RediShred Capital Corp.

Consolidated Financial Statements
December 31, 2013 and 2012

(expressed in Canadian dollars)

April 29, 2013

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 International Financial Reporting Standards 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 are 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.

Grant Thornton 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

Grant Thornton

Grant Thornton LLP
Suite 300
3600 Dundas Street
Burlington, ON
L7M 4B8
T +1 289 313 0300
F +1 289 313 0355
www.GrantThornton.ca

Independent auditor's report

To the Shareholders of RediShred Capital Corp.

We have audited the accompanying consolidated financial statements of RediShred Capital Corp. which comprise the consolidated statements of financial position as at December 31, 2013 and 2012, and the statements of consolidated comprehensive loss, changes in equity and cash flows for the years then ended December 31, 2013 and 2012, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of 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 financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation and fair presentation of the 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 company'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 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 consolidated financial position of RediShred Capital Corp. as at December 31, 2013 and 2012, and its financial performance and its cash flows for the years ended December 31, 2013 and 2012 in accordance with International Financial Reporting Standards.

Grant Thornton LLP

Burlington, Canada
April 29, 2014

Chartered Accountants
Licensed Public Accountants

RediShred Capital Corp.

Consolidated Statements of Financial Position

As at December 31, 2013 and 2012

(expressed in Canadian dollars)

	December 31, 2013 $	December 31, 2012 $
Assets		
Current assets		
Cash	348,998	532,040
Cash attributable to the Advertising Fund (note 5)	63,375	48,031
Trade receivables (note 6)	448,982	424,064
Prepaid expenses	98,018	97,949
Notes receivable from franchisees (note 7)	148,633	40,765
	1,108,006	1,142,849
Non-current assets		
Notes receivable from franchisees (note 7)	166,112	193,669
Equipment (note 9)	2,195,083	1,267,395
Intangible assets (note 10)	4,059,247	3,342,242
Goodwill (notes 11 and 12)	1,455,467	1,361,705
	7,875,909	6,165,011
Total assets	8,983,915	7,307,860
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 14)	606,508	504,510
Current portion of notes payable	112,804	81,383
Deferred revenue (note 15)	57,966	–
Current portion of long-term debt (note 16)	648,004	138,302
Contingent consideration	5,318	14,924
	1,430,600	739,119
Non-current liabilities		
Long-term debt (note 16)	7,476,411	6,359,020
Long-term notes payable	98,452	137,410
Deferred tax liability (note 22)	214,350	214,188
Convertible debenture (note 18)	337,882	333,119
	8,127,095	7,043,737
Total liabilities	9,557,695	7,782,856
Shareholders' Deficiency		
Capital stock	8,585,808	8,585,808
Contributed surplus	372,479	367,957
Accumulated other comprehensive loss	(134,400)	(71,561)
Deficit	(9,397,667)	(9,357,200)
	(573,780)	(474,996)
Total liabilities and shareholders' deficiency	8,983,915	7,307,860

Commitments and contingency (note 23)

Subsequent events (note 28)

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

Approved on behalf of the Board of Directors

(signed) "*Phillip H. Gaunce*" Director (signed) "*Brad Foster*" Director

RediShred Capital Corp.

Consolidated Statements of Comprehensive Loss

For the years ended December 31, 2013 and 2012

(expressed in Canadian dollars)

	2013 $	2012 $
Revenue (note 19)	4,669,083	4,078,560
Corporate operating locations expenses (note 20)	(2,746,466)	(2,808,588)
Selling, general and administrative expenses (note 21)	(1,861,491)	(2,565,820)
Income (loss) before interest, income taxes and other items	61,126	(1,295,848)
Reversal of impairment/(Impairment) of intangible assets (note 12)	431,180	(312,904)
Impairment of goodwill (note 12)	–	(232,103)
Gain on re-acquired rights (Note 8)	–	138,439
Gains (losses) related to business combinations (note 8 and 10)	148,228	(712,567)
Gain on sale of assets (note 9)	2,240	7,540
Income (loss) before interest and income taxes	642,774	(2,407,443)
Interest expense	(712,098)	(595,146)
Interest income	7,055	4,785
Loss before income taxes	(62,269)	(2,997,804)
Income tax recovery (note 22)	21,802	195,268
Net loss for the year	(40,467)	(2,802,536)
Other comprehensive loss		
Foreign currency translation loss	(62,839)	(5,038)
Comprehensive loss for the year	(103,306)	(2,807,574)
Net loss per share		
Basic and diluted	(0.00)	(0.10)
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 financial statements.

RediShred Capital Corp.

Consolidated Statements of Changes in Equity

For the years ended December 31, 2013 and 2012

(expressed in Canadian dollars)

	Capital stock and warrants $ (note 17)	Contributed surplus $	Accumulated other comprehensive income (loss) $	Deficit $	Total shareholders' equity/(deficiency) $
Balance – January 1, 2012	8,585,808	314,947	(66,523)	(6,554,664)	2,279,568
Net loss for the year	–	–	–	(2,802,536)	(2,802,536)
Other comprehensive income					
Foreign currency translation loss	–	–	(5,038)	–	(5,038)
Comprehensive loss for the year	–	–	–	–	(2,807,574)
Issue of convertible debentures (net of costs) (note 18)	–	20,077	–	–	20,077
Stock-based compensation (note 17)	–	32,933	–	–	32,933
Balance – December 31, 2012	8,585,808	367,957	(71,561)	(9,357,200)	(474,996)
Net loss for the year	–	–	–	(40,467)	(40,467)
Other comprehensive income					
Foreign currency translation loss	–	–	(62,839)	–	(62,839)
Comprehensive loss for the year	–	–	–	–	(103,306)
Stock-based compensation (note 17)	–	4,522	–	–	4,522
Balance – December 31, 2013	8,585,808	372,479	(134,400)	(9,397,667)	(573,780)

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, 2013 and 2012

(expressed in Canadian dollars)

Cash provided by (used in)	2013 $	2012 $
Operating activities		
Net loss for the year	(40,467)	(2,802,536)
Items not affecting cash		
Amortization of equipment and intangible assets	997,313	1,024,758
Stock-based compensation	4,522	32,933
Unrealized foreign currency (gain) loss	(388,141)	11,836
Impairment of goodwill	–	232,103
Impairment (reversal) of impairment of intangibles	(431,180)	312,904
Impairment of note receivable	14,001	–
Gain on acquisition	(144,194)	–
Loss on settlement of pre-existing litigation	–	712,566
Gain on re-acquired rights	–	(138,439)
Gain on sale of assets	(2,240)	(7,540)
Income tax recovery	(21,802)	(195,268)
	(12,188)	(816,683)
Net change in non-cash working capital balances		
(Increase) decrease in trade receivables	(24,918)	36,050
(Increase) decrease in prepaid expenses	(69)	(12,355)
(Increase) decrease in notes receivable from franchisees	(80,310)	12,043
Decrease in income taxes recoverable	–	17,603
Increase (decrease) in deferred revenue	57,966	(10,170)
Increase (decrease) in accounts payable and accrued liabilities	101,998	(239,009)
Net cash from (used in) used in continuing operations	42,479	(1,012,521)
Financing activities		
Borrowings from long-term debt	1,472,325	909,651
Repayment of long-term debt	(234,529)	(73,653)
Repayment of notes payable	(7,537)	(36,551)
Proceeds from convertible debentures (net of transaction costs)	–	353,198
	1,230,259	1,152,645
Investing activities		
Cash paid on acquisition of franchises	(1,284,875)	(2,414,260)
(Increase) decrease in cash held by advertising fund	(15,344)	89,787
Proceeds from sale of equipment	53,200	–
Purchase of capital assets	(219,454)	(285,349)
	(1,466,473)	(2,609,822)
Effect of foreign exchange rate changes on cash	10,693	(10,048)
Net change in cash for the year	(183,042)	(2,479,746)
Cash – Beginning of year	532,040	3,011,786
Cash – End of year	348,998	532,040

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

(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. Redishred's common shares are listed for trading on the TSX Venture Exchange under the symbol "KUT". The registered address of the Company is 6559 Mississauga Road, Mississauga, Ontario, L5N 1A6.

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 six locations in the United States, as of December 31, 2013 and, (3) licensing internationally.

2 Basis of presentation

These annual consolidated financial statements have been prepared in compliance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board. The Company has consistently applied the accounting policies used in the preparation of its IFRS statement of financial position at December 31, 2013 and December 31, 2012.

These consolidated financial statements comprise the financial statements of Redishred and its subsidiaries as at December 31, 2013. Together, Redishred and its subsidiaries are referred to as "the Company."

The consolidated financial statements of the Company for the year ended December 31, 2013 were authorized for issue in accordance with a resolution of the Directors on April 29, 2014.

3 Significant accounting policies

The significant accounting policies used in the preparation of these consolidated financial statements are as follows:

Basis of measurement

These consolidated financial statements were prepared on a going concern basis, under the historical cost convention. The consolidated financial statements are presented in Canadian dollars, which is Redishred's presentation currency.

Basis of consolidation

These consolidated financial statements include the accounts of Redishred and its subsidiaries, which are entities controlled by Redishred. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefit from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date control ceases. All significant intercompany balances and transactions have been eliminated.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

The Company's wholly-owned subsidiaries include:

Subsidiary name:	Incorporated in:	Functional currency:
Professional Shredding Corporation	Ontario, Canada	Canadian Dollar
Proshred Franchising Corp.	Delaware, United States	US Dollar
Redishred Holdings US Inc.	Delaware, United States	US Dollar
Redishred Acquisition Inc.	Delaware, United States	US Dollar
Proshred Charlotte Inc.	Delaware, United States	US Dollar

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker is responsible for allocating resources and assessing performance of the operating segments and has been identified as the chief executive officer of Redishred.

