



RUSSELL BREWERIES INC.

**CONDENSED CONSOLIDATED INTERIM
FINANCIAL STATEMENTS**

**FOR THE THREE AND SIX MONTHS ENDED
DECEMBER 31, 2014 AND 2013**

UNAUDITED

NOTICE OF NO AUDITOR REVIEW OF CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated interim financial statements of the Company have been prepared by, and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of the financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of financial statements by an entity's auditor.

RUSSELL BREWERIES INC.**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION****(Unaudited; Expressed in Canadian Dollars)**

	December 31, 2014	June 30, 2014
ASSETS		
Current		
Cash and cash equivalents	\$ 499,021	\$ 662,056
Accounts receivable	692,437	833,078
Inventories (Note 4)	1,022,809	867,530
Prepaid expenses and deposits	134,196	200,710
	2,348,463	2,563,374
PROPERTY AND EQUIPMENT (Note 5)	2,579,590	2,573,345
INTANGIBLE ASSETS (Note 6)	1,935,268	1,935,268
RESTRICTED TERM DEPOSITS (Note 7)	100,000	100,000
LONG-TERM INVESTMENT (Note 9)	100,000	100,000
	\$ 7,063,321	\$ 7,271,987
LIABILITIES		
Current		
Bank indebtedness [Note 19(c)]	\$ 6,558	\$ 36,966
Accounts payable and accrued liabilities	864,082	810,713
Income taxes payable	171,000	171,000
Due to related parties (Note 17)	54,637	215,100
Current portion of long-term debt (Note 10)	229,948	286,417
Current portion of finance lease obligations (Note 11)	20,988	27,052
	1,347,213	1,547,248
LONG-TERM DEBT (Note 10)	454,129	565,653
FINANCE LEASE OBLIGATIONS (Note 11)	16,036	26,651
UNEARNED LICENSE FEES (Note 12)	43,750	56,250
DEFERRED TAX LIABILITIES	698,000	698,000
	2,559,128	2,893,802
SHAREHOLDERS' EQUITY		
SHARE CAPITAL	12,281,714	12,283,087
SHARE-BASED PAYMENTS RESERVES	3,649,327	3,570,648
DEFICIT	(11,426,848)	(11,475,550)
	4,504,193	4,378,185
	\$ 7,063,321	\$ 7,271,987

COMMITMENTS AND CONTINGENCIES (Note 19)

Approved and authorized for issuance on behalf of the Board of Directors on February 25, 2015:

/s/ Benjamin Li Yu

Benjamin Li Yu, Director

/s/ Peter H. Stafford

Peter H. Stafford, Director

RUSSELL BREWERIES INC.**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited; Expressed in Canadian Dollars)**

	Three Months Ended December 31, 2014	Three Months Ended December 31, 2013	Six Months Ended December 31, 2014	Six Months Ended December 31, 2013
REVENUES (Note 21)	\$ 2,552,058	\$ 2,537,387	\$ 5,027,064	\$ 5,014,674
LESS: EXCISE TAX AND PROVINCIAL MARK-UP	560,761	565,797	1,033,125	1,102,614
NET REVENUES	1,991,297	1,971,590	3,993,939	3,912,060
COST OF SALES (Note 4)	875,017	876,719	1,974,207	1,658,660
GROSS MARGIN	1,116,280	1,094,871	2,019,732	2,253,400
EXPENSES				
Depreciation	17,035	19,452	46,275	44,938
Selling, general and administrative	889,425	959,876	1,862,148	1,954,954
	906,460	979,328	1,908,423	1,999,892
EARNINGS BEFORE OTHER INCOME (EXPENSE)	209,820	115,543	111,309	253,508
OTHER INCOME (EXPENSE)				
Interest on long-term debt and convertible debt	(36,429)	(29,910)	(75,760)	(80,445)
Interest Income	—	—	—	54
Other income (Note 12)	6,334	6,250	13,153	12,500
	(30,095)	(23,660)	(62,607)	(67,891)
INCOME BEFORE INCOME TAXES	179,725	91,883	48,702	185,617
INCOME TAXES				
Deferred income tax expense	—	—	—	—
NET INCOME AND COMPREHENSIVE INCOME FOR THE PERIOD	179,725	91,883	48,702	185,617
EARNINGS PER SHARE (Note 15)				
Basic and diluted	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00

RUSSELL BREWERIES INC.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

(Unaudited; Expressed in Canadian Dollars)

	Share Capital		Share-based payments reserves	Deficit	Total Shareholders' Equity
	Number of Shares	Value			
Balance, June 30, 2014	87,083,788	\$ 12,283,087	\$ 3,570,648	\$ (11,475,550)	\$ 4,378,185
Comprehensive income for the period	—	—	—	48,702	48,702
Share issuance cost	—	(1,373)	—	—	(1,373)
Fair value of stock options granted	—	—	78,679	—	78,679
Balance, December 31, 2014	87,083,788	\$ 12,281,714	\$ 3,649,327	\$ (11,426,848)	\$ 4,504,193

