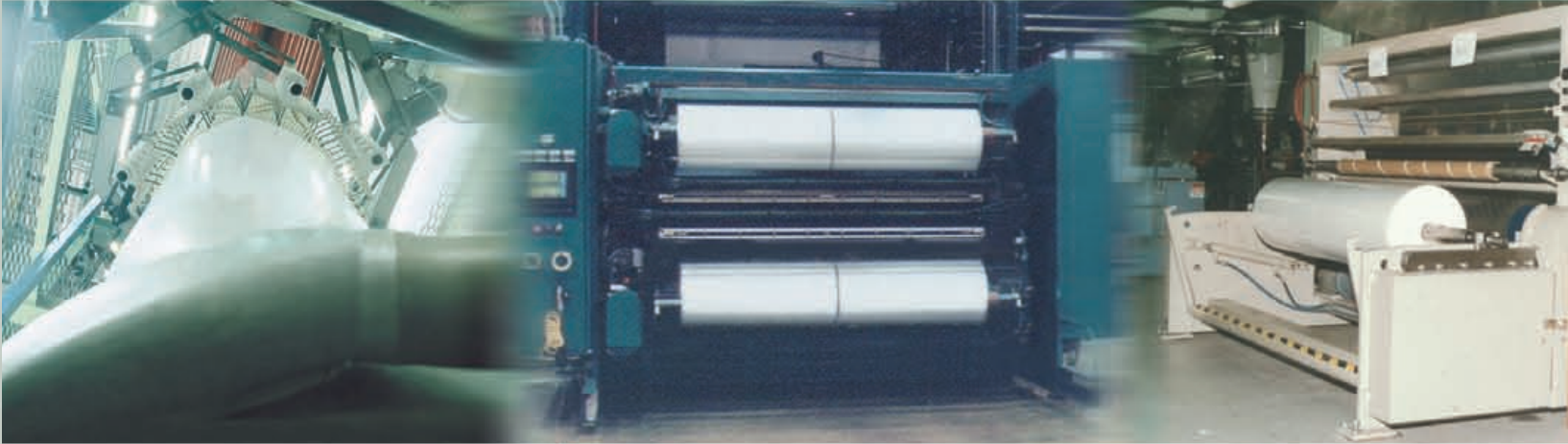


**ANNUAL REPORT**  
2012

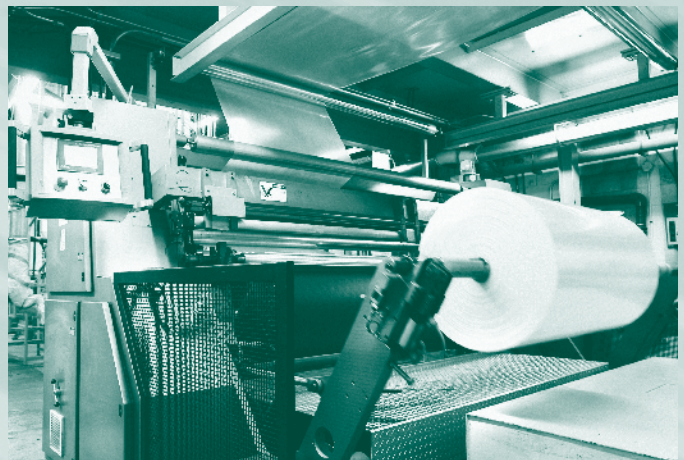
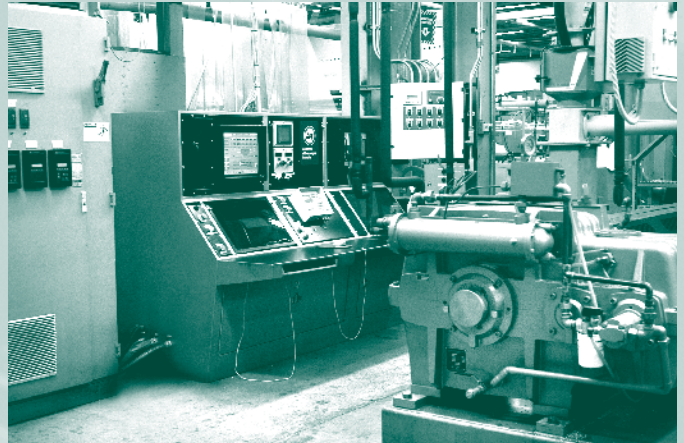
**IMAFLEX**  
*Committed to Excellence*



IN ALL SUCCESSFUL BUSINESSES THE KEY TO SUCCESS RELIES ON MANAGEMENT'S ABILITY TO MASTER THREE FUNDAMENTALS:

- > COMMITMENT TO CUSTOMER
- > CLEAR VISION OF GOALS
- > CORRECT TIMING OF ACTIONS

OUR SENIOR MANAGEMENT TEAM KNOWS, UNDERSTANDS AND LIVES BY THESE PILLARS OF BUSINESS FUNDAMENTALS.





## REPORT TO SHAREHOLDERS

It has been a very remarkable year.

Whereas the year 2011 necessitated that management focus strictly on the short term needs of a turnaround, the year 2012 was one of re-building for the future. Firstly money was raised for the asset purchase in February 2012. This was followed in April by the announcement of a patent application. These stepping stones are the reasons why I believe 2013 will be viewed as a watershed year for our Company.

Imaflex has four manufacturing components to its business. Two of these have been reliable sources of profitability to the Company for years. In this regard, 2012 was no exception as these two parts continued to perform well and in line with expectations. Our U.S. subsidiary, which has been a challenge for years for reasons that have been expounded upon in past reports to shareholders, has seen a marked reversal in fortunes since we completed the business acquisition by way of an asset purchase in the first quarter of 2012. This acquisition will reverse this subsidiary's poor performance even if the process of integrating this business within Imaflex USA limited the contribution to consolidated profitability during the year. Management fully expects that Imaflex USA will contribute to profits in 2013 which it has heretofore never done.

Furthermore, as previously reported, management has been active in preparing the groundwork to create a sales team devoted to its agricultural products. This sales team should allow the Company's weakest division to recapture the revenues it gave up in 2010 with the additional benefit of also increasing revenues for our US entity. The additional growth in revenues from these products, at both Canslit and Imaflex USA begins this year.

I am also pleased to report that Dr. Ralf Dujardin, the head engineer at Bayer Innovation GmbH with whom we collaborated in the creation of new revolutionary agricultural film for which Imaflex and Bayer have jointly applied for a Patent, will be joining Imaflex as of July 1 2013 as V.P. Innovations; Sales and Marketing for the agricultural markets. His international experience, expertise, and contacts, are such that management believes he will prove to be an invaluable asset for the Company. He will not only assist our Canslit division in recovering sales but also help our US entity in expanding its sales as well as assuring our success in launching new products we have and will create.

Management has been busy preparing the groundwork for the superior profitability it expects to generate in the long term. Imaflex invests heavily in research and development. These investments in R & D continue to create a distinction between our Company and the polyethylene industry as a whole. The new active ingredient film for which we have jointly applied for a patent with Bayer is but one example. Further developments will be announced in due course if they prove to be material. By shifting to more innovative products a greater share of our revenues should be generated from non-commodity segments of the market. Management expects that this will create higher margins of profitability.

Management is confident that 2013 will be our break out year.

These earnings will facilitate management's ability to make a reality of its acquisition strategy

I extend special thanks to our polymer engineers for their ingenuity. Our suppliers and employees are to be thanked for their dedication and support in helping us achieve our objectives. Lastly, I wish to thank our board members for their continuing contributions and our shareholders for the patience and trust they have exhibited in our management team.

I believe that the plan to aggressively grow Imaflex, that was conceived years ago but sidetracked by a series of unfortunate circumstances, will soon be a reality. I am truly looking forward to the coming years as we are finally able to execute our plan and resume the growth that marked the Company's early years.

Regards,

Joe Abbadonato  
President and CEO

## FINANCIAL HIGHLIGHTS

(\$ thousands, except per share data)	Year ended December 31,					
	2012	2011	2010	2009	2008	2007
<b>Operating summary</b>						
Sales	\$ 47,269	\$ 46,959	\$ 46,489	\$ 48,190	\$ 54,570	\$ 46,840
Net profit (loss)	(568)	74	(1,751)	(403)	(2,091)	(56)
Profit (loss) per share	(0.013)	0.002	(0.044)	(0.010)	(0.056)	(0.002)
EBIT(1)	201	832	(1,158)	420	(495)	1,176
EBITDA(2)	1,462	2,141	189	3,512	2,901	3,822
EBITDA per share	0.034	0.053	0.005	0.089	0.078	0.102
<b>Financial Position</b>						
Working Capital	2,303	1,748	(550)	249	(2,419)	6,525
Capital assets	15,494	14,602	15,663	16,631	20,337	22,900
Total assets	31,996	31,102	33,005	35,515	39,468	39,301
Total long-term debt (including finance leases)	3,535	3,133	5,573	7,196	11,250	13,717
Shareholder's equity	\$ 14,772	14,926	14,026	15,944	16,591	18,130

(1) Earnings before interest and taxes

(2) Earnings before interest, taxes, depreciation and amortization

## QUARTERLY FINANCIAL INFORMATION

	SALES		NET PROFIT (LOSS)	
	2012	2011	2012	2011
First Quarter	\$ 11,818	\$ 14,343	\$ (104)	\$ 117
Second Quarter	12,202	11,554	149	70
Third Quarter	11,157	10,461	(467)	82
Fourth Quarter	12,092	10,601	(146)	(195)
	\$ 47,269	\$ 46,959	\$ (568)	\$ 74

	EBITDA		PROFIT (LOSS) PER SHARE	
	2012	2011	2012	2011
First Quarter	\$ 378	\$ 742	\$ (0.002)	\$ 0.003
Second Quarter	693	686	0.003	0.002
Third Quarter	(86)	615	(0.011)	0.002
Fourth Quarter	477	98	(0.003)	(0.005)
	\$ 1,462	\$ 2,141	\$ (0.013)	\$ 0,002



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A")

As required by regulators, the purpose of this MD&A is to explain management's point of view on Imaflex Inc.'s (the "Company" or "Imaflex") past performance and future outlook. This report also provides information to improve the reader's understanding of the consolidated financial statements and related notes. Please refer to the consolidated financial statements for the years ending December 31, 2012 and 2011 when reading this MD&A. Unless otherwise indicated, all financial data in this document is prepared in accordance with International Financial Reporting Standards ("IFRS" hereafter) and all amounts are expressed in Canadian dollars. Differences may occur due to the rounding of amounts for the presentation of information in thousands of dollars. In this MD&A we also use financial measures that are not defined by IFRS. Please refer to the section entitled "Non-IFRS Financial Measures" for a complete description of these measures. The consolidated financial statements include the accounts of the Company, those of its wholly-owned subsidiary, Imaflex USA, Inc. ("Imaflex USA") and its divisions, Canguard Packaging ("Canguard") and Canslit ("Canslit"). To facilitate the reading of this report, the terms "Imaflex", "Company", "we", "our", "us" all refer to Imaflex Inc. together with its subsidiary. This MD&A is prepared in conformity with National Instrument 51-102 and Form 51-102F1 and has been approved by the board of directors prior to its release.

### **FORWARD LOOKING STATEMENTS**

From time to time, we make forward-looking statements within the meaning of certain securities laws, including the "safe harbor" provisions of the Securities Act (Ontario). We may make such statements in this document, in other filings with Canadian regulators, in reports to shareholders or in other communications. These forward-looking statements include, among others, statements regarding the business and anticipated financial performance of the Company. The words "may", "could", "should", "would", "outlook", "believe", "plan", "anticipate", "expect", "intend", "objective," the use of the conditional tense and words and expressions of similar nature are intended to identify forward-looking statements.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, which give rise to the possibility that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on these statements, as a number of important factors could cause our actual results to differ materially from the beliefs, plans, objectives, expectations, anticipations, estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to, the length and severity of the current economic downturn, management of credit, market dynamics, liquidity, funding and operational risks; the strength of the Canadian and U.S. economies in which we conduct business; the impact of the movement of the Canadian dollar relative to other currencies, particularly the U.S. dollar; the effects of changes in interest rates; the effects of competition in the markets in which we operate; our ability to successfully align our organization, resources, and processes; the availability and price of raw materials; failure to achieve planned growth associated with the U.S. operations and future sales; changes in accounting policies and methods we use to report our financial condition, including uncertainties associated with critical accounting assumptions and estimates; operational and infrastructure risks; other factors may affect future results including, but not limited to, timely development and introduction of new products and services; changes in tax laws, technological changes, new regulations; the possible impact on our businesses from public-health emergencies, international conflicts and other developments; and our success in anticipating and managing the foregoing risks.

We caution our readers that the foregoing list of important factors that may affect future results is not exhaustive. When relying on our forward-looking statements to make decisions with respect to the Company, investors and others should carefully consider the foregoing factors and other uncertainties and potential events. Unless otherwise required by the securities authorities, we do not undertake to update any forward-looking statement that may be made from time to time by us or on our behalf. The forward-looking statements contained herein are based on information available as of April 16, 2013.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### COMPANY OVERVIEW

The Company operates in one reportable segment being the development, manufacture and sale of packaging materials. The results herein include those of Imaflex, located in Montréal (Québec), its divisions Canguard and Canslit, located in Victoriaville (Québec), and its wholly owned subsidiary, Imaflex USA, located in Thomasville (North Carolina). All intercompany balances and transactions have been eliminated on consolidation.

