

*Interim consolidated financial statements of*

**MTY FOOD GROUP INC.**

*May 31, 2010*

# MTY FOOD GROUP INC.

## Consolidated statement of earnings and comprehensive income

For the six month period ended May 31, 2010

Unaudited

Notice of no auditor review if interim financial statements: MTY's independent auditor has not performed a review of these consolidated financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

	Three months ended May 31, 2010	Six months ended May 31, 2010	Three months ended May 31, 2009	Six months ended May 31, 2009
<b>Revenue</b>				
Franchise locations (Note 15)	15,125,390	27,453,894	9,063,239	16,896,545
Corporate owned locations	2,162,003	4,147,052	2,371,514	4,315,441
	<b>17,287,393</b>	<b>31,600,946</b>	11,434,753	21,211,986
<b>Expenses</b>				
Other operating expenses	8,987,400	15,947,241	4,089,986	7,959,312
Corporate owned locations	1,702,950	3,537,821	2,137,434	4,069,425
Amortization – capital assets	160,639	449,750	212,825	379,789
Amortization – intangible assets	738,574	1,526,048	707,730	1,398,236
	<b>11,589,563</b>	<b>21,460,860</b>	7,147,975	13,806,762
<b>Other income</b>				
Gain (loss) on foreign exchange	(1,221)	3,189	6,789	1,996
Interest income	38,038	71,379	38,718	152,731
Loss on disposal of capital assets	(104,004)	(197,165)	(58,096)	(90,825)
	<b>(67,187)</b>	<b>(122,597)</b>	(12,589)	63,902
<b>Income before income taxes and non-controlling interest</b>	<b>5,630,643</b>	<b>10,017,489</b>	4,274,189	7,469,126
<b>Income taxes (Note 19)</b>				
Current	1,877,688	3,101,357	1,301,349	2,304,012
Future	(86,717)	60,991	50,843	31,934
	<b>1,790,971</b>	<b>3,162,348</b>	1,352,192	2,335,946
<b>Income before non-controlling interest</b>	<b>3,839,672</b>	<b>6,855,141</b>	2,921,997	5,133,180
Non-controlling interest	(30,533)	(42,407)	(20,237)	(31,894)
<b>Net income and comprehensive income</b>	<b>3,809,139</b>	<b>6,812,734</b>	2,901,760	5,101,286

Earnings per share (Note 20)

Basic	0.20	0.36	0.15	0.27
Fully diluted	0.20	0.36	0.15	0.27

See accompanying notes

# MTY FOOD GROUP INC.

## Consolidated statement of retained earnings

for the six month period ended May 31, 2010

Unaudited

	May 31, 2010	May 31, 2009
	\$	\$
Balance, beginning of year	41,338,029	29,076,526
Net income	6,812,734	5,101,286
<b>Balance, end of period</b>	<b>48,150,763</b>	<b>34,177,812</b>

See accompanying notes

# MTY FOOD GROUP INC.

## Consolidated balance sheet

as at May 31, 2010

	May 31, 2010 Unaudited	Nov 30, 2009 Audited
	\$	\$
<b>Assets</b>		
Current assets		
Cash	4,688,318	1,245,844
Temporary investments (Note 4)	19,981,608	14,631,473
Accounts receivable	7,435,000	6,675,037
Inventory	380,161	392,995
Franchise locations under construction held for resale	803,452	1,005,816
Loans receivable (Note 5)	172,477	153,643
Prepaid expenses	148,958	91,210
Deposits	51,251	-
Future income taxes (Note 19)	1,183,935	1,272,003
	34,845,160	25,468,021
Loans receivable (Note 5)	679,961	383,771
Other receivable (Note 3)	2,697,762	2,697,762
Capital assets (Note 6)	3,260,048	3,734,657
Intangible assets (Note 7)	33,566,117	35,092,165
Goodwill	6,834,249	6,834,249
Future income taxes (Note 19)	2,207,414	2,324,834
	84,090,711	76,535,459
<b>Liabilities</b>		
Current liabilities		
Accounts payable and accrued liabilities	9,941,230	9,293,003
Income taxes payable	388,023	44,032
Deferred revenue and deposits (Note 9)	1,567,689	1,593,704
Current portion of long-term debt (Note 10)	1,914,511	1,435,859
	13,811,453	12,366,598
Deferred revenue and deposits (Note 9)	73,189	82,918
Long-term debt (Note 10)	-	545,518
Future income taxes (Note 19)	1,690,296	1,834,793
Non-controlling interest	91,222	93,815
	15,666,160	14,923,642
<b>Commitments and contingent liability (Notes 16, 17 and 18)</b>		
<b>Shareholders' equity</b>		
Capital stock (Note 11)	19,792,468	19,792,468
Contributed surplus	481,320	481,320
Retained earnings	48,150,763	41,338,029
	68,424,551	61,611,817
	84,090,711	76,535,459

