



ZCL Composites Inc.

Consolidated Financial Statements

December 31, 2007 and 2006

AUDITORS' REPORT

To the Shareholders of
ZCL Composites Inc.

We have audited the consolidated balance sheets of **ZCL Composites Inc.** as at December 31, 2007 and 2006 and the consolidated statements of shareholders' equity and comprehensive income (loss), income, and cash flows for the twelve month period ended December 31, 2007 and the nine month period ended December 31, 2006. 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 December 31, 2007 and 2006 and the results of its operations and its cash flows for the twelve month period ended December 31, 2007 and the nine month period ended December 31, 2006 in accordance with Canadian generally accepted accounting principles.

Edmonton, Canada
March 17, 2008

Ernst + Young LLP

Chartered Accountants

ZCL Composites Inc.**CONSOLIDATED BALANCE SHEETS**

As at December 31

(in thousands of dollars)	2007 \$	2006 \$
ASSETS		
Current		
Cash and cash equivalents	2,033	7,802
Accounts receivable	16,595	7,483
Inventories <i>[note 3]</i>	16,218	10,807
Prepaid expenses	661	142
Future tax assets <i>[note 14]</i>	416	11
	35,923	26,245
Property, plant and equipment <i>[note 4]</i>	20,749	10,588
Deferred development costs <i>[note 5]</i>	819	1,050
Intangible assets <i>[note 6]</i>	8,995	687
Goodwill <i>[note 7]</i>	27,327	1,991
Other assets	555	854
	94,368	41,415
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Bank indebtedness <i>[note 8]</i>	150	—
Accounts payable and accrued liabilities	10,886	5,465
Accrued pension liability <i>[note 9]</i>	284	—
Income taxes payable	511	1,398
Deferred revenue	1,490	896
Current portion of long term debt <i>[note 10]</i>	1,960	—
Future tax liabilities <i>[note 14]</i>	—	180
	15,281	7,939
Future tax liabilities <i>[note 14]</i>	4,623	1,228
Long term debt <i>[note 10]</i>	6,978	—
	26,882	9,167
Commitments and contingencies <i>[note 15]</i>		
Shareholders' equity		
Share capital <i>[note 12a]</i>	62,190	23,135
Contributed surplus <i>[note 12a]</i>	449	452
Accumulated other comprehensive loss	(8,729)	—
Retained earnings	13,576	8,661
	67,486	32,248
	94,368	41,415

See accompanying notes

On behalf of the Board:

“Venence G. Côté”
Director

“James S. Edwards”
Director

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME
(LOSS)**

(in thousands of dollars)	Common Shares	Share Capital \$	Contributed Surplus \$	Accumulated Other Comprehensive Loss \$	Retained Earnings \$	Total \$	Comprehensive Income (Loss) \$
Balance, December 31, 2006	21,681,445	23,135	452	—	8,661	32,248	—
Common shares issued for cash <i>[note 12a]</i>	4,000,000	38,147	—	—	—	38,147	—
Shares issued on exercise of options <i>[note 12b]</i>	281,334	282	—	—	—	282	—
Warrants exercised for cash <i>[note 12c]</i>	482,750	459	—	—	—	459	—
Stock-based compensation <i>[note 13]</i>	—	—	164	—	—	164	—
Reclassification of fair value of stock options and warrants previously expensed <i>[note 12a]</i>	—	167	(167)	—	—	—	—
Translation of self-sustaining foreign operations	—	—	—	(8,729)	—	(8,729)	(8,729)
Dividends <i>[note 11]</i>	—	—	—	—	(2,600)	(2,600)	—
Net income	—	—	—	—	7,515	7,515	7,515
Balance, December 31, 2007	26,445,529	62,190	449	(8,729)	13,576	67,486	(1,214)
Balance, March 31, 2006	20,118,953	21,397	348	—	6,686	28,431	—
Shares issued on exercise of options <i>[note 12b]</i>	364,065	451	—	—	—	451	—
Warrants exercised for cash <i>[note 12c]</i>	1,198,427	1,139	—	—	—	1,139	—
Stock-based compensation <i>[note 13]</i>	—	—	252	—	—	252	—
Reclassification of fair value of stock options and warrants previously expensed <i>[note 12a]</i>	—	148	(148)	—	—	—	—
Dividends <i>[note 11]</i>	—	—	—	—	(2,081)	(2,081)	—
Net income	—	—	—	—	4,056	4,056	4,056
Balance, December 31, 2006	21,681,445	23,135	452	—	8,661	32,248	4,056

See accompanying notes

ZCL Composites Inc.

CONSOLIDATED STATEMENTS OF INCOME

	Twelve Months December 31 2007	Nine Months December 31 2006
(in thousands of dollars, except per share amounts)	\$	\$
	<i>[note 1]</i>	<i>[note 1]</i>
Revenue	104,783	41,399
Manufacturing and selling costs <i>[note 13a]</i>	82,482	31,580
	22,301	9,819
General and administration <i>[note 13a]</i>	7,703	2,595
Amortization <i>[note 19b]</i>	3,572	1,269
Financing expense <i>[note 19a]</i>	1,073	—
	12,348	3,864
Income before income taxes	9,953	5,955
Income tax expense (recovery) <i>[note 14]</i>		
Current	3,693	2,177
Future	(1,255)	(278)
	2,438	1,899
Net income	7,515	4,056
Earnings per share <i>[note 16]</i>		
Basic	\$0.29	\$0.19
Diluted	\$0.29	\$0.18

