K·BRO

2012 Annual Report

dependable.

K-Bro Linen Inc.

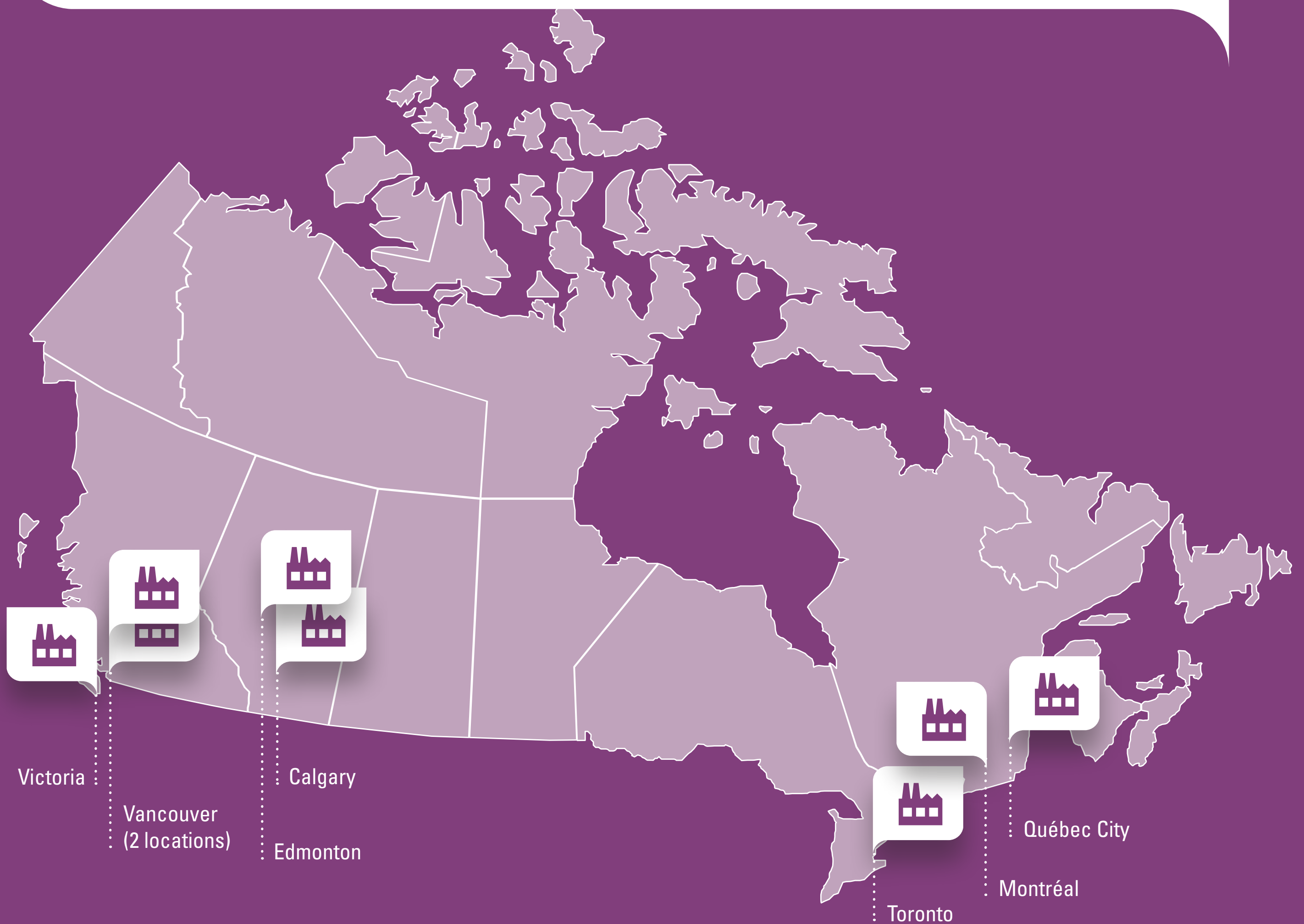
Contents

President's Message	1
Chairman's Message	2
Financial Highlights	5
Management's Discussion and Analysis	10
Management's Responsibility for Financial Reporting	11
Consolidated Financial Statements	28

We are dependable.

Plant Locations

K-Bro is the largest healthcare & hospitality laundry and linen processor in Canada.



President's Message

Since joining K-Bro in 1998, I have enjoyed working with a tremendously hard-working team and seeing record results from work done by people who are passionate about their company, their co-workers and our customers. This teamwork is the foundation of our success and of the positive momentum we have built, all of which will carry us forward as we embark on exciting new initiatives in 2013 and beyond. Last year, we pledged to build on our 2011 achievements, and again, we delivered on that commitment in 2012. K-Bro is at work…for our customers, for our employees, and for you, our shareholders.

Deliberate steps to optimize our operational performance and be the partner of choice to our customers have made a meaningful contribution to K-Bro's financial performance, evident in our 2012 results. 2012 was marked with a number of accomplishments for K-Bro, including:

- total shareholder return of 35.0%;
- revenue in excess of $126 million compared with $116.9 million in 2011;
- EBITDA of $24.5 million compared with $19.9 million in 2011;
- distributable cash of over $19 million compared with $16.8 million in 2011;
- increase in dividend to $1.15 per common share; and a payout ratio of 42%;
- market capitalization of $204 million at December 31, 2012 and a debt to total capitalization ratio of 0.1; and,
- earnings per share for 2012 reached a record $1.60, a 39.3% increase over 2011.

I believe these financial results reflect a compelling story of K-Bro which has set us on a path to strong, sustainable earnings growth. We have built on our long term trend of profitability and 2012 marks our eighth consecutive year of growth in our relatively short history as a public company.

During 2012, continuing into 2013, we commenced the redevelopment of our Edmonton processing facilities with an investment of approximately $26 million into a state-of-the-art processing facility in Edmonton. This investment will result in significant efficiencies and cost savings as well as an increase in our overall capacity in Alberta.

Looking forward, we see opportunities to leverage our scope and scale to grow our business organically and through acquisitions, based on our national capabilities. We remain positive about K-Bro's outlook with our focus on execution and performance. K-Bro's balance sheet, financial liquidity and substantial borrowing capacity continue to provide the financial resources to capitalize on the opportunities on the horizon.

K-Bro has been built as a proud Canadian company. Our employees across Canada are hard at work making K-Bro the best company for our clients, our partners, and you, our valued shareholders.

On behalf of the Board of Directors, our management team and our 1,600 dedicated employees, thank you for your continued support of K-Bro.

Linda McCurdy
President and Chief Executive Officer

Chairman's Message

Much can be learned from a company whose values and principles have been preserved for over half a century and whose growth has been measured, methodical and at all times, deliberate. K-Bro's growth has been focused on financial performance as well as sustainably developing for the future. We have been consistent in our pursuit of quality and steadfast in our commitments to our customers. Keeping commitments is important to all of us, but is hard to actually put into practice. Earning and maintaining the trust of our customers is our commitment. K-Bro's corporate decisions are geared to ensuring we have the resources and financial strength to keep our commitments over the long term.

This past year marked our 59th anniversary of keeping those commitments in the laundry and linen services sector. We have grown along with our cities, their people and our country through the years. We should be very proud of K-Bro's history, but we must also continue to adapt if we are to move forward with strength. Our talented executive team led by Linda McCurdy, is proactively pursuing both organic and new growth opportunities that will provide even greater value to our shareholders. We will pursue new initiatives designed to make K-Bro even more attractive to our investors.

While we are pleased with the significant financial and share price performance achieved this year, our management team and Board remain focused on prudently building the foundation for disciplined growth and future success. In 2012 we continued to make significant investments in our facilities and our employees throughout the country. Collectively, these actions will play a central role in ensuring that K-Bro remains best-positioned to deliver shareholder value in the years to come.

We are proud of our ability to meet our customers needs while maintaining the highest commitment to safety, social and environmental sustainability, and a strong duty of care to the communities in which we operate. We also take pride in K-Bro's employees who are among the most passionate, dedicated and talented anywhere. I would like to thank our employees, as well as K-Bro's management and Board for the hard work that resulted in another record year. I am confident that K-Bro will continue to deliver outstanding performance for all of our stakeholders and firmly believe that K-Bro will rise to the challenges that lie ahead.

Ross Smith
Chairman

Board of Directors

(Left to right) - Matt Hills, Ross Smith, Steve Matyas, Mike Percy, Linda McCurdy

General Managers

(Left to right) - Eric Ouellette, Stany Bergeron, Ken Chu, Jerry Ostrzyzek, Jeff Gannon, Kevin Stephenson, Maxim Lortie, Sean Curtis, Ron Graham

K-Bro is the largest healthcare and hospitality laundry and linen processor in Canada. K-Bro operates eight facilities in seven cities, providing management services and laundry processing of hospitality, healthcare and speciality linens. Our core values are central to our reputation, our quality is industry-leading, and our ability to deliver on commitments to customers is second to none. **We are dependable.**

K-Bro provides the vital products and services that help people heal, travel, live, and play. We're helping hospitals and extended care centres care for the young, old and vulnerable in environmentally responsible ways. Our responsibility also extends to ensuring that we have a safe culture at K-Bro. As our society grows, we integrate our commitment to responsibility into our new businesses, employees and the communities in which we live and work.

By expanding our capabilities into new markets, we have opportunities to leverage our operating strengths, grow our revenue, and further enhance operating margins, ensuring consistent value creation for stakeholders.

Linda McCurdy
President and Chief Executive Officer

K-Bro has a stable business model with strong fundamentals that support our market valuation and reliable shareholder dividends.

Christopher Burrows
Vice-President and Chief Financial Officer

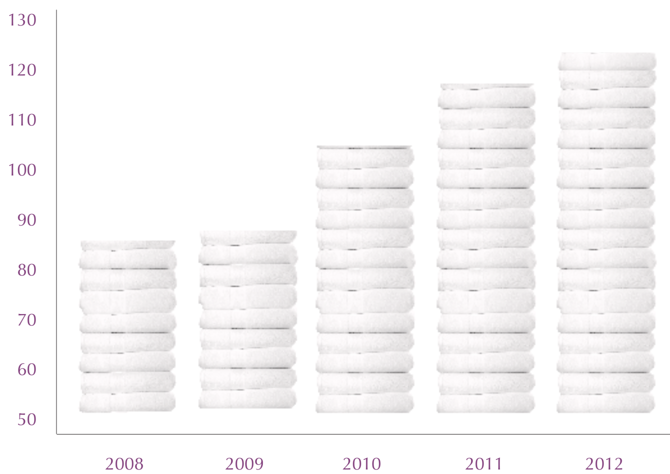
Quality, innovation, and respect for our customers, employees and communities is at the very center of everything we have done for the past 50 years. We have positioned K-Bro to be the preeminent partner of choice by providing services across the country.

Sean Curtis
Senior Vice-President and General Manager

Financial Highlights

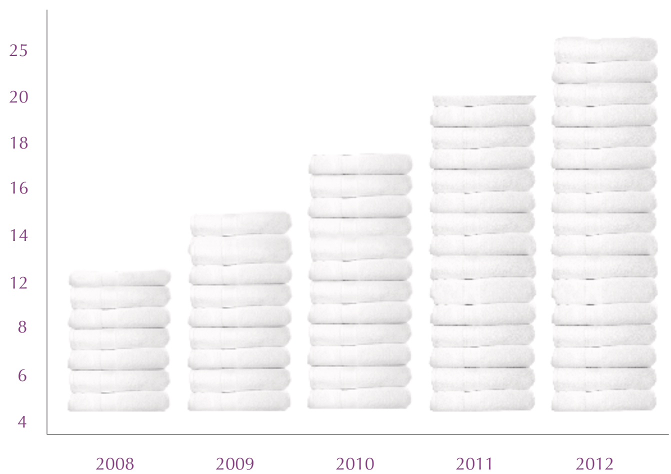
The following unaudited financial data has been derived from K-Bro's consolidated financial statements, which have been audited by PricewaterhouseCoopers LLP. The information set forth below should be read in conjunction with the Management's Discussion & Analysis, Consolidated Financial Statements and Notes sections of this Annual Report.

