

## **ORGANIC RESOURCE MANAGEMENT INC.**

### **Management Discussion and Analysis for the six months ended December 31, 2008**

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#### **Introduction**

The following Management Discussion and Analysis (“MD&A”) is a discussion of the consolidated financial condition and results of operations of Organic Resource Management Inc. (the “Company” or “ORMI”) for the six months ended December 31, 2008. This discussion should be read in conjunction with the Unaudited Interim Consolidated Financial Statements of the Company and notes thereto for the six months ended December 31, 2008, the MD&A for the year ended June 30, 2008 and the Audited Consolidated Financial Statements and notes thereto for the year ended June 30, 2008. This MD&A is prepared as at February 12, 2009.

#### **Forward-Looking Information**

Certain statements made or incorporated by reference in this MD&A are forward-looking and relate to, among other things, anticipated financial performance, business projects, strategies, regulatory developments, new services, market forces, commitments and technological developments. By its nature, such forward-looking information is subject to various risks and uncertainties, including those discussed in this MD&A or in documents incorporated by reference in this MD&A, which could cause the Company’s actual results and experience to differ materially from the anticipated results or expectations expressed. Readers are cautioned not to place undue reliance on this forward-looking information, and the Company undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise, except in accordance with applicable securities laws.

#### **Non-GAAP Measures**

Adjusted net earnings excluding non-cash expenses is not a recognized measure under Canadian generally accepted accounting principles (“GAAP”). Management believes that this is a useful supplemental measure of the Company’s ability to generate cash from operations necessary to fund future reinvestment and is more indicative of actual performance. The Company’s method of calculating this measure may differ from other issuers and accordingly, it may not be comparable to measures used by other issuers. (See further discussion under “Quarterly Review - Adjusted Net Earnings Excluding Non-Cash Expenses”.)

#### **Corporate Overview**

ORMI is Canada’s largest provider of vacuum truck services for the collection, processing and recycling of food-related organic residuals. The residuals the Company collects are from customers in the food service, processing, production or retail business and include industrial, commercial and institutional operations. ORMI services more than 6,000 customers in Ontario, Quebec and British Columbia.

At the heart of the Company are sophisticated, proprietary logistics and operational management software and systems, specifically designed for the Company’s business, vision and growth plans. These systems allow it to schedule and deliver complex customer services from a centralized call and logistics center. Map-based GIS (Geographic Information System) routing and dispatch software, coupled with GPS (Global Positioning System) tracking and live, real-time handheld work order and data collection capabilities, allow the Company to deliver superior customer service at extremely high productivity levels.

On October 31, 2008, the Company sold A&A’s non-core assets to McRae’s Environmental Services Ltd. (“McRae’s”) for \$2,075,000. Under the terms of the agreement, McRae’s purchased 17 trucks and trailers, parts inventory, A&A’s customer list for its non-core business and the rights to A&A’s name.

Conversely, the Company acquired McRae's list of customers that relate to the Company's core area of business. The purchase price was comprised of a cash payment of \$1,245,000, a note receivable for \$575,000 and the assumption of capital lease debt for \$255,000. The asset sale generated a net gain on disposal of \$1,708,000.

Revenue generated from A&A's non-core customers was approximately \$3.1 million in fiscal 2008 and contributed to earnings. Management believes that the reduction in Company revenue and earnings resulting from this transaction will be partially offset by the acquisition of McRae's customer list in ORMI's core business (approximately \$300,000 per year) as well as interest savings from the reduction of the Company's debt and other measures that will be undertaken to reduce overhead, but the final impact on the Company's revenues and earnings is not presently determinable.

The proceeds of the sale will be used to pay off the Company's revolving loan and to fund upgrades of its facilities to support the installation of anaerobic digestion waste management solutions.

On November 5, 2008, A&A's name was changed to Organic Resource Management (BC) Inc. ("ORMI BC").

On September 29, 2008, the Company completed a voluntary wind-up of its two wholly-owned and inactive Bermuda companies, NCS Holdings Ltd. and NCS Environmental Services Ltd.

## **Results of Operations**

### **Revenues**

The Company exited the compactor rental business in January 2008. Compactor rental revenues included in the second quarter of last year were \$42,000 and for the first six months were \$125,000. Exiting the compactor rental business combined with the sale of A&A's non-core customers resulted in a decrease in revenues. For the second quarter of fiscal 2009 revenues were \$3,217,000, a decrease of 15% or \$583,000 from \$3,800,000 in the second quarter of fiscal 2008. For the first six months of the year, total revenues were \$7,265,000, a decrease of 3% or \$258,000 from \$7,523,000 for the same period last year.

Excluding revenue from the compactors and from A&A's non-core business, revenues were 3% greater than last year for the quarter and 4% greater for the first six months of the year. While the Company's grease interceptor revenues were 11% greater than last year for the first six months, all of which can be attributed to higher volumes, revenues from industrial organics services were down 22% as limited cost effective disposal capacity in Ontario continues to affect the Company's ability to service the industrial food processing accounts. The lost revenue from the industrial organics services was very competitively priced and therefore did not have a significant impact on the gross margin of the Company.

### **Gross Margin and Operating Expenses**

The gross margin for the quarter was \$1,038,000, a decrease of 18% or \$226,000 from \$1,264,000 for the same period last year. For the six months ended December 31, 2008, gross margin was \$2,555,000, 4% or \$93,000 greater than the \$2,462,000 recorded last year. As a percentage of revenue, gross margin was 32% for the quarter and 35% for the year to date, compared to 33% for the same periods last year.

During the quarter, the Company continued to utilize the disposal sites in Ontario and New York that it sourced earlier in the year, which contributed to higher margins in the Company's Ontario market. The overall reduction in gross margin was due to additional rent and one-time costs incurred for the relocation to the Company's new facilities in Vancouver and the lower revenues with the sale of the Company's non-core business.

Selling, general and administrative expenses were \$909,000 in the second quarter of fiscal 2009, an increase of 4% or \$35,000 from \$874,000 in the second quarter of fiscal 2008. For the year to date, selling, general and administrative expenses were \$1,834,000, an increase of 8% or \$129,000 from \$1,705,000 last year. This increase mainly relates to advertising expenses for the rebranding of A&A to ORMI as well as salary and rent increases.

Amortization of property, plant and equipment was \$237,000 in the second quarter of fiscal 2009, an increase of 23% or \$44,000 from \$193,000 in the second quarter of fiscal 2008. For the year to date, amortization was \$476,000, an increase of 40% or \$137,000 from \$339,000 last year. This increase was due to the acquisition of ORMI Information Systems Inc., new handheld equipment and four new trucks during the latter half of fiscal 2008.

Other interest expense was \$11,000 in the second quarter of fiscal 2009, a decrease of 65% or \$20,000 from \$31,000 in the second quarter of fiscal 2008. This decrease was mainly due to the proceeds from the sale of A&A's non-core assets which were used to pay down the revolving loan. For the year to date, these costs were \$29,000, a decrease of 52% or \$31,000 from \$60,000 last year.

