SECOND CUP COFFEE CO.

The Second Cup Ltd.

Unaudited Condensed Interim Financial Statements
For the 13 and 39 weeks ended September 26, 2015 and September 27, 2014

Notice to Reader

The management of The Second Cup Ltd. ("Second Cup" or the "Company") is responsible for the preparation of the accompanying condensed interim financial statements. The condensed interim financial statements have been prepared in accordance with International Financial Reporting Standards and are considered by management to present fairly the financial position, financial performance and cash flows of Second Cup.

These condensed interim financial statements have not been reviewed by an auditor. These condensed interim financial statements are unaudited and include all adjustments, consisting of normal and recurring items that management considers necessary for a fair presentation of the financial position, financial performance and cash flows.

(Signed)

Alix Box

President and Chief Executive Officer, The Second Cup Ltd.

(Signed)

Barbara Mallon Chief Financial Officer, The Second Cup Ltd.

October 30th, 2015

Condensed Interim Statements of Financial Position

(Unaudited, expressed in thousands of Canadian dollars)

ASSETS	September 26, 2015	December 27, 2014
Current assets Cash and cash equivalents Restricted cash (note 11) Trade and other receivables Notes and leases receivable Inventories Prepaid expenses and other assets Income taxes recoverable	9,161 651 2,643 85 272 444 43	\$ 10,918 4,026 81 221 485 699
Non-current assets Notes and leases receivable Property and equipment Intangible assets	13,299 242 4,285 32,591	302 4,380 32,337
Total assets \$	50,417	\$ 53,449
LIABILITIES		
Current liabilities Accounts payable and accrued liabilities Provisions Other liabilities Gift card liability Deposits from franchisees Current portion of long-term debt (note 5)	5,295 1,852 514 2,907 621	\$ 6,011 1,937 512 3,727 378 11,119
Non-current liabilities Provisions Other liabilities Long-term debt (note 5) Deferred income taxes	11,189 1,108 329 11,158 2,827	23,684 1,133 368 - 3,270
Total liabilities	26,611	28,455
SHAREHOLDERS' EQUITY	23,806	24,994
Total liabilities and shareholders' equity	50,417	\$ 53,449

Contingencies, commitments and guarantees (note 12).

See accompanying notes to the unaudited condensed interim financial statements.

Approved by the Directors October 30th, 2015

Michael Bregman, Director Rael Merson, Director

The Second Cup Ltd.

Condensed Interim Statements of Loss and Comprehensive Loss (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

		13 weeks ended				39 weeks ended			
		September 26, 2015		September 27, 2014		September 26, 2015		September 27, 2014	
Revenue (note 6)									
Company-owned cafés and product sales	\$	5,703	\$	2,666	\$	16,576	\$	6,479	
Franchise revenue		3,567		4,020		11,129		13,266	
	-	9,270		6,686		27,705		19,745	
Operating costs and expenses (note 7)									
Company-owned cafés and cost of product sales		5,841		2,637		16,687		7,040	
Franchise		3,104		2,735		7,009		5,887	
General and administrative		1,203		1,475		4,222		6,686	
Loss (gain) on disposal of assets		45		(2)		(43)		(90)	
Depreciation and amortization		387		347		1,078		890	
Asset impairment charges	_			29,708				29,708	
		10,580		36,900		28,953		50,121	
Loss from operations	-	(1,310)		(30,214)	-	(1,248)	-	(30,376)	
Interest and financing costs (note 8)	-	137	. <u>-</u>	116		385	. <u>-</u>	372	
Loss before income taxes	-	(1,447)		(30,330)		(1,633)	-	(30,748)	
Recovery of income taxes	=	(348)		(4,100)		(386)		(4,184)	
Net loss and comprehensive loss for the period	\$	(1,099)	\$	(26,230)	\$	(1,247)	\$	(26,564)	
Basic and diluted loss per share (note 9)	\$_	(0.09)	\$	(2.65)	\$	(0.10)	\$	(2.68)	

See accompanying notes to the unaudited condensed interim financial statements.

