

# **RediShred Capital Corp.**

Consolidated Financial Statements  
**December 31, 2010 and 2009**

(expressed in Canadian dollars)

April 29, 2011

## **Management's responsibility for the Financial Statements**

The accompanying consolidated financial statements of **RediShred Capital Corp.** have been prepared by the Company's management. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and contain estimates based on management's judgment. Internal control systems are maintained by management to provide reasonable assurances that assets are safeguarded and financial information is reliable.

The Board of Directors of the Company is responsible for ensuring that management fulfils its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements and the accompanying management discussion and analysis. The Board carries out this responsibility principally through its Audit Committee.

The Audit Committee is appointed by the Board of Directors. It meets with the Company's management and auditors and reviews internal control and financial reporting matters to ensure that management is properly discharging its responsibilities before submitting the financial statements to the Board of Directors for approval.

PricewaterhouseCoopers LLP, appointed as the Company's auditors by the shareholders, has audited these consolidated financial statements and their report follows.

(signed) "*Jeffrey Hasham*"  
Chief Executive Officer  
Mississauga, Ontario

(signed) "*Kasia Pawluk*"  
Chief Financial Officer  
Mississauga, Ontario

April 29, 2011

## **Independent Auditor's Report**

### **To the Shareholders of RediShred Capital Corp.**

We have audited the accompanying consolidated financial statements of RediShred Capital Corp. and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2010 and 2009 and the consolidated statements of operations, shareholders' equity and comprehensive loss and cash flows for the years then ended, and the related notes including a summary of significant accounting policies.

#### **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 Canadian generally accepted accounting principles, 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 audits 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 audits is sufficient and appropriate to provide a basis for our audit opinion.

#### **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of RediShred Capital Corp. and its subsidiaries, as at December 31, 2010 and 2009 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

(signed) "PricewaterhouseCoopers LLP"

#### **Chartered Accountants**

# RediShred Capital Corp.

## Consolidated Balance Sheets

As at December 31, 2010 and 2009

(expressed in Canadian dollars)

|   | 2010<br>\$         | 2009<br>\$         |
|---|--------------------|--------------------|
| <b>Assets</b> (note 10)                           |                    |                    |
| <b>Current assets</b>                             |                    |                    |
| Cash  | 988,592            | 1,086,036          |
| Accounts receivable                               | 414,910            | 321,588            |
| Prepaid expenses                                  | 45,359             | 16,850             |
| Notes receivable from franchisees (note 4)        | 33,178             | 24,445             |
| Income taxes recoverable                          | —                  | 11,062             |
|   | <u>1,482,039</u>   | <u>1,459,981</u>   |
| <b>Notes receivable from franchisees</b> (note 4) | 108,705            | 139,781            |
| <b>Equipment</b> (note 5)                         | 696,581            | 204,998            |
| <b>Deferred financing charges</b> (note 6)        | 88,345             | 110,431            |
| <b>Intangible assets</b> (note 7)                 | <u>5,649,626</u>   | <u>4,364,364</u>   |
|   | <u>8,025,296</u>   | <u>6,279,555</u>   |
| <b>Liabilities</b>                                |                    |                    |
| <b>Current liabilities</b>                        |                    |                    |
| Accounts payable and accrued liabilities          | 513,559            | 340,021            |
| Notes payable                                     | 99,789             | —                  |
|   | <u>613,348</u>     | <u>340,021</u>     |
| <b>Long-term debt</b> (note 10)                   | 2,790,000          | —                  |
| <b>Future income tax liability</b> (note 9)       | <u>533,000</u>     | <u>646,000</u>     |
|   | <u>3,936,348</u>   | <u>986,021</u>     |
| <b>Shareholders' Equity</b>                       |                    |                    |
| <b>Capital stock</b> (note 8)                     | 8,585,808          | 8,585,808          |
| <b>Contributed surplus</b>                        | 295,613            | 208,391            |
| <b>Accumulated other comprehensive income</b>     | 67,303             | 141,621            |
| <b>Deficit</b>                                    | <u>(4,859,776)</u> | <u>(3,642,286)</u> |
|   | <u>4,088,948</u>   | <u>5,293,534</u>   |
|   | <u>8,025,296</u>   | <u>6,279,555</u>   |
| <b>Commitments and contingency</b> (note 11)      |                    |                    |

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

Approved on behalf of the Board of Directors

(signed) "Philip H. Gaunce" Director

(signed) "Robert Richardson" Director

**RediShred Capital Corp.**  
Consolidated Statements of Operations  
For the years ended December 31, 2010 and 2009

(expressed in Canadian dollars)

|  | <b>2010</b> | <b>2009</b> |
|--|-------------|-------------|
|  | <b>\$</b>   | <b>\$</b>   |
| <b>Franchising and licensing operations</b>                                      |             |             |
| Franchise territory and licensing fees   | 355,413     | 139,883     |
| Royalty and service fees   | 934,639     | 828,944     |
|  | <hr/>       | <hr/>       |
| Revenue from franchising   | 1,290,052   | 968,827     |
| Salaries and stock-based compensation  | (904,671)   | (1,086,066) |
| General, administrative and marketing  | (730,658)   | (1,075,598) |
| Franchising broker fees  | (25,527)    | –           |
| Depreciation and amortization - equipment  | (170,936)   | (198,681)   |
|  | <hr/>       | <hr/>       |
|  | (541,740)   | (1,391,518) |
| <b>Corporate operations</b>  |             |             |
| Service and recycling revenue  | 713,711     | –           |
| Operating costs  | (438,580)   | –           |
| Depreciation and amortization – equipment  | (74,295)    | –           |
| Interest expense   | (73,082)    | –           |
|  | <hr/>       | <hr/>       |
|  | 127,754     | –           |
| <b>Loss before the following</b>   | (413,986)   | (1,391,518) |
| Amortization of intangibles  | (585,049)   | (578,859)   |
| Interest income  | 4,945       | 12,669      |
| Foreign currency gain (loss)   | (141,625)   | (31,334)    |
| Loss on settlement of pre-existing relationship (note 3)                         | (149,775)   | –           |
| Write-down of goodwill and intangible assets (note 7)                            | –           | (169,001)   |
|  | <hr/>       | <hr/>       |
| <b>Loss before income taxes</b>  | (1,285,490) | (2,158,043) |
| Recovery of income taxes (note 9)  | (68,000)    | (155,000)   |
|  | <hr/>       | <hr/>       |
| <b>Net loss for the year</b>   | (1,217,490) | (2,003,043) |
|  | <hr/>       | <hr/>       |
| <b>Loss per share – basic and diluted</b>  | (0.04)      | (0.09)      |
|  | <hr/>       | <hr/>       |
| <b>Weighted average number of commons shares outstanding – basic and diluted</b> | 28,884,658  | 23,016,122  |
|  | <hr/>       | <hr/>       |

