

Consolidated Financial Statements

COOLBRANDS INTERNATIONAL INC.

Years ended August 31, 2009 and 2008

CoolBrands International Inc.

AUDITORS' REPORT

To the Shareholders of CoolBrands International Inc.:

We have audited the consolidated balance sheets of CoolBrands International Inc. as at August 31, 2009 and 2008 and the consolidated statements of income and other comprehensive income, shareholders' equity and cash flows for the years ended August 31, 2009 and 2008. These consolidated financial statements are the responsibility of the Company's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of CoolBrands International Inc. as at August 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

“PricewaterhouseCoopers LLP”

Chartered Accountants, Licensed Public Accountants
Toronto, Canada
November 18, 2009

CoolBrands International Inc.

Consolidated Balance Sheets as at August 31, 2009 and 2008
(Amounts expressed in thousands of Canadian dollars)

| | 2009 | 2008 |
|---|-------------|-------------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents (Note 5) | \$ 17,907 | \$ 8,372 |
| Short-term investments (Note 5) | 43,991 | 52,800 |
| Interest receivable | 821 | 726 |
| Current assets of discontinued operations (Note 6) | 135 | 299 |
| Prepaid expenses | 88 | 158 |
| Other assets (Note 8) | 3,575 | 3,489 |
| | <hr/> | <hr/> |
| Total current assets | 66,517 | 65,844 |
| Capital assets (Note 7) | 84 | 157 |
| Other assets (Note 8) | 483 | 532 |
| | <hr/> | <hr/> |
| | \$ 67,084 | \$ 66,533 |
| | <hr/> <hr/> | <hr/> <hr/> |
| Liabilities and Shareholders' Equity | | |
| Current Liabilities: | | |
| Accounts payable and accrued liabilities | \$ 205 | \$ 244 |
| Current liabilities of discontinued operations (Note 6) | 3,163 | 4,550 |
| | <hr/> | <hr/> |
| Total current liabilities | 3,368 | 4,794 |
| Other liabilities (Note 10) | 2,686 | 2,783 |
| | <hr/> | <hr/> |
| Total liabilities | 6,054 | 7,577 |
| | <hr/> | <hr/> |
| Contingencies (Note 17) | | |
| Shareholders' Equity: | | |
| Capital stock (Note 11) | 61,972 | 61,972 |
| Contributed surplus | 54,070 | 53,998 |
| Accumulated other comprehensive loss | (45,466) | (45,466) |
| Deficit | (9,546) | (11,548) |
| | <hr/> | <hr/> |
| Total shareholders' equity | 61,030 | 58,956 |
| | <hr/> | <hr/> |
| | \$ 67,084 | \$ 66,533 |
| | <hr/> <hr/> | <hr/> <hr/> |

See accompanying notes to consolidated financial statements.

Approved by the Board of Directors

“Michael Serruya”

Michael Serruya, Director

“Ron Binns”

Ron Binns, Director

CoolBrands International Inc.

Consolidated Statements of Income and Other Comprehensive Income for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars, except for per share data)

| | 2009 | 2008 |
|--|-----------------|-----------------|
| Revenue | | |
| Interest and other | \$ 1,447 | \$ 2,747 |
| Expenses | | |
| General and administrative | 1,532 | 1,731 |
| Income (loss) before the following | <u>(85)</u> | <u>1,016</u> |
| Gain (loss) on foreign exchange | <u>1,888</u> | <u>(23)</u> |
| Net income from continuing operations before income taxes | <u>1,803</u> | <u>993</u> |
| Provision for income taxes (Note 12): | | |
| Current | - | - |
| Future | <u>-</u> | <u>-</u> |
| | <u>-</u> | <u>-</u> |
| Net income from continuing operations | <u>1,803</u> | <u>993</u> |
| Discontinued operations: | | |
| Net income from discontinued operations (Note 6) | <u>199</u> | <u>4,403</u> |
| Net income and other comprehensive income for the year | <u>\$ 2,002</u> | <u>\$ 5,396</u> |
| Earnings per share (Note 11) | | |
| Continuing operations – basic and diluted | \$ 0.03 | \$ 0.02 |
| Discontinued operations – basic and diluted | \$ 0.00 | \$ 0.08 |
| Total | | |
| - basic | \$ 0.04 | \$ 0.10 |
| - diluted | \$ 0.03 | \$ 0.09 |

See accompanying notes to consolidated financial statements.

CoolBrands International Inc.