Imaflex and Imaflex USA specialize in the manufacture and sale of custom-made polyethylene films and bags suited for various packaging needs of our customers. Canguard specializes in the manufacture and sale of polyethylene garbage bags for both the retail and industrial markets. Canslit specializes in the metallization of plastic film.

The common shares of the Company are listed for trading on the TSX Venture Exchange under the symbol "IFX". The Company's head office is located in Montréal (Québec).

### NON-IFRS FINANCIAL MEASURES

The Company's management uses a non-IFRS financial measure in this MD&A, namely EBITDA. Management wishes to specify that in the performance of the Company's financial results, EBITDA is shown as "Earnings before interest, taxes, depreciation and amortization". The reader may refer to the table below for the reconciliation of the EBITDA used by the Company to its reported profit or loss.

Reconciliation of EBITDA to profit or loss:

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
(Loss) profit	\$ (146)	\$ (195)	\$ (568)	\$ 74
Plus:				
Income taxes	195	(144)	298	264
Finance expense	122	122	509	556
Depreciation and amortization	313	329	1,261	1,309
Change in fair value of derivative financial instrument	(7)	(14)	(38)	(62)
EBITDA	\$ 477	\$ 98	\$ 1,462	\$ 2,141
Basic and diluted EBITDA per share *	\$ 0.011	\$ 0.002	\$ 0.034	\$ 0.053

\*Basic weighted average number of shares outstanding of 42,601,276 for the quarter ended December 31, 2012 (40,665,791 in 2011) and 42,437,341 for the year ended December 31, 2012 (40,103,426 in 2011). Diluted weighted average number of shares outstanding of 42,649,519 for the quarter ended December 31, 2012 (40,706,240 in 2011) and 42,487,091 for the year ended December 31, 2012 (40,127,696 in 2011).

While EBITDA is not a standard IFRS measure, management, analysts, investors and others use it as an indicator of the Company's financial and operating management and performance. EBITDA should not be construed as an alternative to profit determined in accordance with IFRS as an indicator of the Company's performance. The Company's method of calculating EBITDA may be different from those used by other companies.



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### **BUSINESS OVERVIEW**

Imaflex is primarily a provider of polyethylene films to converters, who process film into a finished product. The converting process involves printing the required information on the film that Imaflex supplies them based on their end-customer's needs. Imaflex also manufactures bags that are sold for a variety of uses, including garbage bags. Additionally, the Company produces specialized metallized film for specific agricultural usage.

Imaflex operates four manufacturing facilities, two of which are located in the Province of Québec, in Montréal and in Victoriaville, and two others located in Thomasville, North Carolina, in the United States. The four facilities cover a total area of approximately 22,800 square meters or 228,000 square feet.

### **MARKET OPPORTUNITY**

The North American flexible packaging market is valued at approximately \$25 billion. Although this market is highly fragmented and commoditized in terms of pricing, there are niches within this larger market that offer the opportunity of increased profitability.

Management believes that four factors will contribute to Imaflex's long term growth and its ability to properly position itself within the industry in which it operates.

The first is continued investment in research and development efforts allowing our research teams to develop on a timely basis new products for highly profitable niche markets as the older niches gradually become price sensitive with the entry of new participants.

The second is the efficiency of our equipment, and our commitment to sustain this efficiency with the required capital investments. This will allow us to remain cost competitive in the marketplace.

The third is our access to capital. Being a publicly traded company we have the ability to tap into the equity markets if the right opportunity comes along. This is in addition to the credit facilities currently provided to the Company by its banks.

The fourth is our manufacturing presence in both Canada and the United States which confers to the Company a competitive advantage in terms of logistics, currency, and manufacturing flexibility.

### **OUTSOURCING**

Our industry is capital intensive. Labour is only a minor component in the total cost of production. As a result, outsourcing production to countries with lower wages would not have a material impact on the cost of production, especially when factoring in expenses related to freight and duty.

Furthermore, the risks associated with quality and on-time delivery would far outweigh any minimal benefit to our customers that would be generated by lower labour costs. Accordingly, management does not currently contemplate the establishment of an outsourcing strategy.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### **BUSINESS STRATEGY**

Imaflex is focused on providing its customers the highest quality products on a timely basis and at competitive prices. This strategy has been the backbone of our growth and it has served us well.

Some competitors, experiencing idle operations or producing at below average capacity levels, may attempt to gain market share through reduced pricing, particularly during difficult economic times.

Imaflex still believes that maintaining its focus on the quality of its products and the excellence of its customer service remains its best long term strategy, as these two characteristics define our position and reputation in the market, and this regardless of the fluctuations in the economic cycle.

### **GROWING CUSTOMER BASE**

In our market, it becomes essential to sell value-added products and avoid producing highly commoditized products generating lower margins. The key to the success of this strategy is to identify and build relationships with customers having specific needs and eventually develop products that address their customized specifications. Our sales force's primary mandate is to find such clients.

### **RISK FACTORS**

The Company is involved in a competitive industry and marketplace in which there are a number of participants. To accommodate and effectively manage future growth, the Company continues to improve its operational, financial and management information systems, as well as its production procedures and controls. The Company's success is largely the result of the continued contributions of its employees and the Company's ability to attract and retain qualified management, sales and operational personnel.

The market the Company competes in has historically shown resiliency and growth even at the worst economic times. The Company's customers operate predominantly in the food packaging and agriculture markets. This fact, coupled with the expanding product lines and reliance on newer and faster equipment, should help it weather the potential volatility caused by uncertainty in the North American economic climate.

Factors which can impact the Company include, but are not limited to: management of credit, market dynamics, liquidity, funding and operational risks; the strength of the Canadian and U.S. economies in which we conduct business; the impact of the movement of the Canadian dollar relative to other currencies, particularly the U.S. dollar; the effects of changes in interest rates; the effects of competition in the markets in which we operate; our ability to successfully align our organization, resources, and processes; the availability and price of raw materials; failure to achieve planned growth associated with the U.S. operations; changes in accounting policies and methods we use to report our financial condition, including uncertainties associated with critical accounting assumptions and estimates; operational and infrastructure risks; other factors may affect future results including, but not limited to, timely development and introduction of new products and services; changes in tax laws, technological changes and new regulations; the possible impact on our businesses from public-health emergencies, international conflicts and other developments; and our success in anticipating and managing the foregoing.



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### **GENERAL SITUATION OF THE POLYETHYLENE BLOWN FILM MARKET**

Pricing was fairly flat in the fourth quarter of 2012 compared to the third quarter as polyethylene producers kept production tightly in line with demand, thus avoiding increasing their inventory levels. As the export market improved in the first quarter, pricing increased as well early in 2013. Prices are expected to remain relatively flat for the second quarter of 2013.

### **LOSS OF BUSINESS FROM A SIGNIFICANT CUSTOMER**

One of our business strategies has been to limit the purchases of any particular customer to less than 15% of our revenues. This strategy ensures us that our profitability and financial well-being are not dependent on any one client.

### **COMPETITION FROM OTHER COMPANIES**

Competition in our market is at the moment quite intense due to the imbalance between supply and demand. Nevertheless, because we are dealing in a \$25 billion market; because we have highly skilled teams that are quick to respond to customer needs; because we have a diversified manufacturing base; and because the bulk of our customers deal in food related products, we believe that we have a competitive edge. It may not always translate into a greater net profit, but it certainly does translate into customer loyalty should we decide to match our competitors' prices.

### **SEASONALITY OF OPERATIONS**

Our operations in Victoriaville and in Thomasville are subject to seasonality as a result of their partial manufacturing focus in the production of agricultural film products sold to fruit and vegetable growers. Customer demand in this end-market peaks twice yearly. Inventory is managed in a way to optimize cash flow while remaining able to react to any market opportunities that present themselves. However, because these locations also manufacture products that are destined for other markets which are not affected by seasonal downturns, these two plants are still able to operate all year, albeit at lower capacity levels.

### **EXPOSURE TO PRODUCT LIABILITY**

Due to the nature of its operations, which consist of manufacturing polyethylene films transformed by our customers for their end-customers, Imaflex's exposure to product liability is low. Imaflex is not exposed to liability for personal injury or death arising from negligence in the manufacturing of the films either.

The only market segment that exposes the Company to potential product liability claims is the agricultural market. In this market, proof of negligence in our manufacturing process could entail some form of compensation in the event that the expected crop yields do not materialize.

Although the likelihood of a claim in this market is low, we are nonetheless covered by a product liability insurance policy in the amount of \$ 25,000,000.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### **FLUCTUATIONS IN OPERATING RESULTS**

It is important to note that profitability may vary from quarter to quarter, irrespective of quarterly sales. This is due to many factors, including and not limited to: competitive conditions in the businesses in which the Company participates; general economic conditions and normal business uncertainty; product mix; fluctuations in foreign currency exchange rates; the availability and costs of raw materials; changes in the Company's relationship with its suppliers; and interest rate fluctuations and other changes in borrowing costs.

### **EXPOSURE TO INTEREST RATE FLUCTUATIONS**

We have not, nor do we expect to have, a significant increase in borrowing costs. Although it is possible that a future increase in interest rates will impact our finance expense, the decrease in our current outstanding long term debt should offset the increase in interest rates.

### **ABILITY TO ATTRACT AND RETAIN QUALIFIED PERSONNEL**

Imaflex's core operational management team has been stable over the past years and was able to keep key competencies within the Company. This is because the three founders, who have more than 100 years of combined experience in management and R & D, were and remain at the core of its management team. As the Company has grown, it has strengthened its team with the addition of individuals having a variety of competencies, be it accounting, operations, or engineering.

This has resulted in a work environment that allows for the free exchange of ideas in an effort to ensure that the Company remains at the forefront of our industry. We are confident that we can retain and, if need be, attract qualified individuals that will contribute to our quest of building shareholder value.

### **MANAGEMENT OF GROWTH**

Imaflex's history attests to its management's ability to create and manage growth and to successfully adapt to prevailing and continuously changing market conditions. Management believes that future success will also lie in the ability to properly manage growth whether it comes from new markets and products, acquisitions, mergers, or a combination of any or all three. This success will depend on the Company's ability to seek out new opportunities and to position itself such that it will be able to take advantage of them when they present themselves. Past decisions have been made bearing this in mind and the Company is now in a better position to make this happen.

### **FOREIGN EXCHANGE FLUCTUATIONS**

A portion of the Company's sales and expenses as well as accounts receivable and payable are denominated in US dollars. A portion of the revenue stream in US dollars acts as a natural hedge to cover expenses denominated in US dollars. However management continuously monitors the Company's foreign exchange exposure. The analysis of the Company's exposure for the fourth quarter of 2012 has resulted in management deciding not to hedge the Company's foreign exchange risk.



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### ENVIRONMENTAL HAZARDS

The Company's raw materials, processes and finished goods do not have any hazardous implications. However we do buy a few items which are used in our production equipment such as cooling products which may be hazardous, but their use and manipulation are controlled. Though these products actually pose very little risk, they are handled in a manner that fully complies with existing safety regulations.

### RESULTS OF OPERATIONS

The Company ended the year with a strong quarter after a sluggish beginning. Sales of existing products increased as expected increases in polyethylene prices stimulated customer demand. Moreover, operational improvements that were undertaken in 2011 and completed in 2012 as well as the integration of the acquired business helped grow sales and brought improvements to the bottom line in the fourth quarter.

The fourth quarter has proven that with strong customer demand and with the expected completion of the integration of the acquired business, Imaflex should generate additional growth and the Company will be capable of delivering positive results. Coupled with expected growth in existing mulch products, results are expected to improve in 2013.

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
Sales	\$ 12,092	\$ 10,601	\$ 47,269	\$ 46,959

Sales increased for the three month period ended December 31, 2012 compared to 2011 due to the additional sales generated by the acquired assets as well as an increase in Imaflex's overall sales volume. Sales increased by \$ 310,160 for the year ended December 31, 2012 compared to 2011. The sales trend was relatively stable throughout 2012 whereas in 2011, the very high sales in the first quarter of the year were followed by lower sales for each of the following quarters. These variations are partly explained by the expectation of movements in polyethylene prices. The fourth quarter, although not having the highest sales in 2012, was the quarter where the variance over 2011 was most important.

The Company is still working on rebuilding the mulch film sales that were relinquished late in 2009. Although progress has been made, the Company has yet to reach sales levels achieved prior to the 2010 fiscal year.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### RESULTS OF OPERATIONS (continued)

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
Gross Profit (\$) before amortization of production equipment	\$ 1,555	\$ 1,202	\$ 5,843	\$ 6,093
%	12.9%	11.3%	12.4%	13.0%
Amortization of production equipment	257	264	1,039	992
Gross profit (\$)	\$ 1,298	\$ 938	\$ 4,804	\$ 5,101
Gross profit (%)	10.7%	8.8%	10.2%	10.9%

The gross profit before amortization increased for the three-month period ended December 31, 2012 compared to 2011 mainly due to the stronger sales which generated additional profitability. The gross margin increased from 11.3% to 12.9%. During the fourth quarter of 2012, sales from the acquired assets generated increased contribution over raw material and permitted a higher utilization of the Company's assets during the period.

The amortization decreased slightly for the three-month period ended on December 31, 2012 and the gross profit increased by approximately \$360,000 quarter over quarter.

