



Consolidated Financial Statements



Auditors' Report

To the Shareholders of
ZCL Composites Inc.

We have audited the consolidated balance sheets of ZCL Composites Inc. as at March 31, 2004 and 2003 and the consolidated statements of retained earnings (deficit), income, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these 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 the Company as at March 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Chartered Accountants

Edmonton, Canada
May 21, 2004

Consolidated Balance Sheets

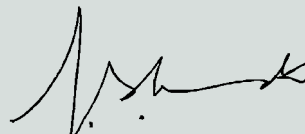
As at March 31 (in thousands of dollars)	2004 \$	2003 \$
Assets		
Current		
Cash	1,880	1,333
Accounts receivable	6,363	6,104
Inventories [note 2]	5,556	5,379
Prepaid expenses	188	115
Future tax assets [note 11]	699	421
	14,686	13,352
Agreement receivable [note 3]	—	880
Property, plant and equipment [note 4]	7,814	7,981
Deferred costs [note 5]	717	1,579
Intangible assets [note 6]	1,324	1,748
Goodwill	1,926	1,926
Future tax assets [note 11]	—	548
	26,467	28,014
Liabilities and Shareholders' Equity		
Current		
Accounts payable and accrued liabilities	4,525	3,870
Income taxes payable	35	82
Current portion of long-term debt [note 8]	—	714
Future tax liabilities [note 11]	27	17
	4,587	4,683
Long-term debt [note 8]	—	3,929
Government grants	160	169
Future tax liabilities [note 11]	838	153
	5,585	8,934
Commitments [note 16]		
Shareholders' equity		
Share capital [note 9]	18,853	27,378
Contributed surplus [note 9]	77	745
Retained earnings (deficit)	1,952	(9,043)
	20,882	19,080
	26,467	28,014

See accompanying notes

On behalf of the Board:



Director



Director

Consolidated Statements of Retained Earnings (Deficit)

Years ended March 31 (in thousands of dollars)	2004 \$	2003 \$
Deficit, beginning of the year	(9,043)	(8,976)
Deficit elimination <i>[note 9]</i>	9,043	—
Net income for the year	1,952	756
Common share issue costs (2003 – net of tax of \$186) <i>[note 9]</i>	—	(362)
Convertible subordinated debenture costs (2003 – net of tax of \$237)	—	(461)
Retained earnings (deficit), end of the year	1,952	(9,043)

See accompanying notes

Consolidated Statements of Income

Years ended March 31 (in thousands of dollars)	2004 \$	2003 \$
Revenue <i>[note 3]</i>	33,932	26,319
Manufacturing and selling costs	25,966	21,171
	7,966	5,148
Amortization	1,968	1,948
General and administration	1,873	1,544
Provision for impairment of agreement receivable <i>[note 3]</i>	880	—
Financing charges <i>[note 8]</i>	370	372
Income before income taxes	2,875	1,284
Income taxes <i>[note 11]</i>		
Current	(42)	28
Future	965	500
	923	528
Net income for the year	1,952	756
Basic and diluted earnings per share <i>[note 12]</i>	\$0.11	\$0.02

See accompanying notes

Consolidated Statements of Cash Flows

Years ended March 31 (in thousands of dollars)	2004 \$	2003 \$
Cash Flows from Operating Activities		
Cash receipts from customers	33,996	26,492
Cash paid to suppliers and employees	(27,714)	(22,646)
Interest paid	(176)	(367)
Income taxes paid	(5)	(44)
	6,101	3,435
Cash Flows from Financing Activities		
Repayment of long-term debt	(4,643)	(3,276)
Repurchase of common shares for cancellation [note 9]	(189)	—
Issue of long-term debt	—	5,000
Finance costs	—	(209)
Issue of common shares and warrants	—	7,000
Common share issue costs	—	(548)
Repayment of convertible subordinated debenture	—	(8,185)
Convertible subordinated debenture costs	—	(348)
	(4,832)	(566)
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	(581)	(455)
Deferred development costs [note 5]	(141)	—
Collection of agreement receivable [note 3]	—	366
Business acquisitions, including bank indebtedness assumed [note 13]	—	(1,638)
	(722)	(1,727)
Increase in cash	547	1,142
Cash, beginning of the year	1,333	191
Cash, end of the year	1,880	1,333

See accompanying notes

Notes to Consolidated Financial Statements

March 31, 2004 and 2003

1. Significant Accounting Policies

ZCL Composites Inc. (the "Company") manufactures and distributes liquid storage systems, including fiberglass underground and aboveground storage tanks and related products and accessories. The Company's financial statements have been prepared following Canadian generally accepted accounting principles. The measurement of certain assets and liabilities is dependent upon future events whose outcome will not be fully known until future periods. Therefore the preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results may vary from those estimated.

