



# **2017 ANNUAL REPORT**

Ten Peaks Coffee Company Inc.

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## Management's Discussion and Analysis

*This Management's Discussion & Analysis ("MD&A") of Ten Peaks Coffee Company Inc. ("Ten Peaks" or the "Company"), dated as of March 20, 2018, provides a review of the financial results for the three and 12 months ended December 31, 2017 relative to the comparable periods of 2016. The three-month period represents the fourth quarter ("Q4") of our 2017 fiscal year. This MD&A should be read in conjunction with Ten Peaks' audited consolidated financial statements for the year ended December 31, 2017, which are available at [www.sedar.com](http://www.sedar.com).*

*All financial information is presented in Canadian dollars, unless otherwise specified.*

## FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements, including statements regarding the future success of our business and market opportunities. Forward-looking statements typically contain words such as "believes", "expects", "anticipates", "continue", "could", "indicates", "plans", "will", "intends", "may", "projects", "schedule", "would" or similar expressions suggesting future outcomes or events, although not all forward-looking statements contain these identifying words. Examples of such statements include, but are not limited to, statements concerning: (i) expectations regarding Ten Peaks' future success in various geographic markets; (ii) future financial results including anticipated future sales and processing volumes; (iii) future dividends; (iv) the expected actions of the third parties described herein; (v) factors affecting the coffee market including supplies and commodity pricing; and (vi) the business and financial outlook of Ten Peaks. In addition, this MD&A contains financial outlook information that is intended to provide general guidance for readers based on our current estimates, but which is based on numerous assumptions and may prove to be incorrect. Therefore, such financial outlook information should not be relied upon by readers. These statements are neither promises nor guarantees but involve known and unknown risks and uncertainties that may cause our actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed in or implied by these statements. These risks include, but are not limited to, risks related to processing volumes and sales growth, operating results, supply of coffee, general industry conditions, commodity price risks, technology, competition, foreign exchange rates, construction timing, costs and financing of capital projects, general economic conditions and those factors described herein under the heading 'Risks & Uncertainties'.

The forward-looking statements contained herein are also based on assumptions that we believe are current and reasonable, including but not limited to, assumptions regarding: (i) trends in certain market segments and the economic climate generally; (ii) the financial strength of our customers; (iii) the value of the Canadian dollar versus the US dollar; (iv) the expected financial and operating performance of Ten Peaks going forward; and (v) the expected level of dividends payable to shareholders. We cannot assure readers that actual results will be consistent with the statements contained in this MD&A. The forward-looking statements and financial outlook information contained herein are made as of the date of this MD&A and are expressly qualified in their entirety by this cautionary statement. Except to the extent required by applicable securities law, Ten Peaks undertakes no obligation to publicly update or revise any such statements to reflect any change in our expectations or in events, conditions, or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those described herein.

## EXECUTIVE SUMMARY

During 2017, we recorded record volumes and revenues, as well as year-over-year improvements in our financial results. Strong growth in the first nine months of the year was offset somewhat in the fourth quarter, as anticipated. A summary of our financial results is shown in the table below:

<i>In \$000s except per share amounts</i>	<b>3 months ended December 31, 2017</b>		<b>3 months ended December 31, 2016</b>		<b>12 months ended December 31, 2017</b>		<b>12 months ended December 31, 2016</b>	
Revenue	\$	20,662	\$	22,449	\$	83,755	\$	81,927
Gross profit		3,178		3,215		12,590		12,050
Operating income		958		1,526		4,812		5,017
Net income		(380)		1,328		4,160		4,149
EBITDA <sup>1</sup>		1,334		1,998		6,923		5,772
<b>Per share:</b>								
Earnings per share, <sup>2</sup> basic	\$	(0.04)	\$	0.15	\$	0.46	\$	0.46
Earnings per share, <sup>2</sup> diluted		(0.04)		0.15		0.42		0.46
Dividend declared		0.0625		0.0625		0.25		0.25

<sup>1</sup> EBITDA is defined under 'Non-IFRS Measures' of this MD&A, which is a "Non-GAAP Financial Measure" as defined by CSA Staff Notice 52-306.

<sup>2</sup> Per-share calculations are based on the weighted average number of shares outstanding during the period.

Our improved financial results for the year ended December 31, 2017 primarily reflect our higher volumes, as we continued to gain market share against our competitors. More importantly, our full year volumes were the highest in SWDCC's history, growing by 5% over 2016 with a slight year-over-year decline in the fourth quarter volumes of 2%. Q4 2016 represented the highest quarterly volume in SWDCC's history until the third quarter of 2017, when a new company record was set for quarterly volumes.

Shipments to roasters increased by 6% for the fourth quarter and by 2% for the full year, while shipments to importers decreased by 17% in Q4 and increased by 11% in the full year, compared to the same periods last year. Volumes to our specialty accounts grew by 4% in the fourth quarter and by 9% for the full year. Shipments to our commercial accounts decreased by 5% in the fourth quarter, while 12-month shipments to commercial accounts rose by 2%.

Revenue for the fourth quarter decreased by 8% to \$20.7 million, primarily due to a lower coffee commodity price, or New York 'C' (NY'C'), compared to the same quarter of 2016. Revenue for the full year rose by 2% to \$83.8 million. Revenue grew in all three categories in 2017, primarily due to the higher volume of shipments.

Gross profit declined by 1%, to \$3.2 million in the fourth quarter. Seaforth's warehousing business grew faster than anticipated in 2017, which resulted in increased warehouse, transportation and labour costs being incurred during the fourth quarter to alleviate backlogs. For the full year, gross profit rose by \$0.5 million, or 4%, to \$12.6 million. The increase was mainly related to higher process revenue, which grew with our increased volumes.

Operating expenses increased in the fourth quarter and for the full year by \$0.5 million and \$0.7 million, or 31% and 11%, respectively. For both periods, the year-over-year increase reflects higher staffing and staff-related expenses including stock-based compensation.

Operating income was down by \$0.6 million, or 37%, to \$1.0 million for the fourth quarter. For the full year, operating income declined by \$0.2 million, or 4%, to \$4.8 million.

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Two non-cash items – a loss on foreign exchange and a loss on the fair value of the embedded option – reduced earnings by \$1.1 million in the fourth quarter. Overall, we recorded a net loss of \$0.4 million in the period, compared to net income of \$1.3 million in Q4 2016. For the full year, net income totaled \$4.2 million. This was unchanged from 2016, as the increases in our gross profit, gains on risk management activities, and a gain on the embedded option were offset by higher operating costs and financing costs.

EBITDA for the fourth quarter decreased by \$0.7 million, or 33%, to \$1.3 million, owing to increased operating costs and reduced gains on risk management activities. For the full year, EBITDA increased by \$1.2 million, or 20%, to \$6.9 million. The increase for 2017 was driven by higher volumes and operating income, as well as improved performance on our risk management activities.

## **BUSINESS OVERVIEW**

Ten Peaks is a leading specialty coffee company doing business through two wholly owned subsidiaries, Swiss Water Decaffeinated Coffee Company Inc. (“SWDCC”) and Seaforth Supply Chain Solutions Inc. (“Seaforth”).

SWDCC is a premium green coffee decaffeinator located in Burnaby, BC, Canada. SWDCC employs the proprietary SWISS WATER® Process to decaffeinate green coffee without the use of chemicals, leveraging science-based systems and controls to produce coffee that is 99.9% caffeine free. We believe that the SWISS WATER® Process is the world’s only 100% chemical free water process for third-party coffee decaffeination. It is certified organic by the Organic Crop Improvement Association and is also the world’s only consumer-branded decaffeination process. Decaffeinating without the use of chemicals is our primary business and the financial results of Ten Peaks are dependent upon the results of SWDCC.

Seaforth provides a complete range of green coffee logistics services including devanning coffee received from origin; inspecting, weighing and sampling coffees; and storing, handling and preparing green coffee for outbound shipments. Seaforth provides all of SWDCC’s local green coffee handling and storage services. In addition, Seaforth handles and stores coffees for several other coffee importers and brokers, and is the main green coffee handling and storage company in Metro Vancouver. Seaforth is organically certified by Ecocert Canada.

As at December 31, 2017, the consolidated financial statements of Ten Peaks included the accounts of Ten Peaks; our wholly owned subsidiaries SWDCC and Seaforth; and two wholly owned subsidiaries of SWDCC, Swiss Water Decaffeinated Coffee Company USA, Inc., and Swiss Water Process Marketing Services Inc. At the end of 2017, Swiss Water Process Marketing Services Inc. was dissolved and its assets and liabilities were assumed by SWDCC. Inter-company accounts and transactions have been eliminated on consolidation.

Ten Peaks’ shares trade on the Toronto Stock Exchange under the symbol ‘TPK’. As at the date of this report 9,061,210 shares were issued and outstanding.

### **Swiss Water Decaffeinated Coffee Company’s Business**

We carry an inventory of premium-grade Arabica coffees that we purchase from the specialty green coffee trade, decaffeinate and then sell to our customers (our “regular” or “non-toll” business). Revenue from our regular business includes both processing revenue and green coffee cost recovery revenue.

We also decaffeinate coffee owned by our customers for a processing fee under toll arrangements (our “toll” business). The value of the coffee processed under toll arrangements does not form part of our inventory, our revenue or our cost of sales. Revenue from toll arrangements consists entirely of processing revenue. In 2017, 22% of the coffee we processed was under toll arrangements, with the balance being regular green coffee sales.

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Our cost of sales is comprised primarily of the cost of green coffee purchased for our regular business, plant labour and other processing costs directly associated with our production facility. This incorporates an allocation of fixed overhead costs, which includes depreciation of our production equipment and amortization of our proprietary process technology.

For our regular business, we work with coffee importers to source premium-grade green coffees from coffee-producing countries located in Central and South America, Africa and Asia. The purchase price is based on the NY'C' coffee futures price on the IntercontinentalExchange, plus a quality differential. The NY'C' component typically makes up more than 80% of the total cost of green coffee, while the quality differential typically accounts for less than 20%. Both the NY'C' price and the quality differential fluctuate in response to fundamental commodity factors that affect supply and demand.

### *Business Strategy*

SWDCC seeks to maintain and enhance profitability and cash flows from operations by pursuing the following business strategies:

- *Offer Superior Quality, 100% Chemical Free Decaffeinated Coffees* – We support our premium brand position by offering superior quality coffees. This starts with buying premium Arabica coffees from top exporters and importers, as the quality of the green coffee directly affects the quality of the finished product. We then ensure the quality and integrity of the original green coffee is maintained throughout our proprietary production process. We operate under the Food Safety Systems Certification (FSSC) 22000 that manages our food safety, as well as HACCP (Hazard Analysis Critical Control Points) and quality assurance programs. In addition, our proprietary carbon management technology captures caffeine while protecting the coffee's body and flavour characteristics. Finally, because we control all aspects of caffeine removal, we can ensure that our process remains 100% chemical free and that our carbon and our green coffee extract never come into contact with methylene chloride. We believe this is an important and relevant competitive distinction that underscores the integrity of our chemical free positioning.
- *Continuously Improve our Production Process* – We are committed to continuous improvement throughout our production process, and to leading the coffee industry in the science of decaffeination. This allows us to further enhance our proprietary process and provide superior quality coffees to our customers. Through Six Sigma methodologies, statistical process controls and lean manufacturing initiatives, we have dramatically improved our production process, thereby improving our production efficiencies, while reducing defects. In addition, these improvements have allowed us to make tangible improvements to the quality of the coffee we process. SWISS WATER® Process decaffeinated green coffees now more closely resemble regular green coffees, which makes it much easier to visually gauge roast level and stage during the roasting process. Additionally, improvements we have made to our proprietary carbon renewal process have resulted in notable improvements at the "cupping", or tasting table. Due to better retention of chlorogenic and amino acids (naturally occurring acids and antioxidants in green coffee which form a key part of a coffee's taste profile) our coffees have better body and flavour than ever before.
- *Create Consumer Demand by Developing Brand Awareness* - Strong brand awareness levels, premium quality and consumer demand encourage retailers to carry decaffeinated coffee products bearing the SWISS WATER® Process brand name. Therefore, we strategically invest in a range of cost-effective initiatives designed to enhance awareness of the SWISS WATER® Process brand and our chemical free proposition, and to increase demand at the consumer level. These activities include regionally

targeted media campaigns; public relations; customer co-marketing events; social media; and website management.

- *Leverage Higher Margin Selling Proposition to Retailers* – As health-aware consumers are willing to pay a premium for healthy food options, coffee retailers can improve their margins - particularly on a by-cup or by-drink basis – simply by switching to chemical free SWISS WATER® Process coffees. This makes our sales proposition very attractive and is a key leverage point in our business development program with major roaster retailers and premium street retail accounts. In addition to higher margins, these retailers are ideally positioned to benefit from the significant value-added elements of the SWISS WATER® Process brand. These include our ongoing efforts to build brand awareness, consultative selling, extensive merchandising programs, and web-based merchandising material fulfillment and customer education tools.

#### *Business and Geographic Segments*

During the year ended December 31, 2017, our only business segment was the decaffeination of green coffee. Due to its relatively small size, results of our Seaforth coffee-handling subsidiary are not separated out for reporting purposes. Our largest geographical market by volume was the United States, followed by Canada, and other international markets. By dollar value, 46% of our sales were to customers located in the United States, 42% were to Canada, and the remaining 12% were to other countries.

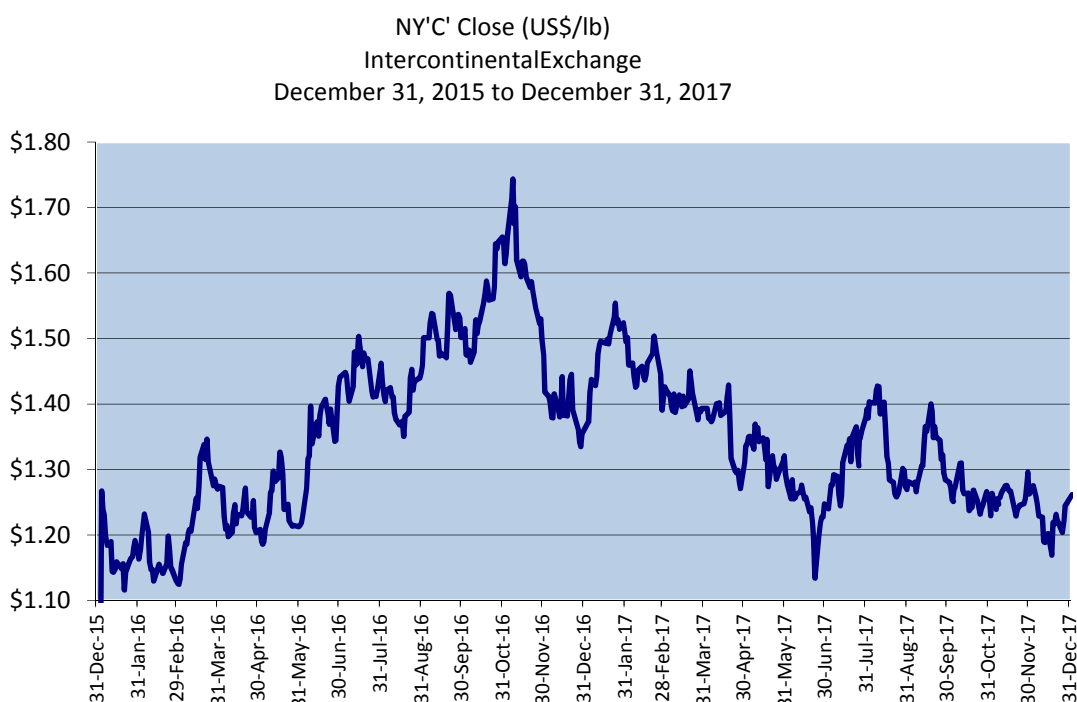
#### *Commodity Futures*

We use derivative instruments to offset the effect of movements in the NY'C' component of coffee pricing between the time we commit to purchase green coffee at a fixed price and the time we sell decaffeinated green coffee to our customers. Our commodity price risk mitigation strategy requires us to short sell a futures contract for one lot (37,500 lbs) of coffee on the IntercontinentalExchange whenever we agree to buy one lot of coffee from a supplier at a fixed price. The short sale protects us from changes in the price of coffee while purchase orders are outstanding and while we hold the coffee in inventory. An increase (decrease) in the NY'C' price will generate an increase (decrease) in the value of the coffee we hold in inventory, and an equivalent decrease (increase) in the value of the derivative instrument. As coffee is sold, the short sales are covered by purchasing offsetting long contracts on the IntercontinentalExchange.

There is no open market to hedge the quality differential component of our green coffee cost. Therefore, in periods of rising differential markets, we may experience a differential cost recovery gain, and in periods of falling differential markets, we may experience a differential cost recovery loss.

Volatility in the NY'C' generates gains or losses on the derivative financial instruments that we hold. These gains and losses offset corresponding losses or gains in the value of the inventory we hold. In 2016, we adopted hedge accounting under International Financial Reporting Standards ("IFRS"), which now allows us to match gains and losses on our derivative financial instruments with the underlying hedged item (e.g. inventory and purchase commitments).

The chart below shows the movement in the NY'C' for the last eight quarters:



In 2017, the NY'C' averaged US\$1.25 in the fourth quarter and US\$1.33 for the year, compared to an average of US\$1.52 in Q4 2016 and US\$1.36 in 2016. The rise and fall of the NY'C' affects our volume of shipments, our revenues and our cost of sales. After the NY'C' reached a seven-year low in January 2016, it rose steadily through the year before peaking in November 2016. In an upward trending market, our customers tend to consume their inventories rather than build them. Subsequently, the NY'C' fell sharply in December, closing 2016 at US\$1.37 per pound. During 2017, the NY'C' declined gradually in the first two quarters, rose somewhat in the third quarter and fell again in the fourth quarter, closing the year at US\$1.26 per pound. When the NY'C' declines over a sustained period, our customers tend to add to their inventories.

