RediShred Capital Corp.

Consolidated Interim Financial Statements
June 30, 2012 and 2011
(Unaudited – Prepared by Management)

(expressed in Canadian dollars)

August 21, 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 June 30, 2012.

RediShred Capital Corp.

Consolidated Statements of Financial Position

(Unaudited – expressed in Canadian dollars)

As at,	June 30, 2012 $	December 31, 2011 $
Assets		
Current assets		
Cash	256,930	3,011,786
Cash attributable to the Ad Fund (note 3)	11,422	137,818
Accounts receivable	614,753	460,114
Prepaid expenses	73,835	63,596
Notes receivable from franchisees	62,485	62,859
Income taxes recoverable	10,536	17,603
Total current assets	1,029,961	3,753,776
Non-current assets		
Notes receivable from franchisees	145,542	183,619
Equipment (note 4)	1,105,860	565,294
Deferred financing charges	55,216	66,259
Intangible assets (note 5)	4,245,732	3,558,806
Goodwill (notes 6)	1,427,085	878,270
Total assets	8,009,396	9,006,024
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	527,797	686,167
Current portion of notes payable	83,083	22,028
Deferred revenue	–	10,170
Current portion of long-term debt (note 7)	55,492	53,176
Total current liabilities	666,372	771,541
Non-current liabilities		
Long-term debt (note 7)	5,767,033	5,544,805
Notes payable	165,017	–
Deferred tax liability	372,902	410,110
Total liabilities	6,971,324	6,726,456
Shareholders' Equity	1,038,072	2,279,568
Total liabilities and shareholders' equity	8,009,396	9,006,024

Commitments and contingency (note 12)

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

RediShred Capital Corp.
Consolidated Statements of Comprehensive Loss

(Unaudited – expressed in Canadian dollars)	*For the 3 months ended June 30* 2012 $	2011 $	*For the 6 months ended June 30* 2012 $	2011 $
Revenue (note 9)	965,831	827,278	2,066,881	1,538,471
Corporate operating locations expenses (note 10)	(746,806)	(378,075)	(1,496,494)	(766,866)
Selling, general and administrative expenses (note 11)	(513,510)	(625,778)	(1,218,445)	(1,211,234)
Loss before interest, income taxes and other items	(294,485)	(176,575)	(648,058)	(439,629)
Loss on settlement of pre-existing relationship	(1,365)	–	(352,065)	–
Interest expense	(140,199)	(69,559)	(278,566)	(138,353)
Interest income	1,971	551	2,453	1,493
Loss before income taxes	(434,078)	(245,583)	(1,276,236)	(576,489)
Income tax recovery	15,693	1,000	34,383	6,000
Net loss for the period	(418,385)	(244,583)	(1,241,853)	(570,489)
Other comprehensive income (loss), net of tax				
Foreign currency translation gain (loss)	5,258	47,150	(544)	115,182
Comprehensive loss for the period	(413,127)	(197,433)	(1,242,397)	(455,307)
Net loss per share				
Basic and diluted	(0.01)	(0.01)	(0.04)	(0.02)
Weighted average number of commons shares outstanding – basic and diluted	28,884,658	28,884,658	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

(Unaudited – expressed in Canadian dollars)

	Capital stock and warrants $ (note 8)	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	–	–	–	(570,489)	(570,489)
Other comprehensive income					
Foreign currency translation loss	–	–	115,182	–	115,182
Comprehensive loss for the period	–	–	–	–	(455,307)
Stock-based compensation	–	16,156	–	–	16,156
Balance – June 30, 2011	8,585,808	313,995	40,732	(6,670,070)	2,270,465
Net loss for the period	–	–	–	115,406	115,406
Other comprehensive income					
Foreign currency translation gain	–	–	(107,255)	–	(107,255)
Comprehensive loss for the period	–	–	–	–	8,151
Stock-based compensation	–	952	–	–	952
Balance – December 31, 2011	8,585,808	314,947	(66,523)	(6,554,664)	2,279,568
Net loss for the period	–	–	–	(1,241,853)	(1,241,853)
Other comprehensive income					
Foreign currency translation gain	–	–	(544)	–	(544)
Comprehensive loss for the period	–	–	–	–	(1,242,397)
Stock-based compensation	–	901	–	–	901
Balance – June 30, 2012	8,585,808	315,848	(67,067)	(7,796,517)	1,038,072

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

RediShred Capital Corp.

