RediShred Capital Corp.

Consolidated Interim Financial Statements
March 31, 2012 and 2011
(Unaudited – Prepared by Management)

(expressed in Canadian dollars)

May 30, 2012

In accordance with National Instrument 51-102, released by the Canadian Securities Administrators, the Corporation discloses that its auditors have not reviewed the unaudited consolidated interim financial statements for the period ended March 31, 2012.

RediShred Capital Corp.

Consolidated Statements of Financial Position

As at March 31, 2012 and December 31, 2011

(Unaudited – expressed in Canadian dollars)

	March 31, 2012 $	December 31, 2011 $
Assets		
Current assets		
Cash	344,182	3,011,786
Cash attributable to the Ad Fund (note 3)	64,675	137,818
Accounts receivable	619,097	460,114
Prepaid expenses	86,466	63,596
Notes receivable from franchisees	50,321	62,859
Income taxes recoverable	10,348	17,603
Total current assets	1,175,089	3,753,776
Non-current assets		
Notes receivable from franchisees	170,329	183,619
Equipment (note 5)	1,146,431	565,294
Deferred financing charges	60,737	66,259
Intangible assets (note 6)	4,392,355	3,558,806
Goodwill (notes 7)	1,401,599	878,270
Total assets	8,346,540	9,006,024
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	683,653	686,167
Current portion of notes payable	82,294	22,028
Deferred revenue	–	10,170
Current portion of long-term debt (note 8)	53,406	53,176
Total current liabilities	819,353	771,541
Non-current liabilities		
Long-term debt (note 8)	5,528,362	5,544,805
Notes payable (note 4)	162,927	–
Deferred tax liability	384,912	410,110
Total liabilities	6,895,554	6,726,456
Shareholders' Equity	1,450,986	2,279,568
Total liabilities and shareholders' equity	8,346,540	9,006,024

Commitments and contingency (note 13)

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

RediShred Capital Corp.

Consolidated Statements of Comprehensive Loss

For the three months ended March 31, 2012 and 2011

(Unaudited – expressed in Canadian dollars)

	2012 **$**	**2011** **$**
Revenue (note 10)	1,101,050	711,192
Corporate operating locations expenses (note 11)	(749,689)	(388,791)
Selling, general and administrative expenses (note 12)	(704,935)	(585,456)
Loss before interest, income taxes and other items	(353,574)	(263,055)
Loss on settlement of pre-existing relationship (note 4)	(350,700)	-
Interest expense	(138,367)	(68,795)
Interest income	481	942
Loss before income taxes	(842,160)	(330,908)
Income taxes	18,690	5,000
Net loss for the period	(823,470)	(325,908)
Other comprehensive income (loss), net of tax		
Foreign currency translation gain (loss)	(5,802)	68,033
Comprehensive loss for the period	(829,272)	(257,875)
Net loss per share		
Basic and diluted	(0.03)	(0.01)
Weighted average number of commons shares outstanding – basic and diluted	28,884,658	28,884,658

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

RediShred Capital Corp.

Consolidated Statements of Changes in Equity

For the three months ended March 31, 2012 and 2011

(Unaudited – expressed in Canadian dollars)

	Capital stock and warrants $ (note 9)	Contributed surplus $	Accumulated other comprehensive income (loss) $	Deficit $	Total shareholders' equity $
Balance – January 1, 2011	8,585,808	297,839	(74,450)	(6,099,581)	2,709,616
Net loss for the period	–	–	–	(325,908)	(325,908)
Other comprehensive income					
Foreign currency translation loss	–	–	68,033	–	68,033
Comprehensive loss for the period	–	–	–	–	(257,875)
Stock-based compensation (note 12)	–	2,096	–	–	2,096
Balance – March 31, 2011	8,585,808	299,935	(6,417)	(6,425,489)	2,453,837
Net loss for the period	–	–	–	(129,175)	(129,175)
Other comprehensive income					
Foreign currency translation gain	–	–	(60,106)	–	(60,106)
Comprehensive loss for the period	–	–	–	–	(189,281)
Stock-based compensation (note 12)	–	15,012	–	–	15,012
Balance – December 31, 2011	8,585,808	314,947	(66,523)	(6,554,664)	2,279,568
Net loss for the period	–	–	–	(823,470)	(823,470)
Other comprehensive income					
Foreign currency translation gain	–	–	(5,802)	–	(5,802)
Comprehensive loss for the period	–	–	–	–	(829,272)
Stock-based compensation (note 12)	–	690	–	–	690
Balance – March 31, 2012	8,585,808	315,637	(72,325)	(7,378,134)	1,450,986

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

RediShred Capital Corp.

