RUSSELL BREWERIES INC.
Management Discussion and Analysis
For the year ended June 30, 2012

This Management's Discussion and Analysis ("MD&A") of Russell Breweries Inc. dated October 29, 2012 provides an analysis of Russell's results of operation and financial condition for the year ended June 30, 2012. This MD&A should be read in conjunction with the audited consolidated financial statements and notes for the years ended June 30, 2012 and 2011. Additional information related to Russell Breweries Inc. is available on SEDAR at www.sedar.com and on the Company's website at www.russellbeer.com.

The financial statements and related notes of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS"). All financial amounts in this MD&A are in Canadian dollars, except as otherwise indicated.

FORWARD LOOKING STATEMENTS

This report contains forward-looking information that is based on the Company's plans, intentions and expectations. By definition, forward-looking information involves risks, uncertainties and assumptions and is not a guarantee of future performance. Actual results could differ significantly from those anticipated, and hence investors should use caution when considering this information and not to put undue reliance on forward-looking statements.

BASIS OF PRESENTATION AND TRANSITION TO IFRS

On July 1, 2011, the Company adopted International Financial Reporting Standards ("IFRS") for Canadian publicly accountable enterprises. Prior to the adoption of IFRS, the Company followed Canadian Generally Accepted Accounting Principles ("CGAAP"). While IFRS has many similarities to CGAAP, some of the Company's accounting policies have changed as a result of its transition to IFRS. The most significant accounting policy changes that have had an impact on the results of operations are discussed within the applicable sections of this MD&A, and in more detail in the Accounting Changes section of this MD&A.

OVERVIEW

Through its wholly-owned subsidiaries, Russell Brewing Company Ltd. located in Surrey, BC, and Fort Garry Brewing Company Ltd. located in Winnipeg, Manitoba, Russell Breweries Inc. ("the Company") operates two craft breweries producing premium quality beers for pubs, restaurants and liquor stores. The Company acquired Fort Garry Brewing Company Ltd. ("Fort Garry") on October 22, 2007. Fort Garry is Manitoba's largest brewer and distributor of premium quality beers. The Company's operations include production facilities in Surrey, BC and Winnipeg, Manitoba, corporate offices in Surrey, BC, storage facilities, brewing equipment, and delivery and sales vehicles. The breweries main product lines are Russell Cream Ale, Russell Pale Ale, Russell Honey Blonde Ale, Russell Extra Special Lager, Russell IP'EH!, Russell A Wee Angry Scotch Ale, Russell Blood Alley Bitter, Russell Lemon Ale, Russell Lime Lager, Rocky Mountain Pilsner, Fort Garry Dark Ale, Fort Garry Pale Ale, Fort Garry Premium Light, Fort Garry Red and Stone Cold Lager.

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BUSINESS DEVELOPMENTS AND SIGNIFICANT EVENTS

On November 4, 2011, the Company's wholly owned subsidiary Russell Brewing Company Ltd. was recognized with a 'Best Business Award' at the Surrey Board of Trade 13th Annual Surrey Business Excellence Awards.

On November 22, 2011, the Company announced financings of $500,000 in the form of equity units consisting of common shares and warrants to purchase common shares of the Company. On January 20, 2012, the Company completed the financing with gross proceeds totaling $765,000 – see Liquidity and Capital Resources: Financing.

On December 5, 2011, the Company and Storm Brewing, two of British Columbia's independent Craft Brewers, join together to release a new collaborative beer called The Big Smoke. This strong, smoky ale was jointly brewed by Storm Brewing and Russell Brewing using 10% Peat Smoked Malt and Bravo and Willamette Hops. This is a malt-forward beer with a big smoke aroma and a well-balanced hop finish. Limited edition, single-batch brew available in 650ml bottles through private liquor stores in BC. This beer is part of the new Collaboration Series which is a succession of small-batch brews created by independent brewers working together to create new beers that push the boundaries of taste.

On March 2, 2012, the Company released its new super-premium, single-batch beer - Nectar of the Gods Wheat Wine Ale. The entire batch was pre-sold and is currently available in select private retailers in Metro Vancouver. Nectar of the Gods Wheat Wine Ale is the first barrel-aged beer from the Company. The beer was carefully aged in Tennessee Whiskey barrels for over four months. The aging process provided the beer with layers of flavour complexity including a fruity-ester character and vanilla-like flavours and tannins.

On March 9, 2012, the Company granted incentive stock options to its employees, consultants, directors and officers on 3,000,000 common shares in its capital, exercisable for up to five years at a price of $0.10 per share. The options shall vest in accordance with the Company's stock option plan. The Company did not proceed with the 2,500,000 stock options announced on March 21, 2010.

On March 29, 2012**,** the Company host the production of the 2012 Vancouver Craft Beer Week (VCBW) Collaboration Ale at its facility in Surrey, BC. In celebration of BC's largest craft beer festival, thirty of BC's finest breweries banded together to create a unique Cascadian Brown Ale.

On April 2, 2012, the Company issued 125,000 common shares in its capital as bonus shares to each of its two directors who provided personal guaranties for a $100,000 working capital loan from the Business Development Bank of Canada.

On April 4, 2012, Fort Garry Brewing Company Ltd., a wholly owned subsidiary of the Company, introduced a new specialty beer to the Manitoba market called Fort Garry Kona Imperial Stout. This is the newest beer from the super-premium Fort Garry Brewmaster Series which is a group of small-batch, limited-edition beers brewed for craft beer enthusiasts. Fort Garry - Kona Imperial Stout is now available in limited supply in single-serve 650ml bottles at the stores of Manitoba Liquor Control Commission (MLCC).

On May 8, 2012, the Company won a silver medal at the prestigious World Beer Cup 2012 for its Russell IP'eh! India Pale Ale. This is the second time this beer has been honoured with a medal at the World Beer Cup – in 2010 it won bronze.

On May 24, 2012, the Company released the Rick August Russian Imperial Stout, Grand Prize Winner of the 2011 Golden Stag Home Brewing Contest.

