

Consolidated financial statements of

MTY FOOD GROUP INC.

August 31, 2010

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MTY FOOD GROUP INC.

Consolidated statement of earnings and comprehensive income

For the nine month period ended August 31, 2010

Unaudited

NOTICE: The consolidated financial statements of MTY Food Group Inc. for the three-month and nine-month periods ended August 31, 2010 and 2009 have not been reviewed by an external auditor.

	Three months ended August 31, 2010	Three months ended August 31, 2009	Nine months ended August 31, 2010	Nine months ended August 31, 2009
	\$	\$	\$	\$
Revenue				
Franchise locations (Note 15)	13,956,568	11,978,799	41,410,462	28,875,344
Corporate owned locations	1,985,207	2,859,579	6,132,259	7,175,020
	15,941,775	14,838,378	47,542,721	36,050,364
Expenses				
Other operating expenses	7,430,423	6,385,689	23,377,664	14,340,987
Corporate owned locations	1,633,783	2,536,191	5,171,604	6,605,616
Amortization – capital assets	265,652	291,751	715,402	671,540
Amortization – intangible assets	738,574	742,180	2,264,622	2,140,416
	10,068,432	9,955,811	31,529,292	23,758,559
Other income				
(Loss) Gain on foreign exchange	(900)	6,541	2,289	4,523
Interest income	60,335	12,466	131,713	165,197
Gain (Loss) on disposal of capital assets	77,022	3,539	(120,143)	(87,286)
	136,457	22,546	13,859	82,434
Income before income taxes and non-controlling interest	6,009,800	4,905,113	16,027,288	12,374,239
Income taxes (Note 19)				
Current	1,821,100	1,173,875	4,366,545	3,477,887
Future	-	328,892	616,903	360,826
	1,821,100	1,502,767	4,983,448	3,838,713
Income before non-controlling interest	4,188,700	3,402,346	11,043,840	8,535,526
Non-controlling interest	(37,886)	(17,842)	(80,293)	(49,736)
Net income and comprehensive income	4,150,814	3,384,504	10,963,547	8,485,790

Earnings per share (Note 20)

Basic	0.22	0.18	0.57	0.44
Fully diluted	0.22	0.18	0.57	0.44

See accompanying notes

MTY FOOD GROUP INC.

Consolidated statement of retained earnings

for the nine month period ended August 31, 2010

Unaudited

	August 31, 2010	August 31, 2009
	\$	\$
Balance, beginning of year	41,338,029	29,076,526
Net income	10,963,547	8,485,790
Balance, end of period	52,301,576	37,562,316

See accompanying notes

MTY FOOD GROUP INC.

Consolidated balance sheet

as at August 31, 2010

	August 31, 2010	Nov 30, 2009
	Unaudited	Audited
	\$	\$
Assets		
Current assets		
Cash	13,948,144	1,245,844
Temporary investments (Note 4)	17,801,501	14,631,473
Accounts receivable	6,682,894	6,675,037
Inventory	264,361	392,995
Franchise locations under construction held for resale	908,352	1,005,816
Loans receivable (Note 5)	264,753	153,643
Prepaid expenses	107,242	91,210
Deposits	50,088	-
Future income taxes (Note 19)	1,183,935	1,272,003
	41,211,270	25,468,021
Loans receivable (Note 5)	639,699	383,771
Other receivable (Note 3)	2,697,762	2,697,762
Capital assets (Note 6)	3,018,180	3,734,657
Intangible assets (Note 7)	32,827,543	35,092,165
Goodwill	6,834,249	6,834,249
Future income taxes (Note 19)	1,605,228	2,324,834
	88,833,931	76,535,459
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	10,744,680	9,293,003
Income taxes payable	421,545	44,032
Deferred revenue (Note 9)	1,664,075	1,593,704
Current portion of long-term debt (Note 10)	1,633,189	1,435,859
	14,463,489	12,366,598
Deferred revenue and deposits (Note 9)	36,893	82,918
Long-term debt (Note 10)	-	545,518
Future income taxes (Note 19)	1,644,022	1,834,793
Non-controlling interest	114,163	93,815
	16,258,567	14,923,642
Commitments, guarantee and contingent liability (Notes 16, 17 and 18)		
Shareholders' equity		
Capital stock (Note 11)	19,792,468	19,792,468
Contributed surplus	481,320	481,320
Retained earnings	52,301,576	41,338,029
	72,575,364	61,611,817
	88,833,931	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 nine month period ended August 31, 2010
Unaudited