### Net Income and Income Taxes

Net income before taxes was \$1,542,000 for the quarter compared to \$124,000 last year, an increase of \$1,418,000. This increase was due to the gain on disposal of A&A non-core assets of \$1,708,000, partially offset by approximately \$180,000 relating to one-time costs incurred in the sale process, rebranding of the Company's BC assets from A&A to ORMI, and the relocation to the new Vancouver facility. For the year to date, net income before taxes was \$1,818,000, an increase of \$1,521,000 from \$297,000 last year.

The Company has future income tax assets which are subject to periodic recoverability assessments. There was no change in these assets in the second quarter of fiscal 2009. Future income tax expense was \$68,000 for the second quarter of 2009 compared to \$41,000 for the same period last year. For the year to date, future income tax expense was \$166,000, compared to \$101,000 last year. The Company has not established a provision for income taxes payable on the sale of A&A non-core assets as it has sufficient non-capital losses available to apply against taxable income.

## Quarterly Review

### FINANCIAL INFORMATION - EIGHT QUARTER SUMMARY

Quarter Ending:	Fiscal 2009		Fiscal 2008				Fiscal 2007	
	Dec. 31 2008	Sep. 30 2008	Jun. 30 2008	Mar. 31 2008	Dec. 31 2007	Sep. 30 2007	Jun. 30 2007	Mar. 31 2007
(in 000's except income (loss) per share)								
Revenue	\$ 3,217	\$ 4,048	\$ 3,855	\$ 3,828	\$ 3,800	\$ 3,723	\$ 3,834	\$ 3,928
Net income (loss)	1,471	174	(1,286)	(139)	82	114	(836)	(264)
Cash flows from operating activities	338	382	83	510	(162)	101	132	297
Income (loss) per share:								
Basic	\$ 0.33	\$ 0.04	\$ (0.29)	\$ (0.03)	\$ 0.02	\$ 0.03	\$ (0.30)	\$ (0.13)
Diluted	0.31	0.04	(0.28)	(0.03)	0.02	0.02	(0.30)	(0.13)

Total revenue levels have remained relatively constant during the prior seven quarters as the Company has replaced its compactor revenues and large volume, lower margin industrial organics business with smaller volume, higher margin core grease interceptor business. During this time, the Company's core grease interceptor revenues have increased 30%. The decrease in revenues for the current quarter was due to the sale of the A&A's non-core business in October.

The net loss of \$264,000 recorded in the third quarter of 2007 reflected intangible amortization and preferred dividend charges (which are no longer applicable). The net loss of \$836,000 for the fourth quarter of 2007 included severance expenses of \$280,000, legal fees of \$173,000 related to restructuring, a \$125,000 MOE fine and several non-cash items described below.

During the third quarter of 2008, the Company incurred higher fuel, fleet repair and maintenance, waste disposal and labour costs, including a \$45,000 severance payment related to a former employee. The net loss for the fourth quarter was mainly due to the non-cash item described below.

During the fourth quarter of fiscal 2008, the Company recognized an impairment loss of \$1,383,000 which represented 100% of the remaining goodwill relating to the acquisition of A&A in 2002.

The net income of \$174,000 in the first quarter of 2009 was mainly due to the higher margins realized as a result of the Company's shift away from Quebec recycling sites to alternative sites in Ontario and New York.

The net income of \$1,471,000 in the current quarter was due to the gain on disposal of non-core assets of \$1,708,000, partially offset by approximately \$180,000 of one-time costs as noted above.

Cash flows from operating activities are a function of net income or loss, changes in operating assets and liabilities, and non-cash expenses. These non-cash items are summarized in the following table.

#### NON-CASH EXPENSES

Quarter Ending:	Fiscal 2009		Fiscal 2008				Fiscal 2007	
	Dec. 31 2008	Sep. 30 2008	Jun. 30 2008	Mar. 31 2008	Dec. 31 2007	Sep. 30 2007	Jun. 30 2007	Mar. 31 2007
(in 000's)								
Amortization of property, plant & equipment	\$ 237	\$ 239	\$ 346	\$ 227	\$ 193	\$ 147	\$ 213	\$ 178
Amortization of intangibles	-	-	-	-	-	-	171	242
Accretion of interest expense	-	-	8	7	7	7	-	-
Share based compensation	6	7	91	8	9	2	-	21
(Gain) loss on disposal of property, plant & equipment	(1,219)	(6)	(10)	(8)	(16)	(20)	(18)	15
Gain on disposal of intangible assets	(500)	-	-	-	-	-	-	-
Write down of property, plant & equipment	-	-	-	-	-	-	235	-
Write-down of intangibles	-	-	-	-	-	-	992	-
Write-down of goodwill	-	-	1,383	-	-	-	-	-
Dividends accrued on preferred shares	-	-	-	-	-	-	62	91
Future income taxes	68	98	(136)	(69)	41	60	(1,135)	-
	<b>\$ (1,408)</b>	<b>\$ 338</b>	\$1,682	\$ 165	\$ 234	\$ 196	\$ 520	\$ 547

The amortization of intangibles in 2007 related to the Company's software license agreement, customer relationships and patent license agreements. These intangible assets resulted from the acquisition of ORMI and A&A in 2002 and became fully amortized in 2007, following the write-off of the \$992,000 remaining on the direct land application patent ("DLAP"). Also in the fourth quarter, rental compactors were written down by \$235,000 and a future income tax recovery of \$1,135,000 was realized on the basis of an assessment of tax recoverability.

The fourth quarter of fiscal 2008 includes the impairment loss of \$1,383,000 on the goodwill relating to the acquisition of A&A by the Company in 2002.

The credit balance in non-cash expenses for the most recent quarter is due to the gain on the sale of the A&A non-core assets.

Adjusted net earnings excluding non-cash expenses as displayed in the table below is a non-GAAP measure that does not have any standardized meaning prescribed by GAAP and is therefore unlikely to be comparable to similar measures presented by other issuers. It should not be construed as an alternative to net earnings or cash flow from operating activities determined in accordance with GAAP.

**ADJUSTED NET EARNINGS  
EXCLUDING NON-CASH EXPENSES**

Quarter Ending:	Fiscal 2009		Fiscal 2008				Fiscal 2007	
	Dec. 31 2008	Sep. 30 2008	Jun. 30 2008	Mar. 31 2008	Dec. 31 2007	Sep. 30 2007	Jun. 30 2007	Mar. 31 2007
(in 000's)								
Net income (loss)	\$ 1,471	\$ 175	\$(1,286)	\$ (139)	\$ 82	\$ 114	\$ (836)	\$ (264)
Non-cash expenses	(1,408)	338	1,682	165	234	196	520	547
Adjusted net earnings excluding non-cash expenses	63	513	396	26	316	310	(316)	283
Changes in operating assets and liabilities	275	(131)	(313)	484	(478)	(209)	448	14
Cash flows from operating activities	\$ 338	\$ 382	\$ 83	\$ 510	\$ (162)	\$ 101	\$ 132	\$ 297

**Liquidity and Capital Resources**

Cash flows from operating activities were \$338,000 for the three months ended December 31, 2008 compared to cash used in operating activities of \$162,000 for the same period last year. The main reason for the change was a \$706,000 decrease in accounts receivable in the current quarter following the sale of A&A's non-core business.

During the quarter, the Company added one vacuum truck and one service vehicle to its fleet under capital lease for a total cost of \$206,000. During the same period last year, the Company added four vacuum trucks at a total cost of \$633,000.