Consolidated Statements of Cash Flows

For the three months ended March 31, 2012 and 2011

(Unaudited – expressed in Canadian dollars)

	2012 $	2011 $
Cash provided by (used in)		
Operating activities		
Net loss for the year before income taxes	(842,160)	(330,908)
Items not affecting cash		
Amortization of equipment and intangible assets	268,652	124,373
Stock-based compensation	690	2,097
Unrealized foreign currency loss	109,769	110,437
Allowance for doubtful receivables	(10,121)	–
Impairment of note receivable	15,030	–
Loss on settlement of pre-existing relationship	350,700	–
Interest income	(481)	(942)
Interest expense	138,367	68,795
Interest received	481	636
Income taxes paid	–	(52,019)
	30,927	(77,531)
Net change in non-cash working capital balances		
Decrease (increase) in trade receivables	(156,095)	(137,858)
Decrease (increase) prepaid expenses	(23,867)	(23,999)
Decrease (increase) in income taxes recoverable	7,255	9,946
Increase (decrease) in deferred revenue	(10,170)	–
Increase (decrease) in accounts payable and accrued liabilities	(2,514)	(1,638)
Increase (decrease) in notes payable	223,192	–
	68,728	(231,080)
Financing activities		
Cash paid on current portion of long-term debt	(16,212)	–
Investing activities		
Cash paid on acquisition of franchise	(2,309,508)	–
Increase of notes payable related to the acquisition of franchise	(223,192)	–
Other consideration paid on acquisition of franchise	(94,085)	–
Cash held by Ad Fund	(64,675)	(96,754)
Purchase of capital assets	(35,571)	(13,586)
Collection of notes receivable from franchisees	6,911	27,078
	(2,720,120)	(83,262)
Effect of foreign exchange rate changes on cash	(8,442)	(14,325)
Net change in cash for the period	(2,659,162)	(300,017)
Cash – Beginning of the period	3,011,786	988,592
Cash – End of the period	344,182	674,250

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

(Unaudited – expressed in Canadian dollars)

1 Corporate information and nature of operations

RediShred Capital Corp. ("Redishred" or the "Company") was incorporated under the Canada Business Corporations Act on October 18, 2006 and is domiciled in Canada. 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. Redishred's common shares are listed for trading on the TSX Venture Exchange under the symbol "KUT". The registered address of the Company is 6790 Century Avenue, Suite 200, Mississauga, Ontario, L5N 2V8.

Redishred manages and operates the Proshred brand and business platform ("system") in the United States and internationally (with the exception of Canada). Redishred operates the Proshred system under three business models, (1) franchising in the United States, (2) via direct ownership of shredding trucks and facilities in four locations in the United States and, (3) licensing internationally.

These condensed consolidated interim financial statements comprise the financial statements of Redishred and its subsidiaries as at March 31, 2012. Together, Redishred and its subsidiaries are referred to as "the Company."

The condensed consolidated interim financial statements of the Company for the three months ended March 31, 2012 were authorized for issue in accordance with a resolution of the Directors on May 30, 2012.

2 Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting.* The condensed consolidated interim financial statements should be read in conjunction with the most recently issued Annual Report of Redishred for the year ended December 31, 2011, which includes information necessary or useful to understanding the Company's business and financial statement presentation.

The Company's significant accounting policies were presented as Note 3 to the Audited Consolidated Financial Statements for the year ended December 31, 2011 and have been consistently applied in the preparation of these interim financial statements.

The results reported in these interim consolidated financial statements should not be regarded as necessarily indicative of results that may be expected for the entire year. Certain prior period amounts have been reclassified to conform to the current period's presentation.

These interim consolidated financial statements of the Company have been prepared on a going concern basis, under the historical cost convention and are presented in Canadian dollars, which is Redishred's presentation currency.

(Unaudited – expressed in Canadian dollars)

3 Cash attributable to the Ad Fund

The Company manages an advertising fund (the "Ad Fund") established to collect and administer funds, based on a percentage of each location's revenue, contributed by franchisees and Company owned and operated locations. It is used for regional and national advertising and marketing programs as well as initiatives designed to increase sales and enhance general public recognition, acceptance and use of the Proshred System. As at March 31, 2012, the Ad Fund was in a net surplus position of $99,589 (December 31, 2011 - $160,100), with cash attributable to the Ad Fund amounting to $64,675 (December 31, 2011 - $137,818) included in the Company's cash balance.

