RUSSELL BREWERIES INC.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

UNAUDITED

NOTICE OF NO AUDITOR REVIEW OF CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated interim financial statements of the Company have been prepared by, and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of the financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of financial statements by an entity's auditor.

RUSSELL BREWERIES INC.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION

(Unaudited; Expressed in Canadian Dollars)

		September 30, 2012	June 30, 2012
ASSETS			
Current			
Cash and cash equivalents	$	**27,494**	$ 29,199
Accounts receivable		**932,456**	876,530
Inventories (Note 4)		**746,974**	735,852
Prepaid expenses and deposits		**199,574**	134,482
		1,906,498	1,776,063
PROPERTY AND EQUIPMENT (Note 5)		**3,123,528**	3,167,586
INTANGIBLE ASSETS (Note 6)		**1,935,268**	1,935,268
RESTRICTED TERM DEPOSITS (Note 7)		**100,000**	100,000
	$	**7,065,294**	$ 6,978,917
LIABILITIES			
Current			
Bank indebtedness (Note 19(c))	$	**98,545**	$ 35,793
Accounts payable and accrued liabilities		**1,404,412**	1,442,437
Dividend payable (Note 13)		**173,400**	163,200
Interest payable on convertible debentures		**18,519**	18,519
Convertible debentures (Note 11)		**716,419**	668,841
Due to related parties		**212,571**	181,447
Current portion of long-term debt (Note 9)		**888,910**	869,719
Current portion of finance lease obligations (Note 10)		**13,119**	19,563
		3,525,895	3,399,519
LONG-TERM DEBT (Note 9)		**168,801**	202,000
FINANCE LEASE OBLIGATIONS (Note 10)		**77,509**	41,559
DEFERRED TAX LIABILITIES (Note 14)		**321,000**	321,000
		4,093,205	3,964,078
SHAREHOLDERS' EQUITY			
SHARE CAPITAL (Note 12)		**9,772,163**	9,772,163
SHARES ALLOTTED BUT UNISSUED (Notes 9(b) and 13)		**5,440**	5,440
EQUITY COMPONENT OF CONVERTIBLE DEBENTURES (Note 11)		**86,484**	86,484
EXCHANGEABLE PREFERRED SHARES (Note 13)		**518,979**	518,979
SHARE-BASED PAYMENTS RESERVES		**3,392,481**	3,361,624
DEFICIT		**(10,803,458)**	(10,729,851)
		2,972,089	3,014,839
	$	**7,065,294**	$ 6,978,917

NATURE OF OPERATIONS AND GOING CONCERN (Note 1)
COMMITMENTS AND CONTINGENCIES (Note 18)
SUBSEQUENT EVENT (Note 22)

Approved on behalf of the Board of Directors on November 29, 2012:

/s/ Andrew Harris	*/s/ Brian Harris*
Richard Shier, Director	Brian Harris, Director

RUSSELL BREWERIES INC.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE LOSS

(Unaudited; Expressed in Canadian Dollars)

		Three Months Ended September 30, 2012		Three Months Ended September 30, 2011
REVENUES (Note 21)	$	**2,325,082**	$	2,196,584
LESS: EXCISE TAX AND PROVINCIAL MARK-UP		**518,293**		540,349
NET REVENUES		**1,806,789**		1,656,235
COST OF SALES (Note 4)		**884,846**		834,624
GROSS MARGIN		**921,943**		821,611
EXPENSES				
Depreciation		**35,357**		33,975
Selling, general and administrative (Notes 12(c) and 17)		**854,841**		785,650
		890,198		819,625
LOSS BEFORE OTHER INCOME (EXPENSE)		**31,745**		1,986
OTHER INCOME (EXPENSE)				
Interest on long-term debt and convertible debt		**(95,486)**		(85,177)
Interest income		**333**		63
		(95,153)		(85,114)
LOSS BEFORE INCOME TAXES		**(63,408)**		(83,128)
INCOME TAXES				
Deferred income tax expense (Note 14)		**–**		–
NET LOSS AND COMPREHENSIVE LOSS FOR THE PERIOD		**(63,408)**		(83,128)
LOSS PER SHARE (Note 15)				
Basic and diluted	$	**(0.00)**	$	(0.00)

RUSSELL BREWERIES INC.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

(**Unaudited; Expressed in Canadian Dollars**)