On June 13, 2012, the Company won a silver medal for Nectar of the Gods Wheat Wine Ale at the Canadian Brewing Awards in Montreal on Saturday June, 2012 in the Wood and Barrel Aged Strong Beer category.Nectar of the Gods Wheat Wine Ale is the Company's first barrel-aged beer. Fort Garry Brewing Company, a wholly owned subsidiary of the Company, was also awarded a silver medal at the Canadian Brewing Awards for their Kona Imperial Stout as part of their new Brewmaster Series.

BUSINESS DEVELOPMENTS AND SIGNIFICANT EVENTS (continued)

On July 13, 2012, the Company announced that it agreed to terms under a letter of intent for the initial non-exclusive rights to import, produce, package, use, market, sell and distribute Russell brands and branded merchandise with FVI Capital Inc. (“FVI”) in China. The letter specifies the principal terms of a technology and trade mark license agreement (“Agreement”) which includes an initial up-front licensing fee, to be paid by a new Company (“Licensee”) being established by FVI to hold the license and ongoing royalties based on volume of beer produced up to 50,000 hectolitres . The Company will take an initial 20% equity position in Licensee. As part of the agreement, the new Company has a 48 month first matching option to acquire an exclusive license for the entire Chinese market for an additional license fee payment and ongoing per hectoliter royalty payments and the Company has an option to increase its stake in the Licensee to 25% at Fair Market Value within the same 48 month term.

On July 27, 2012, the Company announced that it agreed to a one year extension (the “Extension”) and amendment to a loan agreement (the “Loan Agreement”) dated December 31, 2007, pursuant to which the lender (“Lender”), a shareholder of Russell, had provided to the Company a loan (the “Loan”) valued at maturity in the amount of $1,239,000. (see LIQUIDITY AND CAPITAL RESOURCES)

On October 9, 2012, the Company completed a non-exclusive technology and trade mark license agreement (“Agreement”) with Russell Breweries (China) Inc. to import, produce, package, use, market, sell and distribute Russell brands in China, including Hong Kong and Taiwan. The principal terms of the Agreement includes use of name for the new company, an initial up-front licensing fee and ongoing royalties based on volume of beer produced and sold. In addition, the Company will subscribe for a 20% equity position in Licensee with an option to increase its position to 25%.

Currently, the Company’s products are segmented into the following categories:

Categories	Brands
Super Premium	Russell Nectar of the Gods Wheat Wine Ale, Fort Garry Kona Imperial Stout
Premium:	Russell IP’EH!, Black Death Porter, Russell Marzen, A Wee Angry Scotch Ale, Blood Alley Bitter, Fort Garry Munich Eisbock
Session:	Russell Cream Ale, Russell Pale Ale, Russell Honey Blonde Ale, Russell Extra Special Lager, Fort Garry Dark, Fort Garry Pale, Fort Garry Rouge, Fort Garry Light, Citrus Twist, Craft Collection
Value:	Rocky Mountain Pilsner, Stone Cold Lager, Two Rivers
Seasonal:	Russell Lemon Ale, Russell Lime Lager
Partnership:	Chambar Ale, Main Street Pilsner, GUUU Ale, Bayside Shark Lager, Cactus Double Down Draught, The Big Smoke

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SELECTED INFORMATION

The following table summarizes certain financial information of the Company for the years indicated below:

Selected Information	IFRS		Canadian GAAP
	Year Ended 30-June-12	Year Ended 30-June-11	Year Ended 30-June-10
	$	$	$
Statement of Comprehensive Loss Data			
Gross Revenue[(1)]	8,416,964	7,757,308	8,224,740
Net Sales (after excise tax and provincial mark-up)	6,477,995	5,873,872	6,206,354
Earnings (loss) before interest and other income, taxes, depreciation and amortization	32,970	(703,483)	(746,156)
Total income (loss) from continuing operations[(2)(3)]	(788,166)	(1,521,511)	(1,365,064)
Operating income (loss) per share	(0.01)	(0.04)	(0.04)
Net income (loss) [(2)(3)]	(1,109,166)	(1,521,511)	(1,365,064)
Basic and diluted earnings (loss) per share	(0.02)	(0.04)	(0.04)
Statement of Financial Position Data			
Total assets[(4)]	6,978,917	7,626,514	8,184,462
Total long term financial liabilities	243,559	1,576,724	441,592
Cash dividends declared per share	Nil	Nil	Nil

1) In transitioning to IFRS, the Company has reclassified its other income to revenues as such income is part of the Company's normal course of business. The impact of the reclassification adjustment is described in the June 30, 2012 financial statement note 23(e).

2) Under pre-changeover Canadian GAAP, the Company included promotional and marketing materials to be used in the normal course of business with inventory. Under IFRS, these are considered a selling expense at the time the materials are purchased and received. The impact of the adjustment is described in the June 30, 2012 financial statement note 23(a).

3) As a consequence of the application of the componentization rules to certain property, plant and equipment assets, the accumulated impact to depreciation as determined under IAS 16, Property, Plant and Equipment ("IAS 16"), resulted in a cost recovery of property, plant and equipment assets and increase in equity. The impact of the adjustment is described in the June 30, 2012 financial statement note 23(c).

4) In transitioning to IFRS, the Company has reclassified its returnable containers from inventory to property, plant and equipment as their use covers more than one year. The impact of the reclassification adjustment is described in the June 30, 2012 financial statement note 23(b).

PERFORMANCE AND RESULTS OF OPERATIONS

Three Months Ended June 30, 2012 ("Q4 2012F")

The Company had a net loss of $498,442 for Q4 2012F compared to the net loss of $614,672 for the period ended June 30, 2011 ("Q4 2011F"). The decrease in net loss is primarily a result of $284,145 increase in gross margin, $108,739 decrease in selling, general and administrative expenses, and $54,537 decrease in other expenses which is offset by deferred income tax expense of $321,000.

Gross sales for Q4 2012F were $2,352,848 up $304,838 or 15% compared to $2,048,010 for Q4 2011F. Net Sales for Q4 2012F were $1,812,981 up $443,956 or 32% compared to $1,369,025 for Q4 2011F. The sales volumes for Q4 2012F has kept at the 7,200 hectolitres level compared to Q4 2011F. Sales volume in premium and super premium, and value brands increased 77%, and 7% respectively, which were offset by 14% decrease in session brands. The increase in the sales volumes of the Company's premium and super premium brands were key drivers for the increase in gross and net revenue, which reflects the Company's recent marketing strategy with a focus on premium brands.