REVENUE



REVENUE (In millions of Canadian dollars) Years ended December 31

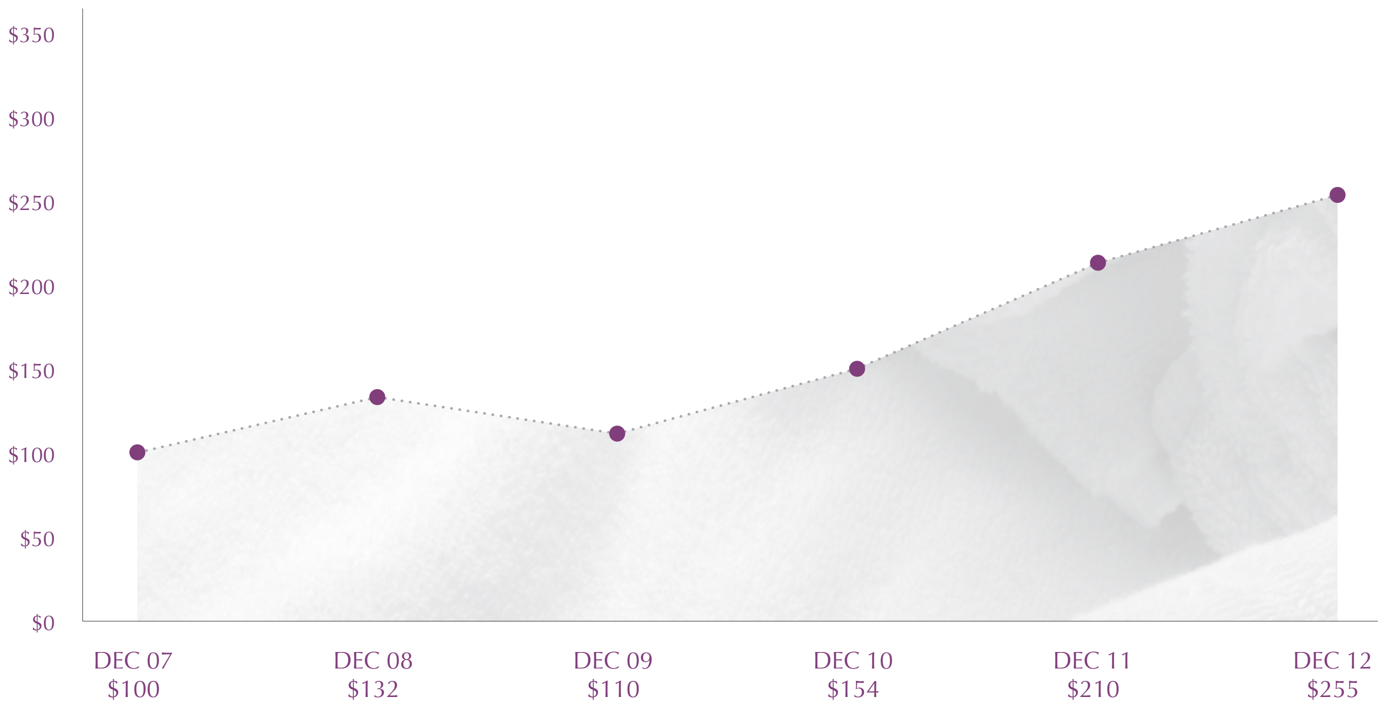
EBITDA



EBITDA (In millions of Canadian dollars) Years ended December 31

TOTAL SHAREHOLDER RETURN

(on a $100 investment in 2007)



In order to be successful, a company must have a vision. We continue to be committed to remaining as Canada's premier linen processing company. We focus on businesses that we know and understand – laundry and linen processing – in regions where we have an existing competitive advantage or can develop one. Long-term contracts supported by an experienced workforce and large scale assets are the priority – relationships coupled with assets that provide attractive and sustainable returns.

Over the past decade, K-Bro has invested over $55 million in high quality plants, investments that have allowed the company to move forward in achieving its vision. Today, we play a significant role in the provision of high quality healthcare and also in business and leisure travel markets.

We are the largest healthcare and hospitality laundry & linen processor in Canada.

We are dependable.

In aggregate, our eight plants provided services to more than 1,500 customers and employed almost 1,600 employees in 2012. At December 31, 2012, total assets were $95 million, equity was $68 million and market capitalization was $204 million.

Diversified and integrated services – we provide critical services, support and management of linen requirements that address each and every one of our customers' needs.

Strategically positioned – K-Bro has 8 plants located in 7 different cities, which ensures our ability to provide uninterrupted service in the wake of disasters, pandemics or other adversity.

Long-term stable contracts – by anticipating our customers' needs, delivering consistently dependable service and acting with integrity, K-Bro has developed long-term relationships with its customers.

Committed workforce – our corporate culture enables us to attract and retain quality laundry staff and our national presence provides opportunities for career advancement. Five members of our senior management team commenced their careers with K-Bro and have an average tenure in excess of 20 years.

Single source for customers – K-Bro is able to deliver total linen management services, including laundering, drying, folding, quota cart development, sterilization, and more that focuses on efficiencies and cost savings. We are one of the largest consumers of linens and textiles in Canada. We leverage our market position to drive savings for our customers. K-Bro works in partnership with our clients to reduce their linen consumption.

One of our key strategies for growth is to pursue opportunities for expansion through acquisition. We follow a strict set of criteria when evaluating another organization's potential, examining every facet of a target company – does it open up a new or strategically placed geographic market or market niche for us? Is there a potential for growth in the market it serves? Will we be able to build on relationships the company already has in place? Can we build on an already-existing base of business? Does it enhance our resources overall?

Taking advantage of relationships already in place includes maintaining the existing labour and management of a company. The ability and commitment demonstrated by staff members is a factor in our decision-making process for acquisitions. The bottom line is that we want profitable, dependable operations where we can bring our expertise and resources to grow the existing base of business. We continue to review and pursue accretive opportunities in new markets and we believe that such opportunities may be available in the future to further add to our growth.

In our industry, we're dependent on our reputation, resources, and track record as we develop relationships with potential and new clients and compete for contracts. These factors are also critical in maintaining stable, responsive, and loyal relationships with our existing customers.

In 2012, K-Bro excelled at discovering and winning new opportunities and clients, building on the successes we've had in our decades of experience as leaders in our sector.

Sean Curtis
Senior Vice-President and General Manager

At K-Bro, we innovate and develop new processes and systems, and further refine business delivery and practices.

In 2012, K-Bro excelled at discovering and winning new opportunities and clients, building on the successes we've had in our decades of experience as leaders in our sector. We obtained significant new business from our competitors in important locations. In British Columbia, we added six major hospitality customers to our base, five in Quebec, three in Ontario, and in Alberta we added one additional hotelier and extended agreements with several more. Our new clients include some of the finest hotels in the country.

Each new customer was a victory for the entire K-Bro team and a reflection of the company as a whole, rather than any individual. The qualities that contribute to our success are the same ones that define us as leaders in customer service – an impeccable and dependable record, comprehensive service programs, financial stability, competitive costs, experience in transitioning large accounts, and having the resources to support growth, including the ability to purchase linen and equipment in anticipation of higher volume.

Our policy at K-Bro has always been one of proactive response. In order to meet our goal of being the absolute best laundry and linen services provider in the country, we continually review our service offerings, adding to our menu and providing more comprehensive service capabilities than other linen companies. We watch our industry and think ahead to strategically address the future needs of the markets we serve. Our established relationships and experience contribute to our thinking – our clients talk to us not only about their present needs, but about the directions they see themselves going in. They **depend** on the knowledge we've accumulated over our history.

During 2012 we commenced the planning and construction of a new Edmonton processing facility. Our customers' needs have outgrown our existing facility. Furthermore, there are significant process efficiencies to be realized from a newly designed facility. While the construction and commissioning of a new facility comes at a cost in excess of $26 million, the productivity gains and efficiency improvements more than offset the costs related to the new build. We are excited about commissioning a state-of-the-art linen processing facility which will increase our capacity in Alberta's capital region.

K-Bro's value-added services provide a 'one-stop shop' for linen services, and currently include:

- Exchange cart preparation
- Delivery of carts to user wards and departments
- Reusable OR linen and pack rental (KOR services)
- Distribution and control of uniforms
- Personal clothing services
- Customer service programs
- Linen purchase and supply
- Linen inventory management reports and services
- Sterilization of operating room linen packs

At K-Bro, we will innovate and develop new processes and systems, and further refine business delivery and practices. When we launched our company on the public markets, we stated that we were ready for whatever lay ahead of us. As the events of the next eight years unfolded, our readiness contributed to our success in dependability and growth. The hands-on nature of our management team and established relationships with open lines of communication with our customers is the very source of our advantage. **We are dependable**.

The following selected unaudited financial data has been derived from K-Bro's consolidated financial statements, which have been audited by PricewaterhouseCoopers LLP. The information set forth below should be read in conjunction with the Management's Discussion & Analysis, Consolidated Financial Statements and Notes sections of this Annual Report.

($ Thousands, except per share data and percentages)	Years ended December 31[1]					
	2012	2011	2010	2009	2008	2007
INCOME STATEMENT DATA						
Revenue	126,290	116,859	104,051	87,533	85,113	74,101
EBITDA	24,517	19,946	16,877	15,547	12,395	9,188
EBITDA *(%)*	19.4	17.1	16.2	17.8	14.6	12.4
Net earnings	11,149	7,928	7,116	7,802	4,722	4,818
Net earnings per Share *(Diluted)*	1.59	1.14	0.99	1.11	0.70	0.71
BALANCE SHEET DATA						
Working capital	8,064	7,245	8,664	7,896	3,533	5,494
Long-term debt	5,818	6,095	10,763	4,043	4,061	16,627
OTHER FINANCIAL DATA						
Distributable cash per share	2.72	2.40	2.15	1.99	1.63	1.40
Payout ratio *(%)*	41.8	49.5	51.4	55.1	68.4	78.5
Price to earnings multiple *(12 month trailing)*	18.1	21.4	18.5	12.1	13.9	18.0
Price to EBITDA multiple *(12 month trailing)*	8.2	7.8	7.6	6.1	5.2	8.1
Return on shareholders' equity *(ROE) (%)*	16.5	12.6	11.4	12.0	6.1	8.5
Total shareholder return, YTD *(%)*	34.9	27.5	43.9	50.0	-19.8	33.0
Total shareholder return, 5 yrs *(%)*	253.8	121.1	146.7	87.5	38.9	65.6
Market capitalization	203,613	155,821	126,866	93,451	67,385	73,168
Share price:						
High	30.18	22.98	19.29	13.84	13.65	14.75
Low	21.20	17.28	13.02	9.70	8.50	10.75
Close	28.86	22.24	18.30	13.48	9.72	13.49

[1] K-Bro's IFRS transition date was January 1, 2010; accordingly 2010 figures have been restated; earlier fiscal periods are presented under Canadian GAAP.

As events have unfolded since entering the public market, our readiness has contributed to our success in dependability and growth.

Management's Discussion and Analysis

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

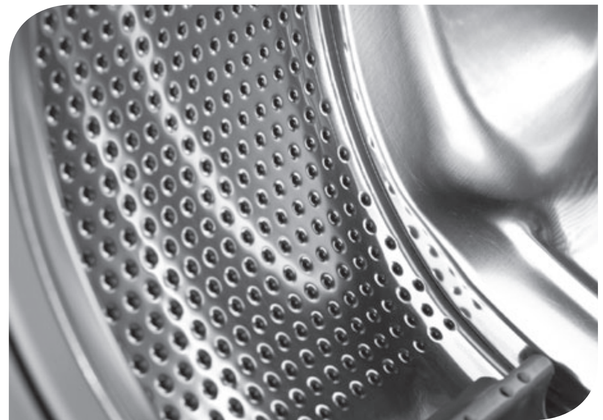
The consolidated financial statements of K-Bro Linen Inc. and the accompanying financial information presented are the responsibility of management of the Corporation and have been approved by its Board of Directors. In management's opinion, the consolidated financial statements have been prepared within reasonable limits of materiality in accordance with International Financial Reporting Standards. The preparation of financial statements necessarily requires judgment and estimation when events affecting the current year depend on determinations to be made in the future. Management has exercised careful judgment where estimates were required, and these consolidated financial statements reflect all information available to March 13, 2013.

To discharge its responsibility for financial reporting, management maintains systems of internal controls designed to provide reasonable assurance that the Corporation's assets are safeguarded, that transactions are properly authorized and that reliable financial information is relevant, accurate and available on a timely basis. The internal control systems are monitored and evaluated by management, which are regularly reported on to the Audit Committee of the Board of Directors.

The consolidated financial statements have been examined by PricewaterhouseCoopers LLP, the Corporation's external auditors. The external auditors are responsible for examining the consolidated financial statements and expressing their opinion on the fairness of the consolidated financial statements in accordance with International Financial Reporting Standards. The auditors' report outlines the scope of their audit examination and states their opinion. The Board of Directors, through the Audit Committee, is responsible for oversight of management's fulfilment of its responsibilities for financial reporting and internal controls. The Audit Committee, which is comprised solely of independent directors, meets regularly with management and the external auditors to satisfy itself that each group is discharging its responsibilities with respect to internal controls and financial reporting. The Audit Committee reviews the consolidated financial statements and recommends their approval to the Board of Directors. The external auditors have full and open access to the Audit Committee, with and without the presence of management. The Audit Committee also recommends to the Board of Directors for nomination, the firm of external auditors, and such nomination on approval of the Board of Directors shall be confirmed annually by the shareholders of the Corporation.

On behalf of management,

Christopher Burrows
Vice-President and Chief Financial Officer



The Board of Directors, through the Audit Committee, is responsible for oversight of management's fulfilment of its responsibilities for financial reporting and internal controls.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis ("MD&A") is supplemental to, and should be read in conjunction with, the audited Consolidated Financial Statements of K-Bro Linen Inc. ("the Corporation") for the years ended December 31, 2012 and 2011, as well as the unaudited interim condensed Consolidated Financial Statements for the periods ended March 31, 2012, June 30, 2012 and September 30, 2012. The Corporation and its wholly-owned subsidiaries, including K-Bro Linen Systems Inc., are collectively referred to as "K-Bro" in this MD&A.

Management is responsible for the information contained in this MD&A and its consistency with information presented to the Audit Committee and Board of Directors. All information in this document has been reviewed and approved by the Audit Committee and Board of Directors. This review was performed by management with information available as of March 13, 2013.

In the interest of providing current Shareholders of K-Bro Linen Inc. and potential investors with information regarding current results and future prospects, our public communications often include written or verbal forward-looking statements. Forward-looking statements are disclosures regarding possible events, conditions, or results of operations that are based on assumptions about future economic conditions and courses of action, and include future-oriented financial information.

This MD&A contains forward-looking information that represents internal expectations, estimates or beliefs concerning, among other things, future activities or future operating results and various components thereof. The use of any of the words "anticipate", "continue", "expect", "may", "will", "project", "should", "believe", and similar expressions suggesting future outcomes or events are intended to identify forward-looking information. Statements regarding such forward-looking information reflect management's current beliefs and are based on information currently available to management.