In particular, the amounts recorded for amortization of property, plant and equipment, deferred costs and intangible assets are based on estimates of the remaining useful lives of such assets. Furthermore, the provision for warranty claims and the impairment of the agreement receivable are based on past experience and the most currently available information regarding warranty costs and the collectibility of the agreement receivable. These estimates, and those related to the cash flows used to assess the potential impairment of property, plant and equipment, deferred costs, intangible assets, and goodwill are subject to measurement uncertainty and the impact on the financial statements of future periods could be material. Such estimates and assumptions have been made using careful judgments, which in management's opinion, are within reasonable limits of materiality and conform to the significant accounting policies summarized below:

Basis of presentation

The consolidated financial statements include the accounts of ZCL Composites Inc. and its wholly-owned subsidiary companies, LeGay Fiberglass (1993) Limited, Mocoat Services Incorporated, and Parabeam Industries BV (Netherlands). All significant intercompany transactions and balances have been eliminated in the preparation of these consolidated financial statements.

Inventories

Raw materials are valued at the lower of cost, determined on an average cost basis, and replacement cost. Work in progress and finished goods are valued at the lower of manufacturing cost and net realizable value on a specific item basis. Manufacturing cost includes the cost of raw material, direct labour costs, and applicable production overheads.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

1. Significant Accounting Policies (continued)**Property, plant and equipment**

Property, plant and equipment are recorded at cost less accumulated amortization. Amortization is computed using the declining balance method at the following annual rates:

Buildings	4%
Land improvements	10%
Manufacturing equipment	10%
Office equipment	20%
Automotive equipment	30%

Amortization of leasehold improvements is computed using the straight-line method over the term of the lease.

Deferred development costs

The Company expenses research and development costs. Certain development costs are deferred when criteria established by the Canadian Institute of Chartered Accountants with respect to development costs are met, and amortized over future periods commencing with commercial production of the product or process.

Deferred development costs are amortized on a straight-line basis over the estimated expected life of the related products. All costs are currently being amortized over five years.

Unamortized deferred development costs are regularly reviewed for recoverability, based on projections of future revenues less relevant costs. The unamortized amount is written-off when the criteria for deferral are no longer met or written-down when the unamortized balance exceeds the amounts of deferred costs that can be reasonably regarded as recoverable.

Deferred start-up and finance costs

Deferred start-up and finance costs are recorded at cost less accumulated amortization. Amortization is computed using the straight-line method over the following periods:

Deferred start-up costs	5 years
Deferred finance costs	term of loan agreements

Deferred finance costs are amortized over periods ranging from three to five years.

Intangible assets

Intangible assets with finite lives are recorded at cost less accumulated amortization. Amortization is computed using the straight-line method over the following periods:

Licenses	term of licensing agreements
Non-patented technology	estimated expected life of related products

Licenses are amortized over periods ranging from eight to twenty years. Non-patented technology is amortized over five years.

Impairment of long-lived assets

Long-lived assets of the Company include property, plant and equipment, deferred start-up costs and intangible assets. These assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is then recognized when the carrying amounts exceed their fair value.

During the years, there were no events or changes in circumstances which indicated that the carrying amounts of long-lived assets may not be recoverable and no impairment loss was recognized.

Goodwill

Goodwill is recorded at cost. The carrying value is tested for impairment annually and when events or circumstances occur that would indicate that this amount may be impaired. An impairment loss would be recognized if the carrying value exceeds the fair value.

Warranties

The Company generally warrants its products for a period of one year after sale, and for up to thirty years for corrosion, if the products are properly installed and are used solely for storage of listed liquids. The Company's complete storage systems marketed under the Prezerver trademark carry a ten-year, insurance-backed warranty covering product replacement and \$2 million of third-party pollution protection. The Prezerver warranty is covered by insurance underwritten by a major international insurer. A number of component materials and parts are similarly warranted by their manufacturers, thereby reducing the Company's exposure to warranty claims.