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

# RediShred Capital Corp.

## Consolidated Statements of Shareholders' Equity and Comprehensive Loss For the years ended December 31, 2010 and 2009

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(expressed in Canadian dollars)

|                                    | Capital stock<br>\$<br>(note 8) | Contributed<br>surplus<br>\$<br>(note 8) | Accumulated<br>other<br>comprehensive<br>income<br>\$ | Deficit<br>\$      | Total<br>shareholders'<br>equity<br>\$ |
|------------------------------------|---------------------------------|--|---|--------------------|--|
| <b>Balance – December 31, 2008</b> | 7,650,565                       | 189,400                                  | 503,873   | (1,639,243)        | 6,704,595                              |
| Net loss for the year              | –                               | –  | –   | (2,003,043)        | (2,003,043)                            |
| Other comprehensive income         |                                 |  |   |                    |  |
| Foreign currency translation loss  | –                               | –  | (362,252)   | –                  | <u>(362,252)</u>                       |
| Comprehensive loss for the year    | –                               | –  | –   | –                  | (2,365,295)                            |
| Issue of shares (net of costs)     | 935,243                         | –  | –   | –                  | 935,243                                |
| Stock-based compensation           | –                               | 18,991                                   | –   | –                  | 18,991                                 |
| <b>Balance – December 31, 2009</b> | <u>8,585,808</u>                | <u>208,391</u>                           | <u>141,621</u>  | <u>(3,642,286)</u> | <u>5,293,534</u>                       |
| Net loss for the year              | –                               | –  | –   | (1,217,490)        | (1,217,490)                            |
| Other comprehensive income         |                                 |  |   |                    |  |
| Foreign currency translation loss  | –                               | –  | (74,318)  | –                  | <u>(74,318)</u>                        |
| Comprehensive loss for the year    | –                               | –  | –   | –                  | (1,291,808)                            |
| Stock-based compensation           | –                               | 87,222                                   | –   | –                  | 87,222                                 |
| <b>Balance – December 31, 2010</b> | <u>8,585,808</u>                | <u>295,613</u>                           | <u>67,303</u>   | <u>(4,859,776)</u> | <u>4,088,948</u>                       |

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

**RediShred Capital Corp.**  
**Consolidated Statements of Cash Flows**  
**For the years ended December 31, 2010 and 2009**

(expressed in Canadian dollars)

|   | <b>2010</b>        | <b>2009</b>        |
|---|--------------------|--------------------|
|   | <b>\$</b>          | <b>\$</b>          |
| <b>Cash provided by (used in)</b>                               |                    |                    |
| <b>Operating activities</b>                                     |                    |                    |
| Net loss for the year   | (1,217,490)        | (2,003,043)        |
| Items not affecting cash  |                    |                    |
| Amortization of tangible and intangible assets                  | 830,280            | 777,540            |
| Stock-based compensation  | 87,222             | 18,991             |
| Unrealized foreign currency loss                                | 66,483             | 34,641             |
| Write-down of goodwill and intangible assets                    | –                  | 169,001            |
| Allowance for doubtful receivables                              | 23,883             | 20,151             |
| Impairment of note receivable                                   | 11,929             | 47,144             |
| Loss on settlement of pre-existing relationship                 | 149,775            | –                  |
| Future income taxes   | (88,000)           | (155,000)          |
|   | <u>(135,918)</u>   | <u>(1,090,575)</u> |
| Net change in non-cash working capital balances                 |                    |                    |
| Decrease (increase) in accounts receivable                      | (128,719)          | (213,118)          |
| Decrease (increase) prepaid expenses                            | (29,546)           | 57,386             |
| Decrease (increase) in deposits and other assets                | –                  | 62,284             |
| Decrease (increase) in income taxes recoverable                 | 10,543             | (96,070)           |
| Increase (decrease) in accounts payable and accrued liabilities | 184,395            | (21,832)           |
|   | <u>(99,245)</u>    | <u>(1,301,925)</u> |
| <b>Financing activities</b>                                     |                    |                    |
| Net cash proceeds from issuance of common shares and warrants   | –                  | 851,443            |
| Deferred financing charges                                      | –                  | (26,631)           |
| Borrowings from long-term debt                                  | 2,790,000          | –                  |
|   | <u>2,790,000</u>   | <u>824,812</u>     |
| <b>Investing activities</b>                                     |                    |                    |
| Cash paid on acquisition of franchises                          | (2,259,490)        | –                  |
| Payment of notes payable related to the acquisition of assets   | (35,135)           | –                  |
| Purchase of capital assets                                      | (473,205)          | –                  |
| Increase in notes receivable from franchisees                   | (25,765)           | (82,775)           |
| Collection of notes receivable from franchisees                 | 28,677             | 72,249             |
|   | <u>(2,764,918)</u> | <u>(10,526)</u>    |
| <b>Effect of foreign exchange rate changes on cash</b>          | <u>(23,281)</u>    | <u>(79,929)</u>    |
| <b>Net change in cash for the years</b>                         | <u>(97,444)</u>    | <u>(567,568)</u>   |
| <b>Cash – Beginning of years</b>                                | <u>1,086,036</u>   | <u>1,653,604</u>   |
| <b>Cash – End of years</b>                                      | <u>988,592</u>     | <u>1,086,036</u>   |
| <b>Cash flows from operating activities include</b>             |                    |                    |
| Interest received   | 3,472              | 12,668             |
| Income taxes paid   | 1,445              | 96,085             |
| Interest paid   | 60,263             | –                  |

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

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

#### 1 Nature of operations

RediShred Capital Corp. (the "Company") was incorporated under the Canada Business Corporations Act on October 18, 2006. The Company's common shares were listed for trading on the TSX Venture Exchange on September 5, 2007, as a Capital Pool Company. The Company's business, until March 17, 2008, was the identification and evaluation of shredding businesses that could qualify as a Qualifying Transaction under TSX Venture Exchange policies. On March 17, 2008, the Company acquired the shares of Professional Shredding Corporation ("PSC"), which directly and indirectly carries on the business of granting and managing shredding business franchises under the "Proshred" trademark. The acquisition served as the Company's "Qualifying Transaction" pursuant to the policies of the TSX Venture Exchange and was approved by the TSX Venture Exchange.

On April 30, 2010, the Company, through its wholly-owned subsidiary, Redishred Acquisition Inc. ("RAI") acquired the business of the Proshred Syracuse, New York ("Syracuse") franchise and on June 30, 2010, the Company acquired the business of the Proshred Albany, New York ("Albany") franchise. The Company has consolidated the Syracuse and Albany management teams and offices, creating a regional head quarters in Syracuse.

On July 26, 2010, the Company awarded the San Diego, California franchise, which commenced operations in October 2010.

On November 1, 2010 the Company entered into an agreement with Averda International FZ-LLC ("Averda") to operate the "Proshred" or "RediShred" shredding platform in 15 countries and four territories throughout the Middle East region. The Company anticipates that Averda will commence shredding operations in 2011.

On December 31, 2010, the Company, through its wholly-owned subsidiary, RAI acquired the business of the Proshred Milwaukee, Wisconsin ("Milwaukee") franchise.

As of December 31, 2010, the Company has 18 locations in operation (December 31, 2009 – 17) of which 15 are franchised and 3 are corporately operated. The Company also has one international licence to operate in the Middle East.

