Consolidated financial statements of

MTY FOOD GROUP INC.

For the three-month period ended February 28, 2011
(unaudited)

MTY FOOD GROUP INC.

Consolidated statements of earnings and comprehensive income

For the three-month period ended February 28, 2011

unaudited

NOTICE: The consolidated financial statements of MTY Food Group Inc. for the three-month periods ended February 28, 2011 and 2010 have not been reviewed by an external auditor.

	February 28, 2011	February 28, 2010
	$	$
Revenues (Notes 17 and 23)	**17,476,037**	14,313,553
Expenses		
Operating expenses (Note 23)	**12,042,605**	8,794,711
Amortization – capital assets	**348,104**	289,111
Amortization – intangible assets	**760,090**	787,474
Interest on long-term debt	**27,843**	-
	13,178,642	9,871,296
Other income		
Gain (loss) on foreign exchange	**(39,535)**	4,409
Interest income	**92,665**	33,341
Gain (loss) on disposal of assets	**708,220**	(93,161)
	761,350	(55,411)
Income before income taxes and non-controlling interest	**5,058,745**	4,386,846
Income taxes (Note 21)		
Current	**132,968**	1,223,669
Future	**1,221,260**	147,708
	1,354,228	1,371,377
Income before non-controlling interest	**3,704,517**	3,015,469
Non-controlling interest	**(236,180)**	(11,874)
Net income and comprehensive income	**3,468,337**	3,003,595
Earnings per share (Note 22)		
Basic	**0.18**	0.16
Fully diluted	**0.18**	0.16

See accompanying notes to consolidated financial statements

MTY FOOD GROUP INC.
Consolidated statements of retained earnings
for the three-month period ended February 28, 2011
unaudited

	February 28, 2011	February 28, 2010
	$	$
Balance, beginning of period	**55,924,397**	41,338,029
Net income	**3,468,337**	3,003,595
Dividends	**(860,426)**	-
Balance, end of period	**58,532,308**	44,341,624

See accompanying notes to consolidated financial statements

MTY FOOD GROUP INC.

Consolidated balance sheets

as at February 28, 2011

	February 28, 2011 unaudited	November 30, 2010 audited
	$	$
Assets		
Current assets		
Cash	**5,716,330**	5,636,912
Temporary investments (Note 4)	**25,450,180**	23,383,261
Accounts receivable	**7,412,272**	7,577,435
Income taxes receivable	**1,266,732**	-
Inventories (Note 5)	**1,070,095**	645,528
Franchise locations under construction held for resale	**377,770**	1,091,488
Loans receivable (Note 6)	**352,632**	336,067
Prepaid expenses	**218,284**	140,549
Deposits	**125,589**	45,292
Future income taxes (Note 21)	**2,403,053**	3,561,864
	44,392,937	42,418,396
Loans receivable (Note 6)	**951,105**	908,619
Other receivable (Note 15)	**2,697,762**	2,697,762
Capital assets (Note 7)	**9,810,576**	7,138,466
Intangible assets (Note 8)	**35,506,024**	36,266,114
Goodwill (Note 9)	**7,424,751**	7,124,751
	100,783,155	96,554,108
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	**11,274,124**	12,529,748
Income taxes payable	**-**	851,138
Deferred revenue (Note 11)	**1,371,368**	1,485,295
Current portion of long-term debt (Note 12)	**1,843,520**	1,873,213
	14,489,012	16,739,394
Deferred revenue (Note 11)	**4,672**	8,708
Long-term debt (Note 12)	**4,557,083**	930,000
Future income taxes (Note 21)	**2,624,124**	2,605,882
Non-controlling interest	**302,168**	71,939
	21,977,059	20,355,923
Commitments, guarantee and contingent liability (Notes 18, 19 and 20)		
Shareholders' equity		
Capital stock (Note 13)	**19,792,468**	19,792,468
Contributed surplus	**481,320**	481,320
Retained earnings	**58,532,308**	55,924,397
	78,806,096	76,198,185
	100,783,155	96,554,108