These statements are not guarantees of future performance and are based on management's estimates and assumptions that are subject to risks and uncertainties, which could cause K-Bro's actual performance and financial results in future periods to differ materially from the forward-looking information contained in this MD&A. These risks and uncertainties include, among other things: (i) risks associated with acquisitions, including the possibility of undisclosed material liabilities; (ii) K-Bro's competitive environment; (iii) utility and labour costs; (iv) K-Bro's dependence on long-term contracts with the associated renewal risk; (v) increased capital expenditure requirements; (vi) reliance on key personnel; (vii) changing trends in government outsourcing; and (viii) the availability of future financing. Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking information include: (i) volumes and pricing assumptions; (ii) expected impact of labour cost initiatives; and (iii) the level of capital expenditures. Although the forward-looking information contained in this MD&A is based upon what management believes are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements. Certain statements regarding forward-looking information included in this MD&A may be considered "financial outlook" for purposes of applicable securities laws, and such financial outlook may not be appropriate for purposes other than this MD&A.

All forward-looking information in this MD&A is qualified by these cautionary statements. Forward-looking information in this MD&A is presented only as of the date made. Except as required by law, K-Bro does not undertake any obligation to publicly revise these forward-looking statements to reflect subsequent events or circumstances.

This MD&A also makes reference to certain measures in this document that do not have any standardized meaning as prescribed by IFRS or previous Canadian GAAP and, therefore, are considered additional GAAP measures. These measures may not be comparable to similar measures presented by other issuers. Please see *"Terminology"* for further discussion.

In order to be successful, a company must have a vision. We continue to be committed to remaining as Canada's leading linen processing company.

MD&A Table of Contents

Introduction	14
Strategy	14
Fourth Quarter Overview	15
Selected Annual Financial Information	15
Summary of 2012 Results and Events	15
Key Performance Drivers	17
Outlook	17
Results of Operations	18
Liquidity and Capital Resources	20
Dividends	21
Distributable Cash Flow	22
Outstanding Shares	23
Related Party Transactions	23
Off-Balance Sheet Arrangements	23
Critical Accounting Estimates	23
Terminology	24
Changes in Accounting Policies	25
Recent Accounting Pronouncements	25
Financial Instruments	25
Critical Risks and Uncertainties	26
Controls and Procedures	26

INTRODUCTION

Core Business

K-Bro is the largest owner and operator of laundry and linen processing facilities in Canada. K-Bro provides a comprehensive range of general linen and operating room linen processing, management and distribution services to healthcare institutions, hotels and other commercial accounts. K-Bro currently has eight processing facilities in seven Canadian cities including Victoria, Vancouver, Calgary, Edmonton, Toronto, Montréal and Québec City.

Industry and Market

K-Bro provides laundry and linen services to Canadian healthcare, hospitality and other commercial customers. Typical services offered by K-Bro include the processing, management and distribution of general and operating room linens, including sheets, blankets, towels, surgical gowns and drapes and other linen. Other types of processors in K-Bro's industry in Canada include independent privately owned facilities (i.e. typically small, single facility companies), public sector central laundries and public and private sector on-premise laundries (known as "OPLs"). Participants in other sectors of the laundry and linen services industry, such as uniform rental companies (which own and launder uniforms worn by their customers' employees) and facilities management companies (which manage public sector central laundries and OPLs), typically do not offer services that significantly overlap with those offered by K-Bro.

Our partnerships with healthcare institutions and hospitality clients across Canada demonstrate K-Bro's commitment to build relationships that foster continuous improvement, provide flexibility to adjust to changing circumstances as required and which incorporate incentives, penalties and sharing of risks and rewards as circumstances warrant. As a result, clients across the country have entered into long-term relationships with us, with most having renewed their contracts several times.

In this competitive industry, K-Bro is distinctive in Canada in its ability to deliver products and services that provide value to our customers. Management believes that the healthcare and hospitality sectors of the laundry and linen services industry represent a stable base of annual recurring business with opportunities for growth as additional healthcare beds and funds are made available to meet the needs of an aging demographic.

Industry Characteristics and Trends

Management believes that the industry in which K-Bro operates exhibits the following characteristics and trends:

Stable Industry with Moderate Cyclicality – As evidenced by the stability in the number of approved hospital beds in the healthcare system and hotel rooms in the hospitality industry. Service relationships are generally formalized through contracts in the healthcare sector that are typically long term (from seven to ten years), while contracts in the hospitality sector usually range from two to five years.

Outsourcing and Privatization – Healthcare institutions and regional authorities are facing funding pressures and must continually evaluate the allocation of scarce resources. Consequently there are often advantages to healthcare institutions in outsourcing the processing of healthcare linen to private sector laundry companies such as K-Bro because of the economies of scale and significant management expertise that can be provided on a more comprehensive and cost-effective basis than customers can achieve in operating their own laundry facilities.

Fragmentation – Most Canadian cities have at least one and sometimes several private sector competitors operating in the healthcare and hospitality sectors of the laundry and linen services industry. Management believes that the presence of these operators provides consolidation opportunities for larger industry participants with the financial means to complete acquisitions.

Customers and Product Mix

K-Bro's customers include some of the largest healthcare institutions and hospitality providers in Canada. Healthcare customers include acute care hospitals and long-term care facilities. Most of K-Bro's hospitality customers (typically >250 rooms) generate between 500,000 and 3 million pounds of linen per year. Most healthcare customers generate between 500,000 pounds of linen per year for a hospital and up to 30 million pounds of linen per year for a healthcare region.

STRATEGY

K-Bro maintains the following three-part strategic focus:

Secure and Maintain Long-Term Contracts with Large Healthcare and Hospitality Customers – K-Bro's core service is providing high quality laundry and linen services at competitive prices to large healthcare and hospitality customers under long-term contracts. K-Bro's contracts in the healthcare sector typically range from seven to ten years in length. Contracts in the hospitality sector typically range from two to five years.

STRATEGY (continued)

Extend Core Services To New Markets – Management has demonstrated its ability to successfully expand K-Bro's business into new markets from its established bases. Since 2005, K-Bro has entered four new geographic markets across Canada. These new markets have contributed significantly to K-Bro's growth. Management believes that new outsourcing opportunities will continue to arise in the near to medium term and that K-Bro is well-positioned for continued growth, particularly as healthcare and hospitality institutions continue to increase their focus on core services and confront pressures for capital and cost savings.

Management may in the future expand its core services to new markets either through acquisitions or by establishing new facilities. Its choice of areas for expansion will depend on the availability of suitable acquisition candidates, the volume of healthcare and hospitality linen to be processed and the policies of applicable governments.

Introduce Related Services – In addition to focusing on its core services, the Corporation also attempts to capitalize on attractive business opportunities by introducing closely related services that enable it to provide more complete solutions to K-Bro's healthcare and hospitality customers. These related service offerings include K-Bro Operating Room ("KOR") services and on-site services. For three major hospitals in Toronto, K-Bro performs the sterilization of operating room linen packs.

FOURTH QUARTER OVERVIEW

In the fourth quarter of 2012, revenue was $31.6 million which was 8.3% higher than the $29.2 million generated in the comparative quarter of 2011. This year-over-year increase was due to a combination of the new volumes from the Saskatoon Health Region and organic growth from new volume and price increases at existing customers across the remainder of the plants. EBITDA increased from $4.6 million in Q4, 2011 to $5.8 million in Q4, 2012, as the result of the new volume from the Saskatoon Health Region coupled with organic growth and favorable variances in utilities.

SELECTED ANNUAL FINANCIAL INFORMATION

($ Thousands, except share and per share amounts)	2012	2011	2010
Revenue	126,290	116,859	104,051
Earnings before income taxes	15,324	10,888	7,116
Net earnings	11,149	7,928	6,953
Net earnings per share:			
Basic	1.60	1.15	1.01
Diluted	1.59	1.14	0.99
Total assets	94,800	91,425	90,679
Long-term debt	5,818	6,095	10,763
Dividends declared to Shareholders	7,977	7,706	7,706
Dividends declared to Shareholders per share	1.13	1.10	1.10
Number of shares outstanding:			
Basic	6,981,432	6,918,955	6,905,369
Diluted	6,993,561	6,980,489	6,992,400

SUMMARY OF 2012 RESULTS AND KEY EVENTS

Financial Growth

K-Bro delivered strong financial results in 2012 driven by the operating results from all eight of its processing plants. Net earnings were $11.1 million or $1.60 per share (basic). Cash flow from operating activities was $20.8 million and distributable cash flow was $19.1 million. Revenue increased in fiscal 2012 to $126.3 million or by 8.0% compared to 2011. This revenue growth in the year is due to the acquisition of the new plant in Montréal (increases in Q1 and Q2, 2012, acquired on July 1, 2011), increased volumes arising from the Saskatoon Health Region contract and organic volume and price growth in the remainder of the plants. EBITDA (see Terminology) increased in the year to $24.5 million from $19.9 million in 2011, which is an increase of 21.8%. The EBITDA margin increased to 19.4% in 2012 compared 17.1% in 2011. The increase in margin is driven by the new volume from the Saskatoon Health Region contract coupled with favorable variances in utilities and organic growth of the plants.

Saskatoon Health Region Contract

In January 2012, K-Bro earned the healthcare linen business of Saskatoon Health Region (the "Region") under a one-year contract, while the Region explores its options for longer-term processing arrangements. Under the terms of the original agreement, K-Bro was awarded a portion of the total volume processed with the remainder being processed internally. The agreement was subsequently extended to May 2013 and K-Bro was awarded the remaining volume once processed internally by the Region.

Alberta Health Services Contract

In May 2012, K-Bro was awarded a ten-year contract with Alberta Health Services ("AHS") for laundry and linen services for the Edmonton and surrounding areas. The contract encompasses a comprehensive linen supply and service program covering general, operating room and specialty linens as well as on-site services at certain facilities. K-Bro has commenced planning and construction of a new Edmonton processing plant with expected commissioning during Q2 and Q3, 2013. Services under the terms and conditions of this contract will commence on April 1, 2013. The contract is renewable for an additional five years at AHS' option.

The new ten-year contract also includes certain price concessions as compared to the existing services agreement that concludes in fiscal 2013. Management believes that efficiencies arising from a newly designed Edmonton facility will directly offset the price concessions made under the terms of the new AHS contract, as well as additional carrying costs of any associated debt. The Corporation intends to finance the construction through its existing credit facilities. It is anticipated that the new facility will be fully operational by Q3, 2013.

Effects of Economic Uncertainty

A significant degree of uncertainty exists with respect to the development of a new Edmonton facility and the resultant decommissioning of the old plant. Management estimates that the costs to commission a new leased facility are expected to be approximately $26 million for new efficiency enhancing equipment, leaseholds and conversion costs, with immediate returns anticipated from reduced labour, lower energy consumption and other work-flow improvements. Costs associated with the new facility have been incurred since Q2, 2012, with over half of the total expenditure forecast to be spent in Q1, 2013. As at December 31, 2012, K-Bro has incurred $5.9 million of the total expected capital cost.

K-Bro feels that it is positioned to withstand market volatility and uncertainty given that:

- Approximately 68.6% of its revenues in the year were from large publicly funded healthcare customers which are geographically diversified across multiple provinces;
- K-Bro routinely enters into natural gas, electricity, and textile supply contracts and typically tries to align terms with existing linen processing contract terms;
- At December 31, 2012, K-Bro had unutilized borrowing capacity of $33.8 million or 84.5% of the revolving credit line available; and,
- K-Bro's prudent approach to managing capital has added cash flow and liquidity to the Corporation, thereby improving its ability to withstand the turmoil in the national and global capital markets.

Sound governance is a principle that is both understood and embraced by our management team.

KEY PERFORMANCE DRIVERS

K-Bro's key performance drivers focus on growth, profitability, stability and cost containment in order to maintain dividends and maximize Shareholder value. The following outlines our results on a period-to-period comparative basis in each of these areas:

($ Thousands, except percentages)

Category	Indicator	Q4, 2012	Q4, 2011	YTD 2012	YTD 2011
Growth	EBITDA[1] *(%)*	26.8	13.6	21.8	18.2
	Revenue *(%)*	8.3	9.1	8.0	12.3
	Distributable cash flow *(%)*	14.9	0.9	13.8	12.0
Profitability	EBITDA[1]	5,777	4,556	24,517	19,946
	EBITDA margin *(%)*	18.3	15.6	19.4	17.1
	Net earnings	2,758	1,643	11,149	7,928
Stability	Debt to total capitalization *(%)*	7.9	8.8	7.9	8.8
	Unutilized line of credit	33,782	33,655	33,782	33,655
	Payout ratio *(%)*	45.8	50.2	41.8	45.9
	Dividends declared per share	0.287	0.275	1.133	1.100
Cost containment	Wages and benefits *(%)*	46.1	46.7	46.1	46.4
	Utilities *(%)*	6.9	7.2	6.6	7.4
	Operating expenses *(%)*	81.7	84.4	80.6	82.9

[1] EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, gain or loss on disposals, financial charges and depreciation and amortization). See *Terminology*.

OUTLOOK

K-Bro's focus is on profitable growth in the years to come as we execute our strategy of expanding geographically and adding new services for our customers. K-Bro is committed to building value for our shareholders, our customers and our employees.

In 2013 K-Bro will commission a new Edmonton facility in a new location and also decommission the former plant site. As a result of the development of the new facility Management expects efficiency and productivity of its Edmonton operations to decline in Q2 and Q3, 2013, and improve once the transition between the two sites is complete. Management believes that EBITDA margin will be negatively impacted during the transition period by up to 3% on a consolidated basis.

K-Bro also has several proposals pending and has entered into discussions with potential new customers. In addition, K-Bro continues to seek potential acquisition candidates. Neither the timing nor the degree of likelihood of success of any of these proposals or acquisitions can be stated with any degree of accuracy.

RESULTS OF OPERATIONS

Overall Performance

For the three month period ended December 31, 2012, K-Bro's revenue was $31.6 million, compared to $29.2 million in the comparable prior year period. This growth in the growth is due to the volumes arising from the Saskatoon Health Region contract and organic volume and price growth in the remainder of the plants. EBITDA increased in the fourth quarter of 2012 by $1.2 million (26.8%) over the fourth quarter of 2011 mainly due to increased volumes and the semi-fixed nature of certain costs.

