EcoSynthetix Inc.

Consolidated Financial Statements

December 31, 2012 and December 31, 2011

(expressed in US dollars)

March 5, 2013

Independent Auditor's Report

To the Shareholders of
EcoSynthetix Inc.

We have audited the accompanying consolidated financial statements of and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2012 and December 31, 2011 and the consolidated statements of operations and comprehensive loss, shareholders' equity (deficiency) 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 EcoSynthetix 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.

(Signed) "PricewaterhouseCoopers LLP"

Chartered Accountants, Licensed Public Accountants
Toronto, Ontario

EcoSynthetix Inc.

Consolidated Balance Sheets

At December 31

(expressed in US dollars)

	2012	2011
Assets		
Current assets		
Cash	93,260,296	105,713,705
Accounts receivable (note 5)	4,309,355	3,116,445
Inventory (note 6)	6,822,619	10,243,410
Government grants receivable (note 7)	184,118	639,685
Prepaid expenses	154,492	182,842
	104,730,880	119,896,087
Non-current assets		
Intangible assets (note 8)	163,501	-
Property, plant and equipment (note 9)	13,174,416	10,766,124
Total assets	118,068,797	130,662,211
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 10)	4,282,296	6,142,668
Deferred government grant (note 7)	226,920	-
Total liabilities	4,509,216	6,142,668
Shareholders' Equity		
Common shares (note 14)	492,065,820	492,353,321
Contributed surplus	6,831,354	6,073,080
Accumulated deficit	(385,337,593)	(373,906,858)
Total shareholders' equity	113,559,581	124,519,543
Total shareholders' equity and liabilities	118,068,797	130,662,211

Approved by the Board of Directors

(Signed) John van Leeuwen, Director

(Signed) John E. Barker, Director

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

EcoSynthetix Inc.

Consolidated Statements Operations and Comprehensive Loss

For the years ended December 31

(expressed in US dollars, unless otherwise noted)

	2012	2011
Net sales	19,552,345	20,769,851
Cost of sales	15,694,487	15,796,830
Gross profit on sales	3,857,858	4,973,021
Expenses		
Selling, general and administrative	11,266,518	8,518,299
Research and development	4,382,854	2,516,360
	15,649,372	11,034,659
Loss from operations	(11,791,514)	(6,061,638)
Interest income	360,779	183,027
Loss related to change in value of warrants and redeemable preferred shares (note 11)	-	(246,829,537)
Net loss and comprehensive loss	(11,430,735)	(252,708,148)
Basic and diluted loss per common share (note 19)	(0.21)	(10.93)
Weighted average number of common shares outstanding (note 19)	55,288,432	23,125,647

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

EcoSynthetix Inc.

Consolidated Statements of Shareholders' Equity (Deficiency)

For the years ended December 31

(expressed in US dollars)

	Common shares	Equity component of redeemable preferred shares	Contributed surplus	Accumulated deficit	Total
Balance - January 1, 2011	143,213	19,793,287	2,180,570	(121,198,710)	(99,081,640)
Issuance of common shares - net of share issuance costs	91,658,551	-	-	-	91,658,551
Conversion of preferred shares and warrants	400,055,391	(19,793,287)	3,265,161	-	383,527,265
Warrants exercised	334,649	-	(305,155)	-	29,494
Common share options exercised	161,517	-	(51,821)	-	109,696
Share-based compensation	-	-	984,325	-	984,325
Net loss and comprehensive loss	-	-	-	(252,708,148)	(252,708,148)
Balance - December 31, 2011	492,353,321	-	6,073,080	(373,906,858)	124,519,543
Balance - January 1, 2012	492,353,321	-	6,073,080	(373,906,858)	124,519,543
Common share options exercised	234,228	-	(88,830)	-	145,398
Common shares repurchased	(521,729)			-	(521,729)
Share-based compensation	-	-	847,104		847,104
Net loss and comprehensive loss	-	-	-	(11,430,735)	(11,430,735)
Balance - December 31, 2012	492,065,820	-	6,831,354	(385,337,593)	113,559,581

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

EcoSynthetix Inc.

Consolidated Statements of Cash Flows

For the years ended December 31

(expressed in US dollars)

	2012	2011
Cash provided by (used in)		
Operating activities		
Net loss	(11,430,735)	(252,708,148)
Items not affecting cash		
Depreciation and amortization	1,207,584	583,380
Share-based compensation (note 13)	847,104	984,325
Change in value of warrants and redeemable preferred shares	-	246,829,537
Changes in non-cash working capital		
Accounts receivable	(1,192,910)	(376,875)
Inventory	3,535,225	(8,055,027)
Government grants receivable (note 7)	455,567	334,066
Prepaid expenses	28,350	(101,753)
Accounts payable and accrued liabilities	(6,120)	226,620
Accrued compensation	-	(1,005,371)
Deferred government assistance	(10,080)	(486,961)
	(6,566,015)	(13,776,207)
Investing activities		
Purchase of intangible assets and property and equipment (notes 8 and 9)	(5,748,063)	(10,012,325)
Financing activities		
Common share issuance costs (note 14)	-	(10,792,531)
Issuance of common shares (note 14)	-	102,451,082
Repurchase of common shares	(521,729)	-
Exercise of share options	145,398	109,696
Exercise of common share warrants	-	29,494
Increase in government grant (note 7)	237,000	2,511,459
	(139,331)	94,309,200
(Decrease) increase in cash during the year	(12,453,409)	70,520,668
Cash - Beginning of year	105,713,705	35,193,037
Cash - End of year	93,260,296	105,713,705
Non-cash financing activities		
Conversion of redeemable preferred shares and related warrants to common shares (note 14)	-	383,527,263