Consolidated Statements of Cash Flows

(Unaudited – expressed in Canadian dollars)

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2012	**2011**	**2012**	**2011**
Cash provided by (used in)	**$**	**$**	**$**	**$**
Operating activities				
Net loss for the period before income taxes	(434,078)	(245,583)	(1,276,236)	(576,489)
Items not affecting cash				
Amortization of equipment and intangible assets	269,646	109,616	538,298	229,596
Stock-based compensation	211	14,061	901	16,158
Unrealized foreign currency loss	(88,132)	151,980	21,637	268,686
Allowance for doubtful receivables	(24,145)	–	(34,266)	–
Impairment of note receivable	59	–	15,089	–
Loss on settlement of pre-existing relationship	1,365	–	352,065	–
Interest income	(1,971)	(551)	(2,452)	(1,493)
Interest expense	140,199	69,559	278,566	138,353
Interest received	1,971	1,052	2,452	1,689
Interest paid	(250,115)	(129,953)	(250,115)	(129,953)
Income taxes paid	–	(2,722)	–	(54,741)
	(384,990)	(32,541)	(354,061)	(108,194)
Net change in non-cash working capital balances				
Decrease (increase) in trade receivables	34,647	(10,290)	(121,448)	(148,148)
Decrease (increase) prepaid expenses	13,623	35,263	(10,243)	11,264
Decrease (increase) in income taxes recoverable	(188)	(9,946)	7,067	–
Increase (decrease) in deferred revenue	–	–	(10,170)	–
Increase (decrease) in accounts payable and accrued liabilities	(155,854)	(143,278)	(158,368)	(144,916)
Increase (decrease) in notes payable	2,880	–	226,072	–
	(489,882)	(160,792)	(421,151)	(389,994)
Financing activities				
Cash paid on current portion of long-term debt	(9,244)	–	(25,456)	–
Borrowings from line of credit facility	250,000	–	250,000	–
	240,756	–	224,544	–
Investing activities				
Cash paid on acquisition of franchise	–	–	(2,309,508)	–
Increase of notes payable related to the acquisition of franchise	(2,880)	–	(226,072)	–
Other consideration paid on acquisition of franchise	–	–	(94,085)	–
Net Ad Fund position	149,151	14,733	84,476	5,834
Purchase of capital assets	(1,161)	(7,707)	(36,732)	(23,171)
Collection of notes receivable from franchisees	16,764	(4,803)	23,672	22,275
Increase of notes receivable from franchisees	–	(27,786)	–	(27,789)
	161,874	(25,563)	(2,558,249)	(22,851)
Effect of foreign exchange rate changes on cash	5,410	(13,153)	(3,032)	(27,478)
Net change in cash for the period	(92,662)	(173,202)	(2,751,824)	(385,364)
Cash – Beginning of the period	344,182	674,250	3,011,786	900,740
Cash – End of the period	256,930	487,895	256,930	487,895

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 June 30, 2012. Together, Redishred and its subsidiaries are referred to as "the Company."

The consolidated financial statements of the Company for the three and six months ended June 30, 2012 were authorized for issue in accordance with a resolution of the Directors on August 21, 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 consolidated 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 consolidated financial statements.

The results reported in these 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 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 June 30, 2012, the Ad Fund was in a net surplus position of $82,051 (December 31, 2011 - $160,100), with cash attributable to the Ad Fund amounting to $11,422 (December 31, 2011 - $137,818) included in the Company's cash balance.

4 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	21,502	–	12,342	–	2,200	–	–	36,044
Foreign exchange	2,299	1,126	3,729	1,533	8,381	1,541	196	18,805
As at June 30, 2012	122,669	60,079	227,555	277,654	779,191	88,003	16,510	1,571,661

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	4,324	1,875	22,142	22,786	60,130	9,589	2,067	122,913
Foreign exchange	2,895	68	447	554	1,400	1,212	44	6,620
As at June 30, 2012	95,683	51,982	33,521	80,921	183,664	15,648	4,382	465,801
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 June 30, 2012	26,986	8,097	194,034	196,733	595,527	72,355	12,128	1,105,860

(Unaudited – expressed in Canadian dollars)

4 Equipment (continued)

The Company acquired equipment as part of the franchise acquisition entered into on January 1, 2012. The Company also purchased computers, bins, shredding containers and handheld devices during the six months ended June 30, 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 June 30, 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.”