Quarterly Financial Information

The following table provides certain selected consolidated financial and operating data prepared by K-Bro management for the preceding eight quarters:

($ Thousands, except per share amounts and percentages)	2012				2011			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Healthcare revenue	22,222	21,418	21,713	21,257	20,432	19,730	20,042	19,941
Hospitality revenue	9,364	11,595	9,813	8,908	8,726	11,414	8,829	7,745
Total revenue	31,586	33,013	31,526	30,165	29,158	31,144	28,871	27,686
Operating expenses	25,809	26,274	25,122	24,568	24,602	25,098	24,006	23,207
EBITDA[1]	5,777	6,739	6,404	5,597	4,556	6,046	4,865	4,479
EBITDA as % of revenue *(%)*	18.3	20.4	20.3	18.6	15.6	19.4	16.9	16.2
Depreciation and amortization	1,924	2,283	2,263	2,207	2,082	2,232	2,036	2,216
Financial charges	(66)	272	67	84	93	131	84	104
Loss (gain) on disposal of equipment	39	1	(10)	129	50	4	20	6
Earnings before income taxes	3,880	4,183	4,084	3,177	2,331	3,679	2,725	2,153
Income tax expense	1,122	1,224	1,121	708	688	953	722	597
Net earnings	2,758	2,959	2,963	2,469	1,643	2,726	2,003	1,556
Net earnings as a % of revenue *(%)*	8.7	9.0	9.4	8.2	5.6	8.8	6.9	5.6
Basic earnings per share	0.393	0.422	0.424	0.356	0.237	0.290	0.290	0.226
Diluted earnings per share	0.393	0.420	0.423	0.353	0.235	0.288	0.288	0.223
Total assets	94,800	94,166	90,505	92,529	91,425	90,350	93,148	90,473
Total long-term financial liabilities	11,023	12,830	11,963	8,795	11,203	12,096	17,554	13,079
Funds provided by operations	7,928	6,223	(110)	6,768	3,929	8,217	2,577	4,137
Long-term debt	5,818	7,787	7,113	4,000	6,095	7,224	13,007	8,838
Dividends declared per share	0.287	0.288	0.283	0.275	0.275	0.275	0.275	0.275

[1] EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, gain or loss on disposals, financial charges and amortization). See *Terminology*.

Revenue, Earnings and EBITDA

For the year ended December 31, 2012, K-Bro's revenue was $126.3 million, compared to $116.9 million in the prior year. This represents an 8.0% increase in revenue and is attributed to a combination of the new volume from the Saskatoon Health Region contract and organic growth from new volume and price increases at existing customers across the remainder of the plants. In 2012 approximately 68.6% of K-Bro's revenue was generated from healthcare institutions compared to 68.6% in 2011.

Net earnings increased in 2012 to $11.1 million from $7.9 million in 2011. Net earnings as a percentage of revenue increased to 8.8% compared to 6.8% in 2011. This net increase in margin resulted from a decline in operating costs of 2.3%. Net earnings before tax increased in 2012 to $15.3 million from $10.9 million in 2011. Net earnings before tax as a percentage of revenues increased to 12.1% compared to 9.3% in 2011. This margin increase is due to a flow through effect of the increase in the EBITDA margin discussed below.

EBITDA was $24.5 million in 2012, compared to $19.9 million in 2011. This 21.8% improvement is a result of the new volume from the Saskatoon Health Region contract coupled with favorable variances in utilities. The increase is also attributable to the increases in volume and price offsetting the semi-fixed nature of certain operating costs (see Operating Expenses for further detail).

Operating Expenses

Wages and benefits increased from $54.2 million in 2011 to $58.2 million in 2012 and decreased as a percentage of revenues to 46.1% from 46.4%. Despite the control over labor costs, pressures continue to increase as the economy recovers, employment rates improve and provincially regulated minimum wage increases. Linen expenses increased to $12.7 million from $12.0 million but remained constant as a percentage of revenues at approximately 10%.

Utility costs decreased from 7.4% in 2011 to 6.6% as a percentage of revenue in 2012. The decrease is as a result of the maturation of several natural gas forward contracts, thereby permitting K-Bro to purchase a larger percentage at the current lower market rate.

Delivery costs have increased to $5.6 million or 4.4% of revenues compared to 4.2% in 2011. The rising cost of diesel fuel has contributed to the increase on a year-over-year basis. Additionally the delivery of linens to Saskatoon Health Region has increased delivery expenses as these services are being performed by the Corporation's Calgary facility. Incremental delivery costs for Saskatoon are offset by additional revenues.

Materials and supplies, occupancy costs and repairs and maintenance as a percentage of revenue remained stable in 2012 compared to 2011.

Corporate costs decreased in 2012 by $0.5 million over the comparative period of 2011 and decreased as a percentage of revenues to 4.1% from 4.9% in 2011. In the prior year comparative period, acquisition costs associated with the acquisition of the Montréal plant ineligible for capitalization were expensed and incurred as corporate costs.

Depreciation of property, plant and equipment and amortization of intangible assets represents the expense related to the appropriate matching of certain of K-Bro's long-term assets to the estimated useful life and period of economic benefit of those assets. Depreciation of property, plant and equipment and amortization of intangibles assets has increased from the comparable period in 2011 primarily due to the purchases of laundry equipment in Montréal, Québec City and Vancouver.

Income tax includes current and future income taxes based on taxable income and the temporary timing differences between the tax and accounting bases of assets and liabilities. The Corporation's effective tax rate remained constant at approximately 27% of net earnings. A decrease in the statutory rate from 26.9% to 25.3% was offset by an increase in non-deductible expenses.

K-Bro has a stable business model with strong fundamentals that support our market valuation and reliable shareholder dividends.

LIQUIDITY AND CAPITAL RESOURCES

In 2012 cash generated by operating activities was $20.8 million, compared to cash generated by operating activities of $18.9 million in 2011. The change in cash from operations is due to the increases in earnings offset by smaller changes in other operating accounts.

During 2012, cash used in financing activities amounted to $8.2 million compared to $11.7 million in 2011 mainly attributable to repayment of revolving debt. Financing activities in 2012 included $2.1 million in net proceeds of long term debt and $7.9 million in dividends paid to Shareholders.

The Corporation used cash of $12.6 million for investing activities during 2012 compared to $7.1 million in 2011. The increase in cash used in investing activities is driven by the purchase of property, plant and equipment for existing operations and the new Edmonton facility.

Contractual Obligations

At December 31, 2012, payments due under contractual obligations for the next five years and thereafter are as follows:

		Payments due by Period			
($ Thousands)	**Total**	<1 Year	1-3 Years	4-5 Years	>5 Years
Long-term debt	5,818	-	5,818	-	-
Operating leases and utility commitments	31,101	4,160	7,927	3,323	15,691
Linen purchase obligations	2,551	2,551	-	-	-
Property, plant and equipment commitments	20,332	20,332	-	-	-

Scheduled lease and forward utility contract payments for 2013 are expected to be $1.5 million. The operating lease obligations are secured by automotive equipment and are more fully described in the audited annual consolidated financial statements. The source of funds for these commitments will be from operating cash flow and, if necessary, the undrawn portion of the revolving credit facility.

Financial Position

($ Thousands, except percentages)	**December 31, 2012**	December 31, 2011
Long term debt	5,818	6,095
Shareholders' equity	67,685	62,933
Total capitalization	73,503	69,028
Debt to total capitalization	7.9%	8.8%

For the year ended December 31, 2012, the Corporation had a payout ratio of 41.8%, a debt to total capitalization of 7.9%, an unused revolving credit facility of $33.8 million and has not incurred any events of default under the terms of its credit facility agreement.

As at December 31, 2012, the Corporation had net working capital of $8.1 million compared to its working capital position of $7.2 million at December 31, 2011. The increase in working capital is attributable to the increased earnings during the year offset by capital expenditures.

Management believes that K-Bro has the capital resources and liquidity necessary to meet its commitments, support its operations and finance its growth strategies. In addition to K-Bro's ability to generate cash from operations and its revolving credit facility, K-Bro may also be able to access equity financing, depending upon pricing and availability, for capital spending to sustain its property, plant and equipment.

DIVIDENDS

Fiscal Period	Payment Date	# of Shares Outstanding	2012 Amount per Share	2012 Total Amount[1]	2011 Amount Per Unit	2011 Total Amount[1]
January	February 15	7,006,365	0.09167	642	0.09167	642
February	March 15	7,006,365	0.09167	642	0.09167	642
March	April 15	7,006,365	0.09167	642	0.09167	642
Q1			0.27501	1,927	0.27501	1,927
April	May 13	7,006,365	0.09167	642	0.09167	642
May	June 15	7,055,207	0.09580	676	0.09167	642
June	July 15	7,055,207	0.09580	676	0.09167	642
Q2			0.28328	1,994	0.27501	1,927
July	August 15	7,055,207	0.09580	676	0.09167	642
August	September 15	7,055,207	0.09580	676	0.09167	642
September	October 14	7,055,207	0.09580	676	0.09167	642
Q3			0.28741	2,028	0.27501	1,927
October	November 15	7,055,207	0.09580	676	0.09167	642
November	December 15	7,055,207	0.09580	676	0.09167	642
December	January 13	7,055,207	0.09580	676	0.09167	642
Q4			0.28741	2,028	0.27501	1,927
YTD			1.13	7,977	1.10004	7,706

[1] The total amount of dividends paid was $0.09167 per share for a total of $642.273 per month for Jan - Apr 2012 and $642.146 per month in 2011; when rounded in thousands $1.927 of dividends were paid for each of the quarterly periods, respectively.

For the year ended December 31, 2012, the Corporation distributed $1.13 per share compared with $2.73 per diluted share of Distributable Cash Flow (see Terminology). The actual payout ratio was 41.8%.

The Corporation's policy is to pay dividends to Shareholders from its available distributable cash flow while considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Directors of the Corporation. All such dividends are discretionary. Dividends are declared payable each month in equal amounts to Shareholders on the last business day of each month and are paid by the 15th of the following month.

The Corporation designates all dividends paid or deemed to be paid as Eligible Dividends for purposes of subsection 89(14) of the Income Tax Act (Canada), and similar provincial and territorial legislation, unless indicated otherwise.

DISTRIBUTABLE CASH FLOW *(See Terminology)*

The Corporation's source of cash for dividends is distributable cash flow provided by operating activities. Distributable cash flow, reconciled to cash provided by operating activities as calculated under IFRS, is presented as follows:

($ Thousands, except per share amounts and percentages)	2012 Q4	2012 Q3	2012 Q2	2012 Q1	2011 Q4	2011 Q3	2011 Q2	2011 Q1
Cash provided by operating activities	7,928	6,223	(110)	6,768	3,929	8,217	2,577	4,137
Deduct (add):								
Net changes in non-cash working capital items[1]	2,866	598	(5,659)	1,774	(80)	2,928	(1,736)	130
Share-based compensation expense[2]	176	177	250	502	503	361	407	390
Maintenance capital expenditures	486	168	232	134	179	9	423	224
Distributable cash flow	4,400	5,280	5,067	4,358	3,830	5,280	3,890	3,783
Distributable cash flow per weighted average diluted shares outstanding	0.627	0.750	0.723	0.622	0.548	0.756	0.559	0.541
Dividends declared	2,028	2,028	1,994	1,927	1,927	1,927	1,927	1,927
Dividends declared per share	0.287	0.288	0.283	0.275	0.275	0.275	0.275	0.275
Payout ratio[3] *(%)*	45.8	38.3	39.2	44.2	50.2	36.4	49.2	50.8
Weighted average shares outstanding during the period, basic	7,007	7,007	6,979	6,932	6,932	6,930	6,918	6,891
Weighted average shares outstanding during the period, diluted	7,019	7,040	7,009	7,003	6,993	6,983	6,961	6,993
TRAILING-TWELVE MONTHS ("TTM")								
Distributable cash flow	19,105	18,535	18,535	17,358	16,783	16,748	16,043	15,763
Dividends	7,977	7,876	7,774	7,706	7,706	7,706	7,706	7,706
Payout ratio[3] *(%)*	41.8	42.5	41.9	44.4	45.9	46.0	48.0	48.9

[1] Net changes in non-cash working capital is excluded from the calculation as management believes it would introduce significant cash flow variability and affect underlying cash flow from operating activities. Significant variability can be caused by such things as the timing of receipts (which individually are large because of the nature of K-Bro's customer base and timing may vary due to the timing of customer approval, vacations of customer personnel, etc.) and the timing of disbursements (such as the payment of large volume rebates done once annually). As well, large increases in working capital are generally required when contracts with new customers are signed as linen is purchased and accounts receivable increase. Management feels that this amount should be excluded from the distributable cash flow calculation.

[2] Share-based compensation expenses have historically been excluded from the calculation of distributable cash flow. Previously the share-based compensation was recorded as part of the net changes in non-cash working capital items, however the amount has been disclosed separately commencing in Q4, 2012. The comparative figures for the quarterly periods as presented have been restated to reflect this revised presentation.

[3] The ratio of dividends paid compared to distributable cash flow is periodically reviewed by the Board of Directors to take into account the current and prospective performance of the business and other items considered to be prudent. Payout ratio is calculated on the dividends declared per share divided by the distributable cash flow per weighted average diluted shares outstanding.

OUTSTANDING SHARES

At December 31, 2012, the Corporation had 7,055,207 common shares outstanding. Basic and diluted weighted average number of common shares outstanding for 2012 were 6,981,432 and 6,993,561 respectively, (6,918,955 and 6,980,489, respectively for the comparative 2011 periods).