Consolidated Statements of Shareholders' Equity for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

| | Capital stock | Contributed surplus | Accumulated other comprehensive loss (Note 2) | Deficit | Total shareholders' equity |
|---|--------------------------|--------------------------------|--|-------------------|---|
| Balance as at August 31, 2007 | \$ 139,388 | \$ 53,941 | \$ (45,466) | \$ (94,360) | \$ 53,503 |
| Income and other comprehensive income for the year | - | - | - | 5,396 | 5,396 |
| Reduction in stated capital (Note 11) | (77,416) | - | - | 77,416 | - |
| Stock-based compensation | - | 57 | - | - | 57 |
| Balance as at August 31, 2008 | 61,972 | 53,998 | (45,466) | (11,548) | 58,956 |
| Income and other comprehensive income for the year | - | - | - | 2,002 | 2,002 |
| Stock-based compensation | - | 72 | - | - | 72 |
| Balance as at August 31, 2009 | <u>\$ 61,972</u> | <u>\$ 54,070</u> | <u>\$ (45,466)</u> | <u>\$ (9,546)</u> | <u>\$ 61,030</u> |

See accompanying notes to consolidated financial statements.

CoolBrands International Inc.

Consolidated Statements of Cash Flows for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

| | 2009 | 2008 |
|---|------------------|-----------------|
| Cash and cash equivalents provided by (used in): | | |
| Operating activities: | | |
| Income from continuing operations | \$ 1,803 | \$ 993 |
| Adjustments to reconcile income to net cash flows from operating activities | | |
| Depreciation and amortization | 73 | 180 |
| Stock-based compensation | 72 | 57 |
| Change in fair value of short-term investments | 21 | (461) |
| Cash effect of changes from continuing operations | | |
| Interest receivable | (72) | (117) |
| Prepaid expenses | 70 | (24) |
| Accounts payable and accrued liabilities | (39) | (361) |
| Income taxes payable | - | (7) |
| Other assets | 364 | 1,743 |
| Other liabilities | (98) | (55) |
| Cash provided by operating activities | <u>2,194</u> | <u>1,948</u> |
| Investing activities: | | |
| Purchase of capital assets | - | (3) |
| Proceeds from sale of capital assets | - | 64 |
| Promissory note advances | (1,000) | - |
| Repayments of promissory note | 725 | - |
| Decrease (increase) in short-term investments | 8,915 | (50,248) |
| Cash provided by (used in) investing activities | <u>8,640</u> | <u>(50,187)</u> |
| Financing activities: | | |
| Repayments of notes payable | - | (9,784) |
| Cash (used in) financing activities | <u>-</u> | <u>(9,784)</u> |
| Decrease in cash flows due to changes in foreign exchange rates | <u>(366)</u> | <u>(2,093)</u> |
| Cash flows provided by discontinued operations: | | |
| Income (loss) from discontinued operations | 199 | (1,560) |
| Operating | (1,132) | 2,477 |
| Investing | - | (780) |
| Financing | - | - |
| Cash provided by (used in) discontinued operations | <u>(933)</u> | <u>137</u> |
| Increase (decrease) in cash and cash equivalents | 9,535 | (59,979) |
| Cash and cash equivalents – beginning of year | 8,372 | 68,351 |
| Cash and cash equivalents – end of year | <u>\$ 17,907</u> | <u>\$ 8,372</u> |
| Non-cash financing activities: | | |
| Payment by trustee in bankruptcy to 2118769 Ontario Inc. (Note 9) | \$ - | \$ (6,469) |
| Supplemental cash flow information: | | |
| Income taxes recovered (paid) relating to discontinued operations | \$ 296 | \$ (208) |
| Interest paid relating to discontinued operations | \$ - | \$ 1,267 |

See accompanying notes to consolidated financial statements.

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Note 1. Description of business:

CoolBrands International Inc. ("CoolBrands") was formed in 1994 and had been focused on the marketing and selling of a broad range of ice cream and frozen snack products.

During fiscal 2006 and 2007, the Board of Directors approved the active marketing of certain of the Company's business lines for sale. As a result, the majority of the Company's operations were disposed of during fiscal 2007. During fiscal 2009, the Company's principal operations consist of the management of its cash resources, including reviewing and considering potential opportunities to deploy such cash resources, and revenue earned from renting an owned building located in New Jersey.

Note 2. Summary of significant accounting policies:

These consolidated financial statements include the accounts of CoolBrands and its principal direct and indirect wholly-owned subsidiaries: Integrated Brands, Inc., Eskimo Pie Corporation, Eskimo Pie Frozen Distribution, Inc., Integrated Brands Franchise Corporation and CoolBrands Smoothies Corporation, collectively referred to as "the Company". All significant intercompany transactions are eliminated. The Company has prepared these consolidated financial statements in accordance with Canadian generally accepted accounting principles.

Use of estimates and measurement uncertainty

The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the year. Significant estimates are used in determining, but are not limited to, the allowance for doubtful accounts, income tax valuation allowances, accrued liabilities and contingencies. By their nature these estimates are subject to measurement uncertainty. Actual results could differ from those estimates. The effect on the financial statements of changes in estimates in future periods could be material and would be accounted for in the period the change occurs.

Cash and cash equivalents and short-term investments

All highly liquid commercial paper purchased with maturities of three months or less is classified as a cash equivalent. Cash equivalents are stated at fair market value. Commercial paper, bank term deposits, bankers acceptances and bonds purchased with maturities greater than three months are classified as short-term investments.

