

## SIF Capital Canada Inc. – Acquisition and Development of Solar Energy Installations in Southern Ontario

Sector/Industry: Renewable Energy

[www.solarincomefund.com](http://www.solarincomefund.com)

Summary of the Proposed Offering	
Issuer	SIF Capital Canada Inc.
Offering	Minimum: \$0.5 million Maximum: Up to \$8.0 million
Securities Offered	10.75% Unsecured Debentures
Unit Price	\$1,000 per debenture
Minimum Subscription	\$5,000 (5 debentures)
Maturity Date	December 31, 2029
Management Compensation and Fees	\$12,000 p.a. management fee to Solar Income Fund Inc.
Other Fees	\$800,000 development fee to Solar Income Fund Inc.
Selling Fees and Compensation	Up to 8% commission of gross proceeds for the sale of the debentures. A one time 1% fee to Sloane Capital Corp. for distribution services.
Auditor	MNP LLP

### Investment Highlights

- SIF Capital Canada Inc. plans to acquire, develop and operate solar power sites in southern Ontario with existing feed-in tariff (FIT) contracts (under the old FIT rules).
- Through the Ontario government's FIT program, the corporation intends to sell the electricity produced from the solar installations at fixed rates through 20 year contracts.
- Most utility companies have long-term purchase agreements, making them relatively low risk investments. SIF Capital Canada Inc. is unique in that its contract will be with the Ontario government which, we believe, provides added certainty and lowers the risk of cash flows.
- A recent review of the FIT program recommended lowering FIT rates which are now effective starting August 10, 2012 – the lower rates will only apply to new contracts, and at this time, will not be retroactive on existing contracts.
- The fund plans to finance approximately 70% of the acquisition costs through a term loan (17 – 19 years) from a reputable financial institution at the higher of the fixed rate of 3.5% plus the 10 year Government Canada bond yield, or 5.4%.
- Investors could potentially receive a 10.75% p.a. cumulative return on their debentures with a maturity date of December 31, 2029.
- The expected holding period is approximately 3-5 years, at which time the corporation will look to sell the assets to an institutional investor(s) seeking stable cash flows.
- The management team has experience in the solar industry; including SIF Capital, they have created 4 different solar energy funds in the past few years.

### Risks

- Competition for available solar projects under the old FIT rates may result in delays in the execution of the business plan.
- There is political risk that the new feed-in tariff rates may be applied retroactively, thus, reducing the business' revenues. We believe that this is not a significant risk since the Ontario Power Authority recently reduced the rates on new contracts, and has stated the latest reduction was not retroactive. Our models indicate that even if the rates are reduced as per the new rules, the company will still be able to pay principal/interest to debenture holders.
- Integration companies do not always deliver projects on time or on budget, which may affect revenues and cash flows.
- This is a blind pool - management has sole discretion on which projects to invest in.
- Timely deployment of cash to acquire projects.
- The investment horizon is at the discretion of the management team as – a) the corporation has the ability to redeem debentures early, and b) debenture holders have no formal redemption option.
- Our base case models indicate that project refinancing may be required when the debentures mature at Year 17, should the company hold on to the project. This is a minor risk as our models indicate that refinancing might not be difficult based on the expected operating cash flows, and fundamentals beyond year 17.
- Interest rate risk

FRC Rating	
Base-Case Return (IRR)	10.75%
Rating	2- (Very Good)
Risk	3 (Average)

\*see back of report for rating and risk definitions

**Background  
and Terms of  
the Offering**

SIF Capital Canada Inc. (“The corporation”) was formed to participate in the clean and renewable solar energy power generation business within the province of Ontario. In 2009, Ontario passed the Green Energy Act with a FIT program that subsidizes the price per kilowatt hour of renewable energy sources. **The corporation intends to take advantage of the FIT program through the development, ownership, and operation, of commercial ground-mount, and/or commercial rooftop solar energy installations, in the province of Ontario, with a capacity of approximately 5,225 kilowatts.** The corporation intends to raise a maximum of \$8.0 million (gross), and obtain debt financing of \$20.3 million. The debenture holders are expected to receive a 10.75% p.a. cumulative return. Below is a summary of the proposed offering:

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**Purpose**

The purpose of this report is to analyze the ability of the corporation to meet the 10.75% p.a. interest for debenture holders.

**Company  
Overview**

SIF Capital Canada Inc. was formed in Alberta on February 23, 2011. The company’s head office is located at 150 Bridgeland Avenue, Suite 202, Toronto, Ontario, M6A 1Z5. The following are brief biographies of the management team:

**Paul Ghezzi, CA – President and Director**

Mr. Ghezzi started his Public Accounting career with Coopers and Lybrand in 1993. In 1996 he moved to a private industry position with Bombardier Inc. in their accounting and corporate finance group. From 1998 to 2005 he operated as an independent financial

consultant in Ontario. In 2005, Mr. Ghezzi sold his financial practice to focus on creating structured investment opportunities in the renewable energy sector. His career of providing financial management advice spans over 15 years and is highlighted by a personal dedication to creating a sustainable future through socially responsible investing. Since 2006 Mr. Ghezzi has been involved in the structuring of over \$50 Million of solar energy deals. Under his leadership SIF has grown their project under development pipeline to over \$100 Million. Mr. Ghezzi is a professional member of the Institute of Chartered Accountants of Ontario (ICAO) and the Socially Responsible Investment Organization (SIO).

### **Allan Grossman, CA – Chief Operating Officer**

Mr. Grossman, a chartered accountant, founded a boutique private equity firm in 1988. Through a worldwide network of financiers, entrepreneurs and professionals, it has facilitated start-ups, product/service extension and market expansions for companies in Canada, the US and Israel and has raised more than \$800 million through private placements. Mr. Grossman has extensive knowledge of the real estate sector and financing of real estate. Mr. Grossman has been actively involved in the solar energy power generation sector since 2008. Until June 30, 2005 Mr. Grossman was also a partner of Horwath Orenstein LLP. His education includes a Bachelor of Arts from the University of Toronto and a Chartered Accountant Designation from the Canadian Institute of Chartered Accountants.

Allan Grossman, has been subject to bankruptcy proceedings. In 2007, Mr. Grossman was a participant in several real estate development projects. Mr. Grossman was required to personally guarantee the debts of one of those projects, where in the past he never had. Due to the global economic deterioration in the debt, and equity markets in 2007, and 2008, a number of such projects suffered severe financial problems resulting from the downturn in the real estate market, and the lenders called upon Mr. Grossman's guarantee. Mr. Grossman was unable to make payments on the personal guarantee. At the same time, Mr. Grossman was reassessed for prior years' income taxes. As a result, on May 26, 2010, Mr. Grossman made a proposal to his creditors under the Bankruptcy and Insolvency Act (Canada) to settle all debts. However, the proposal was rejected by Mr. Grossman's creditors, and therefore, under the bankruptcy laws of Canada, he became a bankrupt. As of the date hereof, Mr. Grossman's bankruptcy proceedings are continuing and he has not yet been discharged. Notwithstanding his bankruptcy, Mr. Grossman remains in good standing with the Institute of Chartered Accountants of Ontario.

In an Offering Memorandum dated November 1, 2011, Solar Income Fund LP (#3) failed to disclose the facts concerning Mr. Grossman's bankruptcy proceedings, and the British Columbia Securities Commission issued a deficiency letter with respect to the prior Offering Memorandum. Solar Income Fund LP (#3) settled with the British Columbia Securities Commission by rectifying the deficiency in the above Offering Memorandum, and offered rights of rescission to unitholders of Solar Income Fund LP (#3) as a result of failing to disclose Mr. Grossman's bankruptcy.

We had analyzed Solar Income Fund LP (#2) in 2011. The OM pertaining to LP #2 at that time had also failed to disclose the facts concerning Mr. Grossman's bankruptcy proceedings.