On October 31, 2008, as part of the sale of A&A's non-core assets, McRae's assumed the face value of obligations under capital lease relating to three trucks that it acquired in the amount of \$255,000. The book value of these obligations was \$272,000 resulting in a gain on disposal of \$17,000.

On December 29, 2008, the Company replaced the privately held mortgage on its Toronto facility, in the amount of \$555,000 with a mortgage held by the Business Development Bank of Canada ("BDC"). Under the terms of the BDC loan, the Company can draw up to \$850,000. The Company plans to utilize the full amount available in order to upgrade the facility. The 25 year mortgage is based on BDC's floating base rate, which on January 29, 2008 was 4.75%. The BDC loan is secured by the Toronto facility and a general security agreement that provides security in all present and future assets that are not subject to prior charges, and by a guarantee of the Company's subsidiary, ORMI BC. The loan is not subject to any specific financial covenants.

The Company's revolving loan decreased in the quarter by \$560,000 from \$816,000 at September 30, 2008 to \$256,000 at December 31, 2008, mainly due to the application of the proceeds from the sale of A&A's non-core assets. For the same reason, the Company's cash and cash equivalents increased by \$589,000 during this period, from \$274,000 to \$863,000.

**Management of Capital**

The Company's objectives in its management of capital are to maintain a flexible capital structure which optimizes the cost of capital at acceptable risk, to maintain investor, creditor and market confidence in order to sustain the future development of the business, and to deliver value to its shareholders.

The capital structure of the Company consists of revolving bank loans, short and long-term debt facilities, and shareholders' equity. The basis for the Company's capital structure is dependent on the Company's expected business growth, reinvestment in plant, property and equipment, and changes in the business environment. Management is responsible for ensuring that financing is structured under the most favourable terms and conditions in light of current and expected economic conditions. Capital transactions are subject to the approval of the Company's Board of Directors.

The Company monitors its capital structure and financial leverage based on a number of key ratios. The Company's Board of Directors reviews these ratios and other key measurements on a quarterly basis and as part of the Company's strategic planning and budgeting process.

The Company is not subject to any financial ratios under its banking covenant, however it must maintain a minimum tangible net worth and comply with certain asset turns measures. The Company is in compliance with its covenant requirements.

## **Financial Instruments and Financial Risk Management**

The Company's financial instruments include cash and cash equivalents, accounts receivable, revolving loans, accounts payable and accrued liabilities, and long term debt. The carrying values of these financial instruments approximate their fair values due to their relatively short periods to maturity.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities. The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments.

Information on the Company's financial instruments and financial risk management is discussed in Note 14 to the unaudited interim consolidated financial statements for the six months ended December 31, 2008.

## **Strategy and Corporate Outlook**

The sale of A&A's non-core assets has strengthened the Company's balance sheet and will allow the Company to focus on its core business of servicing grease interceptors and collecting and recycling food-related organic residuals. In addition, the BC operations moved during the quarter to a new Vancouver area service hub located on Annacis Island, which will allow the Company to expand its grease trap and organics collection business. The new facility is properly zoned for commercial organic recycling and collection and includes the necessary infrastructure required to establish an organic residuals processing facility similar to ORMI's Ontario facilities. The Company plans to use this facility to produce the same type of high-energy feedstock for anaerobic digestion as it does in Ontario.

In July 2007, the Company signed the first exclusive, 20-year contract to supply organic residuals as feedstock to an on-farm anaerobic digester ("AD") for the production of renewable biogas energy. The Klaesi AD located west of Ottawa, was the first Ontario on-farm AD to obtain all the necessary permits, including the Ontario Ministry of Environment ("MOE") Certificate of Approval for the use of off-farm organic residuals as a feedstock. Under the first stage of the contract, ORMI has been delivering small quantities of feedstock to the Klaesi AD for the past 15 months. The expansion of the Klaesi's operations was completed by the end of the Company's second quarter of fiscal 2009; however, the connection to the grid was delayed and is anticipated to be completed during the third quarter of fiscal 2009. The newly expanded AD should reach maximum capacity within 90 days of coming on-stream. Once fully functional, the AD is expected to generate approximately 500 kW, 24 hours per day, 7 days per week.

In August and September 2008 the Company signed three more exclusive, 20-year agreements to supply organic residuals to the following Ontario farm-based ADs:

- (i) Ledgecroft Farms Inc., located north of Kingston at Seeley's Bay;
- (ii) Donnandale Farms Inc., located north of Belleville at Stirling;
- (iii) Clearydale Farms Inc., located north of Prescott at Spencerville.

Two of these ADs are expected to be fully operational by the end of fiscal 2009 and the third AD should be fully operational during the second quarter of fiscal 2010. Each AD is expected to generate approximately the same level of energy output as the Klaesi AD.

During the term of the agreements, ORMI will deliver a minimum of 5,000 cubic metres per year of organic residuals to each facility. ORMI will pay a “Tip Fee” that will be adjusted downward based on the actual performance of biogas renewable energy produced from ORMI’s high-energy organic feedstock, which is expected to generate in excess of 75% of the energy produced by the ADs. The resulting net Tip Fee is expected to be significantly more competitive than other organic residual recycling options currently available. In effect, ORMI will share the power generation revenue that its residuals produce. By the end of fiscal 2010, with the above four farms in full production, the Company expects to be the major feedstock source for the generation of approximately 2.0 MW of electricity, enough energy to supply 1600 homes.

In September 2008, the Company also commenced transporting some of its residuals to New York based ADs. The total cost of this method of disposal is approximately equal to the combined Tip Fee and transport costs related to non-AD Ontario disposal sites.

## **Risks and Uncertainties**

### **Technology and Competition**

The Company’s success depends on remaining competitive in the development of systems, technologies and services in its area of expertise. Competition in the food-related organic residuals waste services industry is intense and expected to increase, both from within the industry and from those diversifying into the field. Some of the Company’s competitors and potential competitors may have greater development, financial or personnel resources.

The Company is subject to the risks generally associated with new systems development and deployment, including lack of acceptance, delays in development and failure of systems to function properly. The market growth potential is subject to certain risks, including costs to develop and deploy such systems, the cost and feasibility of development, introduction of competing technologies and regulatory forces.

The Company has offset the erosion to the gross margin that occurred from the increase in Ontario recycling costs by increasing rates several times to Ontario based customers over the last several years. The Company has successfully increased customer rates in the past, but with any price increase there is a risk that accounts could be lost.

### **Government Regulation**

The Company is actively working on additional potential AD sites that, if successfully funded and permitted, would result in an Ontario in-province solution for the residuals the Company collects. This additional capacity would allow the Company to pursue a number of long-term contracts that it is unable to acquire today because of a lack of secure and competitively priced recycling options. The development of AD sites is subject to regulatory requirements and specific standards that must be met in order to connect to the Hydro One distribution grid.

The movement of residuals across the border to New York ADs is subject to government regulations that stipulate the nature and content of the residuals that can be transported. These regulations are subject to change, which could impact the Company’s ability to continue transporting residuals to these ADs.