The gross margin for Q4 2012F increased $284,145 or 42% to $963,601 compared to $679,456 for Q4 2011F. The gross margin percentage of Q4 2012F was up 3% to 53% compared to 50% for Q4 2011F. The increase in gross margin is primarily a result of the continued sales growth in higher margin premium and super premium brands.

Selling, general and administration expenses for Q4 2012F were $1,255,263 down $108,739 or 9% compared to $1,364,002 for the comparable period ended June 30, 2011 ("Q4 2011F"). Certain categories showed a continued cost reduction as various improvements and operating efficiencies have been implemented since Q1 2011F. The major cost reductions are advertising and promotion (decrease of $65,955 to $419,382 from $485,337), management fees (decrease of $66,952 to $72,500 from $139,452), director fees (decrease $74,000 to $9,000 from $83,000), automotive (decrease $8,707 to $38,600 from $47,307), telephone (decrease of $8,330 to $12,336 from $20,666), office expense (decrease of $9,072 to $24,140 from $33,212), and smallware (decrease $13,476 to $nil from $13,476). In addition, rent and utilities increased $12,300 to $154,138 from $141,838, labour increased $31,538 to $259,263 from $227,725, professional fees increased $2,935 to $93,958 from $91,023, bad debts increased $14,446 to $14,446 from $nil, and repairs and maintenance increased $11,411 to $23,829 from $12,418. The increase in rent and utilities and labour is a result of expansion of production since the Company implemented a new bottle filling and labeling system in April 2011 and obtained additional lease of 3,700 square feet space for storage at a cost of $3,500 per month in August 2011. The Company also included $53,959 (Q4 2011F: $14,246) share based compensation in selling, general and administration expenses,

Other expenses for Q4 2012F were down $54,537 to $92,271 compared to $146,808 for Q4 2011F. The decrease is primarily a result of $27,633 decrease in accretion of convertible debentures and $24,715 decrease in other expense for financing placement fee securing a demand loan.

PERFORMANCE AND RESULTS OF OPERATIONS (continued)

Year Ended June 30, 2012 ("2012F YTD")

The Company had a net loss of $1,109,166 for 2012F YTD compared to the net loss of $1,521,511 for the year ended June 30, 2011 ("2011F YTD"), a decrease of $412,345. The decrease in net loss is primarily a result of $644,255 increase in gross margin and $102,760 decrease in selling, general and administrative expenses which is offset by an increase of $3,263 in other expenses and by deferred income tax expense of $321,000.

Gross sales for 2012F YTD were $8,416,964 up $659,656 or 8.5% compared to $7,757,308 for 2011F YTD. Net Sales for 2012F YTD were $6,477,995 up $604,123 or 10% compared to $5,873,872 for the year ended June 30, 2011 ("2011F YTD"). For 2012F YTD, the Company's overall sales volume was approximately 26,000 hectolitres compared to 25,000 hectolitres for fiscal 2011. Sales volume in premium and super premium, and value brands increased 105%, and 11% respectively, representing approximately incremental sales of $700,000 in premium and super premium brands and $400,000 in value brands, which were offset by $500,000, or 14% decrease in session brands. The increase in the sales volumes of the Company's premium and super premium brands were key drivers for the increase in gross and net revenue, which reflects the Company's recent marketing strategy with a focus on premium brands.

The gross margin for 2012F YTD increased $644,255 or 23% to $3,423,420 compared to $2,779,165 for 2011F YTD. The gross margin percentage of 2012F YTD was up 6% to 53% compared to 47% for 2011F YTD. The increase in gross margin is primarily a result of the continued sales growth in higher margin premium and super premium brands.

Selling, general and administration expenses for 2012F YTD decreased $102,760 to $3,711,816 from $3,814,576 of 2011F YTD. Certain categories showed a continued cost reduction as various improvements and operating efficiencies have been implemented since Q1 2011F. The major cost reductions are advertising and promotion (decrease of $295,729 to $740,306 from $1,036,035), telephone (decrease of $28,405 to $62,284 from $90,689), insurance (decrease of $8,857 to $33,323 from $42,180), director fees (decrease $50,000 to $33,000 from $83,000), automotive (decrease of $6,395 to $168,402 from $174,797), smallware (decrease of $16,999 to $nil from $16,999), office expense (decrease of $9,313 to $138,971 from $148,284) and shop supplies (decrease of $4,709 to $38,957 from $43,666). In addition, management fees increased $31,940 to $290,000 from $258,060, rent and utilities increased $60,717 to $614,425 from $553,708, professional fees increased $39,954 to $309,186 from $269,232, labor increased $80,259 to $907,182 to $826,923, bank charge increased $10,040 to $98,128 from $88,088, bad debts increased $14,446 to $14,446 from $nil, and travel increased $13,301 to $71,473 from $58,172. The increase in management fees and professional fees is a result of renewing management contracts in January 2011 for the Company's CEO, COO and CFO which reflects more workload involved in financing, marketing and financial planning. The increase in rent and utilities and labor is a result of expansion of production since the Company implemented a new bottle filling and labeling system in April 2011 and obtained additional lease of 3,700 square feet space for storage at a cost of $3,500 per month in August 2011. The increase in travel expense is a result of more traveling to the Company's Winnipeg subsidiary which reflects more involvement from the head office in the production and marketing activities of the subsidiary. The Company also included $82,844 (2011F YTD: $54,246) share based compensation in selling, general and administration expenses,

Other expenses for 2012F YTD were up $3,263 to $361,098 compared to $357,835 for 2011F YTD. The increase is primarily a result of $75,601 additional interest recognized on the convertible debentures issued in connection with the private placement closed in December 2010. This increase was partially offset by a $40,223 decrease in interest paid on demand loan, $8,448 decrease in interest paid on finance lease obligations, and $24,965 decrease in other expenses for financing placement fee securing a demand loan.