#### 2 Significant accounting policies

##### Basis of presentation

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries PSC, RAI and Proshred Franchising Corp. ("PFC"). All transactions between the Company and its subsidiaries have been eliminated.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

## 2 Significant accounting policies (continued)

### Use of accounting estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Estimates include, but are not limited to, the following:

- i) Economic useful life of proprietary software system for purposes of calculating depreciation;
- ii) The allocation of the purchase price for the acquisition of Syracuse, Albany and Milwaukee franchises entails various estimates to determine the fair values of, and allocation of purchase prices to the tangible and intangible assets and liabilities acquired;
- iii) Valuation of accounts receivable and notes receivable from franchisees;
- iv) Valuation of intangible assets; and
- v) Assumptions used in the measurement of stock-based compensation and the fair value of warrants.

While management applies its judgment based on assumptions believed to be reasonable under the circumstances at the time, actual results could vary from their assumptions or had different assumptions been used. The Company evaluates and updates its assumptions and estimates based on any new events occurring, additional information being obtained or more experience being acquired.

### Cash

As at December 31, 2010 and 2009, the Company's cash balances were held in bank accounts, which the Company has full access to, and do not include any instruments related to asset-backed securities or commercial paper programs.

### Revenue recognition

#### *Franchising and licensing business*

The Company earns revenue from initial franchise and license fees paid to secure territories for a specific period and from royalties and service fees paid as a percentage of their monthly sales volumes. Initial franchise fees are recognized as revenue when the franchisee has paid the initial franchise fee, has fully executed a franchise agreement and has been provided the required training. Initial licence fees are recognized as revenue when the licensee has fully executed a licence agreement. Royalties and service fees revenue are accrued monthly based on sales reported by franchisees or licensees. Interest income on notes receivable is recognized in the month earned.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

## 2 Significant accounting policies (continued)

### *Corporate operations – shredding and recycling services*

The Company earns revenue from providing shredding services to clients and by way of the sale of recycled paper to recycling facilities. Shredding service revenue is recorded when the shredding service has been performed and the Company has provided a certificate of destruction and an invoice to the client, and collections are reasonably assured. Recycling revenue is recognized when the collected paper has been delivered to the recycling facility and collections are reasonably assured.

### **Advertising fund assets and liabilities**

The Company manages an advertising fund (the “Ad Fund”) established to collect and administer funds contributed for use in regional and national advertising programs, and amongst other things, initiatives designed to increase sales and enhance general public recognition, acceptance and use of the Proshred System. Contributions to the Ad Fund are required to be made from both franchised and Company owned and operated locations and are based on a percentage of each locations’ revenue. The revenue, expenses and cash flows of the Ad Fund are not included in the Company’s consolidated Statements of Operations or Cash Flows because the contributions to the Ad Fund are segregated and designated for a specific purpose. As at December 31, 2010, the Ad Fund was in a net surplus position of \$51,728 (2009 – deficit of \$36,486), with cash attributable to the Ad Fund amounting to \$87,720 (2009 - \$20,983) included in the Company’s cash balance, offset by a corresponding amount included in accounts payable and accrued liabilities.

### **Income taxes**

The Company uses the liability method of accounting for income taxes. Under the liability method, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using substantially enacted tax rates expected to be in effect for the year in which the differences are expected to reverse. Changes in future income tax rates for assets and liabilities as a result of changes to the subsidiary enacted tax rates are included in income tax recovery (expense) in the period that the substantive enactment or enactment occurs. Future income tax assets are evaluated and recorded if realization is considered more likely than not, otherwise a valuation allowance is provided.

### **Stock-based compensation**

The Company accounts for stock options issued under its stock option plan using the fair value method. Under this method, compensation expense is measured at fair value at the grant date using the Black-Scholes option pricing model and is recognized over the vesting period. Option pricing models require the input of highly subjective assumptions, including the expected volatility. Changes in the assumptions can materially affect the fair value estimate.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

## 2 Significant accounting policies (continued)

### Foreign currency translation

The Company's subsidiaries operate autonomously as self-sustaining companies. The functional currency of the Company's foreign subsidiaries, Proshred Franchising Corp. and Redishred Acquisition Inc. is the US dollar. Assets and liabilities of these subsidiaries are translated into Canadian dollars at exchange rates at the balance sheet date. Income and expense items are translated at average exchange rates for the period. Cumulative translation adjustments are included as a component of accumulated other comprehensive income in shareholders' equity.

Foreign currency exchange gains or losses, derived from monetary assets and liabilities denominated in currencies other than the functional currency, are translated into the functional currency at the exchange rate in effect at the balance sheet date with the resulting foreign currency gains or losses included in the determination of the income for the year.

As investments in self-sustaining subsidiaries are excluded from the financial instrument disclosure, the Company's exposure on financial instruments to the Canadian/US dollar foreign currency exchange rate is primarily to the parent company. The parent has no significant financial instruments subject to foreign currency risk.

### Equipment and amortization

Equipment is carried at cost. Amortization is provided for, based on over the estimated useful lives, using the straight-line method over the following periods:

|   |           |
|---|-----------|
| Computer equipment                          | 2 years   |
| Furniture and fixtures                      | 3 years   |
| Computer software                           | 3 years   |
| Bins and shredding containers               | 5 years   |
| Shredding vehicles – chassis                | 3-5 years |
| Shredding vehicles – shredding compartments | 3-5 years |
| Recycling equipment                         | 2 years   |

### Intangible assets

Intangible assets are recorded at their fair value at the date of acquisition. With the exception of re-acquired franchise rights, amortization is provided for intangible assets with limited lives on a straight-line basis over their estimated useful lives of ten years. Amortization on re-acquired franchise rights is based on the remaining initial contractual period, excluding any renewal terms, ranging from 2.3 years to 7.7 years.

### Impairment of long-lived assets

Long-lived assets, including equipment and other intangible assets are reviewed for impairment when events or circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment losses are recognized when the carrying value of the asset is greater than the future undiscounted cash flows expected to be provided by the asset. The amount of impairment loss, if any, which is the excess of net carrying value over fair value, is charged to income for the period.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements December 31, 2010 and 2009

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(expressed in Canadian dollars)

### 2 Significant accounting policies (continued)

#### Deferred financing charges

Deferred financing charges consist of costs incurred relating to the issuance of a revolving line of credit obtained on December 23, 2009 and are amortized over the term of the facility which expires on November 27, 2014.

#### Goodwill

Goodwill represents the excess of the purchase price of an acquired business over the net amount of the fair values assigned to its assets and liabilities and is not subject to amortization.

#### Loss per share

Basic loss per share is computed by dividing net earnings by the weighted average number of common shares outstanding during the reporting period. Diluted loss per share is calculated based on the weighted average number of common shares outstanding during the period, plus the effect of dilutive common share equivalents such as options and warrants. The diluted per share amounts are calculated using the treasury stock method, as if all the common share equivalents where average market prices exceeds issue price had been exercised at the beginning of the reporting period, or the period of issue, as the case may be and that the funds obtained thereby were used to purchase common shares of the Company at the average trading price of the common shares during the period. Since the Company has losses, the exercise of outstanding stock options has not been included in the calculation of diluted loss per share as it would be anti-dilutive.