The gross margin before amortization for the year ended December 31, 2012 decreased despite the increased sales mainly due to the additional costs to run the acquired operations. The Company also incurred additional expenses in its U.S. operations in order to fully complete the integration of the acquired assets and to prepare for 2013. These additional costs were required in order to be able to reach the capacity level required for 2013. Lower sales in mulch film were offset by cost reduction efforts which limited the decrease in profitability due to lower sales.

The amortization of production equipment increased slightly from \$ 991,819 in 2011 to \$ 1,039,086 in 2012. The gross margin after the amortization of production equipment decreased from \$ 5,101,076 in 2011 to \$ 4,804,417 in 2012.

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
Selling and administrative	\$ 1,090	\$ 1,044	\$ 4,266	\$ 4,323
As a % of sales	9.0 %	9.8 %	9.0%	9.2%

Selling and administrative expenses increased slightly for the fourth quarter of 2012 compared to 2011, which was expected given the increase in sales, which generated a higher commission expense. However, as a percentage of sales, selling and administrative expenses decreased from 9.8% to 9.0% given the increase in sales and the fact that the Company did not incur any significant additional administrative expenses.

For the year ended December 31, 2012, expenses also increased slightly compared to 2011 due to the slight increase in sales, however overall expenses remained relatively constant, reaching 9.0% of sales in 2012 down from 9.2% in 2011, given the overall cost structure of the Company remained comparable from 2011 to 2012.



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### RESULTS OF OPERATIONS (continued)

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
Finance expense	\$ 122	\$ 122	\$ 509	\$ 556

Finance expenses remained constant for the three month period ended December 31, 2012 as the decreasing finance expenses on the long term debts and the line of credit were offset by the interest expenses recorded on the balance of sale of the business acquisition which does not have any impact on the Company's cash flow. Increased interest on the finance leases entered into in 2012 also had a minor impact on the Company's finance expense.

Over the year, the finance expense decreased in 2012 over 2011 due to lower interest paid on long term debt and the line of credit borrowings, which was offset by the interest expense recorded on the balance of sale for the business acquisition. The interest rate paid on the Company's line of credit borrowings remained constant throughout most of 2011 and 2012, however payments on interest decreased slightly due to a generally lower usage of the line of credit.

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
Foreign exchange (gain) loss	\$ (94)	\$ 193	\$ 231	\$ (95)

The strengthening of the US dollar against the Canadian dollar in the fourth quarter of 2012 resulted in a foreign exchange gain compared to a foreign exchange loss due to the weakening of the US dollar in the fourth quarter of 2011. This led to a positive impact on the Company's results of \$287,000 in the fourth quarter of 2012 compared to 2011.

For the year ended December 31, 2012 the Company incurred a loss due to the weakening of the US dollar over the period compared to a gain for the same period in 2011 due to the strengthening of the US dollar in 2011. These movements in foreign exchange led to a negative impact on the Company's results of approximately \$326,000 year over year.

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
Income taxes	\$ 195	\$ (144)	\$ 298	\$ 264
As a % of profit before taxes	396.9%	42.6%	(110.6)%	78.2%

The income tax expense was approximately \$195,000 for the quarter ended December 31, 2012 given the positive net income before income taxes realized in the Canadian legal entity. It represents 396.9% of profit before taxes mainly due to the losses suffered in the US subsidiary for part of which a tax benefit was not recorded as well as the low profit before tax, which amplifies the income tax expense as a percentage of pretax income.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### RESULTS OF OPERATIONS (continued)

For the year ended December 31, 2012, the income tax expense increased from \$263,827 to \$298,458. This is mainly due to the increase in taxable income due to items included in profit that are not deductible for the calculation of taxable income. As a percentage of pretax income, the income tax expense represented 78.2% in 2011 compared to (110.6)% in 2012. Given the tax benefits of the taxable losses in the US operations are not entirely recognized, an income tax expense was recorded despite the consolidated pretax loss.

(\$ thousands, except per share data)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
(Loss) profit	\$ (146)	\$ (195)	\$ (568)	\$ 74
Basic earnings per share	\$ (0.003)	\$ (0.005)	\$ (0.013)	\$ 0.002

The Company's results improved for the fourth quarter of 2012 compared to 2011 mainly due to the increase in gross profit due to higher sales and the positive variance on foreign exchange movements. The increases were offset by a significantly higher income tax expense and slightly higher selling and administrative expenses.

The operating results for the year decreased in 2012 compared to 2011 mainly due to the increased expenses incurred following the business acquisition in the U.S., costs incurred in order to prepare for the growth in the U.S. operations as well as unfavourable movements in foreign exchange and a higher income tax expense.

### Financial Position

#### **December 31, 2012 vs. December 31, 2011**

From December 31, 2011 to December 31, 2012, current assets decreased by \$ 638,368, mainly due to the decrease of accounts receivable after part of them were used to finance the purchase of a piece of equipment. Cash also decreased by \$ 116,814 and inventories decreased slightly by \$ 15,831. These decreases were offset by the \$ 100,588 increase in prepaid expenses year over year. The Company continued to optimize its inventory level throughout the year in order to effectively manage its financial position.

Current liabilities decreased by approximately \$ 1,193,291, mainly due to the long-term portion of term debt being included in non-current liabilities, whereas all term debt was included in current liabilities in 2011. The current portion of long-term debt decreased by approximately \$ 2,031,152 year over year. The fair value of the derivative financial instrument decreased by \$ 39,323, due to the lower outstanding notional amount of the underlying debt. This was offset by the \$ 476,628 increase in bank indebtedness and the \$ 382,917 increase in trade and other payables. The current tax liability increased by \$ 22,881.



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### SUMMARY OF QUARTERLY RESULTS

Summary financial data derived from the Company's unaudited quarterly financial statements and audited financial statements for each of the eight most recently completed quarters are as follows:

For the quarters ending March, June, September and December (\$ thousands, except per share data):

	Q4/12	Q3/12	Q2/12	Q1/12	Q4/11	Q3/11	Q2/11	Q1/11
Sales	12,092	11,157	12,202	11,818	10,601	10,461	11,554	14,343
Profit (loss)	(146)	(467)	149	(104)	(195)	82	70	117
Earnings (loss) per share:								
Basic and diluted	(0.003)	(0.011)	0.003	(0.002)	(0.005)	0.002	0.002	0.003

It is important to note that profitability may vary from quarter to quarter, irrespective of quarterly sales due to many factors. These factors include and are not limited to: competitive conditions in the businesses in which the Company participates; general economic conditions and normal business uncertainty; product mix; fluctuations in foreign currency rates; the availability and costs of raw materials; changes in the Company's relationship with its suppliers; and interest rate fluctuations and other changes in borrowing costs.

### LIQUIDITY

Working capital as at December 31, 2012 was \$ 2,303,260 compared to \$ 1,748,337 as at December 31, 2011.

### Cash Flows from Operating Activities

Cash flows from operating activities before movements in working capital were \$ 362,257 for the fourth quarter of 2012 compared to approximately \$ 278,000 in 2011. For the year ended December 31, 2012, cash flow from operating activities before movements in working capital decreased by \$418,988, which is mainly explained by the \$641,862 decrease in net income from 2011 to 2012. Other elements had an opposite impact of \$222,874. Movements in the Company's working capital had a positive impact of \$ 366,297 in 2012 compared to \$ 972,337 in 2011. The Company paid \$ 80,860 less in interest, but paid \$ 286,247 more in income taxes, for a net effect of \$ 205,387.

The Company also entered into transactions that did not have an impact on cash flow by financing the acquisition of machinery through the issuance of a credit note, thus reducing trade receivables.

### Cash Flows from Financing Activities

Cash outflows relating to financing activities for the fourth quarter of 2012 were the repayment of term debt as per the original debt repayment schedule of \$ 149,776 and the repayments on finance leases of \$ 5,820, which were offset by the increase in bank indebtedness of \$ 363,706. In 2011, the cash outflow related to financing activities was \$494,921, due mainly to the receipt of \$250,000 in anticipation of the closing of a private placement, the issuance of subordinated debt of \$165,000, which was offset by the reimbursement of long term debt of \$550,226, \$2,778 on its finance leases and \$356,918 on its bank indebtedness.

For the 2012 fiscal year, the Company had cash inflows for \$ 205,196. It repaid \$739,642 on its long term borrowings and \$17,274 on finance leases. It increased borrowings on its line of credit by \$476,628 and closed a private placement which generated funds received in 2012 of \$485,484. In 2011, the Company had total cash outflows of \$2,212,611, as it repaid \$2,403,711 on its borrowings, \$13,105 on finance leases and decreased borrowings on its line of credit by \$710,795. These outflows were offset by the closing of a private placement for \$500,000 and the receipt of \$250,000 in anticipation of the private placement that closed in the first quarter of 2012 and the issuance of subordinated debt of \$165,000.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### LIQUIDITY (CONTINUED)

#### Cash Flows from Investing Activities

During the quarter ended December 31, 2012, the Company incurred cash outflows relating to investing activities mainly for the completion of leasehold improvements. During the fourth quarter of 2011, the Company incurred cash outflows for investing activities for minor improvements to pieces of equipment. During the year ended December 31, 2012, the Company incurred cash outflows relating to investing activities of \$ 1,547,989, representing a cash payment for a business acquisition of \$ 989,500 as well as payments of \$ 558,489 for leasehold improvements and expenses relating to equipment. In 2011, the Company only incurred \$ 81,441 of cash outflows relating to investing activities as no important purchases were required.

### CONTRACTUAL OBLIGATIONS

The contractual obligations as at December 31, 2012 were as follows:

(\$ thousands)	Payments due by period			
	Total	Less than 1 year	1 – 5 years	After 5 years
Long-term debt	\$ 3,730	\$ 1,194	\$ 2,536	\$ -
Finance leases	66	39	27	-
Operating leases	3,433	845	1,920	668
Bank Indebtedness	6,104	6,104	-	-
Interest rate swap	10	10	-	-
<b>Total contractual obligations</b>	<b>\$ 13,343</b>	<b>\$ 8,192</b>	<b>\$ 4,483</b>	<b>\$ 668</b>

These contractual obligations are sensitive to the fluctuation of interest rates. These obligations are based on interest rates and foreign exchange rates effective as at December 31, 2012.

### CAPITAL RESOURCES

The Company has an operating line of credit with its bankers to a maximum of \$ 8,500,000 bearing interest at a rate of prime plus 2.0%. The line of credit is secured by trade receivables and inventories. As at December 31, 2012, the Company had drawn \$ 6,103,876 on its line of credit (\$ 5,627,248 as at December 31, 2011). The Company's working capital increased since December 31, 2011, going from \$ 1,748,337 to \$ 2,303,260, mainly explained by the inclusion of the long term portion of term debt in non-current liabilities. During the first quarter of 2012, the Company issued 1,935,485 units, each comprising of one common share and one common share purchase warrant entitling the holder to acquire one additional common share for \$0.45, for a consideration of \$735,484, of which \$250,000 was received during the course of the fourth quarter of 2011. The Company also invested \$ 989,500 in cash for the acquisition of operations in North Carolina during the first quarter. The Company believes it has sufficient capital to continue operating efficiently through the liquidity available in its working capital and the liquidity that will be generated by its operations. Within twelve months, only one bank debt will remain outstanding, in addition to the balance of sale on the business acquisition. The Company's current capital structure should therefore enable it to meet all of its short term obligations. As part of its normal management process, the Company continuously monitors its capital structure and considers the increase in indebtedness or the issuance of shares as possible options to optimize its capital structure.



## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### PROPOSED TRANSACTION

The Company is currently considering a potential business acquisition aimed to increase the Company's profitability. There are no agreements currently signed and the Company has no commitment to complete this transaction. Management is still in the process of determining if the target is a proper fit for the Company's operations and any closing is conditional upon obtaining the required financing to complete the transaction.

### RELATED PARTY TRANSACTIONS

In the normal course of operations, the Company had routine transactions with related parties. These transactions are measured at fair value, which is the amount of consideration established and agreed to by the related parties.

The following table reflects the related party transactions recorded for the periods ended December 31, 2012 and 2011. For additional information, please refer to note 26, Related party transactions of the "Notes to the consolidated financial statements" for the years ended December 31, 2012 and 2011.

(\$ thousands)	Three month periods ended		Years ended	
	December 31 2012	December 31 2011	December 31 2012	December 31 2011
<b>Professional fees (a)</b>	<b>\$ 101</b>	\$ 96	<b>\$ 359</b>	\$ 263
<b>Rent (b)</b>	<b>\$ 218</b>	\$ 182	<b>\$ 798</b>	\$ 724

(a) Professional fees include transactions with Polytechnomics Inc., of which Gerald R. Phelps, Imaflex's Vice-President – Operations, is the controlling shareholder and with Lavery de Billy L.L.P., of which Philip Nolan, director of Imaflex, is a partner.

(b) Joseph Abbandonato, Imaflex's President, Chief Executive Officer and Chairman of the Board, is the controlling shareholder of Roncon Consultants Inc. ("Roncon"). The Company's production facilities at Imaflex, Canslit, and Imaflex USA are leased from Roncon and parties related to Roncon under long-term operating lease agreements (see "Contractual Obligations").