Solar Income LP#2 and LP#3 sent out letters to all shareholders giving them the option of rescission. **We have verified documents stating that a total of \$365,000 was rescinded from Solar Income LP#2 and LP#3 – not a significant amount considering that \$9M+ was raised by the two LPs.** An investor base representing \$1.67 million sent back the form letters stating they did not want to rescind their investment. The remaining investors stayed in the fund by default.

**Past Performance**

Below is a summary of the Solar Income Fund LPs that management has previously worked on:

Project	Location	Offering Amount	Amount Raised	Date of Inception	Status	
Solar Income Fund L.P.	Acquisition, construction, ownership and operation of solar photovoltaic installations	Germany	Up to \$33 million	\$1 - \$3 million	18-Nov-08	Management stated that they decided not to go through with the project due to unfavorable currency exchanges; the money raised (approximately \$1-\$3 million) was returned to investors
Solar Income Fund (LP#2)	Development, ownership and operation of 22 micro-fit and 5 commercial rooftop solar energy installations	Windsor, Ontario	Up to \$3.58 million	\$3,405,000	26-Jan-11	For the period of January 26, 2011 to December 31, 2011, they earned revenues of \$21,259 with a net loss of \$14,780 - according to management, the revenues accounted for 1/2 a month of operations. Currently, 26 installations are up and running onto the Ontario electricity grid. 400 Kilowatts connected to the Ontario electricity grid. The remaining 4 commercial rooftop projects are delayed until September/October 2012 due to an industry backlog in Connection Impact Assessments (conducted by local hydro companies in Ontario). Management stated that since the date of the first connection until July 2012 the project has earned \$290,000 in revenue. Management anticipates that the fund will exceed \$400,000 in revenue for the calendar year of 2012.
Solar Income Fund (LP #3)	Development, ownership and operation of 150 micro-fit commercial rooftop solar energy installations	Sarnia, Ontario	Up to \$7.15 million	\$5,783,000	27-Oct-11	Management anticipates these projects to start construction in September/October 2012.

*Source: Company and Fundamental Research Corp.*

The previous funds used a limited partnership structure. Management stated that they chose a corporate structure in this case in order to qualify as a RRSP/TFSA eligible investment.

We discussed with management about the delays in the Connection Impact Assessments mentioned in the chart above. Management provided us the following reasoning on the delay in the connection impact assessments:

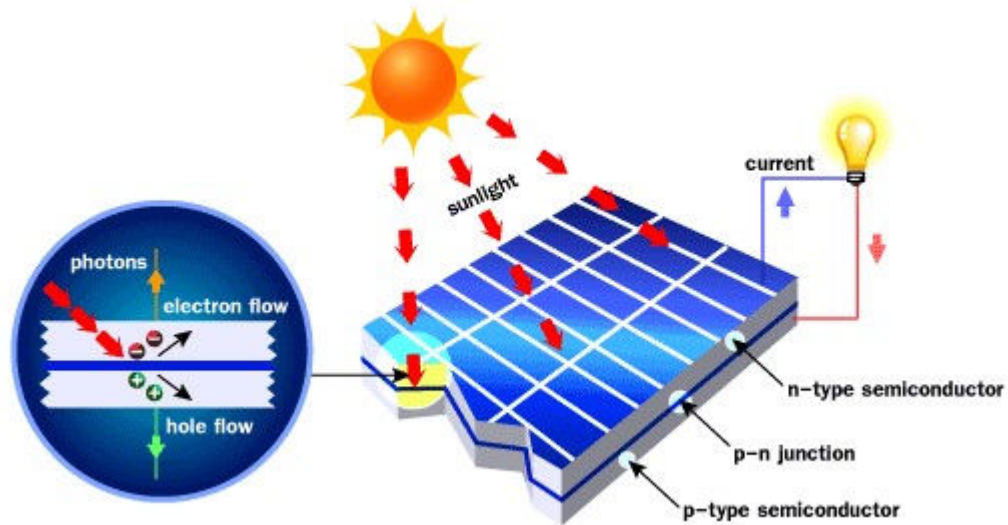
A Connection Impact Assessment (CIA) is the procedural approval from the Local Distribution Company who have control over access to the Ontario electricity grid in their jurisdiction. A CIA can only be initiated after a 20 year power purchase contract is received from the Ontario Power Authority. The purpose of the CIA is to ensure that the impact of the introduction of a solar energy installation on a particular area is properly assessed. While CIAs should take between 60 and 90 days, they are, in the majority of cases, taking between

6 and 9 months. The main cause of the delay is the large number of requests on the LDC and the limited capacity of the LDC’s internal infrastructure to meet the high volume demand.

**Overall, as shown in the chart above, we believe management has made good progress on both SIF LP#2 and SIF LP#3 – which is encouraging for potential investors of the current offering.**

**Solar Photovoltaic Cells**

Solar photovoltaic cells consist of a specially treated semi-conductor material (usually silicone) that forms an electric field, positive on one side and negative on the other. Electrical conductors are attached to the positive and negative side producing an electric circuit. When light energy (photons) hit the solar cell, some of the electrons are knocked loose and are able to form an electric current – i.e. produce electricity in the form of direct current. An inverter is then used to transform the direct current (DC) into an alternating current (AC). The diagram below illustrates the process (absent the inverter).



Source: [www.solar-advice.com](http://www.solar-advice.com)

Energy from the sun was first noted in 1839 to be able to produce electricity in certain kinds of materials, but it was not until the energy crisis in the 1970s, that photovoltaic technology gained recognition as a source of power for commercial and residential use. The major hurdle was the cost of producing electricity via PV cells compared to fossil fuels. To this day, PV cells are significantly more expensive compared to fossil fuels or nuclear energy. However, the costs have come down significantly in recent years.

**Asset Mix**

According to management, the asset mix is yet to be determined. Management expects at least 50% of the fund to be in full operation (connected to the grid) within 6 months, and the remaining 50% within 12 months. Management intends to acquire producing projects with a minimum IRR of 12% (likely in the 14%-15% range).

**From our analysis, we estimate that the valuation of a 5,225kW capacity project will be between \$25 - \$30 million. Management has allocated approximately \$26 million to acquire total capacity of 5,225 kW. We believe that this is possible; however,**



**management will still need to negotiate for the best possible valuations.**

***Integration  
Partners***

The corporation intends to engage Canadian Solar Inc. for the manufacturing and building of their solar energy installations. Should they choose to build solar energy installations where solar energy trackers are required, they will use Magna energy trackers. Below are details of these companies:

*Canadian Solar Inc. (NASDAQ: CSIQ)*

CSIQ is one of the world's largest solar companies. As a leading vertically integrated provider of ingots, wafers, solar cells, solar modules, and other solar applications, CSIQ designs, manufactures and delivers solar products, and solar system solutions, for on-grid and off-grid use to customers worldwide. With operations in North America, Europe and Asia, CSIQ provides solar solutions to support global, sustainable development. CSIQ is one of the world's largest & fastest growing solar companies. **CSIQ has agreed to sell to TransCanada (TSX: TRP), 86 MW of solar projects for approximately C\$470 million.** CSIQ will provide engineering, procurement, and construction services, and will also be the supplier of major components to the projects.

*Magna International Inc. (TSX: MG)*

Magna International, headquartered in Aurora, Ontario, is a global supplier of automotive systems, components and complete modules. Magna Closures, a wholly owned subsidiary of Manga International, will provide the trackers.

***Business Plan***

As mentioned, the corporation intends to use the proceeds of the offering to acquire, operate and construct commercial rooftop solar energy installations in Ontario. From our discussions with management, they indicated that they will **primarily focus on Southern Ontario (including Ottawa, London and Sarnia).**

**One of the major aspects of the business is the acquisition of existing FIT projects/contracts from unrelated third parties seeking construction financing or trying to monetize their projects/contracts.**

Management intends to fund the projects through debt and the proposed debenture offering. In addition, management has indicated that CSIQ has offered to provide interim construction financing, and will only require full payment of the principal when the solar installations are connected to the electricity grid.

