, or they are derivative liabilities that are not part of an effective and designated hedging relationship. Financial liabilities classified as FVTPL are measured at fair value on initial recognition, with subsequent changes recognized in the statement of earnings, and transaction costs are expensed when incurred.

The Company's financial liabilities classified as FVTPL include derivative instruments that are not part of an effective and designated hedging relationship. The Company does not currently apply hedge accounting to any of its derivative instruments.

##### *iii) Loans and receivables*

Loans and receivables are non-derivative financial assets that have fixed or determinable payments and are not quoted in an active market. Subsequent to initial recognition, loans and receivables are carried at amortized cost using the effective interest method.

Accounts receivable are classified as loans and receivables.

##### *iv) Other financial liabilities*

Other financial liabilities are financial liabilities that are not classified as FVTPL. Subsequent to initial recognition, other financial liabilities that are not subject to hedge accounting are measured at amortized cost using the effective interest method.

The Company's other financial liabilities include accounts payable and accrued liabilities, long-term debt and the liability portion of the convertible unsecured subordinated debentures (which have been completely redeemed on June 28, 2011).

The effective interest method is a method of calculating the amortized cost of an instrument and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash flows (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument to the net carrying amount on initial recognition.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Comprehensive income*

Comprehensive income is the change in the Company's net assets during the period that results from transactions and other events and circumstances except those resulting from investments by shareholders and dividends to shareholders. The Company's other comprehensive income includes only the unrealized gain or loss on the translation of financial statements of a foreign operation with a different functional currency than the Company and the unrealized actuarial gain or loss under defined benefit plans.

#### *Foreign currency translation*

The Canadian dollar is the functional and presentation currency of the Company. Functional currency is also determined for each of the Company's subsidiaries, and items included in the financial statements of the subsidiaries are measured using their functional currency.

Transactions in currencies other than the functional currency are translated into the functional currency using the exchange rates prevailing at the dates of the transaction. Monetary assets and liabilities not denominated in the functional currency are translated at the period end rates of exchange. Foreign exchange gains and losses are recognized in the statement of earnings.

Assets and liabilities of entities with functional currencies other than Canadian dollars are translated at the period end rates of exchange, and the results of their operations are translated at average rates of exchange for the period. The resulting translation adjustments are included in other comprehensive income in equity.

Intercompany amounts with foreign operations for which settlement is neither planned nor likely to occur in the foreseeable future are part of the Company's net investment in the foreign operations. Foreign exchange gains and losses related to these intercompany amounts are included in other comprehensive income.

#### *Income taxes*

Income taxes are determined using the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Deferred income tax assets are recognized to the extent that realization is considered probable.

#### *Landfill closure liability*

The Company owns a landfill in Menominee, Michigan. The Company provides for estimated closure and post-closure monitoring costs over the operating life of its landfill as air-space is consumed. Such costs are estimated based on the technical requirements of regulations of the U.S. Environmental Protection Agency or the applicable state requirements, and include such items as a final cap and cover on the site, methane gas and leachate management, and groundwater monitoring. The landfill closure liability is measured based on the best estimate of the obligation, discounted at a credit-free rate.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Landfill closure liability (continued)*

The liability is re-measured at each reporting date to reflect current estimates and changes in the discount rate. Changes in the liability that result from the passage of time (accretion) are recorded as borrowing costs, which are presented as financial expense in the statement of earnings. The estimated costs and estimated total available air-space are reviewed and updated by management on a periodic basis and changes in such estimated amounts are reflected on a prospective basis unless they indicate there is an impairment of the carrying value of the corresponding asset.

#### *Environmental expenditures*

Environmental expenditures, that will benefit the Company in future periods, are capitalized as part of property, plant and equipment. Amortization is charged to earnings over the estimated useful life of the asset. Environmental expenditures that are not expected to provide a benefit to the Company in future periods are accrued and recorded in earnings when a requirement to remedy an environmental exposure is identified.

#### *Employee benefits*

The Company sponsors contributory defined benefit plans that provide for pensions and post-employment benefits for certain employees. Beginning January 1, 2010, all Canadian non-unionized employees have stopped accruing benefits under the defined pension plan and started with a new defined contribution plan. The Company maintains defined contribution 401(K) plans for all US employees that meet service eligibility requirements. The Company also maintains a non-funded non-contributory supplementary defined benefit plan as well as a defined contribution pension plan for executives.

The cost of benefits earned under defined benefit plans is actuarially determined using the projected benefit method. The expected return on plan assets is based on the fair value of pension assets, which are measured at fair market value. The net actuarial gains or losses are recognized in the other comprehensive income in the period they arise which is directly recognized in the deficit and as such, the benefit expense is not impacted by those gains or losses.

Contributions to defined contribution plans are expensed as incurred.

#### *Share-based compensation plans*

The Company has share-based compensation plans under which it receives services from employees against consideration for equity instruments of the Company or cash payments.

For plans that are settled with shares of the Company, the expense is determined based on the fair value of the award granted and recognized over the period during which services are received, which is usually the vesting period. For awards with graded vesting, the fair value of each tranche is recognized over its respective vesting period.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *Share-based compensation plans (continued)*

For cash-settled plans and plans where the employee can choose to settle in equity or cash, the expense is determined based on the fair value of the liability at the end of the reporting period until the award is settled. The fair value of the liability is determined with reference to the market price of the Company's shares at the reporting date or through the use of an option pricing model depending on the nature of awards under the compensation plan.

At the end of each reporting period, the Company re-assesses its estimates of the number of awards that are expected to vest and recognizes the impact of the revisions in the statement of earnings.

#### *Government Grants*

Government grants are recognized when there is reasonable assurance that the Company will comply with the conditions and that the grants will be received.

Government grants related to expenditures for property, plant and equipment are recognized as a reduction in the cost of those assets. Government grants related to expenses are recognized as reduction of those expenses.

The benefit of a government loan at a below-market rate of interest is treated as a government grant, measured as the difference between proceeds received and the fair value of the loan based on prevailing market interest rates.

#### *Accounting Standards Issued but not yet applied*

The following new accounting standards or amendments to existing accounting standards have been published and are required to be applied for accounting periods beginning on or after January 1, 2013, with early adoption permitted. Only the amendments to International Accounting Standards ("IAS") 1 Presentation of Financial Statements, are to be applied for accounting periods beginning on or after July 1, 2012.

#### *IFRS 9 Financial Instruments ("IFRS 9")*

IFRS 9 was issued in November 2009 and provides guidance on the classification and measurement of financial liabilities, and requirements for the derecognition of financial assets and financial liabilities. This standard replaces IAS 39 Financial Instruments – Recognition and Measurement ("IAS 39").