Foreign currency translation

The Company's functional currency is Canadian dollars and the Company has elected to use the Canadian dollar as its presentation currency. The functional currency of the Company's foreign subsidiaries, Proshred Franchising Corp. ("PFC"), Redishred Holdings US Inc. ("RHI"), Redishred Acquisition Inc. ("RAI") and Proshred Charlotte Inc. ("PCI") is the US dollar, as it is the currency of the primary economic environment in which they operate. These consolidated financial statements have been translated to the Canadian dollar in accordance with *IAS 21, The Effects of Changes in Foreign Exchange Rates*.

The financial statements of subsidiaries that have a functional currency different from that of Redishred Capital Corp. ("foreign operations") are translated into Canadian dollars as follows: assets and liabilities - at the closing rate at the date of the statements of financial position and income and expenses - at the average rate of the period (as this is considered a reasonable approximation of actual rates prevailing at the transaction dates). All resulting changes are recognized in other comprehensive income as foreign currency translation adjustments.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in currencies other than an entity's functional currency are recognized in the statement of comprehensive loss in selling, general and administrative expenses.

Cash

The Company's cash balances are held in bank accounts in Canada and the United States, which the Company has full access to. Refer to note 26 for cash balances by operating segment.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognized when the obligation specified in the contract is discharged, cancelled or expires. Financial assets and liabilities are initially recognized at fair value and are subsequently accounted for based on their classification as described below. Transaction costs in respect of an asset or liability not recorded at fair value through net earnings are added to the initial carrying amount. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Except in very limited circumstances, the classification is not changed subsequent to initial recognition.

i) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's financial instruments categorized as loans and receivables are comprised of cash, trade receivables and note receivables from franchisees. Loans and receivables are initially recognized at the amount expected to be received, less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, these instruments are accounted for at amortized cost using the effective interest rate method less a provision for impairment.

ii) Financial liabilities at amortized cost

Financial liabilities at amortized cost include accounts payable, accrued liabilities, notes payable, convertible debentures and long-term debt. Accounts payable and accrued liabilities are initially recognized at the amount required to be paid, less, when material, a discount to reduce the payables to fair value. Subsequently, accounts payable and accrued liabilities are measured at amortized cost using the effective interest method. Long-term debt, notes payable and convertible debentures are recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method. They are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

Impairment of financial assets

At each reporting date, the Company assesses whether there is objective evidence that a financial asset is impaired.

The criteria used to determine if objective evidence of an impairment loss exists include:

(i) significant financial difficulty of the obligor;

(ii) delinquencies in interest or principal payments; and

(iii) if it becomes probable that the borrower will enter bankruptcy or other financial reorganization.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

Impairment of financial assets (continued)

If such evidence exists, the Company recognizes an impairment loss as follows:

Financial assets carried at amortized cost: The loss is the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

Equipment and amortization

Equipment is stated at cost less accumulated depreciation and accumulated impairment losses. The cost consists of expenditures directly attributable to the acquisition of the asset including costs directly attributable to bringing the asset to the location and condition necessary for its intended use. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost can be measured reliably. Maintenance and repair costs are expensed as incurred.

Depreciation is provided for on a straight-line basis over the estimated useful lives of the assets as follows:

Computer equipment	2-5 years
Furniture and fixtures	3 years
Bins and shredding containers	5 years
Shredding vehicles – chassis	3-10 years
Shredding vehicles – box	3-10 years
Recycling equipment	5 years
Vehicles	3-5 years

The Company allocates the amount initially recognized in respect of an item of equipment to its significant parts and depreciates separately each such part. The estimated useful lives and amortization method are reviewed annually, with the effect of any changes in estimate accounted for on a prospective basis.

Intangible assets

Identifiable intangible assets

The Company's identifiable intangible assets are stated at cost less accumulated amortization and impairment losses. These assets are capitalized and amortized on a straight-line basis in the statement of comprehensive loss over their estimated useful lives. The re-acquired franchise rights are amortized over the remaining term of the initial Franchise Agreements.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

The estimated useful lives of these assets are as follows:

Trademarks and intellectual property	10 years
Franchise agreements	10 years
Re-acquired franchise rights	2-8 years
Proshred system	10 years
Customer relationships	10 years
Computer software	3 years

The assessment of the useful lives of the identifiable intangible assets is reviewed annually. Changes in useful lives or the useful life from indefinite to finite are made on a prospective basis.

Goodwill

Goodwill represents the excess of the cost of the business acquisition over the fair value of the Company's share of the identifiable net assets of the acquired business at the date of acquisition. Goodwill is carried at cost less accumulated impairment losses. Goodwill is allocated on the date of acquisition to each cash-generating unit ("CGU") or group of CGUs that are expected to benefit from the related business combination.

Impairment of non-financial assets

Equipment and identifiable definite life intangible assets (other than goodwill) are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units or "CGUs"). An impairment loss is recognized when the carrying value of an asset or CGU exceeds the recoverable amount. The recoverable amount of an asset or CGU is the greater of its value-in-use and its fair value less costs to sell. In assessing value-in-use and fair value less costs to sell, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Goodwill is reviewed for impairment annually or at any time if an indicator of impairment exists. Impairment of goodwill is tested at a level where goodwill is monitored for internal management purposes. Therefore, goodwill may be assessed for impairment at the level of either an individual CGU or a group of CGUs which are expected to benefit from the synergies of the combination. The carrying amount of a CGU is compared to its recoverable amount, which is the higher of its value-in-use or fair value less costs to sell, to determine if impairment exists.

Impairment losses are recognized in the Statement of Comprehensive Loss. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis. Impairment losses for assets other than goodwill are reversed in future periods if the circumstances that led to the impairment no longer exist. The reversal is limited to restoring the carrying amount such that it does not exceed the carrying amount that would have been determined, net of amortization, had no impairment loss been recognized in prior periods.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

Provisions

Provisions are recognized in other liabilities when the Company has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted where the effect is material.

Income tax

Income tax comprises current and deferred income tax. Income tax is recognized in the statement of comprehensive income (loss) except to the extent that it relates to items recognized directly in other comprehensive income (loss) or directly in equity, in which case the income tax is also recognized directly in other comprehensive loss or equity, respectively.

(i) Current income tax

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted, at the end of the reporting period, and any adjustments to tax payable in respect of previous years.

(ii) Deferred income taxes

Deferred income taxes are provided on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements, except where the temporary difference arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination that, at the time of the transaction, affects neither accounting nor taxable profit or loss.

Deferred income taxes are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the date of the statement of financial position. Deferred income tax assets and liabilities are presented as non-current and determined on a non-discounted basis. Deferred income tax assets are recognized only to the extent that it is considered probable that taxable profit will be available against which deductible temporary differences, carried forward tax credits or tax losses can be utilized. The carrying value of deferred income tax assets are reviewed at the end of each reporting period and increased or reduced to the extent it is determined probable that sufficient taxable profits will, or will not, be available to allow all or part of the income tax asset to be recovered.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

Revenue recognition

(i) 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, license and service fees paid as a percentage of the franchisees monthly sales volumes. The initial franchise or license fee is recognized as revenue when the franchisee or licensee has fully executed a franchise or license agreement has been provided the required training and the collection of the initial fee is reasonably assured. Royalties, license and service revenue is accrued monthly based on sales reported by franchisees or licensees if collection is reasonably assured. Interest income on notes receivable is recognized in the month earned.

(ii) Corporate operations – shredding, destruction and recycling services

The Company earns revenue from providing shredding and destruction services to clients and by way of the sale of paper to recycling facilities. Shredding and destruction service revenue is recorded when the service has been performed, 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.

Share-based payments

The Company issues share-based awards to certain employees and non-employee directors whereby employees render services as consideration for equity instruments (equity-settled transactions). The cost of equity-settled transactions is recognized, together with a corresponding increase in contributed surplus in equity, over the period in which the performance and/or service conditions are fulfilled. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value. The fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. Compensation expense is recognized over the tranche’s vesting period by increasing contributed surplus based on the number of awards expected to vest. This number is reviewed at least annually, with any changes in estimate recognized immediately in compensation expense with a corresponding adjustment to contributed surplus.

Where an equity-settled award is cancelled, it is treated as if it vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. This includes any award where non-vesting conditions within the control of either the entity or the employee are not met. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award. All cancellations of equity-settled transaction awards are treated equally.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

Convertible debentures

Convertible debentures are separated into liability and equity components based on the terms of the contract. On issuance of the convertible debentures, the fair value of the liability component is determined using a market rate for an equivalent non-convertible debenture. This amount is classified as a financial liability measured at amortized cost (net of transaction costs) until it is extinguished on conversion or redemption. The remainder of the proceeds is allocated to the conversion option and is recognised and included in equity. Transaction costs are deducted from equity, net of associated income tax. The carrying amount of the conversion option is not re-measured in subsequent years. Transaction costs are apportioned between the liability and equity components of the convertible debenture based on the allocation of proceeds to the liability and equity components when the instruments are initially recognized.