See accompanying notes

### Approved by the Board

..... ``Stanley Ma`` ..... Director      ..... ``Claude St-Pierre`` ..... Director

**MTY FOOD GROUP INC.**  
**Consolidated statement of cash flows**  
**for the six month period ended May 31, 2010**  
Unaudited

	Three months ended May 31, 2010	Six months ended May 31, 2010	Three months ended May 31, 2009	Six months ended May 31, 2009
<b>Operating activities</b>				
Net income	3,809,139	6,812,734	2,901,760	5,101,286
Items not affecting cash:				
Amortization – capital assets	160,639	449,750	212,825	379,789
Amortization – intangible assets	738,574	1,526,048	707,730	1,398,236
Deferred revenue	322,984	(35,744)	432,289	514,344
Non-controlling interest	30,533	42,407	20,237	31,894
Loss on disposal of capital assets	104,004	197,165	58,096	90,825
Future income taxes	(86,717)	60,991	50,843	31,934
Changes in non-cash working capital items (Note 21)	(310,871)	23,430	200,018	(1,595,846)
<b>Cash flows provided by operating activities</b>	<b>4,768,285</b>	<b>9,076,781</b>	4,583,798	5,952,462
<b>Investing activities</b>				
Business acquisitions (Note 3)	-	-	(14,588,501)	(14,588,501)
Temporary investments	(7,018,626)	(5,350,135)	12,068,470	10,481,866
Additions to capital assets	(335,810)	(498,069)	(55,264)	(131,376)
Proceeds on disposal of capital assets	20,763	325,763	7,000	37,000
<b>Cash flows used in investing activities</b>	<b>(7,333,673)</b>	<b>(5,522,441)</b>	(2,568,295)	(4,201,011)
<b>Financing activities</b>				
Repayment of long-term debt	(63,691)	(66,866)	(133,333)	(133,333)
Dividends paid to non-controlling shareholders of subsidiaries	(15,000)	(45,000)	-	(30,000)
<b>Cash flows used in financing activities</b>	<b>(78,691)</b>	<b>(111,866)</b>	(133,333)	(163,333)
Net increase (decrease) in cash	(2,644,079)	3,442,474	1,882,170	1,588,118
Cash, beginning of period	7,332,397	1,245,844	525,297	819,349
<b>Cash, end of period</b>	<b>4,688,318</b>	<b>4,688,318</b>	2,407,467	2,407,467

See accompanying notes

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 1. Description of the business

MTY Food Group Inc. (the “Company”) is a franchisor in the quick service food industry. Its activities consist of franchising and operating corporate-owned locations under a multitude of banners.

During the first six months of its 2010 fiscal year, the company has opened 79 stores, bringing the total number of stores to 1,605. Of this number, 19 were corporate stores at the end of period.

### 2. Accounting policies

#### *a) Basis of consolidation*

These interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) on a basis consistent with those followed in the most recent audited financial statements. These interim consolidated financial statements do not include all of the information and notes required by GAAP for annual financial statements and therefore should be read in conjunction with the audited consolidated financial statements and notes included in the Company’s audited financial statements for the year ended November 30, 2009.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries from the date of their acquisition. In addition, the consolidated financial statements include the accounts of a subsidiary in which it owns 67% of the controlling shares and of another subsidiary in which it owns 49% of the controlling shares and exercises effective control. All significant intercompany accounts and transactions have been eliminated upon consolidation.

The consolidated financial statements must include the variable interest entities (“VIEs”). VIEs are entities in which equity investors do not have controlling financial interest or the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support provided by other parties. VIEs are consolidated by its primary beneficiary (i.e., the party that receives the majority of the expected residual returns and/or absorbs the majority of the entity’s losses). Management of the Company conducted a review of the ownership and contractual interest in entities and determined that no VIEs exist as of May 31, 2010.

Pursuant to the franchise agreements, franchisees must pay a fee to the promotional fund. These amounts are collected by the Company in its capacity as agent and must be used for promotional and advertising purposes, since the amounts are set aside to promote the respective banners for the franchisees’ benefit. The fees collected by the Company for the promotional fund are not recorded in the Company’s consolidated statement of earnings, but rather as operations in the accounts payable to the promotional fund.