**The solar sites will be connected to the electrical grid and sold at fixed rates defined in the FIT schedule (See chart on Page 9). The corporation will only be acquiring projects that are under old FIT pricing rules. The fixed rates are guaranteed by the Ontario government for 20 years after the date of connection to the grid.**

After all defined expenses are paid (operating expenses, capital expenditures, and reserve fund), 10.75% p.a. interest will be distributed to debenture holders. Management owns 100%

of the equity, so they have ownership of all the remaining capital.

**Why Invest in Solar Power Generation?**

The corporation is planning to exit the investment within 3-5 years. The exit strategy will be to sell the assets to a pension fund, institutional investor, or other similar entity seeking stable, low-risk cash flows.

Below we discuss the benefits of solar power generation investments in Ontario.

- **The price that SIF Capital can sell electricity is guaranteed by the Ontario Government for 20 years after the installation is connected to the electricity grid.** Most independent power producers have similar long term contracts (power purchase agreements); however, the feed-in tariff contracts are **backed by the Ontario government** which provides further certainty to the revenue stream. This allows investors to participate in a relatively low risk investment with potential annual distributions.
- **The Government of Ontario has a good investment grade credit rating.** Below is a chart of the different ratings given by the major credit rating agencies.

	Long-term	Short-term
Standard & Poor's	AA- (N)	A-1+
Moody's Investors Service	Aa2	P-1
DBRS	AA (low)	R-1 (mid)

*Short-term Ratings are for debt maturities of less than one year. Ratings are graded into several categories, ranging from the highest-quality obligations to default.*

*Long-term Ratings are also assigned an outlook indicating the likely direction of an issuer's rating over the intermediate term, typically ranging from 6 months to 2 years. The outlook is denoted (P) for Positive Outlook, (N) for Negative Outlook or (D) for Developing Outlook. No identifier is attached to the rating if the outlook is Stable.*

Source: Ontario Financing Authority

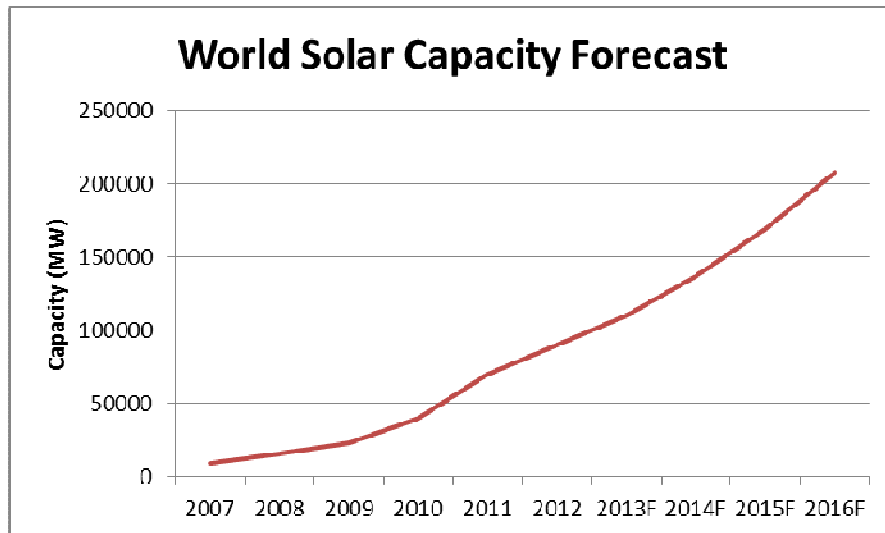
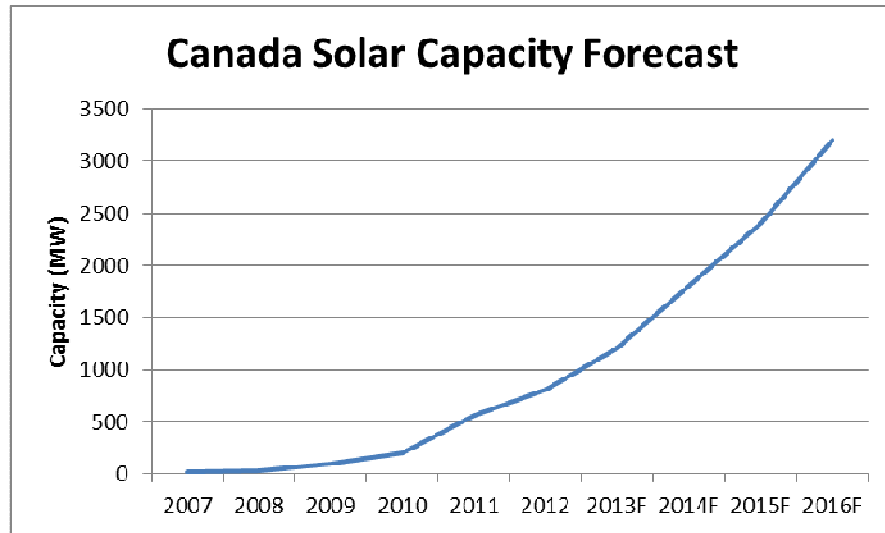
- Solar energy is a “green” investment. Solar PV sites do not pollute and require only the sun’s energy as fuel.

**Canada and the Global Solar PV Market**

As of 2011, Canada had 563 MW of solar PV capacity installed, approximately 0.008% of the world’s capacity of 69,684 MW. Germany is the world’s largest solar PV market, with 24,678 MW of installed capacity (35.41% of the world’s total capacity). Germany started a similar feed-in tariff program in 2000, which has allowed it to become the leader in solar energy production. We are expecting similar growth in Canada’s PV market as Germany experienced over the 12 years since they launched their program.

The **rate of growth in world solar capacity has been significant**, with capacity increasing

by 52% in 2009, and 73% in 2010. **Canadian solar PV capacity increased by 187% in 2009, 111% in 2010, and 182% in 2011.** The charts below illustrates the huge forecasted growth in capacity for the Global market and Canada.



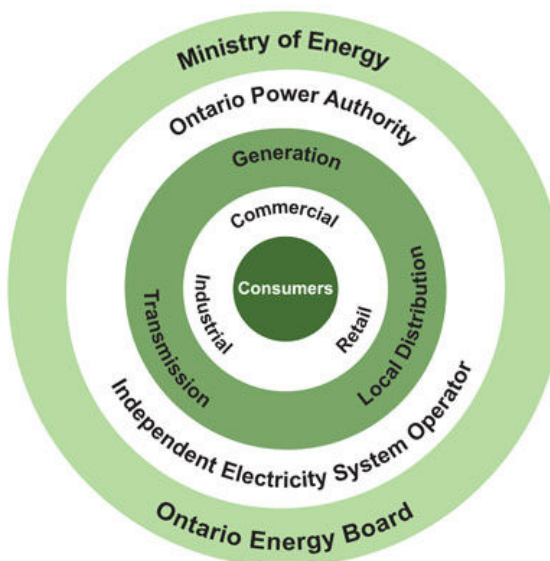
Source: European Photovoltaic Industry Association

**Ontario Power Production**

The picture below summarizes how the electricity market in Ontario works. The Ministry of Energy is responsible for setting policy direction and regulating the energy market. The Ontario Energy Board is responsible for regulating Ontario’s natural gas and electricity sectors. The Ontario Power Authority is responsible for ensuring a reliable, sustainable supply of electricity for Ontario.

The electricity produced by the Generators (such as SIF) is moved across long distances, by Transmitters (such as Hydro One), to where it is needed. The power is finally delivered to homes and businesses by the 80+ Distributors across the province.