	Share Capital							
	Number of Shares	Value	Allotted Shares	Convertible Debentures	Preferred Shares	Share-based payments reserves	Deficit	Total Shareholders' Equity
Balance, July 1, 2012	**62,230,562**	**$9,772,163**	**$5,440**	**$86,484**	**$518,979**	**$3,361,624**	**$(10,729,851)**	**$3,014,839**
Comprehensive loss for the period	**–**	**–**	**–**	**–**	**–**	**–**	**(63,408)**	**(63,408)**
Fair value of stock options granted	**–**	**–**	**–**	**–**	**–**	**30,857**	**–**	**30,857**
Dividends on preferred shares	**–**	**–**	**–**	**–**	**–**	**–**	**(10,200)**	**(10,200)**
Balance, September 30, 2012	**62,230,562**	**$9,772,163**	**$5,440**	**$86,484**	**$518,979**	**$3,392,481**	**$(10,803,459)**	**$2,972,089**

	Share Capital							
	Number of Shares	Value	Allotted Shares	Convertible Debentures	Preferred Shares	Share-based payments reserves	Deficit	Total Shareholders' Equity
Balance, July 1, 2011	46,680,437	$9,036,272	$25,440	$86,484	$518,979	$3,278,779	$(9,579,885)	$3,366,069
Comprehensive loss for the period	–	–	–	–	–	–	(83,128)	(83,128)
Dividends on preferred shares	–	–	–	–	–	–	(10,200)	(10,200)
Balance, September 30, 2011	46,680,437	$9,036,272	$25,440	$86,484	$518,979	$3,278,779	$(9,673,213)	$3,272,741

The accompanying notes are an integral part of these consolidated financial statements

RUSSELL BREWERIES INC.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS

(Unaudited; Expressed in Canadian Dollars)

		Three Months Ended September 30, 2012		Three Months Ended September 30, 2011
CASH FLOWS PROVIDED BY (USED IN):				
OPERATING ACTIVITIES				
Net loss for the period	**$**	**(63,408)**	$	(83,128)
Adjusted for non-cash items:				
Depreciation		**115,901**		115,664
Accretion of long-term debt		**20,493**		20,414
Accretion of convertible debentures		**47,577**		32,690
Accrued interest on convertible debentures		**18,519**		18,519
Share-based compensation		**30,857**		–
		169,939		104,159
Net changes in non-cash working capital items:				
Accounts receivable		**(55,926)**		281,776
Prepaid expenses and deposits		**(65,092)**		(1,038)
Inventories		**(11,122)**		(1,905)
Due to and from related parties		**43,800**		62,446
Accounts payable and accrued liabilities		**(50,700)**		(198,524)
		30,899		246,914
INVESTING ACTIVITIES				
Purchases of property and equipment		**(29,028)**		(2,904)
		(29,028)		(2,904)
FINANCING ACTIVITIES				
Interest payable on convertible debentures		**(18,519)**		(18,519)
Proceeds from (repayment of) bank indebtedness		**62,752**		(27,230)
Repayment of long-term debt		**(34,500)**		(34,500)
Repayment of finance lease obligations		**(13,309)**		(16,262)
		(3,576)		(96,511)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		**(1,705)**		147,499
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD		**29,199**		29,101
CASH AND CASH EQUIVALENTS, END OF PERIOD	**$**	**27,494**	$	176,600
CASH AND CASH EQUIVALENTS CONSIST OF:				
Demand deposits	**$**	**27,494**	$	176,600

SUPPLEMENTAL CASH FLOW INFORMATION (Note 16)

1. NATURE OF OPERATIONS AND GOING CONCERN

Russell Breweries Inc. (the “Company”) was incorporated under the laws of the Province of British Columbia, Canada on March 23, 2000. The head office and principal address of the Company are located at #202 - 13018 80th Avenue, Surrey, British Columbia, V3W 3A8. The Company produces beer primarily for sale to provincial liquor distribution organizations and entities engaged in the food and beverage industries within Canada. The Company’s shares are traded on the TSX Venture Exchange (the “TSX.V”).

These consolidated financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assumes the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. As at September 30, 2012, the Company had a working capital deficiency of $1,619,397 and accumulated losses since inception of $10,803,458. These factors raise significant doubt about the Company’s ability to continue as a going concern. The continued operation of the Company is dependent on its ability to obtain financing sufficient to generate profitable operations in the future. There is no guarantee that the Company will be able to raise this additional financing.