#### *b) Use of estimates*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses during the period reported. Significant areas requiring the use of management estimates relate to the carrying value of long-lived assets, valuation of allowances for accounts receivable and inventories, liabilities for potential claims and settlements, income taxes, the useful life of assets used when calculating amortization, the determination of fair value of assets and liabilities in business acquisitions and impairment testing on goodwill and trademarks.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 2. Accounting policies (cont.)

#### *b) Use of estimates (cont.)*

Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the consolidated financial statements in the period they are determined to be necessary. Actual results could differ from those estimates.

#### *c) Inventory*

Inventory is valued at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis. Cost is equivalent to acquisition costs, net of consideration received from suppliers.

#### *d) Franchise locations under construction held for resale*

The Company constructs franchise locations for resale. The Company capitalizes all direct costs relating to the construction of these franchise locations. If a franchisee is not immediately identified, the Company operates the franchise location as a corporate-owned location until a franchisee is identified. The franchise locations under construction and held for resale are carried at the lower of cost and estimated net realizable value.

#### *e) Capital assets*

Capital assets are recorded at cost. Amortization is based on their estimated useful life using the following methods and rates or terms:

Equipment	diminishing balance	20%
Computer hardware	diminishing balance	30%
Computer software	diminishing balance	50%
Leasehold improvements	straight-line	term of leases
Rolling stock	diminishing balance	30%

#### *f) Goodwill*

Goodwill represents the excess of the purchase price over the fair values assigned to identifiable net assets acquired. Goodwill, which is not amortized, is tested for impairment annually or more frequently if impairment indicators arise to determine whether the fair value of each reporting unit to which goodwill has been attributed is less than the carrying value of the reporting unit's net assets including goodwill, thus indicating impairment. The fair value of a reporting unit is calculated based on future cash flows. Any impairment is then recorded as a separate charge against income and a reduction of the carrying value of goodwill.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 2. Accounting policies (cont.)

#### *g) Intangible assets*

##### *Franchise rights*

Franchise rights include franchise rights and master franchise rights. The franchise rights and master franchise rights represent the fair value of the future revenue stream related to the acquisition of franchises. The franchise rights and master franchise rights are generally amortized on a straight-line basis over the term of the agreements which range between 10 to 20 years. Master franchise rights with an indefinite life are not amortized. They are tested for impairment annually or more frequently when events or circumstances indicate that the master franchise rights might be impaired.

##### *Trademarks*

Trademarks represent the cost incurred to operate under a trade name and are not amortized as they have an indefinite life. They are tested annually for impairment or more frequently when events or circumstances indicate that the trademarks might be impaired. The impairment test compares the carrying amount of the trademarks with their fair market value.

##### *Leases*

Leases, which represent the value associated to preferential terms or locations, are amortized on a straight-line basis over the term of the leases.

##### *Other*

Included in other intangible assets are a sponsorship fee and a licensing agreement acquired in the 2004 acquisition of Mrs. Vanelli's Restaurants Ltd., which are both fully amortized, and distributions rights obtained from the acquisition of Country Style Food Services Inc., which are being amortized over the remaining life of the contracts (three years).

#### *h) Impairment of long-lived assets*

Long-lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is recognized when their carrying value exceeds the total undiscounted cash flows expected from their use and eventual disposition. The amount of the impairment loss is determined as the excess of the carrying value of the asset over its fair value.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 2. Accounting policies (cont.)

#### *i) Revenue recognition*

Revenue is generally recognized on the sale of products or services when the products are delivered or the services performed, all significant contractual obligations have been satisfied and the collection is reasonably assured.

##### *i. Revenue from franchise locations*

Royalties are based either on a percentage of gross sales as reported by the franchisees or on a fixed monthly fee and are recognized as revenue in the period earned.

Initial franchise fees are recognized when substantially all of the initial services as required by the franchise agreement have been performed. This occurs when the location commences operations.

Revenue from the sale of franchise locations is recognized at the time the franchisee assumes control of the franchise location.

Master license fees are recognized when the Company has performed substantially all material initial obligations under the agreement, which usually occurs when the agreement is signed.

Renewal and transfer fees are recognized when substantially all applicable services required by the Company under the franchise agreement have been performed. This generally occurs when the agreement is signed.

The Company earns rent revenues on certain leases it holds and sign rental revenues; both are recognized in the month they are earned.

The Company receives considerations from certain suppliers. Supplier contributions are recognized as revenues as they are earned.