Source: Ontario Power Authority

**Ontario Green Energy Act**

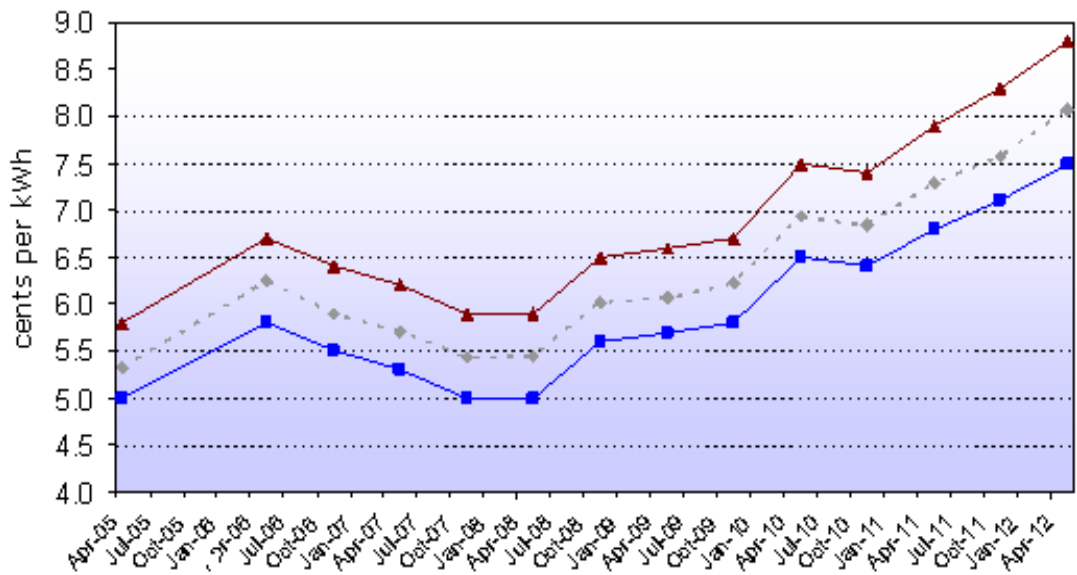
The Green Energy Act, and resulting FIT program, are integral to the corporation’s success; below we discuss its merits and possible future hurdles.

In 2009, the Ontario government passed the Green Energy Act (GEA) which is aimed at creating growth in clean and renewable energy sources in addition to creating jobs and private investment within Ontario. **In order to make renewable energy projects competitive, and profitable, the GEA implemented a FIT program which guarantees fixed contract prices for the power generated from renewable sources for 20 years.** As previously mentioned, the corporation plans to acquire, develop and operate solar energy installations with a total capacity of 5,225 kilowatts. The corporation expects to receive an average rate between 53.9 cents and 71.3 cents per kilowatt hour (kWh). Below is a schedule of the fixed prices that the Ontario government is offering developers of PV sites. As shown below, the old FIT contract prices are significantly higher than the new contract prices. As the corporation will be acquiring contracts under old pricing, it presents a significant advantage over new contract holders.

	Project Size	Old Price (¢/kWh)	New Price (¢/kWh)
Solar Rooftop	≤ 10 kW	80.2	54.9
	> 10 kW ≤ 100 kW		54.8
	≤ 250 kW	71.3	
	> 250 ≤ 500 kW	63.5	
	> 100 kW ≤ 500 kW		53.9
	> 500 kW	53.9	48.7
Solar Groundmount	≤ 10 kW	64.2	44.5
	> 10 kW ≤ 500 kW	44.3	38.8
	> 500 kW ≤ 5 MW	44.3	35
	> 5 MW	44.3	34.7

Source: Ontario Power Authority (August 10 2012)

Based on the historical electricity prices in Ontario (see chart below), we can see that there is an upward trend indicating that there is an increased demand for electricity. With Ontario’s stance on renewable energy, the increase in demand for electricity will also lead to a greater need for solar energy.



	Apr-05	May-06	Nov-06	May-07	Nov-07	May-08	Nov-08	May-09	Nov-09	May-10	Nov-10	May-11	Nov-11	May-12
- ◆ - Ave RPP Price	5.318	6.256	5.896	5.704	5.429	5.450	6.020	6.072	6.215	6.938	6.838	7.298	7.565	8.069
■ Tier 1	5.0	5.8	5.5	5.3	5.0	5.0	5.6	5.7	5.8	6.5	6.4	6.8	7.1	7.5
▲ Tier 2	5.8	6.7	6.4	6.2	5.9	5.9	6.5	6.6	6.7	7.5	7.4	7.9	8.3	8.8

**Outlook on Solar PV installations in Ontario**

Some key achievements and goals in Ontario’s Green Energy Act are detailed below (Source: Ontario.ca, FIT Program 2-year Review):

- Offered contracts for approximately 2,500 medium and large FIT projects, and over

- 11,000 micro FIT projects have connected or are expected to be connected soon.
- Created more than 20,000 jobs and is on track to create 50,000 jobs by the end of 2012.
  - Moved forward towards its goal of replacing coal fired generation by the end of 2014. Compared to 2003, Ontario has reduced its use of coal-fired power by 90%. In October 2010, the province closed four coal-fired power units, four years ahead of schedule. In total, Ontario has shut down eight of 19 coal units; the remaining units will close by the end of 2014.
  - Contracted 4,600 megawatts (MW) worth of solar energy projects through the Green Energy Act
  - Attracted over \$20 billion, along with \$7 billion from the Green Energy Investment Agreement, in private-sector investment to Ontario during the economic slowdown in the past few years.

**Although we do not believe the cancellation of contracts is a significant risk**, due to the integral role the fixed rate contracts play in this investment, we discuss this risk further below.

Green energy is more expensive than fossil fuels when just looking at the cost per kilowatt hour due to the high development costs. The feed-in tariffs that the Ontario government has guaranteed to renewable energy companies (which makes green energy economically feasible) is expected to be passed on to the citizens of Ontario through rate increases. After the enactment of the GEA in 2009, it was expected that electricity bills in Ontario would increase by 7.9% per year over a five year period and then 3.5% per year thereafter (*Source: Ontario Ministry of Energy*). The tables and data on the previous page seem to confirm this expectation. There was some concern during the 2011 election that the FIT program would be scrapped but that has not occurred. In March 2012, a 2-year review was conducted which confirmed that the program was performing as per expectations. From the 2-year review, the most important take-away is that new FIT contracts will be subject to a price reduction of approximately 20% - the price reductions are now effective as of August 10, 2012, for new contracts. **The changes in the FIT pricing, we believe, should not affect this offering or any of existing projects because the new prices will not be applied retroactively, and this offering is acquiring projects that are subject to previous FIT pricing only.**

Countries in Europe have implemented a similar program to promote renewable energy through feed-in tariffs. The Czech Republic instituted a feed-in tariff that fixed rates for 20 years. However in 2011, the government imposed a 26% retroactive tax on recently built solar plants due to higher than expected demand and related costs for the program. Spain is another example where feed-in tariffs produced an enormous amount of interest. Spain offered a subsidy program with a 25 year rate guarantee that made the country one of the world's leading solar markets in 2008. Due to the unexpected demand, and high cost to provide the subsidy, the government implemented a retroactive 30% subsidy cut on existing plants (*Source: CFA Journal, May/August 2011*). **The Czech Republic and Spain have very different economies than Canada. However, the above highlights the possibility of the potential for cancellation/amendment of agreements.** The Czech Republic and Spain now represent a very small share of the global solar power generation market. **Most**

**Countries who have similar feed-in tariff programs, and who have made changes to these programs, have only reduced the fixed rates for new contracts. Typically, the fixed rate reductions are in response to the price drop of solar equipment over the years.** In August 2010, the Ontario Power Authority stated that recent changes made to the feed-in tariff program, which now provide lower fixed rates for electricity, would not be applied retroactively.

The European Union, along with Japan, have filed disputes against Canada through the World Trade Organization stating that the GEA's requirement to have a certain percentage of renewable energy components produced in Ontario is an unfair advantage and breaches WTO agreements. We believe this will have little impact on the fixed rate contracts as the complaints are in regard to trade agreements.