See accompanying notes to consolidated financial statements

Approved by the Board

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

MTY FOOD GROUP INC.
Consolidated statements of cash flows
for the three month period ended February 28, 2011
unaudited

	February 28, 2011	February 28, 2010
	$	$
Operating activities		
Net income	**3,468,337**	3,003,595
Items not affecting cash:		
Amortization – capital assets	**348,104**	289,111
Amortization – intangible assets	**760,090**	787,474
Deferred revenue	**(117,963)**	(358,728)
Investment from non-controlling interest in a subsidiary company	**49**	-
Non-controlling interest	**236,180**	11,874
Dividends paid to non-controlling shareholders of subsidiaries	**(15,000)**	(30,000)
(Gain) loss on disposal of capital assets	**(708,220)**	93,161
Future income taxes	**1,221,260**	147,708
	5,192,837	3,944,195
Changes in non-cash working capital items (Note 24)	**(2,944,490)**	334,301
Cash flows provided by operating activities	**2,248,347**	4,278,496
Investing activities		
Business acquisition (Note 3)	**(3,497,110)**	-
Temporary investments	**(2,066,919)**	1,668,491
Additions to capital assets	**(186,651)**	(162,259)
Proceeds on disposal of assets	**1,144,786**	305,000
Cash flows (used in) provided by investing activities	**(4,605,894)**	1,811,232
Financing activities		
Dividends	**(860,426)**	-
Issuance of long-term debt (Note 3)	**3,500,000**	-
Repayment of long-term debt	**(202,609)**	(3,175)
Cash flows used in financing activities	**2,436,965**	(3,175)
Net increase in cash	**79,418**	6,086,553
Cash, beginning of period	**5,636,912**	1,245,844
Cash, end of period	**5,716,330**	7,332,397

See accompanying notes to consolidated financial statements

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. The Company also operates a distribution center and a food processing plant, both of which are located in the province of Quebec.

During the first three months of its 2011 fiscal year, the company has opened 28 stores, bringing the total number of stores to 1,741. Of this number, 27 were corporate stores at the end of period.

2. Accounting policies

a) Basis of consolidation

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 five subsidiaries in which it owns 50% or more of the controlling shares and two other subsidiaries in which it owns 49% and 45% of the controlling shares respectively and over which it 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 significant VIEs exist as of February 28, 2011.

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 Generally Accepted Accounting Principles ("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 revenues 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 intangible assets.

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) Inventories

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:

Buildings		
Structure	Straight-line	50 years
Components	Straight-line	20 to 30 years
Equipment	Declining balance	10%-20%
Leasehold improvements	Straight-line	Term of lease
Rolling stock	Declining balance	15%-30%
Computer hardware	Declining balance	20%-30%
Computer software	Declining balance	50%
Signs	Straight-line	Term of lease

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 calculated as the difference between the fair value of the reporting unit and the carrying value, and is then recorded as a separate charge against income and a reduction of the carrying value of goodwill.

2. Accounting policies (cont.)

g) Intangible assets

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 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 at the date of acquisition).

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.

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 usually 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.

Restaurant construction and renovation revenue are accounted for in accordance with the completed contract method. Losses are fully recognized as they become probable.

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 distribution center

Distribution revenues are recognized when goods have been delivered and accepted by customers.

iii. Revenue from food processing

Food processing revenues are recognized when goods have been delivered to end-users or when risks and rewards of ownership have been transferred to distributors.

iv. Revenue from corporate-owned locations

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

2. Accounting policies (cont.)

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. The effect of changes in income tax rates on future income tax assets and liabilities is recognized in earnings in the year that includes the date of enactment or substantive enactment of the changes.

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.

2. Accounting policies (cont.)

l) Financial instruments (cont.)

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 February 28, 2011 and 2010.

Derivative financial instruments

Derivative financial instruments that are not eligible for hedge accounting are recognized on the balance sheet at their fair value, with changes in fair value recognized in net earnings.