In accordance with the LTI plan and in conjunction with the performance of the Corporation in the 2011 fiscal year, on May 2, 2012 the Compensation, Nominating and Corporate Governance Committee of the Board of Directors approved LTI compensation of $1.2 million (2011 – $1.8 million under the previous LTI plan) to be paid as shares issued from treasury under the terms of the revised plan approved by Shareholders. As at December 31, 2012, the value of the shares held in trust by the LTI trustee was $1.4 million (2011 – $1.3 million) which was comprised of 48,191 in unvested common shares (December 31, 2011 – 74,511) with an aggregate cost of $0.3 million (2011 – $1.9 million). The basic net earnings per share calculation excludes the unvested common shares held by the LTI Trust.

As at March 13, 2013, there were 7,055,207 common shares issued and outstanding.

RELATED PARTY TRANSACTIONS

The Corporation incurred expenses in the normal course of business for advisory consulting services provided by Mr. Matthew Hills, a director of the Corporation, primarily relating to acquisitions. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the year ended December 31, 2012, the Corporation incurred fees totaling $137,500 (2011 – $137,500).

OFF-BALANCE SHEET ARRANGEMENTS

The Corporation had a foreign exchange forward contract for the purchase of US dollars in place as at December 31, 2012. This forward contract was marked-to-market and was settled on January 31, 2013.

CRITICAL ACCOUNTING ESTIMATES

The Corporation's summary of significant accounting policies are contained in note 2 to the audited consolidated financial statements.

The Corporation's financial statements include estimates and assumptions made by management in respect of operating results, financial conditions, contingencies, commitments, and related disclosures. Actual results may vary from these estimates. The following are, in the opinion of management, the Corporation's most critical accounting estimates, being those that involve the most difficult, subjective and complex judgments, and/or requiring estimates that are inherently uncertain and which may change in subsequent reporting periods.

K-Bro has continuously refined and documented its management and internal reporting systems to ensure that accurate, timely, internal and external information is gathered and disseminated. Management also regularly evaluates these estimates and assumptions which are based on past experience and other factors that are deemed reasonable under the circumstances.

K-Bro has hired individuals and consultants who have the skills required to make such estimates and ensures that individuals or departments with the most knowledge of the activity are responsible for the estimates. Furthermore, past estimates are reviewed and compared to actual results, and actual results are compared to budgets in order to make more informed decisions on future estimates.

K-Bro's leadership team's mandate includes ongoing development of procedures, standards and systems to allow K-Bro staff to make the best decisions possible and ensuring those decisions are in compliance with the Corporation's policies.

Preparation of the Corporation's consolidated financial statements requires management to make estimates and assumptions that affect:

- volume rebates;
- linen in service;
- intangible assets;
- goodwill;
- income taxes; and,
- allowance for doubtful accounts.

Volume Rebates

The Corporation earns revenue from linen management and laundry services based on written service agreements whereby K-Bro has agreed to collect, launder, deliver and replenish linens. K-Bro recognizes revenue in the period in which the services are provided. Volume rebates, where applicable, are recorded based on annualized expected volumes when it is reasonable that the criteria are likely to be met. Based on past experience, management believes that volumes utilized for any estimates are reasonable and would not expect a material deviation to the balance of accrued liabilities or revenue.

Linen in Service

Linen in service is recorded at cost. Operating room linen is amortized on a straight-line method over an estimated service life of 24 months. General linen is amortized based on usage which results in an estimated service life of the linen equal to 24 months. Based on past experience, management believes that a service life of 24 months is representative of the average service life of linen and would not expect a material deviation to the balance of linen in service or linen expense.

Intangible Assets

The Corporation accounts for intangible assets and goodwill in accordance with IFRS 3, Business Combinations and IAS 38, Intangible Assets. In a business combination, K-Bro may acquire the assets and assume certain liabilities of an acquired entity. The allocation of the purchase price for these transactions involves judgment in determining the fair values assigned to the tangible and intangible assets acquired and the liabilities assumed on the acquisition. The determination of these fair values involves a variety of assumptions, including revenue growth rates, expected operating income, discount rates, and earnings multiples. If K-Bro's estimates or assumptions change prior to finalizing the purchase price allocation for a transaction, a revision to the purchase price allocation or the carrying value of the related assets and liabilities acquired may impact our net income in future periods.

At the date of the acquisition, K-Bro must estimate the value of acquired intangible assets that do not have a well defined market value, such as the value of customer lists and relationships and non-competition agreements.

Valuing these assets involves estimates of the future net benefit to K-Bro and the useful life of such benefits and is based upon various internal and external factors. A change in those estimates could cause a material change to the value of the intangible assets.

Although intangible assets are amortized over their useful life, if the estimated value of an intangible asset has declined below its amortized book value, a write-down would be recorded in the period in which the event causing the decline in value occurred, which would increase amortization expense and decrease the intangible assets balance. At this time, K-Bro does not believe any intangible assets have a book value in excess of their fair market value.

TERMINOLOGY

EBITDA

We report on our EBITDA (Earnings before interest, taxes, depreciation and amortization) because it is a key measure used by management to evaluate performance. EBITDA is utilized in measuring compliance with debt covenants and in making decisions relating to dividends to Shareholders. We believe EBITDA assists investors in assessing our performance on a consistent basis as it is an indication of our capacity to generate income from operations before taking into account management's financing decisions and costs of consuming tangible and intangible capital assets, which vary according to their vintage, technological currency and management's estimate of their useful life. Accordingly, EBITDA comprises revenues less operating costs before: financing costs, capital asset and intangible asset amortization, loss on disposal and impairment charges, and income taxes.

EBITDA is not a calculation based on IFRS and is not considered an alternative to net earnings in measuring K-Bro's performance. EBITDA does not have a standardized meaning and is therefore not likely to be comparable with similar measures used by other issuers. EBITDA should not be used as an exclusive measure of cash flow since it does not account for the impact of working capital changes, capital expenditures, debt changes and other sources and uses of cash, which are disclosed in the consolidated statements of cash flows.

	Three Months Ended December 31		Year Ended December 31	
($ Thousands)	2012	2011	2012	2011
Net earnings	2,758	1,643	11,149	7,928
Add:				
Income tax expense	1,122	688	4,175	2,960
Interest expense and financial charges, net	(66)	93	357	412
Depreciation of property, plant and equipment	1,617	1,409	6,350	5,938
Amortization of intangible assets	307	673	2,327	2,628
Loss on disposal of property, plant and equipment	39	50	159	80
EBITDA	5,777	4,556	24,517	19,946

Distributable Cash Flow

Distributable cash flow is a measure used by management to evaluate its performance. While the closest IFRS measure is cash provided by operating activities, distributable cash flow is considered relevant because it provides an indication of how much cash generated by operations is available after maintenance capital expenditures. It should be noted that although we consider this measure to be distributable cash flow, financial and non-financial covenants in our credit facilities and dealer agreements may restrict cash from being available for dividends, re-investment in the Corporation, potential acquisitions, or other purposes. Investors should be cautioned that distributable cash flow may not actually be available for growth or distribution from the Corporation. References to "Distributable cash flow" are to cash provided by (used in) operating activities (including the net change in non-cash working capital balances) less capital expenditures.

CHANGES IN ACCOUNTING POLICIES

The Corporation has prepared its December 31, 2012 audited Consolidated Financial Statements in accordance with IFRS. See note 2 of the Corporation's audited Consolidated Financial Statements for more information regarding the significant accounting principles used to prepare the audited Consolidated Financial Statements. There have been no changes in accounting policies during the year ended December 31, 2012.

RECENT ACCOUNTING PRONOUNCEMENTS

There are no changes in accounting standards applicable to future periods that are relevant and significant to the Corporation other than as disclosed in the most recent audited Consolidated Financial Statements as at and for the year ended December 31, 2012.

FINANCIAL INSTRUMENTS

K-Bro's financial instruments at December 31, 2012 consist of accounts receivable, accounts payable and accrued liabilities and long-term debt. The Corporation does not enter into financial instruments for trading or speculative purposes. Financial assets are either classified as available for sale, held to maturity, trading or loans and receivables. Financial liabilities are recorded at amortized cost. Initially, all financial assets and financial liabilities must be recorded on the balance sheet at fair value. Subsequent measurement is determined by the classification of each financial asset and liability. Unrealized gains and losses on financial assets that are held as available for sale are recorded in other comprehensive income until realized, at which time they are recorded in the consolidated statement of earnings. All derivatives, including embedded derivatives that must be separately accounted for, are recorded at fair value in the consolidated balance sheet. Transaction costs related to financial instruments are capitalized and then amortized over the expected life of the financial instrument using the effective interest method.

Derivative financial instruments are utilized by K-Bro to manage cashflow risk against the volatility in interest rates on its long-term debt and foreign exchange rates on its equipment purchase commitments. K-Bro typically does not utilize derivative financial instruments for trading or speculative purposes. K-Bro has floating interest rate debt that gives rise to risks that its earnings and cash flows may be adversely impacted by fluctuations in interest rates. In order to manage these risks, K-Bro may enter into interest rate swaps, forward contracts on foreign currency, utilities and textiles or option contracts.

CRITICAL RISKS AND UNCERTAINTIES

As at December 31, 2012, there are no material changes in the Corporation's risks or risk management activities since December 31, 2011. The Corporation's results of operations, business prospects, financial condition, cash dividends to Shareholders and the trading price of the Corporation's Shares are subject to a number of risks. These risk factors include: dependence on long-term contracts and the associated renewal risk thereof; the effects of market volatility and uncertainty; potential future tax changes; the competitive environment; our ability to acquire and successfully integrate and operate additional businesses; utility costs; the labour markets; the fact that our credit facility imposes numerous covenants and encumbers assets; and, environmental matters.

For a discussion of these risks and other risks associated with an investment in Corporation Shares, see Risk Factors – *Risks Related to K-Bro and the Laundry and Linen Industry* detailed in the Corporation's Annual Information Form that is available at www.sedar.com.

CONTROLS AND PROCEDURES

In order to ensure that information with regard to reports filed or submitted under securities legislation present fairly in all material respects the financial information of K-Bro, management, including the President and Chief Executive Officer ("CEO") and the Vice-President and Chief Financial Officer ("CFO"), are responsible for establishing and maintaining disclosure controls and procedures, as well as internal control over financial reporting.

Disclosure Controls and Procedures

The Corporation has established disclosure controls and procedures to ensure that information disclosed in this MD&A and the related financial statements of K-Bro was properly recorded, processed, summarized and reported to the Board of Directors and the Audit Committee. The Corporation's CEO and CFO have evaluated the effectiveness of these disclosure controls and procedures for the year ended December 31, 2012, and the CEO and CFO have concluded that these controls were operating effectively.

Internal Controls over Financial Reporting

The CEO and CFO acknowledge responsibility for the design of internal controls over financial reporting ("ICFR"). Consequently the CEO and CFO confirm that the additions to these controls that occurred during the year ended December 31, 2012 did not materially affect, or are reasonably likely to materially affect, the Corporation's ICFR. Based upon their evaluation of these controls for the year ended December 31, 2012, the CEO and CFO have concluded that these controls were operating effectively.

A control system, no matter how well conceived and operated, can provide only reasonable, and not absolute, assurance that the objectives of the control system are met. As a result of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instance of fraud, if any, have been detected. These inherent limitations include, amongst other items: (i) that managements' assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; or, (ii) the impact of isolated errors.

Additionally, controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override. The design of any system of controls is also based, in part, upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

Consolidated Financial Statements

March 13, 2013
Independent Auditor's Report

To the Shareholders of K-Bro Linen Inc.

We have audited the accompanying consolidated financial statements of K-Bro Linen Inc. and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2012 and December 31, 2011 and the consolidated statements of earnings and comprehensive income, changes in equity and cash flows for the years then ended, and the related notes, which comprise 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 K-Bro Linen Inc. and its subsidiaries as at December 31, 2012 and December 31, 2011 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Accountants
Edmonton, Canada

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

($ Thousands of Canadian dollars)	**December 31 2012**	December 31 2011
ASSETS		
Current assets		
Accounts receivable	14,197	14,902
Linen in service	8,888	8,182
Prepaid expenses and deposits	1,071	1,450
	24,156	24,534
Property, plant and equipment *(note 6)*	39,175	33,095
Intangible assets *(note 7)*	11,013	13,340
Goodwill *(note 8)*	20,456	20,456
	94,800	91,425
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	13,001	14,790
Income taxes payable	2,415	1,857
Dividends payable to shareholders	676	642
	16,092	17,289
Long-term debt *(note 9)*	5,818	6,095
Unamortized lease inducements *(note 11)*	415	512
Deferred income taxes *(note 12)*	4,790	4,596
	27,115	28,492
SHAREHOLDERS' EQUITY		
Share capital *(note 14)*	71,444	69,493
Contributed surplus	1,209	1,580
Deficit	(4,968)	(8,140)
	67,685	62,933
Contingencies and commitments *(note 13)*	94,800	91,425

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

Approved on behalf of the Corporation

Ross S. Smith
Chair

Matthew B. Hills
Director

CONSOLIDATED STATEMENTS OF EARNINGS & COMPREHENSIVE INCOME

($ Thousands of Canadian dollars, except share and per share amounts)	Year ended December 31 2012	2011
Revenue	126,290	116,859
Expenses		
Wages and benefits	58,248	54,185
Linen	12,706	12,031
Utilities	8,276	8,688
Delivery	5,583	4,900
Repairs and maintenance	3,832	3,843
Occupancy costs	3,896	3,810
Materials and supplies	4,058	3,765
Corporate	5,174	5,691
	101,773	96,913
EBITDA *(note 19)*	24,517	19,946
Other expenses		
Depreciation of property, plant and equipment	6,350	5,938
Amortization of intangible assets	2,327	2,628
Financial charges *(note 10)*	357	412
Loss on disposal of property, plant and equipment	159	80
	9,193	9,058
Earnings before income taxes	15,324	10,888
Current income tax expense	3,981	1,862
Deferred income tax expense	194	1,098
Income tax expense *(note 12)*	4,175	2,960
Net earnings and Comprehensive income	11,149	7,928
Net earnings per share		
Basic	1.60	1.15
Diluted	1.59	1.14
Weighted average number of shares outstanding *(note 14)*		
Basic	6,981,432	6,918,955
Diluted	6,993,561	6,980,489