	Three months ended August 31, 2010	Three months ended August 31, 2009	Nine months ended August 31, 2010	Nine months ended August 31, 2009
Operating activities				
Net income	4,150,814	3,384,504	10,963,547	8,485,790
Items not affecting cash:				
Amortization – capital assets	265,652	291,751	715,402	671,540
Amortization – intangible assets	738,574	742,180	2,264,622	2,140,416
Deferred revenue	60,090	495,824	24,346	1,010,168
Investment from non-controlling interest	55	460	55	460
Earnings of non-controlling interest	37,886	17,842	80,293	49,736
Dividends paid to non-controlling shareholders of subsidiaries	(15,000)	(10,000)	(60,000)	(40,000)
Loss (Gain) on disposal of capital assets	(77,022)	(3,539)	120,143	87,286
Future income taxes	555,911	331,471	616,902	363,405
Changes in non-cash working capital items (Note 21)	1,590,843	(104,219)	1,614,274	(1,700,065)
Cash flows provided by operating activities	7,307,803	5,146,274	16,339,584	11,068,736
Investing activities				
Business acquisitions (Note 3)	-	-	-	(14,588,501)
Temporary investments	2,180,107	(5,045,510)	(3,170,028)	5,436,356
Additions to capital assets	(146,461)	(137,438)	(644,530)	(268,814)
Proceeds on disposal of capital assets	199,699	11,500	525,462	48,500
Cash flows used in investing activities	2,233,345	(5,171,448)	(3,289,096)	(9,372,459)
Financing activities				
Repayment of long-term debt	(281,322)	(158,604)	(348,188)	(291,937)
Cash flows used in financing activities	(281,322)	(158,604)	(348,188)	(291,937)
Net increase (decrease) in cash	9,259,826	(183,778)	12,702,300	1,404,340
Cash, beginning of period	4,688,318	2,407,467	1,245,844	819,349
Cash, end of period	13,948,144	2,223,689	13,948,144	2,223,689

See accompanying notes

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

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 nine months of its 2010 fiscal year, the company has opened 132 stores, bringing the total number of stores to 1,614. Of this number, 16 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 two other subsidiaries in which it owns 49% and 45% of the controlling shares respectively 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 their 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 August 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 August 31, 2010

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 consists of 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 August 31, 2010

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 August 31, 2010

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 August 31, 2010

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 August 31, 2010.

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

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 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 August 31, 2010

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
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Total purchase price	13,810,564

Net assets acquired:

Current Assets

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
<hr/>	
	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

Current Liabilities

Accounts payable and accrued liabilities	3,970,787
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Total purchase price	13,810,564

The final purchase price for this acquisition has not been finalized.

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

4. Temporary investments

Temporary investments are comprised of short-term notes valued at fair value. They have maturity dates between October 2010 and August 2011 and have rates of return between 0.75% 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>August 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Loans receivable bearing interest between nil and 9% per annum, receivable in monthly instalments of \$34,727.61 in aggregate, including principal and interest, ending in April 2017	<u>904,452</u>	537,414
		537,414
Current portion	<u>264,753</u>	(153,643)
	<u>639,699</u>	383,771

The capital repayments in subsequent years will be:

	\$
12 months ending August 2011	264,753
12 months ending August 2012	257,232
12 months ending August 2013	129,979
12 months ending August 2014	134,150
12 months ending August 2015	78,042
Thereafter	<u>40,296</u>
	<u>904,452</u>

