



RUSSELL BREWERIES INC.

**CONDENSED CONSOLIDATED INTERIM
FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED
SEPTEMBER 30, 2016 AND 2015**

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)**

	September 30, 2016	June 30, 2016
ASSETS		
Current		
Cash and cash equivalents	\$ 720,976	\$ 349,575
Accounts receivable (Note 14(c) (i))	621,680	775,094
Inventories (Note 4)	1,117,493	1,140,360
Prepaid expenses and deposits	79,921	49,183
	2,540,070	2,314,212
PROPERTY AND EQUIPMENT (Note 5)	2,431,263	2,501,480
INTANGIBLE ASSETS (Note 6)	1,957,902	1,955,626
RESTRICTED TERM DEPOSITS (Note 7)	107,006	107,006
DEPOSITS	94,169	94,169
DEFERRED TAX ASSETS	1,045,000	1,045,000
	\$ 8,175,410	\$ 8,017,493
LIABILITIES		
Current		
Accounts payable and accrued liabilities (Note 18)	\$ 987,851	\$ 1,103,190
Due to related parties (Note 13)	11,183	11,183
Current portion of long-term debt (Note 8)	135,960	135,960
	1,134,994	1,250,333
LONG-TERM DEBT (Note 8)	783,950	817,940
UNEARNED LICENSE FEES (Note 9)	–	6,250
	1,918,944	2,074,523
SHAREHOLDERS' EQUITY		
SHARE CAPITAL (Note 10)	12,283,087	12,283,087
SHARE-BASED PAYMENTS RESERVES	3,854,485	3,852,924
DEFICIT	(9,881,106)	(10,193,041)
	6,256,466	5,942,970
	\$ 8,175,410	\$ 8,017,493

COMMITMENTS AND CONTINGENCIES (Note 15)

SUBSEQUENT EVENTS (Note 19)

Approved and authorized for issuance on behalf of the Board of Directors on November 25, 2016:

/s/ Alnesh Mohan

Alnesh Mohan, Director

/s/ Peter H. Stafford

Peter H. Stafford, Director

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

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
REVENUES (Note 17)	\$ 2,228,582	\$ 2,070,393
COST OF SALES (Note 4)	1,001,661	902,528
GROSS MARGIN	1,226,921	1,167,865
EXPENSES		
Depreciation (Note 5)	14,397	22,639
Selling, general and administrative	892,095	1,152,894
	906,492	1,175,533
EARNINGS (LOSS) BEFORE OTHER INCOME (EXPENSE)	320,429	(7,668)
OTHER INCOME (EXPENSE)		
Interest on finance lease obligations	—	(1,130)
Interest on long-term debt	(14,744)	(47,459)
Other income (Note 9)	6,250	6,512
	(8,494)	(42,077)
NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD	311,935	(49,745)
EARNINGS (LOSS) PER SHARE (Note 11)		
Basic and diluted	\$ 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, 2016	87,083,788	\$12,283,087	\$3,852,924	\$(10,193,041)	\$5,942,970
Comprehensive income for the period	—	—	—	311,935	311,935
Share-based compensation	—	—	1,561	—	1,561
Balance, September 30, 2016	87,083,788	\$12,283,087	\$3,854,485	\$(9,881,106)	\$6,256,466

	Share Capital		Share-based payments reserves	Deficit	Total Shareholders' Equity
	Number of Shares	Value			
Balance, June 30, 2015	87,083,788	\$12,283,087	\$3,798,198	\$(9,873,372)	\$6,207,913
Comprehensive loss for the period	—	—	—	(49,745)	(49,745)
Share-based compensation	—	—	28,038	—	28,038
Balance, September 30, 2015	87,083,788	\$12,283,087	\$3,826,236	\$(9,923,117)	\$6,186,206