### CRITICAL ACCOUNTING POLICIES

The Company's significant accounting policies are disclosed in note 2, Significant accounting policies of the consolidated financial statements for the years ended December 31, 2012 and 2011. This note explains the Company's accounting policies under IFRS.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### **FINANCIAL INSTRUMENTS**

Please refer to note 22, Financial instruments of the consolidated financial statements for the years ended December 31, 2012 and 2011 for disclosure on the Company's financial instruments as well as note 24, Risk management for a discussion on the risks the Company is exposed to and how they are managed.

As at December 31, 2012, the fair value of the interest rate swap of \$ 9,745 (December 31, 2011 – \$ 49,068) has been recorded on the balance sheet under derivative financial instrument, with a charge to the income statement under other gains and losses for all movements in the fair value of the swap since December 31, 2011. As at December 31, 2012, the Company is not using any other swap, forward or hedge accounting.

Through the closing of private placements and share-based compensation, as at December 31, 2012, the Company has 100,000 options to purchase shares of the Company at \$0.125 and 3,251,274 warrants entitling the owner to purchase common shares of the Company at \$0.45 outstanding. A maximum of 1,000,000 shares can be issued if the balance of sale of the recently completed business acquisition is settled in shares as the implied value of the settlement is USD\$ 1 per share.

### **MANAGEMENT OUTLOOK**

Having completed the integration of the business acquired last spring by way of an asset purchase carried-out by our US entity, management believes the fourth quarter growth is a trend which will continue in 2013.

Research and development efforts that the Company has invested in over the years are on the point of paying off with new products allowing us to open niche markets as well as allowing us to have a competitive advantage over our counterparts in competitive areas of the industry.

Management is now primarily focussed on its Canslit division. As stated in prior outlooks, management's focus has been on creating the conditions and a sales team to ensure that this division soon becomes profitable again. Management believes this is imminent and is therefore optimistic about the Company's future.

### **OUTSTANDING SHARE DATA**

As of the date of this report, the Company had 42,601,276 common shares outstanding (40,665,791 as at December 31, 2011).

### **RISK FACTORS**

The Company is involved in a competitive industry and marketplace in which there are a number of participants. To effectively manage future growth, the Company continues to improve its operational, financial and management information systems, procedures and controls. The Company's success is largely the result of the continued contributions of its employees and the Company's ability to attract and retain qualified management, sales and operational personnel.



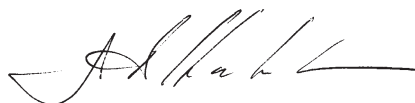
## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A") (CONTINUED)

### RISK FACTORS (CONTINUED)

The \$25 billion market the Company competes in has historically shown resiliency and growth even at the worst economic times. The Company's customers operate predominantly in the food packaging and agricultural markets. This fact, coupled with the expanding product lines and reliance on newer and faster equipment should help it weather the potential volatility caused by uncertainty in the North American economic climate.

Factors which can impact the Company include, but are not limited to: management of credit, market dynamics, liquidity, funding and operational risks; the strength of the Canadian and U.S. economies in which we conduct business; the impact of the movement of the Canadian dollar relative to other currencies, particularly the U.S. dollar; the effects of changes in interest rates; the effects of competition in the markets in which we operate; our ability to successfully align our organization, resources, and processes; the availability and price of raw materials; failure to achieve planned growth associated with the U.S. expansion; changes in accounting policies and methods we use to report our financial condition, including uncertainties associated with critical accounting assumptions and estimates; operational and infrastructure risks; other factors may affect future results including, but not limited to, timely development and introduction of new products and services, changes in tax laws, technological changes, new regulations; the possible impact on our businesses from public-health emergencies, international conflicts and other developments; and our success in anticipating and managing the foregoing risks.

Additional information relating to our Company, including our Annual Report, can be found on SEDAR at [www.sedar.com](http://www.sedar.com).



**Joseph Abbandonato**  
President and Chief Executive Officer

April 16, 2013



**Giancarlo Santella, CPA, CA**  
Corporate Controller

*For investor information, contact*

**JOSEPH ABBANDONATO**  
President and Chief Executive Officer

**514 935-5710**

**IMAFLEX**

5710 Notre-Dame West, Montreal, Quebec, Canada H4C 1V2  
Telephone: 514 935-5710 | Fax: 514 935-0264

Email: [info@imaflex.com](mailto:info@imaflex.com)

[www.imaflex.com](http://www.imaflex.com)

Consolidated Financial Statements of

**IMAFLEX INC.**

Years ended December 31, 2012 and 2011





Deloitte LLP  
1 Place Ville Marie  
Suite 3000  
Montreal QC H3B 4T9  
Canada

Tel: 514-393-5194  
Fax: 514-390-4104

[www.deloitte.ca](http://www.deloitte.ca)

## **INDEPENDENT AUDITOR'S REPORT**

To the Shareholders of Imaflex Inc.

We have audited the accompanying consolidated financial statements of Imaflex Inc., which comprise the consolidated statements of financial position as at December 31, 2012 and 2011, and the consolidated statements of comprehensive (loss) income, the consolidated statements of changes in equity and the consolidated statements of cash flows for the years ended December 31, 2012 and 2011, and a summary of significant accounting policies and other explanatory information.

### **Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Imaflex Inc. as at December 31, 2012 and 2011, and its financial performance and its cash flows for the years ended December 31, 2012 and 2011 in accordance with International Financial Reporting Standards.

Handwritten signature in black ink that reads "J. Schutte" followed by "LLP" with a superscripted "1".

---

<sup>1</sup> CPA auditor, CA, public accountancy permit No. A109522

April 16, 2013



**Consolidated statements of comprehensive (loss) income  
for the years ended  
(in Canadian dollars)**

**December 31,  
2012                      2011**

Revenue	(Note 5.1)	<b>\$ 47,268,941</b>	\$ 46,958,781
Cost of sales		<b>42,464,524</b>	41,857,705
Gross profit		<b>4,804,417</b>	5,101,076
Expenses:			
Selling		<b>1,207,676</b>	1,232,916
Administrative		<b>3,058,410</b>	3,089,853
Finance costs	(Note 8)	<b>509,179</b>	555,875
Other gains and losses	(Note 9)	<b>192,768</b>	(156,889)
Other		<b>106,137</b>	41,843
		<b>5,074,170</b>	4,763,598
(Loss) profit before income taxes		<b>(269,753)</b>	337,478
Income taxes	(Note 10)	<b>298,458</b>	263,827
<b>(LOSS) PROFIT</b>		<b>(568,211)</b>	73,651
<b>Other comprehensive income</b>			
Exchange differences on translating foreign operation		<b>(72,013)</b>	66,499
<b>TOTAL COMPREHENSIVE (LOSS) INCOME</b>		<b>\$(640,224)</b>	\$140,150
<b>(Loss) earnings per share</b>			
Basic and diluted	(Note 11)	<b>\$ (0.013)</b>	\$ 0.002

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

## Consolidated statements of financial position

As at (in Canadian dollars)		December 31, 2012	December 31, 2011
<b>Assets</b>			
<i>Current assets</i>			
Cash		\$ 126,994	\$ 243,808
Trade and other receivables	(Note 12)	8,745,313	9,351,624
Inventories	(Note 13)	6,875,974	6,891,805
Prepaid expenses		113,177	12,589
Total current assets		<u>15,861,458</u>	<u>16,499,826</u>
<i>Non-current assets</i>			
Property, plant and equipment	(Note 14)	15,493,915	14,602,453
Intangible assets	(Note 15)	640,920	-
		<u>16,134,835</u>	<u>14,602,453</u>
Total assets		<u>\$ 31,996,293</u>	<u>\$ 31,102,279</u>
<b>Equity and liabilities</b>			
<i>Current liabilities</i>			
Bank Indebtedness	(Note 17)	6,103,876	5,627,248
Trade and other payables	(Note 16)	6,133,508	5,750,591
Derivative financial instrument		9,745	49,068
Current tax liabilities		173,268	150,387
Long-term debt, current portion	(Note 17)	1,101,425	3,132,577
Finance leases, current portion	(Notes 17, 18)	36,376	41,618
Total current liabilities		<u>13,558,198</u>	<u>14,751,489</u>
<i>Non-current liabilities</i>			
Long-term debt	(Note 17)	2,372,085	165,000
Deferred tax liabilities	(Note 10)	1,269,090	1,259,393
Finance leases	(Notes 17, 18)	25,263	-
Total non-current liabilities		<u>3,666,438</u>	<u>1,424,393</u>
Total liabilities		<u>17,224,636</u>	<u>16,175,882</u>
<i>Capital and reserves</i>			
Share capital	(Note 19)	8,568,452	8,092,323
Reserves		655,967	718,625
Retained earnings		5,547,238	6,115,449
Total equity		<u>14,771,657</u>	<u>14,926,397</u>
Total equity and liabilities		<u>\$ 31,996,293</u>	<u>\$ 31,102,279</u>

Operating lease commitments (Note 23.3)

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

(s) Joseph Abbandonato  
Joseph Abbandonato  
Director

(s) Gilles Émond  
Gilles Émond  
Director



**Consolidated statements of changes in equity**  
**(in Canadian dollars)**

	<u>Reserves</u>					<b>Total Reserves</b>	<b>Retained Earnings</b>	<b>Total</b>
	<b>Share capital</b>	<b>Share-based compensation</b>	<b>Accumulated Foreign currency translation</b>	<b>Warrants</b>	<b>Other</b>			
<b>Balance at January 1, 2011</b>	\$ 7,829,165	\$ 322,500	\$ (167,615)	\$ -	\$ -	\$ 154,885	\$ 6,041,798	\$ 14,025,848
Profit for the year	-	-	-	-	-	-	73,651	73,651
Exchange differences on translating foreign operation	-	-	66,499	-	-	66,499	-	66,499
	-	-	66,499	-	-	66,499	73,651	140,150
Issuance of share capital and warrants (Note 19)	263,158	-	-	236,842	-	236,842	-	500,000
Share-based compensation (Note 20)	-	10,399	-	-	-	10,399	-	10,399
Future issuance of shares and warrants (Note 19)	-	-	-	-	250,000	250,000	-	250,000
<b>Balance at December 31, 2011</b>	<b>\$8,092,323</b>	<b>\$ 332,899</b>	<b>\$ (101,116)</b>	<b>\$ 236,842</b>	<b>\$ 250,000</b>	<b>\$ 718,625</b>	<b>\$ 6,115,449</b>	<b>\$ 14,926,397</b>
Loss for the year	-	-	-	-	-	-	(568,211)	(568,211)
Exchange differences on translating foreign operation	-	-	(72,013)	-	-	(72,013)	-	(72,013)
	-	-	(72,013)	-	-	(72,013)	(568,211)	(640,224)
Issuance of share capital and warrants (Note 19)	476,129	-	-	259,355	(250,000)	9,355	-	485,484
<b>Balance at December 31, 2012</b>	<b>\$8,568,452</b>	<b>\$ 332,899</b>	<b>\$ (173,129)</b>	<b>\$ 496,197</b>	<b>\$ -</b>	<b>\$ 655,967</b>	<b>\$ 5,547,238</b>	<b>\$ 14,771,657</b>

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

**Consolidated statements of cash flows  
for the years ended  
(in Canadian dollars)**

**December 31,  
2012                      2011**

**Cash flows from operating activities:**

(Loss) profit for the year	\$ (568,211)	\$ 73,651
Income tax expense	298,458	263,827
Change in fair value of derivative financial instrument	(38,441)	(62,352)
Depreciation of property, plant and equipment and intangible assets	1,261,483	1,309,689
Finance costs	509,179	555,875
Share-based compensation	-	10,399
Unrealized foreign exchange loss (gain)	135,133	(134,500)
	<u>1,597,601</u>	<u>2,016,589</u>

Movements in working capital

Decrease (increase) in trade and other receivables	228,238	(1,032,073)
Decrease in inventories	291,745	2,127,925
(Increase) decrease in prepaid expenses	(101,174)	1,711
(Decrease) in trade payables and provisions	(52,512)	(125,226)
	<u>366,297</u>	<u>972,337</u>

Cash generated by operations	1,963,898	2,988,926
Interest paid	(470,120)	(550,980)
Net income taxes (paid) received	(265,880)	20,367
<b>Net cash generated by operating activities</b>	<u>1,227,898</u>	<u>2,458,313</u>

**Cash flows from investing activities:**

Business acquisition (Note 27)	(989,500)	-
Payments for property, plant and equipment	(558,489)	(69,206)
Increase in deposits for property and equipment	-	(12,235)
<b>Net cash used in investing activities</b>	<u>(1,547,989)</u>	<u>(81,441)</u>

**Cash flows from financing activities:**

Increase (decrease) in bank indebtedness	476,628	(710,795)
Increase in long-term debt	-	165,000
Repayment of long-term debt	(739,642)	(2,403,711)
Issuance of share capital and warrants	485,484	500,000
Future issuance of shares and warrants	-	250,000
Repayment of finance leases	(17,274)	(13,105)
<b>Net cash generated by (used in) financing activities</b>	<u>205,196</u>	<u>(2,212,611)</u>

**Net (decrease) increase in cash** (114,895) 164,261

Cash, beginning of the year	243,808	82,031
Effects of exchange rate changes on the balance of cash held in foreign currencies	(1,919)	(2,484)
	<u>\$ 126,994</u>	<u>\$ 243,808</u>

**Cash, end of the year**

Non cash transactions (Note 21)

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



## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **1. General information**

Imaflex Inc. (“Imaflex” or “the Company”) is incorporated under the Canada Business Corporations Act. Its registered office and headquarters are located at 5710 Notre-Dame Street West, Montreal, Quebec, Canada. The principal activities of the Company consist in the manufacture and sale of products for the flexible packaging industry, including polyethylene film and bags, as well as the metallization of plastic film for the plasticulture and packaging industries. The common shares of the Company are listed for trading on the TSX Venture Exchange under the symbol “IFX”.