See accompanying notes

ZCL Composites Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Twelve Months December 31 2007	Nine Months December 31 2006
(in thousands of dollars)	\$	\$
	<i>[note 1]</i>	<i>[note 1]</i>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	7,515	4,056
Add items not affecting cash:		
Amortization expense	3,572	1,269
Future tax recovery	(1,255)	(278)
Gain on sale of equipment	(32)	—
Stock based compensation expense <i>[note 13a]</i>	164	252
Pension expense <i>[note 9]</i>	148	—
	10,112	5,299
Changes in non-cash working capital:		
Decrease (increase) in accounts receivable	(2,886)	5,268
Decrease (increase) in inventories	3,430	(1,385)
Decrease (increase) in prepaid expenses	(110)	168
Increase (decrease) in accounts payable and accrued liabilities	104	(370)
Increase in income taxes payable	212	977
Decrease in deferred revenue	(1,139)	—
Cash flows from operating activities	9,723	9,957
CASH FLOWS FROM FINANCING ACTIVITIES		
Issue of common shares, net of transaction costs <i>[note 12a]</i>	38,091	1,590
Net advances (repayment) of bank indebtedness	150	(114)
Dividends <i>[note 11]</i>	(2,600)	(2,081)
Net cash received on long term debt	20,000	—
Repayment of long term debt	(11,000)	—
Cash flows (used in) from financing activities	44,641	(605)
CASH FLOWS FROM INVESTING ACTIVITIES		
Business acquisitions, including bank indebtedness assumed and repaid <i>[note 2]</i>	(55,659)	—
Purchase of property, plant and equipment	(3,791)	(1,495)
Other	22	(55)
Cash flows used in investing activities	(59,428)	(1,550)
Foreign exchange loss on cash held in foreign currency	(705)	—
Increase (decrease) in cash and cash equivalents	(5,769)	7,802
Cash and cash equivalents, beginning of the period	7,802	—
Cash and cash equivalents, end of the period	2,033	7,802

See accompanying notes

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES

ZCL Composites Inc. (the “Company”) manufactures and distributes liquid storage systems, including fibreglass underground and aboveground storage tanks, fibreglass-lined steel tanks, steel tanks, and related products and accessories. The Company also produces and markets fibreglass lining systems and a three dimensional glass fabric material.

Generally accepted accounting principles

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 development costs and intangible assets are based on estimates of the remaining useful lives of such assets. Furthermore, the provision for warranty claims and self-insured liabilities is based on past experience and the most currently available information regarding warranty costs and incurred claims. These estimates and those related to the cash flows used to assess the potential impairment of property, plant and equipment, deferred development costs, intangible assets, and goodwill as well as those used to estimate the fair value of stock-based compensation, income tax assets and liabilities and financial instruments 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. Principal operating subsidiaries include Triple M Fiberglass Mfg. Ltd., Parabeam Industries BV, Radigan Insurance Inc., VRB & Associates SRL, and Xerxes Corporation (“Xerxes”). All significant intercompany transactions and balances have been eliminated in the preparation of these consolidated financial statements.

During 2006, the Company changed its fiscal year-end from March 31 to December 31. Accordingly, these financial statements present the results of operations and cash flows for the twelve month period ended December 31, 2007 and comparative figures are for the nine month period ended December 31, 2006.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and cash equivalents

Cash and cash equivalents consist of all cash balances and highly liquid investments with an original maturity of three months or less. Cash equivalents are invested in money market funds and are carried at fair value.

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 materials, direct labour costs, and applicable production overheads.

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. Amortization of capital work-in-progress commences upon substantial completion of the project and commencement of the asset's service life.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred development costs

Research and development costs are expensed as incurred. 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 subject to a maximum period of 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 development costs that can be reasonably regarded as recoverable.

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:

Non-contractual customer relationships	estimated expected length of relationships
Brand	estimated expected life of brand
Licenses	term of licensing agreements
Patents	term of patent life
Customer order backlog	estimated expected life of backlog
Air permits	estimated expected life of permit
Non-patented technology	estimated expected life of related products

Non-contractual customer relationships are amortized over periods ranging from three to ten years, brand over ten years, licenses over periods ranging from three to nine years, patents over ten years, customer order backlog over three months, air permits over five years, and non-patented technology over five years.

Product certification and safety marks acquired in business acquisitions are indefinite-life intangible assets recorded at cost and are not amortized.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of long-lived assets

Long-lived assets of the Company include property, plant and equipment and intangible assets. These assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Impairment is recognized when the undiscounted cash flows from the assets exceeds the carrying value. An impairment loss is then measured at the amount that the carrying amounts exceed their fair value.

During the year, 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 represents the excess of the purchase price of acquired businesses over the estimated fair value of net identifiable assets acquired. Goodwill is not amortized but must be tested for impairment annually or more frequently when events or circumstances occur that would indicate that the carrying value may be impaired. Recoverability of goodwill is determined at the reporting unit level using a two-step approach. First, the carrying value of the reporting unit is compared to its fair value, which is determined based on discounted future cash flows. If the carrying value of the reporting unit exceeds its fair value, the second step is performed. In this step, the amount of impairment loss, if any, represents the excess of the carrying value of goodwill over its fair value and the loss is charged to income in the period in which it is incurred. For this step of the impairment test, the fair value of the goodwill is estimated in the same way as goodwill is determined in a business combination as the excess of the fair value of the reporting unit over the estimated fair value of its net identifiable assets.

Self-insured liabilities

The Company self-insures certain risks related to pollution protection provided on certain product sales, general liability claims, health benefit claims and patent infringement through Radigan Insurance Inc., its captive insurance company. The provision for self-insured liabilities includes estimates of the costs of reported and expected claims based on estimates of loss using assumptions determined by a certified loss reserve analyst.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Employee Future Benefits

As a result of the Xerxes business acquisition described in note 2a, the Company's consolidated financial statements now include a defined benefit pension plan, a defined contribution retirement benefit plan and a non-retirement employee benefit plan, as described below.

The Company has a noncontributory defined benefit pension plan for former employees of a previously closed plant facility of one of the Company's US-based subsidiaries. The cost of the defined benefit pension is actuarially determined using the projected benefits method. For purposes of calculating the expected return on plan assets, those assets are valued at fair value. Accrued benefit obligations are discounted at the end of each period based on the rate at which obligations could be effectively settled, considering the timing of estimated future cash flows related to the plan. This rate is based on high-quality bond yields, after allowing for call and default risk. See note 9 for additional information.

The Company contributes to a defined contribution 401(k) retirement plan for all US based employees meeting the plan requirements. The Company accounts for such contributions as an expense in the period in which the contributions are due. Total contribution expense recognized during the year ended December 31, 2007 was approximately \$333,000.

The Company has self-insured the liability associated with providing health and welfare insurance benefits to its US-based employees. The Company records an expense in the period in which eligible claims are presented for payment by its employees and third party claims administrator fees are presented for payment. The Company also accrues a liability for the anticipated obligation from health insurance claims not yet submitted based on expected claims experience calculated by the third party administrator. Adjustments to the liability are recorded in the period that actual claims experience is determined.