Capital assets

Capital assets are stated at the lower of cost less accumulated depreciation and net recoverable amount, including any write-downs. Depreciation of buildings and equipment is provided by the straight-line or declining balance methods, using the estimated useful lives of the assets, being 38 years and 2 to 10 years, respectively.

Revenue recognition

Interest revenue is recognized on an accrued basis and rental revenue is recognized as earned.

Financial instruments

The Company carries a number of financial instruments including cash, short-term investments, interest receivable, accounts receivable, promissory notes receivable, accounts payable, and accrued liabilities. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair values of these financial instruments approximate their carrying values, unless otherwise noted, due to the relatively short-term nature of their maturities.

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Concentration of credit risk

Financial instruments, which potentially subject the Company to concentration of credit risk, consist principally of cash, investments and receivables. The Company attempts to minimize credit risk with respect to its cash and short-term investments by adhering to its Statement of Investment Policy that specifies investments be made in institutions with minimum of A or equivalent ratings by recognized rating agencies.

Earnings per share

Basic earnings per share is calculated using the weighted average number of common shares outstanding during the year. The computation of diluted earnings per share assumes the basic weighted average number of shares outstanding during the year is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares had been issued. The dilutive effect of warrants and stock options is determined using the treasury stock method.

Foreign currency translation

Effective April 1, 2007, the Company began to account for its subsidiaries as integrated operations. As a result, the Company no longer defers foreign exchange losses from converting U.S. denominated balances in the Currency Translation Account. Gains or losses on converting U.S. denominated assets and liabilities into Canadian dollars using the temporal method of accounting are included in the statement of income and other comprehensive income. Under this method, monetary assets and liabilities have been translated at the year-end exchange rate. Non-monetary assets and liabilities have been translated at historical rates and revenue and expenses have been translated at the average exchange rate for the year.

Income taxes

The Company provides for income taxes using the asset and liability method of accounting for income taxes. Under this method future income tax assets and liabilities are determined based on temporary differences between financial statement values and tax values of assets and liabilities and are measured using substantively enacted income tax rate laws expected to be in effect when the differences are expected to reverse. The Company establishes a valuation allowance against future income tax assets if it cannot demonstrate through the use of objectively verifiable available information that it is more likely than not that the future income tax asset will be realized.

Stock-based compensation

The Company accounts for stock-based compensation using the fair value method of accounting. Under this method, compensation expense is measured at fair value at the grant date using the Black-Scholes option pricing model and recognized over the vesting period using the graded vesting method with a corresponding increase to contributed surplus. Balances in contributed surplus are transferred to share capital when the options are exercised.

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Note 3. Changes in accounting policies:

i) Capital disclosures:

Effective September 1, 2008, the Company adopted the new recommendations of CICA Handbook Section 1535, Capital Disclosures. This Section requires that an entity disclose information that enables users of its financial statements to evaluate an entities objectives, policies and processes for managing capital, including disclosures of any externally imposed capital requirements and the consequences of non-compliance. These new disclosures are included in Note 16. The adoption of Section 1535 as at September 1, 2008 did not have a material impact on the consolidated financial statements.

ii) Financial Instruments – Presentation and Disclosure:

On September 1, 2008, the Company adopted the new recommendations of CICA Handbook Sections 3862, Financial Instruments – Disclosures and Handbook Section 3863, Financial Instruments – Presentation.

CICA Section 3862 requires entities to provide disclosures in their financial statements that enable users to evaluate the significance of financial instruments on the entity's financial position and its performance and the nature and extent of risks arising from financial instruments to which the entity is exposed during the year and at the balance sheet date, and how the entity manages those risks.

CICA Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. It deals with the classification of financial instruments, from the perspective of the issuer, between liabilities and equities, the classification of related interest, dividends, gains and losses, and circumstances in which financial assets and financial liabilities are offset.

The new disclosures required under these Sections are included in Note 14. The adoption of Section 3862 and 3863 as at September 1, 2008 did not have a material impact on the consolidated financial statements.

Note 4. Recent accounting pronouncements not yet adopted:

i) Goodwill and intangible assets:

CICA Handbook Section 3064, "Goodwill and Intangible Assets", establishes revised standards for recognition, measurement, presentation, and disclosure of goodwill and intangible assets. The standard is effective for fiscal years beginning on or after October 1, 2008. The Company does not expect the adoption of this Section to have a significant effect on its financial statements.

ii) International financial reporting standards ("IFRS"):

In 2006, the Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with IFRS over an expected five year transitional period. In February 2008, the AcSB set January 1, 2011 as the date that IFRS will replace the current Canadian GAAP for publicly accountable enterprises. The transition date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended August 31, 2011. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Note 5. Cash and cash equivalents and short-term investments:

Cash and cash equivalents and short-term investments balances are comprised of the following:

| | 2009 | 2008 |
|--|------------------|------------------|
| Cash and cash equivalents | | |
| On deposit with financial institutions | \$ 190 | \$ 423 |
| Treasury bills | 75 | - |
| Money market accounts | 17,642 | 7,949 |
| | <u>17,907</u> | <u>8,372</u> |
| Short-term investments | | |
| Bank term deposits and bankers acceptances | 21,694 | 10,157 |
| Government guaranteed agency bonds | 18,093 | - |
| TransCanada Pipeline commercial paper | 4,204 | - |
| GE Capital commercial paper | - | 42,643 |
| | <u>43,991</u> | <u>52,800</u> |
| Total cash and cash equivalents and short-term investments | <u>\$ 61,898</u> | <u>\$ 61,172</u> |

Included in cash and cash equivalents and short-term investments is \$4,588 (August 31, 2008 - \$43,005) held in U.S. dollar denominated investments and deposits.

Note 6. Discontinued operations:

Below is a summary of the components of the assets and liabilities arising from the sale of the Company's operations and the respective operating results of the business units sold for each of the years presented. Cash flows are generated from the collection of accounts receivable and deposits remaining from the discontinued operations segments. Cash flows are used primarily for payments of fees associated with litigation matters and for liabilities remaining from the discontinued operations. Due to the uncertainty of the date when the litigation matters are resolved, it is not possible to predict the period of time that cash flows will no longer continue from the discontinued operations.

| | 2009 | 2008 |
|--|-------------------------------------|-----------------|
| Current assets of discontinued operations: | | |
| Accounts receivable, net | \$ 85 | \$ 223 |
| Deposits | 50 | 76 |
| | <u>\$ 135</u> | <u>\$ 299</u> |
| Current liabilities of discontinued operations: | | |
| Accounts payable | \$ 506 | \$ 1,012 |
| Accruals and other liabilities | 2,565 | 3,223 |
| Income taxes payable | 92 | 315 |
| | <u>\$ 3,163</u> | <u>\$ 4,550</u> |
| Net income from discontinued operations: | | |
| | For the year ended August 31 | |
| | 2009 | 2008 |
| Revenue | \$ - | \$ 402 |
| Loss for the year before income taxes | \$ (347) | \$ (2,063) |
| Recovery of income taxes | 546 | 503 |
| Gain on disposal of discontinued operations | - | 5,963 |
| Income from discontinued operations | <u>\$ 199</u> | <u>\$ 4,403</u> |

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Note 7. Capital assets:

| | 2009 | 2008 |
|-------------------------------|--------------|---------------|
| Land | \$ 25 | \$ 25 |
| Building and equipment | 2,157 | 2,157 |
| | <u>2,182</u> | <u>2,182</u> |
| Less Accumulated amortization | (2,098) | (2,025) |
| | <u>\$ 84</u> | <u>\$ 157</u> |

Amortization expense during the year was \$73 (2008 - \$180).

Note 8. Other assets:

| | 2009 | 2008 |
|-------------------------------------|---------------|---------------|
| Promissory notes receivable | \$ 3,575 | \$ 3,186 |
| Warrants | 289 | 289 |
| Investment in marketable securities | 194 | 243 |
| Cash held in escrow | - | 303 |
| | <u>4,058</u> | <u>4,021</u> |
| Less amount due within one year | (3,575) | (3,489) |
| Other assets – long-term portion | <u>\$ 483</u> | <u>\$ 532</u> |

A promissory note receivable, resulting from the sale of CoolBrands Dairy, Inc., was due January 30, 2009 and bears interest at 12.9%. On November 18, 2009, the Company received U.S.\$4,025 in settlement of the promissory note receivable, accrued interest on the note and cancellation of the warrants received by the Company to purchase shares in the entity that acquired CoolBrands Dairy, Inc. The funds received were approximately equal to the recorded amount of the promissory note, accrued interest on the note and the warrants.

Note 9. Secured note payable and interest due to a related company:

In November 2006, 2118769 Ontario Inc. (“2118769”), a company controlled by Michael Serruya, the Chairman, President and CEO of the Company, purchased all of the bank indebtedness of Americana Foods Limited Partnership (“Americana Foods”), which aggregated U.S.\$21,407 from the lender. CoolBrands was the guarantor of the Americana Foods debt. In October 2006, Americana Foods was placed into bankruptcy and the independent trustee sold or liquidated all of the assets of Americana Foods. In March 2007, the trustee made an initial payment to 2118769 of U.S.\$13,000 and a final payment of U.S.\$6,500 was made by the trustee in March 2008. In March 2008, the Company, pursuant to its guarantee, repaid the remaining balance of the secured notes payable and accrued interest owing to the related company of U.S.\$3,166 and the expenses paid by 2118769 in connection with the purchase of the Americana indebtedness of U.S.\$291.