Condensed Interim Statements of Changes in Shareholders' Equity (Unaudited, expressed in thousands of Canadian dollars)

		Share Capital		Contributed Surplus	Deficit		Total
Balance - December 28, 2013	\$	1,000 \$	\$	61,557	\$ (16,593)	\$	45,964
Net loss for the period		-		-	(26,564)		(26,564)
Dividends to shareholders		-		-	(1,684)		(1,684)
Stock option plan expense	_		_	57	_		57
Balance - September 27, 2014	\$	1,000	\$_	61,614	\$ (44,841)	\$	17,773
Balance - December 27, 2014	\$	8,652	\$	61,649	\$ (45,309)	\$	24,992
Net loss for the period		-		-	(1,247)		(1,247)
Stock option plan expense	_		_	61	-	_	61
Balance - September 26, 2015	\$_	8,652	\$	61,710	\$ (46,556)	\$_	23,806

See accompanying notes to the unaudited condensed interim financial statements.

3

Condensed Interim Statements of Cash Flows

(Unaudited, expressed in thousands of Canadian dollars)

		13 weeks ended September 26, September 27,		39 weeks e				
CASH PROVIDED BY (USED IN)		2015		2014		September 26, 2015		September 27, 2014
,								
Operating activities	Φ	(1,000)	Ф	(26,220)	Φ	(1.047)	Φ	(06.564)
Net loss for the period Items not involving cash	\$	(1,099)	\$	(26,230)	\$	(1,247)	\$	(26,564)
Depreciation of property and equipment		267		254		807		645
Amortization of intangible assets		119		94		270		244
Share-based compensation expense		24		37		61		57
Deferred income taxes		(348)		(4,100)		(443)		(4,046)
Loss (gain) on disposal of assets		45		(2)		(43)		(90)
Movement in fair value of interest rate swap Impairment charges		(6)		(9) 29,708		32		15 29,708
Other		33		(8)		(7)		(23)
Changes in non-cash working capital		894		(531)		617		(223)
changes in non-cash working capital	-		_	(001)		017	-	(220)
Cash provided by (used in) operating activities	-	(71)	_	(787)		47		(277)
Investing activities								
Proceeds from disposal of capital related items		77		87		305		312
Cash payments for capital expenditures		(331)		(159)		(964)		(650)
Cash payments for intangible assets		(167)		(35)		(581)		(717)
Proceeds from repayment of leases receivable		42		-		72		-
Proceeds from repayment of notes receivable	-	8	_			15		
Cash used in investing activities	_	(371)	_	(107)		(1,153)	_	(1,055)
Financing activities								
Dividends paid to shareholders		-		_		_		(1,684)
	_		_				-	
Cash used in financing activities	-	-	_			-		(1,684)
Decrease in cash and cash equivalents during the period		(442)		(894)		(1,106)		(3,016)
Cash and cash equivalents - Beginning of period	_	10,254	_	4,379		10,918		6,501
Cash and cash equivalents - End of period	\$	9,812	\$	3,485	\$	9,812	\$	3,485
Restricted cash	\$	651	\$		\$	651	\$	_
Cash and cash equivalents	\$	9,161	\$	3,485	\$	9,161	\$	3,485

See accompanying notes to the unaudited condensed interim financial statements. Supplemental cash flow information is provided in note 10.

Notes to the Condensed Interim Financial Statements

September 26, 2015 and September 27, 2014

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

Table of Contents

		Page
GENI	ERAL APPLICATION	
1.	Organization and nature of business	5
2.	Summary of significant accounting policies	5
3.	Changes in accounting policies	6
STAT	TEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME FOCUSED	
4.	Provisions	6
5.	Borrowings	7
6.	Revenue	8
7.	Operating expenses	9
8.	Interest and financing	10
отні	ER	
9.	Basic and diluted loss per share	10
10.	Supplemental cash flow information	11
11.	Restricted cash	11
12.	Contingencies, commitments and guarantees	12
13.	Related parties	13

1. Organization and nature of business

The Second Cup Ltd. ("Second Cup" or "the Company") is a Canadian specialty coffee retailer with 327 cafés operating under the trade name, Second Cup™, in Canada, of which 42 are Company-operated and the balance are operated by franchisees.

Second Cup owns the trademarks, trade names, operating procedures and systems and other intellectual property used in connection with the operation of Second Cup cafés only in Canada.