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

(expressed in US dollars, unless otherwise noted)

1 Business operations

EcoSynthetix Inc. (EcoSynthetix or the company) is engaged in the development and commercialization of ecologically friendly, bio-based technologies as replacement solutions for synthetic, petrochemical-based adhesives and other related products in North America, Latin America, Europe, Middle East and Africa (EMEA), and Asia Pacific. EcoSynthetix is incorporated and domiciled in Canada. The address of its registered office is 3365 Mainway, Burlington, Ontario, Canada.

2 Summary of significant accounting policies

Statement of compliance

These consolidated financial statements have been authorized for issuance by the board of directors of the company on March 5, 2013.

Basis of preparation

The consolidated financial statements have been prepared under International Financial Reporting Standards (IFRS), using the historical cost convention, except that financial instruments at fair value through profit or loss (FVTPL) are measured at fair value, and liabilities for share-based payment arrangements are measured at fair value.

Use of estimates and judgments

The preparation of consolidated financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. These estimates are based on management's best knowledge of current events and actions that the company may undertake in the future. Actual results may differ from those estimates.

Significant estimates made by the company include estimates of share-based compensation, potentially uncollectible accounts receivable, provisions for inventory that are carried in excess of net realizable value, and the realizability of deferred income tax assets.

Basis of consolidation

The financial statements of the company consolidate the accounts of EcoSynthetix and all of its subsidiaries. All intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Subsidiaries are all entities controlled by the company.

(expressed in US dollars, unless otherwise noted)

Foreign currency translation

i) Functional and presentation currency

Items included in the financial statements of each consolidated entity in the company's consolidated financial statements are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in US dollars, which is the company's reporting currency. The functional currency of all entities is US dollars.

ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign currency exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in currencies other than an organization's functional currency are recognized in the consolidated statements of operations and comprehensive loss.

Cash

Cash consists of cash on hand and deposits held with banks.

Trade receivables

Trade receivables are amounts due from customers for products sold in the ordinary course of business. If collection is expected in one year or less, they are classified as current assets.

Trade receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less a provision for impairment.

Financial instruments

Financial assets and financial liabilities are recognized when the company becomes a party to the contractual provisions of the financial instrument. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or have been transferred and the company has transferred substantially all risks and rewards of ownership.

Financial assets and financial liabilities are offset and the net amount reported in the consolidated balance sheets when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the financial asset and settle the financial liability simultaneously.

(expressed in US dollars, unless otherwise noted)

At initial recognition, the company classifies its financial instruments in the following categories, depending on the purpose for which the financial instruments were acquired:

i) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The company's loans and receivables comprise account receivables, government grants and cash and cash equivalents and are classified as current, except for the portion expected to be realized or paid beyond 12 months of the consolidated balance sheet dates, which is classified as non-current. Loans and receivables are initially recognized at the amount expected to be received less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method, less a provision for impairment.

ii) Financial liabilities at amortized cost

Financial liabilities at amortized cost include trade payables and accrued liabilities. Trade and accrued liabilities are initially recognized at the amount required to be paid less, when material, a discount to reduce the payables to fair value. Subsequently, trade and accrued liabilities are measured at amortized cost, using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within 12 months. Otherwise, they are presented as non-current liabilities.

Impairment of financial assets

At each reporting date, the company assesses whether there is objective evidence that a financial asset is impaired. If such evidence exists, the company recognizes an impairment loss on financial assets carried at amortized cost as follows. The loss is the difference between the amortized cost of the receivable and the present value of the estimated future cash flows, discounted using the financial 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 years if the amount of the loss decreases and the decrease can be related objectively to an event's occurring after the impairment was recognized.

Inventory

Raw materials, work-in-process and finished goods are valued at the lower of cost, determined on a first-in, first-out basis, and net realizable value. Inventory costs include the costs of material, labour, variable overhead and an allocation of fixed manufacturing overhead, including depreciation based on normal production volumes. Net realizable value is the estimated selling price less applicable selling expenses.

(expressed in US dollars, unless otherwise noted)

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 asset. 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 company and the cost can be measured reliably. The carrying amount of a replaced asset is derecognized when replaced. Repairs and maintenance costs are charged to the consolidated statements of operations and comprehensive loss during the year in which they are incurred.