#### Financial instruments

##### i) Financial instruments – recognition and measurement

Section 3855 of the Canadian Institute of Chartered Accountants (“CICA”) Handbook establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for-trading, available-for-sale, held-to-maturity, loans and receivables or other liabilities.

The Company has implemented the following classifications:

- Cash is classified as “Financial Assets Held-for-Trading”. These financial assets are marked-to-market through net income at each period-end.
- Accounts receivable and notes receivable from franchisees are classified as “Loans and Receivables”. After their initial fair value measurement they are measured at amortized cost using the effective interest method.
- Accounts payable and accrued liabilities are classified as “Other Financial Liabilities”. After their initial fair value measurement, they are measured at amortized cost using the effective interest method.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

## 2 Significant accounting policies (continued)

### ii) Financial instruments – disclosures

Section 3862 of the CICA Handbook requires additional disclosure requirements about fair value measurement for financial instruments and liquidity risk disclosures. These requirements include a three-level hierarchy that reflects the significance of the inputs used in making the fair value measurements. Each level is based on the transparency of the inputs used to measure the fair values of assets and liabilities:

- Level 1 inputs are unadjusted quoted prices of identical instruments in active markets.
- Level 2 inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 one or more significant inputs used in a valuation technique are unobservable in determining fair values of the instruments.

Determination of fair value and the resulting hierarchy requires the use of observable market data whenever available. The classification of a financial instrument in the hierarchy is based upon the lowest level of input that is significant to the measurement of fair value. The only financial instrument recorded at fair value is cash, which is valued based on market prices in an active market (Level 1).

### iii) Comprehensive income

Under Section 1530 of the CICA Handbook, comprehensive income is comprised of net earnings and other comprehensive income (“OCI”) which generally would include unrealized gains and losses on financial assets classified as available-for-sale, unrealized foreign currency translation adjustments, net of hedging, arising from self-sustaining foreign operations, and changes in the fair value of the effective portion of cash flow hedging instruments. Accumulated other comprehensive income is presented as a category of shareholders’ equity.

### Future accounting policy changes

#### *International Financial Reporting Standards (“IFRS”)*

In February 2008, the Canadian Accounting Standards Board ratified a strategic plan that will see GAAP converged with and replaced by IFRS for fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require the restatement, for comparative purposes, of amounts reported by the Company for the year ended December 31, 2010. For the quarter ended March 31, 2011, the Company will issue its comparative interim financial statements prepared in accordance with IFRS.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements December 31, 2010 and 2009

(expressed in Canadian dollars)

### 3 Acquisition of franchises

During the year, the Company, through its wholly-owned subsidiary, Redishred Acquisition Inc., acquired the following franchises:

- ProShred Syracuse, on April 30, 2010;
- ProShred Albany, on June 30, 2010; and
- ProShred Milwaukee, on December 31, 2010.

The allocation of the purchase price to the assets acquired (including all identifiable intangible assets arising from the purchases) based on their estimated fair value at the date of each respective acquisition, is as follows:

|   | Syracuse<br>\$ | Albany<br>\$   | Milwaukee<br>\$  | Total<br>\$      |
|---|----------------|----------------|------------------|------------------|
| <b>Assets acquired</b>                  |                |                |                  |                  |
| Equipment                               | 65,113         | 6,659          | 199,800          | 271,572          |
| Customer relationships                  | 30,168         | 62,880         | 189,715          | 282,763          |
| Re-acquired franchise rights            | 80,448         | 272,480        | 189,715          | 542,643          |
| Goodwill                                | 118,055        | 66,602         | 911,631          | 1,096,288        |
| Other current assets                    | 1,203          | 1,769          | 12,626           | 15,598           |
|   | <u>294,987</u> | <u>410,390</u> | <u>1,503,487</u> | <u>2,208,864</u> |
| <b>Consideration given</b>              |                |                |                  |                  |
| Cash                                    | 282,771        | 400,009        | 1,535,439        | 2,218,219        |
| Promissory notes                        | —              | —              | 97,853           | 97,853           |
| Settlement of pre-existing relationship | —              | —              | (149,775)        | (149,775)        |
| Acquisition costs                       | 12,216         | 10,381         | 19,970           | 42,567           |
|   | <u>294,987</u> | <u>410,390</u> | <u>1,503,487</u> | <u>2,208,864</u> |
| <b>Contingent consideration</b>         | <u>35,196</u>  | <u>52,352</u>  | <u>—</u>         | <u>87,548</u>    |

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements December 31, 2010 and 2009

(expressed in Canadian dollars)

### 3 Acquisition of franchises (continued)

The Company is committed to pay contingent consideration in respect of both the Syracuse and Albany acquisitions, if either of the franchises achieves certain performance targets for the period ending June 30, 2011. In accordance with GAAP, contingent consideration is not recorded until the contingent element has been resolved.

Subsequent to the acquisitions, the Company settled the Syracuse contingent consideration with a payment of US\$25,000 and made interim payments towards the Albany contingent consideration totalling US\$9,091 for the year ended December 31, 2010. These amounts have been capitalised to goodwill on the respective acquisition. Any additional contingent consideration in respect of Albany will be capitalised to goodwill when the contingent element is resolved, but is not expected to exceed an additional US\$40,862.

### 4 Notes receivable from franchisees

Notes receivable arise from the financing of the initial franchise fee by franchisees, are guaranteed by the respective owners of the franchises, bear interest rates ranging from 5.25% to 6.25% per annum with monthly blended payments of principal and interest ranging from US\$526 to US\$1,797, commenced between dates ranging from November 1, 2009 to October 1, 2010 and mature between dates ranging from October 1, 2011 to March 13, 2013. The amounts receivable as at December 31, 2010 and 2009 are as follows:

|                                | 2010<br>\$ | 2009<br>\$ |
|--------------------------------|------------|------------|
| Principal                      | 194,670    | 207,559    |
| Less: Allowance for impairment | 52,787     | 43,333     |
| Less: Current portion          | 33,178     | 24,445     |
|                                | 108,705    | 139,781    |

The Company has recorded an allowance for impairment against a note receivable based on the present value of expected future cash flows using a discount rate equal to the effective interest rate on the note receivable prior to the Company ceasing to accrue interest charges. Significant judgment was exercised by management in making this estimate. As such, actual losses could differ from the estimate.

