RediShred Capital Corp.

Consolidated Interim Financial Statements
June 30, 2013 and 2012
(Unaudited – Prepared by Management)

(expressed in Canadian dollars)

August 27, 2013

In accordance with National Instrument 51-102, released by the Canadian Securities Administrators, the Corporation discloses that its auditors have not reviewed the unaudited consolidated interim financial statements for the period ended June 30, 2013.

RediShred Capital Corp.

Consolidated Statements of Financial Position

(expressed in Canadian dollars)

	June 30, 2013 $	December 31, 2012 $
Assets		
Current assets		
Cash	224,024	532,040
Cash attributable to the Advertising Fund (note 3)	65,092	48,031
Trade receivables	383,342	424,064
Prepaid expenses	105,414	97,949
Notes receivable from franchisees	69,625	40,765
	847,497	1,142,849
Non-current assets		
Notes receivable from franchisees	162,835	193,669
Equipment (note 4)	1,380,268	1,112,105
Intangible assets (note 5)	3,141,801	3,210,580
Goodwill (notes 6)	1,439,320	1,361,705
	6,124,224	7,020,908
Assets classified as held for sale (note 7)	–	286,952
Total assets	6,971,721	7,307,860
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	464,216	504,510
Current portion of notes payable	84,487	81,383
Current portion of long-term debt (note 8)	182,587	99,692
Deferred revenue	5,259	–
Contingent consideration	9,669	14,924
	746,218	700,509
Non-current liabilities		
Long-term debt (note 8)	6,410,932	6,292,452
Long-term notes payable	81,642	137,410
Deferred tax liability	209,513	214,188
Convertible debenture	335,501	333,119
	7,037,588	7,677,678
Liabilities directly associated with the assets classified as held for sale (note 7)	–	105,178
Total liabilities	7,783,806	7,782,856
Shareholders' Deficiency	(812,085)	(474,996)
Total liabilities and shareholders' deficiency	6,971,721	7,307,860

Commitments and contingency (note 13)

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

RediShred Capital Corp.

Consolidated Statements of Comprehensive Loss

(expressed in Canadian dollars)

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2013	**2012**	**2013**	**2012**
	$	**$**	**$**	**$**
Revenue (note 10)	1,060,860	965,831	1,980,215	2,066,881
Corporate operating locations expenses (note 11)	(622,823)	(746,806)	(1,238,574)	(1,496,494)
Selling, general and administrative expenses (note 12)	(350,450)	(513,510)	(726,785)	(1,218,445)
Income (loss) before interest, income taxes and other items	87,587	(294,485)	14,856	(648,058)
Loss on settlement of pre-existing relationship	–	(1,365)	–	(352,065)
Gain on sale of assets	–	–	3,725	–
Interest expense	(169,731)	(140,199)	(336,157)	(278,566)
Interest income	1,304	1,971	3,949	2,453
Loss before income taxes	(80,840)	(434,078)	(313,627)	(1,276,236)
Income tax recovery	12,560	15,693	24,929	34,383
Net loss for the period	(68,280)	(418,385)	(288,698)	(1,241,853)
Other comprehensive (loss) income, net of tax				
Foreign currency translation (loss) income	(13,944)	5,258	(48,520)	(544)
Comprehensive loss for the period	(82,224)	(413,127)	(337,218)	(1,242,397)
Net loss per share				
Basic and diluted	(0.00)	(0.01)	(0.01)	(0.04)
Weighted average number of commons shares outstanding – basic and diluted	28,884,658	28,884,658	28,884,658	28,884,658

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

RediShred Capital Corp.

Consolidated Statements of Changes in Equity

(expressed in Canadian dollars)

	Capital stock and warrants $ (note 9)	Contributed surplus $	Accumulated other comprehensive 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 period	–	–	–	(2,802,536)	(2,802,536)
Other comprehensive loss					
Foreign currency translation loss	–	–	(5,038)	–	(5,038)
Comprehensive loss for the period	–	–	–	–	(2,807,574)
Issue of convertible debentures (net of costs)	–	20,077	–	–	20,077
Stock-based compensation (note 9)	–	32,933	–	–	32,933
Balance – December 31, 2012	8,585,808	367,957	(71,561)	(9,357,200)	(474,996)
Net loss for the period	–	–	–	(288,698)	(288,698)
Other comprehensive loss					
Foreign currency translation loss	–	–	(48,520)	–	(48,520)
Comprehensive loss for the period	–	–	–	–	(337,218)
Stock-based compensation (note 9)	–	129	–	–	129
Balance – June 30, 2013	8,585,808	368,086	(120,081)	(9,645,898)	(812,085)

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

RediShred Capital Corp.