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

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
CASH FLOWS PROVIDED BY (USED IN):		
OPERATING ACTIVITIES		
Net income (loss) for the period	\$ 311,935	\$ (49,745)
Adjusted for non-cash items:		
Depreciation	103,443	95,871
Accretion of long-term debt	—	42,671
Accrued interest on long-term debt	—	20,137
Recognition of unearned license fee (Note 9)	(6,250)	(6,250)
Share-based compensation (Note 10 (b))	1,561	28,038
	410,689	130,722
Net changes in non-cash working capital items:		
Accounts receivable	153,414	193,930
Prepaid expenses and deposits	(30,738)	4,154
Inventories	22,867	(25,410)
Due to and from related parties	—	11,647
Accounts payable and accrued liabilities	(115,339)	274,035
	440,893	589,078
INVESTING ACTIVITIES		
Purchases of property and equipment	(32,601)	(46,383)
Acquisition of intangible assets	(2,901)	—
	(35,502)	(46,383)
FINANCING ACTIVITIES		
Repayment of long-term debt	(33,990)	(81,987)
Repayment of finance lease obligations	—	(6,494)
	(33,990)	(88,481)
INCREASE IN CASH AND CASH EQUIVALENTS	371,401	454,214
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	349,575	428,312
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 720,976	\$ 882,526

SUPPLEMENTAL CASH FLOW INFORMATION (Note 12)

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(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 condensed consolidated interim 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 September 30, 2016, the Company had a positive working capital of \$1,405,076 and accumulated losses since inception of \$9,881,106. 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 consolidated 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 consolidated interim financial statements do not include all of the information required for full annual financial statements. These condensed consolidated interim financial statements should be read in conjunction with the Company's June 30, 2016 annual audited consolidated financial statements.

The condensed consolidated interim financial statements were authorized for issuance by the Board of Directors on November 25, 2016.

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

The following companies have been consolidated with Russell Breweries Inc. as at September 30, 2016:

Company Name	Registered	Holding	Functional Currency
Russell Breweries Inc.	British Columbia	Parent Company	Canadian Dollar
Fort Garry Brewing Company Ltd.(i)	Manitoba	100%	Canadian Dollar
Russell USA LLC	United States	0%	United States Dollar

(i) On July 1, 2014, Russell Brewing Company Ltd. ("Russell") amalgamated with Fort Garry Brewing Company Ltd. The continuing amalgamated entity is Fort Garry Brewing Company Ltd.

(ii) 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 consolidated 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 THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(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, 2016. These statements should be read in conjunction with the audited consolidated financial statements for the year ended June 30, 2016.

4. INVENTORIES AND COST OF SALES

	September 30, 2016	June 30, 2016
Finished goods	\$ 213,399	\$ 202,461
Work-in-progress	307,612	310,654
Raw materials	596,482	627,245
	\$ 1,117,493	\$ 1,140,360

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

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
Cash component: Inventories	\$ 912,615	\$ 829,296
Non-cash component: Depreciation (Note 5)	89,046	73,232
	\$ 1,001,661	\$ 902,528

RUSSELL BREWERIES INC.
NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

(Unaudited; Expressed in Canadian Dollars)

5. PROPERTY AND EQUIPMENT

	Computer \$	Equipment \$	Leasehold improvements \$	Office furniture and fixtures \$	Vehicles \$	Refundable containers \$	Total \$
Cost							
Balance as at June 30, 2015	77,931	6,070,239	1,508,294	63,844	486,972	962,354	9,169,634
Additions	1,790	448,147	64,450	–	–	75,452	589,839
Government assistance received	–	(108,695)	(23,094)	–	–	–	(131,789)
Balance as at June 30, 2016	79,721	6,409,691	1,549,650	63,844	486,972	1,037,806	9,627,684
Additions	–	–	–	–	–	32,601	32,601
Balance as at September 30, 2016	79,721	6,409,691	1,549,650	63,844	486,972	1,070,407	9,660,285
Accumulated Depreciation							
Balance as at June 30, 2015	71,800	3,905,239	1,325,482	63,844	447,068	917,364	6,730,797
Depreciation	2,385	271,345	37,200	–	39,904	44,573	395,407
Balance as at June 30, 2016	74,185	4,176,584	1,362,682	63,844	486,972	961,937	7,126,204
Depreciation	652	78,759	10,335	–	–	13,073	102,818
Balance as at September 30, 2016	74,837	4,255,343	1,373,017	63,844	486,972	975,010	7,229,022
Carrying amounts							
June 30, 2015	6,131	2,165,000	182,812	–	39,904	44,990	2,438,837
June 30, 2016	5,536	2,233,107	186,968	–	–	75,869	2,501,480
September 30, 2016	4,884	2,154,347	176,633	–	–	95,397	2,431,263

