EcoSynthetix Inc.

Consolidated Financial Statements
December 31, 2011
(expressed in US dollars)

March 7, 2012

Independent Auditor's Report

To the Shareholders of
EcoSynthetix Inc.

We have audited the accompanying consolidated financial statements of EcoSynthetix Inc. and its subsidiaries, which comprise the consolidated balance sheets at December 31, 2011 and 2010 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 audits 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.

PricewaterhouseCoopers LLP, Chartered Accountants
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Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of EcoSynthetix Inc. and its subsidiaries at December 31, 2011 and 2010 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Accountants, Licensed Public Accountants

EcoSynthetix Inc.

Consolidated Balance Sheets

At December 31

(expressed in US dollars)

	2011	2010
Assets		
Current assets		
Cash	105,713,705	35,193,037
Accounts receivable (note 5)	3,116,445	2,739,570
Inventory (note 6)	10,243,410	1,990,383
Government grants receivable (note 7)	639,685	973,751
Prepaid expenses	182,842	81,089
	119,896,087	40,977,830
Non-current assets		
Intangible assets (note 8)	-	44,315
Property, plant and equipment (note 9)	10,766,124	1,690,069
Total assets	130,662,211	42,712,214
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 10)	6,142,668	3,603,796
Deferred government grant (note 7)	-	486,961
Accrued compensation	-	1,005,371
	6,142,668	5,096,128
Non-current liabilities		
Redeemable preferred shares (note 11)	-	135,196,431
Warrants (note 11)	-	1,501,295
Total liabilities	6,142,668	141,793,854
Shareholders' Equity (Deficiency)		
Common shares (note 14)	492,353,321	143,213
Equity component of redeemable preferred shares (note 11)	-	19,793,287
Contributed surplus	6,073,080	2,180,570
Accumulated deficit	(373,906,858)	(121,198,710)
Total shareholders' equity (deficiency)	124,519,543	(99,081,640)
Total shareholders' equity (deficiency) and liabilities	130,662,211	42,712,214

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)

	2011	2010
Net sales	20,769,851	15,879,080
Cost of sales	15,796,830	11,927,085
Gross profit on sales	4,973,021	3,951,995
Expenses		
Selling, general and administrative	8,518,299	4,841,518
Research and development	2,516,360	1,051,810
	11,034,659	5,893,328
Loss from operations	(6,061,638)	(1,941,333)
Interest income	183,027	6,901
Loss related to change in value of warrants and redeemable preferred shares (note 11)	(246,829,537)	(47,259,599)
Net loss and comprehensive loss	(252,708,148)	(49,194,031)
Basic and diluted loss per common share (note 19)	(10.93)	(61.78)
Weighted average number of common shares outstanding (note 19)	23,125,647	796,278

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, 2010	143,213	15,949,943	1,084,659	(72,004,679)	(54,826,864)
Preferred share warrants exercised	-	3,843,344	-	-	3,843,344
Share-based compensation	-	-	1,095,911	-	1,095,911
Net loss and comprehensive loss	-	-	-	(49,194,031)	(49,194,031)
Balance - December 31, 2010	143,213	19,793,287	2,180,570	(121,198,710)	(99,081,640)
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

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)