The Company has not yet assessed the impact of this new standard or determined whether it will early adopt the standard.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *IFRS 10 Consolidated Financial Statements (“IFRS 10”)*

IFRS 10 was issued in May 2011 and replaces the consolidation requirements in SIC 12 Consolidation – Special Purpose Entities, and IAS 27 Consolidated and Separate Financial Statements. The standard provides a single consolidation model that identifies control as the basis for consolidation for all types of entities. The revised definition of control indicates that control over an investee exists when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

#### *IFRS 11 Joint Arrangements (“IFRS 11”)*

IFRS 11 was issued in May 2011 and supersedes IAS 31 Interests in Joint Ventures, and Standing Interpretations Committee (“SIC”) 13 Jointly Controlled Entities – Non-Monetary Contributions by Venturers. This standard reduces the types of joint arrangement to two: joint operations and joint ventures. It requires a single method of accounting for joint ventures, the equity method, eliminating the proportionate consolidation method.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

#### *IFRS 12 Disclosure of Interests in Other Entities (“IFRS 12”)*

IFRS 12, issued in May 2011, addresses disclosure requirements of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

#### *IAS 28 Investments in Associates and Joint Ventures (“IAS 28”)*

As a consequence of the issuance of IFRS 10, IFRS 11 and IFRS 12, IAS 28 was retitled and amended in May 2011 to include the requirements for the application of the equity method when accounting for joint ventures.

The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

#### *IFRS 13 Fair Value Measurement (“IFRS 13”)*

IFRS 13, issued in May 2011, defines fair value, sets out a framework for measuring fair value and provides disclosure requirements about fair value measurement. This standard applies when other IFRS require or permit fair value measurement.

The Company has not yet assessed the impact of this new standard or determined whether it will early adopt the standard.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 2. Summary of significant accounting policies (continued)

#### *IAS 19 Employee Benefits (“IAS 19”)*

In June 2011, IAS 19 was amended to remove the corridor approach, which was an option to defer some gains and losses that arise from defined benefit plans. The options for presenting gains and losses are also removed. It requires companies to include service cost and finance cost in profit or loss and remeasurements in other comprehensive income. The amendments also improve disclosure requirements relating to the characteristics of defined benefit plans, the amounts recognized in the financial statements and the risks arising from defined benefit plans.

The Company has not yet assessed the impact of this new standard or determined whether it will early adopt the standard.

#### *IAS 1 Presentation of Financial Statements (“IAS 1”)*

Issued in June 2011, the amendments to IAS 1 require companies to group together items within other comprehensive income that may be reclassified to profit or loss.

The Company has not yet assessed the impact of this new standard or determined whether it will early adopt the standard.

### 3. Critical accounting estimates and judgements

The preparation of the condensed consolidated interim financial report using accounting policies consistent with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. The preparation of the condensed consolidated interim financial report also requires management to exercise judgement in the process of applying the accounting policies.

#### *Critical accounting estimates*

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized prospectively from the period in which the estimates are revised.

The following are the key estimate and assumption uncertainties that have a significant risk of resulting in a material adjustment within the next financial year.

#### *i) Impairment of assets*

When there is indication that an asset may be impaired, the Company is required to estimate the asset's recoverable amount. Recoverable amount is the greater of the value in use and the fair value less costs to sell. Determining the value in use requires the Company to estimate expected future cash flows associated with the assets and a suitable discount rate in order to calculate present value.

On adoption of IFRS, the Company recognized an impairment loss of \$136,964. Details of the impairment loss calculation are included in Note 21.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 3. Critical accounting estimates and judgements (continued)

#### *Critical accounting estimates(continued)*

#### *ii) Useful life of property, plant and equipment and intangible assets*

Property, plant and equipment are amortized over the estimated useful life of the assets. Changes in the estimated useful lives could significantly increase or decrease the amount of depreciation recorded during the period.

Total depreciation recorded for the three and nine months ended September 30, 2011 were \$8,584 and \$26,642, respectively (2010: \$8,428 and \$25,933, respectively).

#### *iii) Employee benefits*

The Company sponsors defined benefit plans providing pension and other post-employment benefits to eligible employees. The determination of expense and obligations associated with employee benefits requires the use of assumptions such as the expected return on assets available to fund pension obligations, the discount rate to measure obligations, the expected mortality, the expected rate of future compensation and the expected healthcare cost trend rate. Because the determination of the cost and obligations associated with employee benefits requires the use of various assumptions, there is measurement uncertainty inherent in the actuarial valuation process. Actual results will differ from results that are estimated based on assumptions.

#### *iv) Landfill closure liability*

The Company has obligations associated with closure and post-closure activities over the operating life of a landfill in Menominee, Michigan. The Company is required to make estimates regarding these future costs to establish the current measurement of the landfill closure liability.

Total liability associated with the landfill closure recorded as at September 30, 2011 was \$2,434 (December 31, 2010 - \$1,891).

Further details are included in Note 8.

#### *Critical judgements used in applying accounting policies*

#### *i) Income taxes*

The measurement of income taxes payable and deferred income tax assets and liabilities requires management to make judgements in the interpretation and application of the relevant tax laws. The actual amount of income taxes only become final upon filing and acceptance of the tax return by the relevant authorities, which occurs subsequent to the issuance of the financial statements.

#### *ii) Classification of leases*

The Company is a lessee to a number of leases, the accounting of which is dependent on whether the leases are classified as finance or operating leases. In determining the appropriate classification, the Company applies judgement as to whether the benefits and risks of ownership of associated assets have been substantially transferred to the Company.

Further details on the accounting treatment of finance and operating leases are included in Note 2.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 3. Critical accounting estimates and judgements (continued)

*Critical judgements used in applying accounting policies (continued)*

*iii) Functional currency of foreign operations*

The Company has foreign subsidiaries and therefore needs to determine the functional currency to be used for the translation of their operations. Management used its judgement to determine the functional currency that most faithfully represents the economic effects of the underlying transactions, events and conditions of the Company's foreign operations. As part of this approach, management gives priority to the primary indicators and also considers additional factors, which are designed to provide additional supporting evidence to determine a subsidiary's functional currency.

### 4. Accounts receivable

	September 30, 2011	December 31, 2010
		\$
Trade receivable	61,620	57,527
Grants receivable	5,638	6,794
Sales taxes receivable	2,914	2,725
Others	634	1,378
	<b>70,806</b>	<b>68,424</b>

Accounts receivable are pledged as security for the credit facilities.

### 5. Inventories

	September 30, 2011	December 31, 2010
	\$	\$
Wastepaper	16,327	10,241
Wood fibre	4,210	7,698
Pulp	52,803	34,501
Production and maintenance supplies, and other raw materials	26,674	24,747
	<b>100,014</b>	<b>77,187</b>

Inventories are pledged as security for the credit facilities.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 5. Inventories (continued)

In addition, inventory expense was recognized in cost of products sold in the following three and nine-month periods ended September 30:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Raw materials and consumables used	<b>95,648</b>	90,354	<b>276,992</b>	257,996
Parts, energy, labour costs and other costs	<b>23,819</b>	22,814	<b>69,570</b>	68,845
Net change in pulp inventory	<b>(7,575)</b>	(13,476)	<b>(16,353)</b>	31
Depreciation	<b>8,584</b>	8,428	<b>26,642</b>	25,933
Total	<b>120,476</b>	108,120	<b>356,851</b>	352,805

For the three and nine-month periods ended September 30, 2011, the cost of inventories recognized as an expense includes \$474 – US\$472 and \$590 – US\$592 in respect of write-downs of pulp inventory to net realisable value. For the three and nine-month periods ended September 30, 2010, the cost of pulp has been reduced by Nil and \$76 – US\$78 in respect of the reversal of previous inventories' write-downs as a result of increased price in certain markets.