The Company also contributes to a defined contribution retirement plan for all Canadian based employees meeting the plan requirements. Under the plan, the Company matches employee contributions to a maximum of 4% of an employee's earnings. The Company accounts for such contributions as an expense in the period in which the contributions are made. Total contribution expense recognized in 2007 was \$214,000 (2006 - \$94,000).

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 used solely for storage of listed liquids. A number of component materials and parts are similarly warranted by their manufacturers, thereby offsetting the Company's exposure to warranty claims.

The Company's complete storage systems marketed under the Prezerver trademark carry an enhanced ten-year, insurance-backed warranty covering product replacement and pollution protection up to the limits of the policy. The Prezerver warranty is covered by insurance underwritten by a major international insurer for Prezerver storage systems installed before December 1, 2006. The Prezerver warranty for qualifying storage systems installed thereafter is insured through the Company's captive insurance company, Radigan Insurance Inc.

The Company provides for warranty obligations based on a review of products sold and historical warranty cost experience. Provisions for warranty costs are charged to manufacturing and selling costs and revisions to the estimated provision are charged to earnings in the period in which they occur.

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 using the temporal method 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.

Two of the Company's principal operating subsidiaries, Xerxes Corporation and VRB & Associates SRL are self sustaining foreign operations. The financial statements of these subsidiaries are included in the consolidated financial statements translated using the current rate method. Under this method, all assets and liabilities are translated at the balance sheet date exchange rate, and revenue and expense items are translated at the average exchange rate for the period. The resulting exchange gains and losses are recorded in other comprehensive income (loss).

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition

Revenue from the sale of liquid storage systems and related products and accessories is recorded when persuasive evidence of an arrangement exists, the purchaser's price is fixed and determinable, collection is reasonably assured and ownership is effectively transferred to the purchaser. This normally occurs at the time of shipment of the product, customarily on a FOB-shipping basis. In circumstances where the customer chooses to temporarily store goods on the Company's premises but all other contract performance criteria have been met, revenue is recognized upon manufacturing completion. Amounts received as deposits are recorded as deferred revenue. Where final acceptance of products is specified by the customer, revenue is deferred upon manufacturing completion until all acceptance criteria have been met.

Stock-based compensation

Stock options resulting in 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. The fair value of stock options and warrants at the date of grant or transfer is determined using an option pricing model and compensation expense is recognized over the vesting period of the stock options and warrants.

The Company uses the fair value method to account for specified stock-based compensation awards issued under the Company's Stock Appreciation Rights Plan ("SARs") and Executive Restricted Share Unit Plan ("RSUs) that call for settlement in cash. The Company records compensation expense based on the market value of the Company's common shares for the outstanding RSUs and the difference between the market value of the Company's common shares and the value specified under the SARs plan, if any. Changes in the market value of the Company's common shares result in compensation for the SARs and RSUs being re-measured at each reporting period.

The Company's stock-based compensation, consisting of a stock option plan and warrants, stock appreciation rights and executive restricted share unit plans is more fully described in notes 12 and 13.

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.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 and warrants 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. Anti-dilutive amounts are not considered in computing diluted earnings per share.

Changes in Significant Accounting Policies

a) Financial instruments, equity and comprehensive income (loss)

Effective January 1, 2007, the Company adopted the Canadian Institute of Chartered Accountants (CICA) Section 3855, Financial Instruments – Recognition and Measurement; Section 3861, Financial Instruments – Disclosure and Presentation; Section 3865, Hedges; Section 1530, Comprehensive Income; and Section 3251, Equity, prospectively without restatement of prior periods.

Section 1530 provides guidance on the reporting and presentation of comprehensive income. Comprehensive income is the change in equity of an enterprise during a period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. Other comprehensive income comprises revenues, expenses, gains and losses that are recognized in comprehensive income, but are excluded from net income calculated in accordance with GAAP. The adoption of this standard had no impact on the Company's retained earnings as at January 1, 2007. Subsequent to the adoption of this new standard, the Company recorded unrealized losses of \$8.7 million on the translation of self-sustaining foreign operations acquired during the year in other comprehensive income (loss).

Under Section 3855, financial assets and liabilities are classified as either held for trading, available-for-sale, loans and receivables, investments held to maturity, and other financial liabilities. Financial assets classified as held for trading and available-for-sale are measured on the balance sheet at fair value. Subsequent change in the fair value of held for trading financial assets is recognized into net income immediately. Changes in the fair value of financial assets available-for-sale are recorded in comprehensive income until the investment is derecognized or impaired at which time amounts would be recorded to net income. Loans and receivables, investments held to maturity and other financial liabilities are measured on the balance sheet at amortized cost. All

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

derivative instruments of the Company, including those embedded in other financial instruments, are recorded at fair value and classified as held for trading.

On adopting Section 3855 and 3861, the Company classified its financial assets and liabilities of cash and cash equivalents, accounts receivable, other assets, and accounts payable and accrued liabilities and bank indebtedness as held for trading financial instruments. The adoption of the new standards did not have a material impact on the presentation of the financial statements. The Company classified long term debt as other financial liabilities. The Company has not recorded any financial instruments as available-for-sale, loans or receivables, or held to maturity investments during the year.

For financial assets and liabilities classified as other, the transaction costs that are directly attributable to the acquisition or issue of a financial asset or financial liability are recorded as part of the fair value initially recognized for that financial instrument. These costs are expensed using the effective interest method and recorded within interest expense.

Prior to the adoption of the new standards, derivatives embedded in other financial instruments were not accounted for separately from the host instrument. On adopting the new standards, the Company performed a review of all of its contracts to identify any embedded derivatives. No significant embedded derivatives were identified.

Section 3865 replaces and expands prior guidance on hedging relationships by prescribing when and how hedge accounting may be applied. Application of hedge accounting is optional. Adoption of the new standard had no impact on the financial statements. During the year, the Company entered into foreign currency forward contracts, the price of which were denominated in US dollars. Such 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. As of December 31, 2007, there were no outstanding derivative contracts as they were all settled within the year.