	Share Capital		Share-based payments reserves	Deficit	Total Shareholders' Equity
	Number of Shares	Value			
Balance, June 1, 2013	78,350,455	\$ 11,783,304	\$ 3,398,726	\$ (11,537,270)	\$ 3,644,760
Comprehensive income for the period	—	—	—	185,617	185,617
Share issuance cost	—	(600)	—	—	(600)
Fair value of stock options granted	—	—	(1,193)	—	(1,193)
Balance, December 31, 2013	78,350,455	\$ 11,782,704	\$ 3,397,533	\$ (11,351,653)	\$ 3,828,584

RUSSELL BREWERIES INC.**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS****(Unaudited; Expressed in Canadian Dollars)**

	Six Months Ended December 31, 2014	Six Months Ended December 31, 2013
CASH FLOWS PROVIDED BY (USED IN):		
OPERATING ACTIVITIES		
Net income for the period	\$ 48,702	\$ 185,617
Adjusted for non-cash items:		
Depreciation	216,391	196,600
Accretion of long-term debt	20,895	3,348
Accrued interest on long-term debt	(24,727)	—
Accretion of bridge loan	—	6,793
Recognition of unearned license fee (Note 12)	(12,500)	(12,500)
Share-based compensation (Note 13(b))	78,679	(1,193)
	327,440	378,665
Net changes in non-cash working capital items:		
Accounts receivable	140,642	206,173
Prepaid expenses and deposits	66,514	2,791
Inventories	(155,279)	53,359
Due to and from related parties	(24,000)	14,700
Accounts payable and accrued liabilities	53,369	(317,813)
	408,686	337,875
INVESTING ACTIVITIES		
Purchases of property and equipment	(222,637)	(11,227)
	(222,637)	(11,227)
FINANCING ACTIVITIES		
Share issuance cost	(1,373)	(600)
Proceeds from (Repayment of) bridge loan	(100,000)	100,000
Repayment of bank indebtedness	(30,408)	(36,671)
Repayment of long-term debt	(200,623)	(339,123)
Repayment of finance lease obligations	(16,679)	(18,783)
	(349,083)	(295,177)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(163,034)	31,471
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	662,055	213,452
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 499,021	\$ 244,923
CASH AND CASH EQUIVALENTS CONSIST OF:		
Demand deposits	\$ 499,021	\$ 244,923

SUPPLEMENTAL CASH FLOW INFORMATION (Note 16)

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS****FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**

(Unaudited; Expressed in Canadian Dollars)

1. NATURE OF OPERATIONS

Russell Breweries Inc. (the "Company") was incorporated under the laws of the Province of British Columbia, Canada on March 23, 2000. The head office and principal address of the Company are located at #202 - 13018 80th Avenue, Surrey, British Columbia, V3W 3A8. The Company produces beer primarily for sale to provincial liquor distribution organizations and entities engaged in the food and beverage industries within Canada. The Company's shares are traded on the TSX Venture Exchange (the "TSX.V").

These consolidated financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assumes the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. As at December 31, 2014, the Company had a positive working capital of \$1,001,250 and accumulated losses since inception of \$11,426,848. The continued operation of the Company is dependent on its ability to obtain financing sufficient to generate profitable operations in the future. There is no guarantee that the Company will be able to raise this additional financing.

2. STATEMENT OF COMPLIANCE AND BASIS OF PRESENTATION**a) Statement of Compliance**

These unaudited condensed interim financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting as issued by the International Accounting Standards Board ("IASB"). The unaudited condensed interim financial statements do not include all of the information required for full annual financial statements. These interim consolidated financial statements should be read in conjunction with the Company's June 30, 2014 annual audited consolidated financial statements.

The condensed consolidated interim financial statements were authorized for issuance by the Board of Directors on February 25, 2015.

b) Basis of Presentation, Functional Currency and Basis of Consolidation

These unaudited condensed interim financial statements include the accounts of Russell Breweries Inc. and its wholly owned subsidiaries Russell Brewing Company Ltd. ("Russell"), Fort Garry Brewing Company Ltd. ("Fort Garry") and Russell USA LLC. The following companies have been consolidated with Russell Breweries Inc. as at December 31, 2014:

Company Name	Registered	Holding	Functional Currency
Russell Breweries Inc.	British Columbia	Parent Company	Canadian Dollar
Russell Brewing Company Ltd.	British Columbia	100%	Canadian Dollar
Fort Garry Brewing Company Ltd.	Manitoba	100%	Canadian Dollar
Russell USA LLC	United States	100%	United States Dollar

Inter-company balances and transactions, and any unrealized gains arising from inter-company transactions, are eliminated in preparing the condensed consolidated interim financial statements.