Depreciation is calculated on a straight-line method to reduce the cost of the asset to its residual value over its estimated useful life. The depreciation rates applicable to each category of property, plant and equipment are as follows:

Leasehold improvements	remaining lease term
Computer hardware	3 years
Machinery and equipment	2 to 15 years

Useful lives and residual values are reviewed and adjusted, if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals of property 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 consolidated statements of operations and comprehensive loss.

Intangible assets

Computer software costs are amortized on a straight-line basis over their estimated useful lives, which are approximately three years.

Impairment of non-financial assets

Property and equipment and intangible assets are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units or CGUs). 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. Non-financial assets that have been impaired previously are reviewed for possible reversal of impairment at each reporting date.

Provisions

Provisions are recognized when the company has a present legal or constructing obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the

(expressed in US dollars, unless otherwise noted)

amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period and are discounted to present value where the effect is material. The company performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

Redeemable preferred shares

The company's redeemable preferred shares are compound financial instruments. The liability component of the redeemable preferred shares is recognized initially at the fair value of a similar liability. The equity conversion option is recognized initially at the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts. In conjunction with the initial public offering (the offering) on August 4, 2011, the redeemable preferred shares and related warrants were automatically converted to common shares.

Research and product development costs

Expenditures during the research phase are expensed as incurred. Expenditures during the development phase are expensed as incurred, unless they meet the capitalization criteria of International Accounting Standard (IAS) 38, Intangible Assets. No development costs have been capitalized to date.

Government grants

Government grants include funding for government research and product development support. Research and product development funding is recognized when there is reasonable assurance that the company has complied with the conditions attached to the funding arrangement and is recognized as the applicable costs are incurred. Research and product development funding is presented as a reduction in research and product development expenses, unless it is for reimbursement of an asset, in which case, it is accounted for as a reduction in the carrying amount of the applicable asset.

Revenue recognition

Revenue is recognized when the company has transferred the significant risk and rewards of ownership of the goods to the buyer, it is probable that the economic benefits will flow to the company, delivery has occurred, and the amount of revenue and costs incurred or to be incurred can be measured realibly. These criteria are generally met at the time the product is shipped and risk and rewards have passed to the customer. Revenue is measured based on the price specified in the sales contract, net of discounts and estimated returns at the time of sale. Historical experience is used to estimate and provide for discounts and returns.

Cost of sales and gross profit

Our gross profit is derived from our net sales, less our cost of sales. Cost of sales includes raw material costs, contract manufacturing costs, freight costs and depreciation related to manufacturing equipment. Direct materials consist of the costs of cornstarch feedstock and process chemicals. Cost of sales is mainly affected by the cost of cornstarch and contract manufacturing costs. Cornstarch is the most significant raw material cost.

(expressed in US dollars, unless otherwise noted)

Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issuance of common shares are recognized as a deduction from shareholders' equity (deficiency). The company has classified all outstanding exchangeable shares of its subsidiaries as issued and outstanding of the parent company.

Share-based compensation

The company grants share options to certain employees, advisers and consultants. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value. The fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. Compensation expense is recognized over the tranche's vesting period, based on the number of awards expected to vest, by increasing contributed surplus. The number of awards expected to vest is reviewed at least annually, with any impact being recognized immediately. Any contribution paid by an employee or director on the exercise of share options is credited to common stocks with any previously recognized compensation expense.

Income taxes

Income taxes comprise current and deferred income taxes. Income taxes are recognized in the consolidated statements of operations and comprehensive loss, except to the extent that they relate to items recognized directly in shareholders' equity, in which case the income taxes are also recognized directly in shareholders' equity.

Current income taxes are the expected income taxes payable on the taxable income for the year, using income tax rates enacted or substantively enacted, at the end of the reporting period, and any adjustment to income taxes payable in respect of previous years.

In general, deferred income taxes are recognized in respect of temporary differences arising between the income tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income taxes are determined on a non-discounted basis using income tax rates and laws that have been enacted or substantively enacted at the consolidated balance sheet dates and are expected to apply when the deferred income tax asset or liability is settled. Deferred income tax assets are recognized to the extent that it is probable that the assets can be recovered.

Deferred income taxes are provided on temporary differences arising on investments in subsidiaries and associates, except, in the case of subsidiaries, where the timing of the reversal of the temporary difference is controlled by the company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are presented as non-current.

Loss per share

Basic loss per common share is calculated based on the weighted average number of common shares outstanding for the year. Diluted loss per common share is calculated using the weighted average number of

(expressed in US dollars, unless otherwise noted)

common shares outstanding for the year for basic net loss per common share plus the weighted average number of potential dilutive common shares that would have been outstanding during the year had potentially all common shares been issued at the beginning of the year or when the underlying share options or warrants were granted, if later, unless they were anti-dilutive.

Operating lease

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments under an operating lease (net of any incentives received from the lessor) are recognized in the consolidated statements of operations and comprehensive loss on a straight-line basis over the period of the lease.