### 6. Property, plant and equipment

*Property, plant and equipment*

	Carrying Amounts	
	September 30, 2011	December 31, 2010
Land	<b>5,046</b>	5,006
Buildings	<b>33,920</b>	32,763
Warehouse under finance lease	<b>1,679</b>	1,802
Equipment, roads, lots and other	<b>316,103</b>	329,422
Construction in progress	<b>9,999</b>	7,028
Major maintenance	<b>2,972</b>	6,588
	<b>369,719</b>	382,609

Property, plant and equipment are pledged as security for the credit facilities.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 6. Property, plant and equipment (continued)

	Cost						Total
	Land	Buildings	Warehouse under finance lease	Equipment, roads, lots and other	Construction in progress	Major maintenance	
December 31, 2010	6,149	57,606	4,660	713,827	7,028	10,126	799,396
Additions *	-	1,839	-	4,542	2,875	880	10,136
Disposals	-	(34)	-	(348)	-	(3,532)	(3,914)
Foreign currency translation	43	984	208	6,251	96	-	7,582
<b>September 30, 2011</b>	<b>6,192</b>	<b>60,395</b>	<b>4,868</b>	<b>724,272</b>	<b>9,999</b>	<b>7,474</b>	<b>813,200</b>

\* : The additions are presented net of grants.

	Accumulated depreciation and impairment					Total
	Land	Buildings	Warehouse under finance lease	Equipment, roads, lots and other	Major maintenance	
December 31, 2010	1,143	24,843	2,858	384,405	3,538	416,787
Depreciation	-	1,131	192	20,803	4,483	26,609
Disposals	-	(6)	-	(259)	(3,532)	(3,797)
Adjustments	-	-	-	(106)	13	(93)
Foreign currency translation	3	507	139	3,326	-	3,975
<b>September 30, 2011</b>	<b>1,146</b>	<b>26,475</b>	<b>3,189</b>	<b>408,169</b>	<b>4,502</b>	<b>443,481</b>

### 7. Intangible assets

#### *Application Software*

	Cost	Accumulated amortization	Total
December 31, 2010	1,077	838	239
Additions	-	33	(33)
Disposals	-	-	-
Foreign currency translation	24	24	-
<b>September 30, 2011</b>	<b>1,101</b>	<b>895</b>	<b>206</b>

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 8. Landfill closure liability

The following table presents the carrying amount of the obligations associated with the closure and post-closure activities over the operating life of the landfill:

	September 30, 2011	December 31, 2010
	\$	\$
Balance, beginning of period	1,891	3,611
Liability incurred	(39)	(59)
Accretion and effect of change in discount rate	471	437
Changes in estimates	-	(1,958)
Foreign currency translation	111	(140)
Balance, end of period	2,434	1,891
Current portion (2011 - US\$263; 2010 - US\$161)	273	160
Long-term portion (2011 - US\$2,080; 2010 - US\$1,741)	2,161	1,731
	2,434	1,891

The total undiscounted amount of estimated cash flows required to settle the obligations was \$3,395 – US\$3,268 (December 31, 2010: \$3,252 – US\$3,270), which has been discounted using a credit risk-free rate of 2.5% (December 31, 2010 – 3.9%). The majority of these obligations is expected to be settled over the next 31 years, and will be funded using cash flows from operations at the time of retirement. In 2010, the Company revised the estimated cash flows required to settle the obligations resulting in a reduction of the liability; the offset was applied against property, plant and equipment and the remaining amount was recorded in earnings.

As at September 30, 2011, the Company held restricted cash in the amount of \$112 – US\$107 (December 31, 2010: \$106 - US\$106) to provide for payment of the costs of landfill closure monitoring and maintenance or response activities of the landfill to protect health, safety, and the environment. In addition, as at September 30, 2011, the Company had outstanding letters of credit in the aggregate amount of \$395 – US\$380 (December 31, 2010: \$378 – US\$380) and a deposit of \$101 – US\$98 (December 31, 2010: \$97 – US\$98) to secure a portion of such activities related to closure of the landfill pursuant to a requirement by the Department of Environmental Quality of Michigan.

### 9. Employee benefits

The total employee benefit costs, which include expenses relating to the defined benefit and defined contribution pension plans, for the three-month periods ended September 30, 2011 and 2010, totalled \$678 and \$736, respectively. For the nine-month periods ended September 30, 2011 and 2010, the costs totalled \$2,131 and \$2,249, respectively.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 10. Employee benefits expense

Total employee benefits incurred during the periods are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Salaries and fringe benefits	12,368	10,700	35,008	33,369
Post-employment benefits	604	639	1,904	1,974
Share-based compensation	61	162	506	310
Government pension plans	74	97	227	275
Termination benefits	-	(9)	-	877
	<b>13,107</b>	11,589	<b>37,645</b>	36,805

### 11. Long-term debt

	September 30,	December 31,
	2011	2010
	\$	\$
Term Loan	77,085	77,648
ABL Credit Facility denominated in Canadian dollars	5,000	-
ABL Credit Facility denominated in US dollars (US\$14,000)	14,545	-
Obligation under finance lease at a rate of 14.9%	3,860	3,917
PSIF - Investissement Québec	4,396	5,324
Deferred financing fees	(1,886)	(2,215)
	<b>103,000</b>	84,674
Less: current portion of long-term debt	1,997	1,876
	<b>101,003</b>	82,798

# **FIBREK INC.**

## **Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)**

---

### **11. Long-term debt (continued)**

#### *Credit facilities*

On July 16, 2010, the Company concluded:

- a term loan for an amount of \$78 million (the "Term Loan") maturing July 15, 2015; and
- a \$75 million asset-based secured revolving credit facility (the "ABL Credit Facility") maturing July 15, 2013.

On August 3, 2011, as provided under the ABL Credit Facility, the term was extended for an additional year, bringing the maturity to July 15, 2014.

As at September 30, 2011 and December 31, 2010, the Company was in compliance with all terms and conditions of the Term Loan and ABL Credit Facility.

#### *Deferred financing fees*

Deferred financing fees of \$1,461 (December 31, 2010: \$1,716) are not netted against the related financial liabilities as the ABL Credit facilities are not used on a permanent basis by the Company.

### **12. Convertible unsecured subordinated debentures**

On September 7, 2006, the Company issued convertible extendible unsecured subordinated debentures (the "Debentures") for a principal amount of \$51,750 (including the over-allotment option). The Debentures, which bore interest at 7% payable semi-annually and matured on December 31, 2011, were completely redeemed on June 28, 2011.

Under certain conditions, Debentures may have been converted into shares at the holder's option. Furthermore, the Debentures were redeemable at the Company's option. The Company may, at its option and subject to certain conditions, have elected to satisfy the redemption price of the Debentures by issuing Company shares.