c) Basis of Measurement

The Financial Statements have been prepared on the historical cost basis, presented in Canadian dollars, except where otherwise indicated.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**

(Unaudited; Expressed in Canadian Dollars)

2. STATEMENT OF COMPLIANCE AND BASIS OF PRESENTATION (continued)**d) Significant Accounting Estimates and Judgments**

The preparation of these condensed financial statements requires management to make judgments in applying accounting policies. Judgments that have the most significant effect on the amounts recognized in the financial statements may include recovery of accounts receivable, inventory valuation, the estimated useful life of long-lived assets, assessment of long-term investment, estimates used in impairment assessments of long-lived assets, valuation of deferred income tax assets and liabilities and estimates used in calculating share-based compensation. Management also makes assumptions and critical estimates. Critical estimates are those which are most subject to uncertainty and have the most significant risk of resulting in a material change to the carrying amounts of assets and liabilities within the next year. Judgments, assumptions and estimates are based on historical experience, business trends and all available information that management considers relevant at the time of the preparation of the financial statements. However, future events and their effects cannot be anticipated with certainty and so as confirming events occur, actual results could ultimately differ from assumptions and estimates. Such differences could be material.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies that have been used in the preparation of these condensed interim financial statements are summarized in the audited consolidated financial statements of the Company for the year ended June 30, 2014. These statements should be read in conjunction with the audited consolidated financial statements for the year ended June 30, 2014.

4. INVENTORIES AND COST OF SALES

	December 31, 2014	June 30, 2014
Finished goods	\$ 183,470	\$ 118,273
Work-in-progress	295,315	259,503
Raw materials	544,024	489,754
	\$ 1,022,809	\$ 867,530

The cost of sales of the Company is broken down into its cash and non-cash components as follows:

	Three Months Ended December 31, 2014	Three Months Ended December 31, 2013	Six Months Ended December 31, 2014	Six Months Ended December 31, 2013
Inventories	\$ 799,920	\$ 800,801	\$ 1,804,091	\$ 1,506,998
Depreciation	75,097	75,918	170,116	151,662
	\$ 875,017	\$ 876,719	\$ 1,974,207	\$ 1,658,660

RUSSELL BREWERIES INC.
NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013

(Unaudited; Expressed in Canadian Dollars)

5. PROPERTY AND EQUIPMENT

	Computer		Equipment		Leasehold improvements		Office furniture and fixtures		Vehicles		Returnable containers		Total
Cost													
Balance as at June 30, 2013	\$	69,285	\$	5,961,703	\$	1,309,557	\$	63,844	\$	562,414	\$	895,639	\$ 8,862,442
Additions		8,116		72,189		33,419		—		(9,685)		12,123	116,162
Balance as at June 30, 2014	\$	77,401	\$	6,033,892	\$	1,342,976	\$	63,844	\$	552,729	\$	907,762	\$ 8,978,604
Additions		—		20,829		147,215		—		—		54,593	222,637
Balance as at December 31, 2014	\$	77,401	\$	6,054,721	\$	1,490,191	\$	63,844	\$	552,729	\$	962,355	\$ 9,201,241
Accumulated Depreciation													
Balance as at June 30, 2013	\$	69,285	\$	3,380,730	\$	1,307,871	\$	63,844	\$	402,325	\$	788,537	\$ 6,012,592
Depreciation		419		260,640		1,965		—		56,660		72,983	392,667
Balance as at June 30, 2014	\$	69,704	\$	3,641,370	\$	1,309,836	\$	63,844	\$	458,985	\$	861,520	\$ 6,405,259
Depreciation		1,015		140,242		7,361		—		26,977		40,797	216,392
Balance as at December 31, 2014	\$	70,719	\$	3,781,612	\$	1,317,197	\$	63,844	\$	485,962	\$	902,317	\$ 6,621,651
Carrying amounts													
June 30, 2013	\$	—	\$	2,580,973	\$	1,686	\$	—	\$	160,089	\$	107,102	\$ 2,849,850
June 30, 2014	\$	7,697	\$	2,392,522	\$	33,140	\$	—	\$	93,744	\$	46,242	\$ 2,573,345
December 31, 2014	\$	6,682	\$	2,273,109	\$	172,994	\$	—	\$	66,767	\$	60,038	\$ 2,579,590

Equipment includes assets under finance leases with a cost of \$439,719 (June 30, 2014 – \$439,719) and accumulated depreciation of \$108,837 (June 30, 2014 – \$99,159). Vehicles includes assets under finance leases with a cost of \$537,508 (June 30, 2014 – \$537,509) and accumulated depreciation of \$443,748 (June 30, 2013 – \$416,873).