Operating segments

The company operates in one operating segment and is reported in a manner consistent with the internal reporting provided to the chief operating decision-maker (CODM). The chief executive officer has authority for resource allocation and assessment of the company's performance and is, therefore, the CODM.

3 Risk management and financial instruments

The company has classified its financial instruments into one of the following categories: loans and receivables; and other financial liabilities at amortized cost. The following table summarizes information regarding the carrying amounts of the company's financial instruments:

	2012	2011
Loans and receivables (i)	97,569,651	108,830,150
Other financial liabilities (ii) - amortized cost	4,509,216	6,142,668

i) Includes cash and cash equivalents and accounts receivable
ii) Includes financial liabilities included within accounts payable and accrued liabilities and deferred government grant.

Liquidity

The company has sustained losses and negative cash flows from operations since its inception. Liquidity risk is the risk that the company will encounter difficulty in meeting its financial obligations associated with financial liabilities that are settled by delivering cash or another financial asset. The company is exposed to liquidity risk as it continues to have net cash outflows to support its operations. The company's approach to managing liquidity risk is to ensure it will have sufficient liquidity to meet liabilities when due. The company achieves this by maintaining sufficient cash and cash equivalents. The company monitors its financial position on a monthly basis and updates its expected use of cash resources based on the latest available data. The company's accounts payable and accrued liabilities will be paid within the next 12 months.

(expressed in US dollars, unless otherwise noted)

Credit risk

Credit risk arises from the potential that a counterparty will fail to perform its obligations. The company is exposed to credit risk from customers. At December 31, 2012, the company's three largest customers accounted for 48% (2011 - two customers at 52%) of accounts receivable. In order to minimize the risk of loss for accounts receivable, the company's extension of credit to customers involves a review and approval by senior management. The majority of the company's sales are invoiced with payment terms between 20 and 90 days. The company's objective is to minimize its exposure to credit risk from customers in order to prevent losses on financial assets by performing regular monitoring of overdue balances and to provide an allowance for potentially uncollectible accounts receivable.

The company's accounts receivable have a carrying amount of $4,055,247 at December 31, 2012 (2011 - $2,510,783), representing the maximum exposure to credit risk of those financial assets, exclusive of the allowance for doubtful accounts. Normal credit terms for amounts due from customers call for payment within 20 to 90 days. An insignificant number of these receivables were past due at December 31, 2012. The company's exposure to credit risk for trade receivables by geographic area at December 31 was as follows:

	2012 %	2011 %
North America	23	29
Latin America	9	21
EMEA	14	7
Asia Pacific	54	43
	100	100

The company believes the credit quality is high for trade receivables, which are neither past due nor impaired, based on prior experience of collections of accounts within 0-90 days of billing.

The company may also have credit risk relating to cash, which it manages by dealing with large chartered Canadian and US banks. The company's objective is to minimize its exposure to credit risk in order to prevent losses on financial assets by placing its investments in lower risk deposits of these chartered banks. The company's cash carrying amount is $93,260,296 at December 31, 2012 (2011 - $105,713,705), representing the maximum exposure to credit risk of these financial assets. Approximately 75% (2011 - 99%) of the company's cash at December 31, 2012 was held by one financial institution. The company's exposure to credit risk relating to cash segmented by geographic area at December 31 was as follows:

	2012 %	2011 %
Canada	77.1	98.5
United States of America	22.7	1.0
The Netherlands	0.2	0.5
	100.0	100.0

(expressed in US dollars, unless otherwise noted)

Foreign currency risk

Foreign currency risk arises because of fluctuations in foreign currency exchange rates. The company conducts a portion of its business activities in currencies other than the functional currency of the parent company (US dollars). This primarily includes Canadian dollar and Euro denominated transactions. The company's objective in managing its foreign currency risk is to minimize its net exposure to foreign currency cash flows by converting foreign denominated financial assets into US dollars to the extent practical to match the obligations of its financial liabilities. Financial assets and financial liabilities denominated in foreign currencies will be affected by changes in the exchange rate between the functional currency and these foreign currencies. This primarily includes cash, accounts receivable and accounts payable and accrued liabilities, which are denominated in foreign currencies. The company recognized foreign currency exchange gains (losses) in the years ended December 31, 2012 and 2011 of ($42,066) and $36,501, respectively.

If a shift in the Canadian dollar relative to the US dollar of 10% were to occur, the foreign currency exchange gain or loss on the net financial assets could be plus or minus $25,128 (2011 - $34,084) due to exchange rate fluctuations and this amount would be recorded in the consolidated statements of operations and comprehensive loss.

If a shift in the euro relative to the US dollar of 10% were to occur, the exchange gain or loss on the net financial assets would not be significant.

Interest rate risk

Interest rate risk arises because of the fluctuation in market interest rates. The company's objective in managing interest rate risk is to maximize the return on its cash. The company is subject to interest rate risk on its cash. If a shift in interest rates of 10% were to occur, the impact on the consolidated statements of operations and comprehensive loss for the year is not significant.