The Company provides for warranties based on a review of products and warranties taking into account the collective experience and history of the Company as to warranty claims on its products.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

1. Significant Accounting Policies (continued)**Government grants**

Government grants relating to property, plant and equipment are recorded as a deferred credit and are being amortized on the same basis as the property, plant and equipment to which they relate.

Derivative financial instruments

Derivative financial instruments are used by the Company to manage a portion of its exposure to foreign exchange rate fluctuations. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company enters into foreign currency forward contracts, options and collars to pay for certain raw materials denominated in euros, provided by a foreign subsidiary. These derivative contracts, not accounted for as hedges, are marked to market, and any changes in the market value are recorded in income or expense when the changes occur. The fair value of these instruments is recorded as accounts receivable or payable.

Foreign currency translation

Transactions denominated in a foreign currency and financial statements of an integrated foreign subsidiary included in the consolidated financial statements are translated as follows: monetary items at the rate of exchange in effect at the balance sheet dates; non-monetary items at historical exchange rates; revenue and expense items at average exchange rates that produce substantially the same amounts that would have resulted had the transactions been translated on the dates they occurred; and amortization of assets at the same historical exchange rates as the assets to which they relate. Any resulting exchange gains or losses are included in income in the period incurred.

Revenue recognition

Revenue is recorded upon change of ownership, which normally occurs at the time of shipment of the product. In circumstances where the customer chooses to temporarily store goods on the Company's premises, revenue is recognized upon manufacturing completion.

Income taxes

The Company uses the liability method to account for income taxes. Under this method, future income tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Earnings per share

Basic earnings per share is computed based on the weighted average number of common shares outstanding during the year. Diluted earnings per share is computed using the treasury stock method, which assumes that the cash that would be received on the exercise of options, warrants and the convertible debenture is applied to purchase shares at the average price during the period and that the difference between the shares issued upon their exercise and the number of shares obtainable under this computation, on a weighted average basis, is added to the number of shares outstanding. Antidilutive amounts are not considered in computing diluted earnings per share.

Changes in accounting policies

a) Stock-based compensation

Effective April 1, 2002 the Company adopted the recommendations of the Canadian Institute of Chartered Accountants with respect to stock-based compensation and other stock-based payments. As permitted under those recommendations, the Company applied the change prospectively for new awards granted on or after April 1, 2002. The Company chose to recognize no compensation expense when share options and warrants were granted to employees and directors under plans with no cash or equity settlement features. Pro-forma net income and earnings per share reflecting share options and warrants granted in fiscal year 2003 are disclosed in note 9 using the fair value method. Direct awards of shares to employees and non-employees are accounted for in accordance with the fair value method of accounting for stock-based compensation. In periods prior to April 1, 2002, the Company recognized no compensation when shares, stock options or warrants were issued to employees.

During the fourth quarter of the year ended March 31, 2004, the Company began expensing employee stock-based compensation and other stock-based payments in accordance with the amended recommendations of the Canadian Institute of Chartered Accountants. The change was made with retroactive effect to April 1, 2003, for all employee stock-based compensation using the fair value method for all awards granted or modified on or after April 1, 2003. The fair value of share options and warrants at the date of grant is determined using an option pricing model and compensation expense is recognized over the vesting period of the share options and warrants. As a result of this change, \$10,000 has been recorded as compensation expense in 2004 with a corresponding increase in contributed surplus.

The Company has one share option plan, which is more fully described in note 9.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

1. Significant Accounting Policies (continued)

b) Generally accepted accounting principles

Effective April 1, 2003, the Company prospectively adopted the recommendation of the Canadian Institute of Chartered Accountants with respect to Handbook Section 1100, Generally Accepted Accounting Principles ("GAAP"). This standard establishes what constitutes Canadian generally accepted accounting standards and provides guidance on the GAAP hierarchy. The adoption of this standard had no effect on the Company's financial position, results of operations or cash flows.

2. Inventories

(in thousands of dollars)	2004 \$	2003 \$
Raw materials	2,685	2,159
Work in progress	236	290
Finished goods	2,635	2,930
	5,556	5,379

3. Agreement Receivable

Effective January 1, 2001, the Company sold its 40% interest in ZCL Enviro Systems, Inc. ("Enviro"), a corporation incorporated under the laws of the Philippines, for \$760,000. At that time, the Company had certain trade accounts receivable due from Enviro and Enviro agreed to pay the combined balance plus interest in instalments by June 30, 2003.