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS****FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**(Unaudited; Expressed in Canadian Dollars)

6. INTANGIBLE ASSETS

	Brands and Trademarks	Website	Total
Cost			
Balance as at June 30, 2013	\$ 1,935,268	\$ 5,975	\$ 1,941,243
Balance as at June 30, 2014	\$ 1,935,268	\$ 5,975	\$ 1,941,243
Balance as at December 31, 2014	\$ 1,935,268	\$ 5,975	\$ 1,941,243
Accumulated Depreciation			
Balance as at June 30, 2013	\$ –	\$ 5,975	\$ 5,975
Balance as at June 30, 2014	\$ –	\$ 5,975	\$ 5,975
Balance as at December 31, 2014	\$ –	\$ 5,975	\$ 5,975
Carrying amounts			
June 30, 2013	\$ 1,935,268	\$ –	\$ 1,935,268
June 30, 2014	\$ 1,935,268	\$ –	\$ 1,935,268
December 31, 2014	\$ 1,935,268	\$ –	\$ 1,935,268

7. RESTRICTED TERM DEPOSITS

A term deposit of \$100,000 has been pledged as security for a \$100,000 bank line of credit (June 30, 2014 – \$100,000).

8. BRIDGE LOAN DUE TO RELATED PARTIES

On September 5, 2014, pursuant to the bridge loan agreement entered into on September 3, 2013, the Company repaid in full, the principal of \$100,000 and interest of \$9,203.

9. LONG-TERM INVESTMENT

On October 9, 2012, the Company completed a non-exclusive technology and trade mark license agreement (“License Agreement”) with Russell Breweries (China) Inc. (the “Licensee”). Pursuant to the License Agreement, the Company received 20% of the common shares of the Licensee (“Licensee Common Shares”) with an estimated fair value of \$100,000.

The Company has used the cost method to account for its investment due to the fact that the Company has no significant influence over the Licensee’s management of operations (see Note 12). As of December 31, 2014, the Company’s interest in the Licensee has decreased to 7.69%.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**

(Unaudited; Expressed in Canadian Dollars)

10. LONG-TERM DEBT

	December 31, 2014	June 30, 2014
Term bank loan, bearing interest at a floating base rate plus a variance of 1%, repayable in monthly installments of \$9,750 plus interest prior to October 2010 and thereafter repayable in monthly installments of \$9,750 plus interest maturing November 15, 2014, secured by the assets of Fort Garry (a)	\$ —	\$ 48,750
Term bank loan, bearing interest at floating base rate plus a variance of 1%, repayable in monthly installments of \$1,750 plus interest maturing August 15, 2015, secured by the assets of Fort Garry (b)	13,282	22,896
Term loan, bearing interest at 10% per annum calculated semi-annually, repayable in monthly installments of \$17,500 plus interest maturing on July 31, 2016, secured by the assets of Russell and Fort Garry (c)	340,375	444,121
Term loan due to related parties, bearing interest at 9% per annum calculated semi-annually, secured by a guarantee by a director of the Company, due December 31, 2015 (d)	330,420	336,303
	684,077	852,070
Less: current portion of long-term debt	(229,948)	(286,417)
Long-term portion of long-term debt	\$ 454,129	\$ 565,653

- (a) On December 8, 2008, the bank made an amendment to the existing term loan in accordance with the request of the Company for a six month principal postponement. Pursuant to the amendment, the remaining loan amount on December 8, 2008 of \$787,500 was to be repaid by 42 consecutive monthly principal installments of \$18,750 each commencing June 15, 2009 and ended November 15, 2012. The bank also granted a reduction of the interest rate on the term loan by 1%. With the exception of the amendments agreed, all terms and conditions of the term loan remain unchanged. On September 22, 2010, the bank made a further amendment to the existing term loan in accordance with the request of the Company. Pursuant to the amendment, the remaining loan amount is to be repaid by 50 consecutive monthly principal installments of \$9,750 each commencing October 15, 2010 and ended November 15, 2014.
- (b) On October 5, 2010, the Company's subsidiary Fort Garry Brewing Company Ltd. accepted an offer of a \$100,000 pre-authorized working capital loan from Business Development Bank of Canada ("BDC"). The BDC Loan, bearing interest at floating base rate plus a variance of 1% maturing August 15, 2015, is secured by the assets of Fort Garry and supported by a guarantee made by two directors of the Company. In return for the guarantee, the Company issued 250,000 common shares of the Company as bonus shares with an estimated fair value of \$0.08 per share for a total value of \$20,000, which was recorded as a financing cost against the value allocated to the loan. During the period ended December 31, 2014, the Company recorded interest expense of \$884 (2013 - \$1,728) related to the accretion of the discounted value of the loan, which has been recorded as interest on long-term debt in the statement of operations.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**

(Unaudited; Expressed in Canadian Dollars)

10. LONG-TERM DEBT (continued)

- (c) On December 31, 2007, the Company entered into a loan agreement pursuant to which the lender, a shareholder of the Company, provided a discounted loan to the Company valued at \$1,239,000 at maturity. Under the agreement, a notional principal amount of \$965,000 was assigned to the loan. In connection with the loan, the lender was entitled to a \$25,000 bonus which was deducted from the notional principal amount of \$965,000, resulting in net proceeds to the Company of \$940,000. The Company also issued 250,000 warrants to the lender, each warrant entitling the lender to purchase one common share of the Company at a price of \$0.65 per share for a period of two years expiring on December 31, 2009.