Interest in a joint operation

The Company has a joint arrangement, which is an arrangement between two or more parties that are bound by a contractual agreement which gives the parties joint control of the arrangement. The arrangement requires unanimous consent for the decisions about the relevant activities of the joint arrangement. The arrangement establishes the parties' rights to the assets, and obligations for the liabilities, relating to the arrangement, and the parties' rights to the corresponding revenues and obligations for the corresponding expenses. As such, the Company recognizes the assets and liabilities used for the specific tasks and recognizes its share of the revenues and expenses in accordance to the contractual agreement. The Company earns rental revenue for the use of the shredding vehicle and royalty revenues and service fees based on a percentage of total monthly gross revenues. The Company incurs monthly finance costs on the truck loan payments and incurs depreciation and amortization expense on the tangible and intangible assets.

Business combinations

Acquisitions of subsidiaries and businesses (other than entities which were under the control of the parent) are accounted for using the acquisition method. The cost of the business combination is measured as the aggregate of the fair value (at the date of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3, *Business Combinations* are recognized at their fair value at the acquisition date except for noncurrent assets that are classified as held for sale in accordance with IFRS 5, *Noncurrent Assets Held for Sale and Discontinued Operations,* which are recognized and measured at fair value less cost to sell.

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, 2017.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

Earnings (loss) per share

Basic earnings (loss) per share is computed by dividing net income (loss) for the year attributable to equity owners of the Company by the weighted average number of common shares outstanding during the reporting period. Diluted loss per share is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments such as options and warrants. The number of shares included with respect to options, warrants and similar instruments is computed using the treasury stock method. 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.

New and revised standards that are effective for annual periods beginning on or after January 1, 2013

IFRS 10 'Consolidated Financial Statements' (IFRS 10)

IFRS 10 supersedes IAS 27 'Consolidated and Separate Financial Statements' (IAS 27) and SIC 12 'Consolidation-Special Purpose Entities'. IFRS 10 revises the definition of control and provides extensive new guidance on its application. These new requirements have the potential to affect which of the Company's investees are considered to be subsidiaries and therefore to change the scope of consolidation. The requirements on consolidation procedures, accounting for changes in non-controlling interests and accounting for loss of control of a subsidiary are unchanged. Management has reviewed its control assessments in accordance with IFRS 10 and has concluded that there is no effect on the classification (as subsidiaries or otherwise) of any of the Company's investees held during the period or comparative periods covered by these financial statements.

IFRS 11 'Joint Arrangements' (IFRS 11)

IFRS 11 supersedes IAS 31 'Interests in Joint Ventures' (IAS 31) and SIC 13 'Jointly Controlled Entities- Non-Monetary-Contributions by Venturers'. IFRS 11 revises the categories of joint arrangement, and the criteria for classification into the categories, with the objective of more closely aligning the accounting with the investor's rights and obligations relating to the arrangement. In addition, IAS 31's option of using proportionate consolidation for arrangements classified as jointly controlled entities under that Standard has been eliminated. IFRS 11 now requires the use of the equity method for arrangements classified as joint ventures (as for investments in associates). Management reviewed the implementation of this standard and there was no significant impact on the financial statements.

IFRS 12 'Disclosure of Interests in Other Entities' (IFRS 12)

IFRS 12 integrates and makes consistent the disclosure requirements for various types of investments, including unconsolidated structured entities. It introduces new disclosure requirements about the risks to which an entity is exposed from its involvement with structured entities. The Company consolidates all its subsidiaries and has no special purpose vehicles, large minority holdings, potential voting rights or instances of delegated power. Management reviewed the implementation of this standard and there was no significant impact on the financial statements.

(expressed in Canadian dollars)

3 Significant accounting policies (continued)

IFRS 13 'Fair Value Measurement' (IFRS 13)

IFRS 13 clarifies the definition of fair value and provides related guidance and enhanced disclosures about fair value measurements. It does not affect which items are required to be fair-valued. The scope of IFRS 13 is broad and it applies for both financial and non-financial items for which other IFRSs require or permit fair value measurements or disclosures about fair value measurements except in certain circumstances. IFRS 13 applies prospectively for annual periods beginning on or after 1 January 2013. Its disclosure requirements need not be applied to comparative information in the first year of application. Management reviewed the implementation of this standard and there was no significant impact on the financial statements.

Accounting standards and amendments issued but not yet effective

At the date of authorization of these financial statements, certain new standards, amendments and interpretations to existing standards have been published by the IASB but are not yet effective, and have not been adopted early by the Company. Management anticipates that all of the relevant pronouncements will be adopted in the Company's accounting policies for the first period beginning after the effective date of the pronouncement. Information on new standards, amendments and interpretations that are expected to be relevant to the Company's financial statements is provided below. Certain other new standards and interpretations have been issued but are not expected to have a material impact on the Group's financial statements.

IFRS 9 'Financial Instruments' (IFRS 9)

The IASB aims to replace IAS 39 'Financial Instruments: Recognition and Measurement' (IAS 39) in its entirety with IFRS 9. To date, the chapters dealing with recognition, classification, measurement and derecognition of financial assets and liabilities have been issued. These chapters are effective for annual periods beginning on or after 1 January 2015. Chapters dealing with impairment methodology and hedge accounting are still being developed. Further, in November 2011, the IASB tentatively decided to consider making limited modifications to IFRS 9's financial asset classification model to address application issues. The Company has not yet to assess the impact of this new standard on the consolidated financial statements. Management does not expect to implement IFRS 9 until it has been completed and its overall impact can be assessed.

(expressed in Canadian dollars)

4 Critical accounting estimates and judgements

The preparation of financial statements requires management to use judgment in applying its accounting policies and in developing estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ materially from those estimates and assumptions. These estimates and underlying assumptions are reviewed on an ongoing basis and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. The following discusses the most significant accounting judgements and estimates that the Company has made in the preparation of the financial statements.

Significant accounting judgements

i) Impairment and reversals of impairment

The impairment testing and reversal of impairment testing of long-lived assets such as definite life intangibles involves judgement in making an assessment of whether the assets are exhibiting indicators of impairment or reversal and determining the structure of the impairment review (i.e. determination of cash-generating units ("CGUs") and allocation of intangibles to the CGUs).

Significant accounting estimates

i) Impairment and reversals of impairment

The Company reviews goodwill at least annually and other non-financial assets when there is any indication that the asset might be impaired. The determination of the value in use and fair value of a CGU to which goodwill is allocated to involves the use of estimates by management. The Company uses discounted cash flow based methods to determine these values. These discounted cash flow calculations typically use five-year and seven-year projections that are based on the operative plans approved by management. Cash flow projections take into account past experience and represent management's best estimate of future developments. Cash flows after the planning period are extrapolated using estimated growth rates. Key assumptions on which management has based its determination of fair value less costs to sell and value-in-use include estimated growth rates, discount rates, future cash flows, margins and tax rates. These estimates, including the methodology used, can have a material impact on the respective values and ultimately the amount of any impairment or reversal of impairment. Refer to note 12 for estimates and assumptions made.

ii) Deferred income taxes

The Company, including its subsidiaries, operate and earn income in multiple countries and is subject to changing tax laws in multiple jurisdictions within these countries. Significant judgements are necessary in determining income tax assets and liabilities. Although management believes that it has made reasonable estimates about the final outcome of tax uncertainties, no assurance can be given that the final outcome of these tax matters will be consistent with what is reflected in the historical income tax provisions. Such differences could have an effect on the deferred tax assets and liabilities in the period in which such determinations are made. At each date of Statement of Financial Position, the Company assesses whether the realization of future tax benefits is sufficiently probable to recognize deferred tax assets and liabilities.

(expressed in Canadian dollars)

4 Critical accounting estimates and judgements (continued)

Significant accounting estimates (continued)

ii) Deferred income taxes (continued)

This assessment requires the exercise of judgement on the part of management with respect to, among other things, benefits that could be realized from available tax strategies and future taxable income, as well as other positive and negative factors. The recorded amount of total deferred tax assets and liabilities could be materially affected if changes in current tax regulations are enacted. Refer to note 22 for estimates and assumptions used.

iii) Useful lives of tangible and intangible assets

Management estimates the useful lives of tangible and definite life intangible assets based on the period during which the assets are expected to be available for use. The amounts and timing of recorded expenses for amortization of these assets for any period are affected by these estimated useful lives. On an annual basis, the Company assesses the useful lives of its tangible and intangible assets with definite lives and the useful lives updated if expectations change as a result of physical wear and tear, technical or commercial obsolescence and legal or other limits to use. It is possible that changes in these factors may cause significant changes in the estimated useful lives of the Company's tangible and definite life intangible assets in the future. Refer to note 9, 10 and 11 for estimates and assumptions used.

iv) Business combinations

Management uses valuation techniques in determining the fair values of the various elements of a business combination. Refer to note 8 for estimates and assumptions used.

5 Advertising fund

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 location's revenue. In accordance with *IAS 18 – Revenue*, the revenue, expenses and cash flows of the Ad Fund are not included in the Company's Statements of Comprehensive Loss because the contributions to the Ad Fund are segregated, designated for a specific purpose, and the Company acts, in substance, as an agent with regard to these contributions. As at December 31, 2013, the cash attributable to the Ad Fund amounted to $63,375 (2012 - $48,031).

(expressed in Canadian dollars)

6 Trade receivables

Trade receivables include receivables from franchisees and receivables from shredding customers. The trade receivables as at December 31, 2013 and December 31, 2012 are as follows:

	2013	2012
	$	$
Trade receivables	448,982	426,927
Less: Allowance for doubtful accounts	–	(2,863)
Trade receivables – net	448,982	424,064

7 Notes receivable from franchisees

Notes receivable arise from the financing of the initial franchise fee by franchisees and are guaranteed by the respective owners of the franchises. The notes receivable bear interest rates ranging from 4.25% to 8.25% per annum with monthly blended payments of principal and interest ranging from US$670 to US$1,821. The payments on the notes commence between dates ranging from August 1, 2011 to March 1, 2014 and mature between dates ranging from August 1, 2014 to February 1, 2017.