No payments have been received from Enviro since the fourth quarter of fiscal 2003. Due to business conditions in the Philippines, Enviro has been unable to commit to a repayment schedule. The amounts and timing of future repayment, and the fair value of underlying security, net of expected costs of recovery, cannot be estimated with reasonable reliability. Accordingly, during the year, a provision for impairment of \$880,000 was recorded.

The Company will continue to pursue all available courses of action to collect the balance of the receivable or otherwise realize upon its security. As collateral for the agreement receivable, the Company is entitled to the return of its 40% interest in Enviro, which manufactures products under a long-term license agreement utilizing the Company's technology.

(in thousands of dollars)	\$
Proceeds receivable from sale of interest	760
Accounts receivable	903
Balance due – January 1, 2001	1,663
Additional amounts invoiced	365
Payments received	(782)
Agreement receivable – March 31, 2002	1,246
Payments received	(366)
Agreement receivable – March 31, 2003	880
Provision for impairment	(880)
Agreement receivable – March 31, 2004	—

Revenue includes nil (2003 – \$65,000) from Enviro, and accounts receivable at March 31, 2004 include nil (2003 – \$7,000) due from Enviro.

4. Property, Plant and Equipment

(in thousands of dollars)	2004		2003	
	Cost \$	Accumulated amortization \$	Cost \$	Accumulated amortization \$
Land	293	—	293	—
Buildings	2,876	865	2,852	782
Leasehold and land improvements	279	87	168	75
Manufacturing equipment	10,326	5,588	10,029	5,081
Office equipment	1,405	911	1,261	801
Automotive equipment	165	79	160	43
	15,344	7,530	14,763	6,782
Net book value	7,814		7,981	

Amortization expense includes \$748,000 (2003 – \$730,000) for the amortization of property, plant and equipment and \$9,000 (2003 – \$25,000) for the amortization of government grants.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

5. Deferred Costs

(in thousands of dollars)	2004		2003	
	Cost \$	Accumulated amortization \$	Cost \$	Accumulated amortization \$
Deferred development costs	2,831	2,114	2,690	1,421
Deferred start-up costs	707	707	707	595
Deferred finance costs	213	213	213	15
	3,751	3,034	3,610	2,031
Net book value		717		1,579

Deferred development costs include \$141,000 (2003 – \$nil) incurred during the year. These costs relate to development projects in process at March 31, 2004 and were not amortized during the year. The total amount of research and development charged to expense for the year is not separately identifiable, as such costs are only tracked for development projects that are deferred.

Amortization expense includes \$693,000 (2003 – \$712,000), \$112,000 (2003 – \$140,000), and \$198,000 (2003 – \$18,000) for the amortization of deferred development costs, start-up costs and finance costs respectively. Deferred finance costs were written-off during the year as the related financing was repaid.

6. Intangible Assets

(in thousands of dollars)	2004		2003	
	Cost \$	Accumulated amortization \$	Cost \$	Accumulated amortization \$
Licenses	521	396	521	361
Non-patented technology	1,944	745	1,944	356
	2,465	1,141	2,465	717
Net book value		1,324		1,748

Amortization expense includes \$35,000 (2003 – \$35,000) for the amortization of licenses and \$389,000 (2003 – \$356,000) for non-patented technology.

7. Bank Indebtedness

The Company has operating lines of credit of \$10,250,000 provided by a chartered bank that are not utilized. These lines of credit are payable on demand and bear interest at prime rate plus 0.25% (4.25%; 2003 – 5.00%). The operating lines of credit contain certain restrictive covenants including the maintenance of certain financial ratios and limitations on capital expenditures and additional debt. The Company has pledged as collateral a general security agreement, guarantees of subsidiaries, and a pledge of inventory under section 427 of the Bank Act.

8. Long-term Debt

(in thousands of dollars)	2004 \$	2003 \$
Bank term loan bearing interest at prime rate plus 0.50%, payable in quarterly instalments of \$178,572 plus interest with the remaining balance due in September 2005; the interest rate applied at March 31, 2003 was 5.25%.	—	4,643
Less current portion	—	714
	—	3,929

Financing charges

(in thousands of dollars)	2004 \$	2003 \$
Interest, long-term	154	189
Interest, short-term	6	136
Foreign exchange losses	12	29
Amortization of deferred finance costs [note 5]	198	18
	370	372