##### *ii. Revenue from corporate-owned locations*

Revenue from corporate-owned locations is recorded when services are rendered.

#### *j) Foreign currency*

Foreign currency transactions and balances are translated using the temporal method. Under this method, all monetary assets and liabilities are translated at the exchange rates prevailing at the balance sheet date. Non-monetary assets and liabilities are translated at historical exchange rates.

Revenue and expenses are translated at the average exchange rates for the month, except for amortization which is translated on the same basis as the related assets. Translation gains and losses are reflected in net income.

#### *k) Income taxes*

The Company follows the liability method of accounting for income taxes. Under this method, future income taxes are recognized based on the expected future tax consequences of differences between the carrying amount of balance sheet items and their corresponding tax basis, using the enacted and substantively enacted income tax rates for the years in which the differences are expected to reverse. Future income tax assets are recognized to the extent it is more likely than not they will be realized.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 2. Accounting policies (cont.)

#### *l) Financial instruments*

Financial assets and financial liabilities are initially recognized at fair value and their subsequent measurement is dependent on their classification as described below. Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics and the Company's designation of such instruments.

#### *Classification*

Cash	Held for trading
Temporary investments	Held for trading
Accounts receivable	Loans and receivables
Deposits	Loans and receivables
Loans receivable	Loans and receivables
Other receivable	Loans and receivables
Accounts payable and accrued liabilities	Other liabilities
Long-term debt	Other liabilities

#### *Held for trading*

Held-for-trading financial assets are financial assets typically acquired for resale prior to maturity or that are designated as held for trading. They are measured at fair value at the balance sheet date. Fair value fluctuations including interest earned, interest accrued, gains and losses realized on disposal and unrealized gains and losses are included in other income.

#### *Loans and receivables*

Loans and receivables are accounted for at amortized cost using the effective interest method.

#### *Other liabilities*

Other liabilities are recorded at amortized cost using the effective interest method and include all financial liabilities other than derivative instruments.

#### *Effective interest method*

The Company uses the effective interest method to recognize interest income or expense which includes transaction costs or fees, premiums or discounts earned or incurred for financial instruments.

#### *Embedded derivatives*

An embedded derivative is a component of a contract with characteristics similar to a derivative. Management of the Company conducted a review of its contracts and determined that no embedded derivatives exist as at May 31, 2010.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 2. Accounting policies (cont.)

#### *m) Future accounting policies*

##### *i. International Financial Reporting Standards*

In February 2008, Canada's Accounting Standards Board (AcSB) confirmed that Canadian GAAP, as used by publicly accountable enterprises, will be superseded by International Financial Reporting Standards (IFRS) for fiscal years beginning on or after January 1, 2011. For the Company, the conversion to IFRS will be required for interim and annual financial statements for the year ending November 30, 2012. IFRS uses a conceptual framework similar to Canadian GAAP, but there are significant differences on recognition, measurement and disclosures. The Company is currently preparing its IFRS conversion plan. The plan will be aimed in particular at identifying the differences between IFRS and the Company's accounting policies, assessing their impact and, where necessary, analyzing the various policies that the Company could elect to adopt.

##### *ii. Business Combinations*

In January 2009, the CICA issued the following new Handbook sections: Section 1582, Business Combinations, Section 1601, Consolidated Financial Statements and Section 1602, Non-Controlling Interests which replace Section 1581, Business Combinations and Section 1600, Consolidated Financial Statements. These new Sections will be applicable to financial statements relating to fiscal years beginning on or after January 1, 2011. Early adoption is permitted to the extent the three new Sections are adopted simultaneously. Together, the new Sections establish standards for the accounting for a business combination, the preparation of consolidated financial statements and the accounting for a non-controlling interest in subsidiary in consolidated financial statements subsequent to a business combination. The Company is currently evaluating the impact of the adoption of these new Sections on its consolidated financial statements. The Company does not expect that the adoption of these new Sections will have a material impact on its consolidated financial statements.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

### 3. Business acquisitions

#### I) 2009 acquisition

On May 1, 2009, the Company's wholly-owned subsidiary, MTY Tiki Ming Enterprises Inc., acquired all of the issued and outstanding shares of Country Style Food Services Holdings Inc., the second largest coffee and baked goods franchisor in Ontario's quick service restaurant sector, for a total consideration of \$13,810,564. The Company has paid \$7,936,791 in cash and \$6,750,000 as repayment of long-term debt on closing and retained the amounts of \$997,868 and \$794,576 as holdbacks and withholding taxes respectively. An amount of \$2,697,762 of post-closing adjustments is to be reimbursed by the sellers to the Company in accordance with the provisions of the purchase agreement. The post-closing adjustments are under litigation.