Notes receivable from franchisees past due comprise:

|                      | 30 days<br>\$ | 60 days<br>\$ | 90 days<br>or more<br>\$ | Total<br>\$ |
|----------------------|---------------|---------------|--------------------------|-------------|
| At December 31, 2010 | 2,759         | 2,736         | 109,578                  | 115,073     |
| At December 31, 2009 | 2,618         | 2,596         | 24,785                   | 29,999      |

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

December 31, 2010 and 2009

(expressed in Canadian dollars)

### 5 Equipment

|  |                  |                     | <b>2010</b>         |
|--|------------------|---------------------|---------------------|
|  | <b>Cost</b>      | <b>Accumulated</b>  | <b>Net carrying</b> |
|  | <b>\$</b>        | <b>amortization</b> | <b>amount</b>       |
|  |                  | <b>\$</b>           | <b>\$</b>           |
| Computer equipment                         | 90,364           | (78,695)            | 11,669              |
| Furniture and fixtures                     | 53,103           | (38,258)            | 14,845              |
| Computer software                          | 432,534          | (407,782)           | 24,752              |
| Bins and shredding containers              | 29,755           | (2,350)             | 27,405              |
| Shredding vehicles – chassis               | 312,365          | (19,248)            | 293,117             |
| Shredding vehicles – shredding compartment | 364,586          | (44,551)            | 320,035             |
| Recycling equipment                        | 6,344            | (1,586)             | 4,758               |
|  | <b>1,289,051</b> | <b>(592,470)</b>    | <b>696,581</b>      |

|                        |                |                     | <b>2009</b>         |
|------------------------|----------------|---------------------|---------------------|
|                        | <b>Cost</b>    | <b>Accumulated</b>  | <b>Net carrying</b> |
|                        | <b>\$</b>      | <b>amortization</b> | <b>amount</b>       |
|                        |                | <b>\$</b>           | <b>\$</b>           |
| Computer equipment     | 77,266         | (66,989)            | 10,277              |
| Furniture and fixtures | 47,610         | (21,823)            | 25,787              |
| Computer software      | 432,534        | (263,600)           | 168,934             |
|                        | <b>557,410</b> | <b>(352,412)</b>    | <b>204,998</b>      |

The Company acquired equipment as part of the franchise acquisitions per note 3. The Company also purchased \$6,608 in computer equipment, \$10,357 in bins and shredding containers and \$458,854 in shredding vehicles during the year ended December 31, 2010, to operate its existing operations. The Company did not acquire any equipment in 2009.

### 6 Deferred financing charges

Effective November 27, 2009, the Company arranged a \$4 million revolving line of credit facility with a five-year term (see note 10). Costs associated with this facility of \$110,431, including warrants issued (see note 8 (f)), are being charged to expenses over the five year term of the facility on a straight-line basis.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements December 31, 2010 and 2009

(expressed in Canadian dollars)

### 7 Intangible assets

|   |                  |                     |                    | <b>2010</b>         |
|---|------------------|---------------------|--------------------|---------------------|
|   | <b>Cost</b>      | <b>Accumulated</b>  | <b>Accumulated</b> | <b>Net carrying</b> |
|   | <b>\$</b>        | <b>amortization</b> | <b>write-down</b>  | <b>amount</b>       |
|   |                  | <b>\$</b>           | <b>\$</b>          | <b>\$</b>           |
| Franchise agreements                    | 2,743,924        | (759,347)           | (147,778)          | 1,836,799           |
| ProShred system                         | 978,000          | (277,100)           | –                  | 700,900             |
| Trademarks and<br>intellectual property | 1,672,500        | (473,887)           | –                  | 1,198,613           |
| Re-acquired franchise<br>rights         | 529,205          | (28,327)            | –                  | 500,878             |
| Customer relationships                  | 274,588          | (4,993)             | –                  | 269,595             |
| Goodwill                                | 1,142,841        | –                   | –                  | 1,142,841           |
|   | <b>7,341,058</b> | <b>(1,543,654)</b>  | <b>(147,778)</b>   | <b>5,649,626</b>    |

  

|   |                  |                     |                    | <b>2009</b>         |
|---|------------------|---------------------|--------------------|---------------------|
|   | <b>Cost</b>      | <b>Accumulated</b>  | <b>Accumulated</b> | <b>Net carrying</b> |
|   | <b>\$</b>        | <b>amortization</b> | <b>write-down</b>  | <b>amount</b>       |
|   |                  | <b>\$</b>           | <b>\$</b>          | <b>\$</b>           |
| Franchise agreements                    | 2,883,800        | (528,694)           | (155,311)          | 2,199,795           |
| Proshred system                         | 978,000          | (179,300)           | –                  | 798,700             |
| Trademarks and<br>intellectual property | 1,672,500        | (306,631)           | –                  | 1,365,869           |
|   | <b>5,534,300</b> | <b>(1,014,625)</b>  | <b>(155,311)</b>   | <b>4,364,364</b>    |

As a result of the acquisition of the Syracuse, Albany, and Milwaukee locations, customer relationships, re-acquired franchise rights and goodwill were recorded (see note 3) in 2010.

The Company's franchise agreements, intangible assets, customer lists, re-acquired franchise rights and goodwill are denominated in US dollars and are subject to foreign currency fluctuations. The Company's foreign currency translation gains and losses on other intangible assets are a component of accumulated other comprehensive income or loss.

Intangible assets with a finite life are tested for impairment when events or changes in circumstances indicate their carrying value may not be recoverable. When the undiscounted cash flows of the assets are less than the carrying value of the asset, a write-down is required. There was no impairment required to be recorded in 2010. In 2009 one franchisee ceased their operations, materially affecting the value of future cash flows related to that franchise agreement. At December 31, 2009, the Company assessed the intangible assets for impairment and recorded a write-down of intangible assets of US\$152,000 due to impairment.

**RediShred Capital Corp.**  
Notes to Consolidated Financial Statements  
December 31, 2010 and 2009

(expressed in Canadian dollars)

**8 Capital stock**

**a) Authorized**

Unlimited number of common shares, without nominal or par value  
Unlimited number of preferred shares, without nominal or par value

**b) Issued and fully paid**

The following table summarizes the changes in issued common shares of the Company:

|  | Common stock      |                  | Warrants         |                | Total<br>\$      |
|--|-------------------|------------------|------------------|----------------|------------------|
|  | Number            | \$               | Number           | \$             |                  |
| <b>Balance, December 31, 2008</b>          | 22,884,614        | 7,650,565        | -                | -              | 7,650,565        |
| Shares issued on acquisition of subsidiary | 6,000,044         | 683,033          | 3,000,000        | 216,974        | 900,007          |
| Shares issued for cash                     | -                 | -                | 1,000,000        | 83,800         | 83,800           |
| Share issue costs                          | -                 | (35,996)         | -                | (12,568)       | (48,564)         |
| <b>Balance, December 31, 2009 and 2010</b> | <b>28,884,658</b> | <b>8,297,602</b> | <b>4,000,000</b> | <b>288,206</b> | <b>8,585,808</b> |

**c) Details of share issuances**

On March 17, 2008, the Company issued 9,615,383 common shares for cash of \$5,000,002. In addition, 3,269,231 common shares valued at \$1,700,000 were issued to Professional Shredding Partnership as part of consideration for the purchase of PSC; as at December 31, 2010, 490,385 common shares (2009 – 1,471,154) owned by Professional Shredding Partnership are held in escrow. As at December 31, 2010, a total of 1,389,635 common shares (2009 – 4,168,904) are held in escrow and will be released in future periods with the Escrow Agreement. Subsequent to year-end, on March 19, 2011, the remaining 1,389,635 common shares were released from escrow.

On December 23, 2009, the Company issued 6,000,044 common shares for cash of \$900,007. Of the 6,000,044 common shares issued, existing directors and officers of the Company purchased 3,000,044 common shares at a price of \$0.15 per common share. The Company also granted warrants to acquire 3,000,000 common shares in connection with the issuance (see note 8 (f)) but not to any existing directors and officers. The 6,000,044 common shares had a 4 month holding period from date of issuance. On the same day, the Company granted warrants in connection with the line of credit, entitling the lender to acquire 1,000,000 common shares (see note 8 (f)).