The notes receivable as at December 31, 2013 and December 31, 2012 are as follows:

	2013	2012
	$	$
Principal	329,198	234,434
Less: Current portion	(148,633)	(40,765)
Less: Allowance for impairment	(14,453)	–
	166,112	193,669

At December 31, 2013, there were two notes receivable that were past due from franchisees. The Company has the right to charge additional interest as a penalty if the franchisee is in default on its payments. The Company has assessed these amounts for impairment and has recorded an impairment of $14,453 as at December 31, 2013 based on the present value of estimated future cash flows expected to be received. The Company is working with the franchisee on refinancing options.

8 Acquisition of franchise

The Company acquired the Proshred Charlotte franchise (“Charlotte acquisition”) on July 31, 2013 from its franchisee. The Company conducted the Charlotte acquisition to (1) increase the Company’s long term cash flows, and (2) to enter into a growing market and (3) to establish regional headquarters to allow for further expansion by way of additional acquisitions or by way of establishing satellite offices in cities located in the south east United States.

(expressed in Canadian dollars)

8 Acquisition of franchise (continued)

The business combination resulted in the recognition of a gain on acquisition of $148,228, determined on the basis of an 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.

The business combination also resulted in the removal of the original franchise agreement intangible asset between the Company's subsidiary, Proshred Franchising Corp. and the franchisee. The Company removed the original franchise agreement intangible asset in the amount of $96,700. Refer also to note 10.

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

	Charlotte $
Assets acquired	
Working capital	102,790
Equipment	617,028
Customer relationships	760,646
Re-acquired franchise rights	100,734
Gain on acquisition	(148,228)
Removal of original franchise agreement	(96,700)
Total	1,336,270
Consideration given	
Cash	1,284,875
Note payable	51,395
	1,336,270
Acquisition costs (expensed in statement of comprehensive loss)	21,920

The Company translated the fair values of all assets acquired and consideration given using the exchange rate on the date of the acquisition. In the above table, the acquisition was translated at $1USD = $1.0279CAD. On December 31, 2013, the assets and liabilities acquired are converted at the year-end rate at $1USD = $1.0636CAD in the Statement of Financial Position.

As part of the purchase price, on July 31, 2013, the Company committed to a note payable of $51,395, providing monthly blended payments of principal and interest of US$2,083 over a twenty four month period, referred to as the Note payable. The Company has recorded the Note payable at fair value in accordance with IAS 39 *Financial Instruments: Recognition and Measurement.* Subsequent to the acquisition date, the Company has measured the Note payable at amortized cost using the effective interest method.

The fair values of the assets were determined on the basis of observable market prices, where possible. The fair values of the re-acquired franchise rights were determined by discounting the cash flows from the franchise royalty stream over the remaining contractual term of the franchise agreement. The fair values of the customer relationships were determined by estimating the discounted level of future cash flows anticipated from the recurring customer relationships purchased.

(expressed in Canadian dollars)

8 Acquisition of franchise (continued)

The Company previously reported a preliminary purchase price allocation in its financial statements dated September 30, 2013. The amounts previously reported have been revised and finalized within these financial statements based on the final valuation performed.

The pro forma consolidated results of the Company, as if the acquisition of Proshred Charlotte had been made at the beginning of the year, would include revenue of $5,346,796 (compared to reported revenue of $4,669,083) and net loss of $380,140 (compared to reported net loss of $527,145).

In preparing the pro forma results, revenue and costs have been included as if the business was acquired on January 1, 2013 and intercompany transactions had been eliminated. This information is not necessarily indicative of the results of the Company that would have occurred had the purchases actually been made at the beginning of the period presented or indicative of the future results of the Company.

During the year ended December 31, 2012, the Company acquired the New York City and Miami locations and recorded a settlement of pre-existing litigation loss of $712,567. In addition, the business combinations resulted in the removal of the original franchise agreement intangible assets between the Company's subsidiary, Proshred Franchising Corp. and the franchisee in the amount of $158,289. The recognition of the re-acquired franchise rights and the removal of the original franchise agreements resulted in a net gain on the franchise agreements of $138,439.

(expressed in Canadian dollars)

9 Equipment

Cost	**Computer equipment**	**Furniture & fixtures**	**Bins & shredding containers**	**Shredding vehicles - chassis**	**Shredding vehicles - box**	**Recycling equipment**	**Vehicles**	**Total**
	$	**$**	**$**	**$**	**$**	**$**	**$**	**$**
As at January 1, 2012	91,368	53,203	51,484	219,621	472,610	6,462	6,814	901,562
Additions	28,062	921	16,206	123,696	257,034	–	–	425,919
Acquisitions	7,500	5,750	87,750	125,875	301,290	90,000	46,200	664,365
Sale of assets	–	–	–	(43,144)	(102,559)	(3,000)	–	(148,703)
Foreign exchange	(731)	(389)	(877)	(2,056)	(5,457)	(561)	(304)	(10,375)
As at December 31, 2012	126,199	59,485	154,563	423,992	922,918	92,901	52,710	1,832,768
Additions	1,994	3,411	19,734	279,995	642,292	–	–	947,426
Acquisitions	–	3,172	74,389	154,545	381,211	–	5,152	618,469
Sale of assets	–	–	(1,477)	(142,626)	(304,969)	(95,741)	(16,938)	(561,751)
Foreign exchange	4,063	590	12,841	35,895	128,079	2,840	20,659	204,967
As at December 31, 2013	132,256	66,658	260,050	751,801	1,769,531	–	61,583	3,041,879

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, 2012	88,464	50,039	10,932	57,581	122,134	4,847	2,271	336,268
Depreciation	8,174	3,793	28,500	55,712	121,351	21,539	9,125	248,194
Sale of assets	–	–	–	(3,664)	(9,009)	(3,000)	–	(15,673)
Foreign exchange	(577)	(359)	(285)	(570)	(1,280)	(203)	(142)	(3,416)
As at December 31, 2012	96,061	53,473	39,147	109,059	233,196	23,183	11,254	565,373
Depreciation	10,119	4,929	39,883	75,768	172,887	2,535	12,289	318,410
Sale of assets	–	–	–	(28,886)	(58,487)	(26,778)	(6,676)	(120,827)
Foreign exchange	1,731	177	3,967	2,619	56,709	1,060	17,577	83,840
As at December 31, 2013	107,911	58,579	82,997	158,560	404,305	–	34,444	846,796
Net book value								
As at December 31, 2012	30,138	6,012	115,416	314,933	689,722	69,718	41,456	1,267,395
As at December 31, 2013	24,345	8,079	177,053	593,241	1,365,226	–	27,139	2,195,083

(expressed in Canadian dollars)

9 Equipment (continued)

The Company acquired equipment as part of the franchise acquisition on July 31, 2013 (refer to note 8). During the year ended December 31, 2013, the Company sold five older shredding vehicles and purchased four new shredding vehicles obtaining vendor financing (refer to note 16). The Company also closed its baling facility and sold its recycling equipment, as well as purchased computers, and shredding containers during the twelve months ended December 31, 2013. The foreign exchange adjustment is a result of the translation of corporate equipment from US functional currency dollars to Canadian presentation dollars at December 31, 2013, and December 31, 2012. 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.”

The Company has one shredding vehicle held under a finance lease arrangement. As of December 31, 2013, the net carrying amount of the related shredding vehicles, included as part of equipment is $144,434. The finance lease liability (refer to note 16) is secured by the related asset held under the finance lease. Future minimum finance lease payments at December 31 were as follows:

	Minimum lease payments due		
December 31, 2013	**Within 1 year $**	**1 – 5 years $**	**Total**
Lease payments	29,304	154,853	184,157
Finance charges	(10,819)	(28,904)	(39,723)
Net present values	18,485	125,948	144,434

(expressed in Canadian dollars)

10 Intangible assets

Cost	Franchise agreements	Proshred system	Trademarks & intellectual property	Re-acquired franchise rights	Customer relationships	Total
	$	$	$	$	$	$
As at January 1, 2012	2,790,576	978,000	1,672,500	539,010	279,676	6,259,762
Acquisitions	–	–	–	320,000	760,000	1,080,000
Removal of original franchise agreements	(372,000)	–	–	–	–	(372,000)
Foreign exchange	(53,215)	–	–	(13,344)	(9,954)	(76,513)
As at December 31, 2012	2,365,361	978,000	1,672,500	845,666	1,029,722	6,891,249
Acquisitions	–	–	–	100,969	762,422	863,391
Removal of original franchise agreements (note 8)	(173,321)	–	–	–	–	(173,321)
Foreign exchange	193,492	–	–	61,524	94,081	349,097
As at December 31, 2013	2,385,532	978,000	1,672,500	1,008,159	1,886,225	7,930,416