Consolidated Statements of Cash Flows

(expressed in Canadian dollars)

	For the 3 months ended June 30		*For the 6 months ended June 30*	
Cash provided by (used in)	**2013 $**	**2012 $**	**2013 $**	**2012 $**
Operating activities				
Net loss for the period	(68,280)	(418,385)	(288,698)	(1,241,853)
Items not affecting cash				
Amortization of equipment and intangible assets	229,538	269,646	451,777	538,298
Stock-based compensation	64	211	129	901
Unrealized foreign currency (gain) loss	(166,946)	(93,544)	(290,107)	8,976
Impairment of note receivable	–	59	–	15,089
Gain on sale of assets	–	–	(3,725)	–
Loss on settlement of pre-existing litigation	–	1,365	–	352,065
Income tax recovery	(12,560)	(15,693)	(24,929)	(18,690)
	(18,184)	(256,341)	(155,553)	(345,214)
Net change in non-cash working capital balances				
Decrease (increase) in trade receivables	445	10,502	40,722	(155,714)
Decrease (increase) in prepaid expenses	32,593	13,623	(7,463)	(10,243)
(Increase) decrease in notes receivable from franchisees	(492)	16,764	1,974	23,672
(Increase) decrease in income taxes recoverable	–	(188)	–	7,067
Increase (decrease) in deferred revenue	5,259	–	5,259	(10,170)
(Decrease) in accounts payable and accrued liabilities	(237,479)	(265,770)	(40,294)	(129,917)
Net cash used in operations	(217,858)	(481,410)	(155,355)	(620,519)
Financing activities				
Repayment of long-term debt	(42,070)	(9,244)	(74,945)	(25,456)
(Repayment) borrowing on line of credit	(50,912)	250,000	(50,912)	250,000
Repayment of notes payable	(50,859)	–	(52,664)	–
	(143,841)	240,756	(178,521)	224,544
Investing activities				
Cash paid on acquisition of franchise	–	–	–	(2,403,593)
Cash held by advertising fund	4,597	149,151	(17,061)	84,476
Sale of capital assets	53,200	–	53,200	–
Purchase of capital assets	(1,500)	(1,159)	(20,884)	(36,732)
	56,297	147,992	15,255	(2,355,849)
Effect of foreign exchange rate changes on cash	6,840	5,410	10,605	(3,032)
Net change in cash for the period	(298,562)	(87,252)	(308,016)	(2,754,856)
Cash – Beginning of period	522,586	344,182	532,040	3,011,786
Cash – End of period	224,024	256,930	224,024	256,930

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

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 6790 Century Avenue, Suite 200, Mississauga, Ontario, L5N 2V8.

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

2 Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting.* The consolidated financial statements should be read in conjunction with the most recently issued Annual Report of Redishred for the year ended December 31, 2012, which includes information necessary or useful to understanding the Company's business and financial statement presentation. These interim consolidated financial statements comprise the financial statements of Redishred and its subsidiaries as at June 30, 2013. Together, Redishred and its subsidiaries are referred to as "the Company."

The Company's significant accounting policies were presented as Note 3 to the Audited Consolidated Financial Statements for the year ended December 31, 2012 and have been consistently applied in the preparation of these consolidated financial statements. The results reported in these consolidated financial statements should not be regarded as necessarily indicative of results that may be expected for the entire year. Certain prior period amounts have been reclassified to conform to the current period's presentation.

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

The interim consolidated financial statements of the Company for the three and six months ended June 30, 2013 were authorized for issue in accordance with a resolution of the Directors on August 22, 2013.