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. The Company is currently assessing the impact of the new reporting framework on its consolidated financial statements and is developing an implementation strategy.

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 has elected not to adopt these Sections early.

3. Business acquisitions

I) 2011 acquisition

On December 17, 2010 the Company's wholly-owned subsidiary, MTY Tiki-Ming Enterprises Inc., acquired a 51% interest in a newly formed company established to own a food processing plant. The acquisition was financed by a long-term bank loan of $3,500,000 (Note 12).

	$
Consideration paid	3,497,110

The preliminary purchase price allocation is as follows:

Net assets acquired:	
Current Assets	
Inventories	339,663
Deferred expenses	30,192
	369,855
Land	562,203
Building	986,834
Equipment	1,712,093
Future income tax asset	44,207
Goodwill	300,000
	3,975,192
Current Liabilities	
Accounts payable	178,082
Mandatorily redeemable preferred shares	100,000
	278,082
Mandatorily redeemable preferred shares	200,000
Total purchase price	3,497,110

The final purchase price for the acquisition has not yet been finalized.

3. Business acquisitions (cont.)

II) 2010 acquisition

On September 16, 2010 the Company's wholly-owned subsidiary, MTY Tiki-Ming Enterprises Inc., acquired all of the outstanding shares of Groupe Valentine Inc. as well as seven real estate properties for a consideration of $8,764,126.

Consideration paid

Share purchase	4,989,555
Repayment of long-term debt	402,571
Acquisition of properties	3,372,000
Total purchase price	8,764,126

Of the consideration above, the Company is currently retained $930,000 as holdbacks (Note 12).

The purchase price allocation is as follows:

Net assets acquired:

Current Assets	
Cash	4,336
Accounts receivable	499,247
Inventory	324,962
Franchise locations under construction held for resale	270,631
Current portion of loans receivable	117,695
Prepaid expenses	26,246
	1,243,117
Loans receivable	232,735
Property, plant and equipment	4,322,764
Franchise rights	860,770
Trademark	3,337,895
Goodwill (not tax deductible)	1,446,061
Minority interest	20,657
	11,463,999
Current Liabilities	
Accounts payable	1,193,109
Income taxes payable	87,005
Loans payable	129,683
Unearned revenue	104,860
	1,514,657
Future income taxes	1,185,216
Total purchase price	8,764,126

The final purchase price for the acquisition has not yet been finalized.

4. Temporary investments

Temporary investments are comprised of short-term notes recorded at fair value. They have maturity dates between March 2011 and December 2011 and have rates of return between 0.80% and 1.41% (0.82% to 1.45% in November 2010).

5. Inventories

Inventories expensed during the period amount to $3,977,299 (2010 - $2,649,891).

6. Loans receivable

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

	February 28, 2011	November 30, 2010
	$	$
Loans receivable, carrying no interest and without terms of repayment	**93,287**	-
Loans receivable bearing interest between nil and 9% per annum, receivable in monthly instalments of $44,108 in aggregate, including principal and interest, ending in April 2017	**1,210,450**	1,244,686
	1,303,737	1,244,686
Current portion	**(352,632)**	(336,067)
	951,105	908,619

The capital repayments in subsequent years will be:

	$
12 months ending February 2012	**352,632**
12 months ending February 2013	**354,644**
12 months ending February 2014	**212,016**
12 months ending February 2015	**181,723**
12 months ending February 2016	**80,762**
Thereafter	**121,960**
	1,303,737

7. Capital assets

	February 28, 2011		
	Cost	Accumulated amortization	Net book value
	$	$	$
Corporate-owned locations			
Equipment	1,379,386	444,296	935,090
Leasehold improvements	1,284,027	627,458	656,569
Computer hardware	42,000	31,604	10,396
Land	1,847,484	-	1,847,484
Buildings	3,064,799	44,025	3,020,774
Equipment	2,339,903	217,602	2,122,301
Computer hardware	427,971	230,138	197,833
Computer software	172,941	112,162	60,779
Leasehold improvements	1,671,788	736,756	935,032
Rolling stock	39,558	15,240	24,318
	12,269,857	2,459,281	9,810,576