We believe the feed-in tariff does not carry a significant risk of cancellation for the following reasons (*Source,: Ontario Ministry of Energy, Ontario Ministry of Finance*):

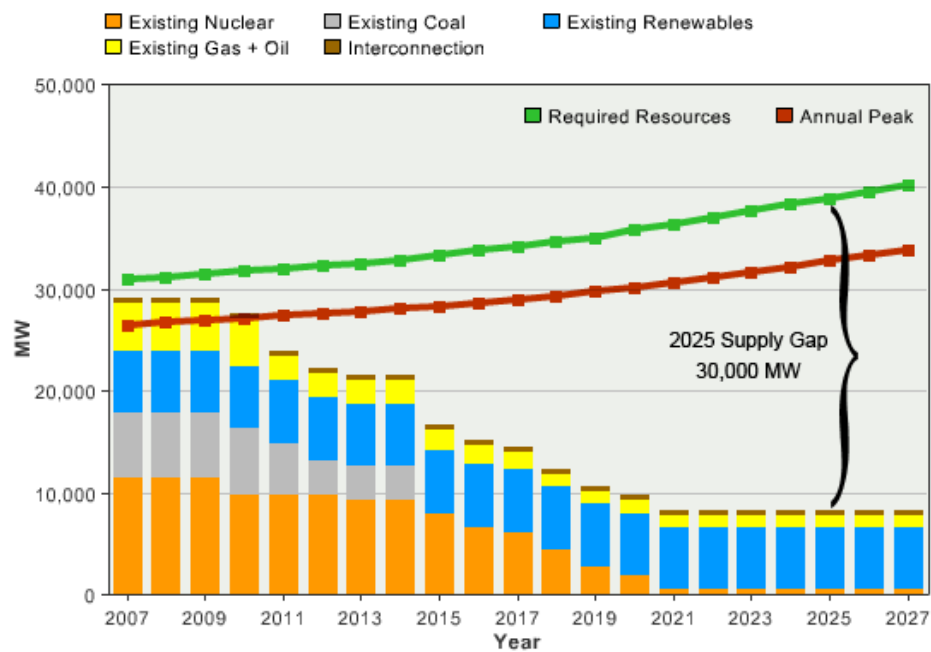
- The OPA previously had an option to terminate a FIT contract prior to the issuance of a Notice to Proceed (NTP). These rights have been waived since 2011.
- Ontario has an aging supply network and little new generation from lack of investment between 1995 and 2003. Therefore, infrastructure and power generation investments are necessary.
- Nuclear generators (which make up approximately 50% of Ontario's power supply) will need to go offline (for extended time periods) while the plants are modernized. New power generation must be in place to compensate for the shut downs.
- Tens of thousands of jobs have been created, and tens of thousands more are expected to be created from the feed-in tariff program, and the associated developments in renewable energy.
- Electrical demand is expected to grow by approximately 15% between 2010 and 2030.
- The Ontario Power Authority estimates more than 15,000 MW will need to be renewed, replaced or added by 2030. Currently, Ontario's electrical system has a capacity of approximately 35,000 MW.
- Ontario's population is projected to rise over 34.4% by 2036, an increase of over 4.5 million people.
- Ontario has approved an Ontario Clean Energy Benefit Act to help small businesses, families, and farms transition to clean energy by providing a 10% rebate off their total monthly electrical bills starting January 1, 2011, that will last until January 1, 2016.

- Ontario is committed to improving the health of Ontarians and fighting climate change through the elimination of coal-fired plants. Ontario plans to replace coal-fired plants with gas fired and renewable energy plants. An Ontario study found the health and environmental costs of coal-fired plants at \$3 billion annually.

**Solar Power Generation in Southern Ontario**

As of 2011, Ontario had 4,600MW worth of solar PV contracts and is expected to add an additional 400-800MW contracts in 2012 (ClearSky Advisors Inc. 2011). **We believe that the market size is large enough for SIF to find projects totalling 5MW in capacity.**

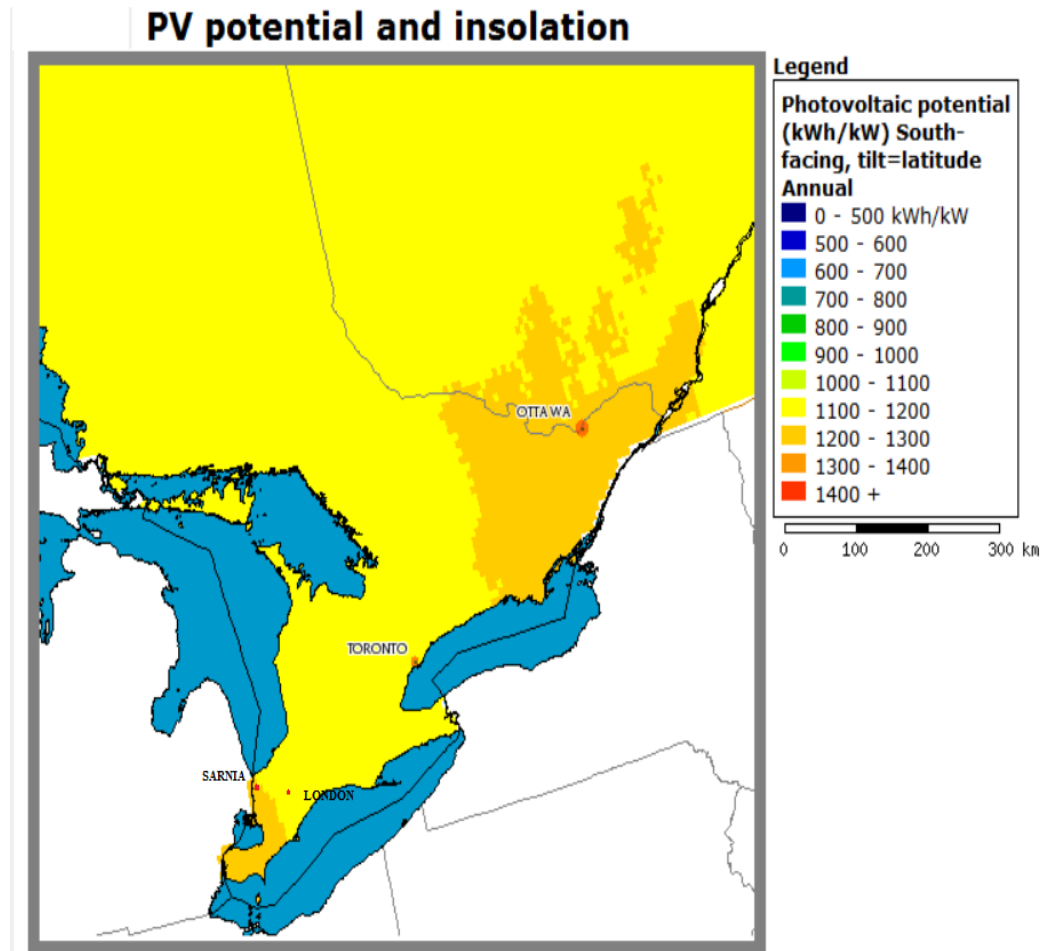
Below is a chart from the Ontario Ministry of Energy from a review of Ontario’s electricity system. From the review, the Ministry concluded that approximately 80% of existing power facilities will have to be replaced or refurbished in the next 20 years.



Source: Ontario Ministry of Energy

There are multiple players in the solar energy market in Ontario, with the two biggest being **TransCanada (TSX: TRP) and Enbridge (TSX: ENB)**. Together, these two companies have over \$1 billion in assets in solar energy contracts in Ontario. **The presence of these two conglomerates in the Ontario solar scene, we believe, is a huge vote of confidence for players such as SIF Capital.**

Below is a chart from Natural Resources Canada depicting the photovoltaic potential (kWh/kW) of Southern Ontario. **As we can see below, Southern Ontario has a potential of between 1,100–1,300 kWh/kW**, which is second only to parts of southern Alberta, Saskatchewan and Manitoba (which have a potential of 1,300-1,400 kWh/kW).