	2011	2010
Cash provided by (used in)		
Operating activities		
Net loss	(252,708,148)	(49,194,031)
Items not affecting cash		
Depreciation and amortization	583,380	351,470
Share-based compensation (note 13)	984,325	1,095,911
Change in value of warrants and redeemable preferred shares	246,829,537	47,259,599
Changes in non-cash working capital		
Accounts receivable	(376,875)	(1,722,598)
Inventory	(8,055,027)	(1,075,867)
Government grants receivable (note 7)	334,066	(973,751)
Prepaid expenses	(101,753)	(43,311)
Accounts payable and accrued liabilities	226,620	2,126,420
Accrued compensation	(1,005,371)	54,043
Deferred government assistance	(486,961)	486,961
	(13,776,207)	(1,635,154)
Investing activities		
Purchase of intangible assets and property and equipment (notes 8 and 9)	(10,012,325)	(2,535,582)
Financing activities		
Common share issuance costs (note 14)	(10,792,531)	-
Issuance of common shares (note 14)	102,451,082	-
Exercise of stock options	109,696	-
Exercise of common share warrants	29,494	-
Exercise of preferred share warrants	-	232,456
Proceeds from issuance of preferred shares, net of transaction costs (note 11)	-	28,405,251
Increase in government grant (note 7)	2,511,459	1,175,932
	94,309,200	29,813,639
Increase in cash during the year	70,520,668	25,642,903
Cash - Beginning of year	35,193,037	9,550,134
Cash - End of year	105,713,705	35,193,037
Non-cash financing activities		
Conversion of redeemable preferred shares and related warrants to common shares	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

Basis of preparation and adoption of International Financial Reporting Standards (IFRS)

Statement of compliance

These consolidated financial statements have been authorized for issuance by the board of directors of the company on March 7, 2012.

Basis of measurement

The consolidated financial statements have been prepared under 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, valuation of redeemable preferred shares and related warrants, 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.

ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Generally, 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. If not, they are presented as non-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) Financial assets and financial liabilities at FVTPL

A financial asset or financial liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the consolidated statements of operations and comprehensive loss. Gains and losses arising from changes in fair value are presented in the consolidated statements of operations and comprehensive loss within other gains and losses in the year in which they arise. Financial assets and financial liabilities at FVTPL 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.

ii) 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 trade receivables 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.

iii) Financial liabilities at amortized cost

Financial liabilities at amortized cost include trade payables and term debt. Trade and other payables 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 other payables 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.

Derivative financial instruments

Derivatives are classified as held-for-trading, and are classified as current or non-current based on the contractual terms specific to the instrument. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value, with changes being recorded in the consolidated statements of operations and comprehensive loss.

(expressed in US dollars, unless otherwise noted)

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.

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 10 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.

(expressed in US dollars, unless otherwise noted)

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 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.

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

(expressed in US dollars, unless otherwise noted)

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 it is probable that the economic benefits will flow to the company and delivery has occurred, the sales price is fixed or determinable and collectibility is reasonably assured. 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

Cost of sales includes costs related to shipping and handling and the cost of the finished goods inventory.

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.

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 (deficiency), in which case the income taxes are also recognized directly in shareholders' equity (deficiency).

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.

(expressed in US dollars, unless otherwise noted)

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.

Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities.

Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

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 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.

(expressed in US dollars, unless otherwise noted)

3 Risk management and financial instruments

Financial instruments are classified into one of the following categories: held-for-trading; held-to-maturity; available-for-sale; loans and receivables; and other financial liabilities. The following table summarizes information regarding the carrying amounts of the company's financial instruments:

	2011	2010
Loans and receivables (i)	108,830,150	37,932,607
Other financial liabilities (ii) - amortized cost	6,142,668	4,609,167
Other financial liabilities (iii) - FVTPL	-	136,697,726

i) Includes cash and cash equivalents and accounts receivable
ii) Includes financial liabilities included within accounts payable and accrued liabilities and accrued compensation
iii) Includes redeemable preferred shares and warrants

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 significant 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.