3 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 June 30, 2013, the Ad Fund was in a net surplus position of $131,618 (December 31, 2012 – $121,469), including cash attributable to the Ad Fund amounting to $65,092 (December 31, 2012 - $48,031)

(expressed in Canadian dollars)

4 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)
Assets held for sale (note 7)	–	–	(17,750)	(39,375)	(84,790)	–	(30,000)	(171,915)
Foreign exchange	(731)	(389)	(877)	(2,056)	(4,819)	(561)	(304)	(9,737)
As at December 31, 2012	126,199	59,485	136,813	384,617	838,766	92,901	22,710	1,661,491
Additions	2,454	2,385	13,276	142,901	371,717	–	–	532,733
Assets held for sale (note 7)	–	–	17,750	39,375	84,790		30,000	171,915
Sale of assets	–	–	(1,433)	(100,741)	(231,000)	(82,925)	–	(416,099)
Foreign exchange	1,969	469	8,620	24,147	61,361	546	2,930	100,042
As at June 30, 2013	130,622	62,339	175,026	490,299	1,125,634	10,522	55,640	2,050,082

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)
Assets held for sale (note 7)	–	–	(1,650)	(3,662)	(7,885)	–	(2,790)	(15,987)
Foreign exchange	(577)	(359)	(285)	(570)	(1,280)	(203)	(142)	(3,416)
As at December 31, 2012	96,061	53,473	37,497	105,397	225,311	23,183	8,464	549,386
Depreciation	3,793	2,137	15,026	30,181	66,529	1,833	5,737	125,236
Assets held for sale (note 7)	–	–	1,650	3,662	7,885	–	2,790	15,987
Sale of assets	–	–	–	(6,903)	(19,933)	(23,157)	–	(49,993)
Foreign exchange	294	2,881	3,811	3,591	17,244	1,296	81	29,198
As at June 30, 2013	100,148	58,491	57,984	135,928	297,036	3,155	17,072	669,814
Net book value								
As at December 31, 2012	30,138	6,012	99,316	279,220	613,455	69,718	14,246	1,112,105
As at June 30, 2013	30,474	3,848	117,042	354,371	828,598	7,367	38,568	1,380,268

During the six months ended June 30, 2013, the Company sold four older shredding vehicles and purchased two new shredding vehicles obtaining vendor financing (refer to note 8). The Company also closed down its' baling facility and sold its' baler and forklift (classified as recycling equipment). The foreign exchange adjustment is a result of the translation of corporate equipment from US functional currency dollars to Canadian presentation dollars at June 30, 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."

5 Intangible assets

Cost	Franchise agreements	Proshred system	Trademarks and 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	6,692,296
Acquisitions	–	–	–	320,000	760,000	1,080,000
Removal of original franchise agreements	(372,000)	–	–	–	–	(372,000)
Assets held for sale (note 7)	–	–	–	(50,000)	(90,000)	(140,000)
Foreign exchange	(53,215)	–	–	(13,344)	(9,954)	(76,513)
As at December 31, 2012	2,365,361	978,000	1,672,500	795,666	939,722	6,751,249
Assets held for sale (note 7)	–	–	–	50,000	90,000	140,000
Foreign exchange	134,595	–	–	46,580	58,891	240,066
As at June 30, 2013	2,499,956	978,000	1,672,500	892,246	1,088,613	7,131,315

Accumulated amortization and impairment	Franchise agreements	Proshred system	Trademarks and 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	3,133,490
Amortization	248,700	92,725	130,453	183,768	98,655	754,301
Removal of original franchise agreements	(190,493)	–	–	–	–	(190,493)
Impairment	158,757	64,237	89,974	–	–	312,968
Assets held for sale (note 7)	–	–	–	(4,625)	(4,163)	(8,788)
Foreign exchange	(22,463)	–	–	(4,500)	(1,312)	(28,275)
As at December 31, 2012	1,424,251	562,681	1,088,452	338,610	126,225	3,540,219
Amortization	92,634	40,596	56,521	81,000	51,746	322,497
Assets held for sale (note 7)	–	–	–	4,625	4,163	8,788
Foreign exchange	85,737	–	–	22,042	10,231	118,010
As at June 30, 2013	1,602,622	603,277	1,144,973	446,277	192,365	3,989,514
Net book value						
As at December 31, 2012	941,110	414,869	584,048	457,056	813,497	3,210,580
As at June 30, 2013	897,328	374,723	527,527	445,969	896,248	3,141,801

There were no additions to intangible assets during the three and six months ended June 30, 2013. The foreign exchange adjustment is a result of the translation of foreign operation intangible assets in US dollars to Canadian dollars at June 30, 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.