Section 3251 requires separate presentation of changes in equity for the period from net income, other comprehensive income (loss), retained earnings, contributed surplus, share capital and reserves and separate presentation of the components of equity, including retained earnings, accumulated other comprehensive income (loss), contributed surplus, share capital and reserves. The adoption of the new standard did not have a material impact on the presentation of equity of the Company.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

b) Accounting changes

Effective January 1, 2007, the Company adopted CICA Section 1506, Accounting Changes. The new standard allows for voluntary changes in an accounting policy only when the changes result in the financial statements providing reliable and more relevant information, requires a change in accounting policy to be applied retroactively unless impracticable, requires prior period errors to be corrected retrospectively and calls for enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements. It includes the disclosure, on an interim and annual basis, of a description and the impact on the Company's financial results of any new primary source of GAAP that has been issued but is not yet effective. The adoption of the new standard did not have an impact on the Company's financial position or on the results of its operations.

Recent Accounting Pronouncements

In October 2006, the CICA issued Section 1535, Capital Disclosures. The new standard requires disclosure of qualitative and quantitative information that enables users of financial statements to evaluate the Company's objectives, policies and processes for managing capital. These recommendations are effective for the Company's interim and annual reporting periods beginning January 1, 2008. The Company expects there will be incremental disclosures required regarding the Company's capital and how it is managed.

The CICA also issued Section 3862, Financial Instruments – Disclosure and 3863, Financial Instruments – Presentation in October 2006. These Sections will effectively replace existing Section 3861, Financial Instruments – Disclosure and Presentation effective for the Company's interim and annual reporting periods beginning January 1, 2008. Section 3862 requires disclosures by class of financial instruments that enable users to evaluate the significance of financial instruments for the Company's financing position and performance. Disclosures are also required of qualitative and quantitative information that enables users of financial statements to evaluate the nature and extent of the Company's exposure to the risks arising from financial instruments, specifically credit risks, liquidity risks and market risks. Quantitative disclosures must also include a sensitivity analysis for each type of market risk the Company is exposed to and how net income and other comprehensive income would be affected. Section 3863 carries forward the presentation requirements of 3861 already adopted by the Company. As a result, the Company expects the only effect of the new standards will be additional disclosures regarding the significance of financial instruments for the Company's financing position and performance and the nature, extent and management of risks arising from financial instruments to which the Company is exposed.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In June 2007, the CICA issued Section 3031, Inventories. The new standard requires inventories to be measured at the lower of cost and net realizable value and provides guidance on the determination of cost, including the allocation of overheads and other costs to inventories. The standard also requires the consistent use of either the FIFO (first in, first out) or weighted average cost formula to measure inventories and the reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories. Disclosure is required for the amount of inventories recognized as an expense, as well as any inventory write-down or reversals. The standard is effective for the Company's interim and annual reporting periods beginning January 1, 2008. The Company does not expect the new standard will have a material impact on the Company's net income.

In February 2008, the CICA issued Section 3064, Goodwill and Intangible Assets, replacing Section 3062, Goodwill and Other Intangible Assets and Section 3450, Research and Development Costs. The new pronouncement establishes standards for the recognition, measurement, presentation, and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. The Company is currently evaluating the impact of adopting the standard.

In February 2008, Canada's Accounting Standards Board confirmed January 1, 2011 as the official changeover date for publicly listed Canadian companies to start reporting under International Financial Reporting Standards ("IFRS"). As the International Accounting Standards Board currently has projects underway that should result in new pronouncements and the Canadian convergence initiative is on-going as of the date of these statements, the Company has not yet assessed the impact of the ultimate adoption of IFRS.

2. BUSINESS ACQUISITIONS

a) XAHC, Inc.

On February 22, 2007, the Company purchased 100% of the shares of XAHC, Inc. ("XAHC"), the sole shareholder of Xerxes, for cash consideration of USD \$39.6 million (CDN \$46.3 million) including acquisition costs. XAHC and Xerxes are based in the United States and are involved in the design, manufacture and marketing of fibreglass reinforced plastic structural products for the petroleum, chemical, water and wastewater industries.

The business acquisition was accounted for using the purchase method and the consolidated financial statements include the results of operations from February 22, 2007. Management concluded that the purchase price allocation was substantially complete as of June 30, 2007.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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2. BUSINESS ACQUISITIONS (CONTINUED)

Subsequently, additional information related to income taxes and pension liabilities was identified that resulted in adjustments to certain assigned fair values at year end. The adjustments identified resulted in a decrease to other long term assets of \$474,000 and future tax liabilities of \$589,000, an increase to non-cash working capital and accrued pension liability of \$315,000 and \$168,000 respectively for a net decrease to goodwill of \$262,000.

The following table summarizes the fair value of acquired assets and liabilities after final adjustments:

(in thousands of dollars)	\$
Bank indebtedness, net	(6,343)
Non-cash working capital	10,712
Property, plant and equipment	5,946
Non-contractual customer relationships	6,934
Customer order backlog	306
Brand	3,418
Air permits	357
International licenses	780
Accrued pension liability	(168)
Future tax liabilities	(5,694)
Goodwill	30,057
Net assets acquired	46,305

Intangible assets are being amortized using the straight line method over the following terms:

Non-contractual customer relationships	3 to 10 years
Customer order backlog	3 months
Brand	10 years
Air permits	5 years
International licenses	9 years

The minimum lease commitments under all non-cancelable operating leases for production facilities, office space and equipment acquired were approximately \$6.7 million. Prior to the acquisition, the Company had a license agreement with Xerxes which gave the Company exclusive rights to manufacture and sell products in certain geographic areas. Aggregate annual royalty payments under the agreement were \$300,000 of which \$43,333 was payable by the Company at the date of the acquisition.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

2. BUSINESS ACQUISITIONS (CONTINUED)

b) Cara Concrete Products Ltd.

On August 9, 2007, the Company purchased certain property, plant and equipment from Cara Concrete Products Ltd. ("CARA") and on October 5, 2007 acquired the remaining operating assets of CARA for a combined cash consideration of \$2,960,000. Acquisition costs of \$51,000 were incurred in respect of the purchase. The business acquisition was accounted for using the purchase method and the consolidated financial statements include the results of operations of CARA from October 5, 2007.