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, 2011, the company's two largest customers accounted for 52% (2010 - 47%) of accounts receivable. In order to minimize the risk of loss for trade receivables, 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 60 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 trade receivables have a carrying amount of $2,510,783 at December 31, 2011 (2010 - $2,687,877), 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 60 days. An insignificant number of these receivables were past due at December 31, 2011. The company's exposure to credit risk for trade receivables by geographic area at December 31 was as follows:

(expressed in US dollars, unless otherwise noted)

	2011 %	2010 %
North America	29	11
Latin America	21	13
EMEA	7	-
Asia Pacific	43	76
	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 0-60 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 $105,713,705 at December 31, 2011 (2010 - $35,193,037), representing the maximum exposure to credit risk of these financial assets. Approximately 99% (2010 - 99%) of the company's cash at December 31, 2011 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:

	2011 %	2010 %
Canada	98.5	99.0
United States of America	1.0	1.0
The Netherlands	0.5	-
	100.0	100.0

Foreign currency risk

Foreign currency risk arises because of fluctuations in foreign currency exchange rates. The company conducts a significant portion of its business activities in currencies other than the functional currency of the parent company (US dollars). This primarily includes Canadian dollar 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 trade payables, which are denominated in foreign currencies. The company recognized foreign currency exchange gains in the years ended December 31, 2011 and 2010 of $36,501 and $65,948, 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 $34,084 (2010 - $245,140) due to exchange rate fluctuations and this amount would be recorded in the consolidated statements of operations and comprehensive loss.

(expressed in US dollars, unless otherwise noted)

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 be nominal (2010 - $48,393) due to exchange rate fluctuations and this amount would be recorded in the consolidated statements of operations and comprehensive loss.

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 and restricted cash. The company is subject to interest rate risk on its cash. The company is not subject to interest rate risk on the redeemable preferred shares, as these have a fixed interest rate. 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 trade payables 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).
- 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 redeemable preferred shares and warrants of the company are measured at fair value at the end of each reporting period and are categorized as level 3, based on the degree to which their fair value is observable. There were no transfers between levels 1 and 2 during the year. The company's redeemable preferred shares were automatically converted into common shares in connection with the offering on August 4, 2011.

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, preferred shares, warrants and shareholder option exercises. The total capital at December 31, 2011 is $158,959,227 (2010 - $67,161,486). The company's primary uses of capital are financing operations, increasing non-cash working capital and capital expenditures. The company currently funds these

(expressed in US dollars, unless otherwise noted)

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

	2011	2010
Trade accounts receivable - net	2,510,783	2,687,877
Commodity taxes receivable	605,662	51,693
	3,116,445	2,739,570

The company has recorded a $82,000 provision for bad debts at December 31, 2011, which is included in trade accounts receivable - net. No provisions for bad debts were recognized at December 31, 2010.

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

	2011	2010
Current	2,671,616	1,508,745
Past due 1-30 days	357,782	1,196,200
Past due 31-60 days	34,309	765
Past due 61-90 days	6,498	-
Past due greater than 91 days	46,240	33,860
Balance at December 31	3,116,445	2,739,570

6 Inventory

	2011	2010
Raw materials	994,440	1,379,736
Finished goods	9,248,970	610,647
	10,243,410	1,990,383

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

(expressed in US dollars, unless otherwise noted)

loan as a government grant receivable at December 31, 2011. 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.

The company also has a non-repayable government grant agreement with the Canadian federal government's Sustainable Development Technology Fund (the Fund or SDTF), pursuant to which the Fund will provide up to a maximum of approximately $1.7 million for a specific research and demonstration project.

The company has recognized the maximum total amount of government incentives of $4.8 million under the IDF and SDTF programs, of which $2.5 million (2010 - $1.2 million) was recorded against capital expenditures and $0.7 million (2010 - $0.3 million) was recorded against operating expenses during 2011. At December 31, 2011, the company has collected $4.1 million and expects to receive the remaining $0.7 million in the next 12 months.