(expressed in Canadian dollars)

6 Goodwill

The following table presents goodwill for the six months ended June 30, 2013 and for the year ended December 31, 2012:

	June 30, 2013	December 31, 2012
	$	$
Opening balance	1,361,705	878,270
Acquisitions	–	737,292
Impairment of goodwill	–	(232,196)
Foreign currency translation	77,615	(21,661)
Closing balance	1,439,320	1,361,705

7 Assets classified as held for sale

On May 27, 2013, the Company decided that the Miami business will be corporately operated and it will not sell the business. 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 18). The Company is expected to operate the Miami location commencing in the fourth quarter of 2013. As the Miami business is no longer held for sale, the results of the operations of the entity previously presented in discontinued operations have been reclassified and included in income from continuing operations. The assets previously held for sale and liabilities directly associated with the assets 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 (please refer to Note 17). 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.

8 Long-term debt

As at June 30, 2013 and December 31, 2012 long-term debt is comprised of:

	June 30, 2013	December 31, 2012
	$	$
Line of credit (i)	5,982,182	6,033,094
Less: deferred financing charges	(33,128)	(44,172)
Line of credit net of deferred financing charges	5,949,054	5,988,922
Truck loans (ii)	644,466	403,222
Total long-term debt	6,593,520	6,392,144
Less: current portion	(182,587)	(99,692)
Total	6,410,932	6,292,452

8 Long-term debt (continued)

(i) The line of credit was entered into on November 27, 2009 with a related party entity (refer to note 26) for a maximum amount of $4 million. The line of credit is 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, Milwaukee in 2010 and New York City and Miami in 2012 and for general business purposes. During the three months ended June 30, 2013, the Company paid down its' line of credit in the amount of $50,912.

(ii) 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 $286,969 at June 30, 2013. The value of the loan on June 30, 2013 is $152,136.

(ii) 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 $105,392 at June 30, 2013. The value of the loan on June 30, 2013 is $91,111.

(ii) 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 $180,728 at June 30, 2013. The value of the loan on June 30, 2013 is $113,537.

(ii) 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 $241,861 at June 30, 2013. The value of the loan on June 30, 2013 is $117,315.

(ii) 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 $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 $249,982 at June 30, 2013. The value of the loan on June 30, 2013 is $170,365.

9 Capital stock

a) Authorized

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

(expressed in Canadian dollars)

9 Capital stock (continued)

b) Issued and fully paid

For the three and six months ended June 30, 2013 and the year ended 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 June 30, 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 three and six months ended June 30, 2013, was 28,884,658 (December 31, 2012 - 28,884,658).

d) Stock options

At June 30, 2013, the Company has 1,423,750 options outstanding (December 31, 2012 – 1,691,250) and a weighted average exercise price of $0.24 (December 31, 2012 - $0.24). During the six months ended June 30, 2013, 267,500 stock options expired (for the six months ended June 30, 2012 – nil). There have been no stock options granted during the six months ended June 30, 2013 (for the six months ended June 30, 2012 – 10,000). The net stock compensation charge, for the six months ended June 30, 2013, after adjusting for stock option forfeitures, amounted to $129 (for the six months ended June 30, 2012 – $901).

e) Warrants

The Company issued two tranches of warrants in 2009. The first tranche was issued in connection with the private placement and the second related to the line of credit obtained. In connection with the line of credit, 1,000,000 warrants were issued on April 28, 2010 when the line of credit was first drawn upon in accordance with the line of credit agreement. These warrants were recorded in the consolidated financial statements in 2009 as performance by the counterparty was complete at that date. The fair value of these warrants has been recorded as deferred financing charges and is being amortized into income over the term of the facility and is also subject to a two-year holding period commencing on the date of issuance. This is a non-cash transaction and has been excluded from the consolidated statements of cash flows. Tranches 1 and 2 of warrants expire on November 27, 2014 and December 23, 2014, respectively.

f) Convertible debentures

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.