PERFORMANCE AND RESULTS OF OPERATIONS (continued)

Summary of Quarterly Results

The following is selected financial information from the Company's eight most recently completed fiscal quarters:

	IFRS							
Fiscal Year Quarter	**2012F Q4**	**2012F Q3**	**2012F Q2**	**2012F Q1**	**2011F Q4**	**2011F Q3**	**2011F Q2**	**2011F Q1**
					Restated	Restated	Restated	Restated
	$	$	$	$	$	$	$	$
Net revenues	1,812,981	1,534,355	1,474,424	1,656,235	1,369,025	1,495,918	1,419,581	1,591,316
SG&A(1)	1,255,263	860,238	841,377	754,938	1,364,002	763,743	936,085	752,714
EBITDA(2)	29,704	(25,459)	(88,925)	117,650	(352,618)	(139,666)	(357,389)	146,190
Net income (loss)	(498,442)	(241,403)	(286,193)	(83,128)	(614,672)	(306,261)	(553,803)	(46,775)
Net earnings (loss) per share	(0.01)	(0.00)	(0.00)	(0.00)	(0.01)	(0.01)	(0.01)	(0.01)

(1) SG&A represents Selling, General and Administrative expenses.

(2) EBITDA represents earnings before interest, income taxes, depreciation and amortization. EBITDA is a non-IFRS earnings measure, therefore it does not have any standardized meaning prescribed by International Financial Reporting Standards and may not be similar to measures presented by other companies. Management uses this measurement to evaluate the operating results of the Company.

The Company has historically experienced a seasonal pattern in its operating results, with the second and third quarters historically exhibiting lower revenues. Q4 2012F net sales were $1,812,981 up $278,626 compared to the net sales of $1,534,355 for Q3 2012F. Q4 2012F net loss were $177,442 down $63,961 compared to the net loss of $241,403 for Q3 2012F. The increase in net sales and decrease in net loss is due to seasonality. The results in any one quarter are not indicative of results in any other quarter, or for the year as a whole.

Other significant impacts on quarterly expense trends may be share-based compensation expense which is included in selling, general and administrative expenses as follows: Q4 2012F $53,959, Q3 2012F $28,885; Q2 2012F $nil, Q1 2012F $nil, Q4 2011F $14,246, Q3 2011F $nil, Q2 2011F $40,000, and Q1 2011F $nil.

LIQUIDITY AND CAPITAL RESOURCES

Financial Condition

At June 30, 2012, the Company had a net working capital deficit of $1,623,456. The Company has $29,199 of cash and $100,000 of restricted cash securing $100,000 of bank indebtedness. Liabilities include $1,442,437 of accounts payable and accrued liabilities, $18,519 of interest payable on convertible debentures, $1,071,719 of long-term debts, $668,841 of convertible debentures and $61,122 of finance lease obligations. The Company has declared $163,200 dividends to its subsidiary's exchangeable preferred shareholders. The Company has not paid any dividends to its common share holders.

The Company has an operating line of credit, four finance leases, six operating leases, two term loans, one discount loan, and three convertible debentures. As at June 30, 2012 and the date of this MD&A, the Company is in compliance with all of these covenants.

Funds on hand are low due to seasonality, continued losses from operations and need for additional financing. The Company will need additional capital to fund its short term operating losses and planned non-discretionary capital expenditures for the next twelve months. The Company is seeking additional cash in the equity and/or debt markets. There is no guarantee that the Company will be able to raise additional equity or debt financing on favorable terms if at all or generate cash flow from operations in the future.

LIQUIDITY AND CAPITAL RESOURCES (continued)

Cash Flow

Year Ended June 30, 2012 ("2012F YTD")

Net cash used in operating activities in 2012F YTD was $361,656 compared to $621,099 cash used in 2011F YTD, a decrease in use of $259,443 due to $811,322 decrease in net loss after adjusting for items not affecting cash, and $184,450 more cash collected from accounts receivable, which was offset by $624,548 more cash used in paying accounts payable and accrued liabilities, $20,452 more cash used in inventory, and $84,001 less cash provided by related parties.

Cash used in 2012F YTD for investing activities was $36,117 for purchasing equipment compared to $38,259 used in purchasing equipments, $1,615 used for acquiring intangible assets, and 100,000 cash provided by the redemption from restricted term deposits in 2011F YTD.

During 2012F YTD, the Company received $100,000 cash from a demand loan and $715,891 from share subscription, repaid $109,082 of bank indebtedness, $100,000 demand loan, $138,000 of long-term debts, and $52,419 of finance lease obligations, paid $18,519 interest on convertible debentures compared to receipts of $805,934 from share subscriptions, and $666,675 from issuance of convertible debentures, $100,000 from issuance of long-term debt, and $250,000 from demand loan, and repayments of $775,750 for long-term debts, $132,678 for finance lease obligations, and $375,000 for demand loan in 2011F YTD.

Outstanding Share Data

As at June 30, 2012, the Company had 62,230,562 common shares issued and outstanding. In addition, the Company had the following outstanding share data at the date of this MD&A:

Outstanding Share Data	Number of Common Shares	Exercise Price per Common Share	Expiry Dates
Issued and outstanding as at October 29, 2012	62,230,562	N/A	N/A
Stock options	3,937,500	$0.10	June 19, 2013 – March 9, 2017
Conversion of preferred shares[(1)]	1,405,560	$0.60	March 31, 2013
Penalty on preferred shares allotted but unissued[(1)]	68,000	N/A	N/A
Conversion of convertible debenture[(2)]	4,938,333	$0.15	November 4 – December 23, 2012
Warrants	28,030,000	$0.10 - $0.15	November 4, 2012 – January 20, 2013
Agent unit warrants	2,120,200	$0.08	November 4 – December 23, 2012
Agent warrants	2,120,200	$0.15	Two years from issuance of the Unit
Fully Diluted as at October 29, 2012	104,850,355	N/A	N/A

(1) After five years (the "Exchange Date") the 68,000 preferred shares will automatically be exchanged into 16.67 common shares of the Company or earlier if certain events occur, including a change in control of the Company or an insolvency event in Russell. Russell will incur a penalty if it has not paid all cumulative dividends due and payable as of March 31, 2011 and for any unpaid dividends calculated each six months thereafter until the Exchange Date. The maximum penalty would result in one additional common share of the Company being exchanged for each Exchangeable Share. At the Exchange Date, the exchange ratio will also increase to account for any unpaid dividends at the Exchange Date such that the additional number of the Company's common shares to be issued is equal to the unpaid dividend amount divided by $0.60. As at June 30, 2012, the unpaid dividend amount was $163,200. The Company did not pay the dividend due and payable as of March 31, 2011. The maximum penalty may result in an aggregate of 68,000 additional common shares of the Company being issued at the Exchange Date.