Financing fees of \$2,838 were incurred in conjunction with the issuance of Debentures. The holders' conversion option was valued at \$6,242 (net of allocated financing fees of \$358) on the date of issuance and was included in Equity. The initial liability portion of the Debentures was being accreted such that the liability at maturity would have equal the face value of the then outstanding Debentures. The remaining portion of the financing fees of \$2,480 was deferred and was being amortized over the term of the Debentures, using the effective interest rate method. On the Transition Date and until the effective date of the Arrangement, the conversion option was recognized as a financial liability and measured at fair value through profit or loss. Further details are included in Note 21.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 12. Convertible unsecured subordinated debentures (continued)

For the nine-month period ended September 30, 2011, the Company redeemed Debentures in an aggregate amount of \$51,749. Redemption was completed in two tranches, on February 28 and June 28, 2011. On the redemption dates, the Company paid to the holders of redeemed Debentures a redemption price equal to the principal amount of the Debentures, plus accrued and unpaid interest up to the date prior to the redemption date. Redemption prices on February 28 and June 28, 2011 were respectively of \$1,011.12 and 1,034.14 per \$1,000.00 principal amount of Debentures. As a result of this redemption, a total gain on redemption of \$2,752 was recognized in the statement of earnings for the nine-month period ended September 30, 2011 (Note 17).

	September 30, 2011	December 31, 2010
	\$	\$
Initial amortized amount	-	45,149
Accretion	-	5,042
Deferred financing costs	-	(582)
	-	49,609
Current portion	-	49,609

### 13. Shareholders' capital/Unitholders' capital

#### *Authorized and issued common shares*

An unlimited number of common shares are issuable. Each share is freely transferable and represents a shareholder's proportionate undivided interest in the Company. Each share confers to its holder the right to one vote at any meeting of shareholders and to participate equally and rateably in any dividends of the Company, if any, and, in the event of any required distribution of all of the property of the Company, in the net assets of the Company remaining after satisfaction of all liabilities. Shares have no conversion or pre-emptive right.

#### *Fund units*

An unlimited number of units were issuable pursuant to the trust agreement. Each unit was freely transferable and represented a unitholder's proportionate undivided interest in the Fund. Each unit conferred to its holder the right to one vote at any meeting of unitholders and to participate equally and rateably in any distributions of the Fund, if any, and, in the event of any required distribution of all of the property of the Fund, in the net assets of the Fund remaining after satisfaction of all liabilities. Units had no conversion or pre-emptive right.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 13. Shareholders' capital/Unitholders' capital (continued)

#### *Shares/Units issued and outstanding*

	September 30, 2011		
	Number of units	shares	Amount \$
Balance, December 31, 2010 and September 30, 2011	-	130,075,556	696,537

	September 30, 2010		
	Number of units	shares	Amount \$
Balance, January 1, 2010	90,472,708	-	658,609
Conversion of units into shares	(90,472,708)	90,472,708	-
Issuance of shares	-	39,602,848	37,928
Balance, September 30, 2010	-	130,075,556	696,537

On May 25, 2010, all the outstanding units of the Fund were exchanged for common shares of the Company on a one-for-one basis.

#### *Rights Offering*

On July 16, 2010, the Company issued an aggregate of 39,602,848 common shares of the Company pursuant to a rights offering at a price of \$1.01 per common share for net proceeds of \$37,928 after deducting standby fees of \$400 and expenses of \$1,671.

#### *Per share/unit information*

The following tables reconcile the net earnings to net earnings adjusted for dilutive effect and the weighted average number of shares outstanding used in computing basic earnings per share to weighted average number of shares outstanding used in computing diluted earnings per share:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Net earnings	6,773	5,355	15,866	14,030
Impact of assumed conversion of Debentures	-	1,391	1,875	4,159
<b>Net earnings adjusted for dilutive effect</b>	<b>6,773</b>	<b>6,746</b>	<b>17,741</b>	<b>18,189</b>

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 13. Shareholders' capital/Unitholders' capital (continued)

*Per share/unit information(continued)*

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Average number of shares outstanding used in computing basic earnings per share	<b>130,075,556</b>	123,618,570	<b>130,075,556</b>	101,642,742
Dilutive effect of Debentures*	-	52,377,530	<b>20,560,820</b>	70,743,677
Dilutive effect of rights offering	-	6,456,986	-	5,512,484
Average number of shares outstanding used in computing diluted earnings per share	<b>130,075,556</b>	182,453,086	<b>150,636,376</b>	177,898,903

\* Assuming a conversion price of \$1.28 and \$1.09 for the three and nine-month periods ended September 30, 2011 (being the trading price of the shares at the beginning of the three and nine-month periods) and \$1.04 and \$0.77 for the three-month and nine-month periods ended September 30, 2010.

For the three and nine-month periods ended September 30, 2011 and 2010, the share options were anti-dilutive.

### 14. Income taxes

*Tax reassessment*

In January 2009, Fibrek received notices of assessment for the 2002 and 2003 taxation years from the Canada Revenue Agency ("CRA") and the Ministère du Revenu du Québec ("MRQ") reassessing the tax value allocated to the assets of the Saint-Félicien Mill at the time such assets were purchased by Fibrek from Abitibi-Consolidated Inc. in August 2002. These assessments do not involve any taxes payable. In October 2009, Fibrek requested a statement of revised losses from CRA and the MRQ. In September 2010, the Company received from CRA a statement of revised losses. In December 2010, the Company filed a notice of objection within the prescribed delay. The CRA has since acknowledged receipt of Fibrek's notice of objection. A reduction in the value allocated to certain assets would reduce the amount of Canadian non capital losses available to reduce future taxable income, among others. Management used its best estimate of the outcome of the tax reassessment in its calculation of future income taxes. The outcome of the tax reassessment may require an adjustment to the recognized future income tax amounts. This adjustment or any revision of the estimation would be recognized prospectively and the impact could be material.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 15. Share-based compensation

Liabilities recorded for share-based compensation plans

	September 30, 2011	December 31, 2010
	\$	\$
Long-term incentive plan	257	285
Share option plan	40	41
	<b>297</b>	326

---

Contributed surplus recorded for share-based compensation plans

	September 30, 2011	December 31, 2010
	\$	\$
Share option plan	<b>812</b>	277

---

Compensation expense (credit) recognized for share-based compensation plans

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Long-term incentive plan	(142)	24	(28)	126
Share option plan	203	140	534	186
	<b>61</b>	164	<b>506</b>	312

---

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 15. Share-based compensation (continued)

#### *i) Long-term incentive plan*

Effective January 1, 2006, the Company implemented a Performance Share Plan under which Performance Shares ("PS") were awarded by the Board of Directors to certain key executives. The PS were awarded as of January 1<sup>st</sup> of each year based on an incentive amount determined by the Board. To determine the awarded amount of PS, the incentive amount was divided by the average trading price of the Company's shares for the 20 trading days immediately preceding the day on which the award was made. The PS vest after three years and are payable in cash once the Board has determined the achievement of the specified performance targets. The amount of cash to be received by the participants is determined by multiplying the number of vested PS by the value of the Company's shares as at the end of the performance cycle (three years), based on the average trading price of the Company's shares for the 20 trading days immediately preceding the vesting date. The participants are also entitled to an amount equivalent to the dividends declared on the Company's shares during the vesting period for all the PS that vest. PS that have not achieved the vesting condition are automatically cancelled.