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

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

($ Thousands of Canadian dollars)	Issued Capital					
	Number of shares (#)	Amount	Contributed surplus	Shares held in trust	Deficit	Total equity
As at December 31, 2010	7,004,973	71,400	1,141	(1,601)	(8,362)	62,578
Net earnings	-	-	-	-	7,928	7,928
Dividends declared *(note 16)*	-	-	-	-	(7,706)	(7,706)
Employee share based compensation expense	1,392	-	439	(306)	-	133
As at December 31, 2011	7,006,365	71,400	1,580	(1,907)	(8,140)	62,933
As at December 31, 2011	7,006,365	71,400	1,580	(1,907)	(8,140)	62,933
Net earnings	-	-	-	-	11,149	11,149
Dividends declared *(note 16)*	-	-	-	-	(7,977)	(7,977)
Employee share based compensation expense	48,842	1,178	(371)	1,626	-	2,433
Unvested treasury shares held in trust	(36,626)	(853)	-	-	-	(853)
As at December 31, 2012	7,018,581	71,725	1,209	(281)	(4,968)	67,685

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

CONSOLIDATED STATEMENTS OF CASH FLOW

($ Thousands of Canadian dollars)	Year ended December 31 2012	2011
OPERATING ACTIVITIES		
Net earnings	11,149	7,928
Depreciation of property, plant and equipment	6,350	5,938
Amortization of intangible assets	2,327	2,628
Amortization of lease inducements	(54)	(54)
Share-based compensation expense	1,105	1,661
Loss on disposal of property, plant and equipment	159	80
Deferred income taxes	194	1,098
	21,230	19,279
Change in non-cash balances relating to operations *(note 17)*	(421)	(419)
Cash provided by operating activities	20,809	18,860
FINANCING ACTIVITIES		
Acquisition of business *(note 5)*	-	4,317
Repayments to revolving credit facility	(277)	(8,985)
Dividends paid to shareholders	(7,943)	(7,064)
Cash used in financing activities	(8,220)	(11,732)
INVESTING ACTIVITIES		
Purchase of property, plant and equipment	(12,650)	(2,847)
Proceeds from disposal of property, plant and equipment	61	36
Acquisition of business *(note 5)*	-	(4,317)
Cash used in investing activities	(12,589)	(7,128)
Change in cash during the year	-	-
Cash, beginning of year	-	-
Cash, end of year	-	-
Supplementary cash flow information		
Interest paid	143	274
Income taxes	3,423	5

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

K-Bro Linen Inc. (the "Corporation" or "K-Bro") is incorporated in Canada under the Business Corporations Act (Alberta). The Corporation and its wholly owned subsidiaries provide a range of linen services to healthcare institutions, hotels and other commercial accounts that include the processing, management and distribution of general linen and operating room linen. The Corporation provides services from eight processing facilities in seven major cities across Canada from Victoria, British Columbia to Québec City, Québec.

The Corporation's common shares are traded on the Toronto Stock Exchange under the symbol "KBL". The address of the Corporation's registered head office is #103, 15023 – 123 Avenue, Edmonton, Alberta, Canada.

These audited annual Consolidated Financial Statements (the "Consolidated Financial Statements") were approved and authorized for issuance by the Board of Directors ("the Board") on March 13, 2013.

1 Basis of Presentation

The consolidated financial statements of the Corporation have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Corporation's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the Consolidated Financial Statements are disclosed in note 4.

2 Significant accounting policies

The principal accounting policies applied in the preparation of these Consolidated Financial Statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

a) Basis of Measurement

The Consolidated Financial Statements have been prepared under the historical cost convention, except for the revaluation of certain financial assets and financial liabilities to fair value, including derivative instruments.

b) Principles of Consolidation

The Consolidated Financial Statements include the Corporation, its wholly owned subsidiaries and the long-term incentive plan trust, a special purpose entity (notes 2(o) (ii) and (iii)). All intercompany balances and transactions have been eliminated upon consolidation.

c) Linen in Service

Linen in service is measured at the lower of cost and net realizable value. The cost is calculated by a method which approximates the weighted average cost method, with operating room linen amortized across its estimated service life of 24 months and general linen amortized based on usage which results in an estimated average service life of 24 months.

d) Revenue Recognition

Revenue from linen management and laundry services is primarily based on written service agreements whereby the Corporation agrees to collect, launder, deliver and replenish linens. The Corporation recognizes revenue in the period in which the services are provided.

2 Significant accounting policies (continued)

e) Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Corporation and the cost of the item can be reliably measured. The carrying amount of a replaced part is derecognized. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

The major categories of property, plant and equipment are depreciated on a straight-line basis as follows:

Asset	Rate
Buildings	15-25 years
Laundry equipment	7-20 years
Office equipment	2-5 years
Delivery equipment	5 years
Computer equipment	2 years
Leasehold improvements	Lease term

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of other gains and losses in the statement of earnings and comprehensive income.

f) Impairment of Financial Assets

At each reporting date, the Corporation assesses whether there is objective evidence that a financial asset is impaired. If such evidence exists, the Corporation recognizes an impairment loss equal to the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

g) Impairment of Non-Financial Assets

Property, plant and equipment and intangible assets are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. Long-lived assets that are not amortized are subject to an annual impairment test. For the purpose of measuring recoverable amounts, assets are grouped at the lowest level for which there are separately identifiable cash flows (cash-generating unit or "CGU"). The recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The Corporation evaluates impairment losses, other than goodwill impairment, for potential reversals when events or circumstances warrant such consideration.

h) Intangible Assets

Intangible assets are recorded at cost and include customer contracts in progress and related relationships, which are being amortized using the straight-line method over the remaining lives of the related contracts and relationships. Intangible assets which relate to computer software are amortized using the straight-line method over five years when put into service. These estimates are reviewed at least annually and are updated if expectations change as a result of changing client relationships or technological obsolescence.

i) Income Taxes

The tax expense for the year comprises current and deferred tax. Tax is recognized in the income statement, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the tax is also recognized in other comprehensive income or directly in equity, respectively.

The current income tax provision is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date of the taxation authority where the Corporation operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Consolidated Financial Statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

j) Business Combinations

Business combinations are accounted for using the acquisition method. The acquired identifiable net assets are measured at their fair value at the date of acquisition. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Any excess of the purchase price over the fair value of the net assets acquired is recognized as goodwill. Any deficiency of the purchase price below the fair value of the net assets acquired is recorded as a gain in net earnings. Associated transaction costs are expensed when incurred.

k) Goodwill

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the identifiable assets acquired, less liabilities assumed, based on their estimated fair values at the acquisition date. Goodwill is allocated as of the date of the business combination. Goodwill is tested for impairment annually in the fourth quarter, or more frequently if events or changes in circumstances indicate a potential impairment.

Goodwill acquired through a business combination is allocated to each CGU or group of CGUs, that are expected to benefit from the related business combination. A CGU represents the lowest level within the entity at which the goodwill is monitored for internal management purposes.

l) Volume Rebates

Certain customers receive a rebate based on specified annual processing volumes. A rebate liability is recorded in the period it is expected that the customer will meet the specified annual volume levels.

m) Earnings Per Share

Basic earnings per share (“EPS”) is calculated by dividing net earnings for the period attributable to Shareholders of the Corporation by the weighted average number of Common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of common shares included within the weighted average is computed using the treasury stock method. The Corporation’s potentially dilutive Common shares are comprised of long-term incentive plan equity compensation granted to officers and key employees (notes 2(o) (ii) and (iii)).

n) Foreign Currency Translation

Foreign currency transactions are translated into Canadian dollars using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement. Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in the income statement within “financial charges”.

o) Employee Benefits

i) Post-employment benefit obligations

The Corporation contributes on behalf of its employees to their individual Registered Retirement Savings Plans subject to an annual maximum of 4% of gross base salary. The Corporation accounts for contributions as an expense in the period that they are incurred. The Corporation does not provide any other post-employment or post-retirement benefits.

ii) Former equity-based compensation plan

The officers and key employees were eligible to participate in a past long-term incentive plan ("LTIP"), which involved equity-settled share-based payments. The Corporation set aside funds each year based on the amount by which distributable cash flow exceeded a base distributable amount for the fiscal year.

The LTIP trustee purchased common shares in the open market and held such common shares until ownership vests to each participant. Subject to the Board's discretion to accelerate vesting, one-quarter of the LTIP grant vested thirty days following the date that the Trustees of the Fund approved the audited Consolidated Financial Statements (the "Determination Date"). The remaining three-quarters vested on the second anniversary of the Determination Date. In most circumstances, unvested grant amounts held by the trustee for an LTIP participant are forfeited if the participant resigns or is terminated for cause prior to the applicable vesting date, and any equity will be sold and the proceeds returned to the Corporation.

As of May 1, 2011 no additional compensation will be issued under this LTIP. Any unvested compensation granted under the terms of this plan will vest under the original terms and conditions of issue.

iii) Existing equity-based compensation plan of the Corporation

On June 16, 2011, the Shareholders of the Corporation approved a new Long-term Incentive Plan ("LTI"). Under the LTI, awards are granted annually in respect of the prior fiscal year to the eligible participants based on a percentage of annual salary. The amount of the award (net of withholding obligations) is satisfied by issuing treasury shares to be held in trust by the trustee pursuant to the terms of the LTI. All awards issued under the provisions of the LTI are recorded as compensation expense.

Subject to the discretion of the Compensation, Nominating and Corporate Governance Committee of the Board of Directors, one-quarter of a Participant's grant will vest on the Determination Date (defined as the first May 15th following the date that the Directors of the Corporation approve the audited consolidated financial statements of the Corporation for the prior year). The remaining three-quarters of the Participant's grant will vest on November 30th following the second anniversary of the Determination Date.

If a change of control occurs, all LTI Shares held by the Trustee in respect of unvested grants will vest immediately. LTI participants are entitled to receive dividends on all common shares granted under the LTI whether vested or unvested. In most circumstances, unvested common shares held by the LTI trustee for a participant will be forfeited if the participant resigns or is terminated for cause prior to the applicable vesting date, and those common shares will be disposed of by the trustee to K-Bro for no consideration and such Common shares shall thereupon be cancelled. If a participant is terminated without cause, retires or resigns on a basis which constitutes constructive dismissal, the participant will be entitled to receive his or her unvested common shares on the regular vesting schedule under the LTI.

p) Financial Instruments

Financial assets and financial liabilities are initially recognized at fair value and are subsequently accounted for based on their classification as described below. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Except in very limited circumstances, the classification is not changed subsequent to initial recognition. Transaction costs are recognized immediately in income or are capitalized, depending upon the nature of the transaction and the associated product.

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

The Corporation has made the following classifications:

	Classification	Measurement
FINANCIAL ASSETS		
Accounts receivable	Loans and receivables	Amortized cost
FINANCIAL LIABILITIES		
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Long-term debt	Other liabilities	Amortized cost

3 Accounting standards issued and not applied

The following new or revised standards are not expected to have a material impact on the amounts recorded in the Consolidated Financial Statements of the Corporation:

- IFRS 9, *Financial instruments* addresses classification and measurement of financial assets. IFRS 9 replaces the model for measuring equity instruments and will require recognition of the Corporation's investment in the LTIP trust (see note 15) at fair value through earnings. This standard is effective for accounting periods beginning on or after January 1, 2015.

- IFRS 10, *Consolidated financial statements* requires an entity to consolidate an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12, Consolidation—Special Purpose Entities and parts of IAS 27, Consolidated and Separate Financial Statements. This standard is effective for accounting periods beginning on or after January 1, 2013.

- IFRS 12, *Disclosures of Interests in Other Entities* establishes disclosure requirements for interests in other entities, such as subsidiaries, joint arrangements, associates, and unconsolidated structured entities. The standard carries forward existing disclosures and also introduces significant additional disclosure that address the nature of, and risks associated with, an entity's interests in other entities. This standard is effective for accounting periods beginning on or after January 1, 2013.

- IFRS 13, *Fair value measurement* defines fair value and provides a single IFRS framework for the measurement and disclosure of fair value within IFRS standards. This standard is effective for accounting periods beginning on or after January 1, 2013.

4 Critical accounting estimates and judgements

The preparation of the Corporation's financial statements, in conformity with IFRS, requires management of the Corporation to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. These estimates and judgments have been applied in a manner consistent with prior periods.

4 Critical accounting estimates and judgements (continued)

The following discusses the most significant accounting judgments and estimates that the Corporation has made in the preparation of the financial statements:

Impairment of goodwill and non-financial assets
The Corporation reviews goodwill at least annually and other non-financial assets when there is any indication that the asset might be impaired. The Corporation applies judgment in assessing the likelihood of renewal of significant contracts included in the intangible assets described in note 7. The Corporation has estimated the value in use and fair value of CGUs to which goodwill is allocated using discounted cash flow models that required assumptions about future cash flows, margins, and discount rates. Refer to Note 8 for more details about methods and assumptions used in estimating net recoverable amount.

Recognition of Rebate Liabilities
In applying its accounting policy for volume rebates, the Corporation must determine whether the processing volume thresholds will be achieved. The most difficult and subjective area of judgment is whether a contract will generate satisfactory volume to achieve minimum levels. Management considers all appropriate facts and circumstances in making this assessment including historical experience, current volumetric run-rates, and expected future events.

Linen in Service
The estimates are reviewed at least annually and are updated if expectations change as a result of physical wear and tear, technical or commercial obsolescence and legal or other limits of use. Linen in service is amortized across its estimated service life of 24 months and general linen is amortized based on usage which results in an estimated average service life of 24 months.