Net proceeds of \$896,040 and \$43,960 were allocated to the loan and warrants, respectively, based on their relative fair values on December 31, 2007. The Company incurred cash debt issue costs of \$14,435 which were recorded as a discount against the value allocated to the loan. The fair values of the warrants issued in connection with the loan were computed using the Black-Scholes option-pricing model.

On December 31, 2010, the Company entered into an amendment and loan extension agreement to the loan agreement dated December 31, 2007, pursuant to which the lender extended the maturity date to July 31, 2012 and reduced the loan amount to \$738,600 from \$1,239,000, provided that the Company repay the loan in the amount of \$619,000 on January 1, 2011 (paid). Pursuant to the amended loan agreement, the lender provides to the Company a new loan valued at maturity in the amount of \$738,600. A discounted value or loan advance amount of \$620,000 is calculated based on a 10% per annum interest rate, calculated semi-annually, with interest payable on maturity resulting in a total loan value at maturity of \$738,600. In consideration of the lender agreeing to amend and extend the loan, the lender will also earn a bonus of \$22,500 to be included in the loan amount. The term of the loan is nineteen months. The Company may repay the loan at any time without penalty by paying the discounted loan advance amount of \$620,000 together with accumulated interest.

On July 11, 2012, the Company agreed to a one-year extension and amendment to the loan agreement dated December 31, 2007. The extension is for one year, maturing on July 31, 2013 and bears interest at 10% per annum, calculated semi-annually. In consideration of the lender's agreement to amend and extend the loan, the lender will earn a bonus of \$24,374. The Company may repay the loan at any time without penalty by paying the outstanding loan amount together with accumulated interest and prorated bonus. The extension is guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd., both wholly-owned subsidiaries of the Company. As security for the loan, the Company will grant to the lender a subordinated security agreement creating a security interest and charge over all of their respective property and assets subordinate to senior debt and senior security of up to \$2.5 million plus finance lease obligations incurred for future acquisitions of equipment and other capital assets. On July 31, 2013, the Company repaid \$206,834 of the loan. The discounted value of the loan as at December 31, 2014 was \$340,375 (2013 - \$444,121).

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**

(Unaudited; Expressed in Canadian Dollars)

10. LONG-TERM DEBT (continued)

- (d) On July 26, 2013, the Company negotiated to further amend and extend repayment of the balance of \$630,000 of the loan in Note 10(c). In consideration of the lender agreeing to amend and extend the loan, the lender will also earn a bonus of \$20,000 to be included in the loan amount. The loan amount of \$650,000 was amended and extended as follows: a 10% per annum interest rate, calculated semi-annually, repayable in monthly installments of \$17,500 plus bonus and interest, subject to a penalty of \$17,500 for each missed monthly installment payment, and maturing July 31, 2016. The loan is guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd., both wholly-owned subsidiaries of the Company. As further security for the loan, the Company and its Canadian subsidiaries will grant to the lender a subordinated security agreement creating a security interest and charge over all of their respective property and assets subordinate to senior debt and senior security of up to \$2.5 million plus finance lease obligations incurred for future acquisitions of equipment and other capital assets. The Company may repay the loan at any time without penalty by paying the discounted loan amount outstanding together with accrued interest and prorated bonus.

During the period ended December 31, 2014, the Company recorded interest expense of \$4,588 (2013 - \$8,608) related to the accretion of the discounted value of the loan, which has been recorded as interest on long-term debt in the consolidated statement of comprehensive income.

- (e) On January 20, 2014, the Company entered into a loan agreement with Weichun Ye, Yan Zeng and Dongbing (Derrick) Ma, (the "Guarantor") for an aggregate principal amount of \$500,000 bearing interest at a rate of 9% per annum calculated and compounded semi-annually. The principal amount of the loan is due and payable on the earlier of December 31, 2015 and the occurrence of an event of default as defined in the loan agreement. The Company's obligations under the loan agreement are guaranteed by the Guarantor and, in consideration for acting as guarantor, the Company has granted to the Guarantor 4,000,000 non-transferable warrants, each warrant entitling the Guarantor to purchase one common share of the Company at an exercise price of \$0.05 per share until December 31, 2015 (Note 13(c)). The Company has granted to the lenders of this loan security interest in all present and future undertakings and property of the Company as described in the security agreement.