Effective January 1, 2009, the Board approved a modification to the plan only for the cycle starting in 2009. Pursuant to this modification, 20% of the PS awarded on January 1, 2009 will vest on December 31, 2011, if the executive is still in his/her position, no matter whether the performance targets are achieved or not.

The Company recognizes the associated compensation costs based on the best available estimates of the outcome of the performance condition. The effect of a change in estimate is recognized over the related vesting period.

The table below summarizes the changes in the number of outstanding PS:

	<b>September 30, 2011</b>	December 31, 2010
Balance, beginning of period	<b>1,693,750</b>	1,943,517
Cancelled	-	(195,745)
Expired	-	(54,022)
Balance, end of period	<b>1,693,750</b>	1,693,750

No incentive was paid as targets were not met.

As a result of the implementation of the share option plan on May 19, 2010, no additional PS were awarded and the plan will terminate at the end of the 2009-2011 cycle.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 15. Share-based compensation (continued)

#### *ii) Share option plan*

Effective May 19, 2010, the Company implemented a share option plan under which options may be awarded by the Board of Directors to executives and key employees. The options normally vest over a four-year period, one third of the options vesting on each anniversary of their date of award, commencing on the second anniversary. The options may also be subject to performance vesting conditions and the Board may accelerate the date upon which any option becomes exercisable. The option holders are entitled to exercise their vested options at a predetermined exercise price. As at September 30, 2011 and December 31, 2010 none of the options outstanding were exercisable.

With the consent of the Board, the option holders are entitled to either (i) elect to exercise their options through a cashless exercise pursuant to which they would receive such number of common shares equal to their “in-the-money” value of the options, or (ii) elect to surrender their options in exchange for a cash payment equal to the “in-the-money” value of the options. Notwithstanding the manner in which the option holders elect to exercise their options, the number of common shares reserved for allotment pursuant to the share option plan, which include all regular and special awards, shall not exceed 4,523,635.

The options which may be awarded under the share option plan shall not exceed ten years. The exercise price of any options awarded under the share option plan shall be the volume weighted average closing price of the common shares on the Toronto Stock Exchange (“TSX”) for the five trading day period following the black-out period relating to the filing of the Company’s annual financial statements, provided that the exercise price shall not be less than the volume weighted average trading price per common share on the TSX over the five trading days preceding the day the option is awarded.

#### *a) Regular grants*

The table below summarizes the changes in the number of outstanding options under the regular grants:

	<b>September 30, 2011</b>	
	Number of options	Weighted Average exercise price
		\$
Outstanding, December 31, 2010	<b>1,135,269</b>	<b>1.35</b>
Granted (*)	<b>939,814</b>	<b>1.56</b>
Outstanding, September 30, 2011	<b>2,075,083</b>	<b>1.45</b>

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 15. Share-based compensation (continued)

ii) Share option plan (continued)

a) Regular grants (continued)

	December 31, 2010	
	Number of options	Weighted Average exercise price
Outstanding, January 1, 2010	-	\$ -
Granted (**)	1,135,269	1.35
Outstanding, December 31, 2010	1,135,269	1.35

\*: On February 23, 2011, the Board awarded 939,814 options to executives having an exercise price of \$1.56 per common share and a term of six years from the award date.

\*\* : On May 25, 2010, the Board awarded 1,135,269 options to executives and key employees having an exercise price of \$1.35 per common share and a term of six years from the award date.

The Company recognizes compensation cost based on the best available estimates of the performance condition, if any, using the Black-Scholes option pricing model. The effect of a change in estimate is recognized over the related vesting period.

For the three and nine-month periods ended September 30, 2011, compensation expenses of \$160 and \$414 were recorded in the statement of earnings in relation to this regular grant (2010: \$90 and \$119). As at September 30, 2011, an amount of \$29 (December 31, 2010 – \$27) was included in accounts payable and accrued liabilities.

b) Special one-time grant

On May 25, 2010, the Board awarded 1,086,009 options under the special one-time grant to executives having an exercise price of \$1.35 per common share and a term of six years from the date of award. The vesting of these options is subject to the achievement of the following minimum performance conditions:

- 50% of the options will vest on the third anniversary of the date of award, provided the Company's weighted average closing share price over the previous 20 trading days is \$3.50 per common share or greater, (the "First Performance Criteria") and
- the other 50% of the share options will vest on the fifth anniversary of their date of award, provided the Company's weighted average closing share price over the previous 20 trading days is \$5.00 per common share or greater (the "Second Performance Criteria"). If the First Performance Criteria has not been met on the third anniversary of the date of award but the Second Performance Criteria is met, then the first 50% will also vest on the fifth anniversary of the award date.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 15. Share-based compensation (continued)

ii) *Share option plan (continued)*

b) *Special one-time grant (continued)*

The table below summarizes the changes in the number of outstanding options under the special one-time grant:

	<b>September 30, 2011</b>	
	Number of options	Weighted Average exercise price
		\$
Outstanding, December 31, 2010 and September 30, 2011	<b>1,086,009</b>	<b>1.35</b>
	<b>December 31, 2010</b>	
	Number of options	Weighted Average exercise price
		\$
Outstanding, January 1, 2010	-	-
Granted	1,086,009	1.35
Outstanding, December 31, 2010	1,086,009	1.35

The Company recognizes compensation costs based on the best available estimates of the performance condition using the binomial option pricing model. The effect of a change in estimate is recognized over the related vesting period.

For the three and nine-month periods ended September 30, 2011 compensation expenses of \$43 and \$120 were recorded in the statement of earnings in relation to this special one-time grant (2010: \$50 and \$67). As at September 30, 2011, an amount of \$11 (December 31, 2010 - \$14) was included in accounts payable and accrued liabilities.

The following assumptions were used to estimate the fair value, at the date of award, of each option issued to executives and key employees:

	Regular grants	Special one-time grant
Risk-free interest rate	2.35%	2.32%
Expected dividend yield	NIL	NIL
Expected life of options	4.5 years	5.0 years
Expected volatility	72.43%	65.41%
Weighted average fair value of issued options	\$0.82	\$0.57

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 15. Share-based compensation (continued)

#### *iii) Deferred share unit plan*

Effective December 9, 2010, the Company implemented a deferred share unit plan for directors of the Company. Under the plan, eligible directors have the right to elect, for the following fiscal year, to receive all or part of their fees and/or annual retainer in share units. The number of share units to be granted is based on the weighted average trading price of the common shares on the TSX for the five (5) business days immediately preceding a given date or in such manner as is required or allowed by the rules and policies of the TSX (the "Market Price"). A participant is entitled to receive, upon such participant's Termination of Board Service (as such expression is defined in the plan), the payment in cash of the share units that are credited to the participant's account on such given date based, for each vested share unit, on the value of a common share at the Market Price on the date of such participant's Termination of Board Service.