Management regularly evaluates these estimates and assumptions. 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.

5 Business Acquisitions

On June 30, 2011, the Corporation completed the acquisition of a laundry business, certain working capital and equipment of a processing plant located in Montréal, Québec from Les Buanderies Pierre R. Dextraze Inc. ("Dextraze"). The acquired business consisted of contracts with hospitality customers in Montréal and surrounding suburbs in Québec which complemented the existing business of the Corporation. The business acquisition has been accounted for using the acquisition method, whereby the purchase consideration was allocated to the fair values of the net assets acquired. The acquisition was funded through the Corporation's revolving credit facility.

The purchase price allocated to the net assets acquired, based on their estimated fair values, was as follows:

($ Thousands)	June 30, 2012
Cash consideration[1]	4,317
Net assets acquired:	
Working capital, net	332
Property, plant & equipment	2,445
Intangible assets	769
Future income tax liabilities	(52)
Goodwill	823
	4,317

[1] Of the cash consideration payable, $632 was deposited with an escrow agent to be released to the vendor upon the confirmation that certain representations and warranties are satisfied and earnings targets are achieved within the 12-24 month period subsequent to the acquisition. As of June 30, 2012 the earnings targets were achieved and the contingent consideration was paid in full.

As part of the acquired working capital, the Corporation received various accounts receivable which when valued at fair value of $548 was equivalent to their exchange amounts. All acquired accounts receivable were subsequently collected.

Intangible assets acquired are made up of customer contracts along with related relationships and customer lists. Goodwill acquired in the transaction arises from the efficiencies and synergies created between the existing business of the Corporation and the acquired assets. Of the acquired goodwill in the transaction $771 is deductible for tax purposes.

Annualized figures of the acquired business as if the acquisition had taken place at the beginning of the year have not been presented for the year ended December 31, 2011 as the Corporation and Dextraze have different fiscal periods and the Corporation does not have access to the necessary information.

6 Property, plant and equipment

($ Thousands)	Land	Buildings	Laundry Equipment[1]	Office Equipment	Delivery Equipment	Computer Equipment	Leasehold Improvements	Spare Parts	Total
Year ended, December 31, 2011									
Opening net book amount	70	461	25,009	219	790	63	6,733	512	33,857
Additions	-	-	2,331	56	10	73	197	180	2,847
Acquisition of business	55	720	1,616	18	-	36	-	-	2,445
Disposals	-	-	(43)	(3)	(69)	(1)	-	-	(116)
Depreciation charge	-	(59)	(4,385)	(90)	(90)	(71)	(1,243)	-	(5,938)
Closing net book amount	125	1,122	24,528	200	641	100	5,687	692	33,095
At December 31, 2011									
Cost	125	1,275	46,712	602	955	1,543	11,437	692	63,341
Accumulated depreciation	-	(153)	(22,184)	(402)	(314)	(1,443)	(5,750)	-	(30,246)
Net book amount	125	1,122	24,528	200	641	100	5,687	692	33,095
Year ended, December 31, 2012									
Opening net book amount	125	1,122	24,528	200	641	100	5,687	692	33,095
Additions	-	103	12,249	15	-	95	107	81	12,650
Disposals	-	-	(184)	-	(34)	(2)	-	-	(220)
Depreciation charge	-	(85)	(4,737)	(63)	(90)	(88)	(1,287)	-	(6,350)
Closing net book amount	125	1,140	31,856	152	517	105	4,507	773	39,175
At December 31, 2012									
Cost	125	1,377	58,637	617	913	1,636	11,544	773	75,622
Accumulated depreciation	-	(237)	(26,781)	(465)	(396)	(1,531)	(7,037)	-	(36,447)
Net book amount	125	1,140	31,856	152	517	105	4,507	773	39,175

[1] Included in additions to laundry equipment are assets under development in the amount of $5,787. These assets are not available for service and accordingly are not presently being depreciated.

7 Intangible assets

($ Thousands)	Healthcare Contracts	Hospitality Contracts	Computer Software	Total
Year ended, December 31, 2011				
Opening net book amount	9,636	4,819	744	15,199
Acquisition of business	-	769	-	769
Amortization charge	(1,616)	(827)	(185)	(2,628)
Closing net book amount	8,020	4,761	559	13,340
At December 31, 2011				
Cost	19,200	8,366	923	28,489
Accumulated amortization	(11,180)	(3,605)	(364)	(15,149)
Net book amount	8,020	4,761	559	13,340
Year ended, December 31, 2012				
Opening net book amount	8,020	4,761	559	13,340
Amortization charge	(1,251)	(891)	(185)	(2,327)
Closing net book amount	6,769	3,870	374	11,013
At December 31, 2012				
Cost	19,200	8,366	923	28,489
Accumulated amortization	(12,431)	(4,496)	(549)	(17,476)
Net book amount	6,769	3,870	374	11,013

8 Goodwill

The Corporation performed its annual assessment for goodwill impairment as at December 31, 2012 in accordance with its policy described in Note 2(k). Goodwill has been allocated to the following CGUs:

($ Thousands)	**2012**	2011
Edmonton	4,346	4,346
Calgary	5,382	5,382
Vancouver 1	2,630	2,630
Victoria	3,208	3,208
Québec	654	654
Vancouver 2	3,413	3,413
Montréal	823	823
Total	20,456	20,456

In assessing goodwill for impairment at December 31, 2012, the Corporation determined that: the assets and liabilities of the Corporation have not changed significantly from the prior year at December 31, 2011; the estimated recoverable amounts of the CGUs exceeded their carrying amounts by a significant amount; no events or circumstances have changed; and, the likelihood of an impairment in goodwill is remote. It was therefore appropriate to continue to rely on the quantitative analysis performed at December 31, 2011.

In performing that analysis, estimated recoverable amounts were determined based on the value in use of the CGUs using available cash flow budgets that made maximum use of observable markets for inputs and outputs, including actual historical performance. For periods beyond the budgeted period, cash flows were extrapolated using growth rates that did not exceed the long-term averages for the business. Key assumptions included a weighted average growth rate of 2% and a pre-tax discount rate of 17% for all CGUs.

The fair value of each CGU was significantly in excess of its carrying amount. Based on sensitivity analysis, no reasonably possible change in key assumptions would cause the carrying amount of any CGU to exceed its recoverable amount. The total recoverable amount for all CGU's exceeded their carrying amount by $77,375.

9 Long-term debt

($ Thousands)	Bankers Acceptances[1]	Prime Rate Loan[2]	Total Long Term Debt
At January 1, 2011	4,000	6,763	10,763
New debt advanced for acquisition	-	4,317	4,317
Repayment of debt	-	(8,985)	(8,985)
Closing Balance at December 31, 2011	4,000	2,095	6,095
Current portion of long-term debt	-	-	-
Non-current portion of long-term debt	4,000	2,095	6,095
At January 1, 2012	4,000	2,095	6,095
Repayment of debt	-	(277)	(277)
Closing Balance at December 31, 2012	4,000	1,818	5,818
Current portion of long-term debt	-	-	-
Non-current portion of long-term debt	4,000	1,818	5,818

[1] Banker's Acceptances bear interest at 30 day BA rates plus 2.5% depending on certain financial ratios, renewable monthly until July 31, 2014. As at December 31, 2012, the interest rate was 3.7%.

[2] Prime rate loan, collateralized by a general security agreement, interest at prime plus 1.0% depending on certain financial ratios, monthly repayment of interest only, maturing on July 31, 2014. As at December 31, 2012, the interest rate was 4.0%.

The Corporation has a revolving credit facility of up to $40,000 of which $6,218 is drawn (including letters of credit totaling $400 per Note 13(a)) as at December 31, 2012. The agreement is a committed facility maturing on July 31, 2014. Interest payments only are due during the term of the facility.

A general security agreement over all assets, a mortgage against all leasehold interests and real property, insurance policies and an assignment of material agreements have been pledged as collateral.

Drawings under the revolving credit facility are available by way of Bankers' Acceptances, Canadian prime rate loans, letters of credit or standby letters of guarantee. Drawings under the revolving credit facility bear interest at a floating rate, plus an applicable margin based on certain financial performance ratios.

The Corporation has incurred no events of default under the terms of its credit facility agreement.

10 Financial charges

($ Thousands)	2012	2011
Interest on long-term debt	94	274
Other charges, net	263	138
	357	412

11 Unamortized lease inducements

The Corporation entered into a long-term lease that included certain lease inducements consisting of a tenant allowance and a rent-free period. Tenant allowances are deferred when credited or received and amortized on a straight-line basis as a reduction of rent expense over the term of the related lease. For lease contracts with escalating lease payments, total rent expense for the lease term is expensed on a straight-line basis over the lease term. The difference between rent expensed and amounts paid is recorded as an increase or deferral in unamortized lease inducements.

($ Thousands)	2012	2011
Lease inducements received	699	699
Accumulated amortization, net	(187)	(133)
	512	566
Less current portion, included in accrued liabilities	(97)	(54)
	415	512

12 Income taxes

A reconciliation of the expected income tax expense to the actual income tax expense is as follows:

($ Thousands)	2012	2011
Current tax:		
Current tax on profits for the year	3,981	1,862
Total current tax	3,981	1,862
Deferred tax:		
Origination and reversal of temporary differences	222	1,136
Impact of change in substantively enacted tax rate	(28)	(38)
Total deferred tax	194	1,098

The tax on the Corporation's earnings differs from the theoretical amount that would arise using the weighted average tax rate applicable to losses of the consolidated entities as follows:

($ Thousands)	2012	2011
Earnings before income taxes	15,324	10,888
Non-deductable expenses	951	293
Income subject to tax	16,275	11,181
Income tax at statutory rate of 25.3% (2011 - 26.9%)	4,118	3,003
Impact of substantively enacted rates and other	57	(43)
Income tax expense	4,175	2,960

The decrease in the statutory rate from 2011 to 2012 is due to a previously legislated decrease in the federal statutory corporate income tax rates.

12 Income taxes (continued)

The analysis of the deferred tax assets and deferred tax liabilities is as follows:

($ Thousands)	2012	2011
Deferred tax assets:		
Deferred tax asset to be recovered after more than 12 months	(184)	(358)
Deferred tax asset to be recovered within 12 months	(152)	(267)
	(336)	(625)
Deferred tax liabilities:		
Deferred tax liability to be recovered after more than 12 months	2,950	2,725
Deferred tax liability to be recovered within 12 months	2,176	2,496
	5,126	5,221
Deferred tax liabilities, net	4,790	4,596

The movement of deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdictions, is as follows:

($ Thousands)	Accounts payable and accrued liabilities	Offering costs and other	Total
Deferred tax assets			
At January 1, 2011	(535)	(240)	(775)
Charged to the statement of earnings	1	149	150
At December 31, 2011	(534)	(91)	(625)
Charged to the statement of earnings	276	13	289
At December 31, 2012	(258)	(78)	(336)

($ Thousands)	Linen in service	Property, plant and equipment	Intangible assets and Goodwill	Total
Deferred tax liabilities				
At January 1, 2011	620	1,095	2,506	4,221
Charged (credited) to the statement of earnings	1,381	(12)	(421)	948
Acquisition of subsidiary	-	-	52	52
At December 31, 2011	2,001	1,083	2,137	5,221
Charged (credited) to the statement of earnings	159	59	(313)	(95)
At December 31, 2012	2,160	1,142	1,824	5,126

13 Contingencies and commitments

a) Contingencies - Letters of credit

The Corporation has standby letters of credit issued as part of normal business operations in the amount of $400 (2011 – $250) which will remain outstanding for an indefinite period of time.

b) Commitments

i) Operating leases and utility commitments

Minimum lease payments for operating leases on buildings and equipment and estimated natural gas and electricity commitments for the next five calendar years are as follows:

(Thousands)	$
2013	4,160
2014	4,234
2015	3,693
2016	3,323
Subsequent	15,691
	31,101

ii) Linen purchase commitments

At December 31, 2012, the Corporation was committed to linen expenditure obligations in the amount of $2,551 (2011 – $1,672) to be incurred over the next twelve months.

iii) Capital equipment commitments

At December 31, 2012, the Corporation was committed to capital expenditure obligations in the amount of $20,332 (2011 – $2,135) to be incurred over the next twelve months.

14 Share Capital

a) Authorized

The Corporation is authorized to issue an unlimited number of Common shares and such number of shares of one class designated as Preferred Shares which number shall not exceed 1/3 of the Common shares issued and outstanding from time to time.

b) Issued and outstanding

	December 31, 2012	
	Shares (#)	Capital ($ Thousands)
Common shares		
Balance, beginning of year	7,006,365	71,400
Issued under LTI	48,842	1,178
Issued under LTI, unvested	(36,626)	(853)
	7,018,581	71,725
Capital held in LTI trust		
Balance, beginning of year	-	(1,907)
Change during the year	-	1,626
	-	(281)
Total Share Capital	**7,018,581**	**71,444**

c) Weighted average number of shares outstanding

	2012	2011
Balance, beginning of year	7,006,365	7,006,365
Weighted average unvested shares purchased for LTI	(24,933)	(87,410)
Basic weighted average shares for the year	6,981,432	6,918,955
Basic weighted average shares for the year	6,981,432	6,918,955
Dilutive effect of LTI shares	12,129	61,534
Fully diluted weighted average shares for the year	6,993,561	6,980,489

15 Long-Term Incentive Plan

A trust was formed to hold equity grants issued under the terms of the LTIP on behalf of the participants (the "LTIP Trust"). The Corporation is neither a trustee nor a direct participant of the LTIP; however, under certain circumstances the Corporation may be the beneficiary of forfeited Common shares held by the LTIP Trust. Consequently, the LTIP Trust is considered a variable interest entity for accounting purposes and the Corporation has consolidated the LTIP Trust in accordance with IFRS 2, Share-based Payment. Compensation expense is recorded by the Corporation in the period earned. Dividends paid by the Corporation with respect to unvested Common shares held by the LTIP Trust are paid to LTIP participants. Unvested Common shares held by the LTIP Trust are shown as a reduction of shareholders' equity.