The following table summarizes the fair value of acquired assets:

(in thousands of dollars)	\$
Non-cash working capital	79
Property, plant and equipment	2,932
Net assets acquired	3,011

3. INVENTORIES

(in thousands of dollars)	2007 \$	2006 \$
Raw materials	7,865	5,420
Work in progress	2,483	748
Finished goods	5,870	4,639
	16,218	10,807

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

4. PROPERTY, PLANT AND EQUIPMENT

(in thousands of dollars)	2007		2006	
	Cost	Accumulated amortization	Cost	Accumulated amortization
	\$	\$	\$	\$
Land	2,983	—	293	—
Buildings	5,205	1,209	3,160	1,081
Leasehold and land improvements	1,659	298	572	182
Manufacturing equipment	19,275	8,351	14,230	7,427
Office equipment	2,743	1,521	2,183	1,290
Automotive equipment	463	200	274	144
	32,328	11,579	20,712	10,124
Net book value	20,749		10,588	

Amortization expense includes \$1,600,000 (2006 - \$801,000) for the amortization of property, plant and equipment. Capital work-in-progress of \$972,000 is included in manufacturing and office equipment (2006 - \$260,000 is included in buildings) and is not subject to amortization.

5. DEFERRED DEVELOPMENT COSTS

(in thousands of dollars)	2007	2006
	\$	\$
Cost	1,652	3,798
Accumulated amortization	833	2,748
Net book value	819	1,050

Deferred development costs include \$26,000 (2006 - \$26,000) of scientific research and development tax credits received or receivable. Deferred development costs of \$13,000 (2006 - \$nil) were incurred during the year. Amortization expense includes \$244,000 (2006 - \$89,000) for the amortization of deferred development costs. 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. Development costs that were fully amortized during the period ended December 31, 2006 were relieved from the accounts at December 31, 2007.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

6. INTANGIBLE ASSETS

(in thousands of dollars)	2007		2006	
	Cost	Accumulated amortization	Cost	Accumulated amortization
	\$	\$	\$	\$
Intangible assets subject to amortization:				
Non-contractual customer relationships	5,970	914	125	94
Brand	2,873	239	—	—
Licenses	1,177	581	521	491
Patents	369	80	369	43
Customer order backlog	264	264	20	20
Air permits	300	50	—	—
Non-patented technology	1,944	1,944	1,944	1,814
	12,897	4,072	2,979	2,462
Intangible assets not subject to amortization:				
Product certification and safety marks	170	—	170	—
	13,067	4,072	3,149	2,462
Net book value	8,995		687	

Amortization expense includes \$887,000 (2006 - \$35,000) for the amortization of non-contractual customer relationships, \$260,000 (2006 - \$nil) for brand, \$96,000 (2006 - \$25,000) for licenses, \$37,000 (2006 - \$28,000) for patents, \$264,000 (2006 - \$nil) for customer order backlog, \$54,000 (2006 - \$nil) for air permits, and \$130,000 (2006 - \$291,000) for non-patented technology.

7. GOODWILL

(in thousands of dollars)	2007	2006
	\$	\$
Balance, beginning of the period	1,991	1,991
Goodwill from business acquisition [note 2a]	30,057	—
Translation adjustment	(4,721)	—
Balance, end of the period	27,327	1,991

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

8. BANK INDEBTEDNESS

Bank indebtedness consists of amounts drawn under available credit facilities and cheques issued in excess of related bank balances. The Company has a revolving operating credit facility to a maximum \$15,250,000 (2006 - \$10,250,000) for working capital and other general corporate purposes. The credit facility is payable on demand and expires on July 29, 2008. Depending on the form under which the credit facility is accessed, rates of interest vary between Canadian prime plus zero or 25 basis points, US base rate plus zero or 25 basis points, or Canadian bankers acceptances with terms of 1, 2, 3, or 6 months, subject to availability plus 150 or 175 basis points. Interest rates are adjusted quarterly based on certain financial performance indicators of the Company. At December 31, 2007 the effective interest rate on this credit facility was prime plus 25 basis points (6.25%; 2006 – 6.25%).

The Company has pledged as general collateral for advances under the operating credit facility and the term loan (see note 10) a general security agreement on present and future assets, guarantees from each present and future direct and indirect subsidiary of the Company supported by a first registered security over all present and future assets, and pledge of shares.

The Company is required to meet certain covenants as a condition of the debt agreements. At December 31, 2007, the Company was in compliance with all restrictive covenants.

9. ACCRUED PENSION LIABILITY

The pension liability relates to a noncontributory defined benefit pension plan (the “Plan”) for former full-time union employees of a previously closed plant facility of Xerxes. The employment of all participants in the Plan was terminated in 2001 and their benefit accrual fully vested. The Plan assets and the accrued benefit obligation are measured on December 31 each year.

In November 2006, trustees of the Plan approved a process that was expected to result in full settlement of plan obligations by the end of 2007. As part of the on-going settlement process, participants will have the option of receiving either a lump sum payment or a guaranteed annuity contract that would be purchased by the plan from a private insurance company. As part of the approved settlement process, the Plan’s investments were all converted to cash and cash equivalents in the form of money market fund investments in December 2006. Settlement of the plan obligations is now expected to occur by the end of 2008.

The Company will fully fund the existing shortfall of the Plan upon final settlement. The expected benefit payments to participants from the Plan for 2008 are approximately \$98,000, assuming no lump sum payments, or \$614,000, assuming approximately one half of the participants opt for lump sum payments.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

9. ACCRUED PENSION LIABILITY (CONTINUED)

Information regarding the Plan is summarized as follows and reflects management's best estimates of the accrued benefit obligation based on assumptions consistent with the approved settlement process.