Equipment includes assets under finance leases with a cost of \$439,719 (June 30, 2016 – \$439,719) and accumulated depreciation of \$142,716 (June 30, 2016 – \$137,876). Vehicles includes assets under finance leases with a cost of \$473,775 (June 30, 2016 – \$473,775) and accumulated depreciation of \$473,775 (June 30, 2016 – \$473,775). The Company has recognized depreciation of \$13,073 in inventory (September 30, 2015 - \$9,834), \$13,772 in expenses (September 30, 2015 - \$22,639) and \$75,973 in cost of sales (September 30, 2015 - \$63,398).

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

6. INTANGIBLE ASSETS

	Brands and Trademarks	Website	Total
Cost			
Balance as at June 30, 2015	\$ 1,941,229	\$ 5,975	\$ 1,947,204
Additions	\$ 8,150	\$ 7,497	\$ 15,647
Balance as at June 30, 2016	\$ 1,949,379	\$ 13,472	\$ 1,962,851
Additions	\$ 2,902	\$ –	\$ 2,902
Balance as at September 30, 2016	\$ 1,952,281	\$ 13,472	\$ 1,965,753
Accumulated Depreciation			
Balance as at June 30, 2015	\$ –	\$ 5,975	\$ 5,975
Depreciation for the year	\$ –	\$ 1,250	\$ 1,250
Balance as at June 30, 2016	\$ –	\$ 7,225	\$ 7,225
Depreciation for the period	\$ –	\$ 625	\$ 625
Balance as at September 30, 2016	\$ –	\$ 7,850	\$ 7,850
Carrying amounts			
June 30, 2015	\$ 1,941,229	\$ –	\$ 1,941,229
June 30, 2016	\$ 1,949,379	\$ 6,247	\$ 1,955,626
September 30, 2016	\$ 1,952,281	\$ 5,621	\$ 1,957,902

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, 2015 – \$100,000). As at September 30, 2016, accrued interest has been earned on the term deposit in the amount of \$7,006 (2015 - \$6,341).

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

8. LONG-TERM DEBT

	September 30, 2016	June 30, 2016
Term bank loan, bearing interest at a base rate of 5.15% plus a variance of 1%, repayable in monthly installments of \$8,750 plus interest maturing on April 15, 2023, secured by the assets of Russell and Fort Garry (a)	\$ 691,250	\$ 717,500
Term bank loan, bearing interest at a base rate of 5.15% plus a variance of 1%, repayable in monthly installments of \$1,750 plus interest maturing on April 15, 2025, secured by the assets of Russell and Fort Garry (b)	185,500	190,750
Term bank loan, bearing interest at a base rate of 4.70% plus a variance of 3%, repayable in monthly installments of \$830 plus interest maturing on April 15, 2025, secured by the assets of Russell and Fort Garry (c)	43,160	45,650
	919,910	953,900
Less: current portion of long-term debt	(135,960)	(135,960)
Long-term portion of long-term debt	\$ 783,950	\$ 817,940