4 Acquisition of franchise

On January 1, 2012, the Company, through its wholly-owned subsidiary, Redishred Acquisition Inc., acquired the Proshred New York City franchise. Redishred conducted the acquisition to increase the Company's cash flows, and to establish a regional headquarters in the market. This will allow for further expansion by way of additional acquisitions or by way of establishing satellite offices in nearby cities.

The business combination resulted in the recognition of goodwill of $548,183, determined on the basis of an allocation of the purchase price to the assets acquired (including all identifiable intangible assets arising from the purchase) based on their estimated fair value at the date of acquisition.

Goodwill from the business combination represents synergies the Company is expected to generate; the assembled workforces of skilled employees that are knowledgeable about the Company's procedures and possess expertise in certain fields that are important to continued profitability and growth; the rights to the entire geographical areas of New York City, Long Island and surrounding counties; the growth potentials in outlying areas; and the ability to secure regional contracts.

The following table outlines the assets purchased and consideration given on the closing date of the acquisition:

	New York City **$**
Assets acquired	
Equipment	628,355
Customer relationships	231,835
Re-acquired franchise rights	857,892
Goodwill	548,183
	2,266,265
Consideration given	
Cash	2,297,925
Promissory notes	229,793
Settlement of accounts receivable	96,002
Total	**2,623,720**
Settlement of pre-existing relationship	(357,455)
	2,266,265
Acquisition costs (expensed in statement of comprehensive loss)	44,755

(Unaudited – expressed in Canadian dollars)

4 Acquisition of franchise (continued)

The Company translated the fair values of all assets acquired using the exchange rate on the date of the acquisition. The acquisition was translated at $1USD = $1.0213CAD.

The promissory notes are due on an annual basis from the closing date over the next three years, payable in the amount of US$75,000.

The fair values of the assets were determined on the basis of observable market prices, where possible. The fair values of intangible assets and goodwill were determined using income-oriented approaches involving estimating the level of future cash flows anticipated from the customer relationships in excess of the cash flow that might otherwise be expected to be generated by the franchise if it did not have access to these existing customer relationships and using a multi-period excess earnings method to value reacquired franchise rights.

5 Equipment

Cost	**Computer equipment**	**Furniture & fixtures**	**Bins & shredding containers**	**Shredding vehicles - chassis**	**Shredding vehicles - box**	**Recycling equipment**	**Vehicles**	**Total**
	$	**$**	**$**	**$**	**$**	**$**	**$**	**$**
As at January 1, 2011	90,544	53,110	30,853	212,939	464,013	6,356	–	857,815
Additions	702	–	19,728	2,691	–	–	6,700	29,821
Foreign exchange	122	93	903	3,991	8,597	106	114	13,926
As at December 31, 2011	91,368	53,203	51,484	219,621	472,610	6,462	6,814	901,562
Acquisitions	7,500	5,750	160,000	56,500	296,000	80,000	9,500	615,250
Additions	20,997	–	12,342	–	2,200	–	–	35,539
Foreign exchange	108	53	(333)	(3,425)	(7,215)	(30)	(99)	(10,941)
As at March 31, 2012	119,973	59,006	223,493	272,696	763,595	86,432	16,215	1,541,410

Accumulated depreciation and impairment	**Computer equipment**	**Furniture & fixtures**	**Bins & shredding containers**	**Shredding vehicles - chassis**	**Shredding vehicles - box**	**Recycling equipment**	**Vehicles**	**Total**
	$	**$**	**$**	**$**	**$**	**$**	**$**	**$**
As at January 1, 2011	81,404	48,185	2,449	19,010	44,672	1,589	–	197,309
Depreciation	6,808	1,811	8,396	37,387	75,474	3,177	2,233	135,286
Foreign exchange	252	43	87	1,184	1,988	81	38	3,673
As at December 31, 2011	88,464	50,039	10,932	57,581	122,134	4,847	2,271	336,268
Depreciation	1,780	938	10,935	11,393	29,957	5,263	1,033	61,299
Foreign exchange	(72)	99	(162)	(971)	(1,907)	460	(35)	(2,588)
As at March 31, 2012	90,172	51,076	21,705	68,003	150,184	10,570	3,269	394,979
Net book value								
As at December 31, 2011	2,904	3,164	40,552	162,040	350,476	1,615	4,543	565,294
As at March 31, 2012	29,801	7,930	201,788	204,693	613,411	75,862	12,946	1,146,431