	November 30, 2010		
	Cost	Accumulated amortization	Net book value
	$	$	$
Corporate-owned locations			
Equipment	1,659,267	497,509	1,161,758
Leasehold improvements	1,624,452	643,851	980,601
Computer hardware	42,000	30,764	11,236
Land	1,285,281	-	1,285,281
Buildings	2,064,144	18,604	2,045,540
Equipment	557,784	161,687	396,097
Computer hardware	409,944	214,709	195,235
Computer software	163,148	105,249	57,899
Leasehold improvements	1,624,204	646,373	977,831
Rolling stock	39,558	12,570	26,988
	9,469,782	2,331,316	7,138,466

8. Intangible assets

	February 28, 2011		
	Cost	Accumulated amortization	Net book value
	$	**$**	**$**
Franchise and master franchise rights[1]	31,375,604	11,313,998	20,061,606
Trademarks	14,856,855	-	14,856,855
Leases	1,000,000	518,205	481,795
Other	504,725	398,957	105,768
	47,737,184	12,231,160	35,506,024

	November 30, 2010		
	Cost	Accumulated amortization	Net book value
	$	**$**	**$**
Franchise and master franchise rights[1]	31,375,604	10,613,665	20,761,939
Trademarks	14,856,855	-	14,856,855
Leases	1,000,000	481,116	518,884
Other	504,725	376,289	128,436
	47,737,184	11,471,070	36,266,114

[1] Franchise and master franchise rights include an amount of $1,500,000 ($1,500,000 in November 2010) of unamortizable master franchise right.

9. Goodwill

The changes in the carrying amount of goodwill for the quarter ended February 28, 2011 are as follows:

	February 28, 2011	February 28, 2010
	$	$
Balance, beginning of the year	**7,124,751**	6,834,249
Goodwill acquired during the year (Note 3)	**300,000**	nil
Balance, end of period	**7,424,751**	6,834,249

10. Bank indebtedness

As at February 28, 2011, 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 (3.00% on February 28, 2011) 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.

11. Deferred revenue and deposits

	February 28, 2011	November 30, 2010
	$	$
Franchise fee deposits	**843,928**	903,876
Distribution rights	**532,112**	590,127
	1,376,040	1,494,003
Current portion	**(1,371,368)**	(1,485,295)
	4,672	8,708

12. Long-term debt

	February 28, 2011	November 30, 2010
	$	$
Non-interest bearing holdbacks on acquisition, repayable upon resolution of remaining disputes and litigation related to events having accrued prior to acquisition	**178,640**	179,070
Non-interest bearing holdbacks on acquisition, repayable between March 2012 and September 2013	**930,000**	961,518
Bank loans backed by the assets of two subsidiaries	**-**	125,916
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	**1,208,563**	1,253,309
Bank loan bearing interest at the bank's prime plus 0.50%, secured by the capital assets of a subsidiary, repayable in fixed monthly capital repayments at $24,305.56 plus interest. The first capital repayment is due in December 2011[i)]	**3,500,000**	-
Mandatorily redeemable preferred shares, non-cumulative, redeemable in three yearly installments beginning December 2011,with redemption value based on the performance of a subsidiary	**300,000**	-
Non-interest bearing loans from non-controlling shareholders of subsidiaries with no terms of repayment	**283,400**	283,400
	6,400,603	2,803,213
Current portion	**(1,843,520)**	(1,873,213)
	4,557,083	930,000

i) This loan is subject to restrictive covenants beginning in our 2012 fiscal year. The requirements are to maintain certain working capital, interest coverage and debt to equity ratios.

13. Capital stock

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

	February 28, 2011		November 30, 2010	
	Number	Amount	Number	Amount
		$		$
Balance, beginning and end of period	**19,120,567**	**19,792,468**	19,120,567	19,792,468

14. 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 February 28, 2011. There are no options outstanding as at February 28, 2011.