Fair value

The carrying amounts of cash, accounts receivable and accounts payable and accrued liabilities approximate their fair values given their short-term nature.

Fair value measurement recognized in the consolidated balance sheets

Financial instruments that are measured at fair value are grouped into levels 1 to 3, based on the degree to which their fair value is observable.

- Level 1 - Fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical financial assets or financial liabilities.

- Level 2 - Fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the financial asset or financial liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

(expressed in US dollars, unless otherwise noted)

- Level 3 - Fair value measurements are those derived from valuation techniques that include inputs for the financial asset or financial liability that are not based on observable market data (unobservable inputs).

The company's financial assets and liabilities at fair value as at December 31, 2012 were as follows:

	Level 1 $	Level 2 $	Level 3 $	Total $
Cash and cash equivalents	-	93,260,296	-	93,260,296
Accounts receivable	-	4,309,355	-	4,309,355
Accounts payable and accrued liabilities	-	4,282,296	-	4,282,296
Government grant receivable	-	184,118	-	184,118
	-	102,036,065	-	102,036,065

4 Capital management

The company's objective in managing capital is to ensure sufficient liquidity to pursue its growth strategy, fund research and product development, while at the same time, taking a conservative approach toward financial leverage and management of financial risk. The company's capital is composed of the net cash received related to common shares, warrants and shareholder option exercises. The total capital at December 31, 2012 is $158,582,896 (2011 - $158,959,227). The company's primary uses of capital are financing operations, increasing non-cash working capital and capital expenditures. The company currently funds these requirements from existing cash resources and cash raised through share issuances. The company's objectives when managing capital are to ensure the company will continue to have enough liquidity so that it can provide its products and services to its customers and returns to its shareholders. The company monitors its capital on the basis of the adequacy of its cash resources to fund its business plan. In order to maximize the capacity to finance the company's ongoing growth, the company does not currently pay a dividend to holders of its common shares.

5 Accounts receivable

	2012	2011
Trade accounts receivable - net	4,055,247	2,510,783
Commodity taxes receivable and other	254,108	605,662
	4,309,355	3,116,445

The company has recorded no provision for bad debts at December 31, 2012 (2011 - $82,126).

(expressed in US dollars, unless otherwise noted)

The aging of accounts receivable at each reporting date was as follows:

	2012	2011
Current	3,180,662	2,671,616
Past due 1-30 days	981,031	357,782
Past due 31-60 days	1,035	34,309
Past due 61-90 days	138	6,498
Past due greater than 91 days	146,489	46,240
Balance at December 31	4,309,355	3,116,445

6 Inventory

	2012	2011
Raw materials	1,118,460	994,440
Finished goods	5,704,159	9,248,970
	6,822,619	10,243,410

7 Government grants

The company has a forgivable loan agreement with the Province of Ontario under its Innovation Demonstration Fund Program (Ontario) (IDF), pursuant to which, Ontario will provide a forgivable loan up to a maximum of approximately $3.1 million for a specific technology demonstration project. This loan is forgivable in the event no conditions of default have occurred, the technology is not commercialized outside the Province of Ontario and various other documentation requirements. Management has determined that there is reasonable assurance that the company will comply with these conditions and, therefore, has recognized this forgivable loan as a government grant receivable at December 31, 2012. The loan is collateralized by a general security agreement over all of the assets of EcoSynthetix Corporation, a subsidiary company, and by the company's guarantee. In the event that the company is required to repay this funding, the company will be obligated to repay the funding plus interest charged at a rate of 4.55% per annum.

During the year ended December 31, 2011, the company had recognized the full amount of this grant and received all cash related to claims made during the year. No further claims were recognized during the year ended December 31, 2012.

In addition to the above, the company also has a non-repayable government grant agreement, Grant 1, with the Canadian federal government's Sustainability Development Technology Fund (the Fund or SDTF), which was formally granted in 2010 to the company. Grant 1 provides up to a maximum of approximately $1.7 million for a special research and development project. During the year ended December 31, 2011, the company had recognized the full amount of this grant and, therefore, no further claims were recognized during the year ended December 31, 2012. The company collected $0.5 million (2011 - $1.0 million) from the SDTF during the year ended December 31, 2012 and expects to collect the remaining balance of $0.2 million within the next 12 months.

(expressed in US dollars, unless otherwise noted)

During 2011, the company recognized $2.5 million and $0.7 million against capital expenditures and operating expenditures, respectively, for the IDF and SDTF Grant 1 programs.

In 2012, the company was formally granted an additional SDTF non-repayable government grant, Grant 2, securing $2.1 million funding on completion of project milestones. For the year ended December 31, 2012, in accordance with the provisions of Grant 2, the company recognized $0.2 million primarily related to operating expenditures and received $0.5 million in cash.