Over the past few years the Company has been impacted by a number of government regulatory changes that directly affect the way liquid organic waste is handled and processed in Ontario. As a result of these changes, most of the third-party recycling facilities in Ontario that receive and process liquid organic waste significantly reduced their capacity, or closed down altogether. This had a major impact on the cost of disposing the Company’s residuals since it has had to transport a large portion of its residuals to alternative third-party recycling sites located in Quebec.

During the first quarter of this year, the Quebec disposal site which received some of the Company’s residuals went out of business. Although the Company was able to source an alternate disposal site in Ontario, the Company, with the exception of its AD contracts, has no long-term contracts with these

recycling sites and therefore cannot predict with certainty the volume of material they will continue to receive. The Company's profitability can be materially impacted by the volume of residuals these disposal sites receive.

### **Environmental Protection**

The Company provides vacuum truck services for the collection and recycling of organic and other food-related organic residuals. The Company does not believe it has any significant risks or exposures with respect to environmental protection, as the residuals it collects and transports are non-hazardous.

The Company stopped using the last of its DLAP sites in 2007 and now transports its food-related organic residuals to third-party disposal sites. The Company has not experienced any significant environmental issues relating to the closure of its DLAP sites.

### **Financial Risk**

Although the Company does not have any significant exposure to credit, liquidity or market risk as a result of its use of financial instruments based on management's assessment, there can be no absolute assurance that operating levels will not change over the ensuing fiscal year such that the Company would be unable to meet its current working capital and debt service requirements. In addition, other factors, not presently known to management, could materially and adversely affect the Company's future cash flow. In such events, the Company would be required to obtain additional capital as is necessary to satisfy working capital and debt service requirements from other sources. Alternative sources of capital could result in increased dilution to shareholders and may be on terms that are not favourable to the Company.

### **Acquisitions**

The Company is seeking acquisitions that are a good fit for its strategic direction. The Company does not have control over the market conditions prevailing or likely to prevail in the future, which may impact the ability to finance and execute this strategy. These variables include market valuations of potential targets and the Company's stock price volatility. There can be no assurances that the Company will be able to identify suitable acquisition candidates available for sale at reasonable valuations, consummate any acquisition or successfully integrate any acquired business into its operations. However, the Company continues to believe that with its technologies, systems and experienced management team, it is uniquely positioned to capitalize on a substantial opportunity.

### **Labour**

ORMI's hourly employees at its Toronto operation are represented by the Universal Workers Union Local 183 under a three year contract that runs from October 1, 2006 to September 30, 2009. The hourly employees at ORMI BC are under a three year collective agreement with the Service Employees Union from May 1, 2007 to April 30, 2010.

### **Dependence on Key Personnel**

The Company's success will depend to a significant extent upon its management group. The loss of the services of key executive personnel could have a material adverse effect on the Company.

### **Contingencies**

On February 3, 2009 the Company received a statement of claim in the amount of \$31 million pertaining to a traffic accident which occurred in September 2008. The claim by the injured party exceeds the combined limit of the Company's insurance coverage of \$10 million. The outcome of this claim is not determinable at this time and accordingly, no provision has been established in the consolidated financial statements ending December 31, 2008.

## **Critical Accounting Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates and assumptions include those related to: the valuation of goodwill; property, plant and equipment; share based compensation; and recoverability of future income tax assets. Actual results could differ from these estimates.

## **Changes in Accounting Policies**

Effective July 1, 2008, the Company adopted the following new accounting standards issued by the Canadian Institute of Chartered Accountants (“CICA”):

- (i) Handbook Section 1400, “General Standards of Financial Statement Presentation”. This section was amended to include requirements to assess and disclose an entity’s ability to continue as a going concern. The adoption of this section did not result in any changes in disclosure within the Company’s interim consolidated financial statements.
- (ii) Handbook Section 1535, “Capital Disclosures”. This section establishes standards for disclosing information about an entity’s objectives, policies, and processes for managing capital, including quantitative data. The additional disclosure required as a result of this section is included in Note 11 of the interim consolidated financial statements.
- (iii) Handbook Section 3031, “Inventories”. This section establishes new standards for the measurement and disclosure of inventories. The adoption of this standard did not affect the presentation of the financial statements. The additional disclosure required as a result of this section is included in Note 4 of the interim consolidated financial statements.
- (iv) Handbook Section 3862, “Financial Instruments’ Disclosure” and Handbook Section 3863, “Financial Instruments’ Presentation”. These sections revise and enhance the disclosure requirements and carry forward, substantially unchanged, the presentation requirements. These standards also emphasize the significance of financial instruments for the entity’s financial position and performance, the nature and extent of risks arising from financial instruments, and how these risks are managed. The additional disclosure required as a result of this section is included in Note 14 of the interim consolidated financial statements.

The above sections have been applied prospectively, with the exception of Section 3031 which is required to be applied retrospectively, although it had no impact on the interim consolidated financial statements.

## **Pending Accounting Pronouncements**

### **Goodwill and Intangible Assets**

CICA Handbook Section 3064, “Goodwill and Intangible Assets” intends to reduce the differences with international financial reporting standards (“IFRS”) in the accounting for intangible assets. Under current Canadian standards, more items are recognized as assets than under IFRS. These changes are effective for fiscal years beginning on or after October 1, 2008. The Company is currently evaluating the effects of adopting this standard which is expected to enhance current note disclosure.

### **International Financial Reporting Standards**

The Canadian Accounting Standards Board has confirmed that the use of IFRS will be required in 2011 for publicly accountable profit-oriented enterprises, replacing Canada’s current GAAP for those enterprises. The official changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. As a result, the Company will be required to provide financial statements on the new basis, with comparative information for the previous fiscal year,

effective July 1, 2011. As of the date of these financial statements, the financial reporting impact of the transition to IFRS cannot be reasonably determined.

## **Disclosure Controls and Procedures and Internal Control Over Financial Reporting**

In accordance with the Canadian Securities Administrators Multilateral Instrument 52-109, the Company has filed certificates signed by the Chief Executive Officer and the Chief Financial Officer that, among other things, report on the design of disclosure controls and procedures and the design of internal control over financial reporting.

The Company has designed disclosure controls and procedures to provide reasonable assurance that material information relating to the Company is made known to the Chief Executive Officer and the Chief Financial Officer, particularly during the period in which the interim filings are being prepared.

The Company has designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

No change in the Company's internal control over financial reporting occurred during the second quarter of fiscal 2009 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **Subsequent Event**

### **Revolving loan**

On January 30, 2009 the Company terminated its relationship with Textron Financial Canada Ltd. and paid off the balance owing on its revolving loan. On February 6, 2009, the Company established with the Royal Bank of Canada ("RBC"), a \$2,000,000 revolving demand facility (at an annual interest rate of prime plus 1.5%) and a \$500,000 term facility (at an annual interest rate of prime plus 1.25%, repayable over 60 months). Security was provided by a general security agreement with a first ranking security interest in all personal property of the Company, a security agreement (chattel mortgage) with a first ranking security interest in all equipment funded by RBC, and a guarantee and postponement of claims in the amount of \$2,000,000 by the Company's subsidiary, ORMI BC. The Company has provided covenants whereby it will maintain on a consolidated basis, to be measured as at the end of each fiscal quarter, debt service coverage of not less than 1.25:1 and the ratio of total liabilities to tangible net worth of not greater than 2.75:1.