(Unaudited – expressed in Canadian dollars)

5 Equipment (continued)

The Company acquired equipment as part of the franchise acquisition entered into on January 1, 2012 (see note 4). The Company also purchased computers, bins, shredding containers and handheld devices during the three months ended March 31, 2012. During the year ended December 31, 2011, the Company purchased bins, shredding containers and a vehicle. The foreign exchange adjustment is a result of the translation of corporate equipment from US dollars to Canadian dollars at March 31, 2012 and December 31, 2011. Depreciation related to the corporate stores is included in the statement of comprehensive loss in "corporate operating expenses." Depreciation related to the franchising and licensing business is included in the statement of comprehensive loss in "selling, general & administrative expenses."

6 Intangible assets

Cost	Franchise agreements	Proshred system	Computer software	Trademarks and intellectual property	Re-acquired franchise rights	Customer relationships	Total
	$	$	$	$	$	$	$
As at January 1, 2011	2,743,927	978,000	432,534	1,672,500	529,205	274,588	6,630,754
Foreign exchange	46,649	–	–	–	9,805	5,088	61,542
As at December 31, 2011	2,790,576	978,000	432,534	1,672,500	539,010	279,676	6,692,296
Acquisitions	–	–	–	–	840,000	227,000	1,067,000
Foreign exchange	(67,480)	–	–	–	(7,777)	(4,224)	(79,481)
As at March 31, 2012	2,723,096	978,000	432,534	1,672,500	1,371,233	502,452	7,679,815

Accumulated amortization and impairment	Franchise agreements	Proshred system	Computer software	Trademarks and intellectual property	Re-acquired franchise rights	Customer relationships	Total
	$	$	$	$	$	$	$
As at January 1, 2011	1,051,426	688,655	429,520	1,248,176	28,327	4,891	3,450,955
Amortization	236,445	40,374	3,014	59,208	132,857	27,492	499,390
Reversal of impairment	(75,546)	(322,860)	–	(439,359)	–	–	(837,765)
Foreign exchange	17,425	–	–	–	2,783	662	20,870
As at December 31, 2011	1,229,750	406,169	432,534	868,025	163,967	33,045	3,133,490
Amortization	62,175	23,177	–	32,614	69,214	12,548	199,728
Foreign exchange	(42,713)	–	–	–	(2,532)	(513)	(45,758)
As at March 31, 2012	1,249,212	429,346	432,534	900,639	230,649	45,080	3,287,460
Net book value							
As at December 31, 2011	1,560,826	571,831	–	804,475	375,043	246,631	3,558,806
As at March 31, 2012	1,473,884	548,654	–	771,861	1,140,584	457,372	4,392,355

(Unaudited – expressed in Canadian dollars)

6 Intangible assets (continued)

As a result of the acquisition of the New York City franchise, the Company recorded customer relationships and re-acquired franchise rights as intangible assets in the first quarter of 2012. The foreign exchange adjustment is a result of the translation of intangible assets denominated in US dollars to Canadian dollars at March 31, 2012 and December 31, 2011.

Amortization of reacquired franchise rights and customer relationships for the year is included in the statement of comprehensive loss in “corporate operating expenses” and amortization of the remaining intangible assets is included in the statement of comprehensive loss in “selling, general and administrative expenses.” The Company’s franchise agreements, customer lists and re-acquired franchise rights are attributed to the Company’s operations in the US.

Intangible assets with a finite life are tested for impairment when events or changes in circumstances indicate their carrying value may not be recoverable. Impairment losses for assets other than goodwill are reversed in future periods if the circumstances that led to the impairment no longer exist. At March 31, 2012, the Company did not record any reversals of previously recorded impairment. At December 31, 2011, the Company recorded a reversal of a portion of the previously reported impairment of $836,919.

7 Goodwill

The following table presents goodwill for the three months ended March 31, 2012 and for the year ended December 31, 2011:

	March 31, 2012	December 31, 2011
	$	$
Opening balance	878,270	1,112,232
Acquisitions (note 4)	536,750	–
Impairment of goodwill	–	(250,494)
Foreign currency translation	(13,421)	16,532
Closing balance	1,401,599	878,270

8 Long-term debt

As at March 31, 2012 and December 31, 2011 long-term debt is comprised of:

	March 31, 2012	December 31, 2011
	$	$
Line of credit	5,370,000	5,370,000
Truck loans	211,768	227,981
Total long-term debt	5,581,768	5,597,981
Less: current portion	53,406	53,176
Total	5,528,362	5,544,805