Note 10. Other liabilities:

| | 2009 | 2008 |
|--|-----------------|-----------------|
| Accrued benefit cost of post-retirement benefits (see Note 13) | \$ 2,432 | \$ 2,432 |
| Accrued benefit cost of non-registered pension plan | 177 | 193 |
| Accrued environmental liability | 77 | 158 |
| | <u>\$ 2,686</u> | <u>\$ 2,783</u> |

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Note 11. Shareholders' equity and stock options:

Capital Stock

On May 31, 2007, the Company filed articles of amendment in order to affect the elimination of its dual class share structure. As a result of the elimination of the Company's dual class structure, a total of 6,025 multiple voting shares and 50,050 subordinate voting shares were changed into 56,075 common shares. The Company's articles of amendment authorize an unlimited number of common shares.

On February 27, 2008, the shareholders of the Company approved a special resolution to reduce the stated capital of the Company by \$77,416, together with a corresponding reduction in the Company's accumulated deficit.

There were no changes in capital stock for the two years ended August 31, 2009.

Stock options

Under the Company's stock option plans, options to purchase common shares were granted to directors, officers, consultants and key employees at exercise prices equal to the fair market value of the stock at the date of grant.

The following table summarizes stock option activity for all stock option plans:

| | Shares (in thousands) | Weighted average exercise price | Weighted avg. contractual life (in years) |
|--|--------------------------|---------------------------------------|---|
| Outstanding at August 31, 2007 | - | \$ - | - |
| Granted | 300 | \$ 0.78 | 5.0 |
| Outstanding at August 31, 2008 | 300 | | |
| Granted | 400 | \$ 0.60 | 5.0 |
| Outstanding at August 31, 2009 | 700 | \$ 0.68 | 4.1 |
| Options exercisable at August 31, 2009 | 400 | \$ 0.69 | 4.0 |

Stock-based compensation expense was recognized in the amount of \$72 (2008 - \$57) in the consolidated statements of income and other comprehensive income. During fiscal 2009, the Company granted an aggregate of 400 stock options (of which 200 options were vested immediately and of which 200 options will vest in March 2010) with a weighted average fair value of \$0.15 using the Black-Scholes options pricing model.

The value of each option granted is estimated on the date of the grant using the Black-Scholes options pricing model with the following assumptions:

| For the year ended August 31 | 2009 | 2008 |
|------------------------------|---------|---------|
| Expected dividend yield | Nil | Nil |
| Risk-free interest rate | 1.73 % | 3.47 % |
| Expected volatility | 25 % | 40 % |
| Expected life | 5 years | 5 years |

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

Warrants

In connection with the purchase of bank indebtedness by 2118769, as described in Note 9, as well as 2118769 entering into a forbearance agreement and providing a letter of credit to the Company's former lenders, the board of directors of CoolBrands issued to Michael Serruya warrants to purchase up to 5.5 million common shares. The warrants expire in November 2011 and the exercise price is \$0.50 per warrant.

Earnings per share

| | 2009 | 2008 |
|---|-----------------|-----------------|
| Numerator: | | |
| Net income from continuing operations | \$ 1,803 | \$ 993 |
| Net income from discontinued operations | 199 | 4,403 |
| Net income for the year | <u>\$ 2,002</u> | <u>\$ 5,396</u> |
| Denominator: | | |
| Basic weighted average shares outstanding | 56,075 | 56,075 |
| Diluted effect of stock awards | 1,604 | 2,147 |
| | <u>57,679</u> | <u>58,222</u> |
| Income from continuing operations – basic and diluted | \$ 0.03 | \$ 0.02 |
| Income from discontinued operations – basic and diluted | - | 0.08 |
| Income for the year | | |
| - basic | <u>\$ 0.04</u> | <u>\$ 0.10</u> |
| - diluted | <u>\$ 0.03</u> | <u>\$ 0.09</u> |

Potentially dilutive securities, calculated in terms of weighted-average share equivalent of stock options outstanding, include 300 stock options with an exercise price of \$0.78 that are excluded from the calculations of diluted loss per share as their inclusion would have an anti-dilutive effect.

Note 12. Income taxes:

The effective income tax rate on income is affected from year to year by the geographic mix of the consolidated income before income taxes. The following table reconciles income tax expense (recovery) computed by applying the combined Canadian Federal/Provincial statutory rate with the actual income tax provision:

| | 2009 | 2008 |
|--|------------|------------|
| Combined basic Canadian Federal and Provincial income tax rate | 33.17 % | 34.38 % |
| Utilization of net operating loss carryforwards | (33.17) | (34.38) |
| Valuation allowance | - | - |
| | <u>- %</u> | <u>- %</u> |

Significant components of the Company's deferred tax assets as of August 31, 2009 and 2008 are as follows:

| | 2009 | 2008 |
|--|-------------|-------------|
| Future tax asset related to losses | | |
| Federal net operating and capital loss carry forwards | \$ 18,281 | \$ 17,952 |
| Valuation allowance | (18,281) | (17,952) |
| | <u>\$ -</u> | <u>\$ -</u> |
| Future tax asset related to other temporary differences | | |
| Deductible temporary differences | \$ 9,642 | \$ 9,098 |
| Valuation allowance | (9,642) | (9,098) |
| | <u>\$ -</u> | <u>\$ -</u> |

CoolBrands International Inc.