	2012		2011	
	Unvested	**Vested**	Unvested	Vested
Balance, beginning of year	74,511	168,466	114,074	115,780
Issued during year	36,626	12,216	11,566	1,557
Vested during year	(62,946)	62,946	(51,129)	51,129
Balance, end of year	48,191	243,628	74,511	168,466

The cost of the 48,191 (2011 - 74,511) unvested Common shares held in trust by the LTIP at December 31, 2012 was $281 (2011 - $1,252).

The basic net earnings per unit calculation exclude the unvested Common shares held by the LTIP Trust.

16 Dividends to Shareholders

During the year ended December 31, 2012, the Corporation declared total dividends to Shareholders of $7,977 or $1.13 per share (2011 - $7,706 or $1.10 per share).

The Corporation's policy is to pay dividends to Shareholders of its available cash to the maximum extent possible consistent with good business practice considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Directors of the Corporation. All such dividends are discretionary. Dividends are declared payable each month to the Shareholders on the last business day of each month and are paid by the 15th day of the following month.

17 Net change in non-cash working capital items

($ Thousands)	**2012**	2011
Accounts receivable	705	(1,002)
Linen in service	(706)	(309)
Prepaid expenses and deposits	379	(620)
Accounts payable and accrued liabilities	(1,357)	(345)
Income taxes payable	558	1,857
	(421)	(419)

18 Financial Instruments

a) Fair value

The Corporation's financial instruments at December 31, 2012 consist of accounts receivable, accounts payable and accrued liabilities, dividends payable and long-term debt. The carrying value of accounts receivable, accounts payable and accrued liabilities, and dividends payable to Shareholders approximate fair value due to the immediate or short-term maturity of these financial instruments. The fair value of the Corporation's interest-bearing debt approximates the respective carrying amount due to the floating rate nature of the debt.

b) Financial risk management

The Corporation's activities are exposed to a variety of financial risks: price risk, credit risk and liquidity risk. The Corporation's overall risk management program focuses on the unpredictability of financial and economic markets and seeks to minimize potential adverse effects on the Corporation's financial performance. Risk management is carried out by financial management in conjunction with overall corporate governance.

c) Price risk

i) Currency risk

Foreign currency risk arises from the fluctuations in foreign exchange rates and the degree of volatility of these rates relative to the Canadian dollar. The Corporation is not significantly exposed to foreign currency risk as all revenues are received in Canadian dollars and minimal expenses are incurred in foreign currencies. For large capital expenditure commitments denominated in a foreign currency, the Corporation will enter into foreign exchange forward contracts if considered prudent to mitigate this risk. At December 31, 2012, one foreign exchange forward option contract was outstanding for the purchase of $7,000 USD.

ii) Interest rate risk

The Corporation is subject to interest rate risk as its credit facility bears interest at rates that depend on certain financial ratios of the Corporation and vary in accordance with market interest rates. Based on the outstanding balance on the Corporation's revolving credit facility, a 1% increase in the Canadian prime rate would result in an additional $58 in annual interest expense.

iii) Other price risk

The Corporation's exposure to other price risk is limited since there are no significant financial instruments which fluctuate as a result of changes in market prices.

d) Credit risk

The Corporation's financial assets that are exposed to credit risk consist of accounts receivable. The Corporation, in the normal course of business, is exposed to credit risk from its customers. The allowance for doubtful accounts and past due receivables are reviewed by management at each balance sheet reporting date. Any amounts greater than 60 days are considered overdue and all impaired amounts have been fully allowed for as at December 31, 2012.

The Corporation updates its estimate of the allowance for doubtful accounts based on the evaluation of the recoverability of accounts receivable balances of each customer taking into account historic collection trends, the contractual relationship with the customer and the nature of the customer which in many cases is a publicly funded health care entity.

Management believes that the risks associated with concentrations of credit risk with respect to accounts receivable are limited due to the nature of the customers and the generally short payment terms.

The aging of the Corporation's receivables and related allowance for doubtful accounts are:

($ Thousands)	Gross	Allowance	Net
December 31, 2011			
Current	9,088	-	9,088
31-60 days	4,935	-	4,935
Greater than 60 days	927	48	879
	14,950	48	14,902
December 31, 2012			
Current	10,486	-	10,486
31-60 days	3,589	-	3,589
Greater than 60 days	152	30	122
	14,227	30	14,197

While the Corporation evaluates a customer's credit worthiness before credit is extended, provisions for potential credit losses are also maintained. The change in allowance for doubtful accounts was as follows:

($ Thousands)	2012	2011
Balance, beginning of year	48	42
Adjustments made during the year	-	87
Write-offs	(18)	(81)
Balance, end of year	30	48

e) Liquidity risk

The Corporation's accounts payable and dividend payable are due within one year.

The Corporation has a credit facility with a maturity date of July 31, 2014 (Note 9). The degree to which the Corporation is leveraged may reduce its ability to obtain additional financing for working capital and to finance investments to maintain and grow the current levels of cash flows from operations. The Corporation may be unable to extend the maturity date of the credit facility.

Management, to reduce liquidity risk, has historically renewed the terms of the credit facility in advance of its maturity dates and the Corporation has maintained financial ratios that management believes are conservative compared to financial covenants applicable to the credit facility. A significant portion of the available facility remains undrawn.

Management measures liquidity risk through comparisons of current financial ratios with financial covenants contained in the credit facility

19 Capital management

The Corporation views its capital resources as the aggregate of its debt, shareholders' equity and amounts available under its credit facility. In general, the overall capital of the Corporation is evaluated and determined in the context of its financial objectives and its strategic plan.

The Corporation's objective in managing capital is to ensure sufficient liquidity to pursue its growth and expansion strategy, while taking a conservative approach towards financial leverage and management of financial risk. The Corporation's capital is composed of shareholders' equity and long-term debt. The Corporation's primary uses of capital are to finance its growth strategies and capital expenditure programs. The Corporation currently funds these requirements from internally-generated cash flows and interest bearing debt.

The Corporation pays a dividend which reduces its ability to internally finance growth and expansion. However the availability of the Corporation's revolving line of credit provides sufficient access to capital to allow K-Bro to take advantage of acquisition opportunities. The merits of the dividend are periodically evaluated by the Board.

The primary measures used by the Corporation to monitor its financial leverage are the ratios of Funded Debt to EBITDA (earnings before income taxes, depreciation and amortization) and Fixed Charge Coverage. EBITDA is an additional GAAP measure as prescribed by IFRS and has been presented in the manner in which the chief operating decision maker assesses performance.

The Corporation manages a Funded Debt to EBITDA ratio calculated as follows:

($ Thousands)	**2012**	2011
Long-term debt, including current portion	5,818	6,095
Issued and outstanding letters of credit	400	250
Funded debt	6,218	6,345
Net earnings for the trailing twelve months	11,149	7,928
Add:		
Income tax expense	4,175	2,960
Financial charges	357	412
Depreciation of property, plant and equipment	6,350	5,938
Amortization of intangible assets	2,327	2,628
Loss on disposal of property, plant and equipment	159	80
EBITDA	24,517	19,946
Funded debt to EBITDA	0.25x	0.32x

The Corporation manages a Fixed Charge Coverage calculated on a trailing twelve-month basis as follows:

($ Thousands)	**2012**	2011
EBITDA	24,517	19,946
Financial charges	357	412
Dividends to shareholders	7,977	7,706
	8,334	8,118
Fixed charge coverage	2.9x	2.5x

20 Related party transactions

The Corporation transacts with key individuals from management and with the Board who have authority and responsibility to plan, direct and control the activities of the Corporation. The nature of these dealings were in the form of payments for services rendered in their capacity as Directors (retainers and meeting fees, including share-based payments) and as employees of the Corporation (salaries, benefits, short-term bonuses and share-based payments).

Key management personnel are defined as the executive officers of the Corporation including the President and Chief Executive Officer, Senior Vice-President and General Manager, Vice-President and Chief Financial Officer and three employees acting in the capacity of General Manager.

During 2012 and 2011, remuneration to directors and key management personnel was as follows:

($ Thousands)	**2012**	2011
Salaries and retainer fees	1,702	1,593
Short-term bonus incentives	750	585
Post-employment benefits	47	46
Unit-based payments	943	1,497
	3,442	3,721

The Corporation incurred expenses in the normal course of business for advisory consulting services provided by a Director primarily relating to acquisitions. The amounts charged are included as salaries and retainer fees. For the year ended December 31, 2012, the Corporation incurred such fees totaling $138 (2011 – $138).

21 Expense by nature

($ Thousands)	**2012**	2011
Wages and benefits	61,831	58,194
Linen	12,706	12,031
Utilities	8,276	8,688
Delivery	5,583	4,900
Repairs and maintenance	3,832	3,843
Occupancy costs	4,012	3,915
Materials and supplies	5,346	5,103
Other expenses	187	239
	101,773	96,913

22 Segmented information

The Corporation provides laundry and linen services to the healthcare and hospitality sectors through eight operating divisions located in Vancouver, Victoria, Calgary, Edmonton, Toronto, Montréal, and Québec City. The services offered and the economic characteristics associated with these divisions are similar, therefore they have been aggregated into one reportable segment which operates exclusively in Canada. The earnings of the acquired Montréal division (Note 5) were reported commencing July 1, 2011.

In Edmonton, the Corporation is the significant supplier of laundry and linen services to the entity which manages all major healthcare facilities in the region. This contract currently expires on March 31, 2013; this contract has been renegotiated for a 10 year term expiring March 31, 2023. In Calgary, the major customer is contractually committed to February 28, 2018 and in Vancouver the major customer is contractually committed to November 12, 2015. For the year ended December 31, 2012, the Corporation has recorded revenue of $59,531 (2011 – $54,743) from these three major customers, representing 47% (2011 – 47%) of total revenue.

	2012		2011	
Healthcare	86,610	68.6%	80,145	68.6%
Hospitality	39,680	31.4%	36,714	31.4%
	126,290	100.0%	116,859	100%

23 Subsequent events

The Corporation's Board of Directors declared an eligible dividend of $0.0958 per Common share of the Corporation payable on each of February 15, March 15 and April 15 to Shareholders of record on January 31, February 28, and March 31, respectively.

24 Comparative figures

Certain of the comparative figures have been adjusted to be consistent with the current period presentation.

Corporate information

CORPORATE OFFICE

103, 15023 – 123 Avenue
Edmonton, Alberta T5V 1J7
Phone 780.453.5218
Fax 780.455.6676
inquiries@k-brolinen.com
www.k-brolinen.com

BOARD OF DIRECTORS

Ross Smith, FCA (Chair)
Corporate Director

Matthew Hills, MBA
Managing Director
LLM Capital Partners LLC

Steven Matyas, BSc
President
Staples Canada Inc.

Michael Percy, PhD
Professor, School of Business
University of Alberta

Linda McCurdy, MBA
President & Chief Executive Officer
K-Bro Linen Systems Inc.

EXECUTIVE OFFICERS

Linda McCurdy, MBA
President & Chief Executive Officer

Sean Curtis
Senior Vice-President &
General Manager (Edmonton)

Christopher Burrows
Vice-President & Chief Financial Officer

VICTORIA PLANT

861 Van Isle Way
Victoria, British Columbia V9B 5R8
Phone 250.474.5699
Fax 250.474.5680

Kevin Stephenson
General Manager

Andrew Mackeen
Plant Manager

VANCOUVER 1 PLANT

8035 Enterprise Street
Burnaby, British Columbia V5A 1V5
Phone 604.420.2203
Fax 604.420.2313

Ron Graham
General Manager

Kevin McElgunn
Operations Manager

VANCOUVER 2 PLANT

4590 Canada Way
Burnaby, British Columbia V5G 1J6
Phone 604.681.3291
Fax 604.685.1458

Ken Chu
General Manager

John Truong
Operations Manager

CALGARY PLANT

6969 – 55 Street SE
Calgary, Alberta T2C 4Y9
Phone 403.724.9001
Fax 403.720.2959

Jeff Gannon
General Manager

Sean Jackson
Operations Manager

EDMONTON PLANT

15253 – 121A Avenue
Edmonton, Alberta T5V 1N1
Phone 780.451.3131
Fax 780.452.2838

Sean Curtis
Senior Vice-President &
General Manager

Trevor Rye
Operations Manager

TORONTO PLANT

15 Shorncliffe Road
Toronto, Ontario M9B 3S4
Phone 416.233.5555
Fax 416.233.4434

Jerry Ostrzyzek
General Manager

Michael Beach
Operations Manager

QUÉBEC PLANT

367 Boulevard Des Chutes
Québec City, Québec G1E 3G1
Phone 418.661.6163
Fax 418.661.4000

Maxim Lortie
Directeur Général

Jessica Lévesque
Directrice des Opérations

MONTRÉAL PLANT

599, rue Simonds Sud
Granby, Québec J2J 1C1
Phone 450.378.3187
Fax 450.378.8245

Stany Bergeron
Directrice Générale

Eric Ouellette
Directeur Général

TRANSFER AGENT AND REGISTRAR

Valiant Trust Company
Calgary, Alberta

AUDITORS

PricewaterhouseCoopers LLP
Edmonton, Alberta

LEGAL COUNSEL

Goodmans LLP, *Toronto*
Bennett Jones LLP, *Edmonton*

PRINCIPAL BANK

TD Bank, *Edmonton*

STOCK EXCHANGE LISTING

TSX: KBL

NOTICE OF ANNUAL MEETING

The annual meeting of Shareholders will be held at the **Sheraton Centre Hotel**, **Kenora Room**, 123 Queen Street West, Toronto, Ontario, Canada on **June 18, 2013** at **1:00pm EDT**

K-Bro Linen Inc.