### **2. Significant accounting policies**

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

#### ***2.1 Statement of compliance***

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) issued by the International Accounting Standards Board (“IASB”) and in effect on December 31, 2012. The designation IFRS also includes the revised International Accounting Standards (“IAS”) and the interpretations of the International Financial Reporting Interpretations Committee (“IFRIC”).

#### ***2.2 Basis of preparation***

The consolidated financial statements have been prepared using the historical cost basis except for the revaluation of certain financial instruments at their fair value. Historical cost is generally based on the fair value of the consideration given in exchange for assets. The Company elected to present the statement of (loss) income and the statement of comprehensive (loss) income in the same statement and chose to present expenses by function, which is how information is presented for internal reporting purposes and is consistent with how management views and manages expenses in its operations. The statement of cash flows has been prepared using the indirect method. The principal accounting policies are set out below.

#### ***2.3 Basis of consolidation***

The consolidated financial statements include the accounts of the Company and its subsidiary Imaflex USA Inc. (“Imaflex USA”), a wholly owned entity. All intercompany transactions and balances are eliminated on consolidation.

#### ***2.4 Foreign currencies***

The functional currency is the currency of the primary economic environment in which an entity operates. The separate financial statements of the entities that are consolidated into the Company’s financial statements are prepared in their individual functional currency. For the purpose of these consolidated financial statements, the results and financial position are expressed in Canadian dollars (“CAD”), the functional currency of Imaflex Inc. and the presentation currency for the consolidated financial statements.

## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **2. Significant accounting policies (continued)**

#### **2.4 Foreign currencies (continued)**

The assets and liabilities of the Company's foreign subsidiary, Imaflex USA, whose functional currency is the US dollar ("USD"), are translated at the exchange rate in effect at the date of the consolidated statement of financial position. Revenues and expenses are translated at the exchange rates in effect on the dates on which such items are recognized into income during the period. Exchange gains or losses arising from the translation of Imaflex USA's financial statements are recognized as accumulated foreign currency translation within Reserves.

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency are recorded at the average exchange rate during the year. If exchange rates fluctuated significantly within these periods, exchange rates in effect on the date of the transactions are used. Monetary items denominated in foreign currencies are translated at the exchange rate prevailing at the end of the reporting period. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rate prevailing at the date when the fair value was determined.

#### **2.5 Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable and is recognized when all the following conditions are satisfied:

- Imaflex has transferred to the buyer the significant risks and rewards of ownership of the goods;
- Imaflex retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Company; and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably.

#### **2.6 Income Tax**

Income tax expense represents the sum of the tax currently payable and deferred tax. The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated statement of comprehensive (loss) income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized.

## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **2. Significant accounting policies (continued)**

#### **2.6 Income Tax (continued)**

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities, when they relate to income taxes levied by the same taxation authority and when the Company intends to settle its current tax assets and liabilities on a net basis.

Current and deferred taxes are recognized as an expense or income in profit or loss, except when they relate to items that are recognized outside profit or loss (whether in other comprehensive income or directly in equity), in which case the tax is also recognized outside profit or loss.

#### **2.7 Earnings per share**

Earnings per share are calculated by dividing net earnings available for common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated by taking into consideration potentially issuable shares that would have a dilutive effect on the earnings per share using the treasury stock method.

#### **2.8 Financial assets and financial liabilities**

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument and initially measured at fair value. Transaction costs directly attributable to the acquisition of financial assets or liabilities at fair value through profit or loss are recognized immediately in profit or loss. Transaction costs directly attributable to the acquisition or issue of financial assets and liabilities other than at fair value through profit or loss are added to or deducted from their fair value, as appropriate, on initial recognition.

Financial assets are classified into the following specified categories:

- fair value through profit or loss (FVTPL)
- available-for-sale (AFS)
- loans and receivables

The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Financial assets are classified as FVTPL when the financial asset is either held for trading or it is designated as FVTPL. The Company's cash and trade receivables are classified as loans and receivables. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment.



## Notes to the consolidated financial statements for the years ended December 31 2012 and 2011

### 2. Significant accounting policies (continued)

#### 2.8 Financial assets and financial liabilities (continued)

##### Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indications of impairment on a regular basis. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the asset have been affected.

Trade receivables that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period, as well as observable changes in economic conditions that correlate with default on receivables.

The carrying amount for most financial assets is reduced by the impairment loss directly. For trade receivables, the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement. Financial liabilities are classified into the following specified categories:

- at FVTPL
- other financial liabilities

Other financial liabilities, including long term debt, are initially measured at fair value, net of transaction costs, and then decreased by any principal payments made.

The Company derecognizes financial liabilities when, and only when, the Company's obligations are discharged, cancelled or they expire.

The issuance cost of debt is included as part of long term debt and is recorded at amortized cost, using the effective interest method. The issuance cost of equity is presented in the statement of changes in equity as a reduction of the proceeds received.

#### 2.9 Inventories

Inventories are stated at the lower of cost and net realizable value. Costs, including an appropriate portion of fixed and variable overhead expenses, are assigned to inventories by the method most appropriate to the particular class of inventory, being valued on a first-in-first-out basis. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion necessary to make the sale.

#### 2.10 Property, plant and equipment

Production equipment, office equipment and computer equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**2. Significant accounting policies (continued)**

**2.10 Property, plant and equipment (continued)**

Depreciation is recognized so as to write off the cost of assets less their residual values over their useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Asset	Basis	Period
Production equipment	Straight-line	20 years
Office equipment	Straight-line	5 years
Computer equipment	Straight-line	3 years

Leasehold improvements are amortized on a straight-line basis over the lesser of the terms of the leases or their useful lives.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

*Assets under finance lease*

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

*Impairment*

At each reporting date, or sooner if there is an indication that an asset may be impaired, the Company reviews the carrying amounts of its assets for each cash generating unit identified to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. When it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the assets for which the estimates of future cash flows have not been adjusted. If the recoverable amount of the assets is estimated to be less than their carrying amount, the carrying amount is reduced to the recoverable amount. An impairment loss is recognized immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the assets is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is recognized immediately in profit or loss.

**2.11 Intangible assets**

Intangible assets acquired in a business combination and recognised separately from goodwill are initially recognised at their fair value at the acquisition date, which is regarded as their cost. Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses.

## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **2. Significant accounting policies (continued)**

#### **2.11 Intangible assets (continued)**

An intangible asset is derecognised on disposal, or when no future economic benefits are expected from its use or disposal. Gains or losses arising from the derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognised in profit or loss when the asset is derecognised.

#### **2.12 Impairment of intangible assets other than goodwill**

At the end of each reporting period, Imaflex reviews the carrying amounts of its intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. When it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired. The asset's recoverable amount is the higher of its fair value less costs to sell and its value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

#### **2.13 Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognized in profit or loss in the period in which they are incurred.



## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **2. Significant accounting policies (continued)**

#### **2.14 Business combinations**

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Company, liabilities incurred by the Company to the former owners of the acquiree and the equity interests issued by the Company in exchange for control of the acquiree. Acquisition-related costs are generally recognized in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognized at their fair value.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and, if applicable, the fair value of the acquirer's previously held interest in the acquiree, the excess is recognised immediately in profit or loss as a bargain purchase gain.

When the consideration transferred by the Company in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with corresponding adjustments against goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the 'measurement period', which cannot exceed one year from the acquisition date, about facts and circumstances that existed at the acquisition date.

The subsequent accounting for changes in the fair value of the contingent consideration that do not qualify as measurement period adjustments depends on how the contingent consideration is classified. Contingent consideration that is classified as equity is not remeasured at subsequent reporting dates and its subsequent settlement is accounted for within equity. Contingent consideration that is classified as an asset or a liability is remeasured at subsequent reporting dates.

#### **2.15 Goodwill**

Goodwill arising on an acquisition of a business is carried at cost as established at the date of acquisition of the business less accumulated impairment losses, if any.

For the purposes of impairment testing, goodwill is allocated to each of the Company's cash-generating units or groups of cash-generating units that is expected to benefit from the synergies of the combination.

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata based on the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognized directly in profit or loss in the consolidated statement of comprehensive income. An impairment loss recognized for goodwill is not reversed in subsequent periods.

## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **2. Significant accounting policies (continued)**

#### ***2.16 Derivative financial instrument***

The interest rate swap is a derivative financial instrument which was initially recognized at fair value at the date the derivative contract was entered into and is subsequently remeasured to fair value at the end of each reporting period. The resulting gain or loss is recognized in profit or loss immediately.

The derivative financial instrument is recognized as a financial asset when it has a positive fair value and as a financial liability when it has a negative fair value.

#### ***2.17 Leasing***

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognized as assets of the Company at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the consolidated statement of financial position as a finance lease obligation.

Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance expenses are recognized immediately in profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the Company's general policy on borrowing costs. Contingent rentals are recognized as expenses in the periods in which they are incurred.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred.

#### ***2.18 Provisions***

Provisions are recognized when the Company has a present obligation, legal or constructive, as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation.

#### ***2.19 Share-based compensation***

Equity-settled share-based compensation to employees is measured at the fair value of the financial instruments at the grant date, estimated using the Black-Scholes option pricing model.

The fair value determined at the grant date of the equity-settled share-based compensation is expensed over the vesting period with a corresponding increase in contributed surplus.

Imaflex has not issued any share-based compensation to non-employees nor did it issue any share-based compensation to be settled in cash.

## Notes to the consolidated financial statements for the years ended December 31 2012 and 2011

### 3. Future accounting changes

The following new and revised IFRSs have been issued but are not yet effective and are not yet applied by the Company.

#### *Financial instruments*

IFRS 9, issued in November 2009, introduced new requirements for the classification and measurement of financial assets. IFRS 9 was amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition.

IFRS 9, effective as of January 1, 2015, requires that all recognised financial assets that are within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* be subsequently measured at amortised cost or fair value. Specifically, debt investments whose objective is to collect the contractual cash flows that are solely payments of principal and interest on the principal outstanding are to be measured at amortised cost at the end of the reporting periods. All other debt investments and equity investments are measured at their fair value at the end of the reporting period. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment that is not held for trading in other comprehensive income, with only dividend income generally recognised in profit or loss.

With regard to the measurement of financial liabilities designated as fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability attributable to changes in that liability's credit risk be presented in other comprehensive income, unless such presentation would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Previously, under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss was presented in profit or loss.

The application of IFRS 9 may have an impact on the Company's financial statements however the Company has not yet assessed its extent.

#### *Consolidation*

In May 2011, a package of five Standards on consolidation, joint arrangements, associates and disclosures was issued, including IFRS 10, IFRS 11, IFRS 12, IAS 27, as revised in 2011, and IAS 28, as revised in 2011, effective as of January 1, 2013.

IFRS 10 replaces the parts of IAS 27 *Consolidated and Separate Financial Statements* that deal with consolidated financial statements. SIC-12 *Consolidation – Special Purpose Entities* will be withdrawn upon the effective date of IFRS 10. Under IFRS 10, control is the only basis for consolidation. Under IFRS 10, the definition of control contains three elements: power over an investee, exposure, or rights, to variable returns from its involvement with the investee, and the ability to use its power over the investee to affect the amount of the investor's returns.

IFRS 11 will replace IAS 31 *Interests in Joint Ventures*. IFRS 11 deals with how a joint arrangement over which two or more parties have joint control should be classified. SIC-13 *Jointly Controlled Entities – Non-monetary Contributions by Venturers* will be withdrawn upon the effective date of IFRS 11. Under IFRS 11, joint arrangements are classified as joint operations or joint ventures, depending on the rights and obligations of the parties to the arrangements as opposed to the three types of joint arrangements existing under IAS 31. In addition, joint ventures under IFRS 11 are required to be accounted for using the equity method of accounting.



## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **3. Future accounting changes (continued)**

#### ***Consolidation (continued)***

IFRS 12 is a disclosure standard and is applicable to entities that have interests in subsidiaries, joint arrangements, associates or unconsolidated structured entities. In general, the disclosure requirements in IFRS 12 are more extensive than those in the current standards.

In June 2012, the amendments to IFRS 10, IFRS 11 and IFRS 12 were issued to clarify certain transitional guidance on the application of these IFRSs for the first time. These five standards together with the amendments regarding the transition guidance are effective for annual periods beginning on or after January 1, 2013, with earlier application permitted provided all of these standards are applied at the same time.

Management does not expect the application of IFRS 10, IFRS 11 and IFRS 12 to have a material impact on the presentation of its financial statements.

#### ***Fair value measurement***

IFRS 13 establishes a single source of guidance for fair value measurements and disclosures about fair value measurements. The Standard defines fair value, establishes a framework for measuring fair value and requires disclosures about fair value measurements. The scope of IFRS 13 is broad and applies to both financial instrument items and non-financial instrument items for which other IFRSs require or permit fair value measurements and disclosures about fair value measurements, except in specified circumstances. In general, the disclosure requirements in IFRS 13 are more extensive than those required in the current standards.