## **Additional Information**

Further information about ORMI may be obtained at the Company's web site at [www.ormi.com](http://www.ormi.com).

Interim Consolidated Financial Statements of  
**ORGANIC RESOURCE MANAGEMENT INC.**

(Unaudited)

For the three and six months ended December 31, 2008

*The accompanying unaudited interim financial statements of the Company for the three and six months ended December 31, 2008 have been prepared by and are the responsibility of the Company's management.*

*The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of the interim financial statements by an entity's auditor.*

**ORGANIC RESOURCE MANAGEMENT INC.**  
**INTERIM CONSOLIDATED BALANCE SHEETS**

	DECEMBER 31 2008 (UNAUDITED)	JUNE 30 2008 (AUDITED)
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash and cash equivalents	\$ 862,916	\$ 33,269
Accounts receivable	1,699,505	2,240,715
Inventory (Note 4)	80,310	132,388
Prepaid expenses	317,952	206,367
Current portion of long-term notes receivable	115,000	-
Current portion of future income tax asset	444,000	444,000
	<b>3,519,683</b>	<b>3,056,739</b>
LONG-TERM NOTES RECEIVABLE (Note 5)	449,545	-
PROPERTY PLANT AND EQUIPMENT (Note 6)	3,828,976	4,130,740
GOODWILL	2,434,793	2,434,793
FUTURE INCOME TAX ASSET	1,078,619	1,267,000
	<b>\$ 11,311,616</b>	<b>\$ 10,889,272</b>
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Revolving loan	\$ 256,078	\$ 765,795
Accounts payable and accrued liabilities	1,403,641	1,740,598
Current portion of long-term debt	213,229	169,886
Current portion of obligations under capital lease	304,851	338,527
Current portion of future income tax liability	44,561	44,561
	<b>2,222,360</b>	<b>3,059,367</b>
LONG-TERM DEBT (Note 8 and Note 15)	1,050,208	1,238,457
OBLIGATIONS UNDER CAPITAL LEASE (Note 9)	876,677	1,065,373
FUTURE INCOME TAX LIABILITY	122,542	144,821
	<b>4,271,787</b>	<b>5,508,018</b>
<b>SHAREHOLDERS' EQUITY</b>		
COMMON SHARES	8,250,051	8,250,052
CONTRIBUTED SURPLUS	334,636	321,254
DEFICIT	(1,544,858)	(3,190,052)
	<b>7,039,829</b>	<b>5,381,254</b>
	<b>\$ 11,311,616</b>	<b>\$ 10,889,272</b>

Contingency (Note 10)

Subsequent events (Note 17)

*See accompanying notes to the consolidated financial statements. These interim financial statements should be read in conjunction with the 2008 annual consolidated financial statements.*

On behalf of the Board of Directors:



Charles H. Buehler, Director



Matthew Gaasenbeek, Director

**ORGANIC RESOURCE MANAGEMENT INC.**
**INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE INCOME AND DEFICIT  
UNAUDITED**

	6 Months Ended December 31		3 Months Ended December 31	
	2008	2007	2008	2007
<b>REVENUES</b>				
Non hazardous vacuum services	\$ 7,265,225	\$ 7,398,044	\$ 3,217,206	\$ 3,758,545
Compactor sales, service & rental income	-	124,985	-	41,702
	<b>7,265,225</b>	<b>7,523,029</b>	<b>3,217,206</b>	<b>3,800,247</b>
<b>COST OF SALES</b>	<b>4,710,616</b>	<b>5,060,917</b>	<b>2,179,170</b>	<b>2,536,169</b>
<b>GROSS MARGIN</b>	<b>2,554,609</b>	<b>2,462,112</b>	<b>1,038,036</b>	<b>1,264,078</b>
<b>OPERATING EXPENSE</b>				
Selling, general and administrative	1,834,489	1,705,092	909,298	873,563
Amortization of property, plant and equipment	476,181	338,967	236,774	192,555
Share based compensation	13,383	10,799	6,692	8,657
	<b>2,324,053</b>	<b>2,054,858</b>	<b>1,152,764</b>	<b>1,074,775</b>
<b>INCOME (LOSS) BEFORE THE UNDERNOTED</b>	<b>230,556</b>	<b>407,254</b>	<b>(114,728)</b>	<b>189,303</b>
<b>OTHER EXPENSE (INCOME)</b>				
Gain on disposal of property, plant and equipment	(1,225,498)	(35,786)	(1,218,972)	(15,720)
Gain on disposal of intangible assets (Note 7)	(500,000)	-	(500,000)	-
Interest on long-term debt and obligations under capital lease	108,613	85,805	51,416	50,275
Other interest	29,153	59,970	10,995	31,127
	<b>(1,587,732)</b>	<b>109,989</b>	<b>(1,656,561)</b>	<b>65,682</b>
<b>NET INCOME BEFORE INCOME TAXES</b>	<b>1,818,288</b>	<b>297,265</b>	<b>1,541,833</b>	<b>123,621</b>
<b>INCOME TAXES</b>				
Current income tax expense	6,993	-	3,499	-
Future income tax expense	166,101	101,189	67,827	41,049
	<b>173,094</b>	<b>101,189</b>	<b>71,326</b>	<b>41,049</b>
<b>NET INCOME AND COMPREHENSIVE INCOME</b> (Note 12)	<b>\$ 1,645,194</b>	<b>\$ 196,076</b>	<b>\$ 1,470,507</b>	<b>\$ 82,572</b>
<b>DEFICIT, BEGINNING OF YEAR / QUARTER</b>	<b>\$ (3,190,052)</b>	<b>\$ (9,541,600)</b>	<b>\$ (3,015,365)</b>	<b>\$ (9,428,096)</b>
Net income	1,645,194	196,076	1,470,507	82,572
Reduction of stated value of common shares	-	7,580,530	-	7,580,530
<b>DEFICIT, END OF QUARTER</b>	<b>\$ (1,544,858)</b>	<b>\$ (1,764,994)</b>	<b>\$ (1,544,858)</b>	<b>\$ (1,764,994)</b>
<b>INCOME PER SHARE</b> (Note 13)				
Basic	\$ 0.37	\$ 0.04	\$ 0.33	\$ 0.02
Diluted	0.35	0.04	0.31	0.02

See accompanying notes to the consolidated financial statements. These interim financial statements should be read in conjunction with the 2008 annual consolidated financial statements.