Excluding finance fees and discounting, the Company's future estimated principal repayments of long-term debt are as follows:

Fiscal Year	Amount	
2015	\$	115,500
2016		713,500
2017		17,500
	\$	846,500

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS****FOR THE SIX MONTHS ENDED DECEMBER 31, 2014 AND 2013**

(Unaudited; Expressed in Canadian Dollars)

11. FINANCE LEASE OBLIGATIONS

The Company finances certain property and equipment using finance leases which bear interest at rates ranging from 6.63% to 20.58% and expire on various dates through June 2016. Estimated future minimum lease payments under these finance leases are as follows:

Fiscal Year:		Amount
2015	\$	14,381
2016		27,483
Total minimum lease payments		41,864
Less: amount representing interest		(4,840)
Net minimum lease payments		37,024
Less: current portion of finance lease obligations		(20,988)
Long-term portion of finance lease obligations	\$	16,036

12. UNEARNED LICENSE FEES

On October 2, 2012, the Company completed a non-exclusive technology and trade mark license agreement ("License Agreement") with Russell Breweries (China) Inc. (the "Licensee") to allow the Licensee to import, produce, package, use, market, sell and distribute Russell brands in China, including Hong Kong and Taiwan.

Pursuant to the License Agreement, the Company received an initial licensing fee of \$100,000. In addition, the Company will be entitled to ongoing royalties of \$23 per hectolitre of beer produced and sold by the Licensee. The term of the agreement is for four years and expires on October 1, 2016.

During the period ended December 31, 2014, the Company has recognized \$653 (2013 - \$nil) in royalties and \$12,500 (2013 - \$12,500) in license fees earned under the agreement, which has been recorded as other income in the statement of operations. As at December 31, 2014, the unearned license fee is \$43,750.

13. SHARE CAPITAL**(a) Authorized Share Capital**

The Company's authorized share capital consists of an unlimited number of common shares without par value.

(b) Stock Options

Under the Company's stock option plan (the "Plan"), the Company's board of directors is authorized to grant stock options to directors, officers, consultants and employees of the Company not to exceed 10% of the issued and outstanding common shares of the Company from time to time. Stock options granted under the Plan are exercisable over a period not exceeding five years from the date granted. Exercise prices may not be less than the market price of the common shares on the date of grant less applicable discounts permitted by the TSX Venture Exchange. Vesting terms are determined by the board of directors on the date of grant.

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13. SHARE CAPITAL (continued)**(b) Stock Options (continued)**

During the period ended December 31, 2014, the Company granted 4,550,000 and vested 1,187,465 (2013 – granted nil and vested 113,889) net of forfeited incentive stock options to key employees and directors exercisable at \$0.07 per share expiring after five years of the grant date, pursuant to its stock option plan. The fair value of each option granted was \$0.07 calculated using the Black-Scholes option-pricing model at the date of grant using the following assumptions: expected option life for 3.48 years; forfeiture rate of 0%~12.9%; risk-free interest rate of 1.47%; expected dividend yield of 0% and expected stock price volatility of 205%. During the period ended December 31, 2014, the Company recorded a total amount of \$78,679 (2013 – recovery of \$1,193) compensation cost included in selling, general and administrative expense relating to these options.

Stock option activity during the period ended December 31, 2014 and the year ended June 30, 2014 is presented below:

	December 31, 2014		June 30, 2014	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of period	50,000	\$ 0.10	1,300,000	\$ 0.10
Granted	4,550,000	0.07	—	—
Forfeited	—	—	(1,250,000)	0.10
Outstanding, end of period	4,600,000	\$ 0.07	50,000	\$ 0.10

At December 31, 2014, the following stock options are outstanding:

Options Outstanding			Options Exercisable		
Exercise Price \$	Number of Shares	Weighted Average Remaining Life (in years)	Exercise Price \$	Number of Shares	Weighted Average Exercise Price \$
0.10	50,000	2.25	0.10	50,000	0.10
0.07	4,550,000	4.52	0.07	1,137,465	0.07
	4,600,000	4.50	0.07	1,187,465	0.07

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13. SHARE CAPITAL (continued)**(c) Warrants**

Warrant activity during the period ended December 31, 2014 and the year ended June 30, 2014 is presented below:

	December 31, 2014		June 30, 2014	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of period	13,640,000	\$ 0.09	9,640,000	\$ 0.10
Granted	—	—	4,000,000	0.05
Outstanding, end of period	13,640,000	\$ 0.09	13,640,000	\$ 0.09

At December 31, 2014, the following warrants were outstanding entitling the holders the right to purchase one common share for each warrant held:

Number of Warrants	Weighted Average Exercise Price	Expiry Date
9,640,000	\$ 0.10	May 17, 2015
4,000,000	0.05	December 31, 2015
13,640,000	\$ 0.09	

14. INCOME TAXES

The Company has non-capital losses of approximately \$11,654,000 which may be carried forward to apply against future years income tax for Canadian income tax purposes, subject to final determination by taxation authorities, and expiring as follows:

Fiscal Year of Expiry	Amount
2014	\$ 74,000
2015	283,000
2026	257,000
2027	750,000
2028	1,696,000
2029	2,213,000
2030	1,831,000
2031	1,937,000
2032	1,150,000
2033	722,000
2034	741,000
	\$ 11,654,000