Source: Natural Resources Canada

**Project**

The management team is currently reviewing different projects for acquisition. **As this offering is essentially a blind pool (meaning that there is no specific project /area), the success of the corporation is highly dependent on the identification of viable projects.** We believe that with the management team’s previous track record, it is likely that they will be able to identify viable/attractive projects.

**Solar Installations, Equipment and Operations and Maintenance**

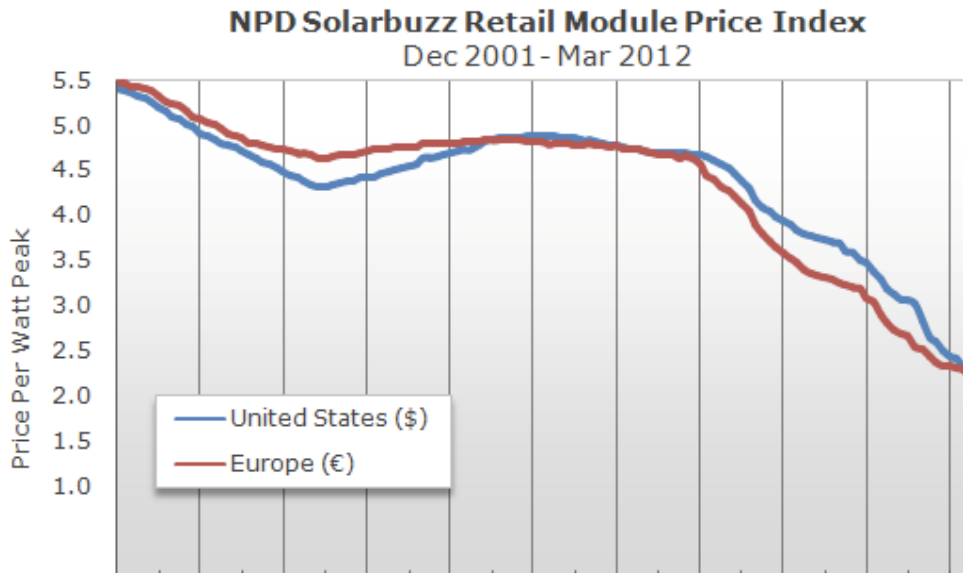
One of the key advantages of solar power installations, other than the environmental benefits, is that solar installations produce peak output during the late afternoon which is when demand for electricity is at its highest point. Ontario, along with most other jurisdictions, typically use coal and gas power plants as “peaking” units to produce electricity at times when demand is high. **Solar power, and other renewable sources, have reduced the need for coal/gas. As previously mentioned, Ontario used 94% less coal over the first 6 months of 2011, compared to the same period in 2003, with plans to eliminate coal by 2014.**

The solar installations that the corporation plans to build require **little maintenance, typically between 1-2% of annual revenues, and the manufacturers provide a 25 year warranty on the power output.** Management has also indicated they have a 10 year



warranty on the inverters, and they will set aside 1.25% of annual revenues as a reserve for replacing inverters at today's prices. As the cost of inverters are expected to decrease (discussed below), and efficiency is expected to increase, we believe management has taken a conservative approach.

**Prices for solar equipment have dropped over the years due to global economic weaknesses and increased supply.** As we can see in the charts below, the global price for modules of solar installations is trending downwards:



Source: Solarbuzz

China is offering the largest discounts for solar modules and have now captured almost 50% of global sales, and almost 60% of profits in the industry (source, Bloomberg New Energy Finance, Spiegel, PRTM management consulting).

For Ontario solar power generation companies to fully realize the benefits of the reduced prices, **Ontario will have to change the existing rules for the feed-in tariff which requires a minimum of 60% of goods and materials to be sourced locally.** However, solar power producers will still continue to **benefit from lower equipment prices as the industry is expected to show further declines in solar equipment prices.**

***Favorable Long Term Financing Agreement***

In addition to the money raised through this offering, the corporation plans to acquire a term loan in the principal amount of \$20,329,925 (assuming the company raises the maximum amount as per this offering). We have reviewed a term sheet from a reputable lending institution regarding a potential acquisition. **The loan bears interest at the higher of the yield on 10 year Canadian Government bonds plus 3.5%, or 5.4%.** The loan will be amortized over a 17 or 19 year period. As of July 26, 2012, the **spot 10-year Government of Canada Bond yield was 1.60%, which would give a 5.4% interest rate on the loan.**

With the term loan and debenture financing (assuming the company raises the maximum amount as per this offering), the corporation will have \$28,329,925 (gross) in available funds. The funds will be used to pay for equipment for the installations, prepaid rent, deposit for term loan, and installation costs. The loan will be guaranteed by the equipment, contracts, warranties, and the leasehold interest, as well as a first priority security interest in all of the corporation's assets.

The bank financing will allow the corporation to use approximately 70% leverage to finance the costs. **Through the use of leverage, the company will be able to acquire more assets in order to achieve a larger fixed stream of revenues.** The use of leverage is common with independent power producers. Most independent power producers have power purchase agreements (similar to the feed-in tariff) which allow them to acquire debt financing due to the high certainty of their cash flows. In the financial analysis section of this report, we will analyze the company's ability to service the debt as well as distributions to the debenture holders.

***Material  
Agreements***

The corporation has engaged a related party, Solar Income Fund Inc. (SIF), for the management and development of the solar installations. Details on these two agreements are described below.

*Management Agreement*

The corporation entered an agreement with SIF on May 14, 2012, in which SIF will provide management services to the corporation with respect to the acquisition, development and operation of solar installations. The corporation will pay SIF an annual fee of \$12,000.

*Development Agreement*

The corporation entered an agreement with SIF on November 14, 2011, in which SIF will provide management services to the corporation with respect to the development and operation of the solar installations. **SIF will receive a one-time fee of \$800,000 and will provide the following services:**

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*SIF shall provide or cause to be provided to the Corporation the following consulting and development services for Installations that are currently not operating:*

- *due diligence including operational, legal and financial analysis for each Installation to the point the solar project is ready for construction;*
- *determining all the costs associated with each installation;*
- *negotiating site selection with respect to each Installation;*
- *negotiating lease agreements including non-disturbance agreements and other lender agreements with respect to each installation;*
- *dealing with the Ontario Power Authority to receive a Feed-in-Tariff contract with respect to each installation;*
- *dealing with development partner(s) who bring opportunities to the Corporation or to SIF for compensation, from whom we acquire each installation or with whom we assist in developing each installation;*

- *negotiating and preparing Engineering, Procurement and Construction Agreements with respect to each installation;*
- *negotiating long-term financing together with all security documentation with respect to each installation;*
- *preparing Connection Impact Assessments with the local hydro companies;*
- *negotiating institutional pricing for the supply of all solar energy equipment with respect to each installation.*

*SIF shall provide or cause to be provided to the corporation the following consulting and development services for installations that will be acquired and are currently operating:*

- *due diligence including operational, legal and financial analysis for each Installation;*
- *negotiating the purchase agreement;*
- *continuing the existence and good standing of FIT contracts and all warranties;*
- *technical inspection of the installation by qualified technicians;*
- *confirming all leases are in good standing or if acquiring the land, ensuring we get good and marketable title;*
- *ensuring compliance with all municipal by-laws and there are no work orders outstanding;*
- *acquiring clear title to all of the solar assets.*

*Source: Offering Memorandum*

The development fee is essentially a service fee paid to SIF to develop the sites. These payments will commence once the corporation has received \$500,000 of subscriptions for debentures under this offering. The development fee will be paid on the first day of each calendar month at a rate no more than \$150,000. SIF can accelerate payment of the development fee in the event of an acquisition of an installation that is already operating and generating electricity.