9. Share Capital, Contributed Surplus and Stock-based Compensation

(a) Share capital

Authorized

Unlimited number of common shares

Issued and outstanding

(in thousands of dollars)	2004		2003	
	Shares #	\$	Shares #	\$
Balance, beginning of the year	17,716,920	27,378	9,295,866	20,078
Reduction of stated capital (i)	—	(8,298)	—	—
Repurchased under normal course issuer bid (ii)	(222,000)	(240)	—	—
Issued to employees under employee recognition program (iii)	16,400	13	—	—
Issued for cash under private placement (iv)	—	—	7,368,422	6,300
Issued for acquisition [note 13]	—	—	1,052,632	1,000
Balance, end of the year	17,511,320	18,853	17,716,920	27,378

- (i) At the Annual General and Special Meeting of Shareholders on August 18, 2003, the shareholders approved the reduction of the stated capital of the Company. Accordingly, contributed surplus was reduced by \$745,000, share capital by \$8,298,000, and accumulated deficit by \$9,043,000.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

9. Share Capital, Contributed Surplus and Stock-based Compensation (continued)**(a) Share Capital (continued)**

- (ii) During the year, 222,000 common shares were repurchased for cancellation pursuant to a normal course issuer bid at a cost of \$189,000. As a result of these repurchases, share capital was reduced by \$240,000 and contributed surplus was increased by \$51,000.
- (iii) In March 2004, 16,400 common shares were issued to employees as recognition for the Canada's 50 Best Managed Companies award received by the Company. As a result of this direct award of shares to employees, share capital and compensation expense of \$13,000 were recorded.
- (iv) In September 2002, the Company completed a private placement to ARC Energy Venture Fund 3 of 7,368,422 units ("Unit") at \$0.95 per Unit for total cash proceeds of \$7,000,000. Each Unit was comprised of one common share and 0.5 Performance Warrants (see Warrants below). Of the total cash proceeds, \$700,000 was attributed to the value of the Performance Warrants, as computed using an option pricing model, and allocated to contributed surplus. Issue costs of \$548,000, net of tax of \$186,000, were charged to deficit.

(b) Share options

Under the Company's share option plan, options to purchase common shares may be granted by the Board of Directors to directors, officers, employees, and persons who provide management or consulting services to the Company. The plan has no cash or equity settlement features. As part of the private placement in September 2002, the Company agreed that the maximum term of options would be no greater than five years, the exercise price would not be less than the price received by the Company upon the completion of the most recent offering of common shares, the total number of options would be no more than 10% of the issued and outstanding common shares, and the options would vest one-third per year, commencing on the first anniversary of the date the option is granted.

At the Annual General and Special Meeting of Shareholders on August 19, 2002, the shareholders authorized the number of options under the plan at 1,500,000 common shares. As part of the approval of the issue of the common shares under the employee recognition program, the Toronto Stock Exchange required that the number of options under the plan be reduced by 16,400, which was the number of common shares issued.

The Company has issued 1,145,000 (2003 – 1,185,000) of these options, which expire on dates between March 2006 and September 2007. The following table presents the changes during the years and the options outstanding:

	2004		2003	
	Shares #	Weighted Average Exercise Price \$	Shares #	Weighted Average Exercise Price \$
Balance, beginning of the year	1,185,000	0.99	180,000	2.28
Issued	125,000	0.95	1,100,000	0.95
Expired	(165,000)	1.05	(95,000)	3.00
Balance, end of the year	1,145,000	0.97	1,185,000	0.99

Exercise Price \$	2004			
	Options Outstanding		Options Exercisable	
	Shares #	Weighted Average Remaining Contractual Life in Years	Shares #	Weighted Average Exercise Price \$
1.35	70,000	1.93	70,000	1.35
0.95	1,075,000	3.59	341,667	0.95
0.95 – 1.35	1,145,000	3.49	411,667	1.02

(c) Warrants

As part of the private placement in September 2002, the Company issued 3,684,211 Performance Warrants (“Warrant”). One-half of these Warrants were segregated, and approved by the shareholders at the Annual General and Special Meeting of Shareholders on August 18, 2003, for transfer to senior management of the Company. Each Warrant entitles the holder to subscribe for one common share at a price of \$0.95 for a period of up to five years subject to a performance vesting provision. The Warrants vest at one-third intervals upon the weighted-average trading price of common shares reaching thresholds, for a period of twenty trading days, of \$1.90, \$2.85 and \$3.80 per common share.