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15. EARNINGS PER SHARE

The computation of net earnings per share attributable to common shareholders is as follows:

	Six Months Ended December 31, 2014	Six Months Ended December 31, 2013
Net earnings and comprehensive earnings	\$ 48,702	\$ 185,617
Net earnings attributable to common shareholders	\$ 48,702	\$ 185,617

The weighted average number of shares outstanding used in the computation of earnings per share for the period ended December 31, 2014 was 87,083,788 (June 30, 2014 – 79,639,085). Outstanding stock options, warrants, and agent unit options have not been considered in the computation of diluted earnings per share as the result is anti-dilutive.

16. SUPPLEMENTAL CASH FLOW INFORMATION

	Six Months Ended December 31, 2014	Six Months Ended December 31, 2013
Cash paid for:		
Interest	\$ 26,752	\$ 70,304
Non-cash investing and financing activities:		
Common shares issued for bridge loan	\$ –	\$ 6,793

17. RELATED PARTY TRANSACTIONS AND BALANCES

The Company has identified its directors and certain senior officers as its key management personnel and the compensation costs for key management personnel and companies related to them were recorded at their exchange amounts as agreed upon by transacting parties as follows:

	Six Months Ended December 31, 2014	Six Months Ended December 31, 2013
Short-term benefits:		
Salaries, management & consulting fees [Notes 17(a)]	\$ 369,832	\$ 223,893
Directors fees [Note 17(b)]	18,000	17,484
Share-based payments [Note 13(b)]	40,637	–
Total short-term benefits:	\$ 428,469	\$ 241,377

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17. RELATED PARTY TRANSACTIONS AND BALANCES (continued)

- (a) During the period ended December 31, 2014, the Company incurred management fees and salaries totaling \$369,832 to a company controlled by the CEO and other key management personnel (2013 – \$223,893). As at December 31, 2014, the Company owed \$10,384 to the CEO and a company controlled by the CEO (2013 – \$26,250), which is non-interest bearing, unsecured and due on demand.
- (b) During the period ended December 31, 2014, the Company granted 4,550,000 (2013 - nil) stock options to directors and officers and key employees and incurred director fees of \$18,000 to the directors of the Company (2013 – \$17,484). As at December 31, 2014, the Company owed \$nil to the independent directors (2013 – \$32,119), which is non-interest bearing, unsecured and due on demand.
- (c) During the period ended December 31, 2014, the Company repaid in full, the principal of \$100,000 and interest totaling \$9,203 to spouses of certain directors pursuant to a bridge loan agreement entered on September 3, 2013.

These transactions were in the normal course of operations and have been recorded at their exchange amounts, which is the consideration agreed upon by the related parties.

18. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS**(a) Fair Values of Financial Instruments**

The carrying values of cash and cash equivalents, accounts receivable, restricted term deposits, bank indebtedness, accounts payable, and due to related parties are reasonable estimates of fair values due to the relatively short periods to maturity and the commercial terms of these instruments. The carrying values of long-term debt and finance lease obligations at December 31, 2014 are considered to be reasonable estimates of fair value based on current market rates for similar financial instruments.

(b) Fair Value Measurements

Certain of the Company's financial assets and liabilities are measured at fair value on a recurring basis and classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Certain non-financial assets and liabilities may also be measured at fair value on a non-recurring basis. There are three levels of the fair value hierarchy that prioritize the inputs to valuation techniques used to measure fair value, with Level 1 inputs having the highest priority. The levels and the valuation techniques used to value the Company's financial assets and liabilities are described below:

Level 1 - Quoted Prices in Active Markets for Identical Assets

Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2 - Significant Other Observable Inputs

Quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Derivative instruments are included in Level 2 of the fair value hierarchy as they are valued using pricing models or discounted cash flow models. These models require a variety of inputs, including, but not limited to, contractual terms, market prices, forward price curves, yield curves, and credit spreads. These inputs are obtained from or corroborated with the market where possible.

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18. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)**(b) Fair Value Measurements (continued)**

Level 3 - Significant Unobservable Inputs

Unobservable (supported by little or no market activity) inputs.

Financial assets and liabilities measured at fair value on a recurring basis were presented on the Company's December 31, 2014 consolidated interim statement of financial position as follows:

Fair Value Measurements Using				
	Quoted Prices in Active Markets For Identical Instruments (Level 1) \$	Significant Other Observable Inputs (Level 2) \$	Significant Unobservable Inputs (Level 3) \$	Balance as of December 31, 2014 \$
Assets:				
Cash and cash equivalents	499,021	—	—	499,021
Restricted term deposits	100,000	—	—	100,000

(c) Financial Risks**(i) Credit Risk**

Credit risk arises from the non-performance by counterparties of contractual financial obligations. The Company maintains substantially all of its cash and cash equivalents and restricted term deposits with major financial institutions. Deposits held with these institutions may exceed the amount of insurance provided on such deposits. As at December 31, 2014, the Company has significant accounts receivable from one major customer totaling \$340,778 (June 30, 2014 - \$335,502). The Company manages credit risk for trade and other receivables through established credit monitoring activities. As at December 31, 2014, the Company's maximum exposure to credit risk is the carrying value of cash and cash equivalents, accounts receivable and restricted term deposits.