2. STATEMENT OF COMPLIANCE AND BASIS OF PRESENTATION

a) Statement of Compliance

These consolidated financial statements are prepared in accordance with International Accounting Standards (“IAS”) 34 *Interim Financial Reporting*. These financial statements do not include all of the information required for full annual financial statements.

These condensed consolidated interim financial statements were authorized for issuance by the Board of Directors on November 29, 2012.

b) Presentation and Functional Currency

These consolidated financial statements are presented in Canadian dollars. Under International Financial Reporting Standards (“IFRS”), the Canadian dollar is the functional currency of the Company and its wholly-owned subsidiaries, Russell Brewing Company Ltd. located in Surrey, British Columbia and Fort Garry Brewing Company Ltd. located in Winnipeg, Manitoba.

c) Basis of Measurement

Depending on the applicable IFRS requirements, the measurement basis used in the preparation of these financial statements is cost, net realizable value, fair value or recoverable amount.

d) Significant Accounting Estimates and Judgments

The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires management to make estimates and judgments 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.

(Unaudited; Expressed in Canadian Dollars)

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies that have been used in the preparation of these condensed consolidated interim financial statements are summarized in the audited consolidated financial statements of the Company for the year ended June 30, 2012. These statements should be read in conjunction with the audited consolidated financial statements for the year ended June 30, 2012.

4. INVENTORIES AND COST OF SALES

		September 30, 2012		June 30, 2012
Finished goods	$	**128,340**	$	107,123
Work-in-progress		**167,285**		155,362
Raw materials		**451,349**		473,367
	$	**746,974**	$	735,852

The cost of sales of the Company is broken down into its cash and non-cash components as follows:

		Three Months Ended September 30, 2012		Three Months Ended September 30, 2011
Operating expenses	**$**	**804,302**	$	752,935
Depreciation		**80,544**		81,689
	$	**884,846**	$	834,624

(Unaudited; Expressed in Canadian Dollars)

5. PROPERTY AND EQUIPMENT

	Computer	Equipment	Leasehold improvements	Office furniture and fixtures	Vehicles	Returnable containers	Total
Cost							
Balance as at June 30, 2011	$ 69,285	$ 5,891,266	$ 1,307,826	$ 62,794	$ 519,599	$ 850,685	$ 8,701,455
Additions	–	21,976	-	1,050	–	13,087	36,113
Balance as at June 30, 2012	**$ 69,285**	**$ 5,913,242**	**$ 1,307,826**	**$ 63,844**	**$ 519,599**	**$ 863,772**	**$ 8,737,568**
Additions		**25,312**			**42,815**	**3,407**	**71,534**
Balance as at September 30, 2012	**$ 69,285**	**$ 5,938,554**	**$ 1,307,826**	**$ 63,844**	**$ 562,414**	**$ 867,179**	**$ 8,809,102**
Accumulated Depreciation							
Balance as at June 30, 2011	$ 66,810	$ 2,802,894	$ 1,221,166	$ 53,284	$ 295,444	$ 670,350	$ 5,109,948
Depreciation	2,199	289,548	53,955	6,594	51,960	55,778	460,034
Balance as at June 30, 2012	**$ 69,009**	**$ 3,092,442**	**$ 1,275,121**	**$ 59,878**	**$ 347,404**	**$ 726,128**	**$ 5,569,982**
Depreciation	**(590)**	**72,921**	**13,488**	**1,661**	**13,730**	**14,382**	**115,592**
Balance as at September 30, 2012	**$ 68,419**	**$ 3,165,363**	**$ 1,288,609**	**$ 61,539**	**$ 361,134**	**$ 740,510**	**$ 5,685,574**
Carrying amounts							
June 30, 2011	$ 2,475	$ 3,088,372	$ 86,660	$ 9,510	$ 224,155	$ 180,335	$ 3,591,507
June 30, 2012	$ 276	$ 2,820,800	$ 32,705	$ 3,966	$ 172,195	$ 137,644	$ 3,167,586
September 30, 2012	**$ 866**	**$ 2,773,191**	**$ 19,217**	**$ 2,305**	**$ 201,280**	**$ 126,669**	**$ 3,123,528**

Equipment includes assets under finance leases with a cost of $387,636 (June 30, 2012 – $387,636) and accumulated depreciation of $74,650 (June 30, 2012 – $70,334). Vehicles includes assets under finance leases with a cost of $515,550 (June 30, 2012 – $494,694) and accumulated depreciation of $324,401 (June 30, 2012 – $311,512).