(in thousands of dollars)	2007 \$	2006 \$
Change in fair value of plan assets during the period		
Fair value of plan assets, upon acquisition of Xerxes	2,178	—
Actual return on plan assets	74	—
Employer contributions	—	—
Benefits paid	(90)	—
Translation adjustment	(346)	—
Fair value of plan assets, end of the period	1,816	—
Change in accrued benefit obligation during the period		
Accrued benefit obligation, upon acquisition of Xerxes	2,346	—
Interest cost	92	—
Actuarial loss	130	—
Benefits paid	(90)	—
Translation adjustment	(378)	—
Accrued benefit obligation, end of the period	2,100	—
Accrued pension liability	(284)	—

Weighted-average actuarial assumptions used to determine obligations at December 31 and periodic benefit cost for the period then ended

Discount rate	4.59%	—
Expected return on assets	5.50%	—
Rate of compensation increase	N/A	—

The discount rate used to determine the accrued benefit obligation was 5.22% and the expected return on assets rate used was 5.50% at February 22, 2007. Pension expense increases as the expected return on assets rate decreases. A decrease in the expected return on plan assets of 25 basis points (from 5.50% to 5.25%) would increase the expected 2008 pension expense by \$3,900. The pension liability and future pension expense both increase as the discount rate is reduced. Lowering the discount rate by 25 basis points (from 4.59% to 4.34%) would increase the 2007 pension expense and liability at December 31, 2007 by \$49,000.

An expense of \$148,000 relating to the increase in the accrued pension liability since acquisition was recorded in general and administration in the consolidated statements of income.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

10. LONG TERM DEBT

(in thousands of dollars)	2007 \$	2006 \$
Term loan	8,938	—
Less current portion	1,960	—
	6,978	—

The term loan bears interest at an annualized rate of Canadian bank prime plus 25 or 50 basis points, adjusted quarterly based on certain financial performance indicators of the Company. The term loan requires quarterly repayments of \$500,000, with the balance due on maturity on February 28, 2009. The Company is also subject to mandatory prepayments of outstanding loan principal equal to 100% of any net proceeds of asset disposal and net proceeds from any insurance proceeds received by the Company. Transaction costs directly attributable to the term loan are recorded as part of the fair value of the debt and reflected in the measurement of the fair value of the obligation using the effective interest method.

The Company's operating and term credit facilities are utilized as required throughout the year. Both credit facilities bear interest at floating rates and changes in interest rates would affect the Company's exposure to interest rate risk in servicing the facilities.

11. DIVIDENDS

During the year ended December 31, 2007 dividends in the amount of \$2,600,000 (\$0.10 per common share for all shareholders of record on March 28, 2007) were paid. In the period ended December 31, 2006, dividends in the amount of \$2,081,000 (\$0.10 per common share for all shareholders of record on June 26, 2006) were paid.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS

a) Share capital and contributed surplus

Authorized

Unlimited number of common shares with no par or stated value

Issued and outstanding

(in thousands of dollars)	Share Capital				Contributed Surplus	
	2007		2006		2007	2006
	Shares #	\$	Shares #	\$	\$	\$
Balance, beginning of the period	21,681,445	23,135	20,118,953	21,397	452	348
Common shares	4,000,000	38,147	—	—	—	—
Stock options exercised for cash	281,334	282	364,065	451	—	—
Warrants exercised for cash	482,750	459	1,198,427	1,139	—	—
Reclassification of fair value of stock options and warrants previously expensed	—	167	—	148	(167)	(148)
Stock-based compensation expense	—	—	—	—	164	252
Balance, end of the period	26,445,529	62,190	21,681,445	23,135	449	452

On February 13, 2007 the Company completed a "bought deal" private placement of subscription receipts with a syndicate of underwriters whereby the underwriters purchased as principals 4,000,000 subscription receipts at a price of \$10.00 per subscription receipt for total gross proceeds of \$40.0 million. After deducting expenses of the offering of \$2,650,000 (\$1,853,000 net of taxes), net cash proceeds of \$37,350,000 were received. Each holder of subscription receipts automatically acquired one common share of the Company (4,000,000 shares were issued) in exchange for every one subscription receipt held without the payment of any additional consideration upon closing of the XAHC/Xerxes acquisition described in note 2a. The issued shares were subject to trading restrictions for a four-month period subsequent to issuance.

During the year, the amount credited to share capital related to options and warrants exercised included \$72,000 (2006 - \$45,000) for options and \$95,000 (2006 - \$103,000) for warrants in respect of compensation expense previously included in contributed surplus.

b) Stock options

On August 9, 2006 the Company's shareholders approved the replacement of its existing share option plan with a new stock option plan. Under the Company's new stock option plan, options to purchase common shares may be granted by the Board of Directors to directors, employees, and persons who provide management or consulting services to the Company. All options issued

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS (CONTINUED)

under the previous share option plan were deemed to be issued under the new plan on the same terms and conditions as existed under the old plan. The shareholders authorized the number of options that may be granted under the new plan to be not more than 10% of the issued and outstanding shares of the Company on a non-diluted basis provided that the number of listed securities that may be reserved for issuance under stock options granted to any one individual or insiders of the Company not exceed 5% of the Company's issued and outstanding securities. The exercise price of options granted cannot be less than the closing market price of the Company's common shares on the last trading day preceding the grant. The Company's Board of Directors may determine the term of the options but such term cannot be greater than 5 years from the date of issuance. Vesting terms, eligibility of qualifying individuals to receive options and the number of options issued to individual participants are determined by the Company's Board of Directors. The plan has no cash or equity settlement features. Options generally expire 90 days from the date on which a participant ceases to be a director, officer, employee, management company employee or consultant of the Company.

The Company has 254,068 (2006 – 498,002) options outstanding, which expire on dates between May 2009 and December 2012. The following table presents the changes during and the options outstanding at the end of each of the fiscal years:

	<u>2007</u>		<u>2006</u>	
	<u>Shares</u>	<u>Weighted Average</u>	<u>Shares</u>	<u>Weighted Average</u>
	<u>#</u>	<u>Exercise Price</u>	<u>#</u>	<u>Exercise Price</u>
		<u>\$</u>		<u>\$</u>
Balance, beginning of the period	498,002	1.69	812,067	1.31
Granted	37,400	10.14	50,000	4.55
Exercised	(281,334)	1.00	(364,065)	1.24
Expired	—	—	—	—
Balance, end of the period	254,068	3.70	498,002	1.69

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS (CONTINUED)

Exercise Price \$	2007			
	Options Outstanding		Options Exercisable	
	Shares #	Weighted Average Remaining Contractual Life in Years	Shares #	Weighted Average Exercise Price \$
1.40	100,001	1.40	100,001	1.40
2.90	66,667	2.92	33,333	2.90
4.55	50,000	3.47	50,000	4.55
10.14	37,400	4.93	—	10.14
1.40 – 10.14	254,068	3.25	183,334	2.53