- (a) On October 1, 2015, the Company entered into a loan agreement with Business Development Bank of Canada ("BDC") for \$788,000. The BDC Loan, bearing interest at a base rate of 5.15% plus a variance of 1% maturing April 15, 2023 secured by the assets of Fort Garry Brewing Company and Russell Brewing Company Ltd. During the period ended September 30, 2016, the Company recorded interest expense of \$10,955 (2015 - \$nil) which has been recorded as interest on long-term debt in the consolidated statement of comprehensive income.
- (b) On February 3, 2016, the Company entered into a loan agreement with Business Development Bank of Canada ("BDC") for \$200,000. The BDC Loan, bearing interest at a base rate of 5.15% plus a variance of 1% maturing April 15, 2025 secured by the assets of Fort Garry Brewing Company and Russell Brewing Company Ltd. During the period ended September 30, 2016, the Company recorded interest expense of \$2,921 (2015 - \$nil) which has been recorded as interest on long-term debt in the consolidated statement of comprehensive income.
- (c) On February 3, 2016, the Company entered into a loan agreement with Business Development Bank of Canada ("BDC") for \$50,000. The BDC Loan, bearing interest at a base rate of 4.70% plus a variance of 3% maturing April 15, 2025 secured by the assets of Fort Garry Brewing Company and Russell Brewing Company Ltd. During the year ended September 30, 2016, the Company recorded interest expense of \$868 (2015 - \$nil) which has been recorded as interest on long-term debt in the consolidated statement of comprehensive income.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

8. LONG-TERM DEBT (continued)

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

Fiscal Year	Amount
2017	\$ 101,970
2018	135,960
2019	135,960
2020	135,960
2021	131,810
2022	126,000
2023	108,500
2024	21,000
2025	21,000
2026	1,750
	<hr/>
	\$ 919,910

9. 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 20% of the common shares of the Licensee ("Licensee Common Shares") with an estimated fair value of \$100,000. During the year ended June 30, 2014, the Company's interest in the Licensee decreased to 7.69% and remained the same as at June 30, 2015 and 2016. As a result, 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. During the year ended June 30, 2015, the Company determined that the long-term investment was not recoverable, and a loss in the amount of \$100,000 was recorded as a write-off of long-term investment in the consolidated statement of comprehensive income.

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 September 30, 2016, the Company has recognized \$nil (2015 - \$262) in royalties and \$6,250 (2015 - \$6,250) in license fees earned under the agreement, which has been recorded as other income in the statement of operations. As at September 30, 2016, the unearned license fee is \$nil (June 30, 2016 - \$6,250).

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

10. 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.

On July 6, 2014, the Company granted 4,550,000 incentive stock options to key employees and directors exercisable at \$0.07 per share expiring five years from the grant date, pursuant to its stock option plan. The options vest with 1/24th of the granted options vesting each monthly anniversary of the date of grant for 24 months. 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 5 years; forfeiture rate of 0%, risk-free interest rate of 1.46%; expected dividend yield of 0% and expected stock price volatility of 112%. During the period ended September 30, 2016, the Company recorded a total amount of \$1,561 (2015 - \$28,038) compensation cost included in selling, general and administrative expense relating to these options.

Stock option activity during the period ended September 30, 2016 and the year ended June 30, 2016 is presented below:

	September 30, 2016		June 30, 2016	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of period	4,400,000	\$ 0.07	4,600,000	\$ 0.07
Forfeited	—	—	(200,000)	—
Outstanding, end of period	4,400,000	\$ 0.07	4,400,000	\$ 0.07

At September 30, 2016, 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	0.01	0.10	50,000	0.00
0.07	4,350,000	2.74	0.07	4,350,000	0.07
	4,400,000	2.75	0.07	4,400,000	0.07

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

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

Warrant activity during the period ended September 30, 2016 and the year ended June 30, 2016 is presented below:

	September 30, 2016		June 30, 2016	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding and exercisable, beginning of period	–	\$ –	4,000,000	\$ 0.05
Expired	–	–	(4,000,000)	0.05
Outstanding, end of period	–	\$ –	–	\$ –

11. EARNINGS (LOSS) PER SHARE

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

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
Net income (loss)	\$ 311,935	\$ (49,745)
Common shares outstanding, beginning of year	87,083,788	87,083,788
Number of common shares outstanding during the year	87,083,788	87,083,788
Earnings (loss) per share (Basic and diluted)	\$ 0.00	\$ (0.00)

The number of shares outstanding used in the computation of loss per share for the period ended September 30, 2016 was 87,083,788 (June 30, 2016 – 87,083,788). Outstanding stock options, warrants, and agent unit options have not been considered in the computation of diluted loss per share as the result is anti-dilutive.