**ORGANIC RESOURCE MANAGEMENT INC.**  
**INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**UNAUDITED**

	6 Months Ended December 31		3 Months Ended December 31	
	2008	2007	2008	2007
<b>CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES</b>				
Net income	\$ 1,645,194	\$ 196,076	\$ 1,470,507	\$ 82,572
Add (deduct) items not involving cash:				
Amortization of property, plant and equipment	476,181	338,967	236,774	192,556
Accretion of interest expense	-	14,593	-	7,296
Share based compensation	13,383	10,799	6,691	8,657
Gain on disposal of property, plant and equipment	(1,225,498)	(35,786)	(1,218,972)	(15,720)
Gain on disposal of intangible assets	(500,000)	-	(500,000)	-
Future income tax expense	166,101	101,189	67,827	41,049
	<b>575,361</b>	<b>625,838</b>	<b>62,827</b>	<b>316,410</b>
Changes in operating assets and liabilities:				
Decrease (increase) in accounts receivable, net	541,211	105,973	706,171	(79,710)
Decrease (increase) in inventory	52,077	(135)	30,265	(7,258)
Increase in prepaid expenses	(111,587)	(11,110)	(80,587)	(27,110)
Decrease in accounts payable and accrued liabilities	(336,957)	(781,545)	(380,321)	(364,568)
	<b>720,105</b>	<b>(60,979)</b>	<b>338,355</b>	<b>(162,236)</b>
<b>CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES</b>				
Acquisition of property, plant and equipment	(296,041)	(422,208)	(127,114)	(376,984)
Acquisition of OIS software and NCS ESL patents	-	(119,663)	-	-
Proceeds on disposal of property, plant and equipment	1,205,947	67,018	1,196,996	31,846
	<b>909,906</b>	<b>(474,853)</b>	<b>1,069,882</b>	<b>(345,138)</b>
<b>CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES</b>				
Repayment of notes receivable	10,455	-	10,455	-
(Repayment) advance of revolving loan	(509,717)	477,184	(560,021)	56,774
Advance of long-term debt	95,530	331,724	4,775	331,724
Repayment of long-term debt	(240,435)	(151,425)	(203,917)	(49,176)
Repayment of capital lease obligations	(156,197)	(124,599)	(71,071)	(72,963)
	<b>(800,364)</b>	<b>532,884</b>	<b>(819,779)</b>	<b>266,359</b>
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>829,647</b>	<b>(2,948)</b>	<b>588,458</b>	<b>(241,015)</b>
<b>CASH AND CASH EQUIVALENTS BEGINNING OF YEAR / QUARTER</b>	<b>33,269</b>	<b>206,771</b>	<b>274,458</b>	<b>444,838</b>
<b>CASH AND CASH EQUIVALENTS END OF QUARTER</b>	<b>\$ 862,916</b>	<b>\$ 203,823</b>	<b>\$ 862,916</b>	<b>\$ 203,823</b>
Supplemental cash flow information:				
Interest paid	\$ 119,427	\$ 131,182	\$ 68,207	\$ 74,105
Non-cash transactions:				
Note receivable on sale of non-core assets (Note 5)	\$ 575,000	\$ -	\$ 575,000	\$ -
Refinancing of mortgage (Note 8)	555,460	-	555,460	-
Transfer of capital leases on sale of non-core assets (Note 9)	272,133	-	272,133	-
Capital assets acquired through capital leases	205,959	400,290	205,959	330,130
Acquisition of OIS software through notes payable	-	600,000	-	-

*See accompanying notes to the consolidated financial statements. These interim financial statements should be read in conjunction with the 2008 annual consolidated financial statements.*

# ORGANIC RESOURCE MANAGEMENT INC.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
DECEMBER 31, 2008

## 1. NATURE OF OPERATIONS

Organic Resource Management Inc. (the “Company” or “ORMI”) is incorporated under the Canada Business Corporations Act. The primary operations of the Company consist of providing vacuum truck services for the collection, processing and recycling of food-related organic residuals. The Company’s shares are listed on the Toronto Stock Exchange under the symbol “ORI”.

On September 29, 2008, the Company completed a voluntary wind-up of its two wholly-owned and inactive Bermuda companies, NCS Holdings Ltd. and NCS Environmental Services Ltd.

On October 31, 2008, the Company sold the non-core assets of its wholly-owned subsidiary, A&A Anderson Tank Services Ltd. (“A&A”), based in British Columbia, to McRae’s Environmental Services Ltd. (“McRae’s”) for \$2,075,000. Under the terms of the agreement, McRae’s purchased 17 trucks and trailers, parts inventory, A&A’s customer list for its non-core business and the rights to A&A’s name. Conversely, ORMI acquired McRae’s list of customers that relate to the Company’s core area of business. The purchase price was comprised of a cash payment of \$1,245,366, a note receivable for \$575,000 and the assumption of capital lease debt for \$254,634. The asset sale generated a net gain on disposal of \$1,707,742.

On November 5, 2008, A&A’s name was changed to Organic Resource Management (BC) Inc. (“ORMI BC”).

## 2. SIGNIFICANT ACCOUNTING POLICIES

### A. Basis of presentation

These unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (“GAAP”) for interim financial statements and follow the same accounting policies and methods outlined in the Company’s audited financial statements for the year ended June 30, 2008, except for the changes to the accounting policies noted below. The results of operations for the interim period are not necessarily indicative of the operating results for the full year. In the opinion of management, all adjustments considered necessary for a fair presentation of the results of operations for the interim period are reflected in these financial statements.

The unaudited interim consolidated financial statements do not include all the disclosures required according to GAAP for annual financial statements and should therefore be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended June 30, 2008 found on SEDAR at [www.sedar.com](http://www.sedar.com) or on the Company’s website at [www.ormi.com](http://www.ormi.com).

### B. Principles of consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, ORMI BC (active) and ORMI Information Systems Inc. (“OIS”, inactive), after the elimination of all material inter-company transactions and balances.

### C. Changes in accounting policies

On July 1, 2008, the Company adopted the following new accounting standards that were issued by the Canadian Institute of Chartered Accountants (“CICA”):

- (i) Handbook Section 1400, “General Standards of Financial Statement Presentation”, was amended to include requirements to assess and disclose an entity’s ability to continue as a going concern. This assessment takes into account all available information, which is at least but not limited to twelve months from the balance sheet date, and should disclose material uncertainties related to events or conditions that may cast doubt on the entity’s ability to continue as a going concern. The adoption of this section did not result in any changes in disclosure within the Company’s interim consolidated financial statements.

## **2. SIGNIFICANT ACCOUNTING POLICIES (cont'd)**

- (ii) Handbook Section 1535, "Capital Disclosures", establishes standards for disclosing information about an entity's objectives, policies, and processes for managing capital, the quantitative data relating to what the entity regards as capital, and whether the entity has complied with externally imposed capital requirements, and if it has not complied, the consequences of such non-compliance. The additional disclosure required as a result of this section is included in Note 11.
- (iii) Handbook Section 3031, "Inventories", establishes new standards for the measurement and disclosure of inventories, replacing the old Section 3030, "Inventories". Under the new section, inventories are required to be measured at the lower of cost and net realizable value, which is different from the existing guidance of the lower of cost and market. This section also requires, where applicable, the reversal of any write-downs previously recognized. The standard requires retrospective application with no restatement of prior year results. The adoption of this standard did not require re-statement of deficit or comparative figures, and does not effect the presentation of the financial statements. The additional disclosure required as a result of this section is included in Note 4.
- (iv) Handbook Section 3862, "Financial Instruments' Disclosure" and Handbook Section 3863, "Financial Instruments' Presentation" replace Handbook Section 3861, "Financial Instruments' Disclosure and Presentation". These new standards revise and enhance the disclosure requirements and carry forward, substantially unchanged, the presentation requirements. These standards also emphasize the significance of financial instruments for the entity's financial position and performance, the nature and extent of risks arising from financial instruments, and how these risks are managed. The additional disclosure required as a result of this section is included in Note 14.

The above sections have been applied prospectively, with the exception of Section 3031 which is required to be applied retrospectively, although it had no impact on these financial statements.