**Valuation of Projects**

According to management, the valuation of the projects will be based on proposals or open bids. Valuation of projects will not be conducted regularly; however, valuations of projects will occur to support a sale. In such cases, management stated that they will hire a 3<sup>rd</sup> party to conduct the valuations.

**Deal Structure**

**Source of Funding:**

- **Debt:** Term loans amounting to approximately \$20.3 million to be obtained from a lender. The term loans will be granted on a project-by-project basis.
- **Debentures:** The corporation intends to raise \$8 million (gross) through 10.75% debentures with a maturity date on December 31, 2029. The interest on the debentures are paid at the end of the first calendar quarter in which the first installation is tied into the Ontario electrical grid, and thereafter, on March 31, June 30, September 30 and December 31 of each year. The debentures are unsecured and the corporation may redeem up to 100% of the principal amount of the debenture at any time by

providing 90 days written notice to the debenture holder and by paying all accrued interest and the principal amount of the debentures within 90 days of the notice. Management stated that debenture holders have no formal redemption option but they will try to accommodate redemptions on a best efforts basis.

- **Shares:** There are two types of shares in the corporation: Class A and Class B. Both of these shares are not available for purchase in this offering. Class A shares are non-voting shares and may participate in dividends when declared by the corporation. Class B shares are voting shares and are not entitled to participate in dividends of the corporation.

Below is a chart outlining the share structure of the company.

Ownership	Type of Security	Number Of Securities Issued	Price per Security
Solar Income Fund	Class A Shares	85,000	\$1.00
	Class B Shares	5	\$3,600
Investors	10.75% Debentures	8,000	\$1,000

As we can see from the structure above, Solar Income Fund has ownership over all outstanding shares. The full ownership of the shares by Solar Income Fund indicates that management has a strong incentive for the fund to perform greater than 10.75% (as the debenture holders have a higher claim on the assets over shareholders).

**Fees**

The following chart summarizes the fees associated with this offering. Overall, we believe the fees are reasonable.

Fees	Description
Management Fee	\$12,000 p.a. Management Fee to Solar Income Fund Inc.
Development Fee	\$800,000 development fee to Solar Income Fund Inc.
Selling Fees and Compensation	Up to 8% commission of gross proceeds for the sale of the debentures. A one time 1% fee on the gross proceeds realized on the sale to Sloane Capital Corp. for distribution services.

**Financial Analysis**

The following are the assumptions we made to construct our base-case financial model:

- We assumed that the fund will raise the full \$8 million (gross) through this offering.
- We assumed that the fund will manage projects with a total of 5,225 kW capacity.
- We used an average FIT price of 53.9¢ per kilowatt – this is on the low end considering that the FIT price will be between 53.9¢ per kilowatt and 71.3¢ per kilowatt. Our Year 1 revenue estimate is \$3,292,038 degrading at 0.50% annually; while, management’s Year 1 revenue estimate is \$3,453,860 degrading at 0.50% annually.

- We used the loan amount of \$20,329,925 with an interest rate of 5.4% amortized over 17 years.
- We used average solar radiation of 1168.93 kWh/year – this was taken from the average of 5 cities in Ontario: Sarnia, Windsor, Kingston, London and Ottawa (Source: Natural Resources Canada).
- We assumed that the projects the fund acquires will have a 20 year life for the contracts.
- The project has the potential to run for 40 years as solar panels have a 40-year life. However, we looked at the project’s cash flows for the first 20 years as the debentures mature in 17 years. Management’s goal is to sell the projects in 3-5 years, but management will only sell if they get a high enough valuation to pay down debt and debenture holders in full. Should the projects not get a high enough valuation, management will hold on to the projects. We assumed such a scenario to see if investors will be able to get their principal and interest back at maturity.
- We assumed that the corporation would not redeem the debentures early.
- The operating and maintenance fee was estimated at 2% of the FIT revenue – we confirmed this fee by reviewing documentation on previous projects that Solar Income Fund has executed.
- We assumed that the excess cash will be distributed to shareholders. As shareholders, management have total discretion on the excess cash flows, management will likely distribute these cash flows to shareholders instead of holding it within the corporation. We show the excess cash flow line in our models to show management's expected returns from this project.

The following shows our financial analysis using our base-case (a FIT rate of 53.9¢ per kilowatt):

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
FIT Revenue (0.50% annual degradation)	\$ 3,292,038	\$ 3,275,578	\$ 3,259,117	\$ 3,242,657	\$ 3,226,197	\$ 3,209,737	\$ 3,193,277
<b>Expenses</b>							
Lease	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)
Insurance, O+M, Inverter Reserve	\$ (162,331)	\$ (162,660)	\$ (163,416)	\$ (164,195)	\$ (164,996)	\$ (165,821)	\$ (166,669)
Annual Bank Loan Fees	\$ (20,000)	\$ (20,400)	\$ (20,808)	\$ (21,224)	\$ (21,649)	\$ (22,082)	\$ (22,523)
Accounting/Audit	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)
Financing Interest	\$ (1,112,636)	\$ (1,071,324)	\$ (1,027,751)	\$ (981,792)	\$ (933,319)	\$ (882,193)	\$ (828,268)
Financing Principal	\$ (754,855)	\$ (796,167)	\$ (839,741)	\$ (885,699)	\$ (934,173)	\$ (985,299)	\$ (1,039,223)
Management Fee	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)
Bank Reserve	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Net Cash Flow</b>	<b>\$ 1,111,600</b>	<b>\$ 1,094,411</b>	<b>\$ 1,076,785</b>	<b>\$ 1,059,131</b>	<b>\$ 1,041,444</b>	<b>\$ 1,023,726</b>	<b>\$ 1,005,978</b>
Debenture Payment	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)
Cash Remaining	\$ 251,600	\$ 234,411	\$ 216,785	\$ 199,131	\$ 181,444	\$ 163,726	\$ 145,978
Tax Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Excess Cash	\$ 251,600	\$ 234,411	\$ 216,785	\$ 199,131	\$ 181,444	\$ 163,726	\$ 145,978
Cash at Beginning	\$ -	\$ 251,600	\$ 486,010	\$ 702,796	\$ 901,927	\$ 1,083,371	\$ 1,247,097
Cash at End	\$ 251,600	\$ 486,010	\$ 702,796	\$ 901,927	\$ 1,083,371	\$ 1,247,097	\$ 1,393,074

	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14
FIT Revenue (0.50% annual degradation)	\$ 3,176,816	\$ 3,160,356	\$ 3,143,896	\$ 3,127,436	\$ 3,110,976	\$ 3,094,515	\$ 3,078,055
<b>Expenses</b>							
Lease	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)
Insurance, O+M, Inverter Reserve	\$ (167,541)	\$ (168,438)	\$ (169,359)	\$ (132,153)	\$ (132,742)	\$ (133,354)	\$ (133,989)
Annual Bank Loan Fees	\$ (22,974)	\$ (23,433)	\$ (23,902)	\$ (24,380)	\$ (24,867)	\$ (25,365)	\$ (25,872)
Accounting/Audit	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)
Financing Interest	\$ (771,393)	\$ (771,404)	\$ (648,133)	\$ (581,398)	\$ (511,012)	\$ (436,773)	\$ (358,471)
Financing Principal	\$ (1,096,099)	\$ (1,156,087)	\$ (1,219,359)	\$ (1,286,093)	\$ (1,356,480)	\$ (1,430,719)	\$ (1,509,020)
Management Fee	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)
Bank Reserve	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Net Cash Flow</b>	<b>\$ 988,193</b>	<b>\$ 910,378</b>	<b>\$ 952,527</b>	<b>\$ 972,796</b>	<b>\$ 955,259</b>	<b>\$ 937,688</b>	<b>\$ 920,087</b>
Debtenture Payment	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ (860,000)
Cash Remaining	\$ 128,193	\$ 50,378	\$ 92,527	\$ 112,796	\$ 95,259	\$ 77,688	\$ 60,087
Tax Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Excess Cash	\$ 128,193	\$ 50,378	\$ 92,527	\$ 112,796	\$ 95,259	\$ 77,688	\$ 60,087
Cash at Beginning	\$ 1,393,074	\$ 1,521,268	\$ 1,571,646	\$ 1,664,173	\$ 1,776,969	\$ 1,872,227	\$ 1,949,916
Cash at End	\$ 1,521,268	\$ 1,571,646	\$ 1,664,173	\$ 1,776,969	\$ 1,872,227	\$ 1,949,916	\$ 2,010,003