(expressed in Canadian dollars)

10 Revenue

The revenue earned by the Company for the three and six months ended June 30, 2013 and 2012 is broken down as follows:

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2013	**2012**	**2013**	**2012**
	$	**$**	**$**	**$**
Royalties	258,469	207,591	484,156	408,479
Franchise fees	–	–	–	93,850
License fees	1,394	694	2,559	1,069
Shredding services	644,078	618,885	1,198,305	1,260,054
Sale of paper products	145,506	138,661	272,541	303,429
Rental revenue	11,413	–	22,654	–
Total revenue	1,060,860	965,831	1,980,215	2,066,881

11 Corporate operating locations expenses by nature

The corporate operating locations expenses incurred by the Company for the three and six months ended June 30, 2013 and 2012 are broken down as follows:

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2013	**2012**	**2013**	**2012**
	$	**$**	**$**	**$**
Shredding expenses	167,752	197,196	316,928	358,739
Employee wages expense	224,314	252,049	441,534	522,554
Employee benefit expense	48,749	49,881	89,208	105,252
Office and administration expense	61,436	102,826	149,273	220,950
Depreciation – equipment	58,743	62,291	122,519	124,510
Amortization – intangible assets	61,829	82,563	119,112	164,489
Total corporate operating expenses	622,823	746,806	1,238,574	1,496,494

(expressed in Canadian dollars)

12 Selling, general and administrative expenses by nature

The selling, general and administrative expenses incurred by the Company for the three and six months ended June 30, 2013 and 2012 are broken down as follows:

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2013	**2012**	**2013**	**2012**
	$	**$**	**$**	**$**
Employee wages expense	170,766	183,811	363,713	375,349
Employee benefits expense	19,919	11,915	32,830	30,573
Share-based compensation	64	211	129	901
Professional fees	54,293	152,711	84,307	280,190
Technology	48,966	37,308	98,689	68,550
Rent and office expense	24,262	16,765	48,363	34,084
Selling and marketing	13,189	25,491	38,402	37,492
Bad debt expense	–	–	–	15,089
Amortization of deferred financing charges	5,522	5,522	11,043	11,043
Amortization – intangible assets	110,470	119,270	219,987	238,256
Foreign exchange (gain) loss	(160,444)	(87,059)	(278,918)	21,637
Other	63,443	47,565	108,240	105,281
Total selling, general and administrative expenses	350,450	513,510	726,785	1,218,445

Compensation of key management

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

	For the 3 months ended June 30		*For the 6 months ended June 30*	
	2013	**2012**	**2013**	**2012**
	$	**$**	**$**	**$**
Wages and benefits	149,796	146,996	303,866	297,368
Share-based compensation	32	61	64	459
Total	149,828	147,057	303,930	297,827

Compensation of key management personnel includes the Chief Executive Officer, Chief Financial Officer, President, and Vice President of Operations.

(expressed in Canadian dollars)

13 Commitments and contingency

Commitments

The Company leases office premises in Mississauga, Ontario, Canada. The lease expires on September 30, 2013. The Company has executed a lease for office premises in Mississauga, Ontario, Canada for October 1, 2013, which 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, 2016 and New York City, which expires on September 30, 2015. Certain contracts include renewal options for various periods of time. For the six months ended June 30, 2013, the Company incurred $138,153 (for the six months ended June 30, 2012 - $143,735) 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	168,944
Between 1 and 5 years	446,406
Over 5 years	9,195
Total	624,545

Contingency

During the second quarter of 2010, four franchisees filed a complaint with the United States District Court, South District of New York, which management of the Company believes is without merit. The complaint has listed the following causes of action, (1) breach of contract and breach of the implied covenant of good faith and fair dealing by PFC, (2) fraudulent misrepresentation by PFC, (3) negligent misrepresentation by PFC, and (4) violation of various state laws by PFC. As of June 30, 2013, one franchisee remains in the legal complaint and three franchisees have permanently withdrawn.

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

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

14 Financial instruments and fair values

The Company has various financial assets that consist of: cash, trade receivables and notes receivable from franchisees. The Company's financial liabilities include accounts payable, 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's cash is subject to cash flow 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.