IFRS 13 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted.

The Company does not expect the application of IFRS 13 to have a material impact on amounts reported in its financial statements although it may require additional disclosure in the presentation of its financial statements.

#### ***Offsetting Financial Assets and Financial Liabilities and the related disclosures***

New disclosure requirements that are intended to help investors and other users to better assess the effects or potential effects of offsetting arrangements on a company's statement of financial position have been issued on December 16, 2011. The new requirements are set out in Disclosures-Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7). The IFRS 7 amendments are effective for annual reporting periods beginning on or after January 1, 2013.

The Company does not expect the application of IFRS 7 to have a material impact on amounts reported in its financial statements although it may require additional disclosure in the presentation of its financial statements.

## **Notes to the consolidated financial statements for the years ended December 31 2012 and 2011**

### **4. Critical accounting judgements and key sources of estimation uncertainty**

The preparation of these financial statements in conformity with IFRS and the application of the Company's accounting policies described in note 2, required management to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

#### ***4.1 Critical judgements in applying accounting policies***

The following are the critical judgements, apart from those involving estimations, that management has made in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements.

##### ***Cash generating units***

Management has identified only one cash generating unit ("CGU") for Imaflex. Revenue generated by the Company's various product lines and facilities are generated through a single sales force whose ability to cross sell products influences the level of sale for each product line.

#### ***4.2 Key sources of estimation uncertainty***

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

##### ***Allowance for doubtful accounts***

The Company analyzes its trade receivables on an account by account basis and on a portfolio basis. Any impairment recognized on these assets is based on historical experience and management's best estimate of the recoverability of the account receivable.

##### ***Inventory***

The Company analyzes its inventory in order to assess the carrying amount of inventory. This assessment is based on management's knowledge of the market and experience regarding obsolescence and valuation of inventory.

##### ***Useful lives of property, plant and equipment***

The Company reviews the estimated useful lives of property, plant and equipment at the end of each annual reporting period in order to ensure that the amortization method used is appropriate.

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

The Company performs impairment tests on its long-lived assets by comparing the carrying amount of the assets to their recoverable amount, which is calculated as the higher of the asset's fair value less costs to sell and its value in use. Value in use is calculated based on a discounted cash flow analysis, which requires the use of estimates of future cash flow and discount rates. The Company also uses judgement to determine whether it identifies any triggering event that may indicate that the long-lived assets have been impaired.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**4. Critical accounting judgements and key sources of estimation uncertainty (continued)**

**4.2 Key sources of estimation uncertainty (continued)**

***Income taxes***

Management uses judgement and estimates in determining the appropriate rates and amounts in recording deferred income taxes, giving consideration to timing and probability of realization. Actual taxes could significantly vary from these estimates as a result of a variety of factors including future events, changes in income tax laws or the outcome of reviews by tax authorities and related appeals. The resolution of these uncertainties and the associated final taxes payable may result in adjustments to the Company's deferred and current tax assets and liabilities.

***Warrants***

The Company issues from time to time equity instruments, comprised of common shares and warrants. Estimates based on market inputs are required in determining the attribution of gross proceeds received between the different instruments issued.

***Business combinations***

In order to complete the purchase price allocation for the business combination concluded during the year, management used judgement and used estimates in order to determine the value of the customer relationships acquired through the business combination as well as the goodwill recorded as part of the business combination.

**5. Segment information**

The Company operates in one reportable segment, comprising the development, manufacture and sale of flexible packaging material in the form of film or bags, for various uses.

**5.1 Revenues by geographical end market**

The Company's revenues by geographical end market are as follows:

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Canada	<b>\$ 24,179,722</b>	\$ 27,453,846
United States	<b>22,803,435</b>	19,098,568
Other	<b>285,784</b>	406,367
Total	<b>\$ 47,268,941</b>	\$ 46,958,781

**5.2 Property, plant and equipment, and intangible assets net, per geographic location**

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Canada	<b>\$ 6,214,416</b>	\$ 6,816,452
United States	<b>9,920,419</b>	7,786,001
Total	<b>\$ 16,134,835</b>	\$ 14,602,453



**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**6. Additional information on the consolidated statements of comprehensive (loss) income**

The Company's consolidated statement of comprehensive (loss) income includes depreciation of production equipment of \$ 1,039,086 for the year ended December 31, 2012 (\$ 991,819 in 2011) classified in cost of sales. Depreciation of other property, plant and equipment and amortization of intangible assets amounting to \$ 222,397 for the year ended December 31, 2012 (\$ 317,870 in 2011) is included in administrative expenses.

The Company's consolidated statement of comprehensive (loss) income includes salaries paid to its employees of \$ 5,643,441 for the year ended December 31, 2012 (\$ 4,480,762 in 2011) classified in cost of sales. Administrative expenses include salaries paid to employees of \$ 986,030 for the year ended December 31, 2012 (\$ 848,792 in 2011) and selling expenses include salaries paid to employees of \$360,178 for the year ended December 31, 2012 (\$ 431,757 in 2011).

**7. Employee benefits**

The Company contributes to state-run pension plans, employment insurance, group insurance and social security for its employees. The costs incurred for the employee benefits noted above amounted to \$1,594,401 during the year ended December 31, 2012 (\$1,291,115 in 2011). These payments are expensed as incurred and the Company does not recognize any gains or losses subsequent to the payment of these benefits. These transactions do not result in any asset or liability on the consolidated statement of financial position.

The Company also offers a defined contribution employee benefit plan to its employees located in North Carolina. For the year ended December 31, 2012, the Company contributed \$ 11,851 to this plan (nil in 2011).

**8. Finance costs**

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Interest on bank indebtedness and long term debt	<b>\$ 505,559</b>	\$ 551,775
Interest on obligations under finance leases	<b>3,620</b>	4,100
	<b>\$ 509,179</b>	<b>\$ 555,875</b>

**9. Other gains and losses**

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Foreign exchange loss (gain)	<b>\$ 231,209</b>	\$ (94,537)
Change in fair value of derivative financial instrument	<b>(38,441)</b>	(62,352)
	<b>\$ 192,768</b>	<b>\$ (156,889)</b>

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**10. Income taxes**

**10.1 Income tax recognized in profit or loss**

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Tax expense comprises:		
Current tax expense in respect of the current year	<b>\$ 227,704</b>	\$ 136,617
Adjustments recognized in the current year relating to prior years	<b>61,057</b>	(45,179)
Deferred tax expense relating to the origination and reversal of temporary differences	<b>9,697</b>	170,904
	<b>298,458</b>	262,342
Effect of changes in tax rates and laws	-	1,485
Total income tax expense	<b>\$ 298,458</b>	\$ 263,827

**10.2 Reconciliation of the income tax rate**

The income tax expense for the year is reconciled as follows:

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
(Loss) profit before taxes	<b>\$ (269,753)</b>	\$ 337,478
Income tax (recovery) expense calculated at 26.9% (28.4% - 2011)	<b>(72,564)</b>	95,844
Permanent differences	<b>53,409</b>	(20,360)
Effect of unrecognized benefit of Imaflex USA's losses	<b>374,570</b>	251,800
Adjustments to deferred income tax	-	52,261
Effect of different tax rates of subsidiaries operating in other jurisdictions	<b>(102,247)</b>	(60,286)
Other	<b>45,290</b>	(55,432)
Income tax expense recognized in profit or loss	<b>\$ 298,458</b>	\$ 263,827

The tax rate used for the 2012 reconciliation above is the corporate tax rate of 26.9% (28.4% in 2011) payable by corporate entities in Quebec, Canada on taxable profits under tax law in those jurisdictions. The combined applicable statutory tax rate has decreased by 1.50% resulting from the reduction in the Canadian federal statutory tax rate.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**10. Income taxes (continued)**

**10.3 Deferred tax balances**

	Opening balance	Recognized in profit or loss	Adjustment to prior year balance	Closing balance
<b>2012</b>				
<i>Assets</i>				
Non-capital losses	\$ 1,057,664	\$ 1,381,169	\$ -	\$ 2,438,833
Finance leases	11,007	(756)	-	10,251
Financing costs	-	565	-	565
Intangible assets	7,157	(501)	-	6,656
	<u>1,075,828</u>	<u>1,380,477</u>	<u>-</u>	<u>2,456,305</u>
<i>Liabilities</i>				
Property, plant & equipment	(2,319,251)	(1,394,833)	(4,892)	(3,718,976)
Investment tax credits	(15,970)	9,551	-	(6,419)
	<u>(2,335,221)</u>	<u>(1,385,282)</u>	<u>(4,892)</u>	<u>(3,725,395)</u>
Deferred tax liability	<u>\$ (1,259,393)</u>	<u>\$ (4,805)</u>	<u>\$ (4,892)</u>	<u>\$ (1,269,090)</u>
	Opening balance	Recognized in profit or loss	Adjustment to prior year balance	Closing balance
<b>2011</b>				
<i>Assets</i>				
Non-capital losses	\$ 1,571,528	\$ (513,864)	\$ -	\$ 1,057,664
Finance leases	13,140	(2,128)	(5)	11,007
Provisions	28,127	(26,642)	(1,485)	-
Other assets	7,695	(538)	-	7,157
	<u>1,620,490</u>	<u>(543,172)</u>	<u>(1,490)</u>	<u>1,075,828</u>
<i>Liabilities</i>				
Property, plant & equipment	(2,707,494)	439,012	(50,769)	(2,319,251)
Investment tax credits	-	(15,970)	-	(15,970)
	<u>(2,707,494)</u>	<u>423,042</u>	<u>(50,769)</u>	<u>(2,335,221)</u>
Deferred tax liability	<u>\$ (1,087,004)</u>	<u>\$ (120,130)</u>	<u>\$ (52,259)</u>	<u>\$ (1,259,393)</u>



**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**10. Income taxes (continued)**

**10.4 Unrecognized deferred tax assets**

The Company's subsidiary, Imaflex USA, has non-capital losses available to carry forward to reduce future taxable income of \$13,470,882 in 2012 and \$11,818,253 in 2011 for part of which a deferred tax asset has not been recognized (\$2,565,541 in 2012 and \$3,355,272 in 2011) that expire as follows:

<b>Expiring in</b>	<b>December 31, 2012</b>	<b>December 31, 2011</b>
2025	\$ 86,256	\$ 88,172
2026	1,445,678	1,477,792
2027	993,743	1,015,817
2028	2,145,791	2,193,456
2029	2,324,452	2,376,085
2030	3,301,393	3,374,727
2031	1,456,112	1,292,204
2032	1,717,457	-
	<u>\$13,470,882</u>	<u>\$11,818,253</u>

Additionally, the Company has not recognized a deferred tax asset on its Canadian capital losses in the amount of \$ 174,677 which can be used indefinitely.

**11. Earnings per share**

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
(Loss) profit for basic and diluted (loss) earnings per share	<u>\$ (568,211)</u>	<u>\$ 73,651</u>
Weighted average number of common shares outstanding	42,437,341	40,103,426
Dilutive effect of share-based compensation	-	24,269
Diluted weighted average common shares outstanding	<u>42,437,341</u>	<u>40,127,695</u>
Basic and diluted (loss) earnings per common share	<b>\$ (0.013)</b>	<b>\$ 0.002</b>

As at December 31, 2012 and 2011, the Company had 100,000 share options outstanding at a strike price of \$ 0.125. Because the Company incurred a net loss for the year ended December 31, 2012, they were not included in the calculation of the diluted earnings per share.

As at December 31, 2012, there were 3,251,274 warrants entitling the holder to purchase common shares of the Company at a strike price of \$ 0.45 and a maximum of 1,000,000 shares may be issued following the business combination given the seller may elect to settle the balance of sale in shares, at the implied strike price is USD\$ 1 per share. These instruments were not included as dilutive because the exercise price was above the share trading price.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**12. Trade and other receivables**

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Trade receivables	<b>\$ 8,933,296</b>	\$ 9,599,496
Allowance for doubtful accounts	<b>(570,400)</b>	(527,876)
	<b>8,362,896</b>	9,071,620
Other	<b>382,417</b>	280,004
	<b>\$ 8,745,313</b>	\$ 9,351,624

Movement in the allowance for doubtful accounts

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Balance, beginning of year	<b>\$ (527,876)</b>	\$ (495,651)
Release of allowance for doubtful accounts	<b>397,741</b>	-
Impairment losses and adjustments recognized on trade receivables	<b>(473,083)</b>	(40,290)
Amounts written off during the year as uncollectible	<b>30,935</b>	10,623
Foreign exchange variance	<b>1,883</b>	(2,558)
Balance, end of year	<b>\$ (570,400)</b>	\$ (527,876)

The Company's maximum exposure to credit risk is limited to the carrying amount of the receivables in the consolidated financial statements as the Company does not make any guarantees above the carrying value. When a counterparty is bankrupt, insolvent or placed under receivership, the allowance for doubtful accounts attributed to the customer is written-off against the account.

Credit risk management

In its normal credit risk management process, the Company uses an external credit service to assess the potential customer's credit quality and uses this information to define the allowed credit limits by customer. The Company uses Export Development Canada to insure trade receivables. As at December 31 2012, \$ 4,009,259 (\$ 4,065,338 as at December 31, 2011) of the total trade receivables are insured.