The preliminary allocation of the purchase price of the acquisition is as follows:

	\$
<u>Consideration paid</u>	
Share purchase	9,729,235
Repayment of long-term debt	6,750,000
Post closing adjustments	(2,697,762)
Acquisition costs	29,091
<hr/>	
Total purchase price	13,810,564
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<u>Net assets acquired:</u>	
<b>Current Assets</b>	
Cash	127,381
Accounts receivable	2,039,936
Inventory	368,768
Franchise locations under construction held for resale	627,542
Prepaid expenses	196,000
Future income taxes	1,290,000
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	4,649,627
Future income taxes	3,303,000
Property, plant and equipment	1,584,724
Franchise rights	1,016,000
Trademarks	4,096,000
Distribution agreements	272,000
Goodwill (not tax deductible)	2,860,000
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	17,781,351
<b>Current Liabilities</b>	
Accounts payable and accrued liabilities	3,970,787
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Total purchase price	13,810,564
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The final purchase price for this acquisition has not been finalized.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 4. Temporary investments

Temporary investments are comprised of short-term notes valued at fair value. They have maturity dates between June 2010 and May 2011 and have rates of return between 0.53% and 1.41% (0.35% to 1.01% in November 2009).

### 5. Loans receivable

The loans receivable result from the sales of franchises and consist of the following:

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Loans receivable bearing interest between nil and 9% per annum, receivable in monthly instalments of \$18,060.61 in aggregate, including principal and interest, ending in April 2017	<b>852,438</b>	537,414
	<b>852,438</b>	537,414
Current portion	<b>(172,477)</b>	(153,643)
	<b>679,961</b>	383,771

The capital repayments in subsequent years will be:

	\$
12 months ending May 2011	172,477
12 months ending May 2012	261,056
12 months ending May 2013	125,589
12 months ending May 2014	190,244
12 months ending May 2015	52,176
Thereafter	50,896
	<b>852,438</b>

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

### 6. Capital assets

	May 31, 2010		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Corporate-owned locations	3,063,911	1,395,668	1,668,243
Equipment	414,420	127,278	287,142
Computer hardware	284,844	178,780	106,064
Computer software	111,012	84,446	26,566
Leasehold improvements	1,601,338	445,403	1,155,935
Rolling stock	24,119	8,021	16,098
	<b>5,499,644</b>	<b>2,239,596</b>	<b>3,260,048</b>

	November 30, 2009		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Corporate-owned locations	3,750,035	1,565,653	2,184,382
Equipment	340,962	103,635	237,327
Computer hardware	252,975	162,928	90,047
Computer software	109,164	75,899	33,265
Leasehold improvements	1,469,000	298,187	1,170,813
Rolling stock	24,119	5,296	18,823
	<b>5,946,255</b>	<b>2,211,598</b>	<b>3,734,657</b>

Corporate-owned locations are comprised of equipment, leasehold improvements and computer equipment having costs of \$1,193,034 (\$1,426,763 in November 2009), \$1,808,878 (\$2,226,297 in November 2009) and \$61,999 (\$96,975 in November 2009), respectively and net book values of \$600,351 (\$728,285 in November 2009), \$1,046,401 (\$1,414,946 in November 2009) and \$21,491 (\$41,151 in November 2009) respectively.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

### 7. Intangible assets

	May 31, 2010		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Franchise and master franchise rights <sup>(1)</sup>	30,514,834	9,234,511	21,280,323
Trademarks	11,518,960	-	11,518,960
Leases	1,000,000	406,938	593,062
Other	504,725	330,953	173,772
	<b>43,538,519</b>	<b>9,972,402</b>	<b>33,566,117</b>

	November 30, 2009		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Franchise and master franchise rights <sup>(1)</sup>	30,514,834	7,827,977	22,686,857
Trademarks	11,518,960	-	11,518,960
Leases	1,000,000	332,760	667,240
Other	504,725	285,617	219,108
	<b>43,538,519</b>	<b>8,446,354</b>	<b>35,092,165</b>

<sup>(1)</sup> Franchise and master franchise rights included the amount of \$1,500,000 (\$1,500,000 in November 2009) of unamortizable master franchise right.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 8. Bank indebtedness

As at May 31, 2010, the Company has an authorized operating line of credit of \$5,000,000. Bank indebtedness is secured by a moveable hypothec on all the assets of the Company. The interest rate charged is the bank's annual prime rate (2.25% on May 31, 2010) plus 1.00%. Under the terms of the line of credit, the Company must satisfy a funded debt to EBITDA ratio of 1 to 1, a current ratio of 1.45 to 1, and a debt service coverage ratio of 1.8 to 1. The company is in compliance with all these ratios. The operating line of credit is payable on demand and is renewable annually.