(Unaudited – expressed in Canadian dollars)

8 Long-term debt (continued)

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. During the year ended December 31, 2010, the Company drew from its line of credit in order to finance the purchase of the Syracuse, Albany and Milwaukee businesses; new shredding vehicles for the Syracuse and Albany markets; and initial working capital for the acquired businesses. On October 31, 2011, the line of credit limit was increased to $5.37 million repayable on November 27, 2014; all other terms of the agreement remained unchanged. During December 2011, the Company drew from its line of credit in order to finance the purchase of the New York City business on January 1, 2012. In March 2012, the line of credit limit was increased by $0.63 million to $6.0 million, repayable on November 27, 2014; all other terms of the agreement remained unchanged.

On November 11, 2011, the Company entered into a loan and security agreement in the amount of US$240,000, repayable on a monthly basis in the amount of US$5,690 principal and interest until October 3, 2015. The loan bears interest at 8.14% per annum and is secured by two shredding vehicles with a carrying value of $322,402.

9 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

For the three months ended March 31, 2012 and March 31, 2011, there were no changes in issued common shares of the Company.

The following are the balances of issued common shares of the Company:

	Common stock		Warrants		
	Number	$	Number	$	Total $
Balance, March 31, 2012 and 2011	28,884,658	8,297,602	4,000,000	288,206	8,585,808

c) Weighted average common shares

The basic weighted average number of common shares outstanding for the quarter ended March 31, 2012, was 28,884,658 (March 31, 2011 - 28,884,658).

(Unaudited – expressed in Canadian dollars)

9 Capital stock (continued)

d) Stock options

At March 31, 2012, the Company has 1,682,500 options outstanding (December 31, 2011 – 1,677,500) and a weighted average exercise price of $0.24 (December 31, 2011 - $0.24). There have been 5,000 stock options granted during the three months ended March 31, 2012 (March 31, 2011 – nil). The net stock compensation charge, after adjusting for stock option forfeitures, amounted to $690 (March 31, 2011 – $2,097).

e) Warrants

The Company issued two tranches of warrants in 2009. The first tranche was issued in connection with the private placement and the second related to the line of credit obtained.

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 financing 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.

10 Revenue

The revenue earned by the Company is broken down as follows:

	For the three months ended	
	March 31, 2012	**March 31, 2011**
	$	**$**
Royalties	201,627	219,428
Franchise fees	93,487	–
Shredding services	641,168	362,323
Sale of paper products	164,768	129,441
Total revenue	1,101,050	711,192

(Unaudited – expressed in Canadian dollars)

11 Corporate operating locations expenses by nature

The corporate operating locations expenses of the Company are broken down as follows:

	For the three months ended	
	March 31, 2012	**March 31, 2011**
	$	**$**
Shredding expenses	161,545	84,209
Employee wages expense	270,505	125,214
Employee benefit expense	55,371	29,299
Office and administration expense	118,123	80,756
Depreciation – equipment	62,219	29,783
Amortization – intangible assets	81,926	39,530
Total corporate operating expenses	749,689	388,791

During the three months ended March 31, 2012, the Company operated four corporate locations – Syracuse, Albany, Milwaukee and New York City. During the three months ended March 31, 2011, the Company operated three corporate locations – Syracuse, Albany and Milwaukee.

12 Selling, general and administrative expenses by nature

The selling, general and administrative expenses of the Company are broken down as follows:

	For the three months ended	
	March 31, 2012	**March 31, 2011**
	$	**$**
Employee wages expense	191,538	195,659
Employee benefits expense	18,658	20,811
Share-based compensation	690	2,097
Professional fees	127,479	98,481
Technology	31,241	29,828
Rent and office expense	17,318	15,499
Selling and marketing	12,061	18,691
Bad debt expense	15,030	14,792
Amortization of deferred financing charges	5,522	5,522
Depreciation – equipment	–	4,727
Amortization – intangible assets	118,985	40,300
Foreign exchange loss	108,696	76,952
Other	57,717	62,097
Total selling, general and administrative expenses	704,935	585,456

(Unaudited – expressed in Canadian dollars)

12 Selling, general and administrative expenses by nature (continued)

Compensation of key management

Included in employee wages and benefits expense above are key management personnel compensation as follows:

	For the three months ended	
	March 31, 2012	**March 31, 2011**
	$	**$**
Wages and benefits	154,793	163,175
Share-based compensation	398	3,070
Total	155,191	166,245

Key management personnel are comprised of the Company's Board of Directors, Chief Executive Officer, Chief Financial Officer, President, Vice President of Operations and former Chief Operating Officer.