(Unaudited; Expressed in Canadian Dollars)

6. INTANGIBLE ASSETS

	Brands and Trademarks	Website	Total
Cost			
Balance as at June 30, 2011	$ 1,935,268	$ 5,975	$ 1,941,243
Balance as at June 30, 2012	**$ 1,935,268**	**$ 5,975**	**$ 1,941,243**
Balance as at September 30, 2012	**$ 1,935,268**	**$ 5,975**	**$ 1,941,243**
Accumulated Depreciation			
Balance as at June 30, 2011	$ –	$ 5,975	$ 5,975
Balance as at June 30, 2012	**$ –**	**$ 5,975**	**$ 5,975**
Balance as at September 30, 2012	**$ –**	**$ 5,975**	**$ 5,975**
Carrying amounts			
June 30, 2011	$ 1,935,268	$ –	$ 1,935,268
June 30, 2012	**$ 1,935,268**	**$ –**	**$ 1,935,268**
September 30, 2012	**$ 1,935,268**	**$ –**	**$ 1,935,268**

7. RESTRICTED TERM DEPOSITS

A term deposit of $100,000 has been pledged as security for a $100,000 bank line of credit (June 30, 2012 – $100,000). During the period ended September 30, 2012, the Company redeemed a $100,000 term deposit in connection with a buy out of a finance lease. As at September 30, 2012, no term deposit has been pledged as security for finance leases (June 30, 2012 – $nil).

8. DEMAND LOAN

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 was to accrue at an interest rate of 2.5% per month commencing 30 days following the due date of January 31, 2012, compounded monthly, not in advance. On January 31, 2012, the Company repaid $100,000 plus $10,000 financing placement fee. There was no interest paid.

(Unaudited; Expressed in Canadian Dollars)

9. LONG-TERM DEBT

		September 30, 2012		June 30, 2012
Term bank loan, bearing interest at a floating base rate plus a variance of 1%, repayable in monthly installments of $18,750 plus interest prior to October 2010 and thereafter repayable in monthly installments of $9,750 plus interest maturing November 15, 2014, secured by the assets of Fort Garry (a)	**$**	**253,500**	$	282,750
Term bank loan, bearing interest at floating base rate plus a variance of 1%, repayable in monthly installments of $1,750 plus interest maturing August 15, 2015, secured by the assets of Fort Garry (b)		**53,301**		57,250
Discount loan, bearing interest at 10% per annum compounded semi-annually, $738,600 due July 31, 2012, secured by the assets of Russell and Fort Garry (c)		**750,910**		731,719
		1,057,711		1,071,719
Less: current portion of long-term debt		**(888,910)**		(869,719)
Long-term portion of long-term debt	**$**	**168,801**	$	202,000

(a) On December 8, 2008, the bank made an amendment to the existing term loan in accordance with the request of the Company for six month principal postponement. Pursuant to the amendment, the remaining loan amount on December 8, 2008 of $787,500 was to be repaid by 42 consecutive monthly principal installments of $18,750 each commencing June 15, 2009 and ending November 15, 2012. The bank also granted a reduction of the interest rate on the term loan by 1%. With the exception of the amendments agreed, all terms and conditions of the term loan remain unchanged. On September 22, 2010, the bank made a further amendment to the existing term loan in accordance with the request of the Company. Pursuant to the amendment, the remaining loan amount is to be repaid by 50 consecutive monthly principal installments of $9,750 each commencing October 15, 2010 and ending November 15, 2014.

(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% 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 an estimated fair 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 period ended September 30, 2012, the Company recorded interest expense of $1,302 (2011 - $1,650) 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.

(c) On December 31, 2007, the Company entered into a loan agreement pursuant to which the lender, a shareholder of the Company, provided a discounted loan to the Company valued at $1,239,000 at maturity. Under the agreement, a notional principal amount of $965,000 was assigned to the loan. In connection with the loan, the lender was entitled to a $25,000 bonus which was deducted from the notional principal amount of $965,000, resulting in net proceeds to the Company of $940,000. The Company also issued 250,000 warrants to the lender, each warrant entitling the lender to purchase one common share of the Company at a price of $0.65 per share for a period of two years expiring on December 31, 2009. Net proceeds of $896,040 and $43,960 were allocated to the loan and warrants, respectively, based on their relative fair values on December 31, 2007. The Company incurred cash debt issue costs of $14,435 which were recorded as a discount against the value allocated to the loan.