5 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	(24,373)	–	–	–	17,157	4,915	(2,301)
As at June 30, 2012	2,766,203	978,000	432,534	1,672,500	1,396,167	511,591	7,756,995

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	124,350	46,362	–	65,226	138,429	25,096	399,463
Foreign exchange	(25,219)	–	–	–	2,982	547	(21,690)
As at June 30, 2012	1,328,881	452,531	432,534	933,251	305,378	58,688	3,511,263
Net book value							
As at December 31, 2011	1,560,826	571,831	–	804,475	375,043	246,631	3,558,806
As at June 30, 2012	1,437,322	525,469	–	739,249	1,090,789	452,903	4,245,732

(Unaudited – expressed in Canadian dollars)

5 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 Company did not acquire any intangible assets during the three months ended June 30, 2012. The foreign exchange adjustment is a result of the translation of intangible assets denominated in US dollars to Canadian dollars at June 30, 2012 and December 31, 2011.

Amortization of reacquired franchise rights and customer relationships for the period 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. For the six months ended June 30, 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.

6 Goodwill

The following table presents goodwill for the six months ended June 30, 2012 and for the year ended December 31, 2011:

	June 30, 2012	December 31, 2011
	$	$
Opening balance	878,270	1,112,232
Acquisitions	536,750	–
Impairment of goodwill	–	(250,494)
Foreign currency translation	12,065	16,532
Closing balance	1,427,085	878,270

7 Long-term debt

As at June 30, 2012 and December 31, 2011 long-term debt is comprised of:

	June 30, 2012	December 31, 2011
	$	$
Line of credit	5,620,000	5,370,000
Truck loans	202,525	227,981
Total long-term debt	5,822,525	5,597,981
Less: current portion	55,492	53,176
Total	5,767,033	5,544,805

(Unaudited – expressed in Canadian dollars)

7 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 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 $318,221.

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

For the three months ended June 30, 2012 and the year ended December 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, June 30, 2012 and December 31, 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 June 30, 2012, was 28,884,658 (December 31, 2011 - 28,884,658).

(Unaudited – expressed in Canadian dollars)

8 Capital stock (continued)

d) Stock options

At June 30, 2012, the Company has 1,687,500 options outstanding (December 31, 2011 – 1,677,500) and a weighted average exercise price of $0.23 (December 31, 2011 - $0.24).

There have been 10,000 stock options granted during the six months ended June 30, 2012 (for the six months ended June 30, 2011 – 140,000). The net stock compensation charge, after adjusting for stock option forfeitures, amounted to $901 (for the six months ended June 30, 2011 – $16,156).

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.

9 Revenue

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

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2012	**2011**	**2012**	**2011**
	$	**$**	**$**	**$**
Royalties	208,285	242,222	409,548	461,650
Franchise fees	–	61,989	93,850	61,989
Shredding services	618,885	365,277	1,260,054	727,600
Sale of paper products	138,661	157,790	303,429	287,232
Total revenue	965,831	827,278	2,066,881	1,538,471

(Unaudited – expressed in Canadian dollars)

10 Corporate operating locations expenses by nature

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

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2012	**2011**	**2012**	**2011**
	$	**$**	**$**	**$**
Shredding expenses	197,196	93,312	358,739	177,522
Employee wages expense	252,049	135,490	522,554	260,703
Employee benefit expense	49,881	26,738	105,252	56,037
Office and administration expense	102,826	49,800	220,950	130,557
Depreciation – equipment	62,291	33,975	124,510	63,757
Amortization – intangible assets	82,563	38,760	164,489	78,290
Total corporate operating expenses	746,806	378,075	1,496,494	766,866

During the six months ended June 30, 2012, the Company operated four corporate locations – Syracuse, Albany, Milwaukee and New York City. During the six months ended June 30, 2011, the Company operated three corporate locations – Syracuse, Albany and Milwaukee.