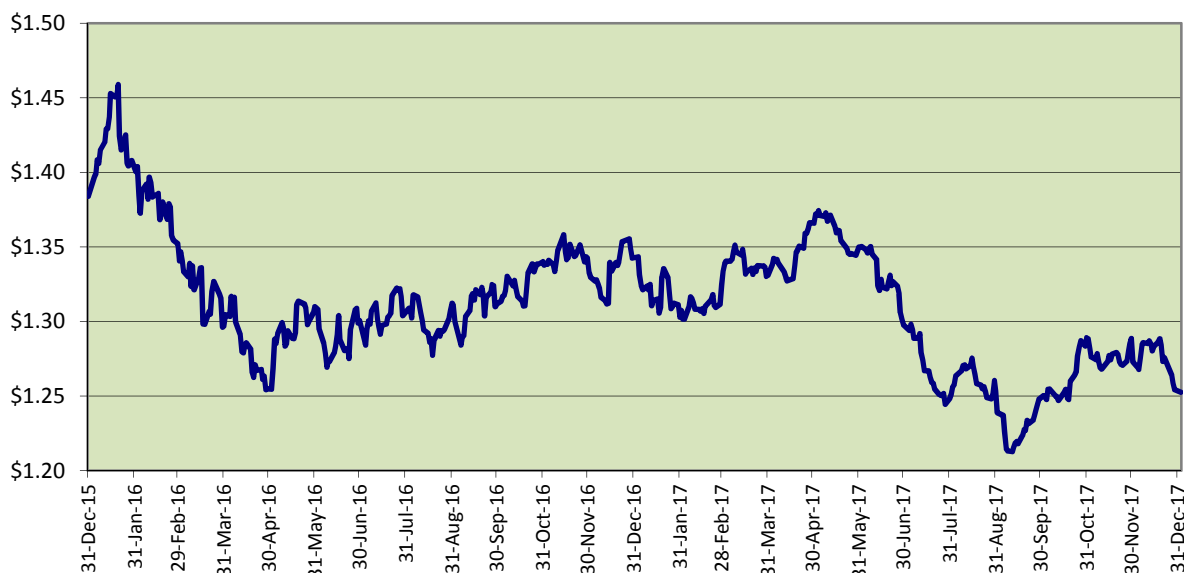
#### *Currency Forwards*

Coffee is traded in US\$, as buyers and sellers reference the NY'C' coffee price when entering into contracts. As a result, the majority of our revenues are denominated in US\$, while a significant portion of our expenses and cash outflows occur in Canadian dollars ("C\$"). Therefore, our financial results are affected by any significant fluctuation in US\$/C\$ exchange rates. In accordance with our foreign exchange risk management policy, we use financial instruments to manage our currency risk based on estimates of our net US\$ cash flows up to 60 months in advance. We purchase forward contracts to sell US\$ at fixed future dates and exchange rates. This enables us to more reliably predict how much Canadian currency we will receive for our US\$ sales. Cash flows in the immediate 12-month period are hedged at a higher percentage of expected future cash flows than those farther out, reflecting greater uncertainty in the 13 to 60-month period. In accordance with our risk management policy, as our assumptions about the timing and amount of US\$ cash flows change over time, we enter into offsetting forward contracts to buy US\$ as required to eliminate any over-hedged positions.

In addition, our risk management policies require us to enter into forward contracts to purchase US\$ when we have large, predictable outlays of US\$ for upcoming expenses or purchase commitments. This allows us to fix the exchange rate for purchases or expenses, as applicable, at the time the commitment is entered into.

The chart below illustrates the US\$/C\$ exchange rates for the last eight quarters:

US Dollars to Canadian Dollars  
Bank of Canada Noon Rates  
December 31, 2015 to December 31, 2017



In Q4 2017, the US\$ averaged \$1.27 Canadian, a decrease of 5% over the same period in 2016. For the full year, the US\$ averaged \$1.30 Canadian, which was 2% lower than in 2016. The US\$/C\$ exchange rate was relatively stable in the first five months of last year, before declining rapidly between May and the end of August. When the US\$ declines rapidly, it reduces our gross profit on green coffee revenues, as we sell our coffee at a lower US\$ than we purchased it for.

### KEY PERFORMANCE DRIVERS

The following key performance drivers are critical to the successful implementation of our strategy and ability to improve profitability and cash from operations:

#### *External Factors*

- *Coffee Commodity Prices* – We buy and sell coffees based on the NY'C' and the quality differentials for specified coffees, both of which rise and fall in response to changes in supply and demand. We manage our exposure to changes in the NY'C' coffee price on the value of our inventories through a commodity hedging program (discussed under 'Hedge Accounting' below), but cannot hedge our exposure to changes in quality differentials.

In addition to the price risks associated with holding coffee inventories, our revenue and cost of sales are affected by changes in the underlying commodity price. Commodity price increases (decreases) raise (lower) the green coffee cost recovery revenue generated through our non-toll business, as well as the costs of green coffee sold to customers to generate sales.

Changes in the NY'C' also affect our statement of financial position, and the amount of working capital we use in our business. When coffee prices rise (fall), our inventory values gradually increase (decrease) as we replace coffee at higher prices. Our accounts receivable and our accounts payable also rise and fall with the NY'C'.



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Finally, there is no open market to hedge the quality differential component of our green coffee cost. We sell coffee at replacement quality differentials, and as such, in a period of falling (rising) differentials we will generate differential cost recovery losses (gains), as green coffee revenues will be less than (exceed) green coffee costs.

- *US\$/C\$ Exchange Rates* – As noted above, the majority of our revenues are generated in US dollars, while a significant portion of our costs are paid in Canadian dollars. We therefore have exposure to changes in the US\$/C\$ exchange rates. This is managed, in part, through derivative financial instruments. All other factors being equal, our profitability and cash from operations will be higher when the US dollar appreciates relative to Canadian dollar. A long-term depreciation of the Canadian dollar will improve our long-term profitability and cash generation.

#### *Internal Factors*

- *Processing Volumes* – Our decaffeination facility generates a certain level of fixed operating costs that are incurred regardless of the volume of coffee processed. Accordingly, our profitability and cash from operations will increase as processing volumes increase. Processing volume is a key performance indicator (“KPI”) that we monitor continuously.
- *Process Consistency* – As discussed in the ‘Business Strategy’ section above, we manage our operations in order to reduce variability in production and drive continuous improvement. Production consistency results in improved product quality. We have developed a number of KPIs designed to monitor process consistency, and have set targets for continuous process improvement.
- *Product Quality* – Quality control is a key part of our operations. We operate under the Food Safety Systems Certification (FSSC) 22000, which manages our food safety, as well as HACCP (Hazard Analysis Critical Control Points) and quality assurance programs. All green coffees delivered to our processing facility are weighed and inspected and are subject to rigorous internal quality-control evaluations. Each lot of green coffee processed is monitored throughout the decaffeination process, and a certificate of analysis is prepared for each lot. A sample from each production lot is also roasted, brewed and cupped to ensure quality. In addition, our focus on reducing the size of production lots and increasing inventory turnover results in fresher coffee being provided to our customers. Production batch size and inventory turns are two other KPIs that we monitor regularly.
- *Order Fulfillment* – Our integrated supply chain management strategy includes maintaining inventories of finished goods at various coffee warehouses throughout North America, and of raw goods for improved inventory replenishment times. Our order fulfillment rates are monitored regularly. An improved order fulfillment rate has contributed to our volume growth and improved customer service levels.
- *Employee Safety* – We are focused on operating our business in a safe manner, and reducing the likelihood that employees will be injured at work. We track employee safety metrics by department, and our safety committee proactively seeks ways to reduce the risks inherent in our operating environment. While we cannot completely eliminate workplace incidents or accidents, we have significantly reduced the number of safety-related incidents over the past four years. We are proud of the fact that SWDCC has not had a lost-time incident in more than four years. We believe that ensuring employee safety leads to improved employee retention and morale, increased efficiency and lower operating costs.
- *Sustainability and Environmental Responsibility* – The SWISS WATER® Process is a 100% chemical free

decaffeination process that enables us to consistently deliver high-quality coffee. Our approach to sustainability is to continually improve and innovate this process to be more efficient by actively managing resource usage in a safe and environmentally responsible manner. In addition to carefully managing our operations, we take steps to ensure sustainable coffee supply by purchasing sustainably certified coffees and organic coffees. We promote social sustainability by participating in programs within the coffee industry that advance the health of women and their families living in coffee-growing communities (Grounds for Health) and that foster research-based approaches to advancing coffee cultivation (World Coffee Research).

### **CAPACITY TO DELIVER RESULTS**

The following resources allow us to deliver on our business strategy:

- *Proprietary Chemical Free Production Lines* – We have two decaffeination production lines. This enables us to align our production capacity with changes in demand throughout the year. We operate one line when demand is lower, and both lines when demand is higher, giving us better control over our variable costs. In 2016, we expanded the capacity of one of our production lines, which enables us to meet near-term growth in demand for our products. Longer term, we have announced plans to construct a new processing plant, which will house a third production line once it is complete. Construction of the new facility is expected to be complete by the end of 2018, and the new production line is expected to be operational in the second quarter of 2019.
- *Consumer Branding as the Premium, 100% Chemical Free Method of Decaffeinating Green Coffee* – We have been successful in establishing our brand as a leading chemical free processor of green decaffeinated coffee. Consumers and participants in the coffee trade are increasingly aware of the value of the chemical free SWISS WATER® Process due to its quality and taste. We believe that there is significant potential to continue to broaden consumer awareness of the benefits of the SWISS WATER® Process.
- *Established Customer Base* - The SWISS WATER® Process has an established customer base across North America and in many international markets. Our customers include some of North America’s largest roasters, roaster-retailers and leading coffee brands.
- *Broad Distribution Channels* - Green coffee decaffeinated using the SWISS WATER® Process is sold through the coffee market’s key distribution channels: roaster retailers, commercial roasters and coffee importers. This diversity ensures that we access all key segments of the specialty coffee trade and consumer coffee markets.
- *Working Capital and Expansion Capital* – We believe we have sufficient lines of credit available to invest in the inventory and working capital required to execute on our business strategy. In 2015 and 2016, we raised equity and debt which is being used to fund the construction of our third production line (to be housed in the new production facility noted above).
- *Management Expertise* - Ten Peaks is highly regarded in the coffee industry for our senior management team’s substantial experience, our close attention to consumer trends in the specialty coffee market, and our in-depth knowledge of green and roasted coffee. In particular, our intense focus on premium product quality and commitment to science-driven insight is well recognized. To maximize these strengths, we have invested significant resources in enhancing our team’s industry-related skills and talents over the past few years. Going forward, we intend to leverage our exceptional experience with, and knowledge of, the specialty coffee industry to continue to build our

business.

### SELECTED ANNUAL INFORMATION

<i>(In \$000s except per share amounts)</i>	<b>December 31, 2017</b>	<b>December 31, 2016</b>	<b>December 31, 2015</b>
<b>Balance Sheet</b>			
Total assets	72,848	67,899	57,688
Total long-term liabilities	19,497	17,733	3,070
<b>Income Statement</b>			
Sales	83,755	81,927	83,641
EBITDA <sup>(1)</sup>	6,923	5,772	8,034
Net income	4,160	4,149	1,312
Dividends paid	2,260	2,256	1,824
<b>Per share, basic<sup>(2)</sup></b>			
EBITDA <sup>(1)</sup>	0.77	0.64	1.04
Net income	0.46	0.46	0.17
Dividends paid	0.25	0.25	0.25
<b>Per share, diluted<sup>(2)</sup></b>			
EBITDA <sup>(1)</sup>	0.64	0.63	1.04
Net income	0.42	0.46	0.17

(1) EBITDA is defined in the section 'Non-IFRS Financial Measures' along with details of its calculation.

(2) Per-share calculations are based on the weighted average number of shares outstanding during the period.

Our total assets and our total liabilities have increased in each of the last two years following an equity offering in 2015 and a convertible debenture offering in 2016. Proceeds from the equity offering in 2015 were used to increase capacity of one production line in 2016, resulting in an increase in fixed assets, and repayment of short-term debt. Proceeds from the debt and equity offerings are also being used to construct a new production line, which will be housed in a new production facility that is currently under construction (see 'Outlook' section, below).

Of note, we adopted hedge accounting on January 1, 2016, and as such the operating results from 2015 are not directly comparable to those in 2016 and 2017. Prior to the adoption of hedge accounting, we experienced considerable volatility in our gross profit, net income and EBITDA numbers. Results of operations including our revenues, net income and EBITDA are discussed in more detail below.

### HEDGE ACCOUNTING

We adopted the hedge accounting provisions of IFRS 9 on January 1, 2016 because it better aligns with our existing hedging strategies. The adoption of hedge accounting reduces the volatility in our financial results, by better matching our accounting practices to our existing hedging practices. We have **not** changed our risk management strategies with the adoption of hedge accounting. The economic impact of our hedges is unchanged, even though the accounting for these derivative instruments has changed.

We enter into three types of hedges:

- 1) Commodity price risk hedges on our coffee purchase commitments and inventory (“commodity hedges”);
- 2) Currency risk hedges on future US\$ process revenues (“revenue hedges”); and
- 3) Customer-specific currency risk hedges on US\$ purchases of green coffee (“customer-specific hedges”).

Each type of hedge is discussed below.

#### *Commodity Hedges:*

When we enter into a purchase commitment to purchase green coffee, the contract specifies that the purchase price will be determined in part based on the future (to-be-determined) futures price or NY’C’. We agree on or ‘fix’ the NY’C’ price with the vendor on or before receiving the coffee into inventory. When we bear the economic risk of a change in the commodity price, we offset this price risk by selling short a futures contract on the IntercontinentalExchange. When we later sell such coffee at a fixed price to a customer, we cover our short by going long on a futures contract on the IntercontinentalExchange. As we always have inventory on hand, we are always net short futures contracts.

At each period-end, commodity hedges are re-measured to their fair value. Under hedge accounting, gains/losses for hedged coffee purchase commitments and inventory are recorded in the statement of financial position until such coffee is sold, at which time the gains/losses on our commodity hedges are recognized in cost of sales. In this way, gains/losses on our commodity hedges are matched to our sales in the period.

#### *Revenue Hedges:*

We enter into forward contracts to sell US\$ at future dates to hedge the foreign exchange cash flow variability of expected US\$ processing fee revenue up to 60 months in advance. The hedged process revenue includes both process revenue from tolling arrangements (processing of customer-owned coffee) as well as the US\$ processing fee layer of inventory sales agreements. This enables us to more reliably predict how much Canadian currency we will receive for our US\$ process revenue. Cash flows in the immediate twelve month period are hedged at a higher percentage of expected future revenues than those farther out, reflecting greater uncertainty in the 13- to 60-month period.

At each period end, revenue hedges are re-measured to their fair value. Under hedge accounting, unrealized gains/losses for open revenue hedges are recorded in other comprehensive income. When a revenue hedge matures, the realized gain/loss on that contract is recycled from accumulated other comprehensive income to process revenue.

#### *Customer-Specific Hedges:*

We enter into forward contracts to buy US\$ for green coffee inventory which, once decaffeinated, will be sold at a fixed Canadian dollar (“C\$”) price pursuant to a customer-specific contract. To mitigate the exposure to changing margin on these transactions arising from fluctuations in the US\$/C\$ exchange rate, we enter into US\$ forward purchase contracts which economically lock in the US\$/C\$ exchange rate, and effectively locks in the C\$ cost of inventory to be sold at the fixed C\$ amount.

The adoption of hedge accounting allows for better matching of US\$ purchases with the associated gains/losses on the forward contracts used to economically hedge these items. At each period-end, customer-specific hedges are re-measured to their fair value. Under hedge accounting, the gains/losses on these hedges

are deferred on the statement of financial position until the inventory is sold, at which time the gains/losses are recorded in cost of sales on the income statement.

## OPERATING RESULTS

### *Processing Volumes and Revenue*

We recorded another record year for processing volumes and revenues in 2017, with shipments growing by 5% over 2016. On a year-over-year basis, volumes grew in each of the first three quarters of 2017, then declined marginally by 2% in Q4. The fourth quarter of 2016 was particularly strong, with volumes in that quarter rising by 9% over the same period in 2015.

Growth in sales to our specialty customers led the way in both the fourth quarter and the full year. Volumes to our specialty accounts increased by 4% in in Q4 2017 and by 9% for year, compared to the same periods of 2016. Fourth quarter shipments to our commercial accounts declined by 5% when compared to fourth quarter of 2016, while full-year shipments to commercial accounts rose by 2%.

We also categorize our customers by the nature of their business: either coffee importers or roasters. Coffee importers act like grocery stores to roasters, sourcing and importing green coffee from various origins and carrying a selection of different origins and quality levels for roasters to choose from. Importers buy from us in order to resell our coffees to roasters when and where they need it. Roasters are in the business of roasting and packaging coffee for sale to consumers in their own coffee shops, or for home or office use. Roasters either buy directly from SWDCC, or they buy from an importer. Roasters generally carry lower inventories, as they tend to take delivery of green coffee shortly before roasting it. As such, shipments to roasters are more stable from period to period.

Shipments to importers declined by 17% in Q4 2017, but rose by 11% for the full year. Shipments to roasters increased by 6% in the fourth quarter and by 2% for the full year. In 2016, several months of rising green coffee costs prompted importers to reduce their inventories and delay buying. In Q4 2016, the NY'C' declined quickly, prompting an influx of orders as importers rebuilt inventories. Importers continued to build inventories through much of 2017, as the NY'C' gradually declined.

We monitor and report our revenue in three categories. "Process revenue" represents the amount we charge our customers for decaffeinating green coffee, and it generally increases as our processing volume increases. "Green coffee cost recovery revenue", or "green revenue", is the amount we charge our customers for the green coffee we purchase for decaffeination. "Distribution revenue" consists of shipping, handling and warehousing charges billed to our customers. It typically rises with processing volumes and with the growth of Seaforth's business.

Our revenue by category for the indicated periods was as follows:

<i>(In \$000s)</i>	3 months ended		3 months ended		12 months ended		12 months ended	
	December 31, 2017		December 31, 2016		December 31, 2017		December 31, 2016	
Process revenue	\$	5,652	\$	5,712	\$	21,781	\$	20,671
Green revenue		13,800		15,661		57,177		57,038
Distribution revenue		1,210		1,076		4,797		4,218
Total	\$	20,662	\$	22,449	\$	83,755	\$	81,927

Our fourth quarter sales totaled \$20.7 million, a decrease \$1.8 million, or 8%, compared to the same quarter in 2016. Process revenue decreased by \$0.1 million, or 1%, reflecting the decrease in sales to commercial customers in the quarter, which was partially offset by hedging gains in the period. Green revenue decreased

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by \$1.9 million, or 12%, reflecting lower volumes and a drop in NY'C' in the quarter. Distribution revenue rose by \$0.1 million, or 12%, due to growth in Seaforth's business.

Annual sales totaled \$83.8 million, an increase of \$1.8 million, or 2%, over 2016. Process revenue increased by 5%, which was in line with our higher volumes. Our revenue hedges contributed \$0.9 million to process revenue, offsetting the impact of a lower US\$ in 2017. Green revenue remained flat, as higher sales volumes were offset by a lower NY'C'. Distribution revenue rose by 14%, with the increase driven by higher volumes and growth in Seaforth's business.

#### *Cost of Sales*

Cost of sales includes the cost of green coffee purchased for our regular business, the plant labour and other processing costs directly associated with our production facility, customer-specific hedges and commodity hedges. Cost of sales incorporates an allocation of fixed overhead costs, which includes depreciation of our production equipment and amortization of our proprietary process technology. In addition, cost of sales includes the costs of operating Seaforth's warehouses.

Cost of sales decreased during the fourth quarter by \$1.8 million, or 9%, to \$17.5 million. The decrease was driven by lower green coffee costs owing to a lower NY'C', as well as lower volumes in Q4 2017. For the full year, cost of sales was \$71.2 million, up by \$1.3 million, or 2%, over 2016. The increase was driven by higher volumes of shipments and a stronger US\$ earlier in the year, mitigated by \$0.9 million in commodity hedges and in customer-specific hedges related to cost of sales.