15. 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:

	February 28, 2011		November 30, 2010	
	Carrying value	**Fair value**	Carrying value	Fair value
	$	**$**	$	$
Financial assets				
Cash	**5,716,330**	**5,716,330**	5,636,912	5,636,912
Temporary investments	**25,450,180**	**25,450,180**	23,383,261	23,383,261
Accounts receivable	**7,412,272**	**7,412,272**	7,577,435	7,577,435
Loans receivable	**1,303,737**	**1,303,737**	1,244,686	1,244,686
Other receivable	**2,697,762**	**N/A**	2,697,762	N/A
Deposits	**125,589**	**125,589**	45,292	45,292
Financial liabilities				
Accounts payable and accrued liabilities	**11,274,124**	**11,274,124**	12,529,748	12,529,748
Long-term debt	**6,400,603**	**6,383,902**	2,803,213	2,786,336

Determination of fair value

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

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

Cash and 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.

Other receivable- The other receivable is the result of post-closing adjustments to be reimbursed by the sellers of Country Style Food Services Holdings Inc. in accordance with the provisions of the purchase agreement. It is currently under litigation. As a result, the timing of the cash flows is undetermined. The other receivable bears no interest.

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.

15. 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 February 2011.

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 the related allowance for doubtful accounts:

	February 28, 2011	November 30, 2010
	$	$
Total accounts receivable	**8,297,633**	8,360,696
Less: Allowance for doubtful accounts	**885,361**	783,261
Total accounts receivable, net	**7,412,272**	7,577,435
Of which:		
Not past due	**5,195,500**	5,665,888
Past due for more than one day but for no more than 30 days	**260,923**	255,948
Past due for more than 31 days but for no more than 60 days	**359,657**	217,314
Past due for more than 61 days	**1,596,192**	1,438,285
Total accounts receivable, net	**7,412,272**	7,577,435
Allowance for doubtful accounts beginning of year	**783,261**	754,110
Additions	**156,274**	384,531
Write-off	**(54,174)**	(355,380)
Allowance for doubtful accounts end of period	**885,361**	783,261

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

The credit risk on the loans receivable is similar to that of accounts receivable. There is currently no allowance for doubtful accounts applicable to the loans receivable.

15. 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 February 28, 2011, the total value of such contracts was approximately $1,570,000. Immediate liquidation of the contracts at February 28, 2011 would have resulted in a loss of $21,000.

Other than the above-mentioned contracts, the Company has minimal exposure to the US$ and is subject to fluctuations as a result of exchange rate variations to the extent that transactions are made in the currency. The Company considers this risk to be relatively limited.

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 February 28, 2011:

	Carrying Amount	Contractual Cash Flows	0 to 6 Months	6 to 12 Months	12 to 24 Months
	$	$	$	$	$
Accounts payable and accrued liabilities	11,274,124	11,274,124	11,274,124	-	-
Long-term debt	6,400,603	6,400,603	1,670,603	172,917	949,667
	17,674,727	17,674,727	12,944,727	172,917	949,667

The following are the contractual maturities of financial liabilities as at November 30, 2010:

	Carrying Amount	Contractual Cash Flows	0 to 6 Months	6 to 12 Months	12 to 24 Months
	$	$	$	$	$
Accounts payable and accrued liabilities	12,529,748	12,529,748	12,529,748	-	-
Long-term debt	2,803,213	2,803,213	1,873,213	-	558,000
	15,332,961	15,332,961	14,402,961	-	558,000

16. 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 the 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 February 28, 2011 and November 30, 2010 were as follows:

	February 28, 2011	November 30, 2010
	$	$
Debt	**21,674,891**	20,283,984
Equity	**78,806,096**	76,198,185
Debt-to-equity ratio	**0.28**	0.27

During the first quarter of 2011, the addition of $3,800,000 of debt related to the acquisition discussed in Note 3 caused the ratio to go up slightly. The Company intends 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.