As at December 31, 2010, no director had elected to receive his or her annual retainer and/or fees for the following year in share units, election which can only be done once a year.

### 16. Supplemental disclosure of cash flow information

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Accounts receivable	12,980	8,664	(1,736)	(7,600)
	(16,165)	(10,891)	(20,149)	(1,604)
Prepaid expenses	(1,750)	(457)	(641)	(154)
Accounts payable and accrued liabilities	2,616	5,051	8,931	9,146
	(2,319)	2,367	(13,595)	(212)

#### Supplemental information:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Income taxes paid (received)	-	(5)	14	(5)
Additions to property, plant and equipment included in accounts payable and accrued liabilities	5,452	1,316	5,452	1,316

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 16. Supplemental disclosure of cash flow information (continued)

Cash and cash equivalents consist of:

	September 30, 2011	September 30, 2010
	\$	\$
Cash	6,700	24,952
Restricted cash (Note 8)	112	109
	<u>6,812</u>	<u>25,061</u>

### 17. Financial instruments

#### Derivative financial instruments

##### *Natural gas contract*

The Company was a party to a gas supply agreement pursuant to which it agreed to purchase approximately 100% of its expected consumption of gas through October 2010. From December 2009 to October 2010, the Company purchased gas under the agreement at market rates, leaving only the transportation portion of the gas agreement at fixed rates. The transportation portion of this agreement met the definition of a derivative financial instrument. All gains or losses to September 30, 2010 have been recognized in the statement of earnings.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 17. Financial instruments (continued)

#### Other information

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
<b>Financial expenses</b>				
Interest on long-term debt and Debentures	1,926	2,530	6,743	8,758
Interest capitalized on term facility and interest accretion on Debentures	-	465	513	2,551
Interest on PSIF - Investissement Québec	60	68	197	201
Amortization of deferred financing fees	219	374	974	1,005
Write-off of deferred financing fees	-	678	-	678
Other financial expenses	156	229	433	494
	<b>2,361</b>	<b>4,344</b>	<b>8,860</b>	<b>13,687</b>
<b>Loss (gain) on financial instruments</b>				
Loss (gain) on financial instrument (*)	8	-	(797)	-
Gain on redemption of Debentures (Note 12)	-	-	(2,752)	-
Loss on Debenture derivative	-	-	-	3,329
Master Retail Gas Sales Agreement	-	(94)	-	(98)
	<b>8</b>	<b>(94)</b>	<b>(3,549)</b>	<b>3,231</b>
<b>(Gain) loss on foreign currency translation</b>				
Cash and cash equivalents denominated in foreign currency	(455)	469	374	421
Loans and receivables	(5,119)	1,695	(3,512)	705
Other	224	(109)	140	(147)
	<b>(5,350)</b>	<b>2,055</b>	<b>(2,998)</b>	<b>979</b>

\*: In December 2010, the Company was allocated an initial 236,226 common shares of AbitibiBowater Inc. as partial settlement for a claim filed pursuant to the procedures undertaken by AbitibiBowater Inc. under the *Companies' Creditors Arrangement Act*, resulting in a gain on settlement of claim totalling \$5,544. A minimal amount of common shares of AbitibiBowater Inc. have been reserved for the benefit of holders of disputed claims and could be distributed subsequently to unsecured creditors in accordance with the terms of the plan of reorganization. On February 3, 2011, the Company sold the 236,226 common shares at a market price of \$26.75 per share resulting in a gain of \$763 net of transaction fees. In April 2011, the Company was allocated an additional 2,122 common shares of AbitibiBowater Inc. from the reserved common shares resulting in an unrealized gain totalling \$34.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report

periods ended September 30, 2011 and 2010

(in thousands of Canadian dollars, except per share amounts)

(unaudited)

### 18. Segmented information

Management has determined that the Company operates in two reportable segments, namely the manufacturing of premium NBSK pulp at the Saint-Félicien mill and the manufacturing of premium RBK pulp at the Fairmont and Menominee mills.

Segmented information is summarized as follows:

	Three months ended September 30, 2011		
	NBSK mill	RBK mills	Total
	\$	\$	\$
Sales	<b>67,084</b>	<b>71,183</b>	<b>138,267</b>
Cost of product sold	<b>46,530</b>	<b>65,362</b>	<b>111,892</b>
Delivery costs	<b>5,289</b>	<b>5,031</b>	<b>10,320</b>
Selling and administrative expenses	<b>1,794</b>	<b>1,887</b>	<b>3,681</b>
Depreciation	<b>7,255</b>	<b>1,329</b>	<b>8,584</b>
Profit (loss) from operations	<b>6,216</b>	<b>(2,426)</b>	<b>3,790</b>

	Three months ended September 30, 2010		
	NBSK mill	RBK mills	Total
	\$	\$	\$
Sales	64,903	67,274	132,177
Cost of product sold	39,511	60,181	99,692
Delivery costs	4,961	4,734	9,695
Selling and administrative expenses	1,086	1,628	2,714
Depreciation	6,932	1,496	8,428
Profit (loss) from operations	12,413	(765)	11,648

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 18. Segmented information (continued)

	Nine months ended September 30, 2011		
	NBSK mill	RBK mills	Total
	\$	\$	\$
Sales	<b>213,683</b>	<b>205,007</b>	<b>418,690</b>
Cost of product sold	<b>147,772</b>	<b>182,437</b>	<b>330,209</b>
Delivery costs	<b>16,726</b>	<b>15,810</b>	<b>32,536</b>
Selling and administrative expenses	<b>5,363</b>	<b>5,841</b>	<b>11,204</b>
Depreciation	<b>22,581</b>	<b>4,061</b>	<b>26,642</b>
Profit (loss) from operations	<b>21,241</b>	<b>(3,142)</b>	<b>18,099</b>

	Nine months ended September 30, 2010		
	NBSK mill	RBK mills	Total
	\$	\$	\$
Sales	212,773	212,312	425,085
Cost of product sold	144,402	182,470	326,872
Delivery costs	16,190	15,201	31,391
Selling and administrative expenses	3,892	5,104	8,996
Depreciation	21,510	4,423	25,933
Profit from operations	26,779	5,114	31,893

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 18. Segmented information (continued)

	Three months ended September 30, 2011			Nine months ended September 30, 2011		
	NBSK mill	RBK mills	Total	NBSK mill	RBK mills	Total
	\$	\$	\$	\$	\$	\$
Acquisition of property, plant and equipment	<b>3,831</b>	<b>1,188</b>	<b>5,019</b>	<b>6,863</b>	<b>3,365</b>	<b>10,228</b>

	Three months ended September 30, 2010			Nine months ended September 30, 2010		
	NBSK mill	RBK mills	Total	NBSK mill	RBK mills	Total
	\$	\$	\$	\$	\$	\$
Acquisition of property, plant and equipment	2,846	1,100	3,946	6,558	2,215	8,773

	September 30, 2011			December 31, 2010		
	NBSK mill	RBK mills	Total	NBSK mill	RBK mills	Total
	\$	\$	\$	\$	\$	\$
Property, plant and equipment	<b>284,816</b>	<b>84,903</b>	<b>369,719</b>	300,514	82,095	382,609
Total assets	<b>371,163</b>	<b>182,461</b>	<b>553,624</b>	396,100	159,800	555,900

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 18. Segmented information (continued)

Geographic information related to sales is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Canada	8,105	5,685	24,007	34,125
United States	106,673	104,572	321,402	302,688
Europe	17,999	18,798	54,353	64,209
Others	5,490	3,122	18,928	24,063
	<b>138,267</b>	132,177	<b>418,690</b>	425,085

Sales have been allocated to geographic regions based on the region in which the customer is domiciled. All property, plant and equipment of the NBSK mill are located in Canada and all property, plant and equipment of the RBK mills are located in the United States.