Notes to Consolidated Financial Statements for the years ended August 31, 2009 and 2008

(Amounts expressed in thousands of Canadian dollars)

At August 31, 2009, the Company has net operating loss carryforwards for federal income tax purposes of approximately Cdn \$9,642 in Canada and U.S.\$37,616 in the United States expiring as follows:

| <i>Canadian losses:</i> | | <i>U.S. losses:</i> | |
|-------------------------|-----------------|---------------------|------------------|
| 2026 | \$ 3,157 | 2026 | \$ 6,810 |
| 2027 | 6,485 | 2027 | 30,087 |
| | <u>\$ 9,642</u> | 2028 | 233 |
| | | 2029 | 486 |
| | | | <u>\$ 37,616</u> |

Note 13. Retirement Plans:

A subsidiary of the Company had maintained two defined benefit pension plans covering substantially all salaried and certain executive employees. Upon the acquisition of the subsidiary by the Company in October 2000, all future participation and all benefits under the plans were frozen. These plans provide retirement benefits based primarily on employee compensation and years of service up to the date of acquisition of the subsidiary by the Company. The above mentioned plans are referred to as the "Pension Benefits."

In addition, the subsidiary entered into an agreement with the seller of the company to indemnify the cost of retiree health care and life insurance benefits for salaried employees who had retired prior to April 1992. Under this agreement, the subsidiary may elect to prepay its remaining obligation. The subsidiary did not provide postretirement health and life insurance benefits for employees who retired subsequent to April 1992. This indemnity agreement is referred to as the "Other Benefits".

The following table reconciles the changes in benefit obligations and plan assets of the registered defined benefit plan in 2009 and 2008, and reconciles the funded status to accrued benefit cost at August 31, 2009 and August 31, 2008:

| | <u>Pension Benefits</u> | <u>Other Benefits</u> |
|--------------------------------------|-------------------------|-----------------------|
| Benefit Obligation | | |
| Beginning balance at August 31, 2007 | \$ 2,257 | \$ 2,432 |
| Interest cost | 127 | - |
| Actuarial gain | (276) | - |
| Benefit payments | (78) | - |
| Balance at August 31, 2008 | <u>2,030</u> | <u>2,432</u> |
| Interest cost | 156 | - |
| Actuarial loss | 433 | - |
| Benefit payments | (98) | - |
| Loss on foreign exchange | 28 | - |
| Ending balance at August 31, 2009 | <u>\$ 2,549</u> | <u>\$ 2,432</u> |
| | | |
| Plan assets – Basic value | | |
| Beginning balance at August 31, 2007 | \$ 2,828 | |
| Actual return on plan assets | (280) | |
| Loss on foreign exchange | (4) | |
| Benefit payments | (78) | |
| Balance at August 31, 2008 | <u>2,466</u> | |
| Actual return on plan assets | (427) | |
| Gain on foreign exchange and other | 114 | |
| Benefit payments | (98) | |
| Ending balance at August 31, 2009 | <u>\$ 2,055</u> | |

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The unfunded status for the post retirement health and life insurance benefits is as follows:

| | |
|--|------------------------------|
| | <u>Other Benefits</u> |
| Benefit obligations in excess of Plan assets | \$ 2,432 |
| Accrued benefit cost | \$ 2,432 |

The following table provides the components of the net periodic benefit cost:

| | | |
|--------------------------------|--------------------------------|------------------------------|
| | <u>Pension Benefits</u> | <u>Other Benefits</u> |
| Interest cost | \$ 157 | \$ - |
| Expected return on Plan assets | (201) | - |
| Recognized net actuarial loss | 44 | - |
| Net period benefit cost | \$ - | \$ - |

The assumptions used in the measurement of the benefit obligations are as follows:

| | |
|---|--------------------------------|
| | <u>Pension Benefits</u> |
| Benefit obligation discount rate | 7.11% (2008 – 6%) |
| Expected return on plan assets, during the year | 7.5% (2008 – 7.5%) |

The Company's allocation of Pension Benefit assets at August 31, 2009 and 2008, target allocations for Fiscal 2010, and expected long-term rate of return by asset category are as follows:

| Fiscal Year | Target allocation | Percentage of Plan Assets | | Weighted-average expected long-term rate of return |
|-------------------------------|-------------------|---------------------------|-------|--|
| | 2010 | 2009 | 2008 | 2010 |
| Asset category | | | | |
| Large capitalization equities | 35.0% | 34.7% | 33.4% | 3.1% |
| Mid capitalization equities | 10.0% | 11.7% | 10.1% | 1.1% |
| Small Capitalization equities | 9.0% | 5.7% | 7.8% | 0.7% |
| International equities | 30.0% | 32.5% | 31.5% | 3.1% |
| Fixed income bonds | 12.0% | 11.6% | 12.7% | 0.5% |
| Cash and cash equivalents | 4.0% | 3.8% | 4.5% | 0.2% |
| | 100% | 100% | 100% | 8.7% |

The Company's investment strategy is to obtain the highest possible return commensurate with the level of assumed risk. Investments are well diversified within each of the major asset categories.