Accumulated amortization and impairment	Franchise agreements	Proshred system	Trademarks & intellectual property	Re-acquired franchise rights	Customer relationships	Total
	$	$	$	$	$	$
As at January 1, 2012	1,229,750	406,169	868,025	163,967	33,045	2,700,956
Amortization	248,700	92,275	130,453	183,768	98,655	753,851
Removal of original franchise agreements	(190,493)	–	–	–	–	(190,493)
Impairment (note 12)	158,757	64,237	89,974	–	–	312,968
Foreign exchange	(22,463)	–	–	(4,500)	(1,312)	(28,275)
As at December 31, 2012	1,424,251	562,681	1,088,452	343,235	130,388	3,549,007
Amortization	171,143	80,741	113,042	155,641	136,248	656,815
Reversal of previous impairment	(132,382)	(72,931)	(225,867)	–	–	(431,180)
Removal of original franchise agreements (note 8)	(73,812)	–	–	–	–	(73,812)
Foreign exchange	128,107	–	–	28,731	13,501	170,339
As at December 31, 2013	1,517,307	570,491	975,627	527,607	280,137	3,871,169
Net book value						
As at December 31, 2012	941,110	415,319	584,048	502,431	899,334	3,342,242
As at December 31, 2013	868,225	407,509	696,873	480,552	1,606,088	4,059,247

(expressed in Canadian dollars)

10 Intangible assets (continued)

As a result of the acquisition of the Proshred Charlotte franchise location, the original franchise agreement intangible asset has been removed in the amount of $96,700. Customer relationships and re-acquired franchise rights were recorded as intangible assets on July 31, 2013 as part of the Proshred Charlotte acquisition. The foreign exchange adjustment is a result of the translation of foreign operation intangible assets in US dollars to Canadian dollars at December 31, 2013 and December 31, 2012. 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 franchises and corporately owned locations in the US.

Intangible assets with a finite life are tested for impairment when events or changes in circumstances indicate that 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 December 31, 2013, the Company recorded a reversal of a portion of the previously reported impairment of $431,180 (December 31, 2012 – $nil). Refer to note 12.

11 Goodwill

The following table presents goodwill for the years ended December 31, 2013 and 2012:

	2013	2012
	$	$
Opening balance	1,361,705	878,270
Acquisitions	–	737,292
Impairment of goodwill (note 12)	–	(232,196)
Foreign currency translation	93,762	(21,661)
Closing balance	1,455,467	1,361,705

12 Impairment of goodwill and long-lived assets

The Company performs an impairment test of long-lived assets when there is an indication of permanent impairment, which includes indicators such as when actual sales are less than budgeted, profits are less than prior years’ profits, and when significant events and circumstances indicate that the carrying amount may not be recoverable. Goodwill is tested for impairment at least annually.

The Company has identified each franchise and corporate location as being a CGU and has completed a review for impairment for each CGU, comparing the carrying amount of the CGU with the recoverable amount of the CGU. The Company’s unallocated assets consist of computer equipment, furniture, computer software, the Proshred system, trademarks and intellectual property. The carrying amount of the group of CGUs that include the unallocated corporate assets is compared with the recoverable amount of the group of CGUs in testing for impairment.

(expressed in Canadian dollars)

12 Impairment of goodwill and long-lived assets (continued)

The Company performed its annual test for goodwill impairment in accordance with its policy described in note 3. The Company compared the aggregate recoverable amount of the assets included in the CGUs of the corporate locations to their respective carrying amounts. The recoverable amount of the corporate location CGU's were more than the carrying amounts. Based on sensitivity analysis, a reasonably possible change in assumptions would not cause an impairment loss. At December 31, 2012, the Company recorded an impairment loss of $232,103, which was allocated to the goodwill of the New York City CGU.

The carrying value of goodwill for each CGU is identified as follows:

Cash Generating Unit	**2013**	**2012**
	$	**$**
Syracuse	138,269	129,587
Albany	96,609	90,369
Milwaukee	683,369	639,229
New York City	537,220	502,520
Total goodwill	1,455,467	1,361,705

The Company assessed its impairment indicators related to its long-lived assets at December 31, 2013 and determined there was sufficient indication of impairment on certain CGUs to warrant an analysis to be performed.

The recoverable amount of each CGU has been determined based on a value-in-use calculation. The value-in-use calculation uses cash flow projections based on financial budgets approved by management. The Company then performed the impairment test for the unallocated, aggregate corporate assets and assessed whether impairment exists at a Company-wide level. The recoverable amount was determined using value-in-use. The value-in-use calculation uses cash flow projections based on financial budgets approved by management.

The key assumptions included the following:

i. Revenue growth of each franchise and corporate location, which reflect the past experience of each location. Management has used growth rate ranges of 2.5% to 100% based on prior results of existing franchisees and the franchisees time in the system. During the first five years of a franchisee's operation, higher growth rates are typically achieved.

ii. Pre-tax discount rates ranging from 16% to 19% (December 31, 2012– 16% to 17%) was used and reflects the risks specific to each CGU.

iii. Cash flows from franchising are based on the current royalty rate charged to each franchise, as the rates are expected to continue in the future.

iv. For franchise CGUs, a cash flow period of up to 5 years was used, covering the remaining useful life of the franchise agreements. Management believes that this period is reasonable in light of the contractual terms of the franchise agreements as this is consistent with the assessed remaining useful life of the franchise agreements as originally determined.

v. For corporate location CGUs, a 5 year cash flow period was used based on financial budgets approved by management including growth rates of 2.5% to 20% and a perpetual growth rate of 2.5%. Revenue growth was determined based on the Company's internal budget and considered past experience.

(expressed in Canadian dollars)

12 Impairment of goodwill and long-lived assets (continued)

vi. For corporate location CGUs, budget-operating margins, which were determined using average operating margins achieved in the periods immediately before the budget period. Management believes the operating margins are reasonably achievable.

Based on the impairment review performed at December 31, 2013, the recoverable amount of the CGUs was higher than the carrying amounts at the Company-wide level and the Company recorded a reversal of impairment of $431,180 related to the Company's Trademarks, Franchise agreements and Proshred system (refer to note 10). The events and circumstances that lead to this reversal include: improved overall cash flow margins, accretion to cash as a result of the Charlotte and Miami acquisitions and the addition of new franchisees and the related cash flows. The reversal of impairment was limited to restoring the carrying amounts such that they did not exceed the carrying amounts that would have been determined, net of amortization, had no impairment loss been recognized in prior periods.

At December 31, 2012, the Company determined the recoverable amount of certain CGUs was lower than their carrying amounts and recorded an impairment loss of $312,904 as well as an impairment of goodwill of $232,103.

13 Assets classified as held for sale

On May 27, 2013, the Company decided that the Miami business will be corporately operated and no longer be sold. Prior to this date, the Company committed to a plan to sell the Miami business acquired on July 13, 2012 and classified the Miami business as a disposal group held for sale and as a discontinued operation. The Company has determined that the Miami location can be operated from its newly acquired Charlotte location (refer to note 8). The Company is expected to operate the Miami location commencing in the first quarter of 2014. As the Miami business is no longer held for sale, the results of the operations of the entity previously presented in discontinued operations of $4,276 have been reclassified and included in income from continuing operations. The assets previously held for sale of $286,952 and liabilities directly associated with the assets of $105,178 classified as held for sale have been re-classified as current and non-current assets and liabilities. The Company currently has a joint arrangement with the franchise in Tampa Bay, Florida to operate the Miami business (see note 27). The results of the Miami business for the period have been accounted for as a joint arrangement with the Tampa Bay franchise. Within the joint arrangement, the Company earns royalty and service fees on the gross Miami revenues and rental revenue for the use of the shredding vehicle. The Company incurs finance costs on the monthly truck loan payments and depreciation and amortization on the Miami tangible and intangible assets.

14 Accounts payable and accrued liabilities

As at December 31, 2013 and December 31, 2012, accounts payable and accrued liabilities are comprised of:

	2013	2012
	$	$
Accounts payable	273,224	235,903
Accrued liabilities	333,284	268,607
Accounts payable and accrued liabilities	606,508	504,510

(expressed in Canadian dollars)

15 Deferred revenue

During the year ended December 31, 2013, the Company received $57,966 from its new franchisee in Southern New Jersey for the down payment of the franchise fee. The down payment and the remaining franchise fee were recognized as franchise fee revenue in January 2014, when the required training was performed. Refer to note 28 for additional information.

16 Long-term debt

As at December 31, 2013 and December 31, 2012 long-term debt is comprised of:

	2013	**2012**
	$	**$**
Line of credit (i)	5,982,184	6,033,094
Less: deferred financing charges	(22,086)	(44,172)
Line of credit net of deferred financing charges	5,960,098	5,988,922
Truck loans (ii)	755,656	508,400
Finance lease liability (iii)	144,434	–
Term loans (iv)	1,264,227	–
Total long-term debt	8,124,415	6,497,322
Less: current portion	(648,004)	(138,302)
Total	7,476,411	6,359,020

(i) The line of credit was entered into on November 27, 2009 with a related party entity (see note 27) for a maximum amount of $4 million. The line of credit was originally 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 are charged to expense over the term of the facility. During the year ended December 31, 2011, the line of credit limit was increased to $5.37 million. During the year ended December 31, 2012, the line of credit was increased to $6.03 million. The terms of the agreement remained unchanged upon increasing the line of credit. The Company has drawn from its line of credit in order to finance the purchase of its corporate locations including Syracuse, Albany, and Milwaukee in 2010 and New York City and Miami in 2012 and for general business purposes. In September of 2013, the Company signed an amendment to its existing line of credit facility, extending the facility's term for an additional three years to November 27, 2017. The terms of the agreement remained unchanged upon extending the facility's term.