11 Selling, general and administrative expenses by nature

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

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2012	**2011**	**2012**	**2011**
	$	**$**	**$**	**$**
Employee wages expense	183,811	180,706	375,349	376,365
Employee benefits expense	11,915	15,746	30,573	36,459
Share-based compensation	211	14,061	901	16,158
Professional fees	152,711	121,853	280,190	220,334
Technology	37,308	26,982	68,550	56,810
Rent and office expense	16,765	19,978	34,084	35,477
Selling and marketing	25,491	36,231	37,492	54,921
Bad debt expense	–	14,515	15,089	29,307
Amortization of deferred financing charges	5,522	5,522	11,043	11,044
Depreciation – equipment	–	826	–	5,553
Amortization – intangible assets	119,270	30,533	238,256	70,833
Foreign exchange loss (gain)	(87,059)	87,562	21,637	164,514
Other	47,565	71,363	105,281	133,459
Total selling, general and administrative expenses	513,510	625,778	1,218,445	1,211,234

(Unaudited – expressed in Canadian dollars)

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

Compensation of key management

Included in employee wages and benefits expense in selling, general and administrative expenses is key management personnel compensation as follows:

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2012	**2011**	**2012**	**2011**
	$	**$**	**$**	**$**
Wages and benefits	146,996	149,837	297,368	301,927
Share-based compensation	61	11,980	459	19,269
Total	147,057	161,817	297,827	321,196

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.

12 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 six months ended June 30, 2012, the Company incurred $143,735 (June 30, 2011 - $54,185) 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	279,033
Between 1 and 5 years	73,385
More than 5 years	–
Total	352,418

(Unaudited – expressed in Canadian dollars)

12 Commitments and contingency (continued)

Contingency

During the second quarter of 2010, four 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 Proshred Franchising Corp. ("PFC"), (2) fraudulent misrepresentation by PFC, (3) negligent misrepresentation by PFC, and (4) violation of various state laws by PFC. As of June 30, 2012, two franchisees remained in the legal complaint and two franchisees had permanently withdrew from the legal complaint in conjunction with the Company purchasing their Proshred business. Subsequent to the second quarter, on July 13, 2012, the Company announced that in conjunction with the purchase of the Proshred Miami business, the Miami franchisee permanently withdrew from the legal complaint. As of August 21, 2012, one franchisee remains in the legal complaint.

The Company intends to vigorously defend against this remaining 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.

13 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 interest rate 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.

(Unaudited – expressed in Canadian dollars)

13 Financial instruments and fair values (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 were conducted with respect to all new franchisees and existing franchisees. In addition, the receivable balances are monitored on an ongoing basis. As of June 30, 2012, 3 franchisees accounted for 38% of the accounts receivable balance (December 31, 2011 - 3 franchises accounted for 50%). For the six months ended June 30, 2012, 3 franchisees accounted for 31% of the Company's revenues in this category (June 30, 2011 - 3 franchisees accounted for 29%). As of June 30, 2012, there is 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 on January 1, 2012.

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 June 30, 2012 and December 31, 2011, no customer accounted for more than 10% of the accounts receivable balance. For the six months ended June 30, 2012 and June 30, 2011, no customer accounted for more than 10% of the Company's revenues in this category. As of June 30, 2012, 12% 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. 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$1.0059 (June 30, 2011 – USD$1.00 = CAD$0.9769). Assets and liabilities have been translated using the exchange rate at the date of the statement of financial position of USD$1.00 = CAD$1.0191 (June 30, 2011 – USD$1.00 = CAD$0.9765). 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 $10,500.

(Unaudited – expressed in Canadian dollars)

13 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 $7.8 million at June 30, 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 $666,372 at June 30, 2012 (December 31, 2011 - $771,541), are due to be settled within one year from the balance sheet date.

At June 30, 2012, the Company has cash of $256,930 and working capital of $363,589. The Company also has access to a $6 million line of credit, of which $5.62 million has been drawn as of June 30, 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)

13 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	527,797	–	–	–
Notes payable	1,600	81,359	165,142	–
Long-term debt	13,363	41,755	5,767,407	–

Interest	**Less than 3 months $**	**3 months to 1 year $**	**2 – 5 years $**	**Over 5 years $**
Notes payable	237	584	592	–
Long-term debt	3,979	616,671	800,006	–

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	527,797	–	–	–
Notes payable	1,837	81,943	165,734	–
Long-term debt	17,342	658,426	6,567,413	–

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 June 30, 2012, amounted to $208,027 (December 31, 2011 - $246,447) with fair value estimated to amount to $203,283 (December 31, 2011 - $225,081), respectively.