The expected long-term rate of return is figured by using the target allocation and expected returns for each asset class as in the table above. The actual historical returns are also relevant.

Based on the latest actuarial report as of January 1, 2009, the Company expects that there will be no minimum regulatory funding requirements that will need to be made during Fiscal 2010. The next actuarial report used for funding purposes will be effective as of January 1, 2010.

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Expected benefit payments under the Eskimo Pie Corporation's defined benefit registered pension plan over future years are as follows:

| Fiscal year | Pension benefits |
|-------------|------------------|
| 2010 | \$ 95 |
| 2011 | 97 |
| 2012 | 96 |
| 2013 | 116 |
| 2014 | 116 |
| 2015 – 2019 | 695 |

Note 14. Financial instruments:

The classification of financial instruments as of August 31, 2009 and 2008 and their respective carrying values and fair values were as follows:

| | Held-for trading \$ | Held-to- maturity \$ | Loans and receivables \$ | Other financial liabilities \$ | Carrying value \$ | Fair value \$ |
|--|---------------------------|----------------------------|--------------------------------|---|-------------------------|---------------------|
| As at August 31, 2009 | | | | | | |
| Cash and cash equivalents | 17,907 | | | | 17,907 | 17,907 |
| Short-term investments | 43,991 | | | | 43,991 | 43,991 |
| Investments in marketable securities | 194 | | | | 194 | 194 |
| Promissory notes receivable and accrued interest | | 4,396 | | | 4,396 | 4,396 |
| Accounts receivable | | | 85 | | 85 | 85 |
| Accounts payable and accrued liabilities | | | | 3,276 | 3,276 | 3,276 |
| As at August 31, 2008 | | | | | | |
| Cash and cash equivalents | 8,372 | | | | 8,372 | 8,372 |
| Short-term investments | 52,800 | | | | 52,800 | 52,800 |
| Interest receivable | 726 | | | | 726 | 726 |
| Investments in marketable securities | 243 | | | | 243 | 243 |
| Promissory note receivable | | 3,186 | | | 3,186 | 3,186 |
| Accounts receivable | | | 223 | | 223 | 223 |
| Accounts payable and accrued liabilities | | | | 4,479 | 4,479 | 4,479 |

Fair value

Fair value is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. The Company uses the following methods and assumptions to establish the fair value for each class of financial instrument for which carrying amounts are included in the consolidated balance sheet as follows:

- **Held for trading**

Cash and cash equivalents and short-term investments – the carrying amount of cash is recorded at the fair market value based upon the amount of funds held in the Company's bank accounts. Cash invested in short-term investments are valued based on quoted market prices provided by the Company's investment managers.

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Investments in marketable securities – the carrying amount is recorded at fair market value based on quoted market prices provided by the investment manager.

- **Held to maturity**

Promissory notes receivable and accrued interest – the carrying amount is recorded at amortized cost using the effective interest method.

- **Loans and receivables**

Accounts receivable – the carrying amount is a reasonable approximation of the fair value due to the short-term nature of these financial instruments.

- **Other financial liabilities**

Accounts payable and accrued liabilities – the carrying amounts included in the balance sheet are measured at amortized cost which approximates fair value due to the short-term nature of accounts payable and accrued liabilities.

The Company records all transaction costs for financial assets and financial liabilities in the consolidated statements of income and other comprehensive income as incurred.

Risk arising from financial instruments

The Company does not use financial derivatives.

Foreign exchange risk and sensitivity on foreign exchange fluctuations:

The Company holds financial assets and liabilities and incurs expenses and earns revenue denominated in U.S. dollars.

Included in the under noted accounts are the following balances denominated in U.S. dollars:

| | 2009 | August 31 | 2008 |
|--|-----------------|-----------|---------------|
| Cash and cash equivalents | \$ 115 | \$ | 346 |
| Short-term investments | 4,075 | | 39,822 |
| Interest receivable | 750 | | 683 |
| Current assets of discontinued operations | 128 | | 495 |
| Other assets | 3,427 | | 3,229 |
| Current liabilities of discontinued operations | (2,926) | | (4,286) |
| Other liabilities | (2,323) | | (2,408) |
| Net U.S. dollar monetary position | <u>\$ 3,246</u> | <u>\$</u> | <u>37,881</u> |

A 1% strengthening/weakening of the Canadian dollar against the U.S. dollar at August 31, 2009 would have decreased/increased net income for the year ended August 31, 2009 and equity as at August 31, 2009 by \$58. This analysis assumes that all other variables remain constant. The Company does not use derivative instruments to reduce its exposure to foreign exchange risk.