The 550,000 warrants associated with the convertible subordinated debenture, at a weighted average exercise price of \$2.47, expired in November 2002.

(d) Stock-based compensation

The Black–Scholes model, used by the Company to calculate the values of options and warrants, as well as other currently accepted option valuation models, were developed to estimate the fair value of freely-tradeable, fully-transferable options and warrants without vesting restrictions. Such options and warrants differ significantly from the share options and warrants granted by the Company. These models require subjective assumptions, including future share price volatility and expected time until exercise, which affect the calculated values. Accordingly, management believes that these models do not necessarily provide a reliable single measure of the fair values of the share options and warrants granted by the Company.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

9. Share Capital, Contributed Surplus and Stock-based Compensation (continued)

(d) Stock-based compensation (continued)

Share options and warrants granted on or after April 1, 2003

The Company uses the fair value method of accounting for all share options and warrants granted to employees on or after April 1, 2003. During the year, the Company granted 50,000 share options and 150,000 warrants, all of which were granted with exercise prices in excess of the market share price on the grant date. Stock-based compensation expense of \$10,000 (2003 – nil) was recognized during the year.

The following estimated fair values of these options and warrants were determined, at the date of the grants, using the Black-Scholes option pricing model with the following weighted-average assumptions:

	Share Options	Warrants
Weighted-average fair value	\$0.29	\$0.18
Risk-free interest rate (%)	3.89	4.37
Expected hold period to exercise (years)	4.0	4.5
Volatility in the price of Company's shares (%)	60.8	60.5
Dividend yield (%)	0.0	0.0

In addition, during the year, 75,000 share options were issued to a non-employee as consideration for consulting services. In accordance with the fair value method of accounting for stock-based compensation for non-employees, \$16,000 (2003 – nil) was recorded as contributed surplus and an expense in the statement of income.

Share options and warrants granted in 2003

The fair value of share options and warrants granted in 2003, all of which were granted with exercise prices in excess of the market share price on the grant date, were determined, at the date of grants, using the Black-Scholes option pricing model. The following table provides the required pro-forma measures of net income and earnings per share had compensation expense been recognized based on the fair value, as at the date of the grant, of the options and warrants granted to employees in 2003, in accordance with the fair value method of accounting for stock-based compensation:

(in thousands of dollars)	2004 \$	2003 \$
Net income for the year	1,952	756
Stock-based compensation expense	215	110
Pro-forma net income for the year	1,737	646

	2004 \$	2003 \$
Earnings per share:		
Reported basic and diluted earnings per share	0.11	0.02
Compensation expense per share	0.01	0.01
Pro-forma basic and diluted earnings per share	0.10	0.01

The following estimated fair values of these options and warrants were determined using the following weighted-average assumptions:

	Share Options	Warrants
Weighted-average fair value	\$0.37	\$0.38
Risk-free interest rate (%)	4.0	4.0
Expected hold period to exercise (years)	4.0	5.0
Volatility in the price of the Company's shares (%)	61.6	56.2
Dividend yield (%)	0.0	0.0

10. Convertible Subordinated Debenture

During 1998, the Company received \$11,000,000 under a convertible subordinated debenture bearing interest at 9.75%. The debenture, plus an amount accruing daily sufficient to generate to the lender an additional rate of return of 8.25% per annum was due on November 30, 2002. The debenture, and any interest payable, were convertible with 120 days notice to common shares of the Company at the Company's option, at any time after May 1, 2002. The conversions were at a price per share equal to the twenty-day weighted average trading price of the shares on the Toronto Stock Exchange, providing that the price was greater than \$3.00.

In 1999 and 2000, the Company repaid \$5,500,000 of the debenture. In May 2002, the Company agreed to make monthly payments of \$100,000, and in September 2002, the debenture was repaid in full. A make-whole premium based on the present value, over the period remaining to maturity of the debenture, of the difference between the debenture interest rate of 9.75% and the lender's reinvestment rate of return, was payable on amounts repaid. No make-whole premium was payable on the monthly repayments made between May 2002 and September 2002. A make-whole premium on the repayment of the debenture in September 2002 of \$56,000 was paid. Warrants to purchase 550,000 common shares of the Company that were issued in connection with the debenture, expired on November 30, 2002.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

11. Income Taxes

The Company's effective income tax expense has been determined as follows:

(in thousands of dollars)	2004 \$	2003 \$
Statutory federal and provincial taxes	1,019	510
Increase (decrease) in income taxes resulting from:		
Recovery of prior years' taxes	(145)	—
Manufacturing and processing allowance	(33)	(75)
Impact of changes in tax rates	15	50
Non-deductible expenses and other items	67	43
	923	528

Significant components of the Company's future tax assets and liabilities are as follows:

(in thousands of dollars)	2004 \$	2003 \$
Future tax assets		
Loss carryforwards	739	1,986
Share issue costs	107	149
Tax basis of development costs in excess of carrying values	419	318
Other	137	101
	1,402	2,554
Future tax liabilities		
Carrying value of property, plant and equipment and intangible assets in excess of tax basis	1,566	1,666
Other	2	89
	1,568	1,755
	(166)	799
Represented by:		
Future tax assets – current	699	421
Future tax assets – long-term	—	548
Future tax liabilities – current	(27)	(17)
Future tax liabilities – long-term	(838)	(153)
	(166)	799

The Company has accumulated losses for Canadian tax purposes of approximately \$2,142,000 which may be carried forward and used to reduce taxable income in future years.

The Canadian tax losses available for carryforward must be claimed in years ending no later than:

(in thousands of dollars)	\$
2006	69
2007	505
2008	18
2009	119
2010	1,431

The potential income tax benefit associated with these losses has been recognized for accounting purposes.

12. Earnings Per Share

The following table sets forth the net income available to common shareholders and weighted-average number of common shares outstanding for the computation of basic and diluted earnings per share:

(in thousands of dollars)	2004 \$	2003 \$
Numerator:		
Net income for the year	1,952	756
Convertible subordinated debenture costs, net of tax	—	(461)
Net income available to common shareholders for basic and diluted earnings per share	1,952	295
Denominator:		
Weighted-average shares for basic earnings per share	17,640,106	13,909,486
Effect of dilutive share options (1,025,000)	48,041	—
Adjusted weighted-average shares for diluted earnings per share	17,688,147	13,909,486

Certain share options are not included in the calculation of diluted shares as their exercise prices exceeded the average market share price for each of the years. The warrants are not included in the calculation of diluted shares as the market prices were below the performance threshold. The convertible subordinated debenture is not included in the calculation of diluted shares in 2003 as the market share price was below the threshold conversion price of \$3.00.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

13. Acquisitions

In May 2002, the Company acquired 100% of the shares of Mocoat Services Inc., an Alberta-based corporation that provides corrosion prevention services to the oil and gas industry in Western Canada and manufactures a proprietary tank lining or internal secondary containment system.

In September 2002, the Company acquired 100% of the shares of Parabeam Industries BV, which is based in The Netherlands and manufactures a three-dimensional glass fabric that is used by the Company in the manufacture of double wall tanks and tank lining products.

The acquisitions were accounted for using the purchase method and the consolidated financial statements include the results of operations from the purchase dates. The aggregate consideration given, including acquisition costs, has been allocated to the fair value of the net assets acquired and liabilities assumed, including those relating to the relocation of certain operations to new premises, as follows:

(in thousands of dollars)	2003 \$
Cash consideration	1,375
Common share consideration [note 9]	1,000
Aggregate purchase price	2,375
Assets and liabilities acquired at fair values:	
Bank indebtedness assumed	(263)
Non-cash working capital	827
Property, plant and equipment	1,305
Non-patented technology	1,944
Long-term debt	(1,007)
Future tax liability	(431)
Net assets acquired	2,375

14. Related Party Transactions

- a) Trucking services of \$352,000 (2003 – \$318,000) were provided by a corporation controlled by a director of the Company. Accounts payable and accrued liabilities at March 31, 2004 included \$6,000 (2003 – \$4,000) owing to the corporation. Normal commercial rates were paid for these services.
- b) During 2003, as part of the approval of the acquisition of Mocoat Services Inc., the convertible subordinated debenture holder required that the Company raise additional capital, subordinated to their position, in the amount of \$550,000. Certain directors of the Company loaned the \$550,000 to the Company in May 2002. The loans were unsecured, bore interest at the annual rate of 25% per annum, and were repaid in September 2002. Interest of \$58,000 was paid to the directors relating to these loans and included in interest on short-term indebtedness.

15. Financial Instruments and Risk Management

Financial instruments

The fair value of accounts receivable, accounts payable and income taxes payable approximate their carrying values, due to the relatively short periods to maturity of these instruments. The fair value of long-term debt at March 31, 2003 approximated its carrying value due to interest rates which reflected market rates.