Second Cup was incorporated under the Business Corporations Act (Ontario) in 2011 and is domiciled in Canada. The address of its registered office is 6303 Airport Road, 2nd Floor, Mississauga, Ontario, L4V 1R8. The Company hereinafter refers to its head office activities as "Coffee Central". The Company's website is www.secondcup.com. The common shares of the Company are listed on the Toronto Stock Exchange under the symbol "SCU".

2. Summary of significant accounting policies

a. Basis of preparation

These unaudited condensed interim financial statements for the 13 and 39 weeks ended September 26, 2015 have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as applicable to condensed interim financial statements including International Accounting Standard (IAS) 34, Interim Financial Reporting ("IAS 34"), and should be read in conjunction with the Company's audited annual financial statements

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

for the year ended December 27, 2014, which have been prepared in accordance with IFRS, as issued by the International Accounting Standards Board.

The accounting policies applied in these unaudited condensed interim financial statements are consistent with those of the previous financial year. The accounting policies are based on IFRS issued and outstanding as at October 30, 2015, the date the Board of Directors approved the unaudited condensed interim financial statements.

Second Cup's fiscal year is such that each quarter will consist of 13 weeks and will end on the Saturday closest to the calendar quarter end. The fiscal year is made up of 52 or 53-week periods ending on the last Saturday of December.

b. Segmented information and reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Executive Officer. The Company substantially operates and is managed as one reportable segment. Operating revenues are comprised of royalties, the sale of goods from Company-operated cafés, the sale of goods through retail and other ancillary channels, and other service fees.

c. Comparative figures

Certain comparative figures have been reclassified to conform to the current period's condensed interim financial statement presentation. Management determined that reclassification better captures the substance of the balances.

3. Changes in accounting policies

The accounting policies adopted in the preparation of these condensed interim consolidated financial statements are consistent with those followed in the preparation of the Company's audited financial statements for the year ended December 27, 2014. There was no significant impact on the Company's condensed interim consolidated financial statements as a result of new standards that became effective during fiscal 2015.

4. Provisions

Provisions for café leases are estimates for costs to be incurred by the Company as a result of closure of cafés and franchisee failure to make payment of occupancy costs.

An expense of \$844 (2014 – expense of \$1,255) was recognized in the 39 weeks ended September 26, 2015 and was reflected in the franchise operating costs and expenses line on the condensed interim statements of operations and comprehensive loss.

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

5. Long term debt

	Sep	tember 26, 2015	December 27, 2014
Face value of borrowings Fair value of interest rate swap Unamortized transaction costs	\$	11,000 \$ 175 (17)	11,000 143 (24)
	\$	11,158	11,119

The credit facility comprise an \$11,000 non-revolving term credit facility, fully drawn. The term credit facility is collateralized by substantially all the assets of the Company. The credit facility matures on September 30, 2016.

Pursuant to the terms of the Company's term loan, the Company is subject to certain financial and other customary covenants. The Company is required to maintain certain covenants, which are defined in the agreements:

- a ratio of senior debt to EBITDA ratio ("Leverage Ratio");
- a fixed charge coverage ratio both of which are based on a trailing four-quarter basis; and
- a maximum amount of permitted distributions and purchases of the Company's own stock based on a trailing cumulative EBITDA, plus a carry-forward legacy surplus of permitted distributions.

In 2014, as a result of the Company's restructuring, certain one-time costs and the decision to acquire a number of cafés, the fixed coverage and leverage ratios were negatively impacted resulting in non-compliance with these covenants. As a result, the debt was classified as current as at December 27, 2014.

Subsequent to year-end, the Company received a waiver of this non-compliance from its lender as well as an amendment to its banking agreement, which reset certain covenants for the next twelve months.

Under the amendment, the Company must maintain a leverage ratio, adjusted for permitted cash balances up to \$5,000, maintained on account with the lender, of less than 1.75 to 1 and also a fixed charge ratio of greater than 1 for fiscal 2015, after which time, the covenants revert back to the original leverage ratio of less than 1.75 to 1 and a fixed charge ratio of greater than 1.5.

The Company's facility matures on September 30th, 2016 and bears interest at the bankers' acceptance ("BA") plus a margin range of 2.25% to 3.25% based on the Company's leverage ratio. As at September 26th, 2015, the applicable margin pertaining to the aforementioned range is 3.25%.