13 Commitments and contingency

Commitments

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, 2013; Syracuse, which expires on August 31, 2015; Milwaukee, which expires on May 31, 2013 and New York City, which expires on April 30, 2013. Certain contracts include renewal options for various periods of time. For the three months ended March 31, 2012, the Company incurred $72,032 (March 31, 2011 - $31,257) in lease payments as an expense included in 'selling, general and administrative expenses' and 'corporate operating expenses.'

Non-cancellable operating lease rentals are payable as follows:

	$
Less than 1 year	477,404
Between 1 and 5 years	95,943
More than 5 years	–
Total	573,347

(Unaudited – expressed in Canadian dollars)

13 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 City joined the aforementioned complaint. On December 31, 2010, in conjunction with the purchase of the Proshred Wisconsin business by the Company, the Wisconsin franchisee permanently withdrew from the legal complaint. On January 1, 2012, in conjunction with the purchase of the Proshred New York City business by the Company, the New York City franchisee permanently withdrew from the legal complaint. As of March 31, 2012, two franchisees remain in 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, other than legal costs, have been accrued in these consolidated financial statements relating to this claim.

14 Financial instruments and fair values

The Company has various financial assets that consist of: cash, trade receivables and notes receivable from franchisees. The Company's financial liabilities include accounts payable and accrued liabilities, notes payable and long-term debt. 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, foreign exchange risk and liquidity 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 is subject to cash flow risk, as it earns interest at prevailing and fluctuating market rates. The fixed rate notes receivable from franchisees, and the line of credit facility that has a fixed interest rate of 10% per annum and truck loans that have a fixed interest rate of 8.14% per annum, are subject to interest rate fair value risk, as their fair values will fluctuate as a result of changes in market rates.

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.

(Unaudited – expressed in Canadian dollars)

14 Financial instruments and fair values (continued)

Credit risk (continued)

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 were conducted with respect to all new franchisees and existing franchisees. In addition, the receivable balances are monitored on an ongoing basis. As of March 31, 2012, 6 franchisees accounted for 33% of the accounts receivable balance (December 31, 2011 - 6 franchises accounted for 73%). For the three months ended March 31, 2012, 3 franchisees accounted for 32% of the Company's revenues (March 31, 2011 - 3 franchisees accounted for 29%). As of March 31, 2012, there are no accounts receivable over 90 days old (December 31, 2011 – 37% of accounts receivable were over 90 days old and related to one franchise). The over 90 day old accounts receivable outstanding at year-end was settled as a result of the purchase of the New York City franchise (refer to note 4).

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 March 31, 2012 and December 31, 2011, no customer accounted for more than 10% of the accounts receivable balance. For the three months ended March 31, 2012 and March 31, 2011, no customer accounted for more than 10% of the Company's revenues in this category. As of March 31, 2012, 5% of accounts receivable in this category were over 90 days old (December 31, 2011 – 10%). The Company has not recorded an allowance for credit losses from accounts receivable from shredding customers as the Company does not have any reason to believe it will not collect all remaining balances.

Foreign exchange risk

Since the Company operates internationally, it is exposed to currency risks as a result of potential exchange rate fluctuations related to non-intragroup transactions. The Company earns revenue in US currency and incurs expenses in both US and Canadian currency. 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 Company's principal operations are located in the United States. The results of these operations have been translated into Canadian dollars at an average rate for the period of USD$1.00 = CAD$1.002 (2011 – USD$1.00 = CAD$0.9888). Assets and liabilities have been translated using the exchange rate at the date of the statement of financial position of USD$1.00 = CAD$1.0009 (2011 – USD$1.00 = CAD$1.017). Fluctuations in the Canadian dollar and the US dollar exchange rates could have a potentially significant impact on the Company's results of operations. If there were a foreign exchange rate variation of -5% (depreciation of the USD) and +5% (appreciation of the USD) against the CAD, from an average rate of USD$1.00 = CAD$1.002, the total impact to net loss would be a decrease/increase of approximately $10,000.

(Unaudited – expressed in Canadian dollars)

14 Financial instruments and fair values (continued)

Liquidity risk

The Company's objective is to have sufficient liquidity to meet liabilities when due. The Company has incurred significant losses to date, and has a deficit of $7.3 million at March 31, 2012. Cash flow forecasting is performed by management, which monitors rolling forecasts of the Company's liquidity requirements to ensure it has sufficient cash to meet operational needs at all times. Although management considers its assumptions used in its cash flow forecasts to be reasonable, there is no assurance that the cash flow forecasts will be achieved. 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. The Company does not have any financial covenants to comply with.