#### *Gross Profit*

Gross profit decreased by 1% in the fourth quarter, with the decline in revenue slightly exceeding the increase in cost of sales. Annual gross profit increased by \$0.5 million, or 4%, over 2016 as our higher revenues and shipments more than offset increases in our cost of sales.

#### *Administration Expenses*

Administration includes general management, inbound and outbound logistics, finance and accounting, quality control and assurance, engineering, research and development, and other administrative or support functions. Administration expenses include compensation expenses, travel and other personnel-related expenses for administrative staff, directors' fees, investor relations expenses, professional fees, depreciation of office-related equipment, and amortization of the brand asset.

Administration expenses increased by \$0.5 million, or 48%, to \$1.5 million for the fourth quarter of 2017, and by \$0.6 million, or 13%, to \$5.1 million for 2017. In both periods, the year-over-year increases reflect higher staffing and staff-related expenses, including stock-based compensation expenses, as well as recruitment expenses for positions filled late in the year.

#### *Sales and Marketing Expenses*

Sales and marketing expenses include compensation and other personnel-related expenses for sales and marketing staff, consumer and trade advertising and promotion costs, as well as related travel expenses.

Sales and marketing expenses were up by \$0.1 million, or 11%, to \$0.7 million in Q4 2017, and by \$0.2 million, or 8%, to \$2.6 million, for the full year. In 2017, we invested in increased marketing activities in support of SWDCC's strategic growth initiatives. These activities included an increased media presence, developing and delivering digital consumer marketing content, and increased participation in international trade shows.

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### *Occupancy Expenses*

Occupancy expenses include the cost of renting offices for sales, marketing and administrative use. Occupancy costs for the fourth quarter and full year were similar to the same periods in 2016.

### *Finance Expenses and Income*

Finance income reflects the charges we bill to customers for financing coffee inventories and interest earned on cash balances and short-term investments. Finance expenses include interest costs on bank debt, other borrowings, the accretion expense on our asset retirement obligation and the interest expense on the convertible debenture and construction loan.

Net finance expenses were \$0.2 million and \$0.8 million for the three months and year ended December 31, 2017, compared to net finance expense of \$0.2 million and nil, respectively, in the same periods last year. In 2017, interest expense for the convertible debenture was \$1.4 million, compared to \$0.3 million in the prior year. The convertible debenture was issued in Q4 2016, such that interest was incurred for only one quarter that year. Interest on the convertible debenture is expensed at an effective interest rate of 12.15% (a rate determined by management in accordance with IFRS), while the contractual interest paid on this loan is at a rate of 6.85%. Interest expenses were partially offset by interest income of \$0.6 million in 2017, compared to \$0.3 million in 2016.

### *Gains and Losses on Risk Management Activities*

With the adoption of hedge accounting, gains or losses on designated hedges are included in either revenue or cost of sales, held on the balance sheet or included in other comprehensive income for future transactions (see 'Hedge Accounting', above). Thus, 'Gain on risk management activities' includes only those gains and losses on derivative financial instruments or portions of such instruments that are not designated as hedging instruments.

For the three months ended December 31, 2017, we recorded a gain of \$0.4 million, while during same period in 2016, the gain was \$0.5 million. For the full year, we recorded a gain of \$1.2 million compared to a gain of \$0.6 million for 2016.

### *Fair Value Adjustment on Embedded Option*

Ten Peaks entered into a convertible debenture in October 2016. Under IFRS, this instrument is deemed to contain an embedded option which must be revalued at each balance sheet date. The fair value of the derivative liability was determined using the Black-Scholes Option Pricing Model. The variables and assumptions used in computing the fair value are based on management's best estimate at each balance sheet date.

The revaluation on this embedded option resulted in a loss of \$0.3 million and a gain of \$0.6 million in the fourth quarter and for the year, respectively (2016: nil and a loss of \$nil).

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*Gains and Losses on Foreign Exchange*

We realize gains and losses on transactions denominated in foreign currencies when they occur, and on assets and liabilities denominated in foreign currencies when they are translated into Canadian dollars as at the financial statement date.

During the fourth quarter, we recorded a loss on foreign exchange of \$0.8 million, compared to a gain of \$0.1 million for the same period in 2016. The rapid depreciation of the C\$ late in the fourth quarter of 2017 contributed to the loss on foreign exchange. For the full year, we recorded no effective net foreign exchange gain or loss, compared to a gain of \$0.1 million in 2016.

*Income Before Taxes and Net Income*

In the fourth quarter, we recorded income before taxes of \$0.1 million, compared to \$1.9 million in the same period of 2016. Current and deferred income taxes reduced net income in Q4 2017 by \$0.5 million due to reconciling items from prior periods, which were recorded in the fourth quarter. By comparison, current and deferred income taxes reduced our net income by \$0.6 million in Q4 2016. Deferred income taxes arise mainly from temporary differences between the depreciation and amortization expenses deducted for accounting purposes, and the capital cost allowances deducted for tax purposes, as well as changes in corporate income tax rates as adjusted for substantively enacted higher future tax rates. The latter are offset by the tax benefit of loss carry forwards recognized. Overall, we incurred a net loss of \$0.4 million for the fourth quarter, compared to net income of \$1.3 million for the same period in 2016.

For the full year, we recorded pre-tax income of \$5.8 million, up from \$5.7 million in 2016. This was reduced by income tax expenses of \$1.6 million, unchanged from 2016. Overall, we earned net income of \$4.2 million for the full year, compared to \$4.1 million in 2016.

*Basic and Diluted Earnings per Share*

Basic earnings per share is calculated by dividing net income by the basic weighted average number of shares outstanding during the period. Similarly, diluted earnings per share is calculated by dividing net income adjusted for the effects of all dilutive potential common shares, by the diluted weighted average number of shares outstanding. For the purposes of the calculation, under IFRS we are required to assume that the maximum number of shares issuable under the convertible debenture will be issued, even though the debenture contains a net share settlement provision (which if exercised would result in far fewer shares being issued).

In Q4 2017, the potential common shares issuable under the convertible debenture are anti-dilutive, and as such they are excluded from the calculation of diluted earnings per share in the quarter. These potential common shares are included in the calculation of the diluted earnings per share for 2017.

The calculations of basic and diluted earnings per share for the current and prior periods are shown in the following table:



	3 months ended		3 months ended		12 months ended		12 months ended	
	December 31, 2017		December 31, 2016		December 31, 2017		December 31, 2016	
<b>Basic EPS:</b>								
Net income attributable to shareholders	\$	(380)	\$	1,328	\$	4,160	\$	4,149
Weighted average number of shares		9,038,862		9,038,862		9,038,862		9,019,621
<b>Basic EPS</b>	<b>\$</b>	<b>(0.04)</b>	<b>\$</b>	<b>0.15</b>	<b>\$</b>	<b>0.46</b>	<b>\$</b>	<b>0.46</b>
<b>Diluted EPS:</b>								
Net income attributable to shareholders	\$	(380)	\$	1,328	\$	4,160	\$	4,149
Effect of diluted securities: RSUs						-		19
After tax effect of diluted securities if debenture converted:								
Interest on convertible debenture		-		-		1,035		-
Loss (gain) on fair value adjustment of embedded option		-		-		(604)		-
Net income after effect of diluted securities	\$	(380)	\$	1,328	\$	4,591	\$	4,168
Weighted average number of shares - basic		9,038,862		9,038,862		9,038,862		9,019,621
Effect of diluted securities: RSUs								83,932
Effect of diluted securities: convertible debenture		-		-		1,818,182		-
Weighted average number of shares - diluted		9,038,862		9,038,862		10,857,044		9,103,553
<b>Diluted EPS</b>	<b>\$</b>	<b>(0.04)</b>	<b>\$</b>	<b>0.15</b>	<b>\$</b>	<b>0.42</b>	<b>\$</b>	<b>0.46</b>

### *Other Comprehensive Income*

Gains or losses on our designated revenue hedges that will mature in future periods are recorded in other comprehensive income, net of income tax expense. Other comprehensive income, net of tax for the fourth quarter was a loss of \$0.3 million, compared to a loss of \$0.8 million in the same period of 2016. For the full year, we reported accumulated gains in other comprehensive income of \$1.1 million, compared to \$0.4 million in 2016. This amount fluctuates with the closing US\$/C\$ exchange rate each period-end.

### **Non-IFRS Measures**

#### *EBITDA*

EBITDA is often used by publicly traded companies as a measure of cash from operations, as it excludes financing costs, taxation and non-cash items. The reporting of EBITDA is intended to assist readers in the performance of their own financial analysis. However, since this measure does not have a standardized meaning prescribed by IFRS, it is unlikely to be comparable to similar measures presented by other entities.

We define EBITDA as net income before interest, depreciation, amortization, impairments, share-based compensation, gains/losses on foreign exchange, gains/losses on disposal of capital equipment, fair value adjustments on embedded options, and provision for income taxes. Our definition of EBITDA also excludes unrealized gains and losses on the undesignated portion of foreign exchange forward contracts.

The reconciliation of net income to EBITDA is as follows:

(In \$000s)

	3 months ended		3 months ended		12 months ended		12 months ended	
	December 31, 2017		December 31, 2016		December 31, 2017		December 31, 2016	
Income for the period	\$	(380)	\$	1,328	\$	4,160	\$	4,149
Income taxes		454		590		1,606		1,593
Income before tax		74		1,918		5,766		5,742
Finance income		(174)		(124)		(580)		(342)
Finance expenses		368		316		1,414		346
Depreciation & amortization		583		596		2,172		2,053
Unrealized gain on foreign exchange forward contracts		(679)		(603)		(1,462)		(1,750)
Fair value loss (gain) on embedded option		305		(6)		(604)		(6)
(Gain) loss of foreign exchange		751		(66)		6		(91)
Share-based compensation		106		(33)		211		(180)
<b>EBITDA</b>	<b>\$</b>	<b>1,334</b>	<b>\$</b>	<b>1,998</b>	<b>\$</b>	<b>6,923</b>	<b>\$</b>	<b>5,772</b>

In order to help readers better understand our financial results, the following table shows the reconciliation of operating income to EBITDA:

(In \$000s)

	3 months ended		3 months ended		12 months ended		12 months ended	
	December 31, 2017		December 31, 2016		December 31, 2017		December 31, 2016	
Operating income for the period	\$	958	\$	1,525	\$	4,812	\$	5,017
<b>Add back:</b>								
Depreciation & amortization		583		596		2,172		2,053
Share-based compensation		106		(33)		211		(180)
Gain (loss) on risk management activities		366		519		1,190		638
<b>Deduct:</b>								
Unrealized (gain) loss on foreign exchange forward contracts		(679)		(609)		(1,462)		(1,756)
<b>EBITDA</b>	<b>\$</b>	<b>1,334</b>	<b>\$</b>	<b>1,998</b>	<b>\$</b>	<b>6,923</b>	<b>\$</b>	<b>5,772</b>

EBITDA for the three months ended December 31, 2017 was \$1.3 million, down by 33% compared to Q4 2016. The year-over-year decrease was related to somewhat lower volumes, increased expenses and reduced gains on risk management activities in Q4 2017. For the full year, EBITDA was \$6.9 million, up by 20% from \$5.8 million for 2016. Volume increases and improved performance on our risk management activities contributed to the rise in EBITDA.

### Quarterly Information / Seasonality

The following table summarizes results for each of the eight most recently completed fiscal quarters. For comparative purposes, we have also provided the averages for the previous 8-quarter period:

*In \$000s except for per share amounts*

	8 Quarter Average	Q4 2017	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016	Q2 2016	Q1 2016
Sales	20,710	20,662	21,955	21,915	19,223	22,448	20,752	18,074	20,653
Gross Profit	3,080	3,178	3,014	3,364	3,035	3,216	3,219	2,601	3,014
Operating income	1,229	958	1,117	1,470	1,267	1,526	1,330	999	1,162
EBITDA <sup>1</sup>	1,587	1,334	1,678	2,235	1,677	1,998	1,515	1,000	1,259
Net income (loss)	1,039	(380)	1,385	1,720	1,435	1,328	879	758	1,184
<b>Per Share<sup>2</sup></b>									
Net income (loss) - basic	0.12	(0.04)	0.15	0.19	0.16	0.15	0.10	0.08	0.13
Net income (loss) - diluted	0.10	(0.04)	0.15	0.17	0.08	0.15	0.10	0.08	0.13

<sup>1</sup> EBITDA is defined in the section on 'Non-IFRS Financial Measures' along with details of its calculation.

<sup>2</sup> Per-share calculations are based on the weighted average number of shares outstanding during the period.

There is an element of seasonality in our business, in that the second half of the year tends to have higher volumes and revenues.

## Liquidity and Capital Resources

### *Cash Flow from Operations*

For the 12 months ended December 31, 2017, we generated \$1.7 million in net cash from operating activities, compared to cash generation of \$9.2 million in 2016. Income taxes paid reduced cash from operating activities in the period by \$0.9 million (2016: Nil). In addition, investments in inventory used \$3.1 million in cash in 2017, compared to a generated cash inflow of \$7.4 million in 2016. In 2017 and 2016, there was an increase in accounts receivable which resulted in a decrease in our cash inflows of \$0.4 million and \$4.5 million, respectively.

### *Investing Activities*

Cash outflows relating to capital expenditures for 2017 were \$8.1 million, compared to \$5.3 million in 2016. Capital costs for both years included investments in support of our capacity expansion.

In 2016, \$12.7 million of cash outflows were related to the purchase of short-term investments, while in 2017, proceeds from short-term investments were \$5.6 million.

### *Financing Activities*

During the 12 months ended December 31, 2017, we paid \$2.3 million in dividends to shareholders. This is unchanged from 2016.

### *Credit Facilities and Liquidity*

Our current credit facilities include a \$14.5 million revolving operating line of credit and a \$1.5 million revolving swing line, each of which bears an interest rate of prime plus 0.75%. Any US\$-denominated debt under the revolving operating line of credit or swing line can be financed using LIBOR loans at the LIBOR rate plus 2.35% per annum.

In addition, we have a US\$8.0 million foreign exchange and commodity futures contract facility. This allows us to enter into spot, forward and other foreign exchange rate transactions with our bank with a maximum term of 60 months.

Our facilities are collateralized by a general security agreement over all of the assets of Ten Peaks and a floating hypothecation agreement over cash balances.

We have certain bank covenants which relate to the maintenance of specified financial ratios and we were in compliance with all covenants as at December 31, 2017.

#### *Inventory*

Our inventory increased 27% by value and 54% by volume between December 31, 2016 and December 31, 2017. The increase reflects growth in both finished goods and raw materials inventory.

With the adoption of hedge accounting, gains/losses on derivative instruments for coffee to be sold in future periods are now recorded in inventory. The hedge accounting component of inventory as at December 31, 2017 was a minor gain, compared to a loss of \$0.6 million in 2016.

#### *Accounts Receivable*

Our accounts receivable increased by \$0.4 million, or 4%, between December 31, 2016 and December 31, 2017. This compares to an increase of \$4.5 million, or 63%, between December 31, 2015 and December 31, 2016. The increases reflect a trend in the coffee industry, in which large coffee roasters have demanded longer accounts payable terms from their suppliers. As a result, we extended payment terms to a number of our larger customers in 2016.

#### *Contractual Obligations*

The following table sets forth our contractual obligations and commitments as at December 31, 2017:

*(In \$000s)*

		<b>Total</b>	<b>Less than 1 year</b>	<b>1-3 Years</b>	<b>4-5 Years</b>	<b>Over 5 Years</b>
Long-term debt <sup>(1)</sup>	\$	15,845	\$ 28	\$ 113	\$ 113	\$ 15,591
Financing leases <sup>(2)</sup>		5,696	786	2,210	2,210	491
Operating leases <sup>(3)</sup>		3,103	1,691	1,412	-	-
Purchase obligations <sup>(4)</sup>		32,984	32,875	109	-	-
<b>Total contractual obligations</b>	<b>\$</b>	<b>57,628</b>	<b>\$ 35,380</b>	<b>\$ 3,844</b>	<b>\$ 2,323</b>	<b>\$ 16,082</b>

<sup>1</sup> Long-term debt represents the principal amounts of the convertible debenture and construction loan.

<sup>2</sup> Minimum obligations for our financing leases.

<sup>3</sup> Minimum obligations for our operating leases.

<sup>4</sup> Represents outstanding coffee and natural gas purchase commitments.

SWDCC leases a facility which houses its decaffeination plant and offices. The current lease term expires in 2018. SWDCC has already exercised its option to renew the lease on the decaffeination facility for one additional five-year term until 2023.

Seaforth leases warehouses in two locations for its primary operations. These leases expire in June 2019 and November 2019.

Swiss Water Decaffeinated Coffee Company USA, Inc. holds a lease for its Seattle, WA sales office, which expires on March 31, 2020.

In 2016, SWDCC signed a lease agreement for a build-to-suit production facility. The lease has an initial term of five years and can be renewed at SWDCC's option in five-year increments up to a total of 30 years. The lease will commence on the earlier of the date of opening of the SWDCC business in any part of the premises, and the date of expiry of the fixturing period, which is estimated to be in May 2018. Under the lease, SWDCC has multiple options to buy-out the lease starting at the end of the second five-year term. The buy-out value will be equal to the fair market value of the property as determined by an appraisal process, subject to specified maximum and minimum values.

The lease also includes a construction management agreement for the construction of a highly specialized building to house the production plant. The landlord will finance a portion of the building, with loan payments commencing on the earlier of substantial completion of construction and January 1, 2019. The loan is repayable in equal monthly installments over 15 years and can be prepaid without penalty at any time. As at the year ended December 31, 2017, Ten Peaks accrued a "Construction loan" to cover amounts due on work completed to date, including accrued interest, in the amount of \$0.8 million (2016: nil).

As at December 31, 2017, the Company's capital commitments for the new facility located in Delta, BC were \$16.0 million.

### Off-Balance Sheet Arrangements

Ten Peaks has no off-balance sheet arrangements.

### Related Party Transactions

We provide toll decaffeination services and/or sell finished goods to, and purchase raw material inventory from, a company that is related to Ten Peaks' Director, Roland Veit.

The following table summarize related party sales and purchases during the periods:

<i>(In \$000s)</i>	<b>3 months ended</b>	<b>3 months ended</b>	<b>12 months ended</b>	<b>12 months ended</b>
	<b>December 31, 2017</b>	<b>December 31, 2016</b>	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Sales	\$ 33	\$ 390	\$ 303	\$ 764
Purchases of raw materials	\$ 1,903	\$ 1,266	\$ 6,934	\$ 4,509

All transactions were in the normal course of operations and were measured at the fair value of the consideration received or receivable, which was established and agreed to by the related parties. As at December 31, 2017, our accounts receivable balance with this company was nil (December 31, 2016: \$0.1 million) while our accounts payable balance with this company was nil (December 31, 2016: \$0.1 million).