In Q3 2015, as a result of the Company's decision to take back additional cafes, the fixed coverage and leverage ratios were negatively impacted resulting in non-compliance with these covenants as at September 26th, 2015. Prior to quarter end, the Company received a waiver of this non-compliance from its lender for the current quarter. The Company is currently finalizing terms with the lender to revise the credit agreement.

Notes to the Condensed Interim Financial Statements

September 26, 2015 and September 27, 2014

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

The Company believes that there is sufficient cash on hand of \$9,161 and working capital to meet ongoing cash requirements. As a result, the Company agreed to eliminate the \$2,000 undrawn revolving operating credit facility prior to quarter end.

The Company has an interest rate swap agreement with a notional value of \$11,000 that expires on September 30, 2016. The swap fixes the interest rate on the Company's non-revolving term credit facility at 2.07% per annum plus the margin noted above, which results in a fixed effective interest rate of 5.32%.

As at September 26, 2015, there was an interest rate swap liability of \$175 recorded in the condensed interim statements of financial position.

6. Revenue

	13 weeks ended				39 weeks ended			
	September 26, September 27, 2015 2014			September 26, 2015		September 27, 2014		
Franchise revenue								
Royalties	\$ 2,464	\$	2,805	\$	7,671	\$	9,283	
Services and other	1,103		1,215		3,458		3,983	
	3,567	_	4,020		11,129		13,266	
Company-owned cafés and product sales	5,703	_	2,666		16,576	_	6,479	
	\$ 9,270	\$	6,686	\$	27,705	\$	19,745	

Royalties

Royalty revenue from franchised cafés is based on agreed percentage royalty rates of the franchise location sales. Revenue is recognized on an accrual basis in accordance with the substance of the relevant agreement, provided that it is probable that the economic benefits will flow to the Company and the amount of revenue can be measured reliably.

Services and other

Services and other consist of initial franchise fees, renewal fees, transfer fees earned on the sale of cafés from one franchisee to another, construction administration fees, purchasing coordination fees, and other ancillary fees (such as IT support and training fees).

Company-owned cafés and product sales

Company owned cafés and product sales revenue includes the sale of goods from Company owned cafés, as well as products sold in grocery stores through wholesale distribution channels and third party licensing agreements.

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

7. Operating expenses

		13 wee	ended		39 weeks ended			
		September 26, 2015		September 27, 2014		September 26, 2015		September 27, 2014
Company owned cafés and cost of								
product sales Cost of product sales	\$	2,297	\$	1,096	\$	6,401	\$	3,107
Labour and related expenses	Ψ	1,895	Ψ	752	Ψ	5,540	Ψ	1,836
Occupancy and other		1,649		788		4,746		2,097
Depreciation of property and equipment		94		37		301		109
(Gain) loss on disposal of assets		45		(2)		(43)		(90)
(C)		5,980		2,671		16,945	-	7,059
				,	-		-	. ,
Franchise								
Labour and related expenses		1,115		630		3,049		2,330
Travel and franchisee meetings		114		85		738		407
Business development initiatives		71		22		613		110
Professional fees and other		1,804		1,998		2,609		3,040
		3,104		2,735		7,009		5,887
General and administrative								
Labour and related expenses		431		790		1,995		4,617
Professional fees and other		664		578		1,897		1,743
Occupancy		109		108		330		326
Depreciation and amortization		292		310		777		781
1		1,496		1,786		4,999	-	7,467
		•		•		•	-	·
Asset impairment charge		-		29,708		-		29,708
- -	\$	10,580	\$	36,900	\$	28,953	\$	50,121
		: 					-	

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

8. Interest and financing

	13 weeks ended				39 weeks ended			
	September 26, 2015		September 27, 2014		September 26, 2015		September 27, 2014	
Interest expense	\$ 160	\$	125	\$	471	\$	421	
Amortization of deferred financing costs	5		6		17		20	
Interest income	(28)		(15)		(103)		(69)	
	\$ 137	\$	116	\$	385	\$	372	

9. Basic and diluted loss per share

Loss per share is based on the weighted average number of shares outstanding during the period. Basic and diluted loss per share is determined as follows:

		13 we	ended		39 weeks ended				
	September 26, 2015			September 27, 2014	• /			September 27, 2014	
Net loss Weighted average number of shares	\$	(1,099)	\$	(26,230)	\$	(1,247)	\$	(26,564)	
issued and outstanding		12,830,945		9,903,045		12,830,945		9,903,045	
Basic and diluted loss per share	\$	(0.09)	\$	(2.65)	\$	(0.10)	\$	(2.68)	

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

10. Supplemental cash flow information

		13 weeks ended				39 w	eeks	ended
Changes in non-cash working capital (inflow (outflow)):		September 26, 2015		September 27, 2014		September 26, 2015		September 27, 2014
Trade and other receivables Notes and leases receivable Inventories Prepaid expenses and other assets Accounts payable and accrued liabilities Provisions Other liabilities Gift card liability Deposits from franchisees Income taxes	\$	(379) (33) (6) (141) 615 962 (154) (113) 94 49	\$	(690) (48) (11) (229) 506 490 (66) (180) (296) (7)	\$	1,383 (32) (51) 41 (716) (77) (10) (820) 243 656	\$	999 65 (3) (192) (107) 1,325 (123) (1,045) (430) (712)
Cash payments for capital expenditures	\$	894	\$	(531)	\$	617	\$_	(223)
Purchase of property and equipment Purchase of intangible assets	\$ \$	(331) (167) (498)	\$ \$	(159) (35) (194)	\$	(964) (581) (1,545)	\$	(650) (717) (1,367)
Supplementary information								
Interest paid Income taxes paid	\$ \$	95 -	\$ \$	136 7	\$ \$	410		406 666

11. Restricted cash

The Company has established certain accounts that have been classified restricted cash primarily representing a) deposits from franchisees for the cost of constructing a new café or the renovation of an existing café, and b) funds contributed for use in advertising and promotional programs where the Company is acting as an agent on behalf of the co-operative fund.

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

12. Contingencies, commitments and guarantees

The Company has lease commitments for Company-operated cafés and acts as the head tenant on most leases, which it in turn subleases to franchisees. To the extent the Company may be required to make rent payments due to head lease commitments, a provision has been recognized. The Company's lease commitments at September 26, 2015 are as follows:

		Head lease commitments	Sublease to franchisees		Net
September 24, 2016	\$	19,317	\$ 15,973	\$	3,344
September 30, 2017		17,344	14,138		3,206
September 29, 2018		15,399	12,334		3,065
September 28, 2019		13,690	10,726		2,964
September 26, 2020		11,062	8,372		2,690
Thereafter		28,586	20,909		7,677
	\$ _	105,398	\$ 82,452	<u> </u>	22,946

The Company believes it will have sufficient resources to meet the net commitment of \$22,946.

The Company is involved in litigation and other claims arising in the normal course of business. Judgment must be used to determine whether or not a claim has any merit, the amount of the claim and whether to record a provision, which is dependent on the potential success of the claim. It is believed that no significant losses or expenses will be incurred with such claims. However, there can be no assurance that unforeseen circumstances will not result in significant costs. The outcome of these actions is not determinable at this time, and adjustments, if any, will be recorded in the period of settlement.

Contracts are in place with third party companies to purchase the coffee that is sold in all cafés. In terms of these supply agreements, there is a guaranteed minimum volume of coffee purchases of \$2,990 USD (September 27, 2014 – \$5,093 USD). The coffee purchase commitment comprises three components: unapplied futures commitment contracts, fixed price physical contracts and flat price physical contracts.

Due to the Company acting as the primary coordinator of café construction costs on behalf of its franchisees and for Company-operated cafés, there is \$1,865 (\$726 for Company-owned cafés and \$1,139 on behalf of Franchisees) of contractual commitments pertaining to construction costs for new locations and renovations as at the end of the quarter. Construction costs financed for franchise projects are from deposits received from franchisees and for corporate projects from the Company's cash flows.

Notes to the Condensed Interim Financial Statements September 26, 2015 and September 27, 2014 (Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

13. Related parties

Related parties are identified as key management, members of the Board of Directors and shareholders that effectively exercise significant influence over the Company. Such related parties include any entities acting with or on behalf of the aforementioned parties.

For the 13 and 39 weeks ended September 26, 2015, one of the Company's vendors purchased \$806 and \$1,816, respectively, of product in the ordinary course of business, on behalf of the Company and its franchisees from a company previously controlled by a board member.