(Unaudited; Expressed in Canadian Dollars)

9. LONG-TERM DEBT (continued)

(c) The fair values of the warrants issued in connection with the loan were computed using the Black-Scholes option-pricing model. The Company may repay the loan at any time without penalty by paying the notional principal amount of $965,000 plus accumulated interest. As at September 30, 2012, the fair value of this early settlement option was estimated to be $nil.

On December 31, 2010, the Company entered into an amendment and loan extension agreement to the loan agreement dated December 31, 2007, 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 was 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 was guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd., both wholly-owned subsidiaries of the Company.

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. The Extension is for one year, maturing on July 31, 2013 and bears interest at 10% per annum, calculated semi-annually. In consideration of the Lender’s agreement to amend and extend the Loan, the Lender will earn a bonus (the “Bonus”) of $24,374. 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.

During the period ended September 30, 2012, the Company recorded interest expense of $19,191 (2012 - $18,764) 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 comprehensive loss.

Excluding finance fees and discounting, the Company’s future estimated principal repayments of long-term debt are as follows:

Fiscal Year		**Amount**
2013	$	**842,100**
2014		**138,000**
2015		**69,750**
2016		**3,250**
	$	**1,053,100**

(Unaudited; Expressed in Canadian Dollars)

10. FINANCE LEASE OBLIGATIONS

The Company finances certain property and equipment using finance leases which bear interest at rates ranging from 6.6% to 27.9% and expire on various dates through June 2016. Estimated future minimum lease payments under these finance leases are as follows:

Fiscal Year:		**Amount**
2013	**$**	**22,378**
2014		**40,722**
2015		**26,682**
2016		**12,970**
Total minimum lease payments		**102,752**
Less: amount representing interest		**(12,124)**
Net minimum lease payments		**90,628**
Less: current portion of finance lease obligations		**(13,119)**
Long-term portion of finance lease obligations	**$**	**77,509**

11. CONVERTIBLE DEBENTURES

		September 30, 2012		June 30, 2012
Convertible debentures with a face value of $531,000, bearing interest at 10%, unsecured and due on November 4, 2012	$	**516,967**	$	482,116
Convertible debentures with a face value of $158,000, bearing interest at 10%, unsecured and due on December 3, 2012		**150,788**		141,155
Convertible debentures with a face value of $51,750, bearing interest at 10%, unsecured and due on December 24, 2012		**48,664**		45,570
Liability component of convertible debentures		**716,419**		668,841
Less: current portion		**(716,419)**		(668,841)
Long-term portion	$	**–**	$	–

During the year ended June 30, 2011, the Company completed, in three tranches, a private placement of convertible debentures (the “Debenture Offering” – see Note 12(b)). 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.

The Company used the residual value method to allocate the principal amount of the convertible debentures between the liability and equity components. Under this method, the value of the equity component of $119,691 was determined by deducting the fair value of the liability component of $621,059 from the principal amount of $740,750. The fair value of the liability component was computed as the present value of future principal and interest payments discounted at a rate of 20% per annum.

(Unaudited; Expressed in Canadian Dollars)

11. CONVERTIBLE DEBENTURES (continued)

The following tables summarize the changes in the liability and equity components of the convertible debentures during the period ended September 30, 2012:

Liability component		**September 30, 2012**		June 30, 2012
Balance, beginning of period	$	**668,841**	$	518,387
Accretion		**47,578**		150,454
Balance, end of period		**716,419**		668,841
Less: current portion		**(716,419)**		(668,841)
Long-term portion, end of period	$	**–**	$	–

Equity component		**September 30, 2012**		June 30, 2012
Balance, beginning of period	$	**86,484**	$	86,484
Gross proceeds from issuance		**–**		–
Amount allocated to the liability component		**–**		–
Direct issuance costs allocated to the equity component		**–**		–
Balance, end of period	$	**86,484**	$	86,484

The liability components of the convertible debentures are recorded at amortized cost and accreted to the principal amount over the estimated term of the convertible debentures using an effective interest rate of 20%.