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 June 30, 2013, 6 franchisees accounted for 75% of the accounts receivable and notes receivable balance related to franchising and licensing (December 31, 2012 - 6 franchises accounted for 83%). For the six months ended June 30, 2013, 3 franchisees accounted for 29% of the Company's revenues related to franchising and licensing (for the six months ended June 30, 2012 - 3 franchisees accounted for 31%). As of June 30, 2013, there are no accounts receivable over 90 days old (December 31, 2012 – nil).

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 June 30, 2013 and December 31, 2012, no customer accounted for more than 10% of the accounts receivable balance. For the six months ended June 30, 2013 and for the year ended December 31, 2012, no customer accounted for more than 10% of the Company's revenues in this category. As of June 30, 2013, 6% of accounts receivable in this category were over 90 days old (December 31, 2012 – 13%). The Company does not have any reason to believe it will not collect all remaining balances.

14 Financial instruments and fair values (continued)

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$1.0155, the total impact to net loss would be a decrease/increase of approximately $30,000.

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 $9.6 million at June 30, 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 Company does not have any financial covenants to comply with.

The current liabilities of $746,218 at June 30, 2013 (December 31, 2012 - $700,509), are due to be settled within one year from the date of the Statement of Financial Position.

At June 30, 2013, the Company has cash of $224,024 and working capital of $101,279.

(expressed in Canadian dollars)

14 Financial instruments and fair values (continued)

Liquidity risk (continued)

Principal	**Less than 3 months $**	**3 months to 1 year $**	**2 – 5 years $**	**Over 5 years $**
Accounts payable and accrued liabilities	464,216	–	–	–
Notes payable	1,740	82,748	81,641	–
Contingent consideration	9,669	–	–	–
Convertible debentures	–	–	335,501	–
Long-term debt	44,231	155,199	6,394,087	–

Interest	**Less than 3 months $**	**3 months to 1 year $**	**2 – 5 years $**	**Over 5 years $**
Notes payable	153	326	118	–
Convertible debentures	–	28,125	112,500	–
Long-term debt	10,882	329,368	636,676	–

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	464,216	–	–	–
Notes payable	1,893	83,074	81,759	–
Contingent consideration	9,669	–	–	–
Convertible debentures	–	28,125	448,001	–
Long-term debt	55,113	484,567	7,030,763	–

Fair value of financial instruments

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

These techniques involve uncertainties and are affected by the assumptions used and the judgments made regarding risk characteristics of various financial instruments, discount rates, estimate of future cash flows, future expected loss experience and other factors. The carrying value of the Company's notes receivable from franchisees at June 30, 2013, amounted to $232,460 (December 31, 2012 - $234,434) with fair value estimated to amount to $209,899 (December 31, 2012 - $212,694), respectively.

(expressed in Canadian dollars)

15 Capital management

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

16 Segment reporting

The business segments presented reflect the management structure of the Company and the way in which the Company's management reviews business performance. The Company operates three reportable operating segments, (1) the granting and managing of shredding business franchises under the "Proshred" trademark (Franchising and licensing), (2) the operation of corporately owned shredding businesses (Corporate locations) and (3) supporting the franchises and corporately owned shredding businesses (Corporate Overhead). Total assets and liabilities by reportable operating segment are as follows:

	Franchising and licensing	Corporate locations	Corporate Overhead	Total
	June 30, 2013	June 30, 2013	June 30, 2013	June 30, 2013
ASSETS	$	$	$	$
Current assets				
Cash	72,085	82,997	68,942	224,024
Cash attributable to the Ad Fund	65,092	–	–	65,092
Trade receivables	78,382	292,982	11,978	383,342
Prepaid expenses	28,885	29,835	46,694	105,414
Notes receivable from franchisees	69,625	–	–	69,625
Total current assets	314,069	405,814	127,614	847,497
Non-current assets				
Notes receivable from franchisees	162,835	–	–	162,835
Equipment	–	1,380,268	–	1,380,268
Intangible assets	897,328	1,342,218	902,255	3,141,801
Goodwill	–	1,439,320	–	1,439,320
Total assets	1,374,232	4,567,620	1,029,869	6,971,721
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities	74,092	185,570	204,554	464,216
Current portion of notes payable	12,671	71,816	–	84,487
Current portion of long-term debt	–	182,587	–	182,587
Contingent consideration	–	9,669	–	9,669
Deferred revenue	5,259	–	–	5,259
Total current liabilities	92,022	449,642	204,554	746,218
Non-current liabilities				
Long-term debt	–	6,410,932	–	6,410,932
Current portion of notes payable	–	81,642	–	81,642
Convertible debenture	–	–	335,501	335,501
Deferred tax liability	209,513	–	–	209,513
Total liabilities	301,535	6,942,216	540,055	7,783,806