Exercise Price \$	2006			
	Options Outstanding		Options Exercisable	
	Shares #	Weighted Average Remaining Contractual Life in Years	Shares #	Weighted Average Exercise Price \$
0.95	250,000	0.87	250,000	0.95
1.40	131,335	2.40	54,667	1.40
2.90	66,667	3.92	—	2.90
4.55	50,000	4.50	50,000	4.55
0.95 – 4.55	498,002	2.05	354,667	1.53

c) Warrants

As part of a private placement in September 2002, the Company issued 3,684,211 Performance Warrants (“Warrants”). 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 entitled 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 vested 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 first two thresholds were reached during the fiscal year ended March 31, 2005; the third vesting threshold was reached in the fiscal period ended December 31,

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS (CONTINUED)

2006 and the remaining 1,228,070 unvested warrants vested. All remaining warrants were exercised during the year ended December 31, 2007.

	2007		2006	
	Warrants #	Exercise Price \$	Warrants #	Exercise Price \$
Balance, beginning of the period	482,750	0.95	1,681,177	0.95
Exercised	(482,750)	0.95	(1,198,427)	0.95
Expired	—	—	—	—
Balance, end of the period	—	—	482,750	0.95

13. 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. These models require subjective assumptions, including future share price volatility and expected time until exercise, which affect the calculated values. The options and warrants contemplated by the Black-Scholes model differ significantly from the stock options granted and warrants transferred by the Company. Accordingly, management believes that these models do not necessarily provide a reliable single measure of the fair values of the stock options granted and warrants transferred by the Company.

a) Stock options granted

The Company uses the fair value method of accounting for all stock options granted to employees. During the fiscal period ended December 31, 2007, the Company granted 37,400 stock options with exercise prices at the market share price on the grant date (December 31, 2006 – granted 50,000 options with exercise prices at the market price on the grant date). Stock-based compensation expense of \$120,000 (December 31, 2006 - \$131,000) and \$44,000 (December 31, 2006 - \$121,000) is recorded in manufacturing and selling costs and general and administration costs respectively in the consolidated statements of income.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

13. STOCK-BASED COMPENSATION (CONTINUED)

The following estimated fair values of stock options granted at market during the year were determined, at the date of the grant, using the Black-Scholes option pricing model with the following weighted-average assumptions:

Weighted-average fair value	\$4.08
Risk-free interest rate (%)	3.88
Expected hold period to exercise (years)	4.0
Volatility in the price of the Company's shares (%)	50.0
Dividend yield (%)	1.0

Prior to adopting the fair value method of accounting for share options granted and warrants transferred to employees, the Company had granted or transferred share options and warrants with exercise prices in excess of the market share price on the grant or exercise date to employees. Pro forma earnings per share, had compensation expense been recognized based on the fair value as at the date of the grant or transfer of the options granted and warrants transferred to employees, is the same as the reported basic and diluted earnings per share for the periods ended December 31, 2007 and 2006.

b) Stock appreciation rights

On December 3, 2007 the Company's Board of Directors approved a Stock Appreciation Rights Plan where SARs may be granted to Directors, officers and employees of the Company at the Board's discretion. Each SAR entitles the holder to the cash amount for the difference between the value specified under the Plan and the market value of the Company's common shares on the exercise date. The rights vest equally over a three year period and expire at the end of 2011. There were 230,250 SARs granted and outstanding and not vested at December 31, 2007. Compensation expense of \$4,200 was recorded relating to SARs during 2007.

c) Restricted share units

On December 3, 2007 the Company's Board of Directors approved an Executive Restricted Share Unit Plan where each designated executive receives an annual grant of RSUs as part of their compensation at the Board's discretion. Each RSU represents one notional common share that entitles the participant to an equivalent cash amount. The RSUs granted are generally scheduled for payout after five years and vest upon attainment of performance targets or at the later of the end of five years following the year of the date of grant. There were 21,000 RSUs granted and

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

13. STOCK-BASED COMPENSATION (CONTINUED)

outstanding and not vested at December 31, 2007. Compensation expense of \$3,800 was recorded relating to RSUs during 2007.

14. INCOME TAXES

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

(in thousands of dollars)	2007 \$	2006 \$
Statutory federal and provincial taxes at 32.55% (2006 – 32.25%)	3,239	1,920
Increase (decrease) in income taxes resulting from:		
Rate differences for foreign jurisdictions	185	—
Effect of enacted future rates on temporary differences	(82)	(121)
Non-taxable foreign income net of non-creditable withholding taxes and other tax exempt income and other items	(904)	100
	<u>2,438</u>	<u>1,899</u>

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

14. INCOME TAXES (CONTINUED)

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

(in thousands of dollars)	2007 \$	2006 \$
Future tax assets		
Share issue costs	631	8
Tax basis in excess of carrying value of:		
Deferred development costs	372	446
Non-deductible reserves and pension liability	1,019	—
State loss carry forward	200	—
Other	90	43
	2,312	497
Future tax liabilities		
Carrying value in excess of tax basis of:		
Property, plant and equipment	2,211	1,364
Intangible assets	3,349	80
Deferred development costs	238	310
Inventories	603	—
Other	118	140
	6,519	1,894
	(4,207)	(1,397)
(in thousands of dollars)	2007 \$	2006 \$
Represented by:		
Future tax assets - current	416	11
Future tax assets - long-term	—	—
Future tax liabilities - current	—	(180)
Future tax liabilities - long-term	(4,623)	(1,228)
	(4,207)	(1,397)

The Company has state loss carry forwards of approximately \$4.0 million that are available to reduce the taxable income of certain US subsidiaries that expire at varying times from 2009 to 2027. The potential income tax benefits that will result from the application of US tax losses have been recognized in these financial statements.