8 Intangible assets

The composition of the net carrying amount of the company's intangible assets is presented in the following table:

	Computer software
Cost	
December 31, 2011	194,841
Additions	186,679
December 31, 2012	381,520
Accumulated amortization	
December 31, 2011	194,841
Amortization	23,178
	218,019
Carrying amount	
December 31, 2011	-
December 31, 2012	163,501

Amortization expense has been charged to selling, general and administrative.

(expressed in US dollars, unless otherwise noted)

9 Property, plant and equipment

The composition of the net carrying amount of the company's property, plant and equipment is presented in the following table:

	Machinery and equipment	Leasehold improvements	Computer hardware	Construction-in-process and deposits placed on property and equipment	Total
Cost					
January 1, 2011	2,031,796	-	75,749	225,757	2,333,302
Additions	(865,220)	91,009	67,366	10,454,808	9,747,963
Transfers	6,653,237	680,783	-	(7,334,020)	-
December 31, 2011	7,819,813	771,792	143,115	3,346,545	12,081,265
Additions	3,520,390	19,566	66,592	101,949	3,708,497
Transfers	3,208,545	-	-	(3,208,545)	-
December 31, 2012	14,548,748	791,358	209,707	239,949	15,789,762
Accumulated depreciation					
January 1, 2011	(610,733)	-	(32,500)	-	(643,233)
Depreciation expense	(560,083)	(75,547)	(36,278)	-	(671,908)
December 31, 2011	(1,170,816)	(75,547)	(68,778)	-	(1,315,141)
Depreciation expense	(1,171,368)	(78,191)	(50,646)	-	(1,300,205)
December 31, 2012	(2,342,184)	(153,738)	(119,424)	-	(2,615,346)
Net carrying amount					
December 31, 2011	6,648,997	696,245	74,337	3,346,545	10,766,124
December 31, 2012	12,206,564	637,620	90,283	239,949	13,174,416

The company incurred $3.7 million (2011 - $9.7 million) in capital asset additions for the year ended December 31, 2012, net of $0.1 million (2011 - $2.5 million) in government grants. The additions primarily relate to both the manufacturing equipment required for the company's production expansion and the company's research and development facility in Burlington, Ontario. Approximately $0.5 million (2011 - $2.3 million) of capital asset additions were included in accounts payable and accrued liabilities at December 31, 2012.

10 Trade payables and accrued liabilities

	2012	2011
Trade payables	2,093,659	4,335,632
Accrued liabilities	2,188,637	1,807,036
	4,282,296	6,142,668

(expressed in US dollars, unless otherwise noted)

11 Redeemable preferred shares

The movement of redeemable preferred shares for the years ended December 31, 2011 and 2010 are as follows:

	Series A-3-C preferred shares	Series A-3-B preferred shares	Series A-3-A preferred shares	Series A-2 preferred shares	Series A-1 preferred shares	Total
Opening balance - January 1, 2011	26,854,800	10,460,686	14,080,679	31,700,734	52,099,532	135,196,431
Issuances	-	2,464,560	-	-	-	2,464,560
Charges	24,324,893	14,568,254	24,598,765	67,448,022	111,661,177	242,601,111
Conversion to equity	(51,179,693)	(27,493,500)	(38,679,444)	(99,148,756)	(163,760,709)	(380,262,102)
Closing balance - December 31, 2011	-	-	-	-	-	-

On June 30, 2011, the company issued 273,841 Series A-3-B preferred shares to certain holders of the company's preferred shares for $nil. The preferred shares were issued pursuant to the original A-3-B preferred share agreement, whereby if the company did not complete a qualified event by June 30, 2011, the Series A-3-B preferred shares would be issued. The company has expensed $2,464,560 in the year ended December 31, 2011 related to this issuance. The expense is included in the consolidated statements of operations and comprehensive loss, loss related to warrants and redeemable preferred shares.

Charges related to the warrants for the years ended December 31, 2012 and 2011 were $nil and $1,763,865, respectively.

On August 4, 2011, the company's redeemable preferred shares were automatically converted into common shares in connection with the offering. Further, warrants to acquire redeemable preferred shares were automatically converted to warrants to acquire common shares. As a result, the company's liability relating to redeemable preferred shares was reclassified into common shares and warrants were reclassified to a separate component of shareholders' equity (deficiency).

12 Related party transactions

Key management personnel includes those individuals having authority and responsibility for planning, directing and controlling the activities of the company directly or indirectly. Key management personnel includes the directors, chief executive officer, chief financial officer and other key members of the executive team. The compensation paid or payable to key management personnel for employee services is shown below:

	2012	2011
Salaries and other short-term employee benefits	2,028,605	1,797,249
Share-based payments	490,775	666,873
	2,519,380	2,464,122

(expressed in US dollars, unless otherwise noted)

13 Common share options

The company has issued share options to employees, directors, officers, advisers and consultants under its two share option plans. The 2001 plan is an incentive share option plan, which provides for granting incentive share options, as defined under current income tax laws for common shares. The share options are exercisable at fixed prices established at the date of the grant. The 2003 plan provides for granting both incentive share options and non-statutory stock options, as determined by the administrator, at the date of the grant. Employees and officers become vested in their share option rights at a rate of 25% per year, following the date of the grant of the share options. Certain share option agreements also have accelerated vesting periods in the event of a sale of the company or change of control. Vested share options may be exercised at any time before the expiration date. These share options expire ten years from the date of the grant or later if extended further by the board of directors in accordance with the terms of the plans.