Excluding finance fees and discounting, the Company's future estimated principal repayments of convertible debentures are as follows:

Fiscal Year		**Amount**
2013		**740,750**
	$	**740,750**

12. SHARE CAPITAL

(a) Authorized Share Capital

The Company's authorized share capital consists of an unlimited number of common shares without par value.

(b) Issued Share Capital

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"). The first tranche of each of the Offerings closed on November 4, 2010, the second tranche of each of the Offerings closed on December 3, 2010, and the third tranche closed on December 23, 2010.

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. These agent warrants were assigned a fair value of $161,063 for the Units and $61,169 for the Convertible Debentures which was determined using the Black-Scholes option-pricing model at the date of issuance using the following assumptions: expected warrant life of 2 years; risk-free interest rate of from 1.39% to 2.25%; expected dividend yield of 0% and expected stock price volatility of from 114% to 114%. 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.

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 paid finder's fees totalling $35,000 and incurred other share issuance costs totalling $14,140 in connection with the Private Placement in accordance with the policies of the TSX Venture Exchange.

(Unaudited; Expressed in Canadian Dollars)

12. SHARE CAPITAL (continued)

(b) Issued Share Capital (continued)

On April 2, 2012, the Company issued 250,000 common shares in its capital as bonus shares to each of its two directors who provided personal guarantees for the $100,000 working capital loan from Business Development Bank of Canada (Note 9(b)).

(c) Stock Options

Under the Company's stock option plan (the "Plan"), the Company's board of directors is authorized to grant stock options to directors, officers, consultants and employees of the Company not to exceed 10% of the issued and outstanding common shares of the Company from time to time. Stock options granted under the Plan are exercisable over a period not exceeding five years from the date granted. Exercise prices may not be less than the market price of the common shares on the date of grant less applicable discounts permitted by the TSX Venture Exchange. Vesting terms are determined by the board of directors on the date of grant.

During the period ended September 30, 2012, the Company granted nil and vested 500,000 (2011 – granted nil and vested nil) incentive stock options to key employees and directors exercisable at $0.10 per share expiring after five years of the grant date, pursuant to its stock option plan. The fair value of each option granted was $0.05 calculated using the Black-Scholes option-pricing model at the date of grant using the following assumptions: expected option life for 5 years; forfeiture rate of 0%; risk-free interest rate of 1.50%; expected dividend yield of 0% and expected stock price volatility of 128%. During the period ended September 30, 2012, the Company recognized compensation cost of $30,857 (2012 – $nil) as selling, general and administrative expense.

The estimated fair value of options granted to the Company's employees and directors is calculated at the grant date and each tranche is recognized on the graded vesting method over the period during which the options vest. The fair value of non-employee awards is estimated at each reporting period until the final measurement date.

Stock option activity during the period ended September 30, 2012 and the year ended June 30, 2012 is presented below:

	September 30, 2012			June 30, 2012		
	Number of Shares		**Weighted Average Exercise Price**	Number of Shares		Weighted Average Exercise Price
Outstanding, beginning of period	**4,077,500**	**$**	**0.10**	1,627,500	$	0.10
Granted	**–**		**–**	3,000,000		0.10
Expired	**(140,000)**		**0.10**	(550,000)		0.10
Forfeited	**–**		**–**	–		–
Outstanding, end of period	**3,937,500**	**$**	**0.10**	4,077,500	$	0.10

(Unaudited; Expressed in Canadian Dollars)

12. SHARE CAPITAL (continued)

(c) Stock Options (continued)

At September 30, 2012, the following stock options are outstanding:

	Options Outstanding			Options Exercisable	
Exercise Price $	**Number of Shares**	**Weighted Average Remaining Life (in years)**	**Weighted Average Exercise Price $**	**Number of Shares**	**Weighted Average Exercise Price $**
0.10	**837,500**	**0.72**	**0.10**	**837,500**	**0.10**
0.10	**100,000**	**3.05**	**0.10**	**100,000**	**0.10**
0.10	**3,000,000**	**4.44**	**0.10**	**1,066,667**	**0.10**
	3,937,500	**3.61**	**0.10**	**2,004,167**	**0.10**

On August 29, 2012, 140,000 stock options exercisable at $0.10 per share expired unexercised.