(expressed in Canadian dollars)

16 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	–	1,109,993	2,112	1,112,105
Intangible assets	941,110	1,270,551	998,919	3,210,580
Goodwill	–	1,361,705	–	1,361,705
Assets held for sale	–	286,952	–	286,952
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	–	99,692	–	99,692
Contingent consideration	–	14,924	–	14,924
Total current liabilities	159,823	428,871	111,815	700,509
Non-current liabilities				
Long-term debt	–	6,292,452	–	6,292,452
Current portion of notes payable	–	137,410	–	137,410
Convertible debenture	–	–	333,119	333,119
Deferred tax liability	214,188	–	–	214,188
Liabilities associated with assets held for sale	–	105,178	–	105,178
Total liabilities	374,011	6,963,911	444,934	7,782,856

The Company sold $333,174 in capital assets relating to its corporate operations during the six months ended June 30, 2013 and purchased $559,465 in capital assets relating to its corporate operations during the same period. The Company incurred $653,700 in capital expenditures relating to the acquisition of New York City, during the six months ended June 30, 2012. The Company did not incur capital expenditures related to its franchising operations for the six months ended June 30, 2013 (for the six months ended June 30, 2012 - $1,585).

(expressed in Canadian dollars)

16 Segment reporting (continued)

Geographic information

	June 30, 2013	December 31, 2012
Canada	**$**	**$**
Equipment	–	2,112
Intangible assets	902,253	998,919
United States		
Notes receivable from franchisees	232,460	234,434
Equipment	1,380,268	1,109,993
Intangible assets	2,239,548	2,211,661
Goodwill	1,439,320	1,361,705
Assets held for sale	–	286,952
Total		
Notes receivable from franchisees	232,460	234,434
Equipment	1,380,268	1,112,105
Intangible assets	3,141,801	3,210,580
Goodwill	1,439,320	1,361,705
Assets held for sale	–	286,952

Revenue

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

For the three months ended,	June 30, 2013	June 30, 2012
	$	**$**
United States		
Royalties	258,469	207,591
Franchise fees	–	–
Shredding services	644,078	618,885
Sale of paper products	145,506	138,661
Rental revenue	11,413	–
Middle East		
License fees	1,394	694

(expressed in Canadian dollars)

16 Segment reporting (continued)

Geographic information (continued)

For the six months ended,	June 30, 2013	June 30, 2012
	$	$
United States		
Royalties	484,156	408,479
Franchise fees	–	93,850
Shredding services	1,198,305	1,260,054
Sale of paper products	272,541	303,429
Rental revenue	22,654	–
Middle East		
License fees	2,559	1,069

Net loss by operating segment

Total net loss by reportable operating segment is as follows:

	For the three months ended June 30, 2013			
	Franchising and licensing	Corporate locations	Corporate overhead	Total
	$	$	$	$
Revenue	259,935	800,925	–	1,060,860
Direct costs	–	(501,916)	–	(501,916)
Corporate overhead	(133,997)	(105,221)	(155,858)	(395,076)
Depreciation and amortization	(115,991)	(120,570)	–	(236,561)
Foreign exchange gain	–	–	160,280	160,280
Interest expense	–	(161,507)	(8,224)	(169,731)
Interest income	1,304	–	–	1,304
Income tax recovery	12,560	–	–	12,560
Net income (loss) from operations	23,811	(88,289)	(3,802)	(68,280)

	For the three months ended June 30, 2012			
	Franchising and licensing	Corporate locations	Corporate overhead	Total
	$	$	$	$
Revenue	208,285	757,546	–	965,831
Direct costs	–	(601,949)	–	(601,949)
Corporate overhead	(123,578)	(70,577)	(281,625)	(475,780)
Loss on pre-existing relationship	–	(1,365)	–	(1,365)
Depreciation and amortization	(124,792)	(144,854)	–	(269,646)
Foreign exchange gain	–	–	87,059	87,059
Interest expense	–	(140,199)	–	(140,199)
Interest income	1,971	–	–	1,971
Income tax recovery	15,693	–	–	15,693
Net loss from operations	(22,421)	(201,398)	(194,566)	(418,385)