Interest rate risk and sensitivity analysis on interest rate changes:

The Company is exposed to interest rate risks arising from its investment of its cash resources in interest-bearing securities. Reductions in interest rates would reduce the amount of interest revenue earned by the Company.

At August 31, 2009, the weighted average interest rate earned on invested funds was 0.51%. A 100 basis point change in this interest rate would result in a change in income of \$154.

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Credit risk:

The Company is exposed to credit risk as certain of its cash funds are invested in securities issued by financial institutions and commercial enterprises with maturities extending between one and nine months. The Company attempts to mitigate credit risk by investing only in institutions that provide strong liquidity and by restricting investments to less than one year maturities.

Note 15. Related party transactions:

The following transactions are in the normal course of business and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. The party is considered related as one of the Company's directors is also a director of the related party.

| | <u>2009</u> | <u>2008</u> |
|--|-------------|-------------|
| Rent paid in respect of shared premises | \$ 48 | \$ 48 |
| Expenses recovered in respect of shared employee | \$ 36 | \$ 30 |

There were no outstanding amounts receivable or amounts payable to related parties as at August 31, 2009.

Note 16. Capital

The Company considers its shareholders equity as its capital source. At the present time, the majority of the Company's capital is held in cash, cash equivalents and short-term investments.

The Company is not subject to any externally imposed capital requirements and has no long-term debt. The Company has not historically paid dividends to its shareholders.

The Company's objectives when managing its capital are:

- to safeguard its cash resources by investing funds so as to minimize collection risk;
- to identify opportunities to deploy its capital to provide positive returns for its shareholders; and,
- to be diligent in executing implementation strategies that maximize the potential of capital investments.

During 2009, the Company continued to invest its cash resources and earn investment returns. There were no acquisitions completed during the year.

Note 17. Contingencies:

Litigation

On October 31, 2006, Capricorn Investors III, L.P. ("Capricorn"), the parent of Americana Foods Corporation, filed a complaint in the Supreme Court of the State of New York against CoolBrands, Integrated Brands, Inc., CBA Foods LLC, CB Americana LLC and certain officers and directors of CoolBrands asserting allegations against the defendants for breaches of contract, breach of fiduciary duty, fraud and conspiracy and sought injunctive relief and damages of over \$60 million. On June 8, 2007, the Company and its co-defendants moved to dismiss the Complaint. On June 13, 2008, the Court granted the Company's motion to dismiss as to seven of the ten claims made by Capricorn in its complaint. The Court provisionally dismissed all of Capricorn's claims against CoolBrands and its subsidiary company Integrated Brands, Inc. but permitted the plaintiff an opportunity to re-plead its case to include these parties. On September 22, 2008, Capricorn filed its submission with the Court to oppose the Court's earlier decision on the defendant's motion to dismiss. On October 6, 2008, the Company filed its reply brief refuting the matters contained in Capricorn's submission and reiterating its position that the case should not continue against CoolBrands and Integrated Brands. On July 16, 2009, the Court rendered its decision and dismissed all claims made by Capricorn against CoolBrands and its affiliated companies. In May 2009 Capricorn filed an appeal of the June 13, 2008 decision. In September 2009 Capricorn filed its Notice to Appeal the Court's July 16, 2009 decision that dismissed the litigation and all remaining claims brought by Capricorn. On October 1, 2009, the Supreme Court, Appellate Division, issued its decision affirming the June 13, 2008 decision previously issued by the Supreme Court. The amount of loss, if any, cannot be determined at this time.

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Legal matters

The Company is also a party to other legal proceedings and disputes with former franchisees and others, which arise in the ordinary course of business. In the opinion of the Company, it is unlikely that the liabilities, if any, arising from the legal proceedings and disputes will have a material adverse effect on the consolidated financial position of the Company. The amount of loss, if any, cannot be determined at this time.

Environmental liabilities:

In February 1992, a subsidiary of the Company entered into an agreement with the former owner of the subsidiary whereby the former owner agreed to indemnify the subsidiary for damages or expenses resulting from environmental contamination caused by the former owner and its predecessors on the subsidiary's owned property located in New Jersey. Litigation has commenced by the Company to demand that the former owner abide by the terms of the agreement. In the event the Company is not successful in this litigation, it may be required to pay the costs associated with remediating the environmental contamination on the property. The cost of remediation cannot be reasonably estimated at this time. The subsidiary has provided a self-guarantee to the State of New Jersey in the amount of \$370 to cover potential clean up costs.

Note 18. Segment information:

As a result of the sale or closure of the operating businesses of the Company, the assets and liabilities of each of these businesses have been classified to assets and liabilities of discontinued operations on each of the consolidated balance sheets as of August 31, 2009 and 2008 and the components of their operating results have been included in income from discontinued operations on each of the consolidated statements of operations. At August 31, 2009, the Company has one segment.