### 9. Deferred revenue and deposits

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Franchise fee deposits	<b>1,165,903</b>	1,241,500
Distribution rights	<b>474,975</b>	435,122
	<b>1,640,878</b>	1,676,622
Current portion	<b>(1,567,689)</b>	(1,593,704)
	<b>73,189</b>	82,918

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### 10. Long-term debt

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Non-interest bearing holdbacks on acquisition, repayable in semi-annual instalments of \$100,000 ending 2010	<b>185,055</b>	189,415
Non-interest bearing holdbacks and withholding taxes on the acquisition of Country Style Food Services Holdings Inc., repayable at various dates, due no later than 2011.	<b>1,525,456</b>	1,587,962
Non-interest bearing loans from non-controlling shareholders of subsidiary with no terms of repayment	<b>204,000</b>	204,000
	<b>1,914,511</b>	1,981,377
Current portion	<b>(1,914,511)</b>	(1,435,859)
	-	545,518

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# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 11. Capital stock

Authorized, unlimited number of common shares without nominal or par value

	<u>May 31, 2010</u>		<u>November 30, 2009</u>	
	<u>Number</u>	<u>Amount</u>	<u>Number</u>	<u>Amount</u>
		\$		\$
Balance, beginning and end of period	19,120,567	19,792,468	19,120,567	19,792,468

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### 12. Stock options

Under various plans, the Company may grant stock options on the common shares at the discretion of the Board of Directors, to senior executives, directors and certain key employees. Of the 3,000,000 common shares initially reserved for issuance, 699,500 were available for issuance under the share option plan as at May 31, 2010. There are no options outstanding as at May 31, 2010.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 13. Financial instruments

In the normal course of business, the Company uses various financial instruments which by their nature involve risk, including market risk and the credit risk of non performance by counterparties. These financial instruments are subject to normal credit standards, financial controls, risk management as well as monitoring procedures.

#### *Fair value of recognized financial instruments*

Following is a table which sets out the fair values of recognized financial instruments using the valuation methods and assumptions described below:

	<u>May 31, 2010</u>		<u>November 30, 2009</u>	
	<u>Carrying value</u>	<u>Fair value</u>	<u>Carrying value</u>	<u>Fair value</u>
	\$	\$	\$	\$
Financial assets				
Cash	4,688,318	4,688,318	1,245,844	1,245,844
Temporary investments	19,981,608	19,981,608	14,631,473	14,631,473
Accounts receivable	7,435,000	7,435,000	6,675,037	6,675,037
Loans receivable	852,438	852,438	537,414	537,414
Deposits	51,251	51,251	-	-
Financial liabilities				
Accounts payable and accrued liabilities	9,941,230	9,941,230	9,293,003	9,293,003
Long-term debt	1,914,511	1,912,577	1,981,377	1,977,559

#### *Determination of fair value*

The following methods and assumptions were used to estimate the fair values of each class of financial instruments:

**Cash, accounts receivable, deposits, accounts payable and accrued liabilities** - The carrying amounts approximate fair values due to the short maturity of these financial instruments.

**Temporary investments** - The carrying amounts are reflected at market values, which are determined by quoted prices in active markets for identical securities (Level 1).

**Loans receivable** - The loans receivable bear interest at market rates and therefore it is management's opinion that the carrying value approximates the fair value.

**Long-term debt** - The fair value of long-term debt is determined using the present value of future cash flows under current financing agreements based on the Company's current rate of return on its treasury bank accounts.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

### 13. Financial instruments (cont.)

#### *Risk management policies*

The Company, through its financial assets and liabilities, is exposed to various risks. The following analysis provides a measurement of risks as at the balance sheet date of May 31, 2010.

#### **Credit risk**

The Company's credit risk is primarily attributable to its trade receivables. The amounts disclosed in the balance sheet are net of allowances for bad debts, estimated by the Company's management based on prior experience and their assessment of the current economic environment. The Company believes that the credit risk of accounts receivable is limited for the following reasons:

- The Company's broad client base is spread mostly across Canada.
- The Company accounts for a specific bad debt provision when management considers that the expected recovery is less than the actual account receivable.