At December 31, 2012, the company had outstanding share options to purchase 5,775,285 common shares of the company. The share options expire at various dates through August 31, 2020.

	Number of share options outstanding	Weighted average exercise price
Outstanding - December 31, 2010	5,741,484	0.36
Share options cancelled	-	-
Share options granted	981,453	3.00
Share options exercised	(885,297)	(0.12)
Outstanding - December 31, 2011	5,837,640	0.80
Share options cancelled	-	-
Share options granted	99,471	4.04
Share options exercised	(161,826)	0.92
Outstanding - December 31, 2012	5,775,285	0.85

The weighted average contractual life of the outstanding share options at December 31, 2012 is 2.18 years (2011 - 3.02 years). The total number of share options exercisable at December 31, 2012 is 4,826,715 (2011 - 4,158,257), which have a weighted average exercise price of $0.55 (2011 - $0.31) per share.

	Number	
	2012	2011
Range of exercise prices		
$0.01 - $0.50	2,897,097	2,897,097
$0.51 - $1.00	1,562,717	1,702,717
$1.01 - $10.00	1,315,471	1,237,875
	5,775,285	5,837,640

(expressed in US dollars, unless otherwise noted)

For the years ended December 31, the company determined the fair values of share options using the Black-Scholes option pricing model with the following assumptions for share option grants:

	2012	2011
Expected dividend yield	-	-
Risk-free interest rate	1.0% to 2.0%	1.2% to 2.2%
Expected share option life (in years)	5	5
Volatility	70%	50% - 70%

The aggregate fair value of share options granted during the year is $215,082 (2011 - $1,681,376). The weighted average fair value of the share options is $2.16 (2011 - $1.72) per share.

For the year ended December 31, 2012, expected volatility is based on a review of historical volatilities for the company and similar publicly listed companies.

The expected share option life is based on the employees' historical exercise behaviour.

The risk-free interest rate used for each grant is equal to the US Treasury's yield curve and Canadian treasury bill rates in effect at the date of grant for instruments with a term similar to the expected life of the related share option.

14 Common shares

	2012	2011
Common shares (unlimited number of shares authorized, 55,259,085 (2011 - 55,242,741) shares issued and outstanding)	492,065,820	492,353,321

Share exchange

On August 17, 2012, the company received regulatory approval for a normal course issuer bid (the Bid) to repurchase a certain number of its outstanding common shares through the facilities of the Toronto Stock Exchange (TSX). The number of shares to be purchased will not exceed 2,348,261 common shares. The period of the Bid will occur from August 20, 2012 to August 19, 2013. During the year ended December 31, 2012, the company repurchased 145,800 common shares for total consideration of $521,729.

Outstanding warrants

During the year ended December 31, 2012 (2011 - 37,240), no warrants were exercised into common shares, generating proceeds of $nil (2011 - $29,494). At December 31, 2012, the company had outstanding warrants for the purchase of 361,228 common shares of the company, exercisable at $0.81 per share. These shares are exercisable up to February 28, 2014.

(expressed in US dollars, unless otherwise noted)

15 Income taxes

The difference between income tax expense and the income taxes, as computed, based on the statutory rate, is as follows:

	2012	2011
Net loss before income taxes	(11,430,735)	(252,708,148)
Income tax benefit at statutory rate	(3,029,144)	(66,335,889)
Cost (benefit) resulting from		
Redeemable preferred share losses, net of foreign tax rate differential	-	65,277,327
Research and development credit	(439,603)	(212,000)
Income tax assets expired	89,348	100,000
Valuation allowance and other	3,379,399	1,170,562
Income tax expense	-	-

Estimated temporary differences in the timing of recognition of expenses for accounting and income tax purposes at December 31 result in deferred income taxes as follows:

	2012	2011
Estimated deferred income tax assets attributable to		
Net operating loss carry-forwards	14,851,129	11,583,331
Research and development credits	1,147,998	934,869
Deferred compensation and other	2,437,490	2,575,614
Deferred income tax assets	18,436,617	15,093,814
Valuation allowance	(18,436,617)	(15,093,814)
Net deferred income tax assets	-	-

(expressed in US dollars, unless otherwise noted)

The estimated net operating loss carry-forwards and estimated research and development credits expire as follows:

	United States of America		Canada and the Netherlands	Canada
	Net operating loss carry-forwards	Research and development credits	Net operating loss carry-forwards	Research and development credits
Year ending December 31,				
2013	-	-	102,869	-
2014	-	-	17,766	-
2015	-	-	410,651	-
2016	252,561	-	8,389	-
2017	317,961	-	9,094	-
2018	1,009,888	-	11,850	-
2019	1,561,172	25,236	13,162	-
2020	2,063,163	42,132	50,259	-
2021	2,564,511	55,822	-	-
2022	1,338,594	52,731	-	-
2023	1,321,285	44,965	-	-
2024	1,532,264	46,333	-	-
2025	1,629,456	47,245	-	-
2026	1,562,856	41,905	397,347	-
2027	2,011,361	35,351	-	-
2028	2,717,038	69,118	1,512,105	-
2029	2,854,334	63,226	-	-
2030	1,207,399	96,302	-	54,600
2031	3,927,982	-	6,114,577	474,525
2032	1,243,610	-	9,100,304	177,078
	29,115,435	620,366	17,748,373	706,203

16 Commitments

a) The company has entered into the following financial commitments:

	$
Year ending December 31, 2013	7,843,944
2014	378,504
2015	378,318
2016	378,318
Thereafter	1,087,976
	10,067,060

(expressed in US dollars, unless otherwise noted)

During the normal course of operations, the company may enter into feedstock contracts to secure raw material availability over a 12-month period based on market pricing at the time of purchase. As at December 31, 2012, the company was committed to purchases of feedstock of approximately $6.0 million prior to September 30, 2013.

At December 31, 2012, the company is committed to property, plant and equipment purchases or equipment rental commitments in the approximate amount of $0.1 million.

17 Segmented information and enterprisewide disclosures

Segmented reporting

The company operates in one reportable segment and generated revenue primarily from the sale of its Ecosphere Biolatex (r) Binders.

Sales by geographic location

The company is domiciled in Canada. During the year ended December 31, 2012, revenue from external customers located in Canada was $65,606 (2011 - $nil). The total revenue from external customers in the following regions is as follows:

	2012	2011
North America	5,938,119	4,193,156
Latin America	1,685,437	2,063,238
EMEA	2,315,804	599,493
Asia Pacific	9,612,985	13,913,964
	19,552,345	20,769,851

The revenue has been assigned to each jurisdiction, based on the location of the customer. In situations where a sale is made through a reseller, revenue associated with that sale is attributed to the geographic region of the end customer. During the year ended December 31, 2012, revenue attributeable to the individual countries representing greater than 10% of total revenues included Japan, United States, China and Germany which represented 33%, 30%, 10%, and 10% respectively. During the year ended December 31, 2011, revenue attributable to individual countries representing greater than 10% of total revenue included Indonesia, Japan, United States and China which represented 26%, 23%, 20% and 17%, respectively.

Sales to major customers

The company derives a significant portion of its revenues from certain customers. Three customers represented 33%, 12% and 10% of total revenue for the year ended December 31, 2012 (2011 two customers represented 26% and 23%, respectively). The concentrations listed do not necessarily apply to the same customer year over year.

(expressed in US dollars, unless otherwise noted)

Property, plant and equipment and intangible assets

The company's property, plant and equipment and intangible assets, reported at net carrying amount, are located in the following countries:

	2012	2011
Canada	2,727,975	1,971,731
United States of America	6,087,898	4,277,777
The Netherlands	4,522,044	4,516,616
	13,337,917	10,766,124

18 Expenses by nature

Additional information on the nature of amounts included in cost of sales, selling, general and administrative and research and development is as follows:

	2012	2011
Wages and salaries	6,793,528	5,624,771
Share-based compensation	847,104	984,325
Depreciation and amortization	1,207,584	583,980

19 Loss per share

Basic loss per share is calculated by dividing the profit attributable to equityholders of the company by the weighted average number of common shares in issue during the year.

Diluted loss per share is equivalent to basic loss per share, as the consideration of potentially dilutive securities would be anti-dilutive.

20 Contingencies and guarantees

In connection with the company's initial public offering on August 4, 2011, the company agreed to provide an indemnity to each of the retained interest holders for any (i) loss of deferral of US income taxes attributable to the execution of the put/call agreement that are incurred by a retained interest holder before the third anniversary of the closing of the offering; (ii) interest and penalties paid that are attributable to any US federal, state or local income tax liability of a retained interest holder that arises as a result of a final determination by any US taxing authority relating to the execution of the put/call agreement (taxes); and (iii) certain reasonable fees, costs and expenses paid by a retained interest holder to defend any demand, claim or notice from a US taxing authority with respect to taxes. The company's liability under the indemnity will not exceed the indemnity cap, which is determined based on $2.72 per covered share (which equates to $0.3885 per common share into which each covered share may be exchanged), representing a maximum liability to the company under the indemnity of approximately $4 million. The indemnity will terminate on the fifth anniversary of the

(expressed in US dollars, unless otherwise noted)

closing. The company has assessed the likelihood of incurring the liability as remote and, accordingly, has not recorded a provision at December 31, 2012.

21 Comparative balances

Certain comparative balances have been reclassified to conform to the consolidated financial statement presentation adopted in the current year.