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

6. Capital assets

	August 31, 2010		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Corporate-owned locations			
Equipment	1,071,933	549,796	522,137
Leasehold improvements	1,678,210	773,375	904,835
Computer hardware	52,000	36,047	15,953
Equipment	432,559	141,648	290,911
Computer hardware	362,460	195,505	166,955
Computer software	137,929	93,526	44,403
Leasehold improvements	1,617,895	559,497	1,058,398
Rolling stock	24,119	9,531	14,588
	5,377,105	2,358,925	3,018,180

	November 30, 2009		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Corporate-owned locations			
Equipment	1,426,763	698,478	728,285
Leasehold improvements	2,226,297	811,351	1,414,946
Computer hardware	96,975	55,824	41,151
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
	5,946,255	2,211,598	3,734,657

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

7. Intangible assets

	August 31, 2010		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Franchise and master franchise rights ⁽¹⁾	30,514,834	9,913,328	20,601,506
Trademarks	11,518,960	-	11,518,960
Leases	1,000,000	444,027	555,973
Other	504,725	353,621	151,104
	43,538,519	10,710,976	32,827,543

	November 30, 2009		
	Cost	Accumulated amortization	Net book value
	\$	\$	\$
Franchise and master franchise rights ⁽¹⁾	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
	43,538,519	8,446,354	35,092,165

⁽¹⁾ Franchise and master franchise rights include \$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 August 31, 2010

8. Bank indebtedness

As at August 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 (2.75% on August 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>August 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Franchise fee deposits	971,250	1,241,500
Distribution rights	729,718	435,122
	<u>1,700,968</u>	<u>1,676,622</u>
Current portion	<u>1,664,075</u>	<u>(1,593,704)</u>
	<u>36,893</u>	<u>82,918</u>

10. Long-term debt

	<u>August 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Non-interest bearing holdbacks on acquisition, repayable in semi-annual instalments of \$100,000 ending 2010	182,750	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	1,277,039	1,587,962
Non-interest bearing loans from non-controlling shareholders of subsidiary with no terms of repayment	173,400	204,000
	<u>1,633,189</u>	<u>1,981,377</u>
Current portion	<u>(1,633,189)</u>	<u>(1,435,859)</u>
	<u>-</u>	<u>545,518</u>

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

11. Capital stock

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

	<u>Aug 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

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 August 31, 2010. There are no options outstanding as at August 31, 2010.

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

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>August 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	13,948,144	13,948,144	1,245,844	1,245,844
Temporary investments	17,801,501	17,801,501	14,631,473	14,631,473
Accounts receivable	6,682,894	6,682,894	6,675,037	6,675,037
Loans receivable	904,452	904,452	537,414	537,414
Deposits	50,088	50,088	-	-
Financial liabilities				
Accounts payable and accrued liabilities	10,744,680	10,744,680	9,293,003	9,293,003
Long-term debt	1,633,189	1,632,197	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 August 31, 2010

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 August 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>August 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Total accounts receivable	7,425,498	7,429,147
Less: Allowance for doubtful accounts	742,604	754,110
Total accounts receivable, net	6,682,894	6,675,037

Of which:

Not past due	3,979,667	5,003,899
Past due for more than one day but for no more than 30 days	610,227	147,782
Past due for more than 31 days but for no more than 60 days	586,490	616,139
Past due for more than 61 days	1,506,510	907,217
Total accounts receivable, net	6,682,894	6,675,037
Allowance for doubtful accounts beginning of year	754,110	648,934
Additions	177,128	443,939
Acquisition	-	115,107
Write-off	(188,634)	(453,870)
Allowance for doubtful accounts end of period	742,604	754,110

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 August 31, 2010

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 August 31, 2010, the total value of such contracts was approximately \$1,253,000.