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, 2010	129,684
Additions	65,157
December 31, 2011	194,841
Accumulated depreciation	
December 31, 2010	(85,369)
Amortization	(109,472)
	(194,841)
Carrying amount	
December 31, 2010	44,315
December 31, 2011	-

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, 2010	946,095	-	39,454	-	985,549
Additions	1,085,701	-	336,295	1,401,689	2,523,685
Government grants	-	-	-	(1,175,932)	(1,175,932)
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
Accumulated depreciation					
January 1, 2010	(302,339)	-	(32,500)	-	(334,839)
Additions	(308,394)	-	-	-	(308,394)
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)
Net carrying amount					
December 31, 2010	1,421,063	-	43,249	225,757	1,690,069
December 31, 2011	6,648,997	696,245	74,337	3,346,545	10,766,124

The company incurred $9.7 million in capital asset additions for the year ended December 31, 2011, net of $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 $2.3 million of capital asset additions were included in accounts payable and accrued liabilities at December 31, 2011.

10 Trade payables and accrued liabilities

	2011	2010
Trade payables	4,335,632	2,659,378
Accrued liabilities	1,807,036	944,418
	6,142,668	3,603,796

(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, 2010	-	7,867,030	9,794,813	17,517,172	28,562,130	63,741,145
Issuances	24,799,363	-	79,400	-	-	24,878,763
Charges	2,055,437	2,593,656	4,206,466	14,183,562	23,537,402	46,576,523
Closing balance - December 31, 2010	26,854,800	10,460,686	14,080,679	31,700,734	52,099,532	135,196,431
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, 2011 and 2010 were $1,763,865 and $683,076, 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:

(expressed in US dollars, unless otherwise noted)

	2011	2010
Salaries and other short-term employee benefits	1,797,249	1,433,855
Share-based payments	666,873	240,738
	2,464,122	1,674,593

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, 2011, the company had outstanding share options to purchase 5,837,640 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

The weighted average contractual life of the outstanding share options at December 31, 2011 is 3.02 years (2010 - 3.35 years). The total number of share options exercisable at December 31, 2011 is 4,158,257 (2010 - 4,499,572), which have a weighted average exercise price of $0.31 (2010 - $0.21) per share.

	Number
Range of exercise prices	
$0.01 - $0.50	2,897,048
$0.56 - $1.00	1,702,717
$1.01 - $10.00	1,237,875
	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:

	2011	2010
Expected dividend yield	-	-
Risk-free interest rate	1.2% to 2.2%	1.40% to 1.80%
Expected share option life (in years)	5	5
Volatility	50% - 70%	70%

The aggregate fair value of share options granted during the year is $1,681,376 (2010 - $191,967). The weighted average fair value of the share options is $1.72 (2010 - $0.71) per share.

For the year ended December 31, 2011, 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

	2011	2010
Common shares (unlimited number of shares authorized, 55,242,741 (2010 - 796,278) shares issued and outstanding)	492,353,321	143,213

On August 4, 2011, the company completed its offering by issuing 11,150,000 common shares at a price of CA$9.00 per share, for aggregate gross proceeds of CA$100,350,000, subject to the terms of an underwriting agreement.

The company granted to the underwriters of the offering an over-allotment option, exercisable, in whole or in part, at the sole discretion of the underwriters, for a period of 30 days from the closing of the offering, to purchase up to an additional 1,672,500 common shares. On September 12, 2011, the company announced that the underwriters had purchased an additional 300,000 common shares of the company at a price of CA$9.00 per share, pursuant to the partial exercise of the over-allotment option granted to the underwriters in connection with the offering, discussed above. The company did not receive any proceeds from the sale of these additional shares.

Concurrent with the closing of the offering, the company acquired 77% of the issued and outstanding common shares of EcoSynthetix US in exchange for 33,640,663 common shares of the company, assuming no exercise of the over-allotment option. The remaining 23% of the outstanding common shares of the company continue to be held by certain securityholders of the company that are US holders (the retained interest holders).