(2) The Company issued convertible debentures (the "Convertible Debentures") in the aggregate principal amount of $740,750. The Convertible Debentures are convertible into common shares at a price of $0.15 per common share for a two-year period from the date of issue.

LIQUIDITY AND CAPITAL RESOURCES (continued)

Financing

(a) On June 18, 2010, the Company entered into a loan facility agreement with a primary lender under which the lender and its partners may advance up to $500,000 to the Company at their discretion. The purpose of the loan is to finance amounts receivable from the British Columbia Liquor Distribution Branch. Amounts advanced bear interest at the lesser of 2% of the average loan balance during the month and 2% of the proceeds advanced under the agreement. The loan is repayable on demand and is secured by a general security agreement over the assets of the Company and by specific assignment of a joint signing account. On November 22, 2010, the Company repaid $375,000. As at June 30, 2012, the outstanding balance of the loan is $nil.

(b) On October 5, 2010, the Company's subsidiary Fort Garry Brewing Company Ltd. accepted an offer of $100,000 pre-authorized working capital loan from Business Development Bank of Canada ("BDC"). The BDC Loan, bearing interest at floating base rate plus a variance of 1%, repayable in monthly installments of $1,750, maturing August 15, 2015, is secured by the assets of Fort Garry and supported by a guarantee made by two directors of the Company. In return for the guarantee, the Company is allowed to issue 250,000 common shares of the Company as bonus shares for a deemed value of $0.08 per share for a total value of $20,000, which was recorded as a discount against the value allocated to the loan. During the year ended June 30, 2012, the Company repaid $21,000 plus interest of $4,680. The Company also recorded interest expense of $6,059 (2011 - $4,941) related to the accretion of the discounted value of the loan, which has been recorded as interest on long-term debt in the statement of operations. As at June 30, 2012, the outstanding balance of the loan is $57,250.

The Company also has a term bank loan with BDC, bearing interest at a floating base rate plus a variance of 1%, repayable in monthly installments of $9,750 plus interest maturing November 15, 2014, secured by the assets of Fort Garry. During the year ended June 30, 2012, the Company repaid $117,000 plus interest of $21,253. As at June 30, 2012, the outstanding balance of the loan is $282,750.

(c) On December 31, 2010, the Company entered into an amendment and extension loan agreement to the loan agreement described in the June 30, 2011 financial statement note 10(c), pursuant to which the lender extended the maturity date to July 31, 2012 and reduced the loan amount to $738,600 from $1,239,000, provided that the Company repay the loan in the amount of $619,000 on January 1, 2011 (paid). Pursuant to the amended loan agreement, the lender provides to the Company a new loan valued at maturity in the amount of $738,600. A discounted value or loan advance amount of $620,000 is calculated based on a 10% per annum interest rate, calculated semi-annually, with interest payable on maturity resulting in a total loan value at maturity of $738,600. In consideration of the lender agreeing to amend and extend the loan, the lender will also earn a bonus of $22,500 to be included in the loan amount. The term of the loan is nineteen months. The Company may repay the loan at any time without penalty by paying the discounted loan advance amount of $620,000 together with accumulated interest. The loan is guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd., both wholly-owned subsidiaries of the Company. During the year ended June 30, 2012, the Company recorded interest expense of $76,773 (2011 - $103,737) related to the accretion of the discounted value of the loan, which has been recorded as interest on long-term debt in the statement of operations.

(d) On December 19, 2011, the Company entered into a loan facility agreement with a primary lender in the amount of $100,000, repayable at any time prior to January 31, 2012. An additional financing placement fee of $10,000 was charged to the Company to secure this loan. Interest on the unpaid balance of the loan would accrue at an interest rate of 2.5% commencing 29 days following the due date of January 31, 2012, compounded monthly, not in advance. Before January 31, 2012, the Company repaid $100,000 plus $10,000 financing placement fee. There was no interest paid.

LIQUIDITY AND CAPITAL RESOURCES (continued)

Financing (continued)

(e) During the year ended June 30, 2011, the Company completed, in three tranches, a private placement of units (the “Unit Offering”) and a private placement of convertible debentures (the “Debenture Offering”) (together, the “Offerings”). Under the Unit Offering, the Company issued 12,730,000 units (the “Units”), at a price of $0.08 per Unit, for aggregate gross proceeds of $1,018,400. Each Unit is comprised of one common share and one common share purchase warrant (a “Warrant”). Each Warrant is exercisable for two years after the issuance of the Units to acquire one common share at an exercise price of $0.15 per common share. Under the Debenture Offering, the Company issued convertible debentures (the “Convertible Debentures”) in the aggregate principal amount of $740,750. The Convertible Debentures are convertible into common shares at a price of $0.15 per common share for a two-year period from the date of issue. The Convertible Debentures bear interest at 10% per annum, payable quarterly in arrears.

Canaccord Genuity Corp. (“Canaccord”) acted as agent for the Offerings and as consideration for its services received a cash commission equal to 10% of the gross proceeds from the Offerings and 2,120,200 warrants (the “Agent’s Warrants”) equal to 12% of the number of Units and 12% of the number of common shares underlying the Convertible Debentures sold pursuant to the Offerings. Each Agent’s Warrant entitles the holder, on exercise, to acquire one unit on the same terms as the Units for a price of $0.08 per unit for a period of 24 months from date of issue. The Company also issued 625,000 common shares with a fair value of $56,250 to the Agent as a corporate finance fee. Other share issue costs were $96,607.

(f) On January 20, 2012, the Company closed a non-brokered private placement (the “Private Placement”). Under the Private Placement, the Company issued 15,300,000 units (the “Units”) at a purchase price of $0.05 per Unit, for aggregate gross proceeds of $765,000. Each Unit is comprised of one common share (“Common Share”) in the capital of the Company, and one half of one non-transferable share purchase warrant (“Warrant”). Each whole Warrant entitles the holder to purchase one additional Common Share at a price of $0.10 for a period of one year from closing the Private Placement. The term of the Warrants is subject to an acceleration right at the option of the Company, provided that the daily volume-weighted average trading price of the Common Shares is $0.15 or higher for at least 10 consecutive trading days and the Company has provided Warrant holders with 30 days prior written notice of the accelerated exercise date. The Company has paid finder’s fees totaling $35,000 and share issue cost totaling $14,140 in connection with the Private Placement in accordance with the policies of the TSX Venture Exchange.