The following table sets forth details of the age receivables that are not overdue as well as an analysis of overdue amounts and related allowance for the doubtful accounts:

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Total accounts receivable	8,354,573	7,429,147
Less: Allowance for doubtful accounts	919,573	754,110
<b>Total accounts receivable, net</b>	<b>7,435,000</b>	<b>6,675,037</b>

Of which:

Not past due	4,120,036	5,003,899
Past due for more than one day but for no more than 30 days	1,490,733	147,782
Past due for more than 31 days but for no more than 60 days	197,550	616,139
Past due for more than 61 days	1,626,681	907,217
<b>Total accounts receivable, net</b>	<b>7,435,000</b>	<b>6,675,037</b>
Allowance for doubtful accounts beginning of year	754,110	648,934
Additions	334,960	443,939
Acquisition	-	115,107
Write-off	(169,497)	(453,870)
<b>Allowance for doubtful accounts end of period</b>	<b>919,573</b>	<b>754,110</b>

The credit risk on cash and temporary investments is limited because the Company invests its excess liquidity in high quality financial instruments.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 13. Financial instruments (cont.)

#### Foreign exchange risk

The Company has entered into a contract to minimize its exposure to fluctuations in foreign currencies, mainly on purchases of coffee. As of May 31, 2010, the total value of such contracts was approximately \$334,000.

#### Interest rate risk

The Company is exposed to interest rate risk with regards to cash, temporary investments and its operating line of credit.

#### Liquidity risk

The Company actively maintains credit facilities to ensure it has sufficient available funds to meet current and foreseeable financial requirements at a reasonable cost.

The following are the contractual maturities of financial liabilities as at May 31, 2010:

	Carrying Amount	Contractual Cash Flows	0 to 6 Months	6 to 12 Months	12 to 24 Months
	\$	\$	\$	\$	\$
Accounts payable and accrued liabilities	9,941,230	9,941,230	9,941,230	-	-
Long-term debt	1,914,511	1,914,511	1,431,498	483,013	-
	<u>11,855,741</u>	<u>11,855,741</u>	<u>11,372,728</u>	<u>483,013</u>	<u>-</u>

The following are the contractual maturities of financial liabilities as at November 30, 2009:

	Carrying Amount	Contractual Cash Flows	0 to 6 Months	6 to 12 Months	12 to 24 Months
	\$	\$	\$	\$	\$
Accounts payable and accrued liabilities	9,293,003	9,293,003	9,293,003	-	-
Long-term debt	1,981,377	1,981,377	1,142,444	293,415	545,518
	<u>11,274,380</u>	<u>11,274,380</u>	<u>10,435,447</u>	<u>293,415</u>	<u>545,518</u>

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 14. Capital Disclosures

The Company's objectives when managing capital are:

- 1- To safeguard the Company's ability to obtain financing should the need arise;
- 2- To provide an adequate return to its shareholders;
- 3- To maintain financial flexibility in order to have access to capital in the event of future acquisitions.

The company defines its capital as follows:

- 1- Shareholders' equity;
- 2- Long-term debt including current portion;
- 3- Deferred revenue including the current portion;
- 4- Cash and temporary investments.

The Company's financial strategy is designed and formulated to maintain a flexible capital structure consistent with the objectives stated above and to respond to changes in economic conditions and the risk characteristics of the underlying assets. The Company may invest in longer or shorter-term investments depending on eventual liquidity requirements.

The Company monitors capital on the basis of the debt-to-equity ratio. The debt-to-equity ratios at May 31, 2010 and November 30, 2009 were as follows:

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Debt	15,574,938	14,829,827
Equity	68,424,551	61,611,817
Debt-to-equity ratio	0.23	0.24

The decrease is due to the positive cash flows generated by the company's operations. The Company intends to continue to reduce its total debt with the positive cash flows generated from its operations. Maintaining a low debt-to-equity ratio is a priority in order to permit the Company to secure financing at a reasonable cost for future acquisitions.

### 15. Franchise fees

Included in revenue from franchise locations are initial franchise fees in the amount of \$1,369,848. (\$568,340 in 2009).