On March 16, 2017, a subsidiary of Ten Peaks and a member of Key Management (the borrower) entered into a promissory note in the amount of US\$0.1 million. For as long as the borrower remains an employee, the obligation to repay the principal is forgiven against current and future awards under the RSU Plan, by forfeiture of awards. The loan is interest-free other than in the event of default, in which case the promissory note shall bear simple interest at a rate of 10% per annum.

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## OUTLOOK

Overall, management expects double-digit volume increases in 2018. Demand for our premium quality decaffeinated coffees is rising, due to a number of factors. First, the market for decaffeinated coffee is expanding, with decaf being the fastest growing segment of the US coffee market<sup>1</sup>. Total decaffeinated coffee sales are up year-over-year, with specialty decaffeinated coffee sales being particularly strong, especially in out-of-home markets.

We believe this is due, in part, to the premiumization of the coffee market, as well as growing awareness and consumption of premium decaffeinated coffee. In fact, the largest consumers of decaffeinated coffee are 18 to 24 year olds<sup>2</sup>, who want to drink great-tasting coffee all day long, without worrying about the potential side effects of caffeine.

Additionally, younger consumers are more conscious of artificial ingredients and chemicals in the production of their food and drink. As a result, we've seen increased demand for our methylene chloride free, sustainable organically certified and conventional SWISS WATER® Process coffees, as more food companies now employ our branded coffees to help them respond to this growing consumer demand.

More importantly, various media sources<sup>3</sup> have recently underscored the health and environmental hazards associated with methylene chloride (the primary chemical used by our competitors to decaffeinate coffee). This has drawn attention to the real and perceived harmful effects of using chemicals to decaffeinate coffee. At present, our marketing team is leveraging this increased consumer awareness, and highlighting the availability of our premium quality, 100% chemical free coffees. We expect this rise in consumer awareness to stimulate market pull for our coffees over the coming months and year ahead, and we will continue to proactively employ positive messaging to accentuate our amazing coffees without caffeine.

In addition to consumer-driven trends, changes in the global decaffeination market are enhancing our growth prospects. An older decaffeination plant in Europe closed in 2017, reducing the number of available chemical free, third-party decaffeimators. We have already won some additional business from coffee companies affected by this shutdown, and we expect additional growth in the future.

As we have noted previously, we are building a state-of-the-art production facility which will enable us to meet the anticipated long-term growth in demand for our decaffeinated coffees. Construction of the new facility, which is located in Delta, BC, began in May 2017 and is expected to be completed in 2018. Initially, this facility will house one new production line, although the site is large enough for expansion well into the future. The new production line is expected to be completed and commissioned in Q2 2019. The additional capacity that was added in Q1 2016 at our current Burnaby, BC facility, together with additional de-

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<sup>1</sup> [National Coffee Association 2017 Coffee Drinking Trends](#)

<sup>2</sup> [National Coffee Association 2017 Coffee Drinking Trends](#)

<sup>3</sup> [New York Times](https://www.nytimes.com/2017/10/21/us/epa-toxic-chemicals.html) has published (<https://www.nytimes.com/2017/10/21/us/epa-toxic-chemicals.html>) and podcasted ([https://www.nytimes.com/podcasts/the-daily?\\_r=0](https://www.nytimes.com/podcasts/the-daily?_r=0)) a piece on EPA regulations, and they are highlighting methylene chloride as a key chemical that isn't, but should be, regulated, because it's a hazard to people's health.

Earlier this year, [New Scientist](#) published a report (<https://www.newscientist.com/article/2138753-ozone-layer-recovery-will-be-delayed-by-chemical-leaks/>) about how methylene chloride is slowing the regeneration of the ozone layer. This report was picked up by other media companies as well.

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bottlenecking initiatives currently underway, is expected to be sufficient to fulfill expected business growth until the new line is operational.

In short, our unbending commitment to 100% chemical free processing, and to preserving the unique quality of fine coffees through the decaffeination process, are already well recognized, valued and respected by the coffee trade and our customers, while attracting new supporters all the time. Accordingly, we believe our reputation for excellence will continue to drive incremental growth in SWDCC's decaffeination business in 2018 and beyond.

During the coming year, our primary focus will be to position SWDCC for steady future growth, which includes securing new business to fill our current capacity and leveraging the production capacity that will be coming online in 2019. In the second quarter of this year, we expect to open a European sales office, to better serve customers in the largest decaffeinated coffee market in the world. In addition, we are expanding our ability to target specific customer groups by selectively adding to our sales and marketing team. These initiatives will increase our expenses somewhat, and are expected to generate increased sales orders in the second half of this year. Overall, we expect our volume growth to exceed that achieved in 2017.

#### **RISKS AND UNCERTAINTIES**

Ten Peaks' ability to pay dividends is dependent upon the earnings and cash flow generated from SWDCC's operations, as well as our current and planned future investments in capital equipment. Cash from operations may fluctuate with the performance of the business, which can be susceptible to a number of risks. These risks may include, but are not limited to, foreign exchange fluctuations, labour relations, coffee prices (notwithstanding hedging programs, as exact hedging correlation is not attainable), the availability of coffee, competition from existing chemical and other natural or chemical free coffee decaffeimators, competition from new entrants with alternate processing methods or agricultural technologies, environmental and regulatory risks, terms of credit agreements, commodity futures losses, ability to maintain organic certification, adequacy of insurance, risks related to information technology, dependence on key personnel, product liability, uncollectable debts, and general economic downturns. The future effect of these risks and uncertainties cannot be quantified or predicted. In addition, SWDCC leases the building that houses its decaffeination lines. The option to renew this lease for an additional five-year term has been exercised, with the new lease term expiring in 2023. The lease also provides for an additional five-year renewal term (to 2028), subject to the express approval of the landlord. Any plans to relocate the production equipment would result in significant capital expenditures and the payment of the asset retirement obligation (currently recorded as a long-term liability on our financial statements).

#### **ENVIRONMENTAL RISKS**

The Canadian Securities Administrators ("CSA") identifies five categories of risks: litigation, physical, regulatory, reputational and business model, for which issuers are asked to identify material risks and if they are reasonably likely to affect financial statements in the future.

Environmental matters relate to a broad range of issues, including those related to air, water, waste and land. As a small company with limited human and financial resources, we focus on only those risks that we believe could have a materially adverse impact on our operations and/or financial results within our planning horizon, rather than seeking to identify all possible future risks. Risk assessment involves judgment, uncertainty and estimates, which can provide only reasonable, rather than absolute, assurance that all the applicable risks and their expected impacts on Ten Peaks are considered.

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The most pervasive environmental risks that we face relate to the fact that we buy, sell and store an agricultural commodity. The supply of green coffee can be impacted by numerous environmental conditions such as frosts, drought, plant disease and insect damage, which can impact the quality and size of the coffee crop. In addition, certain environmental conditions, such as excessive rains, can hamper crop harvesting. A shortage of coffee can impact our processing volumes and revenues. We seek to mitigate the risks of coffee shortages by maintaining an extensive list of coffee suppliers; by dealing with importers who themselves have multiple suppliers rather than contracting directly with farmers or coffee co-operative organizations; by maintaining up to three months of coffee inventories at any time; by developing and modifying coffee blends that take into consideration coffee availability and cost from various coffee origins; and, by entering into purchase contracts with suppliers for future delivery of coffee (rather than relying on 'spot' deliveries). In addition, the coffee commodity price is closely tied to available supplies of coffee globally. We mitigate the commodity price risk through our commodity price risk management policy.

Our leased facilities are located in the Metro Vancouver area of British Columbia. Vancouver is considered to be at high risk of a major earthquake. Any significant earthquake in the vicinity could have a material impact on our operations for a period of time, depending on the extent of the damage to the facilities, our equipment, and the transportation infrastructure in the region. In short, a major earthquake could have a material adverse impact on our revenues. We carry property and business interruption insurance, including earthquake coverage, which would help offset the cash flow impact of such an event. In addition, we keep some finished goods inventory in third-party coffee warehouses in other regions, and we would be able to sell these finished goods even if our production and distribution of coffee were temporarily interrupted by an earthquake. Nevertheless, the financial and operational impact of a major earthquake cannot be reasonably predicted.

We are subject to a number of environmental laws and regulations related to our facilities in British Columbia, which mandate, among other things, the maintenance of air and water quality. We routinely monitor our compliance with these standards. Based on our compliance record and our maintenance programs, as well as currently enacted laws and regulations, we do not believe that these regulatory risks are material.

We expect to incur increased costs for energy and water consumption over time. If we cannot pass on such increased costs to our customers, our profitability may be adversely impacted.

We believe that all known environmental obligations and provisions have been appropriately reflected in our financial statements. We have not identified any material litigation, reputational, or business model risks related to environmental matters. Nevertheless, we may be subject to potential unknown or unforeseeable environmental impacts arising from, or related to, our business. Costs associated with such issues could be material.

We believe that the trend toward increased environmental awareness creates an opportunity for us to grow our business, as consumers and coffee industry participants place greater emphasis on reducing their impact on the environment. As one of the few chemical free decaffeinator in the world, we believe that an increased focus on environmental matters will allow us to win more business away from decaffeinator that use chemicals such as methylene chloride to decaffeinate coffee.



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## FINANCIAL INSTRUMENTS

We use financial instruments to mitigate economic risks associated with our business. The three types of hedges we enter into, and the hedging instruments used, are discussed in more detail under 'Hedge Accounting' above.

As of January 1, 2016, we classify our financial assets and financial liabilities in the following measurement categories (i) those to be measured subsequently at fair value (either through other comprehensive income or through profit or loss); and (ii) those to be measured at amortized cost. We have implemented the following classifications for financial instruments other than derivatives:

- Cash and cash equivalents and short-term investments are classified as assets at fair value and any period change in fair value is recorded through interest income in the consolidated statement of income, as applicable.
- Accounts receivable and other receivables are classified as assets at amortized cost using the effective interest rate method. Interest income is recorded in the consolidated statement of income, as applicable.
- Accounts payable, credit facilities, the debt portion of the convertible debenture and other liabilities are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method. Interest expense is recorded in the consolidated statement of income, as applicable.

### *Commodity Price Risk*

Commodity price risk is the risk that the fair value of inventory will fluctuate as a result of changes in commodity prices. We utilize futures contracts to manage our commodity price exposure. We buy and sell futures contracts for coffee on the IntercontinentalExchange in order to offset our inventory position and future purchase commitments, and fix the input cost of green coffee. As at December 31, 2017 we had futures contracts to buy 2.2 million lbs of green coffee with a notional value of US\$2.7 million, and contracts to sell 4.5 million lbs of green coffee with a notional value of US\$5.5 million (December 31, 2016 – buy 2.0 million lbs with a notional value of US\$ 2.7 million, and sell 6.4 million lbs with a notional value of US\$8.8 million), with the furthest contract maturing in December 2018. The net notional value of the contracts outstanding at December 31, 2017 was approximately US\$2.8 million (2016: US\$6.1 million).

### *Foreign Currency Risk*

We realize a significant portion of our sales in US dollars, and purchase green coffee in US\$ which is, in some cases, sold to customers in Canadian dollars. We enter into forward exchange contracts to manage our exposure to currency rate fluctuations and to minimize the effect of exchange rate fluctuations on business decisions. These contracts relate to our future net cash flows in US\$ from sales. In addition, we enter into forward contracts to purchase US\$ for coffee that we resell in Canadian dollars.

At December 31, 2017, we had forward currency contracts to buy US\$7.2 million and sell US\$46.2 million (December 31, 2016: buy US\$9.5 million and sell US\$42.7 million) from January 2018 through to December 2021 at various Canadian exchange rates ranging from \$1.2147 to \$1.3837. The net notional value of the contracts outstanding at December 31, 2017 was approximately US\$39.0 million (2016: US\$33.2 million).

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**CRITICAL ACCOUNTING ESTIMATES***Measurement Uncertainty*

The preparation of financial statements in accordance with IFRS requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Estimates are used when accounting for asset retirement obligations, share-based compensation and convertible debt with embedded derivatives and income taxes. Actual results may be different from these estimates.

An accounting estimate is deemed critical only if it requires us to make assumptions about matters that are highly uncertain at the time the accounting estimate is made, and different estimates that we could have used in the current period would have a material impact on our financial condition or results of operations.

*Asset Retirement Obligation*

The undiscounted future value of the asset retirement obligation (“ARO”) in respect of our leased decaffeination facility is estimated at \$0.9 million. This estimate assumes that we relocate from the current location upon expiry of the third lease renewal term in 2023. Further, the estimate reflects the expected costs of vacating the leased facility in 2023, having regard for the contract language in the lease, the expected useful lives of our plant and equipment, and the expected costs that would be paid to a third party to remove equipment.

*Convertible Debenture with Embedded Derivatives*

On October 11, 2016, the Company issued an unsecured subordinated convertible debenture for gross proceeds of \$15,000,000. The convertible debenture bears interest at a rate of 6.85% per annum to be paid quarterly in arrears and is due on October 11, 2023. The convertible debenture is convertible into common shares of the Company at a conversion price of \$8.25 per common share. Under the terms of the agreement, Ten Peaks has the option to pay interest-in-kind for the first two years. If elected, this option will increase the principal sum by the interest owing. As of December 31, 2017, this option was not elected.

The convertible debenture also includes a Net Share Settlement feature that allows Ten Peaks, upon conversion, to elect to pay cash equal to the face value of the convertible debenture and to issue common shares equal to the excess value of the underlying equity above the face value of the convertible debenture. If the Net Share Settlement option is elected, it will result in fewer common shares being issued. In 2016, the Company paid financing costs of \$0.5 million in respect of issuing the convertible debenture.

Under IFRS, we are required to estimate the interest rate on a similar instrument of comparable credit status and providing for substantially the same cash flows, on the same terms, but without the equity conversion option, in order to estimate the fair value of the liability portion of the convertible debenture upon initial recognition. We have estimated the effective interest rate to be 12.15%, such that the fair value of the liability component of the convertible debenture was initially measured at \$11.2 million. During 2017, the company estimated and recorded \$1.4 million in interest expense (2016: \$0.3 million) and paid \$1.0 million (2016: \$0.3 million).

We are also required to estimate the fair value of the embedded derivative liability related to the convertible debenture at initial recognition, and at the end of each reporting period. We use the residual value method to allocate the fair value of the convertible debenture between the liability component and the derivative liability. Under this method, the value of the derivative liability was determined to be \$3.3 million at inception. The fair value of the derivative liability was determined using the Black-Scholes Option Pricing Model. The

variables and assumptions used in computing the fair value are based on management's best estimate. The value varies with different variables of certain subjective assumptions.

Inputs into the Black-Scholes Option Pricing Model to determine the fair value of the conversion option:

	December 31, 2017	December 31, 2016
Share price	\$ 6.70	\$ 7.37
Exercise price	\$ 8.25	\$ 8.25
Option life	5.79 years	7 years
Volatility	40%	39%
Risk-free interest rate	1.90%	0.92%
Dividend yield	3.73%	3.39%

#### *Income Taxes*

We compute income taxes using the liability method, under which deferred income taxes are provided for the temporary differences between the financial reporting bases and the tax bases of our assets and liabilities. Deferred tax assets and liabilities are measured using the enacted and substantively enacted income tax rates that are expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

Deferred tax assets also reflect estimates of the recoverability of non-capital loss carry forwards. We have recognized the benefit of loss carry forwards to the extent that it is probable that taxable income will be available in the future against which our non-capital loss carry forwards can be utilized. As at December 31, 2017, Ten Peaks and its subsidiaries had combined non-capital tax loss carry forwards totaling \$0.6 million, which can be used to reduce income taxes payable in future years.

The financial reporting bases of our assets reflect the useful lives of depreciable assets, as well as the carrying amounts of assets with indefinite useful lives. Accordingly, management estimates that impact the carrying amounts of depreciable and non-depreciable assets also have an impact on deferred income tax assets and liabilities.

#### **CHANGES IN ACCOUNTING STANDARDS**

The following standards became effective for annual periods beginning on or after January 1, 2017, with earlier application permitted.

- *IAS 7 Statement of Cash Flows*: requires additional disclosures about changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.
- *IAS 12 Income Taxes*: implements a 'comprehensive balance sheet method' of accounting for income taxes which recognizes both the current tax consequences of transactions and events and the future tax consequences of the future recovery or settlement of the carrying amount of an entity's assets and liabilities. IAS 12 clarifies the requirements for recognizing deferred tax assets on unrealized loss, deferred tax where an asset is measured at fair value below the assets tax base and certain other aspects of accounting for deferred tax assets.
- *Investment Entities*: (Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12: Disclosures of Interest in other entities, and IAS 28: Investments in Associates and joint

Ventures): to address issues that have arisen in the context of applying the consolidation exception for investment entities.

- *IFRSs (Amendment)*: The Annual Improvements to IFRSs 2012-2016.

We have adopted these amended standards and interpretations, and we assessed that there was no impact on our consolidated financial statements.

The following new standards, amendments to accounting standards and interpretations have been issued and will be effective in future periods, with earlier adoption permitted:

- *IFRS 9 Financial Instruments*: The Company has early adopted all of the requirements of IFRS 9 as of January 1, 2016.
- *IFRS 2: Share-based payment*: contains amendments to classification and measurement of share-based payment transactions. It is effective for annual periods beginning on or after January 1, 2018.
- *IFRS 15: Revenue from Contracts with Customers*: replaces IAS 11, IAS 18, IFRIC 13, IFRIC 15, IFRIC 18 and SIC-31. IFRS 15 establishes principles to address the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The core principle of IFRS 15 is that revenue related to the transfer of promised goods or services should be recognized when the control of the goods or services passes to customers. The Company has evaluated the impact of applying IFRS 15, analyzing its toll revenue, regular decaffeinated coffee sales and coffee handling agreements. The Company concluded there is no material change in the timing of revenue recognized under the new standard as the point of transfer of risk and reward for goods and services and transfer of control occurs at the same time. In addition, IFRS 15 requires entities to apportion revenue earned from contracts to distinct performance obligations on a relative standalone selling price basis. The impact of this change on the amount of revenue recognized in a year is insignificant. IFRS 15 contains additional presentation and disclosure requirements which are more detailed than the current standards. Upon the adoption of IFRS 15, the Company will provide disclosures for each of the Company's revenue streams to supplement the revenue data that is currently presented in the segmented information disclosure. It is effective for annual periods beginning on or after January 1, 2018.
- *IFRS 16: Leases*: requires an application of control model to the identification of leases, distinguishing between a lease and a service contract. Also, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to the current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. A lessee can choose to apply IFRS 16 using either a full retrospective or a modified retrospective approach. The Company plans to apply IFRS 16 at the date it becomes effective but has not yet selected a transition approach. It is effective for annual periods beginning on or after January 1, 2019.
- *IFRIC 22: Foreign Currency Transactions and Advance Consideration*: clarifies the appropriate exchange rate to use on initial recognition of an asset, expense or income when advance consideration is paid or received in a foreign currency. Management expects this IFRIC may change the exchange rate used to translate advances received for revenue in a foreign currency. The impact on the initial measurement of revenue would depend on the

movements in exchange rates. It is effective for annual periods beginning on or after January 1, 2018.