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

15. COMMITMENTS AND CONTINGENCIES

a) Commitments

Operating leases

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

(in thousands of dollars)	\$
2008	1,779
2009	1,637
2010	1,115
2011	953
2012	861
Thereafter	1,758

Purchase obligations

The Company has purchase obligations for equipment in the amount of \$699,000 at December 31, 2007 that are expected to be paid in the first quarter of 2008.

b) Contingencies

In the normal conduct of operations, various legal claims or actions are pending against the Company in connection with its products and/or other commercial matters. The Company carries liability insurance, subject to certain deductibles and policy limits, against such claims. Based on advice and information provided by legal counsel, management believes that no provision for these matters is required and that their ultimate resolution will not have a material adverse effect on the financial position of the Company or its operations. The amount of loss, if any, incurred upon resolution of these matters will be recorded in the period in which the uncertainty regarding the matter is resolved and the amount of the loss can be reasonably estimated.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

16. 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)	Twelve Months ended December 31, 2007 \$	Nine Months ended December 31, 2006 \$
Numerator:		
Net income	7,515	4,056
Denominator:		
Weighted-average shares outstanding - basic	25,536,328	21,049,658
Effect of dilutive securities		
Stock options	192,788	440,197
Warrants	—	715,572
Weighted-average shares outstanding - diluted	25,729,116	22,205,427

17. STATEMENT OF CASH FLOWS

Supplementary disclosures required in respect of the Statement of Cash Flows are as follows:

(in thousands of dollars)	Twelve Months ended December 31, 2007 \$	Nine Months ended December 31, 2006 \$
Net interest paid	536	39
Income taxes paid	3,545	1,200

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

18. RELATED PARTY TRANSACTIONS

A corporation controlled by a director of the Company provided trucking services to the Company during 2007. This director resigned from the Board effective September 18, 2007 and is no longer a related party. Included in manufacturing and selling costs in the consolidated statements of income in 2007 was \$428,000 (2006 - \$473,000) related to these services. The transactions were recorded at the exchange amounts being normal commercial rates for the services. Accounts payable and accrued liabilities included \$22,000 (2006 - \$26,000) owing to the corporation.

Certain components purchased for \$103,000 (2006 - \$165,000), included in manufacturing and selling costs in the consolidated statements of income, were provided by a corporation whose Chairman and CEO is an individual who became a director of the Company on May 15, 2007. The value of the components purchased from May 15, 2007 to the end of the year is \$53,000. The transactions were recorded at the exchange amount being normal commercial prices for the products. Accounts payable and accrued liabilities included \$1,000 (2006 - \$3,800) owing to the corporation. There are no ongoing contractual or other commitments resulting from these transactions.

19. OTHER EXPENSES (INCOME)

a) Financing expense (income)

	Twelve months ended December 31, 2007	Nine months ended December 31, 2006
(in thousands of dollars)	\$	\$
Short term interest, net of interest income	57	(39)
Interest, long term debt	506	—
Foreign exchange losses	510	39
	1,073	—

b) Amortization

	\$	\$
(in thousands of dollars)		
Property, plant and equipment	1,600	801
Deferred development costs	244	89
Intangible assets	1,728	379
	3,572	1,269

ZCL Composites Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2007 and 2006

20. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments

The fair value of cash and cash equivalents approximate the carrying value due to the relatively short periods to maturity of these instruments. The fair value of long term debt approximates the carrying value due to the variable interest component of the debt.

Foreign currency risk management

The consolidated financial statements are reported in Canadian dollars, including the results of its foreign subsidiaries. The Company operates globally, which gives rise to a risk that earnings and cash flows may be adversely affected by fluctuations in foreign currency exchange rates. The Company is primarily exposed to the US dollar but also transacts in the Euro. The US operations account for approximately one half of the Company's revenues and expenses. The Company's Canadian operations also purchase materials that are denominated in US dollars and in 2007 these purchases approximated the earnings generated by the US operations resulting in a natural hedge of the Company's overall earnings. While the Company's overall earnings were generally naturally hedged against fluctuations in the US-Canadian dollar conversion rate, the gross amount of revenue and expenses can fluctuate based on changes in the conversion rate. For example, in 2007 the average conversion rate was \$1.05, a \$0.01 change in this rate would have increased or decreased the reported US revenue amount of \$55.9 million by approximately \$0.6 million. There can be no assurance that this natural hedge will continue to occur and as a result the Company's earnings may be positively or negatively impacted by fluctuations in the value of the Canadian dollar. The Company does not currently use financial instruments to hedge these risks.

Interest rate risk management

Available lines of credit are being utilized by the Company as required throughout the year. The lines of credit and long term debt bear interest at floating rates and changes in interest rates expose the Company to cash flow risk. The Company does not use financial instruments to reduce its exposure to interest rate risk.

Credit risk management

The maximum exposure to credit risk is represented by the carrying amount of the accounts receivable. 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, distributors, and independent retail oil and gas companies. Ongoing credit evaluations are performed and allowances for potential doubtful accounts maintained. No one customer generally makes up more than 10% of revenue, but at a particular point in time, depending on the

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20. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

timing of sales, there may be higher proportionate exposure in accounts receivable. At December 31, 2007 and 2006, one customer accounted for 17% and 10% of accounts receivable respectively.

21. 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 substantially all of its activities in one reportable segment, liquid containment storage systems, which include the manufacture and distribution of liquid storage systems including fiberglass underground and aboveground storage tanks and related products and accessories. Previous to this fiscal year, the Company's home heating oil tank operations also qualified as a reportable segment. This segment no longer meets the criteria for a reportable segment.

Information about geographic areas

(in thousands of dollars)	Property, plant, equipment and goodwill					
	Revenues		and goodwill		Total Assets	
	2007	2006	2007	2006	2007	2006
	\$	\$	\$	\$	\$	\$
Canada and Foreign	48,834	41,399	17,408	12,579	39,308	41,415
United States	55,949	—	30,668	—	55,060	—
	104,783	41,399	48,076	12,579	94,368	41,415

Revenue is attributed to the geographic area based on location of the Company's operations. Revenue and property, plant and equipment and goodwill related to operations outside of Canada and the US is insignificant and therefore has been included in the Canadian and Foreign results.

Information about major customers

The Company has long-term contracts and alliance arrangements with many of the major oil and gas companies in Canada and provides products for distributors and retail oil and gas companies in the US. For the year ended December 31, 2007 and the nine months ended December 31, 2006, no single customer exceeded 10% of total revenue.

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21. SEGMENTED INFORMATION (CONTINUED)

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 consolidated statements of income.

22. COMPARATIVE FIGURES

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current period consolidated financial statements.