(g) On July 27, 2012, the Company agreed to an one year extension (the “Extension”) and amendment to a loan agreement (the “Loan Agreement”) dated December 31, 2007, pursuant to which the lender (“Lender”), a shareholder of the Company, had provided to the Company a loan (the “Loan”) valued at maturity in the amount of $1,239,000.

The Extension is for one year, with $812,460 due on maturity on July 31, 2013. The Company has negotiated a discounted value or loan advance amount (the “Loan Advance Amount”) of $738,600, that is calculated based on a 10% per annum interest rate, calculated semi-annually, with interest payable on maturity, resulting in a total loan value of $812,460 at maturity. In consideration of the Lender’s agreement to amend and extend the Loan, the Lender will earn a bonus (the “Bonus”) of $24,374 to be included in the Loan amount. Russell may repay the Loan at any time without penalty by paying the Loan Advance Amount together with accumulated interest and prorated Bonus.

The Loan is guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd. both wholly-owned subsidiaries of the Company. As security for the Loan, the Company will grant to the Lender a subordinated security agreement creating a security interest and charge over all of their respective property and assets subordinate to senior debt and senior security of up to $2.5 million plus capital lease obligations incurred for future acquisitions of equipment and other capital assets.

Contractual Obligations, Commitments

The Company utilizes several operating leases to finance manufacturing equipment and vehicles. The Company also leases the building in Surrey, BC and Winnipeg, Manitoba where it has its warehousing and packaging operations. By entering into operating leases, the Company is able to update its equipment more frequently, not utilize its cash to invest in these assets and in so doing lower its overall average cost compared with purchasing the assets. All leases are evaluated at inception for appropriate accounting treatment.

A summary of the Company's contractual obligations for the next five years is as follows:

	Less Than 1 Year	Years 2 and 3	Years 4 and 5	More Than 5 Years	Total
	$	$	$	$	$
Bank indebtedness	**35,793**	–	–	–	35,793
Accounts payable and accrued liabilities	**1,442,437**	–	–	–	1,442,437
Dividend payable	**193,800**	–	–	–	193,800
Interest payable on convertible debentures	**55,557**	–	–	–	55,557
Long-term debt	**876,600**	207,750	3,250	–	1,087,600
Finance lease obligations	**26,247**	44,153	–	–	70,400
Convertible debentures	**740,750**	–	–	–	740,750
	3,371,184	251,903	3,250	–	3,626,337

RELATED PARTIES

The Company has identified its directors and certain senior officers as its key management personnel and the compensation costs for key management personnel and companies related to them were recorded at their exchange amounts as agreed upon by transacting parties and on terms and conditions similar to non-related parties as follows:

Currently, the Company is accruing $1,000 per month to each of three independent directors. The Company also pays $12,083 monthly management fees to a company controlled by the CEO of the Company and $12,083 monthly management fees to the COO of the Company. The Company pays $10,417 monthly professional fees to a company controlled by the CFO of the Company. In addition, the Company pays $1,500 monthly consulting fees to a company controlled by a director of the Company.

The compensation costs for key management personnel and companies related to them were recorded as follows:

		2012		2011
Management fees (a) and (b)	**$**	**290,000**	$	257,250
Directors fees (e)		**33,000**		83,000
Share-based payments (e)		**82,844**		44,645
	$	**405,844**	$	384,895

(a) During the year ended June 30, 2012, the Company incurred management fees of $45,000 to the CEO of the Company (20110 – $128,625) and $100,000 to, a company controlled by the CEO of the Company (2011 - $nil). As at June 30, 2012, the Company owed $31,240 to the CEO and a company controlled by the CEO (2011-$10,000), which is non-interest bearing, unsecured and due on demand.

(b) During the year ended June 30, 2012, the Company incurred management fees of $55,000 to the COO of the Company (2011 – $128,625) and $90,000 to a company controlled by the COO of the Company (2011 - $nil). As at June 30, 2012, the Company owed $52,435 to the COO and a company controlled by the COO (2011 - $10,000), which is non-interest bearing, unsecured and due on demand.

(c) During the year ended June, 2012, the Company incurred accounting fees of $125,000 to a company controlled by the CFO of the Company (2011 – $107,798). As at June 30, 2012, the Company owed $42,640 to this company, which is non-interest bearing, unsecured and due on demand.

(d) During the year ended June 30, 2012, the Company incurred salaries and wages expense of $97,707 to relatives of directors and officers of the Company (2011 – $158,074). As at June 30, 2012, the Company owed $14,132 to relatives of directors of the Company, which is non-interest bearing, unsecured and due on demand.

(e) During the year ended June 30, 2012, the Company granted 2,900,000 stock options to directors and officers and incurred director fees of $33,000 to directors of the Company (2011 – $83,000). As at June 30, 2012, the Company owed $41,000 to the directors (2011 - $83,000), which is non-interest bearing, unsecured and due on demand.

(f) During the year ended June 30, 2012, the Company paid consulting fees of $21,000 to a company controlled by a director of the Company (2011 – $nil).

These transactions were in the normal course of operations and have been recorded at their exchange amounts, which is the consideration agreed upon by the related parties.

TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STARDARDS

The Company has adopted IFRS effective July 1, 2011 with a transition date of July 1, 2010. Prior to the adoption of IFRS the Company prepared its financial statements in accordance with Canadian GAAP.

The comparative information presented in the first annual consolidated financial statements for the year ended June 30, 2011 and the opening financial position as at July 1, 2010 (the "Transition Date") have been prepared in accordance with the accounting policies referenced in Note 2 of the consolidated financial statements for the years ended June 30, 2012 and 2011, and IFRS 1, *First-Time Adoption of International Financial Reporting Standards* ("IFRS 1").