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements December 31, 2010 and 2009

(expressed in Canadian dollars)

### 8 Capital stock (continued)

#### d) Weighted average common shares

The basic weighted average number of common shares outstanding for the year ended December 31, 2010, was 28,884,658 (2009 - 23,016,122).

#### e) Stock options

Under the terms of the stock option plan:

- i) From time to time, the Company designates eligible participants to whom options will be granted and the number of shares to be optioned to each;
- ii) Eligible participants are persons who are directors, officers, employees and technical consultants of the Company;
- iii) Options to purchase shares are non-transferable and are exercisable for a period of up to five years from the date of grant;
- iv) Shares to be optioned shall not exceed 2,888,465 and the total number of shares to be optioned to any eligible participant shall not exceed 10% of the issued and outstanding shares of the class as at the date such option is granted;
- v) The option price for the shares is determined at the time of granting of the option but cannot be less than the fair market value of the shares at the time the option is granted less any applicable discount permitted by the Toronto Venture Exchange; and
- vi) The term during which any option granted may be exercised is determined by the Company at the time the option is granted but may not exceed the maximum period permitted from time to time by the Toronto Venture Exchange.

The following table summarizes the movements in the Company's stock options during the year:

|                                 | 2010              |                                    | 2009              |                                    |
|---------------------------------|-------------------|------------------------------------|-------------------|------------------------------------|
|                                 | Number of options | Weighted average exercise price \$ | Number of options | Weighted average exercise price \$ |
| Outstanding – Beginning of year | 1,673,349         | 0.34                               | 2,050,849         | 0.33                               |
| Granted                         | 360,000           | 0.14                               | –                 | –                                  |
| Forfeited                       | (100,000)         | 0.20                               | (107,500)         | 0.52                               |
| Expired                         | (340,849)         | 0.50                               | (270,000)         | 0.20                               |
| Outstanding – End of year       | <u>1,592,500</u>  | 0.26                               | <u>1,673,349</u>  | 0.34                               |

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

December 31, 2010 and 2009

(expressed in Canadian dollars)

### 8 Capital stock (continued)

#### e) Stock options (continued)

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

|                      |              |                                     |   | <b>2010</b>            |                                     | <b>2009</b>   |                        |
|----------------------|--------------|-------------------------------------|---|------------------------|-------------------------------------|---|------------------------|
| Exercise price<br>\$ | Issue date   | Number of<br>options<br>outstanding | Weighted<br>average<br>remaining<br>contractual<br>life (yrs) | Options<br>exercisable | Number of<br>options<br>outstanding | Weighted<br>average<br>remaining<br>contractual<br>life (yrs) | Options<br>exercisable |
| 0.20                 | Aug 29, 2007 | 875,000                             | 1.66  | 875,000                | 975,000                             | 2.66  | 975,000                |
| 0.52                 | Mar 17, 2008 | 352,500                             | 2.21  | 177,500                | 352,500                             | 3.21  | 88,125                 |
| 0.52                 | Mar 17, 2008 | —                                   | —   | —                      | 335,849                             | 0.21  | 335,849                |
| 0.60                 | May 26, 2008 | 5,000                               | 2.40  | 5,000                  | 10,000                              | 3.40  | 2,500                  |
| 0.14                 | May 27, 2010 | 350,000                             | 3.40  | 350,000                | —                                   | —   | —                      |
| 0.15                 | Oct 19, 2010 | 10,000                              | 4.81  | —                      | —                                   | —   | —                      |
|                      |              | <u>1,592,500</u>                    | 2.16  | <u>1,407,500</u>       | <u>1,673,349</u>                    | 2.29  | <u>1,401,474</u>       |

The compensation charge for the options issued was determined based on the fair value of the options at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

|                         | <b>2010</b> |
|-------------------------|-------------|
| Expected option life    | 4 years     |
| Risk-free interest rate | 2.78%       |
| Expected dividend yield | nil         |
| Expected volatility     | 214%        |

360,000 options were granted during the twelve months ended December 31, 2010 (2009 - \$nil). The weighted average grant-date fair value of options granted during 2010 amounted to \$0.12 per option. The net stock compensation charge, after adjusting for stock option forfeitures, amounted to \$87,222 (2009 - \$18,991).

**RediShred Capital Corp.**  
Notes to Consolidated Financial Statements  
**December 31, 2010 and 2009**

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(expressed in Canadian dollars)

**8 Capital stock** (continued)

**f) Warrants**

The Company issued two tranches of warrants in 2009. The first tranche was issued in connection with the private placement and the second relates to the line of credit obtained. Details are as follows:

|           |                       |   |                                   | <b>2010</b>           |
|-----------|-----------------------|---|-----------------------------------|-----------------------|
|           | <b>Exercise price</b> | <b>Number of warrants outstanding or to be issued</b> | <b>Remaining contractual life</b> | <b>Assigned value</b> |
|           | <b>\$</b>             |   |                                   | <b>\$</b>             |
| Tranche 1 | 0.25 to 0.45          | 3,000,000   | 3.98 years                        | 204,406               |
| Tranche 2 | 0.25 to 0.45          | 1,000,000   | 3.90 years                        | 83,800                |

The fair values for both tranches of warrants was determined using the following assumptions under the Black-Scholes option pricing model:

|                         |         |
|-------------------------|---------|
| Expected warrant life   | 5 years |
| Risk-free interest rate | 1.06%   |
| Expected dividend yield | nil     |
| Expected volatility     | 234%    |

In connection with the line of credit, 1,000,000 warrants were issued on April 28, 2010 when the line of credit was first drawn upon in accordance with the line of credit agreement. These warrants were recorded in the consolidated financial statements in 2009 as performance by the counterparty was complete at that date. The fair value of these warrants has been recorded as deferred finance charges and is being amortized into income over the term of the facility and is also subject to a two year holding period commencing on the date of issuance. This is a non-cash transaction and has been excluded from the consolidated statements of cash flows.