12. SUPPLEMENTAL CASH FLOW INFORMATION

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
Cash paid for: Interest	\$ 14,744	\$ 403

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

13. 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:

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
Short-term benefits:		
Salaries and management fees [Note 13(a)]	\$ 72,685	\$ 58,050
Directors fees [Note 13(b)]	13,603	9,000
Share-based payments [Note 13(c)]	1,561	28,038
	\$ 87,849	\$ 95,088

- (a) During the period ended September 30, 2016, the Company incurred management fees to a company controlled by the CEO in the amount of \$32,125 (2015 - \$31,187) and salaries and benefits to the CFO in the amount of \$40,560 (2015 - \$26,863). As at September 30, 2016, the Company owed \$11,183 to a company controlled by the CEO (June 30, 2016 - \$11,183), which is non-interest bearing, unsecured and due on demand.
- (b) During the period ended September 30, 2016, the Company incurred director fees of \$13,603 (2015 - \$9,000). As at September 30, 2016, the Company owed \$Nil to the independent directors (2016 - \$Nil), which were non-interest bearing, unsecured and due on demand.
- (c) During the period ended September 30, 2016, the Company granted nil (2015 - nil) stock options to directors and key employees and recorded share-based compensation in the amount of \$1,561 (2015 - \$28,038) (Note 10 (b)).

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.

14. 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, 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 value of long-term debt at September 30, 2016 are considered to be reasonable estimates of fair value based on current market rates for similar financial instruments.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

14. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)**(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.

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 September 30, 2016 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 September 30, 2016 \$
Assets:				
Cash and cash equivalents	720,976	—	—	720,976
Restricted term deposits	107,006	—	—	107,006

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

14. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)**(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 September 30, 2016, the Company has significant accounts receivable from two major customer totaling \$529,221 (June 30, 2016 - \$654,971). The Company manages credit risk for trade and other receivables through established credit monitoring activities. As at September 30, 2016, 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:

	September 30, 2016		June 30, 2016	
	Over 90 days	Total	Over 90 days	Total
Provincial Liquor Boards	\$ –	\$ 549,253	\$ –	\$ 681,400
Other receivables	271	72,427	–	93,694
Total	\$ 271	\$ 621,680	\$ –	\$ 775,094

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.

(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 September 30, 2016 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	987,851	–	–	–	987,851
Due to related parties and long-term debt	147,143	237,930	267,770	278,250	931,093
	1,134,994	237,930	267,770	278,250	1,918,944

As at September 30, 2016, the Company had a positive working capital of \$1,405,076.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

14. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)**(c) Financial Risks (continued)****(iii) Interest Rate Price Risk**

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

Certain of the Company's long-term debt instruments 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.

15. COMMITMENTS AND CONTINGENCIES

- (a) The Company has entered into operating lease agreements for premises, vehicles and office equipment. The remaining terms of these leases range between 4 and 9 years. Future minimum operating lease payments due as at September 30, 2016 are:

Not later than one year	\$	395,498
Later than one year and not later than five years		1,714,550
Later than five years		608,872
	\$	2,718,920

- (b) At September 30, 2016, the Company had issued a general excise bond of \$45,000 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% secured by a term deposit of \$100,000 (see Note 7). As at September 30, 2016, \$100,000 is undrawn from the line of credit.

16. 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, 2016 - \$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:

	September 30, 2016	June 30, 2016
Long-term debt (Note 8)	\$ 919,910	\$ 953,900
Shareholders' equity	6,256,466	5,942,970
	\$ 7,176,376	\$ 6,896,870

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

17. REVENUES

During the period ended September 30, 2016, the Company had sales of \$1,398,325 (2015 - \$1,368,369) to the Manitoba Liquor and Lotteries Commission which accounted for 56% of its revenues (2015 - 58%).