- *IAS 40 Investment Property*: contains amendments to transfers of investment property. It is effective for annual periods beginning on or after January 1, 2018.
- *IFRIC 23 Uncertainty over Income Tax Treatments*: clarifies the application of recognition and measurement requirements in IAS 12, Income taxes, where there is uncertainty over income taxes. It is effective for annual periods beginning on or after January 1, 2019.

Other than IFRS 9 Financial Instruments (2014), which we early adopted on January 1, 2016, we have not yet adopted any of these new and amended standards or interpretations, and we are currently assessing the impact of adoption.

#### **INTERNAL CONTROLS OVER FINANCIAL REPORTING AND DISCLOSURE CONTROLS AND PROCEDURES**

The Chief Executive Officer (“CEO”) and the Chief Financial Officer (“CFO”) of Ten Peaks are responsible for establishing and maintaining adequate internal control over financial reporting (“ICFR”) to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. Under the supervision and with the participation of management, including the CEO and CFO, we conducted an evaluation of the design and effectiveness of our ICFR as of December 31, 2017, based on the updated framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO 2013”). Based on this assessment, the CEO and the CFO concluded that, as of December 31, 2017, Ten Peaks’ ICFR were effective.

The CEO and the CFO are also responsible for establishing and maintaining adequate disclosure controls and procedures. Disclosure controls and procedures are controls and other procedures designed to provide reasonable assurance that information required to be disclosed in documents filed or submitted under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation and includes controls and procedures designed to ensure that information required to be disclosed in documents filed or submitted under securities legislation is accumulated and communicated to the Company’s management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

The CEO and the CFO evaluated, or caused to be evaluated under their supervision, the effectiveness of our disclosure controls and procedures and based on this evaluation, the CEO and the CFO concluded that, as of December 31, 2017, Ten Peaks’ disclosure controls and procedures were effective.

There were no changes in our ICFR that occurred during the period beginning on October 1, 2017 and ended on December 31, 2017 have materially affected, or are reasonably likely to materially affect, Ten Peaks’ ICFR.

#### **SUBSEQUENT EVENTS**

On January 15, 2018, Ten Peaks paid an eligible dividend in the amount of \$0.6 million (\$0.0625 per share) to shareholders of record on December 29, 2017.

On February 21, 2018 the Company issued 22,348 of shares pursuant to Restricted Share Unit Plan.

On March 19, 2018, Ten Peaks declared an eligible dividend of \$0.0625 per share, to be paid on April 16, 2018 to shareholders of record on March 29, 2018.



**CONSOLIDATED FINANCIAL STATEMENTS**

**For the Year Ended December 31, 2017**



March 20, 2018

## **Independent Auditor's Report**

### **To the Shareholders of Ten Peaks Coffee Company Inc.**

We have audited the accompanying consolidated financial statements of Ten Peaks Coffee Company Inc. and its subsidiaries, which comprise the consolidated statement of financial position as at December 31, 2017 and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity, and consolidated statement of cash flows for the year then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

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

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

#### **Auditor's responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

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**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Ten Peaks Coffee Company Inc. and its subsidiaries as at December 31, 2017 and their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards.

**Other matter**

The financial statements of the Company for the year ended December 31, 2016, were audited by another auditor who expressed an unmodified opinion on those statements on April 21, 2017.

**(Signed) “PricewaterhouseCoopers LLP”**

**Chartered Professional Accountants**



# TEN PEAKS COFFEE COMPANY INC.

## Consolidated Statements of Financial Position as at (Tabular amounts in thousands of Canadian dollars)

	Note	December 31, 2017		December 31, 2016	
<b>Assets</b>					
Current assets					
Cash and cash equivalents	25	\$	9,486	\$	12,497
Accounts receivable	7		12,127		11,707
Inventories	6		14,671		11,574
Short-term investments	8		7,067		12,700
Prepaid expenses and other receivables			1,031		524
Derivative assets and hedged firm commitments	9, 23		1,244		95
Total current assets			45,626		49,097
Non-current assets					
Receivables	7		230		-
Plant and equipment	10		23,341		16,278
Intangible assets	11		1,427		1,687
Deferred tax assets	12		1,484		837
Derivative assets	9, 23		740		-
Total non-current assets			27,222		18,802
Total assets		\$	72,848	\$	67,899
<b>Liabilities and shareholders' equity</b>					
Current liabilities					
Accounts payable		\$	2,639	\$	2,392
Accrued liabilities			1,844		1,166
Income tax payable	12		105		405
Other liabilities	15		591		488
Dividend payable	20		565		565
Derivative liabilities	9, 23		229		815
Total current liabilities			5,973		5,831
Non-current liabilities					
Convertible debenture	14		11,658		11,283
Other liabilities	15		45		81
Asset retirement obligation	16		802		797
Deferred tax liabilities	12		3,426		1,676
Construction loan	24		844		-
Derivative liabilities	9, 14, 23		2,722		3,896
Total non-current liabilities			19,497		17,733
Total liabilities			25,470		23,564
Shareholders' equity					
Share capital	17		43,496		43,496
Retained earnings			2,257		357
Accumulated other comprehensive income			1,485		419
Share-based compensation reserve			140		63
Total equity			47,378		44,335
Total liabilities and shareholders' equity		\$	72,848	\$	67,899

### Commitments (Note 24)

### Subsequent Events (Note 27)

### Approved on behalf of the Board

(signed) "David Rowntree", Director

(signed) "Frank Dennis", Director

## TEN PEAKS COFFEE COMPANY INC.

### Consolidated Statements of Income

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

for the	Note	12 months ended December 31, 2017	12 months ended December 31, 2016
Revenue		\$ 83,755	\$ 81,927
Cost of sales		(71,165)	(69,877)
Gross profit		12,590	12,050
Operating expenses			
Administration expenses		(5,077)	(4,499)
Sales and marketing expenses		(2,586)	(2,398)
Occupancy expenses		(115)	(136)
Total operating expenses		(7,778)	(7,033)
Operating income		4,812	5,017
Non-operating or other			
Gain on risk management activities	23	1,190	632
Fair value gain on embedded option	14	604	6
Finance income		580	342
Finance expense		(1,414)	(346)
(Loss) gain on foreign exchange		(6)	91
Total non-operating or other		954	725
Income before tax		5,766	5,742
Income tax expense	12	(1,606)	(1,593)
<b>Net income</b>		<b>\$ 4,160</b>	<b>\$ 4,149</b>
Basic earnings per share	22	\$ 0.46	\$ 0.46
Diluted earnings per share	22	\$ 0.42	\$ 0.46

# TEN PEAKS COFFEE COMPANY INC.

## Consolidated Statements of Comprehensive Income and Consolidated Statements of Changes in Equity

(Tabular amounts in thousands of Canadian dollars)

### Consolidated Statements of Comprehensive Income for the

	12 months ended December 31, 2017	12 months ended December 31, 2016
<b>Net income</b>	\$ 4,160	\$ 4,149
<b>Other comprehensive income, net of tax</b>		
Items that may be subsequently reclassified to income:		
Unrealized gains		
Derivatives designated as cash flow hedges - currency risk hedges on US\$ future revenue	2,333	566
Items reclassified to income:		
Realized gains		
Derivatives designated as cash flow hedges - currency risk hedges on US\$ future revenue, recognized in revenue	(931)	-
Other comprehensive income related to hedging activities	1,402	566
Tax on other comprehensive income relating to hedging activities	(384)	(147)
Cumulative translation adjustment	48	-
<b>Other comprehensive income, net of tax</b>	1,066	419
<b>Net income and other comprehensive income</b>	\$ 5,226	\$ 4,568

### Consolidated Statements of Changes in Equity

	Note	Share capital		Share-based compensation reserve	Accumulated other comprehensive income	Retained earnings	Total equity
		Shares	Amount				
<b>Balance at December 31, 2015</b>		9,011,566	\$ 43,448	72	-	(1,536)	41,984
Shares issued for restricted share units		27,296	48	(48)	-	-	-
Share-based compensation		-	-	39	-	-	39
Dividends	20	-	-	-	-	(2,256)	(2,256)
Net income and other comprehensive income		-	-	-	419	4,149	4,568
<b>Balance at December 31, 2016</b>		9,038,862	\$ 43,496	63	419	357	44,335
Share-based compensation		-	-	77	-	-	77
Dividends	20	-	-	-	-	(2,260)	(2,260)
Net income and other comprehensive income		-	-	-	1,066	4,160	5,226
<b>Balance at December 31, 2017</b>		9,038,862	\$ 43,496	140	1,485	2,257	47,378

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

# TEN PEAKS COFFEE COMPANY INC.

## Consolidated Statements of Cash Flows

(Tabular amounts in thousands of Canadian dollars)

for the	Note	12 months ended December 31, 2017	12 months ended December 31, 2016
			Restated Note 26
<b>Operating activities</b>			
Net income		\$ 4,160	\$ 4,149
Items not affecting cash:			
Depreciation and amortization		2,172	2,053
Share-based compensation expense (recovery)		211	(180)
Unrealized gain on risk management activities	26	(1,463)	(1,755)
Unrealized gain on fair value adjustment of embedded option		(604)	(6)
Payment of restricted and deferred share units settled in cash		(60)	(147)
Finance income		(580)	(342)
Finance expense		1,414	346
Income taxes expense		1,606	1,593
		<hr/> 6,856	<hr/> 5,711
Change in non-cash working capital relating to operating activities	25, 26	(3,661)	3,357
<b>Net cash generated from operations</b>		<hr/> <b>3,195</b>	<hr/> <b>9,068</b>
Interest received		500	337
Interest paid		(1,033)	(251)
Income taxes paid		(915)	-
<b>Net cash generated from operating activities</b>		<hr/> <b>1,747</b>	<hr/> <b>9,154</b>
<b>Investing activities</b>			
Proceeds from (purchase of) short-term investments		5,633	(12,700)
Additions to plant and equipment		(8,131)	(5,293)
<b>Net cash used in investing activities</b>		<hr/> <b>(2,498)</b>	<hr/> <b>(17,993)</b>
<b>Financing activities</b>			
Dividends paid		(2,260)	(2,256)
Proceeds from convertible debenture, net of financing costs		-	14,527
<b>Net cash (used in) generated from financing activities</b>		<hr/> <b>(2,260)</b>	<hr/> <b>12,271</b>
<b>(Decrease) increase in cash and cash equivalents</b>		<hr/> <b>(3,011)</b>	<hr/> <b>3,432</b>
<b>Cash and cash equivalents, beginning of the year</b>		<hr/> <b>12,497</b>	<hr/> <b>9,065</b>
<b>Cash and cash equivalents, end of the year</b>		<hr/> <b>\$ 9,486</b>	<hr/> <b>\$ 12,497</b>

# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

### 1. NATURE OF BUSINESS

Ten Peaks Coffee Company Inc. (“Ten Peaks” or the “Company”) is a company incorporated under the Canada Business Corporations Act. The common shares of the Company are listed on the Toronto Stock Exchange under the symbol ‘TPK’. The Company’s registered office is located at 3131 Lake City Way, Burnaby, British Columbia, V5A 3A3.

Ten Peaks is a leading specialty coffee company that owns all of the interests of Swiss Water Decaffeinated Coffee Company Inc. (“SWDCC”), a British Columbia company, and Seaforth Supply Chain Solutions Inc. (“Seaforth”), a company incorporated under the Canada Business Corporations Act.

SWDCC is a premium green coffee decaffeinator located in Burnaby, BC. SWDCC employs the proprietary SWISS WATER® Process to decaffeinate green coffee without the use of chemicals, leveraging science-based systems and controls to produce coffee that is 99.9% caffeine free. The SWISS WATER® Process is certified organic by the Organic Crop Improvement Association and is the world’s only branded decaffeination process. SWDCC purchases premium grade green coffee, which it decaffeinate and offers for sale to coffee importers, coffee roasters and other customers (classified as its “regular” or “non-toll” business). In addition, SWDCC decaffeinate green coffee that belongs to its customers (classified as “toll” business). Coffee decaffeinate under toll arrangements is not included in inventory, as SWDCC does not take title to these coffees. SWDCC is the primary operating entity of the Company, and Ten Peaks results of operations are dependent upon those of this subsidiary.

SWDCC has a subsidiary, Swiss Water Decaffeinated Coffee Company USA, Inc., a Washington State corporation that acts as a marketing and sales company. It does not have significant assets. At the end of 2017, another subsidiary, Swiss Water Process Marketing Services Inc., a British Columbia company, was dissolved and its assets and liabilities were assumed by SWDCC.

Seaforth provides a complete range of green coffee handling and storage services, including devanning coffee received from origin; inspecting, weighing and sampling coffees; and storing, handling and preparing green coffee for outbound shipments. Seaforth, which is certified organic by Ecocert Canada, serves SWDCC and other coffee importers and brokers.

### 2. BASIS OF PREPARATION

The Company’s consolidated financial statements for the years ended December 31, 2017 and December 31, 2016 have been prepared in accordance with International Financial Reporting Standards (“IFRSs”).

These consolidated financial statements are presented in Canadian dollars, the Company’s functional currency.

The following standards became effective for annual periods beginning on or after January 1, 2017. The adoption of the new and revised standards by the Company in 2017 did not have a material impact on its consolidated financial statements apart from the adoption of IFRS 9 (2014) Financial Instruments, which is discussed in Note 3.9.

# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

- *IFRS 9 Financial Instruments*: The Company has early adopted all of the requirements of IFRS 9 as of January 1, 2016.
- *IAS 7 Statement of Cash Flows*: requires additional disclosures about changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.
- *IAS 12 Income Taxes*: implements a 'comprehensive balance sheet method' of accounting for income taxes which recognizes both the current tax consequences of transactions and events and the future tax consequences of the future recovery or settlement of the carrying amount of an entity's assets and liabilities. IAS 12 clarifies the requirements for recognizing deferred tax assets on unrealized loss, deferred tax where an asset is measured at fair value below the assets tax base and certain other aspects of accounting for deferred tax assets.
- *Investment Entities* (Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12: Disclosures of Interest in other entities, and IAS 28: Investments in Associates and joint Ventures): to address issues that have arisen in the context of applying the consolidation exception for investment entities.
- *IFRSs (Amendment)*: The Annual Improvements to IFRSs 2012-2016.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below.

#### 3.1 Basis of preparation

The consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments that are measured at fair values, as explained in the accounting policies below. Historical cost is based on the fair value of the consideration given in exchange for assets.

These accounting policies have been used throughout all periods presented in these consolidated financial statements.

#### 3.2 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries, all of which are wholly owned. Subsidiaries are all entities over which the Company has the power to control the financial and operating policies generally accompanying a shareholding of more than half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls another entity.

All intercompany transactions, balances, income and expenses are eliminated on consolidation.

#### 3.3 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

A geographical segment reflects the provision of products or services within a particular economic environment that is subject to risks and returns that are different from those of other economic environments.

## TEN PEAKS COFFEE COMPANY INC.

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### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

The Company's sales are primarily generated in a single business segment of decaffeination of green coffee beans. As such, management reports operating activities for geographical information only.

#### 3.4 Foreign currency translation

Functional and presentation currency:

Items included in the consolidated financial statements of each of the Company's subsidiaries are measured using the currency of the primary economic environment in which each entity operates ("the functional currency"). These consolidated financial statements are presented in Canadian dollars, which has been determined to be the Ten Peaks Coffee Company Inc. functional and presentation currency.

Transactions and balances:

Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the exchange rate prevailing at the reporting date.

Non-monetary items which are measured using historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Resulting foreign exchange gains or losses are recognized in income.

Foreign currency transactions are translated into functional currency of the entity at the exchange rates prevailing at the date of the transaction. Foreign exchange gains and losses are recognized in profit or loss in the period in which they occur. Foreign operations are translated from their functional currencies into Canadian dollars on consolidation as follows:

- a) Assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of the statement of financial position;
- b) Income and expenses for each statement of loss are translated at a quarterly average exchange rate (unless this rate is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions);
- c) Share capital for each statement of financial position presented are translated at historical rate; and
- d) All resulting exchange differences are recognized in other comprehensive income as cumulative translation adjustments.

Exchange differences that arise relating to long-term intercompany balances that form part of the net investment in a foreign operation are also recognized in this separate component of equity through other comprehensive income.

#### 3.5 Inventories

Raw materials are stated at the lower of cost, determined on a specific identification basis, and net realizable value, being the estimated selling price of finished goods less the estimated cost of completion of the finished goods.

Finished goods are stated at the lower of cost and net realizable value. Cost of finished goods includes all expenses directly attributable to the manufacturing process like direct labour and

# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

direct materials, as well as suitable portions of related fixed and variable production overheads, based on normal operating capacity. Costs of ordinarily interchangeable items are assigned on a first-in-first-out basis. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

### 3.6 Plant and equipment

The Company leases three facilities which house its production facility, offices and warehouse facilities. All plant and equipment is carried at acquisition cost or manufacturing cost less depreciation and impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the items. Subsequent costs are recognized in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance expenditures are recognized in the statement of income and comprehensive income during the financial period in which they are incurred.

Borrowing costs directly attributed to the construction of any qualifying asset are capitalized during the period of time that is required to complete and prepare the asset for its intended use.

Major renovations are depreciated over the remaining useful life of the related asset or to the date of the next major renovation, whichever is sooner.

The costs related to the plant and equipment in the course of construction are classified as construction-in-progress. Such items are transferred to the appropriate category of plant and equipment when it is completed and ready for intended use. Depreciation of these assets commences when the asset is available for use.

Depreciation is recognized on a straight-line basis to allocate the cost or valuation of each asset to its residual value over its estimated useful life commencing when the asset is ready for its intended use. The estimated useful lives of plant and equipment are as follows:

Leasehold improvements	to expiry of the lease renewal option or lease term
Production machinery	to expiry of the lease renewal option or lease term
Assets under financial lease	to expiry of the lease renewal option or lease term
Warehouse and office equipment	10 years
Computer hardware and software	5 years
Furniture and fixtures	5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

### 3.7 Intangible assets

(a) Proprietary process technology ("PPT")

PPT represents intangible assets of SWDCC with a finite life and is carried at cost less accumulated amortization. Amortization is recognized on a straight-line basis to allocate the cost of PPT to its residual value over its estimated useful life of 14 years.



# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

(b) Brand

SWDCC's brand has a finite useful life and is carried at cost less accumulated amortization. Amortization is recognized on a straight-line basis over its estimated useful life of 14 years.

### 3.8 Impairment of assets

Plant and equipment and intangible assets with finite lives and that are subject to depreciation or amortization are tested for impairment indicators at the end of each reporting period. If any such indicator exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss.