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 August 31, 2010:

	Carrying Amount	Contractual Cash Flows	0 to 6 Months	6 to 12 Months	12 to 24 Months
	\$	\$	\$	\$	\$
Accounts payable and accrued liabilities	10,744,680	10,744,680	10,744,680	-	-
Long-term debt	1,633,189	1,633,189	1,398,594	234,595	-
	<u>12,377,869</u>	<u>12,377,869</u>	<u>12,143,274</u>	<u>234,595</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 August 31, 2010

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 August 31, 2010 and November 30, 2009 were as follows:

	<u>August 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Debt	16,144,404	14,829,827
Equity	72,575,364	61,611,817
Debt-to-equity ratio	0.22	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 \$2,174,448 (\$907,906 in 2009).

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

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 August 2011	33,685,237	31,935,610	1,749,627
12 months ending August 2012	32,051,094	30,007,792	2,043,302
12 months ending August 2013	29,320,669	27,404,999	1,915,670
12 months ending August 2014	26,995,436	25,191,532	1,803,904
12 months ending August 2015	23,825,400	22,141,103	1,684,297
Thereafter	68,297,709	62,365,387	5,932,322
	<u>214,175,545</u>	<u>199,046,423</u>	<u>15,129,122</u>

The Company has entered into supplier agreements for purchases of coffee beans, wheat, sugar and shortening for delivery between September and December 2010. The total commitment amounts to approximately \$636,000. Based on market rates at August 31, 2010, a gain of \$171,465 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 August 31, 2010

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>August 31, 2010</u>		<u>August 31, 2009</u>	
	\$	%	\$	%
Statutory income tax rate	4,888,323	30.4	3,846,912	31.1
Add effect of:				
Loss on disposition of capital assets	36,523	0.3	26,971	0.2
Permanent impact of tax assessment	52,310	0.3	-	-
Non-deductible interest	19,130	0.1	-	-
Other – net	(12,838)	(0.0)	(35,170)	(0.3)
Provision for income taxes	4,983,448	31.1%	3,838,713	31.0

As at August 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 \$14,163,990 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>August 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Future income tax assets		
Non-capital loss carry-forward	2,789,163	3,596,837
Future income tax liabilities		
Capital assets	(51,986)	65,092
Intangible assets	1,696,008	1,769,701
	1,644,022	1,834,793

20. Earnings per share

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

	Three months ended August 31, 2010	Three months ended August 31, 2009	Nine months ended August 31, 2010	Nine months ended August 31, 2009
Weighted daily average number of common shares	19,120,567	19,120,567	19,120,567	19,120,567
Diluted effect of stock options	-	-	-	-
Weighted average number of diluted common shares	19,120,567	19,120,567	19,120,567	19,120,567

MTY FOOD GROUP INC.

Notes to the consolidated financial statements

As at August 31, 2010

21. Statement of cash flows

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

	Three months ended Aug 31, 2010	Three months ended Aug 31, 2009	Nine months ended Aug 31, 2010	Nine months ended Aug 31, 2009
	\$	\$	\$	\$
Accounts receivable	752,106	(541,454)	(7,857)	(827,427)
Income taxes receivable	-	342,848	-	184,229
Inventory	115,800	104,756	128,634	334,656
Franchise locations under construction held for resale	(104,900)	(144,790)	97,464	46,893
Loans receivable	(52,014)	18,020	(367,038)	148,974
Prepaid expenses	41,716	94,620	(16,032)	39,288
Deposits	1,163	-	(50,088)	-
Accounts payable and accrued liabilities	803,450	21,781	1,451,677	(1,626,678)
Income taxes payable	33,522	-	377,514	-
	1,590,843	(104,219)	1,614,274	1,700,065
Supplemental disclosure of cash flows				
Income taxes paid	1,407,201	889,419	4,255,601	3,359,379
Income tax refund received	175,535	271	266,569	271

22. Subsequent Events

On September 16, 2010, the Company completed the acquisition of 100% of the issued shares of Groupe Valentine Inc., 9180-7420 Quebec Inc., as well as seven real estate properties owned by an affiliated corporation.

The purchase price has not been finalized at the date of issuance of these financial statements. The estimated consideration amounts to \$9.0 million. At closing, an amount of \$7.8 million was disbursed and \$1.2 million was held back by the Company.