The guidance for the first time adoption of IFRS is set out in IFRS 1 *First-time Adoption of International Financial Reporting Standards'.* Under IFRS 1 the IFRS are applied retrospectively at the transition date with all adjustments to assets and liabilities as stated under GAAP taken to retained earnings unless certain exemptions are applied. The Company has applied the following optional exemptions in its conversion of previous GAAP to IFRS:

<u>Share-based Payment</u>

IFRS 1 encourages, but does not require, first-time adopters to apply IFRS 2 *Share-based Payment* to equity instruments that were granted on or before November 7, 2002, or equity instruments that were granted subsequent to November 7, 2002 and vested before the later of the date of transition to IFRS and January 1, 2005. The Company has elected not to apply IFRS 2 to awards that vested prior to July 1, 2010.

<u>Business Combination</u>

The Company elected under IFRS 1 to not to apply IFRS 3, *Business Combinations* retrospectively to any business combinations that have occurred prior to its Transition Date and such business combinations have not been restated.

<u>Compound Financial Instruments</u>

The Company has elected under IFRS 1 not to retrospectively separate the liability and equity components of any compound instruments for which the liability component is no longer outstanding at the Transition Date.

IFRS 1 also outlines specific guidelines that a first-time adopter must adhere to under certain circumstances. The Company has applied the following mandatory exception in its conversion of previous GAAP to IFRS:

<u>Estimates</u>

In accordance with IFRS 1, an entity's estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error. The Company's IFRS estimates as of July 1, 2010 are consistent with its GAAP estimates for the same date.

IFRS employs a conceptual framework that is similar to Canadian GAAP. However, some differences exist in certain matters of recognition, measurement and disclosure. While adoption of IFRS has not changed the Company's actual cash flows, it has resulted in changes to the Company's reported financial position. In order to allow the users of the financial statements to better understand these changes, the Company's Canadian GAAP statements of comprehensive loss, statements of financial position and statements of cash flows for the year ended June 30, 2011 have been reconciled to IFRS, with the resulting differences explained below.

TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STARDARDS (continued)

a) Under pre-changeover Canadian GAAP, the Company included promotional and marketing materials to be used in the normal course of business in inventory. Under IFRS, these are considered a selling expense at the time the materials are purchased and received. The impact of the adjustment is $71,360 decrease of the beginning balance of equity as of July 1, 2010, and $2,325 increase in selling, general and administrative and net loss for the year ended June 30, 2011. The cumulative impact of such adjustment is a decrease of $71,360 and $73,685 in equity as of July 1, 2010 and June 30, 2011 respectively.

b) In transitioning to IFRS, the Company has reclassified its returnable containers from inventory to property, plant and equipment as their use covers more than one year. The impact of the reclassification adjustment is $222,073 and $180,335 increase in property, plant and equipment, and $222,073 and $180,335 decrease in inventory at July 1, 2010 and June 30, 2011 respectively. There is no impact on equity.

c) As a consequence of the application of the componentization rules to certain property, plant and equipment assets, the accumulated impact to depreciation as determined under IAS 16, Property, Plant and Equipment (“IAS 16”), resulted in a cost recovery of property, plant and equipment assets and increase in equity of $21,892 and $27,324 as at July 1, 2010 and June 30, 2011 respectively. The net impact of the adjustment is $5,432 decrease in amortization and net loss, and increase in equity for the year ended June 30, 2011.

d) Under pre-changeover Canadian GAAP, the Company presented its website costs under property, plant, and equipment, which were recorded at historical cost less amortization. Under IFRS, these assets are considered intangible assets. The impact of the reclassification adjustment is $85 increase in intangible assets and $85 decrease in property, plant, and equipment at July 1, 2010. There is no impact on equity.

e) In transitioning to IFRS, the Company has reclassified its other income to revenues as this income is part of the Company’s normal course of business. For the year ended June 30, 2011, the impact of the reclassification adjustment is $12,080 increase in revenues, net revenues, and gross margin and $3,603 decrease in selling, general and administrative, and $15,683 decrease in net loss before other items, and other income. There is no impact on equity.

f) In transitioning to IFRS, the Company has reclassified the depreciation charge for manufacturing property and equipment to cost of sales and certain selling and distribution costs to selling, general and administrative expense. For the year ended June 30, 2011, the impact of the reclassification adjustment is $26,784 increase in cost of sales and $26,784 decrease in gross margin, $331,928 decrease in depreciation and $305,144 increase in selling, general and administrative expense. There is no impact on net loss or equity.

There were no material differences between the consolidated statement of cash flows presented under IFRS and the consolidated statement of cash flows presented under previous Canadian GAAP.

CRITICAL ACCOUNTING ESTIMATES

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses for the reporting period. Significant areas requiring the use of management estimates may include recovery of accounts receivable, inventory valuation, the estimated useful life of long-lived assets, the recoverability of amounts recorded for long-lived assets, estimates used in impairment analysis of long-lived assets, container liabilities, valuation of deferred tax assets and liabilities and estimates used in calculating share-based compensation. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant. Actual results could differ from management's best estimates as additional information becomes available.

Property, Plant and Equipment

The accounting for property, plant and equipment requires that management make estimates involving the life of the assets, the selection of an appropriate method of depreciation and determining whether an impairment of assets exists.

The Company reviews the residual values, useful lives of depreciable assets and depreciation method on an annual basis and where revisions are made, the Company applies such changes in estimates on a prospective basis.

The net carrying amounts of property, plant and equipment are reviewed for impairment either individually or at the cash generating unit level at the end of each reporting period. If there are indicators of impairment, an evaluation is undertaken to determine whether the carrying amounts are in excess of their recoverable amounts. An asset's recoverable amount is determined as the higher of its fair value less cost to sell and its value-in-use. To the extent that an asset's carrying amount exceeds its recoverable amount, the excess is fully provided for in the period in which it is determined to be impaired. Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior periods. There is uncertainty in these estimates as the related recoverable amounts are projected for future years based on underlying assumptions such as volume growth, inflation factors and industry trends which may not materialize. Management uses its best estimates to forecast these amounts, but the actual amounts may vary from estimates. Should future results differ from management's estimates, an impairment of these assets and a related write-down may result. As at the date of this report, the Company believes that its estimates are materially correct.