For the nine-month period ended September 30, 2011, sales to two customers representing 10% or more of the Company's total sales reached \$98,755 (\$54,940 and \$43,815) spread among NBSK and RBK segments. For the nine-month period ended September 30, 2010, only one major customer contributed for \$58,466 of the Company's total sales, also spread among NBSK and RBK segments.

### 19. Special termination benefits

On December 1, 2009, the Company announced a reorganization of its activities in its NBSK and RBK mills which took effect in the last quarter of 2009 and at the beginning of 2010. As a result, expenses of \$Nil were recognized in the three and nine-month periods ended September 30, 2011 relating to separation payments for terminated employees (2010: a credit of \$8 and an expense of \$877); the expenses are included in Cost of products sold and Selling and administrative expenses.

	September 30, 2011	December 31, 2010
	\$	\$
Special termination benefit liability		
Balance, beginning of period	68	1,237
Benefits incurred	-	879
Benefits paid	(5)	(2,048)
Balance, end of period	<b>63</b>	68

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 20. Related party transactions and balances

Related party transactions conducted in the normal course of business are measured at the exchange value (the amount established and agreed to by the related parties), unless specific requirements within IFRS require different treatment.

Compensation of Directors and key management:

	Three months ended September 30,		Nine months ended September 30	
	2011	2010	2011	2010
	\$	\$	\$	\$
Short-term benefits	712	974	2,096	2,345
Post-employment benefits	31	15	158	105
Termination benefits	-	(6)	-	639
Share-based compensation	61	164	506	312
	<b>804</b>	1,147	<b>2,760</b>	3,401

### 21. Conversion to IFRS

#### *i) Overview*

The Canadian Accounting Standards Board determined that IFRS replaced previous Canadian GAAP for publicly accountable enterprises, including the Company, for interim financial report and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

This condensed consolidated interim financial report is prepared in accordance with IAS 34 using accounting policies consistent with IFRS. Prior to January 1, 2011, the Company prepared its interim and annual consolidated financial statements in accordance with Canadian GAAP.

The accounting policies described in Note 2 have been selected to be consistent with the IFRS expected to be in effect on December 31, 2011, the Company's first annual IFRS reporting date.

#### *ii) First-time adoption of IFRS*

The adoption of IFRS requires the application of IFRS 1, which provides guidance for an entity's initial adoption of IFRS. IFRS 1 generally requires retrospective application of IFRS effective at the end of its first annual IFRS reporting period. However, IFRS 1 also provides optional exemptions and mandatory exceptions to this retrospective treatment.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 21. Conversion to IFRS (continued)

#### *ii) First-time adoption of IFRS (continued)*

The Company has elected to apply the optional exemptions, as outlined in Note 22 of the condensed consolidated interim financial report for the period ended March 31, 2011, in its preparation of an opening IFRS statement of financial position as at January 1, 2010, the Company's Transition Date.

IFRS 1 does not permit changes to estimates that have been made previously. Accordingly, estimates used in the preparation of the Company's opening IFRS statement of financial position as at the Transition Date are consistent with those made under current Canadian GAAP.

The Company's IFRS condensed consolidated statement of financial position as at the Transition Date is included as comparative information in *iv)* below.

#### *iii) Changes to accounting policies*

The Company has changed certain accounting policies to be consistent with IFRS as is expected to be effective on December 31, 2011, the Company's first annual IFRS reporting date.

The following summarizes the significant changes to the Company's accounting policies on adoption of IFRS.

#### **Property, Plant & Equipment**

IAS 16 *Property, Plant and Equipment* ("IAS 16") requires the Company to choose, for each class of capital assets, between the cost model and the revaluation model. The Company has selected the cost model in accounting for all of its capital assets.

The Company has changed its accounting policies to reflect the requirement under IAS 16 that when an item of property, plant and equipment comprises major components with different useful lives, the components are amortized separately over their respective useful lives.

#### **Impairment of Assets**

IAS 36 *Impairment of Assets* ("IAS 36") requires a write-down of assets if the recoverable amount (defined as the greater of the fair value less costs to sell and the value in use of an asset or a cash generating unit) is less than its carrying amount. Value in use is determined using discounted estimated future cash flows. Under Canadian GAAP, a write down to estimated fair value was required only if the undiscounted estimated future cash flows of a group of assets were less than its carrying amount. The Company has changed its accounting policies related to impairment of assets to be consistent with the requirements under IFRS.

IAS 36 also requires the reversal of any previous impairment losses, with the exception of goodwill, where circumstances have changed such that the level of impairment in the value of the assets has been reduced. Canadian GAAP prohibits the reversal of impairment losses.

# **FIBREK INC.**

## **Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)**

---

### **21. Conversion to IFRS (continued)**

#### *iii) Changes to accounting policies (continued)*

##### **Impairment of Assets (continued)**

Under IFRS the determination of an impairment is calculated on a different basis from Canadian GAAP. As a result of the transition, the Company carried out a review of the recoverable amount of plant and related equipment in its business units. This review led to the recognition of an impairment loss of \$136,964, which has been recognized directly into the opening deficit and accumulated other comprehensive income as a component of the transition to IFRS.

The recoverable amount of the relevant assets has been determined on the basis of their value in use. The discount rate used in measuring value was 12% per annum. There was no impairment previously under Canadian GAAP.

##### **Provisions**

IFRS requires the recognition of a decommissioning liability for legal or constructive obligations, while Canadian GAAP required the recognition of such liabilities only for legal obligations. A constructive obligation exists when an entity has created reasonable expectations that it will take certain actions.

The Company has changed its accounting policies to reflect these requirements, however this change did not result in the recognition of additional provisions. Therefore, under IFRS, no constructive obligation was recognized.

##### **Financial Instruments**

IFRS requires that the liability portion of compound instruments be evaluated first and the residual allocated to equity, which is the case for the Convertible Debentures. Under Canadian GAAP, there are no specific requirements. The Company has changed its valuation method for compound instruments to be consistent with the requirements under IFRS.

##### **Employee Benefits**

IFRS requires that the past service cost element of defined benefit plans be expensed on an accelerated basis, with vested past service costs expensed immediately and unvested past service costs recognized on a straight-line basis over the vesting period. Under Canadian GAAP, past service costs were generally amortized on a straight-line basis over the expected average remaining service period of active employees under the plan.