Tranches 1 and 2 of warrants expire on November 27, 2014 and December 23, 2014, respectively.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

December 31, 2010 and 2009

(expressed in Canadian dollars)

### 9 Income taxes

The following table reconciles the expected income taxes payable (recoverable) at the statutory income tax rate to the amounts recognized in the statements of operations for the years ended December 31, 2010 and 2009:

|   | <b>2010</b><br>\$ | <b>2009</b><br>\$ |
|---|-------------------|-------------------|
| Loss before income taxes                          | (1,285,490)       | (2,158,043)       |
| Income tax rate                                   | 31%               | 33%               |
| Expected income tax recovery based on above rates | (398,000)         | (712,000)         |
| Other non-deductible expenses                     | 41,000            | 23,000            |
| Increase in valuation allowance                   | 239,000           | 721,000           |
| Effect on changing income tax rates and other     | 50,000            | (187,000)         |
| Provision for income taxes                        | <u>(68,000)</u>   | <u>(155,000)</u>  |

Provision for (recovery of) income taxes is comprised of:

|                                 | <b>2010</b><br>\$ | <b>2009</b><br>\$ |
|---------------------------------|-------------------|-------------------|
| Current income taxes            | 20,000            | -                 |
| Future income taxes             | (327,000)         | (876,000)         |
| Increase in valuation allowance | 239,000           | 721,000           |
|                                 | <u>(68,000)</u>   | <u>(155,000)</u>  |

The following reflects the components of future income tax assets at December 31, 2010 and 2009:

|  | <b>2010</b><br>\$  | <b>2009</b><br>\$  |
|--|--------------------|--------------------|
| <b>Future tax assets</b>                                     |                    |                    |
| Non-capital losses carried forward                           | 1,232,000          | 997,000            |
| Deductible share issue costs                                 | 68,000             | 81,000             |
| Other  | 83,000             | 29,000             |
|  | <u>1,383,000</u>   | <u>1,107,000</u>   |
| Less: Valuation allowance                                    | <u>(1,332,000)</u> | <u>(1,093,000)</u> |
|  | <u>51,000</u>      | <u>14,000</u>      |
| <b>Future tax liabilities</b>                                |                    |                    |
| Accounting value of intangible assets in excess of tax value | (561,000)          | (660,000)          |
| Accounting value of equipment in excess of tax value         | (23,000)           | -                  |
|  | <u>(584,000)</u>   | <u>(660,000)</u>   |
| <b>Net future tax liability</b>                              | <u>(533,000)</u>   | <u>(646,000)</u>   |

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

December 31, 2010 and 2009

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(expressed in Canadian dollars)

### 9 Income taxes (continued)

The Company has accumulated losses for Canadian income tax purposes of approximately \$4,917,000, which may be carried forward and used to reduce taxable income in future years. These losses expire as follows:

|                               | \$        |
|-------------------------------|-----------|
| Year ending December 31, 2026 | 6,000     |
| 2027                          | 63,000    |
| 2028                          | 1,752,000 |
| 2029                          | 1,943,000 |
| 2030                          | 1,153,000 |

The Corporation has undeducted share issuance costs of approximately \$223,000 which will be deducted from Canadian taxable income over the next four years.

### 10 Long-term debt

|                | 2010<br>\$ | 2009<br>\$ |
|----------------|------------|------------|
| Line of credit | 2,790,000  | —          |

The line of credit was entered into on November 27, 2009 for a maximum amount of \$4 million, repayable on November 27, 2014, bearing interest at a fixed rate of 10% per annum, and secured by a general security agreement over the Company's assets. Deferred financing charges in respect of this facility will be charged to expense over the term of the facility (see note 6).

### 11 Commitments and contingency

#### Commitments

As of August 1, 2008, the Company leases office premises in Mississauga, Ontario, Canada. The lease expires on September 30, 2013. Additionally, the Company leases facilities in Albany, which expires on March 31, 2011, Syracuse, which expires on August 31, 2015 and Milwaukee, which expires on May 31, 2010. Future minimum lease payments for the Company are as follows:

|                               | \$      |
|-------------------------------|---------|
| Year ending December 31, 2011 | 169,592 |
| 2012                          | 159,989 |
| 2013                          | 114,122 |
| 2014                          | 12,246  |
| 2015                          | 8,164   |

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

#### 11 Commitments and contingency (continued)

##### Contingency

On June 18, 2010, three franchisees filed a complaint with the United States District Court, South District of New York, which management of the Company believes is without merit. The Complaint has listed the following causes of action, (1) breach of contract and breach of the implied covenant of good faith and fair dealing by PFC, (2) fraudulent misrepresentation by PFC, (3) negligent misrepresentation by PFC, and (4) violation of various state laws by PFC. These franchisees are located in Florida, North Carolina and Wisconsin. On July 13, 2010, one additional franchisee located in New York State joined the aforementioned complaint. On December 31, 2010, in conjunction with the purchase of the ProShred Wisconsin business by RAI, the Wisconsin franchisee permanently withdrew from the legal complaint.

The Company intends to vigorously defend against this claim. The Company is strongly of the view that it (1) has not breached any contracts or agreements with its franchisees and has acted in good faith with all franchisees, (2) has not made any fraudulent misrepresentations to any franchisees, (3) has not made any negligent misrepresentations to any franchisees, and (4) has complied with all state laws as well as Federal Trade Commission rules and regulations regarding franchising.

The final outcome with respect to this claim cannot be predicted nor can the costs to defend this claim be quantified with certainty and therefore there can be no assurance that its resolution will not have an adverse effect on the Company's consolidated financial position. No amounts have been accrued in these consolidated financial statements relating to this claim.

#### 12 Financial risk management

The Company has various financial assets that consist of: cash, accounts receivable and notes receivable from franchisees. The Company's financial liabilities include accounts payable, accrued liabilities and notes payable.

The Company, through its financial assets and liabilities, has exposure to the following risks from its use of financial instruments: interest rate risk, credit risk, liquidity risk and currency risk. Senior management is responsible for setting acceptable levels of risk and reviewing risk management activities as necessary.

##### Interest rate risk

The Company's cash earns interest at prevailing and fluctuating market rates. The Company manages its exposure to interest rate risk through fixed rate lending to franchisees. The fixed rate notes receivable from franchisees are subject to interest rate pricing risk, as the value will fluctuate as a result of changes in market rates.

The Company has a line of credit facility that has a fixed interest rate of 10% per annum; the Company has no other interest bearing debt.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

## 12 Financial risk management (continued)

### Credit risk

In accordance with its investment policy, the Company maintains cash deposits with banks. The credit risk on cash is limited because the counterparties are banks with high-credit ratings assigned by international credit-rating agencies.

#### *Receivables from franchisees*

The accounts receivable from franchisees are exposed to credit risk from the possibility that franchisees may experience financial difficulty. The Company mitigates the risk of credit loss by limiting its exposure to any one franchisee. Credit assessments are conducted with respect to all new franchisees and all existing franchisees. In addition, the receivable balances are monitored on an ongoing basis with the result that the Company's exposure to bad debt is not significant. As of December 31, 2010, 6 franchisees accounted for 61% of the accounts receivable balance (December 31, 2009 – 6 franchises accounted for 66%). For the year ended December 31, 2010, 3 franchisees accounted for 32% of the Company's revenues (December 31, 2009 – 34%). As of December 31, 2010, 26% of accounts receivable was over 90 days old and related to one franchise (December 31, 2009 – 17% of accounts receivable was over 90 days old and related to two franchises).

#### *Receivables from shredding customers*

The accounts receivable are exposed to credit risk from the possibility that customers may experience financial difficulty. The Company mitigates the risk of credit loss by limiting its exposure to any one customer. All new customers are required to make payments for services by way of preapproved credit card, and credit is extended only after a credit assessment is conducted. In addition, the receivable balances with customers are monitored on an ongoing basis with the result that the Company's exposure to bad debt is not significant. At December 31, 2010, no customer accounted for more than 10% of the accounts receivable balance. For the twelve months ended December 31, 2010, no customer accounted for more than 10% of the Company's revenues in this category.