Trade receivables past due but not impaired

Trade receivables disclosed above include amounts that are past due at the end of the reporting period but not impaired, because the amounts are still considered recoverable based on the Company's analysis of reimbursements. In situations where the Company believes there may be increased credit risk, netting agreements are signed in order to be able to settle any payables to the same customer on a net basis. At the end of the reporting period, there were \$ 1,951,000 of past due receivables that were not impaired (\$ 2,678,238 in 2011). Of that amount, \$ 832,016 was over 90 days (\$ 1,456,298 as at December 31, 2011).

Aging of accounts receivable

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Current	<b>\$ 3,501,492</b>	\$ 3,726,576
31 days to 60 days	<b>3,161,599</b>	2,729,332
61 days to 90 days	<b>1,118,984</b>	1,222,217
Over 90 days	<b>963,238</b>	1,673,499
Total	<b>\$ 8,745,313</b>	\$ 9,351,624

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**13. Inventories**

	December 31, 2012	December 31, 2011
Raw materials and supplies	\$ 3,997,193	\$ 4,337,113
Finished goods	2,771,312	2,554,692
Work in process	107,469	-
Total	<u>\$ 6,875,974</u>	<u>\$ 6,891,805</u>

The cost of inventories recognized as an expense during the year was \$27,286,421 (\$28,400,577 in 2011). There were no write-downs of inventory recognized in the fiscal year ended on December 31, 2012 (write-downs of inventory represented an expense of \$64,493 of cost of goods sold in 2011).

**14. Property, plant and equipment**

	Production equipment	Leasehold improvements	Office equipment	Computer equipment	Equipment under finance lease	Total
<i>At cost,</i>						
January 1, 2011	\$ 36,070,537	\$1,304,142	\$ 40,987	\$ 384,733	\$ 70,500	\$ 37,870,899
Additions	65,541	15,900	-	-	-	81,441
Foreign exchange	242,139	5,351	313	260	-	248,063
December 31, 2011	36,378,217	1,325,393	41,300	384,993	70,500	38,200,403
Additions	849,775	308,714	-	-	37,633	1,196,122
Business acquisition	1,088,450	-	-	-	-	1,088,450
Foreign exchange	(231,301)	(8,698)	(308)	(257)	(264)	(240,828)
December 31, 2012	<u>\$ 38,085,141</u>	<u>\$1,625,409</u>	<u>\$ 40,992</u>	<u>\$384,736</u>	<u>\$ 107,869</u>	<u>\$ 40,244,147</u>

*Accumulated depreciation*

January 1, 2011	\$(20,903,638)	\$ (1,062,073)	\$ (18,398)	\$(193,464)	\$ (30,550)	\$(22,208,123)
Depreciation expense	(991,819)	(166,634)	(9,036)	(128,100)	(14,100)	(1,309,689)
Foreign exchange	(73,665)	(5,833)	(313)	(327)	-	(80,138)
December 31, 2011	(21,969,122)	(1,234,540)	(27,747)	(321,891)	(44,650)	(23,597,950)
Depreciation expense	(1,039,086)	(100,424)	(9,036)	(63,007)	(18,839)	(1,230,392)
Foreign exchange	72,406	5,224	308	162	10	78,110
December 31, 2012	<u>\$(22,935,802)</u>	<u>\$(1,329,740)</u>	<u>\$ (36,475)</u>	<u>\$(384,736)</u>	<u>\$ (63,479)</u>	<u>\$(24,750,232)</u>

*Net book value, as at*

December 31, 2011	14,409,095	90,853	13,553	63,102	25,850	14,602,453
<b>December 31, 2012</b>	<b>\$ 15,149,339</b>	<b>\$ 295,669</b>	<b>\$ 4,517</b>	<b>\$ -</b>	<b>\$ 44,390</b>	<b>\$ 15,493,915</b>

The Company's production equipment with a carrying amount of approximately \$ 7,000,000 (December 31, 2011: approximately \$ 12,043,929) is pledged as collateral for the Company's operating lines of credit and long-term debt.



**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**15. Intangible assets**

	<u>Year ended</u>	
	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Balance, beginning of year	\$ -	\$ -
Additions:		
Goodwill (Note 27)	371,513	-
Customer relationships (Note 27)	296,850	-
Foreign exchange variance	3,648	-
Amortization of customer relationships	(31,091)	-
Balance, end of year	<u>\$ 640,920</u>	<u>\$ -</u>

**16. Trade and other payables**

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Trade payables	\$ 4,820,870	\$ 4,577,653
Other payables and accrued liabilities	1,312,638	1,172,938
	<u>\$ 6,133,508</u>	<u>\$ 5,750,591</u>

**17. Credit facilities**

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Bank indebtedness (a)	\$ 6,103,876	\$ 5,627,248
Bank loans (b)	2,370,604	3,132,577
Subordinated debt (c)	165,000	165,000
Total long-term debt	<u>2,535,604</u>	<u>3,297,577</u>
Finance lease liabilities (Note 18)	61,639	41,618
Balance of sale on business acquisition (Note 27) (d)	937,906	-
Total borrowings	<u>9,639,025</u>	<u>8,966,443</u>
Current		
Bank indebtedness	6,103,876	5,627,248
Bank loans and subordinated debt	1,101,425	3,132,577
Finance leases	36,376	41,618
	<u>7,241,677</u>	<u>8,801,443</u>
Non-current		
Long-term debt	2,372,085	165,000
Finance leases	25,263	-
	<u>2,397,348</u>	<u>165,000</u>
Total credit facilities	<u>\$ 9,639,025</u>	<u>\$ 8,966,443</u>

Interest on long-term debt amounted to \$ 191,870 for the year ended December 31, 2012 (\$ 230,537 in 2011).

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**17. Credit facilities (continued)**

(a) The Company has an operating line of credit with its bankers to a maximum of \$8,500,000, bearing interest at prime plus 2.0% (5.0% effective interest rate at December 31, 2012). The line of credit is secured by trade receivables and inventories. The line of credit may be reviewed periodically by the bank and is repayable on demand. The operating line of credit is subject to working capital, debt to equity, fixed coverage and interest bearing debt to EBITDA covenants (as defined in the lending agreement). As at December 31, 2012, the Company had drawn \$ 6,103,876 (\$ 5,627,248 as at December 31, 2011) on its line of credit and was in compliance with the bank covenants.

(b) The Company's bank loans are comprised of the following :

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Loan (December 31 2012 US\$ 460,714, December 31 2011 US\$ 1,075,000), bearing interest at the 30-day LIBOR rate (0.21% as at December 31, 2012), reset monthly, plus 1.24%, repayable in monthly principal installments of \$ 50,929 (US\$ 51,190) up to September 2013 and secured by production equipment. (i)	<b>\$ 458,364</b>	\$ 1,093,275
Loan, bearing interest at the lender's base rate (5.00% as at December 31, 2012) plus 0.25%, repayable in monthly principal installments of \$43,460 to September 2016, secured by production equipment.	<b>1,912,240</b>	1,955,700
Loans, bearing interest at rates varying between prime plus 1.50% and the 30-day LIBOR rate plus 2.00%, retired during the year.	-	83,602
	<b>2,370,604</b>	3,132,577
Current portion of bank loans (ii)	<b>(936,425)</b>	(3,132,577)
Long term portion of bank loans	<b>\$ 1,434,179</b>	\$ -

i. On September 28, 2006, the Company borrowed from Wachovia Corporation US\$ 4,300,000 at a variable interest rate for seven years by entering into a long-term debt facility entered into to fund its capital expenditures. The Company then entered into an interest rate swap for the same amount and maturity. Under the terms of this interest rate swap, the Company receives, on a monthly basis, a variable interest rate and pays a fixed interest rate of 6.54%. The Company uses this derivative financial instrument to manage the risk from fluctuations in interest rates. The intent is to fix the interest cost on this long-term debt.

ii. As at December 31, 2011, the Company was in breach of the interest bearing debt to EBITDA covenant relating to bank indebtedness of \$ 5,627,248 and term debt totalling \$ 50,000. All of the Company's credit agreements for term-debt and finance leases, with the exception of subordinated debt, include cross default provisions, giving the right to demand repayment of the loan prior to the scheduled maturity. Accordingly, the term debt, except subordinated debt, was presented with the current portion of long-term debt for the year ended December 31, 2011.

The aggregate scheduled repayment of bank loans is as follows:

Not later than one year	\$ 936,425
Later than one year and not later than five years	1,434,179
Later than five years	-
	<b>\$ 2,370,604</b>

## Notes to the consolidated financial statements for the years ended December 31 2012 and 2011

### 17. Credit facilities (continued)

- c) On December 5, 2011, the Company received a subordinated loan of \$165,000 from a significant shareholder and officer of the Company pursuant to the Company's agreement with a creditor. This loan does not bear interest and matures on June 30, 2013, and may be prepaid by the Company with no penalties subject to certain conditions.
- d) During the year, the Company completed a business acquisition and assumed a non-interest bearing balance of sale which was recorded at the discounted value of \$894,096 (USD\$904,584), payable on the two-year anniversary date of the acquisition. The initially recorded discounted value is recorded at amortized cost using the effective interest method with an effective rate of 5.2%.

### 18. Obligations under finance leases

The Company has entered into certain finance lease agreements. Finance lease payments are as follows:

Not later than one year	\$ 39,298
Later than one year and not later than five years	26,942
Later than five years	-
Total minimum lease payments	66,240
Less amount representing interest at approximately 6.4%	(4,601)
Present value of minimum lease payments	61,639
Less current portion	(36,376)
	\$ 25,263

The fair value of the finance lease liabilities is approximately equal to their carrying amount.

### 19. Share capital

The Company's outstanding share capital consists of an unlimited number of common shares, voting, participating, without par value. During the 2012 fiscal year, the Company's shareholders voted in favour of cancelling the Company's Class B shares without diminishing the existing rights and privileges associated with the Class A shares of the Company. At the time of the cancellation, there were no Class B shares outstanding.

At December 31 2012, there were 42,601,276 common shares outstanding (40,665,791 common shares at December 31, 2011).

During the year, the Company issued, through a non-brokered private placement, 1,935,485 Units for proceeds of \$ 735,484, of which \$ 250,000 had been received in advance in contemplation of this transaction on December 30, 2011. Each Unit is comprised of one common share and one common share purchase warrant entitling its holder to acquire one additional common share at a price of \$ 0.45 per share until February 1, 2015.

Each share issued was attributed a value of \$ 0.246 and each warrant issued was attributed a value of \$ 0.134. Of the \$ 250,000 received during the 2011 fiscal year and included in Other reserves as at December 31, 2011, \$ 161,842 was attributed to the shares issued and \$ 88,158 was attributed to the warrants issued. Of the \$ 485,484 received during the course of the first quarter of 2012, \$ 314,287 was attributed to the shares issued and \$ 171,197 was attributed to the warrants issued.



## Notes to the consolidated financial statements for the years ended December 31 2012 and 2011

### 19. Share capital (continued)

During 2011, the Company issued, through a non-brokered private placement, 1,315,789 Units to a significant shareholder and officer of the Company for cash consideration of \$ 500,000. Each unit consists of one common share and one common share purchase warrant, entitling the holder to acquire one additional common share of Imaflex at a price of \$ 0.45 per share until June 6, 2014.

Each share issued was attributed a value of \$ 0.20, for a total consideration for shares of \$ 263,158. Each warrant issued was attributed a value of \$ 0.18, for a total consideration for warrants of \$ 236,842.

### 20. Share-based compensation

Pursuant to the Stock Option Plan (the "Plan") of the Company, 3,735,000 of the common shares are reserved for options. The Plan provides that the term of the options shall be fixed by directors. Officers and employees of the Company or its subsidiary are eligible to receive options. Options are granted at an exercise price of not less than the fair value of the Company's shares on the date the options are granted. Options may be exercisable for a period no longer than five (5) years and the exercise price must be paid in full upon exercise of the option.

The opening balance as at January 1, 2011 relates to stock options issued prior to 2009, which expired unexercised. On May 27 2011, the Company issued 100,000 options to an officer of the Company, each option entitling the holder to acquire, from the grant date, one common share of Imaflex at \$0.125 for a period of 5 years. These options, none of which were exercised, are the only options outstanding as at December 31, 2012.

At the grant date, the fair value of the options was \$ 10,399 (\$ 0.10 per option) and was recognized as an expense with a corresponding increase to the share-based compensation reserve. Options were valued using the Black-Scholes option pricing model using assumptions based on management's best estimate of when the options are expected to be exercised. Expected volatility is based on the historic volatility of Imaflex's shares.

#### Fair value assumptions

#### May 27, 2011 issue

Expected life of options	2.5 years
Expected share price volatility	172.86%
Dividend yield	0%
Risk free rate	1.67%
Exercise price	\$0.125
Share price on grant date	\$0.125

The Company did not issue any share-based compensation for the fiscal year ended on December 31, 2012.

### 21. Non-cash transactions

During the year ended December 31, 2012, the Company financed the acquisition of equipment through the issuance of a credit note of \$600,000, decreasing its trade receivables.

The Company also financed the business acquisition completed during the year by assuming debt towards the sellers for \$894,096.