Intangible Assets

Indefinite life intangible assets consist of brands and trademarks. These assets are recorded at cost and are not amortized but instead are reviewed for impairment at the end of each reporting period. If there are indicators of impairment, an evaluation is undertaken to determine whether the carrying amounts are in excess of their recoverable amounts. An asset's recoverable amount is determined as the higher of its fair value less cost to sell and its value-in-use. There is uncertainty in these estimates as the related recoverable amounts are projected for future years based on underlying assumptions such as volume growth, inflation factors and industry trends which may not materialize. Management uses its best estimates to forecast these amounts, but the actual amounts may vary from estimates. Should future results differ from management's estimates, an impairment of these assets and a related write-down may result. As at the date of this report, the Company believes that its estimates are materially correct.

RISKS AND UNCERTAINTIES

Credit Risk

The Company grants credit to its customers in the normal course of business. However as the major portion of the accounts receivable are held by the BCLDB, the MLCC, and AGLC, management believes exposure to credit risk is limited.

Competition

The Company considers its main competitors to be other participants in the Canadian brewing industry, which includes imported beer and specialty and value priced brands brewed by both small regional brewers and the national brewers. Existing regional breweries are increasing their production capacities and marketing programs. National brewers are aggressively promoting their own specialty and value brands as well as premium brands. The Company also anticipates increasing competition as new brewers enter markets in which the Company currently operates.

The principal competitive factors affecting the market for the Company's products include quality and taste, packaging, advertising and promotional support, brand recognition and price. There can be no assurance that the Company will be able to compete successfully in this category against current and future competitors based on these and other factors. The Company competes with a variety of domestic and international brewers, many of whom have substantially greater financial, production, distribution and marketing resources. The Company anticipates increased competition in the premium beer category from the major domestic brewers, each of whom has introduced and is marketing premium-priced products. The large domestic brewers dominate the domestic beer market and the Company expects that certain of these companies may seek further participation in the premium beer market through the acquisition of equity positions in, or the formation of, distribution alliances with other brewers.

Increased competition could result in price reductions, reduced profit margins and loss of market share, all of which could have a material adverse effect on the Company's operations. The Company's products also compete generally with other alcoholic beverages.

Government Regulation

The Company's business is regulated by federal, provincial and municipal laws and regulations regarding such matters as licensing requirements, trade and pricing practices, permitted and required labeling, advertising, promotion and marketing practices, relationships with distributors and related matters. Failure on the part of the Company to comply with federal, provincial or municipal laws and regulations could result in the loss, revocation or suspension of the Company's licenses, permits or approvals and could have a material adverse effect on the Company's business. The Company believes that it has obtained all regulatory permits and licences necessary to operate its business where the Company's products are currently being produced and distributed. In addition, changes to taxes, environmental regulations or any other laws or regulations which affect the Company's products or their production, handling or distribution could have a material adverse effect on the Company's operations.

Trends in Consumer Preferences and Attitudes

The domestic premium beer market has grown dramatically over the past decade. The Company believes that one factor in such growth has been consumer demand. No assurance can be given however that consumer demand for these products will continue in the future. The Company's success also depends upon a number of factors related to the level of discretionary consumer spending, such as the general state of the economy, tax laws and consumer confidence in future economic conditions.

RISKS AND UNCERTAINTIES (continued)

Protection of Intellectual Property Rights; Risk of Third Party Claims of Infringement

The Company considers its trademarks, particularly certain brand names and product packaging, advertising and promotion design and artwork, to be of considerable value and critical to its business. The Company relies on trademark laws and other arrangements to protect its proprietary rights. There can be no assurance that the steps taken by the Company to protect its intellectual property rights will preclude competitors from developing similar brand names or promotional materials. While the Company believes that its proprietary rights do not infringe upon those third parties, it possesses no assurances of such a situation. The Company has applied for registration of the following trademarks: Russell, Fort Garry and Rock Mountain.

Dependence on Key Personnel

The Company's success depends to a significant degree upon the continuing contributions of key personnel, and on its ability to attract and retain qualified management, sales, production and marketing personnel. The loss of any of such persons or the failure to recruit additional key personnel in a timely manner, could adversely affect the Company. The Company does not maintain any key man life insurance on any of its personnel.

Operating Hazards

The Company's operations are subject to certain hazards and liability risks faced by all brewers, such as the potential contamination of ingredients or products and equipment defects. While the Company has not experienced a contamination problem in its products, the occurrence of such a problem could result in a costly product recall and serious damage to the Company's reputation for product quality. Although the Company maintains insurance against certain risks under various general liability and product liability insurance policies, there can be no assurance that the Company's insurance will be adequate or that claims resulting from such incidents will be accepted as filed.

Trade Regulations

The 1994 North America Free Trade Agreement ("NAFTA") among Canada, Mexico and the United States expanded the 1989 Free Trade Agreement between Canada and the United States. To date, NAFTA has had no material effect on the Company's business or operations. However, the adoption of new trade regulations or future trade disputes that result in retaliatory practices or increased tariffs between the United States and Canada could adversely affect the Company's business.

Proprietary Rights

Although the formulas for the Company's beers are proprietary trade secrets of the Company, there can be no assurance that others will not develop beers of the same or similar tastes and qualities as the Company's beers.

Seasonal Nature of Business

The alcoholic beverage industry in Canada is seasonal in nature. Accordingly, the Company has historically experienced a seasonal pattern in its operating results, with the second and third quarters historically exhibiting lower revenues. Therefore, the results in any one quarter are not indicative of results in any other quarter, or for the year as a whole.

RISKS AND UNCERTAINTIES (continued)

Uncertainty of Additional Capital

In the past, the Company relied on the issuance of equity and debt securities to meet its capital requirements. The ability of the Company to arrange additional financing in the future will depend, in part, on the prevailing capital market conditions as well as the business performance of the Company. There can be no assurance that additional capital or other types of financing will be available if needed or that, if available, the terms of such financing will be favourable to the Company. If additional financing is raised by the Company through the issuance of securities from treasury, control of the Control may change and security holders may suffer significant dilution. The Company also requires continued support from its lenders to maintain its financial condition. The loss of this support could limit expansion opportunities and put strain on the Company's continuing operations.