(ii) Truck loans

On November 11, 2011, the Company entered into a loan and security agreement in the amount of US$240,000, repayable with monthly blended payments of principal and interest of US$5,690 maturing October 3, 2015. The loan bears interest at 8.14% per annum and is secured by two shredding vehicles with a carrying value of $269,225 at December 31, 2013. The value of the loan on December 31, 2013 is $123,282.

(expressed in Canadian dollars)

16 Long-term debt (continued)

ii) Truck loans (continued)

On July 5, 2012, the Company entered into a loan and security agreement in the amount of US$121,128, repayable with monthly blended payments of principal and interest of US$3,718 maturing July 5, 2015. The loan bears interest at 6.502% per annum and is secured by one shredding vehicle with a carrying value of $93,368 at December 31, 2013. The value of the loan on December 31, 2013 is $71,164.

On August 3, 2012, the Company entered into a loan and security agreement in the amount of US$125,556, repayable with monthly blended payments of principal and interest of US$2,545 maturing August 13, 2017. The loan bears interest at 8% per annum and is secured by one shredding vehicle with a carrying value of $172,701 at December 31, 2013. The value of the loan on December 31, 2013 is $102,962.

On January 3, 2013, the Company traded in one of its shredding vehicles for a larger shredding vehicle. The related loan and security agreement entered into on August 8, 2012, in the amount of US$121,000, was replaced with a new loan and security agreement. The new loan and security agreement for US$119,906 is repayable with monthly blended payments of principal and interest of US$2,382 maturing January 5, 2018. The loan bears interest at 7% per annum and is secured by one shredding vehicle with a carrying value of $231,750 at December 31, 2013. The value of the loan on December 31, 2013 is $107,488.

On January 31, 2013, the Company entered into a loan and security agreement in the amount of US$171,516, repayable with monthly blended payments of principal and interest of US$3,407 maturing February 5, 2018. The loan bears interest at 7% per annum and is secured by one shredding vehicle with a carrying value of $233,766 at December 31, 2013. The value of the loan on December 31, 2013 is $156,434.

On October 24, 2013, the Company entered into a loan and security agreement in the amount of US$187,950, repayable with monthly blended payments of principal and interest of US$3,731 maturing October 24, 2018. The loan bears interest at 7% per annum and is secured by one shredding vehicle with a carrying value of $195,218 at December 31, 2013. The value of the loan on December 31, 2013 is $194,324.

iii) Finance lease liability

On November 15, 2013, the Company entered into a finance lease in the amount of US$137,035, repayable with monthly blended payments of principal and interest of US$2,296 with a final payment of $37,680, maturing December 20, 2018. The loan bears interest at 7.95% per annum and is secured by one shredding vehicle with a carrying value of $195,615 at December 31, 2013. The balance of the loan on December 31, 2013 is $144,434.

(expressed in Canadian dollars)

16 Long-term debt (continued)

(iv) Term loans

In order to finance the purchase of the Proshred Charlotte franchise on July 31, 2013, the Company entered into the following loan agreements with related parties (refer to note 27):

(a) A 5 year loan agreement in the amount of CAD$525,750 maturing July 31, 2018. The loan bears interest at 9% per annum with interest payable semi-annually. The loan is secured by a general security agreement over the assets of the Proshred Charlotte entity;

(b) A 5 year loan agreement in the amount of US$75,000 maturing July 31, 2018. The loan bears interest at 9% per annum with interest payable semi-annually. The loan is secured by a general security agreement over the assets of the Proshred Charlotte entity;

(c) A 4 year loan agreement in the amount of CAD$100,000 with monthly blended payments of principal and interest of CAD$2,488 maturing July 31, 2017. The loan bears interest at 9% per annum. The loan is secured by a general security agreement over the assets of the Proshred Charlotte entity;

(d) A 4 year loan agreement in the amount of US$50,000 with monthly blended payments of principal and interest of US$1,244 maturing July 31, 2017. The loan bears interest at 9% per annum. The loan is secured by a general security agreement over the assets of the Proshred Charlotte entity; and

(e) A 5 year loan and security agreement in the amount of US$500,000, repayable with monthly blended payments of principal and interest of US$12,681 maturing August 5, 2017. The loan bears interest at 10% per annum and is secured by four shredding vehicles and two non-shredding vehicles with a carrying value of $518,881 at December 31, 2013. The value of the loan on December 31, 2013 is $495,513.

17 Capital stock

a) Authorized

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

(expressed in Canadian dollars)

17 Capital stock (continued)

b) Issued and fully paid

For the years ended December 31, 2013 and December 31, 2012, 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, December 31, 2012 and December 31, 2013	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 years ended December 31, 2013, was 28,884,658 (December 31, 2012 - 28,884,658).

d) 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;

vi) 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

vii) 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.

(expressed in Canadian dollars)

17 Capital stock (continued)

d) Stock options (continued)

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

	2013		2012	
	Number of options	Weighted average exercise price $	Number of options	Weighted average exercise price $
Outstanding – Beginning of year	1,691,250	0.24	1,677,500	0.24
Granted	50,000	0.10	992,500	0.20
Expired	(278,750)	0.50	(978,750)	0.20
Outstanding – End of year	1,462,500	0.18	1,691,250	0.24

The following table summarizes the stock options outstanding as at:

		2013			2012		
Exercise price $	Issue date	Number of options outstanding	Weighted average remaining contractual life (yrs)	Options exercisable	Number of options outstanding	Weighted average remaining contractual life (yrs)	Options exercisable
0.52	Mar 17, 2008	–	0.00	–	262,500	0.21	262,500
0.14	May 27, 2010	280,000	0.40	280,000	280,000	1.40	280,000
0.15	Oct 19, 2010	10,000	1.81	7,500	10,000	2.81	5,000
0.12	May 2, 2011	140,000	1.33	140,000	140,000	2.34	140,000
0.10	Sept 26, 2011	5,000	2.74	2,500	5,000	3.74	1,250
0.10	Oct 26, 2011	–	0.00	–	5,000	3.82	1,250
0.10	Jan 2, 2012	–	0.00	–	5,000	3.01	1,250
0.10	May 31, 2012	–	0.00	–	5,000	4.42	5,000
0.10	July 9, 2012	–	0.00	–	1,250	9.53	1,250
0.10	Aug 1, 2012	2,500	1.58	2,500	2,500	2.58	2,500
0.20	Nov 23, 2012	975,000	3.90	975,000	975,000	4.90	975,000
0.10	Aug 6, 2013	50,000	3.58	–	–	–	–
		1,462,500		1,407,500	1,691,250	3.35	1,675,000

(expressed in Canadian dollars)

17 Capital stock (continued)

d) Stock options (continued)

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:

	2013	**2012**
Expected option life	4 years	5 years
Risk-free interest rate	1.57%	1.27%
Expected dividend yield	$nil	$nil
Expected volatility	229%	193%

50,000 options were granted during the year ended December 31, 2013 (2012 - 992,500). The weighted average grant-date fair value of options granted during 2013 amounted to approximately $0.10 per option. The net stock compensation charge, after adjusting for stock option forfeitures, amounted to $4,522 (2012 - $32,933).

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. Details are as follows:

				2013
	Exercise price $	**Number of warrants outstanding or to be issued**	**Remaining contractual life**	**Assigned value $**
Tranche 1	0.25 to 0.45	3,000,000	0.98 years	204,406
Tranche 2	0.25 to 0.45	1,000,000	0.90 years	83,800

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

Expected warrant life	1 year
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 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.

(expressed in Canadian dollars)

18 Convertible debentures

On December 31, 2012, the Company issued $375,000 convertible, unsecured subordinated, debentures. The debentures have a five year term and a coupon of 7.5% interest per annum. Each $1,000 principal amount of debenture entitles the holder to convert to approximately 3,333 common shares at a conversion price of $0.30 per share at any time prior to maturity. Conversion may occur at any time prior to the maturity date of December 31, 2017. The Company may, at its option, redeem the debentures, in whole or in part, at a redemption price equal to the principal amount plus accrued interest and unpaid interest. Interest of 7.5% per annum will be paid annually on the anniversary of the grant date. Debenture holders may defer interest otherwise due and payable until the next interest payment date, in which case such deferred interest payment shall accrue additional interest at 7.5% per annum. The convertible debentures contain two components: liability and equity elements. The equity element is presented in equity under the label of 'issue of convertible debentures' as contributed surplus. The effective interest rate of the liability element on initial recognition is 9.5% per annum (2012 – 9.5%).

	2013	2012
	$	$
Opening balance of liability component net of transaction costs	333,119	–
Accretion expense	4,763	–
Closing balance of liability component net of transaction costs	337,882	333,119
Equity component net of transaction costs	27,710	27,710
Deferred tax liability related to the equity component	7,633	7,633
Equity component net of transaction costs and tax	20,077	20,077

19 Revenue

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

	2013	2012
	$	$
Royalties	970,989	823,577
Franchise fees	263,963	300,100
License fees	6,848	4,378
Shredding services	2,788,373	2,363,002
Sale of paper products	592,943	568,920
Rental revenue	45,967	18,583
Total revenue	4,669,083	4,078,560

On July 31, 2013, the Company acquired the Charlotte franchise location. In 2013, the Company earned revenue from shredding services and through the sale of paper products related to the Charlotte corporate location. Prior to July 31st of 2013, the Company earned royalty revenue from the Charlotte franchise location.