(expressed in Canadian dollars)

16 Segment reporting (continued)

Net loss by operating segment (continued)

	For the six months ended June 30, 2013			
	Franchising and licensing $	Corporate locations $	Corporate overhead $	Total $
Revenue	486,715	1,493,500	–	1,980,215
Direct costs	–	(996,942)	–	(996,942)
Corporate overhead	(255,964)	(202,642)	(316,068)	(774,674)
Depreciation and amortization	(231,030)	(241,631)	–	(472,661)
Foreign exchange gain	–	–	278,918	278,918
Interest expense	–	(319,712)	(16,445)	(336,157)
Interest income	3,949	–	–	3,949
Gain on sale of assets	–	3,725	–	3,725
Income tax recovery	24,929	–	–	24,929
Net income (loss) from operations	28,599	(263,702)	(53,595)	(288,698)

	For the six months ended June 30, 2012			
	Franchising and licensing $	Corporate locations $	Corporate overhead $	Total $
Revenue	503,399	1,563,482	–	2,066,881
Direct costs	–	(1,207,495)	–	(1,207,495)
Corporate overhead	(274,925)	(138,632)	(533,952)	(947,509)
Loss on pre-existing relationship	–	(352,065)	–	(352,065)
Depreciation and amortization	(249,299)	(288,999)	–	(538,298)
Foreign exchange loss	–	–	(21,637)	(21,637)
Interest expense	–	(278,566)	–	(278,566)
Interest income	2,453	–	–	2,453
Income tax recovery	34,383	–	–	34,383
Net income (loss) from operations	16,011	(702,275)	(555,589)	(1,241,853)

17 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 June 30, 2013, is $345 (December 31, 2012 - $1,945) due from this franchise. During the six months ended June 30, 2013, the Company earned royalty and service fees amounting to $42,801 (for the six months ended June 30, 2012 - $39,423) from this franchise.

The Director’s franchise is currently jointly managing the Proshred Miami business acquired by the Company. The Company earned royalty and service fees of $13,779 during the six months ended June 30, 2013 from the Miami operations. Included in accounts receivable at June 30, 2013 is $2,072 due from the Miami operations (December 31, 2012 - $2,528).

17 Related party balances and transactions (continued)

The Company has a line of credit facility with a related party entity, one of the Company's significant shareholders, for a maximum of $6.03 million, repayable on November 27, 2014, bearing interest at a fixed rate of 10% per annum. 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 8 for additional information.

Included in selling, general and administrative expenses for the six months ended June 30, 2013 are insurance premium amounts of $9,275 (for the six months ended June 30, 2012- $9,843) 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.

Subsequent to the second quarter of 2013, the Company acquired the Proshred Charlotte business from an existing franchisee. In order to finance the acquisition, Proshred Charlotte Inc. has obtained loans aggregating $1,250,000 from a group comprised of members of the Company's Board of Directors and their affiliates and associates.

18 Subsequent events

i) On June 24, 2013, the Company entered into an agreement with a new franchisee to operate a Proshred shredding business in San Francisco/San Jose, California. The franchise fee of US$153,650 associated with this new franchise will be recognized in the third quarter of 2013. The Company expects its new franchise to commence operations in the third quarter of 2013.

ii) On July 10, 2013, the Company entered into an agreement with a new franchisee to operate a Proshred shredding business in Seattle, Washington. The franchise fee of US$102,550 associated with this new franchise will be recognized in the third quarter of 2013. The Company expects its new franchise to commence operations in the third quarter of 2013.

iii) On August 1, 2013, the Company acquired the Proshred Charlotte business from an existing franchisee for an aggregate purchase price of $1,300,000. In order to finance the acquisition, Proshred Charlotte Inc. has obtained loans aggregating $1,250,000 from a group comprised of members of the Company's Board of Directors and their affiliates and associates. The Company is in the process of allocating the assets acquired to determine a preliminary purchase price allocation.