The current liabilities of $819,353 at March 31, 2012 (December 31, 2011 - $771,541), are due to be settled within one year from the balance sheet date.

At March 31, 2012, the Company has cash of $344,182 and working capital of $355,731. The Company also has access to a $6 million line of credit, of which $5.37 million has been drawn as of March 31, 2012. The line of credit is repayable on November 27, 2014 and interest payments are due semi-annually.

The table below analyzes the Company's non-derivative financial liabilities into relevant maturity groupings based on the remaining period from the statement of financial position date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. The analysis is based on foreign exchange and interest rates in effect at the consolidated statement of financial position date, and includes both principal and interest cash flows for notes payable and long-term debt.

(Unaudited – expressed in Canadian dollars)

14 Financial instruments and fair values (continued)

Liquidity risk (continued)

Principal	**Less than 3 months $**	**3 months to 1 year $**	**2 – 5 years $**	**Over 5 years $**
Accounts payable and accrued liabilities	683,653	–	–	–
Notes payable	1,551	79,843	163,827	–
Long-term debt	12,861	40,186	5,528,722	–

Interest	**Less than 3 months $**	**3 months to 1 year $**	**2 – 5 years $**	**Over 5 years $**
Notes payable	256	645	762	–
Long-term debt	260,227	324,450	1,041,806	–

Liquidity risk

Total principal and interest	**Less than 3 months $**	**3 months to 1 year $**	**2 – 5 years $**	**Over 5 years $**
Accounts payable and accrued liabilities	683,653	–	–	–
Notes payable	1,807	80,488	164,589	–
Long-term debt	273,088	364,636	6,570,528	–

Fair value of financial instruments

The carrying value amounts of many of the Company’s financial instruments, including cash, trade receivables, trade payables and accrued liabilities, which are all carried at amortized cost, approximate their fair value due primarily to the short-term maturity of the related instruments. The fair value estimates of the Company’s notes receivable from franchisees are made as at a specific point in time based on estimates using present value or other valuation techniques. The carrying value of the Company’s notes payable and long-term debt approximates fair value as the rates are similar to rates currently available to the Company.

These techniques involve uncertainties and are affected by the assumptions used and the judgments made regarding risk characteristics of various financial instruments, discount rates, estimate of future cash flows, future expected loss experience and other factors. The carrying value of the Company’s notes receivable from franchisees at March 31, 2012, amounted to $220,650 (December 31, 2011 - $246,447) with fair value estimated to amount to $215,991 (December 31, 2011 - $225,081), respectively.

(Unaudited – expressed in Canadian dollars)

15 Capital management

The Company defines capital as shareholders' equity. The primary objective of the Company's capital management is to ensure that it maintains the appropriate capital levels 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.

16 Segment reporting

The business segments presented reflect the management structure of the Company and the way in which the Company's management reviews business performance. The Company operates two reportable operating segments, (1) the granting and managing of shredding business franchises under the "Proshred" trademark (Franchising and licensing), and (2) the operation of corporately owned shredding businesses (Corporate locations).

(Unaudited – expressed in Canadian dollars)

16 Segment reporting (continued)

Total assets and liabilities by reportable operating segment are as follows:

	Franchising and licensing		Corporate locations		Total	
	March 31, 2012 $	December 31, 2011 $	March 31, 2012 $	December 31, 2011 $	March 31, 2012 $	December 31, 2011 $
ASSETS						
Current assets						
Cash	171,671	218,286	172,511	2,793,500	344,182	3,011,786
Cash attributable to Ad Fund	64,675	137,818	–	–	64,675	137,818
Trade receivables	223,832	201,972	395,265	258,142	619,097	460,114
Prepaid expenses	58,587	22,789	27,879	40,807	86,466	63,596
Notes receivable from franchisees	50,321	62,859	–	–	50,321	62,859
Income tax recoverable	10,348	17,603	–	–	10,348	17,603
Total current assets	579,434	661,327	595,655	3,092,449	1,175,089	3,753,776
Non-current assets						
Notes receivable from franchisees	170,329	183,619	–	–	170,329	183,619
Equipment	692	–	1,145,739	565,294	1,146,431	565,294
Deferred financing charges	60,737	66,259	–	–	60,737	66,259
Intangible assets	2,794,395	2,937,129	1,597,960	621,677	4,392,355	3,558,806
Goodwill	–	–	1,401,599	878,270	1,401,599	878,270
Total assets	3,605,587	3,848,334	4,740,953	5,157,690	8,346,540	9,006,024
LIABILITIES						
Current liabilities						
Accounts payable and accrued liabilities	116,456	370,980	567,197	315,187	683,653	686,167
Deferred revenue	–	10,170	–	–	–	10,170
Notes payable	–	–	82,294	22,028	82,294	22,028
Current portion of long-term debt	–	–	53,406	53,176	53,406	53,176
Total current liabilities	116,456	381,150	702,897	390,391	819,353	771,541
Non-current liabilities						
Long-term debt	–	–	5,528,362	5,544,805	5,528,362	5,544,805
Notes payable	–	–	162,927	–	162,927	–
Deferred tax liability	384,912	410,110	–	–	384,912	410,110
Total liabilities	501,368	791,260	6,394,186	5,935,196	6,895,554	6,726,456

(Unaudited – expressed in Canadian dollars)

16 Segment reporting (continued)

The Company incurred $653,700 in capital expenditures relating to its corporate operations during the three months ended March 31, 2012 (December 31, 2011- $29,821). The Company incurred $1,585 in capital expenditures relating to its franchising operations for the three months ended March 31, 2012 (December 31, 2011 - $nil). T

Geographic information

	March 31, 2012	December 31, 2011
Canada	**$**	**$**
Equipment	692	–
Deferred financing charges	60,737	66,259
Intangible assets	1,320,515	1,376,307
United States		
Notes receivable from franchisees	220,650	246,477
Equipment	1,145,739	565,294
Intangible assets	3,071,840	2,182,499
Goodwill	1,401,599	878,270
Total		
Notes receivable from franchisees	220,650	246,477
Equipment	1,146,431	565,294
Deferred financing charges	60,737	66,259
Intangible assets	4,392,355	3,558,806
Goodwill	1,401,599	878,270

Revenue

All revenues were attributed to the United States.

(Unaudited – expressed in Canadian dollars)

16 Segment reporting (continued)

Net loss by operating segment

Total net loss by reportable operating segment is as follows:

	For the three months ended March 31, 2012			
	Franchising and licensing $	Corporate locations $	Corporate overhead $	Total $
Revenue	295,114	805,936	–	1,101,050
Direct costs	–	(605,545)	–	(605,545)
Corporate overhead	(312,333)	(68,055)	(91,343)	(471,731)
Loss on pre-existing relationship	(350,700)	–	–	(350,700)
Depreciation and amortization	(124,507)	(144,145)	–	(268,652)
Foreign exchange loss	–	–	(108,696)	(108,696)
Interest expense	–	(138,367)	–	(138,367)
Interest income	481	–	–	481
Income tax recovery	18,690	–	–	18,690
Net income (loss)	(473,255)	(150,176)	(200,039)	(823,470)

	For the three months ended March 31, 2011			
	Franchising and licensing $	Corporate locations $	Corporate overhead $	Total $
Revenue	219,428	491,764	–	711,192
Direct costs	–	(319,479)	–	(319,479)
Corporate overhead	(305,493)	(72,975)	(79,486)	(457,954)
Depreciation and amortization	(50,549)	(69,313)	–	(119,862)
Foreign exchange loss	–	–	(76,952)	(76,952)
Interest expense	–	(68,795)	–	(68,795)
Interest income	942	–	–	942
Recovery of income taxes	5,000	–	–	5,000
Net income (loss)	(130,672)	(38,798)	(156,438)	(325,908)

For the three months ended March 31, 2012, the Company operated four corporate locations. For the three months ended March 31, 2011, the Company operated three corporate locations.

(Unaudited – expressed in Canadian dollars)

17 Related party balances and transactions

A Director of the Company is the owner of the Tampa, Florida Proshred franchise. At March 31, 2012, there is a nil balance included in trade receivables due from the Director's franchise (December 31, 2011 - $1,592). During the three months ended March 31, 2012, the Company earned royalty and service fee amounts of $19,312 (March 31, 2011 - $22,254) from the Director's franchise.

Included in selling, general and administrative expenses for the three months ended March 31, 2012 are insurance premium amounts of $6,650 (March 31, 2011 - $6,450) paid to an insurance brokerage firm owned by a Director of the Company.

All related party transactions have been recorded at their exchange amounts