(Unaudited – expressed in Canadian dollars)

14 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.

15 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)

15 Segment reporting (continued)

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

	Franchising and licensing		Corporate locations		Total	
	June 30, 2012 $	December 31, 2011 $	June 30, 2012 $	December 31, 2011 $	June 30, 2012 $	December 31, 2011 $
ASSETS						
Current assets						
Cash	79,026	218,286	177,904	2,793,500	256,930	3,011,786
Cash attributable to Ad Fund	11,422	137,818	–	–	11,422	137,818
Trade receivables	193,349	201,972	421,404	258,142	614,753	460,114
Prepaid expenses	52,603	22,789	21,232	40,807	73,835	63,596
Notes receivable from franchisees	62,485	62,859	–	–	62,485	62,859
Income tax recoverable	10,536	17,603	–	–	10,536	17,603
Total current assets	409,421	661,327	620,540	3,092,449	1,029,961	3,753,776
Non-current assets						
Notes receivable from franchisees	145,542	183,619	–	–	145,542	183,619
Equipment	–	–	1,105,860	565,294	1,105,860	565,294
Deferred financing charges	55,216	66,259	–	–	55,216	66,259
Intangible assets	2,702,039	2,937,129	1,543,693	621,677	4,245,732	3,558,806
Goodwill	–	–	1,427,085	878,270	1,427,085	878,270
Total assets	3,312,218	3,848,334	4,697,178	5,157,690	8,009,396	9,006,024
LIABILITIES						
Current liabilities						
Accounts payable and accrued liabilities	389,266	370,980	138,531	315,187	527,797	686,167
Deferred revenue	–	10,170	–	–	–	10,170
Notes payable	–	–	83,083	22,028	83,083	22,028
Current portion of long-term debt	–	–	55,492	53,176	55,492	53,176
Total current liabilities	389,266	381,150	277,106	390,391	666,372	771,541
Non-current liabilities						
Long-term debt	–	–	5,767,033	5,544,805	5,767,033	5,544,805
Notes payable	–	–	165,017	–	165,017	–
Deferred tax liability	372,902	410,110	–	–	372,902	410,110
Total liabilities	762,168	791,260	6,209,156	5,935,196	6,971,324	6,726,456

(Unaudited – expressed in Canadian dollars)

15 Segment reporting (continued)

The Company incurred $653,700 in capital expenditures relating to its corporate operations during the six months ended June 30, 2012 (for the year ended December 31, 2011- $29,821). The Company incurred $1,585 in capital expenditures relating to its franchising operations for the six months ended June 30, 2012 (for the year ended December 31, 2011 - $nil).

Geographic information

	June 30, 2012	December 31, 2011
Canada	**$**	**$**
Equipment	–	–
Deferred financing charges	55,216	66,259
Intangible assets	1,264,718	1,376,307
United States		
Notes receivable from franchisees	208,027	246,477
Equipment	1,105,860	565,294
Intangible assets	2,981,014	2,182,499
Goodwill	1,427,085	878,270
Total		
Notes receivable from franchisees	208,027	246,477
Equipment	1,105,860	565,294
Deferred financing charges	55,216	66,259
Intangible assets	4,245,732	3,558,806
Goodwill	1,427,085	878,270

Revenue

All revenues were attributed to the United States.

(Unaudited – expressed in Canadian dollars)

15 Segment reporting (continued)

Net loss by operating segment

Total net loss by reportable operating segment is as follows:

	For the three months ended June 30, 2012			
	Franchising and licensing $	Corporate locations $	Corporate overhead $	Total $
Revenue	208,285	757,546	–	965,831
Direct costs	–	(601,949)	–	(601,949)
Corporate overhead	(259,151)	(70,577)	(146,052)	(475,779)
Loss on pre-existing relationship	–	(1,365)	–	(1,365)
Depreciation and amortization	(124,792)	(144,854)	–	(269,646)
Foreign exchange gain	–	–	87,059	87,059
Interest expense	–	(140,199)	–	(140,199)
Interest income	1,971	–	–	1,971
Income tax recovery	15,693	–	–	15,693
Net income (loss)	(157,994)	(201,398)	(58,993)	(418,385)