The Company's concentration of, and past due, accounts receivable are summarized as follows:

	December 31, 2014		June 30, 2014	
	Over 90 days	Total	Over 90 days	Total
Provincial Liquor Boards	\$ —	\$ 653,181	\$ —	\$ 741,080
Other Receivables	3,918	39,255	—	91,198
Total	\$ 3,918	\$ 692,436	\$ —	\$ 833,078

The Company has a concentration of credit risk because a majority of its accounts receivable are from provincial liquor boards, under provincially regulated industry sale and payment terms. The Company is not exposed to significant credit risk as receivables are with government agencies. While substantially all of the Company's accounts receivable are from provincial government liquor authorities, the timing of receipts of large balances may vary significantly from period to period.

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18. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)**(c) Financial Risks (continued)****(ii) Liquidity Risk**

Liquidity risk arises from the Company's general and capital financing needs. The Company continuously monitors and reviews both actual and forecasted cash flows, and also matches the maturity profile of financial assets and liabilities, when feasible.

Contractual undiscounted cash flow requirements for financial liabilities as at December 31, 2014 are as follows:

	Less Than 1 Year \$	Years 2 and 3 \$	Years 4 and 5 \$	More Than 5 Years \$	Total \$
Accounts payable and accrued liabilities	864,082	—	—	—	864,082
Long-term debt (Note 10)	115,500	731,000	—	—	846,500
Finance lease obligations (Note 11)	20,988	16,036	—	—	37,024
	1,000,570	747,036	—	—	1,747,606

As at December 31, 2014, the Company had a positive working capital of \$1,001,250.

(iii) Interest Rate Price Risk

Certain of the Company's long-term debt instruments and finance lease obligations are subject to interest rate price risk as they carry fixed rates of interest.

Certain of the Company's long-term debt instruments and bank indebtedness are subject to interest rate cash flow risk as they carry variable rates of interest. A plus or minus 1% change in market interest rates would not have a significant effect on the Company's income (loss) and comprehensive income (loss) for the year.

19. COMMITMENTS AND CONTINGENCIES

- (a) The Company's future minimum operating lease payments for premises, vehicles and office equipment for the next five years are as follows:

Fiscal Year	Amount
2015	\$ 265,416
2016	439,326
2017	331,478
2018	331,478
2019	331,316
	\$ 1,699,014

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19. COMMITMENTS AND CONTINGENCIES (continued)

- (b) At December 31, 2014, the Company had issued a general excise bond of \$55,000 in favour of the Minister of National Revenue of Canada.
- (c) The Company has a bank operating line of credit with a limit of \$100,000 which bears interest at prime plus 1%, matures on October 31, 2015 and is extended automatically on a quarterly basis, and is secured by a term deposit of \$100,000 (see Note 7).

20. CAPITAL MANAGEMENT

The Company manages its capital structure in order to ensure sufficient resources are available to meet operational requirements. The Company is required to maintain term deposits of \$100,000 (June 30, 2014 - \$100,000) related to its bank line of credit (see Note 7). There are no other externally imposed capital requirements.

The Company seeks to manage capital to provide adequate funding for its operations while minimizing dilution for its existing shareholders. The Company's principal source of funds is from the issuance of common shares and warrants.

Management considers its long-term debt, finance lease obligations and shareholders' equity as capital, which consists of the following:

	December 31, 2014	June 30, 2014
Long-term debt (Note 10)	\$ 684,077	\$ 852,070
Finance lease obligations (Note 11)	37,024	53,703
Shareholders' equity	4,504,193	4,378,185
	\$ 5,225,294	\$ 5,283,958

21. MAJOR CUSTOMER

During the period ended December 31, 2014, the Company had sales of \$2,624,445 (2013 - \$2,479,143) to the Manitoba Liquor Control Commission which accounted for 52% of its gross revenues (2013 - 49%).

22. CONTINGENT LIABILITIES

- (a) A claim was made against the Company from a company controlled by a former director of the Company in relation to legal services provided over the last two years and services provided pursuant to the purported Legal Services Agreement dated April 1, 2013 in the amount of \$62,961. In addition, a severance claim has been made amounting to six months' payments under the purported Legal Services Agreement. The Company believes it has a good defense to the claim and no amount has been accrued for settlement.
- (b) A claim was made against the Company by the former CEO and director of the Company in relation to company expenses incurred from September 2012 in the amount of \$16,652 including interest.