### **D. Use of estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates and assumptions include those related to: the valuation of goodwill and intangibles; estimated useful lives of intangibles, property, plant and equipment; share based compensation; and recoverability of future income tax assets. Actual results could differ from these estimates.

## **3. NEW ACCOUNTING PRONOUNCEMENTS**

### **A. Goodwill and intangible assets**

CICA Handbook Section 3064, "Goodwill and Intangible Assets", will replace CICA Handbook Section 3062, "Goodwill and Other Intangible Assets", and results in withdrawal of CICA Handbook Section 3450, "Research and Development Costs", and amendments to Accounting Guideline 11, "Enterprises in the Development Stage" and CICA Handbook Section 1000, "Financial Statement Concepts". Handbook Section 3064 intends to reduce the differences with International Financial Reporting Standards ("IFRS") in the accounting for intangible assets. Under current Canadian standards, more items are recognized as assets than under IFRS. The objectives of Handbook Section 3064 are to reinforce the principle-based approach to the recognition of assets only in accordance with the definition of an asset and the criteria for asset recognition; and clarify the application of the concept of matching revenues and expenses such that the current practice of recognizing as assets items that do not meet the definition and recognition criteria is eliminated. The standard will also provide guidance for the recognition of internally developed intangible assets (including research and development activities), ensuring consistent treatment of all intangible assets, whether separately acquired or internally developed. These changes are effective for fiscal years beginning on or after October 1, 2008. The Company is currently evaluating the effects of adopting this standard, which is expected to enhance current note disclosure.

### 3. NEW ACCOUNTING PRONOUNCEMENTS (cont'd)

#### B. International Financial Reporting Standards

The Canadian Accounting Standards Board has confirmed that the use of IFRS will be required in 2011 for publicly accountable profit-oriented enterprises, replacing Canada's current GAAP for those enterprises. This includes listed companies and other profit-oriented enterprises that are responsible to large or diverse groups of stakeholders. The official changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. As a result, the Company will be required to provide financial statements on the new basis, with comparative information for the previous fiscal year, effective July 1, 2011. As of the date of these financial statements, the financial reporting impact of the transition to IFRS cannot be reasonably determined.

### 4. INVENTORY

The Company's inventory is comprised of costs related to the manufacturing of grease traps, the purchase of spare parts for its fleet of trucks, the purchase for resale of Organic Resource Recovery System ("ORRS") machines and the purchase of diesel fuel. Inventory is valued at the lower of cost and net realizable value. Cost is determined on a first-in, first out ("FIFO") basis and net realizable value is considered to be the amount the Company expects to realize from the sale of its inventory in the ordinary course of business. Inventory is not pledged as security for the Company's credit facilities.

On October 31, 2008, the Company sold \$40,000 of its truck parts inventory to McRae's as part of the non-core asset sale described in Note 1, for proceeds of \$40,000.

### 5. NOTES RECEIVABLE

On October 31, 2008, the Company received a note from McRae's in the amount of \$575,000 as part of the non-core asset sale described in Note 1. The note is secured by a first charge on certain trucks and is repayable in 55 equal monthly installments of principal with interest at prime plus 0.25%. On December 31, 2008, the effective rate of interest on the note was 3.75%.

### 6. PROPERTY, PLANT AND EQUIPMENT

On October 31, 2008, the Company sold its non-core property, plant and equipment to McRae's as described in Note 1, comprised of the following:

	<b>Cost</b>	<b>Accumulated Amortization</b>	<b>Net</b>
Vehicles (owned)	<b>1,759,145</b>	1,709,260	49,885
Vehicles under capital lease	<b>435,262</b>	196,619	238,643
Machinery and equipment	<b>50,852</b>	32,529	18,323
Office furniture, equipment and computers	<b>25,379</b>	10,973	14,406
	<b>2,270,638</b>	1,949,381	321,257

The net proceeds of the sale allocated to property, plant and equipment was \$1,511,500 resulting in a gain on disposal of \$1,190,243.

## **7. INTANGIBLE ASSETS**

The sale of the Company's customer list relating to its non-core business to McRae's on October 31, 2008 for proceeds of \$500,000, as described in Note 1, generated a gain on disposal of intangible assets of \$500,000.

As part of the sale, the Company acquired McRae's list of customers that relate to the Company's core area of business. The Company estimates that the revenue generated from these customers could be approximately \$300,000 per year. The Company has not established any asset value for these prospective customer relationships since the Company does not have control of the asset as there are no contracts in force, and since the costs that will have to be incurred to secure the relationships can not be reliably measured. In addition, the impact of these customer relationships on incremental revenues is estimated to be less than 3% of the Company's total revenue.

## **8. LONG-TERM DEBT**

On December 29, 2008, the Company replaced the privately held mortgage on its Toronto facility, in the amount of \$555,460, with a mortgage held by the Business Development Bank of Canada ("BDC"). Under the terms of the BDC loan, the Company can draw up to \$850,000. The Company plans to utilize the full amount available in order to upgrade the facility. The 25 year mortgage is based on BDC's floating base rate, which on January 29, 2008 was 4.75%.

The BDC loan is secured by the Toronto facility and a general security agreement that provides security in all present and future assets that are not subject to prior charges, and by a guarantee of the Company's subsidiary, ORMI BC, for 25% of the total loan commitment. The loan is not subject to any specific financial covenants.

## **9. OBLIGATIONS UNDER CAPITAL LEASE**

On October 31, 2008, McRae's assumed the face value of obligations under capital lease relating to three trucks that it acquired, as described in Note 1, in the amount of \$254,634. The book value of these obligations was \$272,133 resulting in a gain on disposal of \$17,499.

## **10. CONTINGENCY**

On February 3, 2009 the Company received a statement of claim in the amount of \$31 million pertaining to a traffic accident which occurred in September 2008. The claim by the injured party exceeds the combined limit of the Company's insurance coverage of \$10 million. The outcome of this claim is not determinable at this time and accordingly, no provision has been established in these consolidated financial statements.

## **11. MANAGEMENT OF CAPITAL**

The Company's objectives in its management of capital are to maintain a flexible capital structure which optimizes the cost of capital at acceptable risk, to maintain investor, creditor and market confidence in order to sustain the future development of the business, and to deliver value to its shareholders. The capital structure of the Company consists of revolving bank loans, short and long-term debt facilities, and shareholders' equity. The basis for the Company's capital structure is dependent on the Company's expected business growth, reinvestment in plant, property and equipment, and changes in the business environment. Management is responsible for ensuring that financing is structured under the most favourable terms and conditions in light of current and expected economic conditions. Capital transactions are subject to the approval of the Company's Board of Directors.

The Company monitors its financial leverage based on the ratio of total debt (net of future tax liabilities) to tangible net worth, which is defined as shareholders' equity less goodwill, intangible assets, future tax assets and deferred charges. The Company's objective is to maintain a total debt to tangible net worth ratio of less than 5.0:1. As at December 31, 2008, the Company's total debt to tangible net worth was 1.3:1 compared to a ratio of 3.7:1 as at June 30, 2008. The Company is not subject to any financial ratios under its banking covenant, however

## 11. MANAGEMENT OF CAPITAL (cont'd)

it must maintain a minimum tangible net worth of \$900,000 and accounts receivable turns cannot exceed 60 days on average. The Company is in compliance with these covenants.