(expressed in US dollars, unless otherwise noted)

Pursuant to a put/call agreement entered into by the company and the retained interest holders, the retained interest holders will be entitled to sell their common shares of EcoSynthetix US and common shares of EcoSynthetix US issued on exercise of warrants (the covered shares) to the company at any time prior to the date that is five years following the closing of the offering (the put expiry date) in exchange for common shares of the company on the basis of seven common shares for one covered share, subject to adjustment. In addition, the company will be entitled to purchase the covered shares held by the retained interest holders at any time from the period commencing one year following the put expiry date to the date that is two years following the put expiry date in exchange for seven common shares for one covered share, subject to adjustment. In addition, the company will be entitled to exercise its right to purchase the covered shares in the event of a change of control of the company or a bankruptcy event of the company that occurs prior to the put expiry date. The shares held by the retained interest holders have been presented on an as "exchanged basis" as outstanding common shares of the company effective August 4, 2011.

Share exchange

On August 4, 2011, the company completed a share exchange of its issued and outstanding common shares with EcoSynthetix (EcoSynthetix US) in conjunction with the offering with a ratio of seven post-exchange shares for every one pre-exchange share. The company has amended the disclosures in the consolidated financial statements to reflect the share exchange as if it had occurred on January 1, 2010.

Conversion of redeemable preferred shares to common shares and related warrants

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 component of shareholders' equity (deficiency).

Outstanding warrants

During the year ended December 31, 2011, 37,240 warrants were exercised into common shares, generating proceeds of $29,494. At December 31, 2011, 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:

	2011	2010
Net loss before income taxes	(252,708,148)	(49,194,031)
Income tax benefit at statutory rate	(66,335,889)	(16,725,971)
Cost (benefit) resulting from		
Redeemable preferred share losses, net of foreign tax rate differential	65,277,327	15,941,108
Research and development credit	(212,000)	(58,226)
Income tax assets expired	100,000	218,000
Valuation allowance and other	1,170,562	625,089
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:

	2011	2010
Estimated deferred income tax assets attributable to		
Net operating loss carry-forwards	11,583,331	9,253,243
Research and development credits	934,869	602,030
Deferred compensation and other	2,575,614	486,700
Deferred income tax assets	15,093,814	10,341,973
Valuation allowance	(15,093,814)	(10,341,973)
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,				
2012	-	-	74,101	-
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	-	98,735
2031	4,055,465	-	5,554,415	208,850
	27,999,308	620,366	8,162,008	307,585

(expressed in US dollars, unless otherwise noted)

16 Commitments

a) The company has entered into a real property operating lease with the following commitments:

Year ending December 31, 2012	362,244
2013	362,244
2014	356,904
2015	378,318
2016	378,318
Thereafter	1,450,220
	3,288,248

b) At December 31, 2011, the company is committed to property, plant and equipment purchases or equipment rental commitments in the approximate amount of $90,000.

17 Segmented information and enterprisewide disclosures

Segmented reporting

The company operates in one reportable segment.

Sales by geographic location

The company is domiciled in Canada. Revenue from external customers located in Canada is $nil (2010 - $nil). The total revenue from external customers in the following regions is as follows:

	2011	**2010**
North America	4,193,156	630,290
Latin America	2,063,238	1,005,250
EMEA	599,493	-
Asia Pacific	13,913,964	14,243,540
	20,769,851	15,879,080

The revenue has been assigned to each jurisdiction, based on the location of the customer.

Sales to major customers

The company derives a significant portion of its revenues from two customers, representing 26% and 23% of total revenue for the year ended December 31, 2011 (2010 - 37% and 17%). 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:

	2011	2010
Canada	1,971,731	480,298
United States of America	4,277,777	912,000
The Netherlands	4,516,616	342,086
	10,766,124	1,734,384

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:

	2011	2010
Wages and salaries	5,624,771	3,193,045
Share-based compensation	984,325	1,095,911
Depreciation and amortization	583,980	351,470

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 offering (note 14), 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 closing. The company has assessed the

(expressed in US dollars, unless otherwise noted)

likelihood of incurring the liability as remote and, accordingly, has not recorded a provision at December 31, 2011.

21 Comparative balances

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