Foreign currency risk management and derivative financial instruments

The consolidated financial statements are reported in Canadian dollars, including the results of an integrated foreign subsidiary. Certain transactions, revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. The exchange rate risk, on an annual basis, primarily reflects the impact of fluctuating exchange rates on the net difference between revenue, expenses and other transactions in each of the currencies. Substantially all business activities are currently carried out in Canada, but it is anticipated that this will be a continuing risk in the future as the Company continues to expand into global markets.

At March 31, 2004, the Company had entered into foreign currency collar arrangements not accounted for as hedges. These arrangements provided for the purchase of euros, up to a total Canadian dollar equivalent of \$1.5 million, at rates of \$1.566 or \$1.6175 per euro. The fair values of these arrangements, estimated using market rates at March 31, 2004, are nil (2003 – nil). During the year, net realized and unrealized gains of less than \$5,000 (2003 – nil) relating to derivative financial instruments were recorded in financing charges.

Interest rate risk management

All long-term debt was repaid during the year, and the convertible subordinated debenture was repaid in 2003.

Credit risk management

The maximum exposure to credit risk is represented by the carrying amount of the accounts receivable and agreement receivable. A provision for impairment of the full amount of the agreement receivable has been recorded as described in note 3. The credit risk related to accounts receivable results from the possibility of customers defaulting on payment of these accounts. The Company deals largely with major oil and gas companies in Canada, and performs ongoing credit evaluations and maintains allowances for potential doubtful accounts. No one customer generally makes up more than 10% of revenue, but at a particular point in time, depending on the timing of sales, there may be higher proportionate exposure in accounts receivable. At March 31, 2004, two customers accounted for 26% (2003 – one customer, 17%) of accounts receivable.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

16. Commitments**License agreements**

The Company has license agreements which expire between October 2006 and December 2008. The agreements give the Company exclusive rights to manufacture and sell products in certain geographic areas utilizing the licensors' technology.

These license agreements provide for the payment of royalties based on revenues from related products during the license terms. Aggregate minimum royalty payments under these license agreements are as follows:

(in thousands of dollars)	\$
2005	467
2006	467
2007	433
2008	380
2009	245
	1,992

Operating leases

The minimum annual rentals under the terms of operating leases for premises and for automotive, office and other equipment are as follows:

(in thousands of dollars)	\$
2005	429
2006	298
2007	233
2008	124
2009	62
Thereafter	217
	1,363

17. Segmented Information

Operating segments are defined as components of the Company for which separate financial information is available that is evaluated regularly by the chief operating decision maker in allocating resources and assessing performance. The chief operating decision maker of the Company is the Chief Executive Officer.

The Company operates in one reportable segment, which is the manufacture and distribution of liquid storage systems including fiberglass underground and aboveground storage tanks and related products and accessories.

Information about products

Providing information relating to revenue from external customers for each product, or group of similar products, is impractical and accordingly, only total revenue has been presented in the statements of income.

Information about geographic areas

(in thousands of dollars)	Revenues		Property, plant and equipment and goodwill	
	2004 \$	2003 \$	2004 \$	2003 \$
Canada	32,436	25,291	8,934	9,046
Foreign countries	1,496	1,028	806	861
	33,932	26,319	9,740	9,907

Revenue is attributed to the geographic area based on location of the Company's operations. No revenue attributed to any individual foreign country is material. The property, plant and equipment relating to foreign countries are located in The Netherlands.

Information about major customers

The Company has long-term contracts and alliance arrangements with many of the major oil and gas companies in Canada. The top seven customers (of which four were the same in 2004 and 2003) accounted for approximately 38% (2003 – 38%) of revenue, with the largest customer making up 11% (2003 – 10%) of revenue.

18. Subsequent Event

Subsequent to March 31, 2004, the Company acquired the business assets of Durex Steel & Alloy Industries Ltd. ("Durex") located in Edmonton, Alberta. Durex manufactures steel aboveground storage tanks. The purchase price was \$1,000,000 paid in cash on closing.

19. Comparative Figures

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current consolidated financial statements. In the current year, freight amounts billed to customers are recorded as revenue, rather than netted against freight costs which are recorded as part of manufacturing and selling costs. Accordingly, freight billed to customers of \$861,000 (2003 – \$821,000) is included in revenue.