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
GROSS REVENUES	\$ 2,481,430	\$ 2,347,093
LESS: EXCISE TAX AND PROVINCIAL MARK-UP	252,848	276,700
REVENUES	\$ 2,228,582	\$ 2,070,393

18. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

The following is a breakdown of accounts payable and accrued liabilities:

	September 30, 2016	June 30, 2016
Trade accounts payable	\$ 609,760	\$ 522,818
GST payable	112,065	132,330
Accrued payroll and bonuses	218,538	219,304
Other accrued liabilities	47,488	228,738
	\$ 987,851	\$ 1,103,190

19. SUBSEQUENT EVENTS

- (a) On October 5, 2016, the Company entered into an agreement to sell the non-current assets and working capital of its Fort Garry Brewing Company business, utilized for the production of beer in Manitoba, for a purchase price of \$7,715,545 ("Fort Garry Sale Agreement"), subject to a required working capital of \$857,328. The purchase price will be adjusted on the closing date on a dollar for dollar basis for any variance in the working capital from the required amount. The closing date of the agreement is December 15, 2016 or any other date as agreed by the parties. The purchase price is to be paid as follows:

- (i) \$6,165,545 in cash;
- (ii) The surrender of a \$200,000 deposit paid in trust on execution of Fort Garry Sale Agreement;
- (iii) The deposit with Computershare Trust Company of Canada of \$1,350,000.

The Company is subject to non-solicitation provisions. The Fort Garry Sale Agreement provides that the Company's Board may, under certain circumstances, terminate the agreement in favour of an unsolicited superior proposal. If the proposal is terminated, the Company will be subject to payment of a termination fee of \$750,000 to the purchaser, and the purchaser is granted a right to match a superior proposal. The sale is subject to the approval by the Company's shareholders.

RUSSELL BREWERIES INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015**

(Unaudited; Expressed in Canadian Dollars)

19. SUBSEQUENT EVENTS (continued)

- (b) On October 5, 2016, the Company entered into an agreement to sell the non-current assets and working capital of its Russell Brewing Company business, utilized for the production of beer in British Columbia, for a purchase price of \$1,800,000 ("Russell Sale Agreement"), subject to a required working capital of \$548,123. The purchase price will be adjusted on the closing date on a dollar for dollar basis for any variance in the working capital from the required amount. The closing date of the agreement is December 31, 2016 or any other date as agreed by the parties. The purchase price is to be paid as follows:
- (i) on closing, payment of:
 - \$180,000 in cash; and
 - the surrender of a \$180,000 deposit paid in trust on the execution of the sale agreement; and
 - (ii) the remainder of the purchase price will be payable by the purchaser in instalments as follows:
 - approximately 120 days from the closing date, payment of \$80,000, subject to any working capital adjustments; and
 - at the election of the purchaser, either:
 - i. on the date that is 6 months from the closing of the sale, the deposit with the Escrow Agent of \$200,000, to cover any indemnification claims that may be made by the purchaser for a period of one year following closing, and payment of the remainder of the purchase price, being \$1,160,000, plus interest of 7.5% per annum, compounded annually, on such amounts; or
 - ii. on the date that is 6 months from the closing of the sale, payment of \$680,000 and, on the date that is 12 months from the closing of the sale, payment of \$200,000, subject to any indemnification claims that may be made by the purchaser, and the remainder of the purchase price, being \$480,000, plus interest of 7.5% per annum, compounded annually, on such amounts.

As collateral security for the payment of the remaining instalments of the purchase price, the purchaser has agreed to execute and deliver in favour of the Company, a first ranking general security agreement covering all of the Russell Brewing Company assets.

The Company is subject to non-solicitation provisions. The Russell Sale Agreement provides that the Company's Board may, under certain circumstances, terminate the Agreement in favour of an unsolicited superior proposal. In case of the termination of the Agreement, the Company will be subject to payment of a termination fee of \$160,000 to the purchaser, and the purchaser will be granted a right to match a superior proposal. The sale is subject to the approval by the Company's shareholders.