	For the three months ended June 30, 2011			
	Franchising and licensing $	Corporate locations $	Corporate overhead $	Total $
Revenue	304,211	523,068	–	827,279
Direct costs	–	(305,341)	–	(305,341)
Corporate overhead	(336,226)	(33,353)	(131,756)	(501,335)
Depreciation and amortization	(39,761)	(69,855)	–	(109,616)
Foreign exchange loss	–	–	(87,562)	(87,652)
Interest expense	–	(69,559)	–	(69,559)
Interest income	551	–	–	551
Income tax recovery	1,000	–	–	1,000
Net income (loss)	(70,225)	44,960	(219,318)	(244,583)

(Unaudited – expressed in Canadian dollars)

15 Segment reporting (continued)

Net loss by operating segment (continued)

	For the six months ended June 30, 2012			
	Franchising and licensing	**Corporate locations**	**Corporate overhead**	**Total**
	$	**$**	**$**	**$**
Revenue	503,399	1,563,482	–	2,066,881
Direct costs	–	(1,207,494)	–	(1,207,494)
Corporate overhead	(571,484)	(138,632)	(237,394)	(947,510)
Depreciation and amortization	(249,299)	(288,999)	–	(538,298)
Foreign exchange loss	–	–	(21,637)	(21,637)
Interest expense	–	(278,566)	–	(278,566)
Interest income	2,453	–	–	2,453
Income tax recovery	34,383	–	–	34,383
Loss on pre-existing relationship	–	(352,065)	–	(352,065)
Net income (loss)	(280,548)	(702,274)	(259,031)	(1,241,853)

	For the six months ended June 30, 2011			
	Franchising and licensing	**Corporate locations**	**Corporate overhead**	**Total**
	$	**$**	**$**	**$**
Revenue	523,639	1,014,832	–	1,538,471
Direct costs	–	(624,700)	–	(624,700)
Corporate overhead	(639,285)	(106,329)	(213,794)	(959,408)
Depreciation and amortization	(87,430)	(142,048)	–	(229,478)
Foreign exchange loss	–	–	(164,514)	(164,514)
Interest expense	–	(138,353)	–	(138,353)
Interest income	1,493	–	–	1,493
Income tax recovery	6,000	–	–	6,000
Net income (loss)	(195,583)	3,402	(378,308)	(570,489)

For the three and six months ended June 30, 2012, the Company operated four corporate locations. For the three and six months ended June 30, 2011, the Company operated three corporate locations.

(Unaudited – expressed in Canadian dollars)

16 Related party balances and transactions

A Director of the Company is the owner of the Tampa, Florida Proshred franchise. At June 30, 2012, there is a balance of $785 included in trade receivables due from the Director's franchise (December 31, 2011 - $1,592). During the six months ended June 30, 2012, the Company earned royalty and service fee amounts of $39,423 (June 30, 2011 - $39,965) from the Director's franchise.

Included in selling, general and administrative expenses for the six months ended June 30, 2012 are insurance premium amounts of $9,843 (June 30, 2011 - $12,450) paid to an insurance brokerage firm owned by a Director of the Company and $3,142 in recruiting services paid to a recruiting firm owned by a Director of the Company.

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

17 Subsequent events

i) On July 13, 2012, the Company completed the acquisition of the assets of Sunshine State Shredding LLC, from an existing Proshred franchisee in Miami for an aggregate purchase price of $405,000 USD. The Company satisfied the purchase price in part by setting off approximately $270,000 USD owed by the vendor and an additional $15,000 USD of the purchase price is subject to earn-out. The Company funded the $120,000 USD balance of the purchase price by drawing from its line of credit facility. In conjunction with the purchase of the business, the exiting franchisee withdrew from the legal complaint filed against the Company in June 2010.

The Company is in the process of allocating the assets acquired. The preliminary purchase price allocation is as follows:

	$
Assets acquired	
Equipment	22,460
Customer lists	86,777
Re-acquired franchise rights	122,508
	231,745
Consideration given	
Cash	122,507
Contingent consideration	15,314
Settlement of accounts and notes receivable	275,643
Total	**413,464**
Settlement of pre-existing relationship	(181,720)
	231,744
Acquisition costs (expensed in statement of comprehensive loss)	7,092

ii) On August 13, 2012, the Company entered into an agreement with a new franchisee to operate a Proshred shredding business in Houston, Texas. The franchise fee associated with this new franchise will be recognized in the third quarter of 2012. The Company expects its new franchise to commence operations in the fourth quarter of 2012.