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

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### 16. Commitments

The Company has entered into various long-term leases and has sub-leased substantially all of the premises based on the same terms and conditions as the original lease to unrelated franchisees. The minimum rentals, exclusive of occupancy and escalation charges, and additional rent paid on a percentage of sales basis, payable under the leases are as follows:

	<u>Lease commitments</u>	<u>Sub leases</u>	<u>Net commitments</u>
	\$	\$	\$
12 months ending May 2011	33,352,398	31,473,599	1,878,799
12 months ending May 2012	31,797,472	29,771,147	2,026,325
12 months ending May 2013	29,168,215	27,224,726	1,943,489
12 months ending May 2014	26,774,217	24,970,306	1,803,911
12 months ending May 2015	23,740,543	22,016,398	1,724,145
Thereafter	68,354,717	62,526,617	5,828,100
	<u>213,187,562</u>	<u>197,982,793</u>	<u>15,204,769</u>

The Company has entered into supplier agreements for purchases of coffee beans, wheat, sugar and shortening for delivery between June and December 2010. The total commitment amounts to \$1,212,913. Based on market rates at May 31, 2010, a loss of \$9,809 would result from immediate liquidation of all contracts.

### 17. Guarantee

The Company has provided a guarantee in the form of a letter of credit for an amount of \$45,000.

### 18. Contingent liability

The Company is involved in legal claims associated with its current business activities, the outcome of which is not determinable. Management believes that these legal claims will have no significant impact on the financial statements of the Company.

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

### 19. Income taxes

Variations of income tax expense from the basic Canadian Federal and Provincial combined tax rates applicable to income from operations before income taxes are as follows:

	<u>May 31, 2010</u>		<u>May 31, 2009</u>	
	\$	%	\$	%
Statutory income tax rate	3,055,334	30.5	2,312,341	31.0
Add effect of:				
Loss on disposition of capital assets	60,135	0.6	28,374	0.4
Permanent impact of tax assessment	57,935	0.6	-	-
Non-deductible interest	3,852	0.0	-	-
Other – net	(14,908)	(0.1)	(4,769)	(0.1)
<b>Provision for income taxes</b>	<b>3,162,348</b>	<b>31.6</b>	<b>2,335,946</b>	<b>31.3</b>

As at May 31, 2010 there were approximately \$6,706,035 of net allowable capital losses which may be applied against capital gains for future years and be carried forward indefinitely. The future income tax benefit of these capital losses has not been recognized. The Company also has non-capital carry-forwards of \$11,226,918 which may be used to reduce future years' taxable income. The future income tax benefit of the non capital losses has been recognized.

Significant components of future income tax assets and liabilities are as follows:

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Future income tax assets		
Non-capital loss carry-forward	<b>3,391,349</b>	3,596,837
Future income tax liabilities		
Capital assets	<b>36,548</b>	65,092
Intangible assets	<b>1,653,748</b>	1,769,701
	<b>1,690,296</b>	1,834,793

### 20. Earnings per share

The following table provides a reconciliation between the number of basic and fully diluted shares outstanding:

	<u>Three months</u>	<u>Six months</u>	<u>Three months</u>	<u>Six months</u>
	<u>ended</u>	<u>ended</u>	<u>ended</u>	<u>ended</u>
	<u>May 31, 2010</u>	<u>May 31, 2010</u>	<u>May 31, 2009</u>	<u>May 31, 2009</u>
Weighted daily average number of common shares	<b>19,120,567</b>	<b>19,120,567</b>	19,120,567	19,120,567
Diluted effect of stock options	-	-	-	-
Weighted average number of diluted common shares	<b>19,120,567</b>	<b>19,120,567</b>	19,120,567	19,120,567

# MTY FOOD GROUP INC.

## Notes to the consolidated financial statements

As at May 31, 2010

Unaudited

### 21. Statement of cash flows

Net changes in non-cash working capital balances relating to continuing operations are as follows:

	<b>Three months ended May 31, 2010</b>	<b>Six months ended May 31, 2010</b>	Three months ended May 31, 2009	Six months ended May 31, 2009
	\$	\$	\$	\$
Accounts receivable	(757,674)	(759,963)	340,702	(285,973)
Income taxes receivable	66,169	-	-	-
Inventory	(11,873)	12,834	52,013	229,900
Franchise locations under construction held for resale	88,541	202,364	243,850	191,683
Loans receivable	(353,357)	(315,024)	109,390	130,954
Prepaid expenses	(22,626)	(57,748)	87,691	(55,332)
Deposits	5,449	(51,251)	-	-
Accounts payable and accrued liabilities	286,477	648,227	(900,740)	(1,648,459)
Income taxes payable	388,023	343,991	267,112	(158,619)
	<b>(310,871)</b>	<b>23,430</b>	200,018	(1,595,846)
Supplemental disclosure of cash flows				
Income taxes paid	1,558,562	2,848,400	1,113,960	2,469,960
Income tax refund received	91,034	91,034	-	-