	Year 15	Year 16	Year 17	Year 18	Year 19	Year 20
FIT Revenue (0.50% annual degradation)	\$ 3,061,595	\$ 3,045,135	\$ 3,028,675	\$ 3,012,215	\$ 2,995,754	\$ 2,979,294
<b>Expenses</b>						
Lease	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)	\$ (103,616)
Insurance, O+M, Inverter Reserve	\$ (134,646)	\$ (135,327)	\$ (136,031)	\$ (135,759)	\$ (137,512)	\$ (138,290)
Annual Bank Loan Fees	\$ (26,390)	\$ (26,917)	\$ (27,456)	\$ -	\$ -	\$ -
Accounting/Audit	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)	\$ (15,000)
Financing Interest	\$ (275,884)	\$ (188,777)	\$ (96,903)	\$ -	\$ -	\$ -
Financing Principal	\$ (1,591,607)	\$ (1,678,715)	\$ (1,770,589)	\$ -	\$ -	\$ -
Management Fee	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)	\$ (12,000)
Bank Reserve	\$ -	\$ -	\$ 700,000	\$ -	\$ -	\$ -
<b>Net Cash Flow</b>	<b>\$ 902,452</b>	<b>\$ 884,783</b>	<b>\$ 1,567,080</b>	<b>\$ 2,745,840</b>	<b>\$ 2,727,626</b>	<b>\$ 2,710,388</b>
Debtenture Payment	\$ (860,000)	\$ (860,000)	\$ (860,000)	\$ -	\$ -	\$ -
Cash Remaining	\$ 42,452	\$ 24,783	\$ 707,080	\$ 2,745,840	\$ 2,727,626	\$ 2,710,388
Tax Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Excess Cash	\$ 42,452	\$ 24,783	\$ 707,080	\$ 2,745,840	\$ 2,727,626	\$ 2,710,388
Cash at Beginning	\$ 2,010,003	\$ 2,052,455	\$ 2,077,238	\$ 2,784,318	\$ 5,530,157	\$ 8,257,783
Cash at End	\$ 2,052,455	\$ 2,077,238	\$ 2,784,318	\$ 5,530,157	\$ 8,257,783	\$ 10,968,172

As can be seen above, using the above assumptions, the corporation should be able to pay the 10.75% interest owed to debenture holders during the 17 years; however, it will not have enough cash to pay the \$8 million in principal at maturity. Solar panels have a useful life of approximately 40 years, so the company may still be able to sell energy after the FIT contract expires at the spot rate at that time – using this information, and seeing that the company will have no other debt obligations after year 17, we can assume that the corporation can take on additional debt. Our research indicates that the solar industry has similar characteristics to the utility industry. The average total debt to EBITDA ratio of the utility industry is 6.6x (Source: Capital IQ). Using the base-case scenario assumptions, we calculated that the corporation can take on maximum debt of approximately up to \$18 million (using total debt to EBITDA of 6.6x) in year 17 to pay off debenture holders' principal and cumulative interest. The debt servicing fee (interest and financing), assuming the corporation takes on \$8 million in debt, will be approximately \$1.03 million a year (5.4% interest rate



and a 10 year amortization). Our operating cash flows estimate for Year 18 is \$2.75 million; therefore, our models indicate the company will be able to easily service the \$8 million debt.

**Using this information, we can conclude that it is likely that the corporation will refinance in order to pay back the principal and cumulative interest of debenture holders should it hold the project.**

*Breakeven Point*

As the interest payments are cumulative, we have conducted an analysis to determine what is the minimum capacity the corporation needs to achieve in order to be able to pay back the cumulative interest and principal to debenture holders in year 17 (using the assumptions in the base-case scenario). Using the utility industry’s total debt to EBITDA ratio of 6.6x, we determined that the breakeven point is reached when the project’s total capacity is 4,310kW. As mentioned earlier, we believe management will have to negotiate for the best possible valuations to acquire total capacity of 5,225 kW with \$26 million. This break-even analysis shows that they cannot go below 4,310 kW.

*FIT Prices Decreasing*

From the new rules effective August 10, 2012, the FIT price for the 53.9¢ per kW rate was reduced by 9.6% to 48.7¢ per kW.

We built a financial model in order to determine whether or not a FIT rate of 48.7¢ per kW will still be feasible for the corporation. From our analysis, we determined that debenture holders will not receive the full interest payments every year until Year 17 (maturity date). However, we believe the corporation will be able to take on debt of up to \$16.2 million at year 17 – which will enable it to pay off all the cumulative interest and principal for debenture holders at year 17. Note that the IRR in this case will be slightly lower than 10.75% p.a. as investors do not receive the full interest payments every year.

From our research, we believe it is unlikely that the rates will be retroactive on existing FIT contracts. However, our analysis indicates that even if the prices are retroactive (based on the new rules), the debenture holders will be able to receive their cumulative interest and principal should the company hold on to the project.

***Rating***

**Therefore, based on our review of the offering and our projections, we assign a Rating of 2- (on a scale of 1 to 7) on the debentures issued by SIF Capital.**

<b>FRC Rating</b>	
Base-Case Return (IRR)	10.75%
<b>Rating</b>	<b>2- (Very Good)</b>
Risk	3 (Average)

***Risks***

We assign a risk rating of 3 (Average) on the debentures. The following points highlights the

primary risks associated with this offering:

- Competition for available solar projects under the old FIT rates may result in delays in the execution of the business plan.
- There is political risk that the new feed-in tariff rates may be applied retroactively, thus, reducing the business' revenues. We believe that this is not a significant risk since the Ontario Power Authority recently reduced the rates on new contracts, and has stated the latest reduction was not retroactive. Our models indicate that even if the rates are reduced as per the new rules, the company will still be able to pay principal/interest to debenture holders.
- Integration companies do not always deliver projects on time or on budget, which may affect revenues and cash flows.
- This is a blind pool - management has sole discretion on which projects to invest in.
- Timely deployment of cash to acquire projects.
- The investment horizon is at the discretion of the management team as – a) the corporation has the ability to redeem debentures early, and b) debenture holders have no formal redemption option.
- Our base case models indicate that project refinancing may be required when the debentures mature at Year 17, should the company hold on to the project. This is a minor risk as our models indicate that refinancing might not be difficult based on the expected operating cash flows and fundamentals beyond year 17.
- Interest rate risk

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- Rating – 1: Excellent Return to Risk Ratio
- Rating – 2: Very Good Return to Risk Ratio
- Rating – 3: Good Return to Risk Ratio
- Rating – 4: Average Return to Risk Ratio
- Rating – 5: Weak Return to Risk Ratio
- Rating – 6: Very Weak Return to Risk Ratio
- Rating – 7: Poor Return to Risk Ratio

A “+” indicates the rating is in the top third of the category, A “-“ indicates the lower third and no “+” or “-“ indicates the middle third of the category.

**Fundamental Research Corp. Risk Rating Scale:**

- 1 (Low Risk)
- 2 (Below Average Risk)
- 3 (Average Risk)
- 4 (Speculative)
- 5 (Highly Speculative)

FRC Distribution of Ratings			
Rating - 1	-	Risk - 1	-
Rating - 2	36%	Risk - 2	-
Rating - 3	50%	Risk - 3	50%
Rating - 4	5%	Risk - 4	50%
Rating - 5	9%	Risk - 5	-
Rating - 6	-		
Rating - 7	-		

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