An impairment loss is recognized for the amount by which the carrying amount of an asset or cash generating unit ("CGU") exceeds its recoverable amount. The Company has determined that it has only one CGU and that all assets relate to that CGU. To determine the recoverable amount, management estimates either the fair value less costs to sell, or the value-in-use based on the present value of expected future cash flows from the CGU. In estimating the value-in-use, management must determine the appropriate discount rate in order to calculate the present value of those cash flows, as well as make certain assumptions about future profits which relate to future events and circumstances. Discount factors are determined individually for each asset or CGU and reflect their respective risk profiles as assessed by management. There were no indicators of impairment during the year.

### 3.9 Financial instruments

The Company has early adopted IFRS 9 as issued in July 2014 with a date of initial application of January 1, 2016. IFRS 9 introduces new requirements for the classification and measurement of financial assets. IFRS 9 requires all recognized financial assets to be measured at amortized cost or fair value in subsequent accounting periods following initial recognition. IFRS 9 also amends the requirements around hedge accounting, and introduces a single, forward-looking expected credit loss impairment model.

All financial assets, other than accounts receivable, are included in the measurement category of fair value through profit and loss. There was no change to the measurement category for financial liabilities at amortized cost.

#### Recognition

Financial assets and financial liabilities, including derivatives, are recognized on the consolidated statement of financial position when the Company becomes a party to the financial instrument or derivative contract.

#### Classification

From January 1, 2016, the Company classifies its financial assets and financial liabilities in the following measurement categories i) those to be measured subsequently at fair value (either through other comprehensive income or through profit or loss) and ii) those to be measured at amortized cost. The classification of financial assets depends on the business model for managing the financial assets and the contractual terms of the cash flows. Financial liabilities are classified as those to be measured at amortized cost unless they are designated as those to be measured subsequently at fair value through profit or loss (irrevocable election at the time of recognition).

## TEN PEAKS COFFEE COMPANY INC.

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### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

For assets and liabilities measured at fair value, gains and losses are either recorded in profit or loss or other comprehensive income.

The Company reclassifies financial assets when and only when its business model for managing those assets changes. Financial liabilities are not reclassified.

The Company has implemented the following classifications for financial instruments, other than derivatives:

- Cash and cash equivalents and short-term investments are classified as assets at fair value and any period change in fair value is recorded through interest income in the consolidated statement of income, as applicable.
- Accounts receivable and other receivables are classified as assets at amortized cost using the effective interest rate method. Interest income is recorded in the consolidated statement of income, as applicable.
- Accounts payable, credit facilities, the debt portion of the convertible debenture, the construction loan and other liabilities are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method. Interest expense is recorded in the consolidated statement of income, as applicable.

With the adoption of hedge accounting, “gains/losses on risk management activities” reflects the change in fair value of undesignated revenue hedges and gains or losses on designated hedging instruments that are not otherwise recorded in the income statement with the hedged item (revenue or cost of sales).

Also, with the adoption of hedge accounting, “fair value gains/losses on embedded option” are gains or losses on embedded derivative in the convertible debenture debt instrument.

#### **Measurement**

All financial instruments are required to be measured at fair value on initial recognition, plus, in the case of a financial asset or liability not at fair value through profit and loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability. Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit and loss. Financial assets and financial liabilities with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Financial assets that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of the subsequent accounting periods. All other financial assets are measured at their fair values at the end of the subsequent accounting periods, with any changes taken through profit and loss or other comprehensive income. The requirements for classification and measurement of financial liabilities largely carried forward existing requirements in IAS 39, Financial Instruments – Recognition and Measurement, except that fair value changes due to credit risk for liabilities designated at fair value through profit and loss would, under IFRS 9, generally be recorded in other comprehensive income.

## TEN PEAKS COFFEE COMPANY INC.

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### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

#### Impairment

The Company assesses all information available, including on a forward-looking basis, the expected credit losses associated with its assets carried at amortized cost. The Company's only financial asset at amortized cost are accounts receivable and other receivables, for these the Company applies the simplified approach as permitted by IFRS 9 which requires expected lifetime credit losses to be recognized from initial recognition of the receivables.

#### Derivatives and Hedge Accounting

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged, and the type of hedge relationship designated.

The Company designates derivatives as hedges for the risk of changes in fair value of the purchase commitment due to changes in benchmark coffee commodity prices and foreign exchange as fair value hedges.

The Company also designates derivatives as hedges of foreign exchange risk associated with the cash flows of highly probable forecast transactions as cash flow hedges.

The Company documents at the inception of the hedging transaction the economic relationship between hedging instruments and hedged items including whether the hedging instrument is expected to offset changes in cash flows of hedged items. The Company documents its risk management objective and strategy for undertaking various hedge transactions at the inception of each hedging relationship.

The Company applied hedge accounting prospectively to economic hedges entered into in accordance with its Foreign Exchange Risk Management Policy (FX Policy) and the Commodity Price Risk Management Policy (Commodity Policy). Economically, the specific hedging activities carried out under these policies by the Company are as follows:

##### *Currency risk hedges on US\$ purchases ("customer-specific hedges"):*

The Company enters into forward contracts to buy US dollars (US\$) for significant purchase commitments, such as green coffee inventory which, once decaffeinated, is sold at a fixed Canadian dollar (C\$) price. To mitigate the exposure to changing margin on these transactions arising from fluctuations in the US\$/C\$ exchange rate, the Company enters into US\$ forward purchase contracts which economically lock in the US\$/C\$ exchange rate, and effectively locks in the C\$ cost of inventory to be sold at the fixed C\$ amount.

At each period end, currency risk hedges on US\$ purchases are re-measured to their fair value. Under hedge accounting, the effective portion of the gains (losses) will be held on the consolidated statement of financial position until the inventory is received and subsequently sold, at which time the gains (losses) will flow to cost of sales on the consolidated statement of income.

## TEN PEAKS COFFEE COMPANY INC.

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### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

#### *Commodity price risk hedges on purchase commitments and inventory ("commodity hedges"):*

When the Company enters into a purchase commitment to purchase green coffee and fixes the New York 'C' ("NY'C") price component (which it will later sell at a to-be-determined price based on the NY'C), the Company enters into an offsetting short position on the IntercontinentalExchange. The Company monitors, on a macro basis, the amount of purchase commitments and amount of inventory on hand for which the ultimate sale price is variable and has not yet been fixed based on the NY'C' and compares this to the amount of coffee covered by future net short positions to determine whether the net short position requires adjustment.

At each period end, commodity price risk hedges are re-measured to their fair value. Under hedge accounting, the effective portion of the gains (losses) for price fixed hedged coffee contracts and coffee inventory will be held on the consolidated statement of financial position until inventory for such contracts is received and subsequently sold, at which time the gains (losses) will flow to cost of sales on the consolidated statement of income.

#### *Currency risk hedges on US\$ future revenue ("revenue hedges"):*

The Company enters into forward contracts to sell US\$ at future dates to hedge the foreign exchange cash flow variability of expected US\$ processing fee revenue. The hedged processing revenue includes both processing fee revenue from tolling arrangements (processing of customer owned coffee) as well as the US\$ processing fee layer of inventory sales agreements.

At each period end, currency risk hedges on US\$ future revenues are re-measured to their fair value. Under hedge accounting, unrealized gains (losses) for US\$ forward contracts are reclassified so that the impact on the consolidated statement of income is deferred through other comprehensive income, until the hedge instrument matures, at which time the realized gain (loss) is reflected in revenue on the consolidated statement of income.

On all hedges entered into, if the hedge ratio for risk management purposes is no longer optimal but the risk management objective remains unchanged and the hedge continues to qualify for hedge accounting, the hedge relationship will be rebalanced by adjusting either the volume of the hedged instrument or the volume of the hedged item so that the hedge ratio aligns with the ratio used for risk management purposes. Any hedge ineffectiveness is calculated and accounted for in profit or loss at the time of the hedge relationship rebalancing.

#### **Fair Value Hierarchy**

The Company classifies and discloses the fair value measurements of its financial instruments using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 – valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – valuation techniques based on inputs other than quoted prices that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. The Company classifies a financial instrument to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

### 3.10 Current and deferred income taxes

Income tax expense comprises current and deferred tax. Income tax expense is recognized in the statement of income and comprehensive income except to the extent that it relates to items recognized either in other comprehensive income or directly in equity.

The income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the reporting date, and any adjustments to taxes payable in respect of previous years. The Company periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

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

Deferred income tax assets are recognized only to the extent that it is probable that future taxable income will be available against which temporary differences and non-capital loss carry forwards can be utilized.

### 3.11 Provisions

Provisions are recognized when the Company has a present legal or constructive obligation as a result of a past event, it is probable that it will lead to an outflow of economic resources from the Company and amounts can be estimated reliably, although timing or amount of the outflow may still be uncertain.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the reporting date, including the risks and uncertainties associated with the present obligation. The discount rate used to determine the present value reflects current market assessments of the time value of money and the increases specific to the liability.

Any reimbursement that the Company can be virtually certain to collect from a third party with respect to the obligation is recognized as a separate asset. However, this asset may not exceed the amount of the related provision.

All provisions are reviewed at the end of each reporting period and adjusted or reversed to reflect management's current best estimate of the expenditure required to settle the present obligation at the end of the reporting period. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision is reversed. Provisions are reduced by actual expenditures for which the provision was originally recognized.

## TEN PEAKS COFFEE COMPANY INC.

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### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

Where discounting has been used, the carrying amount of a provision is accreted during the period to reflect the passage of time.

#### **3.12 Leases as the lessee**

Leases where the lessor retains a significant portion of the risks and rewards of ownership are classified as operating leases. Payments on operating lease agreements are recognized as an expense on a straight-line basis over the lease term.

#### **3.13 Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable. Revenue is reduced for estimated customer returns, rebates and other similar allowances.

Revenue is recognized when all the following conditions are satisfied:

- persuasive evidence of an arrangement exists;
- the goods are shipped;
- title has passed to the customer;
- the price has been substantively determined; and
- collection is reasonably assured.

#### **3.14 Employee benefits**

The Company provides benefits to employees through a registered retirement savings plan ("RRSP"). The Company contributes a percentage of earnings into an RRSP administered by an independent entity. Ultimately, each employee manages his or her own RRSP within the scope of the plan provided by the third-party administrator. The RRSP has no assurance of defined benefits to employees, and as such the Company has no legal or constructive obligations to make further contributions.

The Company also pays contributions to government pension insurance plans. The contributions are recognized as employee benefit expenses when they are due.

#### **3.15 Share-based compensation**

The Company has a restricted share unit ("RSU") plan for certain officers and employees and a deferred share unit ("DSU") plan for non-employee directors (collectively, "participants").

The RSUs granted are compound financial instruments as they are expected to be settled using a combination of cash and equity.

The equity-settled share-based compensation is measured at the fair value of the Company's common shares as at the grant date using a volume weighted average share price in accordance with the terms of the RSU Plan. The fair value determined at the grant date is charged to income on a straight-line basis over the vesting period, based on the estimate of the number of RSUs that will eventually vest and be converted to common shares, with a corresponding increase in equity (share-based compensation reserve). As necessary, the Company revises its estimate if subsequent information indicates that the number of RSUs expected to vest differs from previous estimates. On the vesting date, the Company revises the estimate to equal the number of equity instruments that ultimately vested. The impact of the revision of estimates, if any, is recognized

# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

in income or expense such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the share-based compensation reserve.

For cash-settled share-based compensation, a long-term liability is recognized, measured initially at the fair value of the long-term liability using a volume weighted average share price. The amount of the liability is charged to income on a straight-line basis over the vesting period, based on the estimate of the number of RSUs that will eventually vest and be settled in cash. As necessary, the Company revises its estimate if subsequent information indicates that the number of RSUs expected to vest differs from previous estimates. On the vesting date, the Company revises the estimate to equal to the number of RSUs that ultimately vested and are settled in cash. The impact of the revision of estimates, if any, is recognized in income or expenses such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the long-term liability or current liability depends on the timing when the liability become due. At the end of each reporting period until the liability is settled, and at the date of settlement, the fair value of the liability is remeasured using a volume weighted average share price, with any change in fair value recognized in income or expense for the year.

DSUs are issued to participants who elect to defer a portion of their current compensation in exchange for DSUs. DSUs are classified as cash-settled share-based payment transactions as participants receive cash following a Redemption Event. The DSUs do not contain any vesting conditions or forfeiture provisions, as they are issued in exchange for deferred compensation. The Company recognizes the expense and the liability to pay for the eventual redemption when the DSUs are issued. Thereafter, the Company re-measures the liability at the end of each reporting date and the date of settlement, with the difference recognized in income or expense for the period. The fair value of DSUs is determined in accordance with the DSU Plan, which uses the average closing price for Ten Peaks shares for the five trading days immediately preceding the relevant date.

### 3.16 Earning per share (“EPS”)

The Company presents basic and diluted EPS for its common shares. Basic EPS is calculated by dividing income or loss attributable to shareholders of the Company by the weighted average number of common shares outstanding during the year. Diluted EPS is calculated by dividing income or loss attributable to shareholders of the Company by the weighted average number of common shares outstanding, adjusted for the effects of all dilutive potential common shares.

### 3.17 Application of revised IFRSs

The following new standards, amendments to accounting standards and interpretations have been issued and will be effective in future periods, with earlier adoption permitted:

- *IFRS 2: Share based payment*: contains amendments to classification and measurement of share-based payment transactions. It is effective for annual periods beginning on or after January 1, 2018.
- *IFRS 15: Revenue from Contracts with Customers*: replaces IAS 11, IAS 18, IFRIC 13, IFRIC 15, IFRIC 18 and SIC-31. IFRS 15 establishes principles to address the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity’s contracts with customers. The core principle of IFRS 15 is that revenue related to the transfer of promised goods or services should be recognized when the control of the goods or services passes to customers. The

# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

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Company has evaluated the impact of applying IFRS 15, analyzing its toll revenue, regular decaffeinated coffee sales and coffee handling agreements. The Company concluded there is no material change in the timing of revenue recognized under the new standard as the point of transfer of risk and reward for goods and services and transfer of control occurs at the same time. In addition, IFRS 15 requires entities to apportion revenue earned from contracts to distinct performance obligations on a relative standalone selling price basis. The impact of this change on the amount of revenue recognized in a year is insignificant. IFRS 15 contains additional presentation and disclosure requirements which are more detailed than the current standards. Upon the adoption of IFRS 15, the Company will provide disclosures for each of the Company's revenue streams to supplement the revenue data that is currently presented in the segmented information disclosure. It is effective for annual periods beginning on or after January 1, 2018.

- *IFRS 16: Leases:* requires an application of control model to the identification of leases, distinguishing between a lease and a service contract. Also, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to the current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. A lessee can choose to apply IFRS 16 using either a full retrospective or a modified retrospective approach. The Company plans to apply IFRS 16 as at the date it becomes effective but has not yet selected a transition approach. It is effective for annual periods beginning on or after January 1, 2019.
- *IFRIC 22: Foreign Currency Transactions and Advance Consideration:* clarifies the appropriate exchange rate to use on initial recognition of an asset, expense or income when advance consideration is paid or received in a foreign currency. Management expects this IFRIC may change the exchange rate used to translate advances received for revenue in a foreign currency. The impact on the initial measurement of revenue would depend on the movements in exchange rates. It is effective for annual periods beginning on or after January 1, 2018.
- *IAS 40 Investment Property:* contains amendments to transfers of investment property. It is effective for annual periods beginning on or after January 1, 2018.
- *IFRIC 23 Uncertainty over Income Tax Treatments:* clarifies the application of recognition and measurement requirements in IAS 12, Income taxes, where there is uncertainty over income taxes. It is effective for annual periods beginning on or after January 1, 2019.

The Company has not yet adopted any of these new and amended standards or interpretations and is currently assessing the impact of adoption.

#### 4. MANAGEMENT JUDGMENTS AND ESTIMATION UNCERTAINTY

Judgment is used by management in selecting accounting policies, the determination of functional currency, the identification of CGUs, and the identification of revenue streams. In addition, judgment is often required in applying accounting policies, and in respect of items where the choice of a specific policy, accounting estimate or assumption to be followed could materially affect the reported results or net asset position of the Company should it later be determined that a different choice would be more appropriate.



# TEN PEAKS COFFEE COMPANY INC.

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## Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

Management considers the accounting estimates and assumptions discussed below to be its critical accounting estimates and accordingly, provides an explanation of each below. Actual results could differ from those estimates and assumptions.

### 4.1 Useful lives of depreciable assets

Management reviews the useful lives of depreciable assets at each reporting date. At December 31, 2017 management determined that the useful lives represent the expected utility of the assets to the Company.

### 4.2 Provision for asset retirement obligations

Analysis and estimates are performed by the Company in order to determine the amount of restoration costs to be recognized as a provision in the Company's consolidated financial statements. The estimates consider the contract language in the lease, the expected useful lives of the Company's equipment, and the expected costs that would be paid to a third party to remove equipment.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When the final determination of such obligation amounts differs from the recognized provisions, the Company's financial statements will be impacted.

### 4.3 Income taxes

The Company computes income taxes using the liability method, under which deferred income taxes are provided for the temporary differences between the financial reporting bases and the tax bases of the Company's assets and liabilities. Deferred tax assets and liabilities are measured using the enacted and substantively enacted income tax rates that are expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

Deferred tax assets also reflect estimates of the recoverability of non-capital loss carry forwards. The Company has recognized the benefit of loss carry forwards to the extent that it is probable that taxable income will be available in the future against which the non-capital loss carry forwards can be utilized.

The financial reporting bases of the Company's assets reflect the useful lives of depreciable assets, as well as the carrying amounts of assets with indefinite useful lives. Accordingly, management estimates that impact the carrying amounts of depreciable and non-depreciable assets also have an impact on deferred income tax assets and liabilities.

### 4.4 Convertible Debenture

Management estimates the interest rate on a similar instrument of comparable credit status and providing for substantially the same cash flows, on the same terms, but without the equity conversion option in the calculation of the fair value of the liability portion of the convertible debenture upon initial recognition. Management also estimates the fair values of the derivative liability related to the convertible debenture at initial recognition and at the end of each

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

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reporting period using the Black-Scholes option pricing model which requires management estimates. Details of these can be found in Note 14.

#### 5. CAPITAL MANAGEMENT

The Company's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. The Company considers its capital structure to include shareholders' equity and indebtedness. In order to maintain or adjust the capital structure, the Company may from time to time issue common shares, issue additional debt, adjust its capital spending, modify its dividend policy, and/or dispose of certain assets to manage current and projected debt levels.

The Company manages its capital in order to meet its growth objectives while continuing to pay quarterly dividends to its shareholders. The dividend policy of Ten Peaks is subject to the discretion of the Board of Directors, which reviews the level of dividends periodically on the basis of a number of factors including Ten Peaks' financial performance, future prospects, and the capital requirements of the business. Quarterly dividends are paid on a level basis in order to smooth out normal seasonal fluctuations that occur over the course of a year.