(expressed in Canadian dollars)

20 Corporate operating locations expenses by nature

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

	2013	2012
	$	$
Shredding vehicle and related expenses	634,971	714,298
Employee wages expense	960,945	997,022
Employee benefit expense	190,965	200,957
Office and administration expense	407,276	417,887
Depreciation – equipment	318,410	251,160
Amortization – intangible assets	233,899	227,264
Total corporate operating expenses	2,746,466	2,808,588

During the year ended December 31, 2013, the Company operated five corporate locations – Syracuse, Albany, Milwaukee, New York City and Charlotte (since July 31, 2013). During the year ended December 31, 2012, the Company operated four corporate locations – Syracuse, Albany, Milwaukee and New York City.

21 Selling, general and administrative expenses by nature

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

	2013	2012
	$	$
Employee wages expense	744,296	795,339
Employee benefits expense	54,132	60,834
Share-based compensation	4,522	32,933
Professional fees	247,281	379,494
Technology	209,194	154,491
Rent and office expense	111,072	73,604
Selling and development	165,277	160,334
Impairment of note receivable	14,453	–
Amortization of deferred financing charges	22,086	22,086
Amortization – intangible assets	422,918	524,253
Foreign exchange (gain) loss	(352,971)	132,505
Other	219,231	229,947
Total selling, general and administrative expenses	1,861,491	2,565,820

(expressed in Canadian dollars)

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

Compensation of key management

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

	2013	2012
	$	$
Wages and benefits	617,026	593,033
Severance pay	–	71,250
Share-based compensation	4,475	32,933
Total	621,501	697,216

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.

22 Income taxes

Reconciliation of total tax recovery

The effective rate on the Company's loss before income tax differs from the expected amount that would arise using the statutory income tax rates. A reconciliation of the difference is as follows:

	2013	2012
	$	$
Statutory income tax rate	26.5%	26.5%
Expected income tax recovery based on above rates	(16,502)	(795,552)
Non-deductible expenses	(41,467)	329,088
Unrecognized deductible temporary differences and other	19,001	425,164
Effect of foreign tax rates	40,219	(153,968)
Other	(23,053)	–
Income tax recovery	(21,802)	(195,268)

The enacted tax rate in Canada, is 26.50% (26.50% in 2012) and in the United States is 38.82% (2012 – 42.02%), where the Company operates has been applied in the tax provision calculation. The decrease in the United States rate is due to the change in income allocation among different states from last year.

(expressed in Canadian dollars)

22 Income taxes (continued)

Reconciliation of total tax recovery (continued)

	2013	2012
	$	$
Provision for (recovery of) income taxes is comprised of:		
Current income taxes	(21,964)	–
Deferred income taxes	162	(195,268)
	(21,802)	(195,268)

Deferred tax

Components of the net deferred income tax liability are as follows:

	2013	2012
	$	$
Deferred income tax liability:		
Taxable temporary difference on property and equipment and intangibles	(460,873)	(249,620)
Deferred financing costs and other	(135,822)	–
Non-capital losses	382,345	35,432
Net deferred income tax liability	(214,350)	(214,188)

The following temporary differences and non-capital losses have not been recognized as realization is not considered probable:

	2013	2012
	$	$
Non-capital losses	6,987,369	6,462,591
Property, plant and equipment	16,810	20,565
Intangible assets	1,696,960	1,851,816
Tax deductible share issue costs	–	33,400
Financing costs	12,812	17,083
Other	14,001	176,343
	8,727,952	8,561,798

The Company has incurred Canadian non-capital losses of $6,813,550 that can be carried forward to reduce taxes payable in Canada. The losses expire at various times through December 31, 2033. The Company has incurred US non-capital losses of $1,170,253 that can be carried forward to reduce taxes payable in the US. The losses expire at various times through December 31, 2033.

(expressed in Canadian dollars)

23 Commitments and contingency

Commitments

The Company leases office premises in Mississauga, Ontario, Canada. The lease expires on September 30, 2018. Additionally, the Company leases facilities in Albany, which expires on March 31, 2014, Syracuse, which expires on August 31, 2015, Milwaukee, which expires on August 31, 2017 and New York City, which expires on September 30, 2015. During the year ended December 31, 2013, the Company entered into two new leases in Charlotte, North Carolina and Mississauga, Ontario. Certain contracts include renewal options for various periods of time. For the year ended December 31, 2013, the Company incurred $240,528 (December 31, 2012 - $248,314) 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	182,633
Between 1 and 5 years	468,389
Total	651,022

Contingency

During the second quarter of 2010, four franchisees filed a complaint with the United States District Court, South District of New York. As of December 31, 2013, three franchisees have permanently withdrawn from the legal complaint and the remaining litigant’s claim was dismissed by the United States District Court on September 4, 2013. In October 2013, the franchisee issued an appeal to the Federal Courts. Subsequent to year-end, on February 14, 2014, the franchisee dismissed the appeal to the Federal Courts. As of April 29, 2014, all legal claims have been settled. No amounts, other than legal costs, have been accrued in these consolidated financial statements relating to this appeal.

24 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, accrued liabilities, notes payable, long-term debt and convertible debenture liability.

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 is subject to interest rate risk, as it earns interest at prevailing and fluctuating market rates. The Company has a fixed rate on notes receivable from franchisees ranging from 4.25% to 8.25% per annum, and the line of credit facility has a fixed interest rate of 10% per annum. The truck loans have fixed interest rates ranging from 6.502% to 8.14% per annum. These financial instruments are subject to interest rate fair value risk, as their fair values will fluctuate as a result of changes in market rates.

(expressed in Canadian dollars)

24 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 related to franchising and licensing

The accounts and notes 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 existing franchisees. In addition, the receivable balances are monitored on an ongoing basis. As of December 31, 2013, 6 franchisees accounted for 79% of the accounts receivable and notes receivable balance related to franchising and licensing (December 31, 2012 - 6 franchises accounted for 83%). For the year ended December 31, 2013, 3 franchisees accounted for 31% of the Company's revenues related to franchising and licensing (December 31, 2012 - 3 franchisees accounted for 36%). As of December 31, 2013, there are no accounts and notes receivable over 90 days old (December 31, 2012 – nil).

The following is a reconciliation of the allowance for credit losses from accounts and notes receivables from franchisees:

	2013	2012
	$	$
Opening balance	–	86,764
Additions	14,453	–
Recovery of trade receivables	–	(86,764)
Foreign exchange	–	–
Closing balance	14,453	–

Also refer to note 7 for details of notes receivable from franchisees.

Receivables related to corporate operations

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, one-time customers are required to make payments for services by way of preapproved credit card. In addition, the receivable balances with customers are monitored on an ongoing basis and collection efforts are dedicated on an ongoing basis to limit the Company's exposure to bad debt. At December 31, 2013 and December 31, 2012, no customer accounted for more than 10% of the accounts receivable balance. For the years ended December 31, 2013 and December 31, 2012, no customer accounted for more than 10% of the Company's revenues in this category. As of December 31, 2013, 2% of accounts receivable in this category was over 90 days old (December 31, 2012 – 13%). The Company has not recorded an allowance for credit losses from accounts receivable from shredding customers (December 31, 2012 - $2,682). The Company does not have any reason to believe it will not collect all remaining balances.

(expressed in Canadian dollars)

24 Financial instruments and fair values (continued)

Credit risk (continued)

The aging analysis for accounts receivable past due related to corporate operations is as follows:

	2013	2012
	$	$
Past due but not impaired		
60 to 90 days	21,209	22,130
91 days to 180 days	9,979	39,133
Impaired		
60 to 90 days	–	2,863
91 days to 180 days	–	–

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. Fluctuations in the Canadian dollar (CAD) and the US dollar (USD) 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) or a +5% (appreciation of the USD) against the CAD, from an average rate of USD$1.00 = CAD$1.0303, the total impact to net loss would be a decrease/increase of approximately $64,000.

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 $9.3 million at December 31, 2013. 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 current liabilities of $1,430,600 at December 31, 2013 (December 31, 2012 - $739,119), are due to be settled within one year from the date of the Statement of Financial Position. At December 31, 2013, the Company has cash of $348,998.

(expressed in Canadian dollars)

24 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	606,508	–	–	–
Notes payable	87,384	25,420	98,451	–
Contingent consideration	5,318	–	–	–
Convertible debentures	–	–	337,882	–
Long-term debt	96,539	551,465	7,476,411	–

Interest	**Less than 3 months** **$**	**3 months to 1 year** **$**	**2 – 5 years** **$**	**Over 5 years** **$**
Notes payable	939	1,924	563	–
Convertible debentures	-	28,125	84,375	–
Long-term debt	30,711	666,456	1,697,463	–

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	606,508	–	–	–
Notes payable	88,323	27,344	99,014	–
Contingent consideration	5,318	–	–	–
Convertible debentures	-	28,125	422,257	–
Long-term debt	127,250	1,217,921	9,173,874	–

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 (note 7), 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 December 31, 2013, amounted to $314,744 (December 31, 2012 - $234,434) with fair value estimated to amount to $306,286 (December 31, 2012 - $212,694), respectively.

(expressed in Canadian dollars)

25 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.

26 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).