The Company also monitors its capital structure based on the ratio of net debt to annualized cash flow (before changes in non-cash working capital from operating activities). Net debt is defined as long-term debt, long-term obligations under capital lease and net working capital, excluding future tax assets and liabilities. The Company's objective is to maintain a net debt to annualized cash flow from operations ratio of less than 3.0:1. As at December 31, 2008, the Company's net debt to annualized cash flow from operations was 0.9:1 compared to a ratio of 2.6:1 as at June 30, 2008.

The Company's Board of Directors reviews these ratios and other key measurements on a quarterly basis and as part of the Company's strategic planning and budgeting process.

## 12. COMPREHENSIVE INCOME

Comprehensive income is defined as the change in net assets of an enterprise during a reporting period from transactions and other events and circumstances from non-owner sources. It includes all changes in net assets during a period except those resulting from investments by owners and distributions to owners. A separate statement of comprehensive income has not been presented as there is no difference between net income and comprehensive income.

## 13. INCOME PER SHARE

The following table sets forth the number of shares used in the computation of basic and fully diluted income per share as at December 31, 2008:

	2008	2007
Weighted average shares for basic income per share	4,404,935	4,404,935
Stock options	284,959	250,429
Adjusted weighted average shares for diluted income per share	4,689,894	4,655,364

Income per share data has been restated for the prior year on the basis of the one-for-twenty share consolidation which occurred on November 30, 2007.

## 14. FINANCIAL INSTRUMENTS

### A. Fair value

The Company classifies its financial instruments into one of the following categories:

- cash and cash equivalents as “assets held-for-trading” - measured at fair value;
- trade and other accounts receivable and notes receivable as “loans and receivables” - measured at amortized cost;
- revolving loans, accounts payable and accrued liabilities, and long-term debt as “other financial liabilities” - measured at amortized cost.

All financial instruments are initially recognized at fair value on the balance sheet date. Subsequent measurement of financial instruments is based on their classification. Assets held-for-trading are measured at fair value with changes recognized in net income. Loans and receivables and other financial liabilities are measured at amortized cost using the effective interest method. The carrying values of current financial instruments approximate their fair values due to the relatively short period to maturity. The carrying values of long-term debt and obligations under capital lease also approximates their fair values since the terms and interest rates are consistent with current market terms and rates for such borrowings.

## 14. FINANCIAL INSTRUMENTS (cont'd)

### B. Risk Management

The Company is exposed to financial risks of varying degrees of significance which could affect its ability to achieve its strategic objectives. The main objectives of the Company's risk management process are to ensure that risks are properly identified and that measures are taken to mitigate the risks whenever possible.

#### Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to interest rate risks on its revolving loan and a portion of its long-term debt which bear variable interest rates. Management does not believe that the impact of interest rate fluctuations on the current level of borrowings bearing variable rates will be material and therefore, has not provided a sensitivity analysis of the impact of fluctuations on net earnings and comprehensive income.

#### Credit risk

Credit risk is the risk that a customer will be unable to pay the Company in full when amounts become due. Management considers accounts not paid within 60 days to be past due. As at December 31, 2008, the portion of receivables aged over 60 days represented 20% of total receivables. Of this amount, less than 8% of the accounts were aged over 90 days.

An allowance for doubtful accounts is established based upon factors surrounding the credit risk of specific customers, historical trends and other information. When a receivable balance is considered uncollectible, it is written off against the allowance for doubtful accounts. The Company updates its estimate of the allowance for doubtful accounts on a monthly basis, based on a customer-by-customer review of past due balances. As at June 30, 2008 and December 31, 2008, the allowance for doubtful accounts was \$12,000. During the six months ending December 31, 2008, \$10,000 was written off to bad debts.

Considering that historically, bad debt expense has been less than 1% of total revenue, management does not believe the Company is subject to any material credit risk corresponding to accounts receivable.

The Company's exposure to credit risk is limited to the total carrying value of its accounts receivable recognized on the balance sheet.

#### Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with its financial obligations as they become due. The Company's growth is financed through a combination of the cash flow from operations, borrowing under the existing credit facilities and potentially, the issuance of equity. The Company manages its liquidity risk by forecasting cash flows from operations and anticipated investing and financing activities, and maintaining credit facilities to ensure it has sufficient funds available to meet current and foreseeable financial requirements.

As at December 31, 2008, the following are the contractual maturities of the Company's liabilities:

	Carrying Amount	Less Than 1 Year	1 to 2 Years	More Than 2 Years
Revolving loan	256,078	256,078	-	-
Accounts payable and accrued liabilities	1,403,641	1,403,641	-	-
Long-term debt	1,263,437	212,944	233,829	816,664
Obligations under capital lease	1,181,528	305,273	331,343	544,912
Total	4,104,684	2,177,936	565,172	1,361,576

Cash and cash equivalents and accounts receivable were \$2,562,421 on this date. The Company generated a positive cash flow from operating activities of \$575,000 for the first six months of the year (\$626,000 for the same period last year), before changes in non-cash working capital.

Given the Company's positive cash flows and liquid resources as compared to the timing of the payments of its liabilities, management assesses the Company's liquidity risk to be minimal.

## 14. FINANCIAL INSTRUMENTS (cont'd)

### Currency risk

The foreign exchange risk is the risk to the Company's earnings that arises from fluctuations in foreign exchange rates and the degree of volatility of these rates. The Company does not have a material exposure to these risks as the extent of business transactions in foreign currencies is minimal.

## 15. RELATED PARTY TRANSACTIONS

During the quarter, the Company paid down the note held by one of the Company's directors by \$150,000. This note relates to the purchase of the outstanding shares of OIS on September 19, 2007. As at December 31, 2008, the Company had notes payable of \$344,131 to directors and/or companies related to them, down from \$538,003 on June 30, 2008. These amounts are included in long-term debt.

## 16. COMPARATIVE FIGURES

Certain of the comparative figures have been reclassified to conform to the financial statement presentation adopted in the current year. This reclassification includes transaction costs which were accounted for as deferred financing costs in the first three quarters of fiscal 2008.

## 17. SUBSEQUENT EVENT

On January 30, 2009 the Company terminated its relationship with Textron Financial Canada Ltd. and paid off the balance owing on its revolving loan. On February 6, 2009, the Company established the following lines of credit with the Royal Bank of Canada ("RBC"):

- (i) \$2,000,000 revolving demand facility based on 75% of eligible accounts receivable at an annual interest rate of RBC prime plus 1.5%;
- (ii) \$500,000 term facility at an annual interest rate of RBC prime plus 1.25%, repayable over 60 months.

Security is provided by:

- (i) a general security agreement constituting a first ranking security interest in all personal property of ORMI and ORMI BC;
- (ii) a security agreement (chattel mortgage) constituting a first ranking security interest in all equipment; and
- (iii) a guarantee and postponement of claim in the amount of \$2,000,000 by ORMI BC.

The Company has provided covenants whereby it will maintain on a consolidated basis, to be measured as at the end of each fiscal quarter:

- (i) debt service coverage, calculated on a rolling four quarter basis, of not less than 1.25:1;
- (ii) a ratio of total liabilities to tangible net worth of not greater than 2.75:1.