The Company's accounting policies related to employee benefits have been changed to reflect these requirements under IFRS.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 21. Conversion to IFRS (continued)

#### iv) Reconciliations of Canadian GAAP to IFRS

The following provides reconciliations from Canadian GAAP to IFRS on the Transition Date.

	Note	December 31, 2009 (Canadian GAAP)	Transition Adjustments	January 1, 2010 (IFRS)
<b>Assets</b>				
Current assets				
Cash and cash equivalents		19,174	-	19,174
Accounts receivable		53,424	-	53,424
Inventories	c	79,003	(748)	78,255
Prepaid expenses		4,036	-	4,036
		155,637	(748)	154,889
Deferred financing fees		421	-	421
Property, plant and equipment	a,b	542,360	(134,918)	407,442
Intangible assets	a	395	(86)	309
Other assets		856	-	856
		699,669	(135,752)	563,917
<b>Liabilities</b>				
Current liabilities				
Accounts payable and accrued liabilities		45,213	-	45,213
Landfill closure liability		445	-	445
Derivative instruments		113	-	113
Current portion of long-term debt		36,682	-	36,682
		82,453	-	82,453
Debenture derivative at fair value through profit or loss	d	-	859	859
Landfill closure liability	e	2,075	1,091	3,166
Employee benefits	f	14,022	10,538	24,560
Convertible unsecured subordinated debentures		47,696	-	47,696
Long-term debt		118,776	-	118,776
		265,022	12,488	277,510
<b>Equity</b>				
Unitholders' Capital		658,609	-	658,609
Equity Component of Debentures	d	6,242	(6,242)	-
Deficit		(225,500)	(146,702)	(372,202)
Other Comprehensive Income	g	(4,704)	4,704	-
		434,647	(148,240)	286,407
		699,669	(135,752)	563,917

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

### 21. Conversion to IFRS (continued)

#### iv) Reconciliations of Canadian GAAP to IFRS (continued)

##### Reconciliation of Equity

	Note	December 31, 2010	September 30, 2010
		\$	\$
Equity under Canadian GAAP		472,508	481,842
Reconciling items:			
Property, Plant and Equipment, and Intangible assets	a, b	(120,933)	(128,790)
Employee Benefits	f	(15,185)	(10,276)
Inventories	c	(578)	(735)
Landfill Closure Liability	e	(539)	(1,436)
Debenture derivative	d	-	-
Equity under IFRS		335,273	340,605

##### Reconciliation of comprehensive income (loss):

	Note	Year ended December 31, 2010	Nine months ended September 30, 2010	Three months ended September 30, 2010
		\$	\$	\$
Comprehensive (loss) income under Canadian GAAP		(344)	9,107	130
Reconciling items:				
Property, Plant and Equipment, and Intangible assets	a, b	11,134	5,085	1,842
Employee Benefits	f	350	262	87
Inventories	c	160	7	(311)
Landfill Closure Liability	e	490	(369)	(70)
Debenture derivative	d	(3,329)	(3,329)	-
Unrealized gain (loss) on translation of financial statements of foreign operations	g	3,009	1,159	1,656
Comprehensive income (loss) under IFRS		11,470	11,922	3,334

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 21. Conversion to IFRS (continued)

#### *iv) Reconciliations of Canadian GAAP to IFRS (continued)*

##### Explanation of Reconciling Items

#### *a) Impairment of Assets*

On retrospective application of the new accounting policy related to impairment of assets the Company has reduced the carrying amount of certain assets to their value in use as at the Transition Date. As a result, the carrying amount of property, plant and equipment and intangible assets was reduced by \$136,964 with a corresponding reduction of equity at January 1, 2010.

#### *b) Property, Plant and Equipment*

The new accounting policy related to property, plant and equipment was applied retrospectively as at the Transition Date. As a result of applying the change in accounting policy to account for major components of items of property, plant and equipment as separate items, the carrying value of property, plant and equipment was reduced by \$2,722 as at January 1, 2010. A corresponding \$2,722 decrease in equity was recorded at January 1, 2010.

IAS 16 requires for major inspections and overhauls to be accounted as a separate component of property, plant and equipment. The Company has determined that, under IFRS, a significant part of its major maintenance program qualifies as a separate component of property, plant and equipment. As at January 1, 2010 the carrying value of property, plant and equipment was increased by \$4,682 with a corresponding increase in equity.

For the periods ended December 31 and September 30, 2010, this change modified profit from operations by reducing cost of products sold and increasing depreciation.

The change in policy also increased expenditures on items of property, plant and equipment reported in the statements of cash flows by \$6,594 for the year ended December 31, 2010, and by \$506 and \$2,054 for the three and nine-month periods, respectively ended September 30, 2010.

#### *c) Inventories*

The valuation of the pulp cost was affected by the application of the new accounting policies relating to impairment and property, plant and equipment as depreciation expenses are part of the pool of cost to determine the weighted average cost.

#### *d) Equity component of Debentures*

Under Canadian GAAP, the option related to the Convertible Debentures was recognized as equity. Under IFRS and until the effective date of the Arrangement, the conversion option was recognized as a financial liability measured at fair value through profit or loss. The effect of this change was recognized in the Company's equity.

# FIBREK INC.

## Notes to the condensed consolidated interim financial report periods ended September 30, 2011 and 2010 (in thousands of Canadian dollars, except per share amounts) (unaudited)

---

### 21. Conversion to IFRS (continued)

#### *iv) Reconciliations of Canadian GAAP to IFRS (continued)*

Explanation of Reconciling Items (continued)

#### *e) Landfill closure liability*

On adoption of IFRS, the Company's accounting policy was changed to follow the guidance of IFRIC 1, which resulted in an increase of the landfill closure liability of \$1,091 as at January 1, 2010, with a corresponding decrease in equity.

#### *f) Employee Benefits*

On adoption of IFRS, the Company's accounting policy related to employee benefits was changed so that vested past service costs are expensed immediately and unvested past service costs are recognized on a straight-line basis over the vesting period. The accounting policy was also changed so that actuarial gains or losses are recognized immediately in other comprehensive income. In addition, the Company elected to apply the first-time adoption exemption to recognize all unrecognized actuarial gains and losses at the Transition Date in the deficit.

The application of the first-time exemption and the retrospective application of the changes in the accounting policy resulted in an increase in the employee benefit obligation of \$10,538 as at January 1, 2010, with a corresponding decrease in equity.

#### *g) Foreign Currency Translation*

The Company elected to apply the first-time adoption exemption to recognize the unrealized loss on translation of financial statements of self-sustaining subsidiary at the Transition Date immediately in the deficit. As a result, the accumulated other comprehensive loss was reduced to zero, and the deficit was increased by \$4,704 as at January 1, 2010. The net effect on total equity was zero.

For the periods ended December 31 and September 30, 2010, the IFRS transition changes relating to the translation of the self-sustaining subsidiary modified the comprehensive income.

#### *h) Presentation Reclassification*

IFRSs permit a choice as to how cash flows from interests paid are classified, so that the classification is consistent from period to period. Management has decided to present interests paid as financing activities since these represent costs of obtaining financial resources.