(expressed in Canadian dollars)

26 Segment reporting (continued)

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

	Franchising and licensing	**Corporate locations**	**Corporate Overhead**	**Total**
ASSETS	**December 31, 2013 $**	**December 31, 2013 $**	**December 31, 2013 $**	**December 31, 2013 $**
Current assets				
Cash	100,857	140,902	107,239	348,998
Cash attributable to the Ad Fund	63,375	–	–	63,375
Trade receivables	74,980	357,917	16,085	448,982
Prepaid expenses	27,128	46,482	24,408	98,018
Notes receivable from franchisees	148,633	–	–	148,633
Total current assets	414,973	545,301	147,732	1,108,006
Non-current assets				
Notes receivable from franchisees	166,112	–	–	166,112
Equipment	–	2,195,083	–	2,195,083
Intangible assets	866,422	2,088,437	1,104,388	4,059,247
Goodwill	–	1,455,467	–	1,455,467
Total assets	1,447,507	6,284,288	1,252,120	8,983,915
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities	119,022	235,562	251,924	606,508
Current portion of notes payable	9,271	103,533	–	112,804
Current portion of long-term debt	–	648,004	–	648,004
Contingent consideration	–	5,318	–	5,318
Deferred revenue	57,966			57,966
Total current liabilities	186,259	992,417	251,924	1,430,600
Non-current liabilities				
Long-term debt	–	7,476,411	–	7,476,411
Long- portion of notes payable	–	98,452	–	98,452
Convertible debenture	–	–	337,882	337,882
Deferred tax liability	214,350	–	–	214,350
Total liabilities	400,609	8,567,280	589,806	9,557,695

(expressed in Canadian dollars)

26 Segment reporting (continued)

	Franchising and licensing	Corporate locations	Corporate Overhead	Total
	December 31, 2012	December 31, 2012	December 31, 2012	December 31, 2012
ASSETS	$	$	$	$
Current assets				
Cash	47,781	96,716	387,543	532,040
Cash attributable to the Ad Fund	48,031	–	–	48,031
Trade receivables	117,373	295,503	11,188	424,064
Prepaid expenses	31,059	46,562	20,328	97,949
Notes receivable from franchisees	40,765	–	–	40,765
Total current assets	285,009	438,781	419,059	1,142,849
Non-current assets				
Notes receivable from franchisees	193,669	–	–	193,669
Equipment	–	1,265,284	2,112	1,267,395
Intangible assets	941,110	1,402,213	998,919	3,342,242
Goodwill	–	1,361,705	–	1,361,705
Total assets	1,419,788	4,467,982	1,420,090	7,307,860
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities	144,610	248,085	111,815	504,510
Current portion of notes payable	15,213	66,170	–	81,383
Current portion of long-term debt	–	138,302	–	138,302
Contingent consideration	–	14,924	–	14,924
Total current liabilities	159,823	467,481	111,815	739,119
Non-current liabilities				
Long-term debt	–	6,359,020	–	6,359,020
Long-term portion of notes payable	–	137,410	–	137,410
Convertible debenture	–	–	333,119	333,119
Deferred tax liability	214,188	–	–	214,188
Total liabilities	374,011	6,963,911	444,934	7,782,856

The Company incurred $947,006 in capital expenditures and sold equipment of $561,751 relating to its corporate operations during the year ended December 31, 2013 (December 31, 2012 - $423,726). The Company incurred $618,469 in capital acquisitions relating to its corporate operations during the year ended December 31, 2013 (December 31, 2011 – $661,342). The Company incurred $420 in capital expenditures related to its franchising operations for the year ended December 31, 2013 (December 31, 2012 - $4,059).

(expressed in Canadian dollars)

26 Segment reporting (continued)

Geographic information

	December 31, 2013	December 31, 2012
Canada	**$**	**$**
Equipment	–	2,112
Intangible assets	1,104,388	998,919
United States		
Notes receivable from franchisees	314,745	234,434
Equipment	2,195,083	1,265,283
Intangible assets	2,954,859	2,343,323
Goodwill	1,455,467	1,361,705
Total		
Notes receivable from franchisees	314,745	234,434
Equipment	2,195,083	1,267,395
Intangible assets	4,059,247	3,342,242
Goodwill	1,455,467	1,361,705

Revenue

All revenues were attributed to the United States, with the exception of license fees, which were attributed to the Middle East.

(expressed in Canadian dollars)

26 Segment reporting (continued)

Net loss by operating segment

Total net loss by reportable operating segment is as follows:

	For the year ended December 31, 2013			
	Franchising and licensing	**Corporate locations**	**Corporate overhead**	**Total**
	$	**$**	**$**	**$**
Revenue	1,241,800	3,427,283	–	4,669,083
Direct costs	–	(2,194,157)	–	(2,194,157)
Corporate overhead	(755,201)	(403,805)	(610,452)	(1,769,458)
Depreciation and amortization	(445,004)	(552,309)	–	(997,313)
Foreign currency gain, net	–	–	352,971	352,971
Interest expense	–	(679,208)	(32,890)	(712,098)
Interest income	7,055	–	–	7,055
Gain on sale of assets	–	2,240	–	2,240
Gains (losses) related to business combinations	(96,700)	244,928	–	148,228
Reversal of impairment of intangible assets	132,382	–	298,798	431,180
Income tax recovery	21,802	–	–	21,802
Net income (loss)	106,134	(155,028)	8,427	(40,467)

	For the year ended December 31, 2012			
	Franchising and licensing	**Corporate locations**	**Corporate overhead**	**Total**
	$	**$**	**$**	**$**
Revenue	1,128,055	2,950,505	–	4,078,560
Direct costs	–	(2,330,170)	–	(2,330,170)
Corporate overhead	(653,889)	(302,793)	(930,292)	(1,886,974)
Depreciation and amortization	(546,339)	(478,420)	–	(1,024,759)
Foreign currency loss, net	–	–	(132,505)	(132,505)
Interest expense	–	(595,146)	–	(595,146)
Interest income	4,785	–	–	4,785
Gain on franchise agreements	138,439	–	–	138,439
Gain on sale of assets	–	7,540	–	7,540
Loss on settlement of pre-existing litigation	(712,567)	–	–	(712,567)
Impairment of intangible assets	(158,757)	–	(154,147)	(312,904)
Impairment of goodwill	–	(232,103)	–	(232,103)
Income tax recovery	195,268	–	–	195,268
Net loss	(605,005)	(980,587)	(1,216,944)	(2,802,536)

For the year ended December 31, 2013, the Company operated five corporate locations. For the year ended December 31, 2012, the Company operated four corporate locations.

(expressed in Canadian dollars)

27 Related party balances and transactions

A Director of the Company is the owner of the Tampa Bay, Florida Proshred franchise. Included in accounts receivable at December 31, 2013, is $727 (2012 - $1,945) due from this franchise. During the year ended December 31, 2013, the Company earned royalty and service fees amounting to $88,981 (2012 - $78,289) from this franchise.

Until December 31, 2013, the Director's franchise managed the corporately owned Proshred Miami business on the Company's behalf. The Company earned royalty and service fees of $27,099 during the year ended December 31, 2013 from the Miami operations. Included in accounts receivable at December 31, 2013 is $2,137 due from the Miami operations.

The Company has a line of credit facility with a related party entity, the Company's largest shareholder, for a maximum of $6.03 million, repayable on November 27, 2017, bearing interest at a fixed rate of 10% per annum (refer to note 16). The Company has drawn from its line of credit in order to finance the purchase of its corporate locations including Syracuse, Albany, Milwaukee in 2010 and New York City and Miami in 2012 as well as for general business purposes. Refer to Note 16 for additional information.

Included in selling, general and administrative expenses for the year ended December 31, 2013 are insurance premium amounts of $18,564 (December 31, 2012 - $13,037) paid to an insurance brokerage firm, managed by a Director of the Company.

On December 31, 2012, the Company obtained equity and debt funding, directly or indirectly, from certain members of the Company's Board of Director's. The Company issued $375,000 convertible, unsecured subordinated, debentures. The debentures have a five year term and a coupon of 7.5% interest per annum payable annually. The debenture holders may defer interest otherwise due and payable until the next interest payment date, in which case the deferred interest payment will accrue additional interest at 7.5% per annum. Each $1,000 principal amount of debenture entitles the holder to convert to approximately 3,333 common shares at a conversion price of $0.30 per share.

In order to finance the purchase of the Proshred Charlotte franchise on July 31, 2013, the Company entered into the following loan agreements with certain members of the Company's Board of Directors and their affiliates:

(a) A 5 year loan and security agreement in the amount of CAD$525,750 maturing July 31, 2018. The loan bears interest at 9% per annum with interest payable semi-annually;

(b) A 5 year loan and security agreement in the amount of US$75,000 maturing July 31, 2018. The loan bears interest at 9% per annum with interest payable semi-annually;

(c) A 4 year loan and security agreement in the amount of CAD$100,000 with monthly blended payments of principal and interest of CAD$2,488 maturing July 31, 2017. The loan bears interest at 9% per annum;

(d) A 4 year loan and security agreement in the amount of US$50,000 with monthly blended payments of principal and interest of US$1,244 maturing July 31, 2017. The loan bears interest at 9% per annum; and

(expressed in Canadian dollars)

27 Related party balances and transactions (continued)

e) A 5 year loan and security agreement in the amount of US$500,000, repayable with monthly blended payments of principal and interest of US$12,681 maturing August 5, 2017. The loan bears interest at 10% per annum and is secured by four shredding vehicles and two non-shredding vehicles with a carrying value of $518,881 at December 31, 2013. The value of the loan on December 31, 2013 is $495,513.

28 Subsequent events

In December of 2013, the Company entered into an agreement with a new franchisee to operate a Proshred shredding business in Southern New Jersey. The Company recognized franchise fee revenue in January of 2014. The Company expects its new franchisee to commence operations in the second quarter of 2014.

On February 14, 2014, the Company and the franchisee agreed to settle all litigation and the appeal filed with the US District Court was withdrawn. As of April 29, 2014, all legal claims have been settled.