During the year, the Company acquired production and office equipment through capital leases. The amount of capital leases entered into during the year totaled \$37,633.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**22. Financial instruments**

**22.1 Categories of financial instruments**

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
<b>Financial assets</b>		
Cash	\$ 126,994	\$ 243,808
Trade and other receivables	8,745,313	9,351,624
<b>Financial liabilities</b>		
Derivative financial instrument	9,745	49,068
<b>Other financial liabilities</b>		
Bank Indebtedness	6,103,876	5,627,248
Long term debt and finance leases	3,535,149	3,339,195
Trade and other payables	\$ 6,133,508	\$ 5,750,591

**22.2 Fair value of financial instruments**

Fair value estimates are made as of the date of the consolidated statement of financial position, using available information about the financial instrument. These estimates are subjective in nature and often cannot be determined with precision. The Company has determined that the fair value of its current financial assets and liabilities approximates their respective carrying amounts as at the date of the consolidated statement of financial position because of the short-term maturity of those instruments. The fair value of the bank debts, which bear interest at floating rates, approximates their carrying amounts due to the nature of the financial liability and the Company's ability to contract debt with similar rates and conditions. The balance of sale on the business acquisition was initially recorded at a discounted value and is increased by applying an interest rate which reflects the current time-value of money and risks associated with a counterparty like Imaflex. It's carrying value therefore approximates its fair market value. Finance leases, given the collateral given as guarantee on the agreement, are also deemed to bear interest at rates which resemble rates the Company could obtain on the market in current conditions.

**23. Operating lease arrangements**

**23.1 Leasing arrangements**

The Company leases its premises for manufacturing locations from related parties under operating leases. Rent is paid monthly on a triple net basis. There are no restrictions imposed on the Company under these leasing arrangements. There is no contingent lease under those leasing agreements and no sublease payments received by the Company. The leases expire at various dates to August 2020, and include renewal provisions.

**23.2 Payments recognized as an expense**

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Lease payments for premises	\$ 850,967	\$ 724,129
Vehicles	21,105	-
Office equipment	6,702	6,688

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**23. Operating lease arrangements (continued)**

**23.3 Non-cancellable operating lease commitments**

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Not later than 1 year	<b>\$ 844,530</b>	\$ 741,186
Later than 1 year and not later than 5 years	<b>1,920,125</b>	2,120,373
Later than 5 years	<b>668,287</b>	814,973
	<b><u>\$ 3,432,942</u></b>	<u>\$3,676,532</u>

**24. Risk management**

**24.1 Capital management**

The Company's objective in managing capital is to ensure sufficient liquidity to pursue its growth while at the same time taking a conservative approach towards financial leverage and financial risk.

The Company's capital is composed of net debt and shareholders' equity. Net debt consists of interest-bearing debt less cash. The Company's primary uses of capital are to finance increases in non-cash working capital and capital expenditures for capacity expansion and integration.

The Company's primary measure to monitor financial leverage is Debt to Earnings before Interest, Taxes, Depreciation and Amortization ("EBITDA").

Credit facility arrangements require that the Company meet certain financial ratios at fixed points in time. The financial ratios are, as at December 31, 2012:

- Working capital ratio, defined as current assets divided by current liabilities greater than or equal to 1.10:1.00;
- Debt to equity ratio, defined as total debt excluding deferred taxes divided by equity of less than or equal to 2.50:1.00;
- Fixed charge coverage ratio, including all capital and interest payments on borrowings due, as defined, greater than or equal to 1.00:1.00; and
- Interest bearing debt divided by EBITDA ratio less than or equal to 6.00:1.00.

As at December 31, 2012, the Company was in compliance with all these financial ratios.

**24.2 Foreign currency risk management**

The Company's Canadian operations face foreign currency risk as a result of a significant portion of the costs of raw material for these sales being in USD. The Company's sales in U.S. dollars act as a hedge against this risk, mitigating the risk.

The Company also faces foreign currency risk through its foreign subsidiary Imaflex USA, whose functional currency is the USD. Imaflex does not specifically hedge this foreign currency risk.

The Company also has a portion of its long term debt in USD. The majority of the cash flows generated by the assets financed by these borrowings in USD are in USD.



**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**24. Risk management (continued)**

**24.2 Foreign currency risk management (continued)**

The Company's management has decided not to hedge its foreign currency risks. The decision of whether or not to hedge its foreign currency risk is determined by the Company's net exposure, expected movements in the main currencies in which the Company transacts, important changes in the mix of currencies in which the Company transacts, the expected net cash flow in foreign currencies as well as availability of derivative financial instruments or additional debt in foreign currency at reasonable terms.

The following is the Company's financial assets and liabilities denominated in U.S. dollars in its statement of financial position:

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Cash	<b>\$ 103,181</b>	\$ 53,890
Trade receivables	<b>4,273,373</b>	4,043,946
Trade payables	<b>(4,110,600)</b>	(3,491,025)
Derivative financial instrument	<b>(9,745)</b>	(49,068)
Long term debt	<b>(1,419,921)</b>	(1,126,877)
Gross financial position exposure	<b><u>\$ (1,163,712)</u></b>	<u>\$(569,134)</u>

A 5% appreciation of the Canadian dollar against the USD would impact its financial position by \$58,186 as at December 31, 2012 (December 31, 2011 - \$28,456). Conversely a 5% depreciation of the Canadian dollar against the U.S. dollar would have the opposite effect. Management estimates that every \$ 0.01 appreciation of the U.S. dollar against the Canadian dollar would have a negative impact on the Company's result of approximately \$60,000. Every \$ 0.01 depreciation of the U.S. dollar against the Canadian dollar would have the opposite effect.

**24.3 Interest rate risk management**

The Company's exposure to interest rate fluctuations is with respect to its short-term and long-term financing, which bear interest at floating rates.

At the reporting date, the carrying value of the Company's interest-bearing financial liabilities was as follows:

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Variable rate instruments		
Financial liabilities	<b>\$ 8,474,538</b>	\$ 8,924,825
Derivative financial instrument		
Interest rate swap	<b>9,745</b>	49,068
Gross financial position exposure	<b><u>\$ 8,484,283</u></b>	<u>\$ 8,973,893</u>

**Sensitivity analysis**

The Company is exposed to interest rate risk with respect to its variable rate non-derivative financial instruments and its interest rate swap. A 100 basis point increase in interest rates at the reporting date would result in an increase in cash outflows for the year ended December 31, 2013 of approximately \$78,166 (\$83,671 for 2012 as at December 31, 2011). Conversely a decrease would have the opposite effect.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**24. Risk management (continued)**

**24.4 Liquidity risk management**

Liquidity risk, the risk that the Company will not be able to meet its financial obligations as they fall due, is managed through the Company's capital structure and financial leverage. The Company obtains financing through a mix of share issuance on the capital markets and borrowing from financial institutions. An analysis of financial leverage is used to determine the required mix between the different sources of liquidity offered to the Company while keeping an acceptable risk level in the Company's leverage.

The Company ensures that it maintains sufficient cash flow to pay its obligations within the next 12 months. Cash flows generated from operations are matched to the liquidity required to meet its financial obligations for the sources of financing used to generate that cash flow.

The Company has an operating line of credit of up to \$8,500,000, of which an amount of \$6,103,876 was utilized as at December 31, 2012. Borrowings under the Company's operating line of credit bear interest at the bank's prime rate plus 2.0%. In order to ensure that this line of credit is sufficient to fund the Company's obligations, management follows the movements in the collateral against which the line of credit is given.

As at December 31, 2012, the carrying amount and undiscounted contractual cash flows for the Company's financial liabilities are as follows:

	Carrying amount	Contractual cash flow	1 year or less	2-5 years	More than 5 years
<i>Non-derivative financial liabilities</i>					
Bank indebtedness	\$6,103,876	\$ 6,103,876	\$ 6,103,876	\$ -	\$ -
Long term debt	2,535,604	2,535,604	1,101,425	1,434,179	-
Interest on borrowings (1)	-	199,334	92,715	106,619	-
Finance leases (2)	61,639	66,240	39,298	26,942	-
Trade Payables (3)	6,133,508	6,133,508	6,133,508	-	-
Balance of sale	937,906	994,900	-	994,900	-
<i>Derivative financial liabilities</i>					
Interest rate swap (1,4)	9,745	9,796	9,796	-	-
	<b>\$15,782,278</b>	<b>\$16,043,258</b>	<b>\$13,480,618</b>	<b>\$ 2,562,640</b>	<b>\$ -</b>

(1) The interest on the long term debt and derivative is based on prevailing interest rates at the date of the consolidated statement of financial position.

(2) The contractual cash flow for finance leases includes interest on the borrowings.

(3) The accounts payable exclude the interest rate swap, presented separately and with payments settled on a net basis.

(4) The interest rate swap's undiscounted contractual cash flow is based on net settlements and assumes that the derivative financial instrument will be held until maturity.

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**24. Risk management (continued)**

**24.5 Fair value hierarchy**

Financial instruments recorded at fair value on the consolidated statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level-1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level-2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (ie derived from prices);

Level-3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The Company has determined its interest rate swap using level 2 valuation techniques using forward interest rates.

**25. Subsidiaries**

Details of the Company's subsidiaries at December 31, 2011 and 2012 are as follows:

<u>Name of subsidiary</u>	<u>Principal activity</u>	<u>Place of incorporation and operation</u>	<u>Proportion of ownership interest and voting power held</u>
Imaflex USA	Manufacturing of plastic film	North Carolina, USA	100%

**26. Related party transactions**

***Transactions with related parties***

During the year, in the normal course of business, the Company had routine transactions with entities owned by shareholders of the Company and with the Company's directors and entities in which they hold an interest. These transactions are measured at fair value, which is the amount of consideration established and agreed to by the related parties. Details of these transactions not disclosed elsewhere in these financial statements, are as follows:

	<u>Year ended</u>	
	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Rent	\$ 798,475	\$ 724,129
Professional fees	358,572	263,079
	<u>\$ 1,157,047</u>	<u>\$ 987,208</u>

Rent is paid on the first day of the month for the current month. As at December 31, 2012, there was an amount of \$ 186 886 recorded as payable to related parties (\$ 85 828 as at December 31, 2011).

**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**26. Related party transactions (continued)**

*Compensation of key management personnel*

The table below details the compensation paid to the four key members of management, which include the Company's chief executive officer, the vice-president of operations, the production director and the corporate controller.

	<b>Year ended</b>	
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Salary	<b>\$ 422,103</b>	\$ 429,623
Management fees	<b>171,686</b>	177,251
Short-term employee benefits	<b>3,467</b>	2,981
Share based compensation	-	10,399
Post-employment benefits – State-run plans	<b>9,050</b>	8,093
Other benefits	<b>22,667</b>	26,065
	<b>\$ 628,973</b>	\$ 654,412

**27. Business acquisition**

On February 29, 2012, Imaflex USA acquired the operations of a North Carolina-based converter enabling partial vertical integration of its activities for a total consideration of \$ 1,883,596 (USD\$ 1,903,584). This acquisition benefits from synergies from the greater usage of the Company's extrusion equipment in its Thomasville, North Carolina plant as well as lower production costs for the acquired business.

The acquisition is comprised of an immediate cash payment of \$ 989,500 (USD\$ 1,000,000), a non-interest bearing balance of sale which was recorded at the discounted value of \$ 894,096 (USD\$ 904,584), payable on the two-year anniversary date of the acquisition, accounted for using the effective interest method. The balance of sale can be settled in cash or through the issuance of shares of the Company at a fixed value of USD\$ 1 per share at the option of the seller. The balance of sale was recorded as a liability.

The purchase price was as follows:

Immediate cash payment	\$ 989,500
Balance of sale	894,096
	<u>\$1,883,596</u>

The final allocation of the purchase price to net assets acquired is as follows:

Accounts receivable	\$ 573,574
Inventory	330,076
Production equipment	1,088,450
Customer relationships	296,850
Goodwill	371,513
Debt related to equipment	(50,806)
Accounts payable	(726,061)
	<u>\$1,883,596</u>



**Notes to the consolidated financial statements  
for the years ended December 31 2012 and 2011**

**27. Business acquisition (continued)**

Based on the seller's past history in collecting accounts receivable, all acquired accounts receivable were expected to be collected. The Asset Purchase Agreement ("PA") provides for a deduction from the balance of sale for any material amount of uncollectable accounts receivable. Based on the open orders on hand, the inventory was expected to be realizable in its entirety. The production equipment includes all the equipment that the seller was using at its production facility.

The customer relationships represent the value of the seller's current business relationships which are expected to continue after the acquisition date. During the year, following the finalization of the analysis of the useful life of the customer relationships, the Company revised the carrying value initially recognized at \$ 272,036 (USD\$ 274,923). During the year, the Company recorded amortization of customer relationships of \$ 31,091.

Goodwill includes the value of the assembled workforce, the current organization of the plant for which the Company did not have to incur any additional expenses and the synergies that can be created through the combination of the production assets through cost savings. The goodwill was recorded at an amount of \$ 371,513 (USD\$ 375,456) and was included in intangible assets in the consolidated statement of financial position. The value of goodwill was decreased from the value initially reported in the prior period of \$ 389,632 following the increase in value of the customer relationships. The goodwill did not have any tax impact at closing or on the reported income tax expense.

The Company did not have access to the information required to determine what sales or net income would have been had the transaction taken place on January 1, 2012. During the year ended December 31, 2012, the acquired business generated sales of \$ 4,930,957 and a net income of \$ 557,378.

**28. Approval of the consolidated financial statements**

The consolidated financial statements were approved by the board of directors and authorized for issue on April 16, 2013.