17. Franchise fees

Included in revenue from franchise locations are initial franchise fees in the amount of $448,209 ($545,730 in 2010).

18. 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:

	Lease commitments	Sub leases	Net commitments
	$	$	$
12 months ending February 2012	35,504,271	33,691,285	1,812,986
12 months ending February 2013	33,115,375	31,202,501	1,912,874
12 months ending February 2014	30,527,188	28,817,858	1,709,330
12 months ending February 2015	27,742,769	26,179,862	1,562,907
12 months ending February 2016	24,021,685	22,615,754	1,405,931
Thereafter	67,528,684	62,235,065	5,293,619
	218,439,972	204,742,325	13,697,647

The Company has entered into supplier agreements for purchases of coffee beans, wheat, sugar and shortening for delivery in March 2011. The total commitment amounts to approximately $596,000. Based on market rates at February 28, 2011, a gain of $77,000 would result from immediate liquidation of all contracts.

19. Guarantee

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

20. Contingent liabilities

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 consolidated financial statements of the Company.

21. 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:

	February 28, 2011		February 28, 2010	
	$	**%**	$	%
Statutory income tax rate	**1,456,918**	**28.8**	1,355,875	30.9
Add effect of:				
Impact of disposition of capital property	**(102,102)**	**(2.0)**	3,987	0.1
Non-deductible meals	**2,968**	**0.1**	-	-
Non-deductible car rental expenses	**1,522**	**0.0**	-	-
Other – net	**(5,078)**	**(0.1)**	11,515	0.3
Provision for income taxes	**1,354,228**	**26.8**	1,371,377	31.3

As at February 28, 2011 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 losses carry-forwards of $11,268,131 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:

	February 28, 2011	November 30, 2010
	$	$
Future income tax assets		
Non-capital loss carry-forward	**2,403,053**	3,561,864
Future income tax liabilities		
Capital assets	**35,654**	(61,834)
Intangible assets	**2,588,470**	2,667,716
	2,624,124	2,605,882

22. Earnings per share

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

	February 28, 2011	February 28, 2010
Weighted daily average number of common shares	**19,120,567**	19,120,567
Diluted effect of stock options	**-**	-
Weighted average number of diluted common shares	**19,120,567**	19,120,567

23. Segmented Information

The Company's activities are comprised of Franchise operations, Corporate store operations, Distribution operations and Food processing operations. The Company considers its Real estate activities as part of the franchise operations segment.

	February 28, 2011			
	Franchise operations	**Corporate stores**	**Distribution center**	**Food processing**
	$	**$**	**$**	**$**
Revenues	**12,777,509**	**2,497,154**	**1,177,472**	**1,023,902**
Operating expenses	**7,330,847**	**2,480,802**	**1,068,043**	**1,162,913**
Operating margin	**5,446,662**	**16,352**	**109,429**	**(139,011)**

	February 28, 2010			
	Franchise operations	Corporate stores	Distribution center	Food processing
	$	$	$	$
Revenues	12,328,504	1,985,049	nil	nil
Operating expenses	6,959,840	1,834,871	nil	nil
Operating margin	5,368,664	150,178	nil	nil

24. Statement of cash flows

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

	February 28, 2011	February 28, 2010
Accounts receivable	**165,163**	(2,289)
Income taxes receivable	**(1,266,732)**	(66,169)
Inventory	**(84,904)**	24,707
Franchise locations under construction held for resale	**713,718**	113,823
Loans receivable	**(59,051)**	38,333
Prepaid expenses	**(47,543)**	(35,122)
Deposits	**(80,297)**	(56,700)
Accounts payable and accrued liabilities	**(1,433,706)**	361,750
Income taxes payable	**(851,138)**	(44,032)
	(2,944,490)	334,301

Supplemental disclosure of cash flows

Income taxes paid	2,250,838	1,289,838

25. Comparative Figures

Certain comparative figures have been reclassified to conform to the current year’s presentation.