As of December 31, 2010, 10% of accounts receivable in this category was over 90 days old.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

#### 12 Financial risk management (continued)

##### Currency risk

The Company incurs revenue primarily in US currency and both expenses in US and Canadian currency and as such, is subject to fluctuations as a result of foreign exchange rate variation. The Company manages its exposure to currency risk by billing for its services in US currency and in the underlying currency related to the expenditure.

The following financial instruments denominated in US funds have been translated at December 31, 2010, at an exchange rate of 0.9985 (2009 - 1.0494):

|  | 2010<br>\$ | 2009<br>\$ |
|--|------------|------------|
| Cash                                     | 463,591    | 239,726    |
| Accounts receivable                      | 214,494    | 246,253    |
| Prepaid expenses                         | 32,304     | -          |
| Notes receivable from franchisees        | 142,096    | 156,495    |
| Accounts payable and accrued liabilities | (285,345)  | (90,251)   |

Since the Company's foreign subsidiaries are considered self-sustaining, unrealized foreign exchange fluctuations are recorded in accumulated other comprehensive income (loss) and are only recorded in net income once realized on liquidation of the subsidiary.

At December 31, 2010, and assuming that all other variables remain constant, a 10% rise or fall in the Canadian dollar against the US dollar would have resulted in approximately \$18,500 increase (decrease) in the income before taxes or in other comprehensive income for the year.

##### Liquidity risk

The Company's objective is to have sufficient liquidity to meet liabilities when due. The Company monitors its cash balances and cash flows generated from operations to meet requirements. Based on overall cash generation capacity and overall financial position, while there can be no assurance, management believes the Company will be able to meet financial obligations as they come due while maintaining compliance with all financial covenants. The accounts payable and accrued liabilities and notes payable of \$613,348 at December 31, 2010 (2009 - \$340,021), are due to be settled within one year from the balance sheet date.

The Company also has cash of \$988,592 at December 31, 2010 and access to a \$4 million line of credit, of which \$2.79 million has been utilized at December 31, 2010, to be used for acquisitions as well as general corporate purposes.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

### December 31, 2010 and 2009

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(expressed in Canadian dollars)

#### 12 Financial risk management (continued)

##### Fair value of financial instruments

The carrying value amounts of many of the Company's financial instruments, including cash, accounts receivable, accounts payable and accrued liabilities approximate their value due primarily to the short-term maturity of the related instruments. The fair value estimates of the Company's notes receivable from franchisees (note 4), are made as at a specific point in time based on estimates using present value or other valuation techniques. These techniques involve uncertainties and are affected by the assumptions used and the judgments made regarding risk characteristics of various financial instruments, discount rates, estimates of future cash flows, future expected loss experience and other factors. The carrying value of the Company's notes receivable from franchisees at December 31, 2010, amounted to \$194,670 (2009 - \$207,559) with fair value estimated to amount to \$121,008 (2009 - \$130,399).

##### Carrying value of financial instruments

|  | 2010<br>\$  | 2009<br>\$ |
|--|-------------|------------|
| Held-for-trading                                 | 988,592     | 1,086,036  |
| Loans and receivables measured at amortized cost | 566,793     | 485,814    |
| Financial liabilities measured at amortized cost | (3,403,130) | (340,021)  |

#### 13 Capital management

The Company defines capital as shareholders' equity. The primary objective of the Company's capital management is to ensure that it maintains a conservative capital ratio in order to support its business and maximize shareholder value. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may issue new shares or issue debt securities.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements

December 31, 2010 and 2009

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(expressed in Canadian dollars)

### 14 Segmented information

The Company operates two reportable operating segments, (1) the granting and managing of shredding business franchises under the "ProShred" trademark (Franchising operations), and (2) the operation of corporately owned shredding businesses (Corporate operations).

Geographic information is as follows:

|   | 2010<br>\$ | 2009<br>\$ |
|---|------------|------------|
| <b>Equipment and other intangibles used in operations</b> |            |            |
| <b>Canada</b>   |            |            |
| Equipment   | 40,670     | 204,998    |
| Other intangible assets                                   | 1,899,513  | 2,164,569  |
| <b>United States</b>                                      |            |            |
| Equipment   | 655,912    | —          |
| Other intangible assets                                   | 3,750,113  | 2,199,795  |

### Revenue

All revenues were attributed to the United States with the exception of the \$250,000 license fee (2009 - \$nil), which was attributed to the Middle East region.

# RediShred Capital Corp.

## Notes to Consolidated Financial Statements December 31, 2010 and 2009

(expressed in Canadian dollars)

### 14 Segmented information (continued)

|                                  | For the year ended December 31, 2010 |                              |                 |             |
|----------------------------------|--------------------------------------|------------------------------|-----------------|-------------|
|                                  | Franchising<br>and licensing<br>\$   | Corporate<br>locations<br>\$ | Corporate<br>\$ | Total<br>\$ |
| Revenue                          | 1,290,052                            | 713,711                      | –               | 2,003,763   |
| Direct costs                     | –                                    | (438,580)                    | –               | (438,580)   |
| Corporate overhead               | (1,084,969)                          | (90,340)                     | (485,547)       | (1,660,856) |
| Depreciation and amortization    | (662,969)                            | (108,424)                    | (58,887)        | (830,280)   |
| Unrealized foreign currency gain | –                                    | –                            | (141,625)       | (141,625)   |
| Loss on purchase of Wisconsin    | –                                    | (149,775)                    | –               | (149,775)   |
| Interest expense                 | –                                    | (73,082)                     | –               | (73,082)    |
| Interest income                  | 4,945                                | –                            | –               | 4,945       |
| Income tax (expense) recovery    | 68,000                               | –                            | –               | 68,000      |
| Net loss                         | (384,941)                            | (146,490)                    | (686,059)       | (1,217,490) |

|                      | As at December 31, 2010            |                              |                 |             |
|----------------------|------------------------------------|------------------------------|-----------------|-------------|
|                      | Franchising<br>and licensing<br>\$ | Corporate<br>locations<br>\$ | Corporate<br>\$ | Total<br>\$ |
| Equipment            | 23,675                             | 655,911                      | 16,995          | 696,581     |
| Total assets         | 4,495,112                          | 2,898,651                    | 631,533         | 8,025,296   |
| Capital expenditures | –                                  | 468,941                      | 6,608           | 475,549     |
| Goodwill             | –                                  | 1,142,841                    | –               | 1,142,841   |
| Goodwill Additions   | –                                  | 1,142,841                    | –               | 1,142,841   |

### 15 Related party balances and transactions

A Director of the Company is the owner of the Tampa, Florida ProShred franchise. Included in accounts and notes receivable at December 31, 2010, is \$9,141 (December 31, 2009 - \$14,332) due from the Director's franchise. During the twelve months ended December 31, 2010, the Company earned royalty and service fee amounts of \$79,560 (December 31, 2009 - \$78,443).

Included in general, administrative and marketing expense for the twelve months ended December 31, 2010 are insurance premium amounts of \$16,929 (December 31, 2009 - \$16,879) paid to Alfred J. Bell & Grant Ltd, a company owned by a Director of the Company.

All related party transactions have been recorded at their exchange amounts.