#### 6. INVENTORIES

	December 31, 2017		December 31, 2016	
Raw materials	\$	8,147	\$	5,863
Finished goods		6,072		5,836
Carbon		397		315
Packaging		32		147
Hedge accounting component		23		(587)
	\$	14,671	\$	11,574

During the year ended December 31, 2017, the cost of inventories recognized in cost of sales was \$68 million (2016: \$65 million). The inventory provision was \$0.08 million during the year (2016: \$0.07 million).

#### 7. ACCOUNTS RECEIVABLE

	December 31, 2017		December 31, 2016	
Accounts receivable	\$	12,127	\$	11,707
Receivables, non-current		230		-

The Company's accounts receivable has been reviewed for indicators of impairment. No accounts were found to be impaired and therefore no allowance for credit losses was provided as at December 31, 2017 and December 31, 2016. Non-current accounts receivable includes a \$0.1 million balance due from a related party, refer to Note 19.

## TEN PEAKS COFFEE COMPANY INC.

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#### 8. SHORT-TERM INVESTMENTS

Short-term investments consist of guaranteed investment certificates with maturities greater than three months and less than nine months from the day of their acquisition, with a fixed interest rate of 1.4% (2016: 1.2% to 1.5%).

#### 9. DERIVATIVE FINANCIAL INSTRUMENTS

The Company's derivative financial instruments were carried at fair value through profit or loss as follows:

	December 31, 2017	December 31, 2016
Coffee futures contracts, net	\$ 247	\$ 95
US Dollar forward contracts, current	(3)	(815)
US Dollar forward contracts, long term	(13)	(582)
Derivative financial liability, convertible debenture	(2,709)	(3,314)
	\$ (2,478)	\$ (4,616)

#### 10. PLANT AND EQUIPMENT

	Machinery and equipment	Leasehold improvements	Computer equipment	Furniture and fixtures	Construction in progress	Total
<b>Cost</b>						
Balance January 1, 2017	\$ 33,557	\$ 5,052	\$ 1,062	\$ 181	\$ 2,083	\$ 41,935
Additions	187	61	142	8	8,577	8,975
Balance December 31, 2017	\$ 33,744	\$ 5,113	\$ 1,204	\$ 189	\$ 10,660	\$ 50,910
<b>Accumulated depreciation</b>						
Balance January 1, 2017	\$ (21,546)	\$ (3,227)	\$ (750)	\$ (134)	\$ -	\$ (25,657)
Depreciation	(1,515)	(274)	(112)	(11)	-	(1,912)
Balance December 31, 2017	\$ (23,061)	\$ (3,501)	\$ (862)	\$ (145)	\$ -	\$ (27,569)
<b>Balance, December 31, 2017</b>	<b>\$ 10,683</b>	<b>1,612</b>	<b>342</b>	<b>44</b>	<b>10,660</b>	<b>23,341</b>
<b>Cost</b>						
Balance January 1, 2016	\$ 28,284	\$ 4,952	\$ 998	\$ 304	\$ 2,127	\$ 36,665
Additions	-	63	-	-	5,230	5,293
Disposals	(23)	-	-	-	-	(23)
Transfers	5,296	37	64	(123)	(5,274)	-
Balance December 31, 2016	\$ 33,557	\$ 5,052	\$ 1,062	\$ 181	\$ 2,083	\$ 41,935
<b>Accumulated depreciation</b>						
Balance January 1, 2016	\$ (20,229)	\$ (2,882)	\$ (641)	\$ (157)	\$ -	\$ (23,909)
Depreciation	(1,285)	(345)	(109)	(9)	-	(1,748)
Transfers	(32)	-	-	32	-	-
Balance December 31, 2016	\$ (21,546)	\$ (3,227)	\$ (750)	\$ (134)	\$ -	\$ (25,657)
<b>Balance, December 31, 2016</b>	<b>\$ 12,011</b>	<b>1,825</b>	<b>312</b>	<b>47</b>	<b>2,083</b>	<b>16,278</b>

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

#### For the year ended December 31, 2017

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For the year ended December 31, 2017, depreciation expense of \$1.8 million (2016: \$1.7 million) has been charged to cost of sales and \$0.1 million (2016: \$0.1 million) was included in administrative expenses. There was no impairment loss recognized for the years ended December 31, 2017 and 2016.

#### 11. INTANGIBLE ASSETS

	PPT		Brand		Total
<b>Cost</b>					
Balance January 1, 2017	\$	3,246	\$	1,000	\$ 4,246
Balance December 31, 2017	\$	3,246	\$	1,000	\$ 4,246
<b>Amortization</b>					
Balance January 1, 2017	\$	(1,680)	\$	(879)	\$ (2,559)
Amortization		(240)		(20)	(260)
Balance December 31, 2017	\$	(1,920)	\$	(899)	\$ (2,819)
<b>Carrying amount December 31, 2017</b>	\$	1,326	\$	101	\$ 1,427
<b>Cost</b>					
Balance January 1, 2016	\$	3,246	\$	1,000	\$ 4,246
Balance December 31, 2016		3,246		1,000	4,246
<b>Amortization</b>					
Balance January 1, 2016	\$	(1,440)	\$	(859)	\$ (2,299)
Amortization		(240)		(20)	(260)
Balance December 31, 2016	\$	(1,680)	\$	(879)	\$ (2,559)
<b>Carrying amount December 31, 2016</b>	\$	1,566	\$	121	\$ 1,687

For the year ended December 31, 2017, amortization expense of \$0.2 million (2016: \$0.2 million) relating to proprietary process technology ("PPT") has been charged to cost of sales and \$0.02 million (2016: \$0.02 million) relating to Brand was included in administrative expenses. There was no impairment loss recognized for the years ended December 31, 2017 and 2016.

#### 12. TAX

##### 12.1 Income tax expense

	December 31, 2017		December 31, 2016	
Current expense	\$	890	\$	403
Deferred tax expense		716		1,190
Total income tax expense	\$	1,606	\$	1,593

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

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#### 12.2 Reconciliation

Income tax expense for the year can be reconciled to the accounting profit as follows:

	December 31, 2017	December 31, 2016
Statutory rate	26%	26%
Income before tax	\$ 5,766	\$ 5,742
Income tax calculated at applicable tax rate	\$ 1,503	\$ 1,493
Non-deductible expenses	109	88
Foreign tax rate differential	(6)	12
Income tax expenses	\$ 1,606	\$ 1,593

#### 12.3 Current income tax payable

	December 31, 2017	December 31, 2016
Income tax payable	\$ 105	\$ 405

#### 12.4 Deferred income tax assets (liabilities)

The movement in deferred income tax assets and liabilities during the year was as follows:

	Goodwill and intangibles	Share and debt issue costs and other	Property plant and equipment	Share based ARO	Derivative liability and convertible debenture	Other comprehensive income	Tax Losses	Total
Balance January 1, 2016	\$ 698	\$ 392	(2,819)	\$ 182	\$ 360	-	-	\$ 1,515
Expense (recovery)	(19)	41	193	25	16	(123)	(147)	(1,167)
Balance, December 31, 2016	\$ 679	\$ 433	(2,626)	\$ 207	\$ 376	(123)	(147)	\$ 362
Balance, January 1, 2017	679	433	(2,626)	207	376	(123)	(147)	(839)
Expense (recovery)	13	(208)	(97)	10	(204)	(48)	(385)	(1,103)
Balance, December 31, 2017	\$ 692	\$ 225	(2,723)	\$ 217	\$ 172	(171)	(532)	\$ 178

SWDCC has no non-capital tax losses carry forwards as the end of December 31, 2017. Ten Peaks has non-capital tax loss carry forwards of \$0.2 million which begin to expire in 2036. Seaforth has non-capital tax loss carry forwards of \$0.4 million that begin to expire in 2033.

#### 13. CREDIT FACILITIES

The Company had no outstanding debt as at December 31, 2017 or December 31, 2016. As at December 31, 2017, the company had the following credit facilities:

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

- a. a \$14.5 million revolving operating line of credit which bears interest at the bank's prime lending rate plus 0.75% per annum; and
- b. a \$1.5 million swing operating line of credit which bears interest at the bank's prime lending rate plus 0.75% per annum.

Any US\$ denominated debt under the revolving operating line of credit or swing line can be financed using LIBOR loans at the LIBOR rate plus 2.35% per annum.

In addition, the Company has a US\$8.0 million foreign exchange and commodity futures contract facility, which allows the Company to enter into spot, forward and other foreign exchange rate transactions and commodity futures transactions with the bank with a maximum term of up to 60 months.

These facilities are collateralized by a general security agreement over all of the assets of the Company and a floating hypothecation agreement over cash balances.

As at December 31, 2017, the Company was in compliance with its debt covenants and had not made use of any of its credit facilities.

#### 14. CONVERTIBLE DEBENTURE

	December 31, 2017	December 31, 2016
<b>Balance, open</b>	\$ 11,283	\$ -
Proceeds from issuance	-	15,000
Debt issuance costs	-	(473)
Fair value of derivative	-	(3,319)
Interest charged	1,403	306
Interest paid	(1,028)	(231)
<b>Balance, end</b>	\$ 11,658	\$ 11,283

On October 11, 2016, the Company issued an unsecured subordinated convertible debenture for gross proceeds of \$15,000,000. The Convertible Debenture bears interest at a rate of 6.85% per annum to be paid quarterly in arrears and is due on October 11, 2023.

The Convertible Debenture is convertible into Common Shares of the Company at a conversion price of \$8.25 per Common Share. Under the terms of the agreement, Ten Peaks has the option to pay interest-in-kind for the first two years. If elected, this option will increase the principal sum by the interest owing.

The Convertible Debenture also includes a net share settlement feature that allows Ten Peaks, upon conversion, to elect to pay cash equal to the face value of the Convertible Debenture and to issue Common Shares equal to the excess value of the underlying equity above the face value of the Convertible Debenture. If the Net Share Settlement option is elected, it will result in fewer Common

## TEN PEAKS COFFEE COMPANY INC.

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Shares being issued. In 2016, the Company paid financing costs of \$0.5 million in respect of issuing the convertible debenture.

The liability component was initially measured at a fair value of \$11.2 million, which represents the present value of the contractually determined stream of cash flows discounted at the prevailing market interest rate at that time applicable to instruments of comparable credit status and providing substantially the same cash flows, on the same terms, but without derivative components, of 12.15% per annum.

	December 31, 2017	December 31, 2016
<b>Balance, open</b>	\$ 3,313	\$ -
Fair value of derivative liability	-	3,319
Change in fair valuation of derivative embedded option	(604)	(6)
<b>Balance, end</b>	\$ 2,709	\$ 3,313

The Company uses the residual value method to allocate the fair value of the convertible debentures between the liability component and the derivative liability. Under this method, as at balance sheet date, the derivative liabilities include fair value of the derivative liability related to convertible debenture in the amount of \$2.7 million (2016: \$3.3 million at inception). The fair value of the derivative liability was determined using the Black-Scholes Option Pricing Model. The variables and assumptions used in computing the fair value are based on management's best estimate. The value varies with different variables of certain subjective assumptions.

Inputs into the Black-Scholes Option Pricing Model to determine the fair value of the conversion option:

	December 31, 2017	December 31, 2016
Share price	\$ 6.70	\$ 7.37
Exercise price	\$ 8.25	\$ 8.25
Option life	5.79 years	7 years
Volatility	40%	39%
Risk-free interest rate	1.90%	0.92%
Dividend yield	3.73%	3.39%

#### 15. OTHER LIABILITIES

The balance represents the fair value of the deferred share units ("DSUs") and of the cash-settled portion of the restricted share units ("RSUs") outstanding as follows:

	December 31, 2017	December 31, 2016
Other liabilities, current	\$ 591	\$ 488
Other liabilities, non-current	45	81
	636	569

## TEN PEAKS COFFEE COMPANY INC.

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### Notes to the Consolidated Financial Statements

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#### 16. ASSET RETIREMENT OBLIGATION

The Company estimates the total undiscounted amount of any cash flows required to settle its ARO is approximately \$0.9 million, which will be incurred on or about the expiry of the third lease renewal term in 2023. As at December 31, 2017, the Company has a long-term liability ARO of \$0.8 million (2016: \$0.8 million), reflecting the present value of the ARO using a credit adjusted risk free rate of 1.90%.

#### 17. SHARE CAPITAL

Ten Peaks is authorized to issue an unlimited number of common shares. Each share is equally eligible to receive dividends when declared and represents one vote at meetings of shareholders.

As of December 31, 2017, there were 9,038,862 (2016: 9,038,862), common shares, and 100,783 (2016: 48,285), restricted share units outstanding, respectively.

##### Restricted share units

The Company has a restricted share unit plan ("RSU Plan") which allows it to grant RSUs to officers, employees and consultants of Ten Peaks or its subsidiaries. The RSU Plan is administered by the Board of Directors, which sets the terms of incentive awards under the RSU Plan. The maximum number of common shares available for issue under the RSU Plan is 333,760, being 5% of the issued and outstanding common shares of the Company as at the date it was approved by shareholders. These grants vest on the third anniversary of issuance (with certain exceptions) provided the grant recipient is still employed by Ten Peaks or one of its subsidiaries as at the date of vesting. Grants are forfeited (with certain exceptions) if a recipient is no longer employed by Ten Peaks or one of its subsidiaries. Upon vesting, each RSU converts to one common share. These grants allow participants to receive up to 50% of the market value of the award in cash (instead of shares) upon vesting, in order to facilitate payment of taxes owing on the awards. Any RSUs paid in cash are returned to the pool and may be re-issued, subject to the maximum number of common shares available under RSU.

Periodically, the Company grants RSU awards. Each award is increased by the value of dividends paid to shareholders during the vesting period, using a formula which uses the higher of the then-current share price or \$3.20.

The movement in RSUs for the years ended December 31, 2017 and December 31, 2016 is as follows:



## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

	Number of RSUs	Volume based weighted average share price	Average remaining vesting period (years)	Performance based
<b>Balance at January 1, 2016</b>	<b>97,304</b>	<b>\$ 12.01</b>	<b>1.45</b>	
RSUs issued for dividends	2,477	\$ 8.62	1.03	No
RSUs forfeited	(3,136)	\$ 6.92	-	No
RSUs cash-settled	(21,064)	\$ 6.96	-	No
RSUs exercised	(27,296)	\$ 6.96	-	No
<b>Balance at December 31, 2016</b>	<b>48,285</b>	<b>\$ 7.86</b>	<b>1.14</b>	
<b>Balance at January 1, 2017</b>	<b>48,285</b>	<b>\$ 7.86</b>	<b>0.14</b>	
RSUs granted	52,480	\$ 6.15	2.15	No
RSUs issued for dividends	3,522	\$ 6.30	1.06	No
RSUs forfeited	(3,504)	\$ 6.26	-	No
<b>Balance at December 31, 2017</b>	<b>100,783</b>	<b>\$ 6.58</b>	<b>1.15</b>	

#### Deferred share units

The Company has a deferred share unit plan (the “DSU Plan”) in order to issue deferred share units (“DSUs”) to non-employee directors (collectively, “participants”) of Ten Peaks. The DSU Plan was adopted to allow participants the opportunity to defer compensation and encourage a sense of ownership in Ten Peaks. Under the DSU Plan, participants may elect to defer compensation and receive DSUs equal to the value of the deferred compensation.

The first DSUs were issued in April 2012. The number of DSUs was determined by dividing the amount of deferred compensation by the Fair Market Value. The Fair Market Value of DSUs is defined in the DSU Plan as the weighted average closing price of Ten Peaks shares for the five business days immediately preceding the relevant date.

Upon the occurrence of the Redemption Event, the affected participant will be entitled to receive a lump sum cash payment, net of applicable withholding taxes, equal to the product of number of DSUs held by that participant and the Fair Market Value on the date of the Redemption Event. The DSUs do not contain any vesting conditions or forfeiture provisions, as they are issued in exchange for deferred compensation.

Under the DSU Plan, outstanding DSUs as at the record date are increased by the Dividend Rate whenever dividends are paid to shareholders.

The movement in DSUs for the years ended December 31, 2017 and December 31, 2016 is as follows:

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	Number of DSUs	Weighted average share price	Performance based
<b>Balance at January 1, 2016</b>	57,391	\$ 12.06	
DSUs issued	11,488	\$ 8.79	No
<b>Balance at December 31, 2016</b>	68,879	\$ 7.08	
<b>Balance at January 1, 2017</b>	68,879	\$ 7.08	
DSUs issued	11,276	\$ 6.63	No
DSUs exercised	(9,581)	\$ 6.24	No
<b>Balance at December 31, 2017</b>	<b>70,574</b>	<b>\$ 6.60</b>	

### 18. EMPLOYEE BENEFITS EXPENSES

Expenses recognized for employee benefits are detailed below:

	12 months ended December 31, 2017	12 months ended December 31, 2016
Short-term benefits	\$ 6,965	\$ 6,794
Long-term benefits	220	(180)
Post-employment benefits	680	607
	<b>\$ 7,865</b>	<b>\$ 7,221</b>

Short-term benefits are comprised of salaries, accrued bonuses, benefits and director fees. Long-term benefits comprise share-based compensation under the RSU Plan and the DSU Plan.

Post-employment benefits are contributions to employee retirement accounts, as well as statutory remittances related to post-employment benefits. These are recognized as an expense when employees have rendered service entitling them to the contributions.

### 19. RELATED PARTY TRANSACTIONS

The Company's related parties include its subsidiaries, key management personnel and a company related to a director.

Details of transactions between the Company and related parties (other than its subsidiaries) are discussed below. All intercompany transactions, balances, income and expenses are eliminated on consolidation.

#### Compensation of Key Management Personnel

The remuneration of directors and key management personnel during the year was as follows:

## TEN PEAKS COFFEE COMPANY INC.

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	12 months ended	
	December 31, 2017	December 31, 2016
Short-term benefits	\$ 1,395	\$ 1,132
Long-term benefits	173	(181)
Post-employment benefits	58	53
	\$ 1,626	\$ 1,004

#### Promissory note

On March 16, 2017, a subsidiary of the Company and a member of key management (the “borrower”) entered into a promissory note in the amount of US\$0.1 million. For as long as the borrower remains an employee, the obligation to repay the principal is forgiven against current and future awards under the RSU Plan, by forfeiture of awards. The loan is interest free other than in the event of default, in which case the promissory note shall bear simple interest at a rate of 10% per annum.

#### Trading transactions

During the year, the Company entered into the following transactions with a company that is related to a director:

	12 months ended	
	December 31, 2017	December 31, 2016
Sales	\$ 303	\$ 764
Purchases of raw materials	\$ 6,934	\$ 4,509

As at the balance sheet date, the Company had the following balances receivable from and payable to a company that is related to director:

	December 31, 2017		December 31, 2016	
Accounts receivable	\$	15	\$	121
Accounts payable	\$	-	\$	94

These transactions were in the normal course of operations and were measured at the fair value of the consideration received or receivable, which was established and agreed to by the related party.

## 20. DIVIDENDS

For the year ended December 31, 2017, the Company declared quarterly eligible dividends to shareholders totaling \$2.3 million or \$0.25 per share (2016: \$2.3 million or \$0.25 per share) of which, \$0.6 million was payable at December 31, 2017 (2016: \$0.6 million).

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements For the year ended December 31, 2017

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#### 21. SEGMENT REPORTING

The Company's sales are primarily generated in a single segment (decaffeination of green coffee) and in three geographic areas – Canada, United States and other international markets.

The Company's revenue from external customers and its non-current assets by location are detailed below. Revenues:

	December 31, 2017		December 31, 2016	
Canada	\$	35,103	\$	31,908
United States		38,808		37,173
Other		9,844		12,846
	\$	83,755	\$	81,927

Non-Current Assets (not including deferred tax assets):

	December 31, 2017		December 31, 2016	
Canada	\$	25,663	\$	17,951
United States		75		14
	\$	25,738	\$	17,965

#### 22. BASIC AND DILUTED EARNINGS PER SHARE

	12 months ended		12 months ended	
	December 31, 2017		December 31, 2016	
<b>Basic EPS:</b>				
Net income attributable to shareholders	\$	4,160	\$	4,149
Weighted average number of shares		9,038,862		9,019,621
<b>Basic EPS</b>		<b>0.46</b>	<b>\$</b>	<b>0.46</b>
<b>Diluted EPS:</b>				
Net income attributable to shareholders	\$	4,160	\$	4,149
Effect of diluted securities: RSUs		-		19
After tax effect of diluted securities if debenture converted:				
Interest on convertible debenture		1,035		-
Loss (gain) on fair value adjustment of embedded option		(604)		-
Net income after effect of diluted securities	\$	4,591	\$	4,168
Weighted average number of shares - basic		9,038,862		9,019,621
Effect of diluted securities: RSUs				83,932
Effect of diluted securities: convertible debenture		1,818,182		-
Weighted average number of shares - diluted		10,857,044		9,103,553
<b>Diluted EPS</b>	<b>\$</b>	<b>0.42</b>	<b>\$</b>	<b>0.46</b>

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

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The following potential common shares are anti-dilutive and are therefore excluded from the weighted average number of common shares outstanding for the purposes of calculating the diluted earnings per share:

	12 months ended December 31, 2017	12 months ended December 31, 2016
Weighted average number of RSUs granted	46,556	-
Share units from the conversion of the convertible debenture	-	407,352

### 23. FINANCIAL RISK MANAGEMENT

The Company's risk management program focuses on the unpredictability of commodity prices and foreign exchange rates, and seeks to minimize potential adverse effects on the Company's financial performance and cash flows. The Company uses derivative financial instruments to hedge these risk exposures. In addition, the Company monitors other financial risks on a regular basis.

Risk management is carried out under policies approved by the Board of Directors. The Company's exposure to and management of financial risks is discussed in more detail below.

#### 23.1 Commodity price risk

Commodity price risk is the risk that the fair value of inventory will fluctuate as a result of changes in commodity prices. The Company utilizes futures contracts to manage its commodity price exposure. The Company buys and sells futures contracts for coffee on the IntercontinentalExchange in order to offset its inventory position and fix the input cost of green coffee. As at December 31, 2017, the Company had futures contracts to buy 2.2 million lbs of green coffee with a notional value of US\$2.7 million, and contracts to sell 4.5 million lbs of green coffee with a notional value of US\$5.5 million. The furthest contract matures in in December 2018 (December 31, 2016: buy 2.0 million lbs, with a notional value of US\$2.7 million, and sell 6.4 million lbs with a notional value of US\$8.8 million). The net notional value of the contracts outstanding at December 31, 2017 was approximately US\$2.8 million (2016: US\$6.1 million).

The following tables provide a summary of commodity hedges designated as hedging instruments:

## TEN PEAKS COFFEE COMPANY INC.

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Carrying amount of hedging instruments	December 31, 2017		December 31, 2016	
Fair value hedge	Commodity price risk Coffee futures		Commodity price risk Coffee futures	
Nominal amount of hedging instruments (in US\$'000)	\$	2,804	\$	6,055
Line item in the statement of financial position where hedging instrument is located	Derivative Assets		Derivative Assets	
Assets	\$	247	\$	497
Liabilities		-		-
Changes in fair value used for calculating hedge ineffectiveness		-		-
Accumulated amount of fair value hedge adjustment on hedged item included in the carrying amount of the hedged items	December 31, 2017		December 31, 2016	
Fair value hedge	Purchase commitments and coffee inventory		Purchase commitments and coffee inventory	
Nominal amount of hedged item (in '000 lbs)		2,285		4,432
Line items in the statement of financial position where hedged item is located	Inventories & hedged firm commitments		Inventories & hedged firm commitments	
Assets	\$	28	\$	-
Liabilities		128		565
Changes in fair value used for calculating hedge ineffectiveness		-		-

As at December 31, 2017 the Company has entered into contracts to hedge purchase commitments, coffee inventory as well as sales agreements for net notional volumes of 2.3 million pounds of coffee (2016: 4.4 million).

### 23.2 Foreign currency risk

The Company realizes a significant portion of its sales in US\$, and purchases green coffee in US\$ which is, in some cases, sold to customers in Canadian dollars. The Company enters into forward foreign currency contracts to manage its exposure to currency rate fluctuations and to minimize the effect of exchange rate fluctuations on business decisions. These contracts relate to the Company's future cash flows in US\$ from sales. In addition, the Company enters into forward contracts to buy US\$ for coffee that it resells in Canadian dollars.

At December 31, 2017, the Company had forward currency contracts to buy US\$7.2 million and sell US\$46.2 million (2016: buy US\$9.5 million and sell US\$42.7 million) from January 2018 through to December 2021 at various Canadian exchange rates ranging from \$1.2147 to \$1.3837 from January 2018 through to December 2021. The net notional value of the contracts outstanding at December 31, 2017 was approximately US\$39.0 million (2016: US\$33.2 million).

The following provides a summary of amounts related to foreign currency forward contracts designated as hedging instruments.

#### Currency risk hedges on US\$ purchases

As at December 31, 2017 the Company has entered into forward contracts, where from the nominal value of US\$7.2 million (2016: US\$6.8 million), US\$7.0 million (2016: US\$6.8 million) were designated as hedging instruments.

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

<b>Carrying amount of hedging instruments</b>	<b>December 31, 2017</b>		<b>December 31, 2016</b>	
Fair value hedge		Foreign currency purchase forwards		Foreign currency purchase forwards
Nominal amount of hedging instruments (in US\$'000)	\$	6,962	\$	6,773
Line item in the statement of financial position where hedging instrument is located		Derivative liabilities		Derivative assets
Assets	\$	-	\$	128
Liabilities		229		1
Changes in fair value used for calculating hedge ineffectiveness		-		-
<hr/>				
<b>Accumulated amount of fair value hedge adjustment on hedged item included in the carrying amount of the hedged items</b>	<b>December 31, 2017</b>		<b>December 31, 2016</b>	
Fair value hedge		Firm purchase commitments & inventories		Firm purchase commitments & inventories
Nominal amount of hedged item (in US\$'000)	\$	6,962	\$	6,773
Line item in the statement of financial position where hedged item is located		Inventories & hedged firm commitments		Inventories & hedged firm commitments
Assets		380		-
Liabilities		-		23
Changes in fair value used for calculating hedge ineffectiveness		-		-

#### Currency risk on hedge on US\$ future revenue

The Company also entered into forward contracts, where from the nominal value of US\$46.2 million, US\$34.0 million (2016: US\$32.6 million) were designated to hedge future forecasted sales revenue.

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

Carrying amount of hedging instruments	December 31, 2017	December 31, 2016
Cashflow hedge	Currency risk Foreign currency forwards	Currency risk Foreign currency forwards
Nominal amount of hedging instruments (in US\$'000)	\$ 34,015	\$ 32,560
Line items in the statement of financial position where hedging instrument is located	Derivative assets and Derivative liabilities	Derivative assets and Derivative liabilities
Assets	1,292	59
Liabilities	13	1,144
Changes in fair value used for calculating hedge ineffectiveness	-	-
Accumulated amount of fair value hedge adjustment on hedged item included in the carrying amount of the hedged items	December 31, 2017	December 31, 2016
Cashflow hedge	Currency risk Foreign currency forwards	Currency risk Foreign currency forwards
Nominal amount of hedged item (in US\$'000)	34,015	32,560
Line items in the statement of financial position where hedged item is located	Accumulated other comprehensive income	Accumulated other comprehensive income
Assets	n/a	n/a
Liabilities	n/a	n/a
Changes in fair value used for calculating hedge ineffectiveness	-	-
Cashflow hedge reserve	1,969	567

Not included in tables above are fair value changes for swap contracts, as these are not designated hedge instruments.

### 23.3 Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market interest rates. The Company believes that interest rate risk is low as all cash equivalents and short-term investments are made in fixed rate instruments. The Company does have some interest rate risk related to its credit facilities; however, the obligations are small enough that any exposure is not material at this time. There is no interest rate risk on the convertible debenture as the interest rate is fixed.

### 23.4 Credit risk

The Company is exposed to credit risk with respect to its cash and cash equivalents, short-term investments, accounts receivable and derivative financial instruments.

The Company does not have significant credit risk related to cash and cash equivalents and short-term investments as amounts are held with major financial institutions.

The Company follows a program of credit evaluations of customers and limits the amount of credit extended when deemed necessary. For the year ended December 31, 2017, revenues from three major customers of \$29 million (2016: \$31 million) represented 35% (2016: 38%) of total



## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

#### For the year ended December 31, 2017

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revenues for the year. These customers represented 47% of total accounts receivable as at December 31, 2017 (2016: 34%).

The Company had 16% of its accounts receivable past due as at December 31, 2017 (December 31, 2016: 13%). Of the accounts receivable past due, 83% are 1-30 days past due (2016: 94%) and 17% are 31-60 days past due (2016: 6%).

The Company manages the credit risk related to its derivative financial instruments by entering into such contracts only with high credit quality institutions.

### 23.5 Liquidity risk

The Company has in place a planning and budgeting process to assist in determining the funds required to support the Company's normal operating requirements on an ongoing basis and its future plans. The Company ensures that there are sufficient committed financing facilities to meet its short-term business requirements, taking into account its anticipated cash flows from operations, its existing bank indebtedness and additional borrowing capacity. The Company has maintained compliance with its banking covenants and remains able to satisfy its liabilities as they become due. Non-derivative financial liabilities are as follows:

	Carrying Amount		Contractual Cash Flows							
	December 31, 2017		2018	2019 to 2020	2021 to 2022	Thereafter				
Accounts payable	\$	2,639	\$	2,639	\$	-	\$	-	\$	-
Other liabilities		636		591		45		-		-
Construction loan		844		28		113		113		590
Convertible debenture		11,658		-		-		-		15,000
Total	\$	15,777	\$	3,258	\$	158	\$	113	\$	15,590

### 23.6 Fair value of financial instruments

Financial instruments that are measured at fair value are categorized as follows:

# TEN PEAKS COFFEE COMPANY INC.

## Notes to the Consolidated Financial Statements For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

	December 31, 2017	Level 1	Level 2	Level 3
<b>Financial assets</b>				
Cash, cash equivalents and short-term investments	\$ 16,553	\$ 16,553	\$ -	-
Derivative assets	1,984	275	1,709	-
	\$ 18,537	\$ 16,828	\$ 1,709	-
<b>Financial liabilities</b>				
Derivative liabilities	\$ 2,951	\$ -	\$ 2,951	-
Other liabilities	636	-	636	-
	\$ 3,587	\$ -	\$ 3,587	-
<b>December 31, 2016</b>				
<b>Financial assets</b>				
Cash, cash equivalents and short-term investments	\$ 25,197	\$ 25,197	\$ -	-
Derivative assets	95	95	-	-
	\$ 25,292	\$ 25,292	\$ -	-
<b>Financial liabilities</b>				
Derivative liabilities	\$ 4,711	\$ -	\$ 4,711	-
	\$ 4,711	\$ -	\$ 4,711	-

During the year, there were no transfers between level 1 and 2 instruments.

## 24. COMMITMENTS AND CONSTRUCTION LOAN

### 24.1 Operating lease commitments

SWDCC leases a facility which houses its decaffeination plant and offices. SWDCC has exercised a renewal option such that the lease will expire in 2023. Beyond 2023, the landlord has to approve any subsequent renewal of the lease.

Seaforth leases a warehouse facility for its primary operations; the lease expires on June 30, 2019. In November of 2017 Seaforth entered into an agreement to sub-lease a warehouse facility for a two-year period to allow Seaforth's meet significant growth in demand for third-party coffee storage.

Swiss Water Decaffeinated Coffee Company USA, Inc. holds a lease for its Seattle, Washington, sales office, which expires on March 31, 2020.

A summary of future minimum payments under these operating leases as at December 31, 2017 is as follows:

Minimum lease payments due:	
No later than 1 year	\$ 1,691
Later than 1 year and no later than 5 years	1,412
Later than 5 years	-
	\$ 3,103

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements

For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

#### 24.2 Other lease commitments and Construction loan

On August 26, 2016, SWDCC signed a lease agreement for a build-to-suit production facility. The lease has an initial term of five years, and can be renewed at SWDCC's option in five-year increments up to a total of 30 years. The lease will commence the earlier of the date of opening of the SWDCC business in any part of the premises, and the date of expiry of the fixturing period, which is estimated to be May 2018. Under the lease, SWDCC has multiple options to buy-out the lease starting at the end of the second five-year term. The buy-out value will be equal to the fair market value of the property as determined by an appraisal process, subject to specified maximum and minimum values.

A summary of future minimum payments under this lease as at December 31, 2017 is as follows:

Minimum lease payments due:	
No later than 1 year	\$ 786
Later than 1 year and no later than 5 years	4,419
Later than 5 years	491
	\$ 5,696

#### Construction loan

The lease on the build-to-suit production facility also includes a construction management agreement for the construction of the highly specialized building to house the production plant. The landlord will finance a portion of the building, with loan payments commencing on the earlier of substantial completion of construction and January 1, 2019.

The loan is repayable in equal monthly installments over fifteen years, and can be repaid without penalty at any time. Interest is calculated monthly on the total expended cost, at an annual rate of RBC's prime commercial lending rate for commercial loans in Canada plus 1.5%, compounded semi-annually, up to the date of substantial completion of construction or up to December 31, 2018, whichever is earlier. Subsequently, the interest rate will be 8% per annum, compounded semi-annually. As at December 31, 2017 the Company accrued \$0.8 million for the construction loan related to work done to date plus two months of interest (2016: nil). That interest is accrued in construction in progress.

#### 24.3 Other commitments

The Company has provided a standby letter of credit in the amount of \$0.3 million as security to the landlord.

The Company has, in the normal course of business, entered into various contracts. As at December 31, 2017, these contracts related to the purchase of green coffee in the amount of \$33.0 million (2016: \$34.0 million), and natural gas purchase commitments in the amount of \$0.2 million (2016: \$0.3 million). \$32.9 million (2016: \$34.2 million) of these contracts will become

## TEN PEAKS COFFEE COMPANY INC.

### Notes to the Consolidated Financial Statements For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

payable within twelve months from December 31, 2017. As at December 31, 2017 the Company's capital commitments for the new facility's plant and equipment were \$16 million.

#### 25. SUPPLEMENTAL CASH FLOW INFORMATION

Cash and cash equivalents comprise cash on hand together with short-term investments. These investments consist of highly rated and liquid money market instruments with original maturities of three months or less.

	December 31, 2017		December 31, 2016	
Cash	\$	619	\$	6,490
Cash equivalents		7,685		6,007
	\$	9,486	\$	12,497

Changes in non-cash working capital.

	12 months ended December 31, 2017		12 months ended December 31, 2016	
Inventories	\$	(3,097)	\$	7,387
Accounts receivable		(420)		(4,506)
Other assets and liabilities		(238)		-
Accounts payable and accrued liabilities		927		276
Prepaid expenses and other receivables		(653)		(64)
Derivative assets at fair value through profit or loss		(180)		259
Derivative liabilities at fair value through profit or loss		-		5
	\$	(3,661)	\$	3,357

Construction loan was used to fund a \$0.8 million addition to Construction in progress. These are financing and investing transactions which did not require the use of the Company's cash or cash equivalents.

#### 26. RESTATEMENT OF CONSOLIDATED STATEMENT OF CASH FLOWS

Subsequent to the issuance of the previously filed consolidated financial statements, for the year ended December 31, 2016, (filed on SEDAR on March 15, 2017), management discovered an error relating to the amount of unrealized gain on derivative financial instruments presented within cash from operating activities before changes in non-cash working capital accounts. The correction of such error resulted in a decrease in unrealized loss (gain) on derivative financial instruments and the corresponding subtotal before change in non-cash working capital relating to operating activities of \$3.5 million, and a corresponding increase of \$3.5 million in change in non-cash working capital relating to operating activities. The following identifies the error that was corrected by management for the year ended December 31, 2016.

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### Notes to the Consolidated Financial Statements For the year ended December 31, 2017

(Tabular amounts in thousands of Canadian dollars)

<u>Line Item on Cash Flow Statement ('000s)</u>	<u>As Reported</u>	<u>Adjustment</u>	<u>Adjusted</u>
Net income for the year	\$ 4,149	\$	4,149
Items not affecting cash			
Depreciation and amortization	2,053		2,053
Unrealized loss (gain) on derivative financial instruments	1,761	(3,522)	(1,761)
Share-based compensation recovery	(180)		(180)
Payment of restricted share units settled in cash	(147)		(147)
Foreign exchange loss on cash held and on debt	2		2
Income taxes recognized in profit and loss	1,593		1,593
Finance expense recognized in profit and loss	4		4
	9,235	(3,522)	5,713
<u>Change in non-cash working capital relating to operating activities</u>	<u>(165)</u>	<u>3,522</u>	<u>3,357</u>
<b>Cash generated from operations</b>	<b>9,070</b>	<b>-</b>	<b>9,070</b>
Interest received	337	-	337
Interest paid	(251)	-	(251)
<b>Net cash generated from operating activities</b>	<b>\$ 9,156</b>	<b>-</b>	<b>\$ 9,156</b>

The restatement did not impact net cash generated from operating activities, or any other cash flows for the years presented. The restatement only affected the consolidated statement of cash flows. There was no change to the consolidated statements of financial position, income, comprehensive income or the changes in equity for the years presented, and there was no impact to basic and diluted earnings per share.

## 27. SUBSEQUENT EVENTS

These consolidated financial statements for the year ended December 31, 2017 were approved for issuance on March 19, 2018. There were no significant non-adjusting events that occurred between the reporting date and the date of authorization other than as noted below.

On January 15, 2018, the Company paid an eligible dividend in the amount of \$0.6 million (\$0.0625 per share) to shareholders of record on December 29, 2017.

On February 21, 2018 the Company issued 22,348 of shares pursuant to its Restricted Share Unit Plan.

On March 19, 2018, the Company declared an eligible dividend of \$0.0625 per share, to be paid on April 16, 2018 to shareholders of record on March 29, 2018.