(d) Warrants

Warrant activity during the period ended September 30, 2012 and the year ended June 30, 2012 is presented below:

	September 30, 2012		June 30, 2012	
	Number of Shares	**Weighted Average Exercise Price**	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of period	**20,380,000**	**$ 0.13**	12,730,125	$ 0.15
Granted	**–**	**–**	7,650,000	0.10
Exercised	**–**	**–**	(125)	0.25
Expired	**–**	**–**	–	–
Outstanding, end of period	**20,380,000**	**$ 0.13**	20,380,000	$ 0.13

At September 30, 2012, the following warrants were outstanding entitling the holders the right to purchase one common share for each warrant held:

Number of Warrants	Weighted Average Exercise Price	Expiry Date
10,402,500	**$ 0.15**	**November 4, 2012**
827,500	**0.15**	**December 3, 2012**
1,500,000	**0.15**	**December 23, 2012**
7,650,000	**0.10**	**January 20, 2013**
20,380,000	**$ 0.13**	

(Unaudited; Expressed in Canadian Dollars)

12. SHARE CAPITAL (continued)

(e) Agent Unit Warrants

Agent unit warrants activity during the period ended September 30, 2012 and the year ended June 30, 2012 is presented below:

	September 30, 2012			June 30, 2012		
	Number of Shares		**Weighted Average Exercise Price**	Number of Shares		Weighted Average Exercise Price
Outstanding, beginning of year	**2,120,200**	**$**	**0.08**	–	$	–
Granted	**–**		**–**	2,120,200		0.08
Expired	**–**		**–**	–		–
Outstanding, end of year	**2,120,200**	**$**	**0.08**	2,120,200	$	0.08

At September 30, 2012, the following agent unit warrants were outstanding entitling the holders the right to purchase one unit, consisting of one common and one common share purchase warrant exercisable for two years after issuance at an exercise price of $0.15 per share, for each warrant held:

Number of Warrants		**Weighted Average Exercise Price**	**Expiry Date**
1,673,100	**$**	**0.08**	**November 4, 2012**
225,700		**0.08**	**December 3, 2012**
221,400		**0.08**	**December 23, 2012**
2,120,200	**$**	**0.08**	

(Unaudited; Expressed in Canadian Dollars)

13. EXCHANGEABLE PREFERRED SHARES

On March 31, 2008, the Company's wholly-owned subsidiary, Russell Brewing Company Ltd. ("Russell"), completed a brokered private placement for 68,000 exchangeable, non-voting preferred shares (the "Exchangeable Shares") at a price of $10 per share for gross proceeds of $680,000 under the Equity Capital Program of the Province of British Columbia (the "Program"). In connection with the private placement, the Company issued 6,800 agent warrants allowing the holder to purchase 16.67 common shares of the Company per warrant at a price of $0.60 per common share until March 31, 2010. These agent warrants were assigned a fair value of $21,396 which was determined using the Black-Scholes option-pricing model. The Company also paid a commission of $54,400 and incurred other cash issuance costs of $60,000.

The Exchangeable Shares have a 6% per annum cumulative dividend, payable semi-annually, in accordance with rules under the Program. After five years (the "Exchange Date"), each Exchangeable Share 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. At the Exchange Date, the exchange ratio will be increased for any penalty incurred or for any unpaid dividends.

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. 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 September 30, 2012, the unpaid dividend amount was $173,400 (June 30, 2012 - $163,200). The maximum penalty may result in an aggregate of 68,000 additional common shares of the Company being issued at the Exchange Date. During the year ended June 30, 2011, the penalty shares were recorded as shares allotted but unissued. The shares were valued at $5,440 measured using the market price of the shares on March 31, 2011, the date the penalty was incurred.

14. INCOME TAXES

The Company has non-capital losses of approximately $12,191,000 which may be carried forward to apply against future years income tax for Canadian income tax purposes, subject to final determination by taxation authorities and expiring as follows:

Fiscal Year of Expiry	**Amount**
2014	**$ 52,000**
2015	**283,000**
2026	**257,000**
2027	**1,538,000**
2028	**1,696,000**
2029	**2,213,000**
2030	**1,831,000**
2031	**1,937,000**
2032	**2,384,000**
	$ 12,191,000

(Unaudited; Expressed in Canadian Dollars)

15. LOSS PER SHARE

Net loss attributable to common shareholders in the computation of loss per share is as follows:

		Three Months Ended September 30, 2012		Three Months Ended September 30, 2011
Net loss and comprehensive loss	**$**	**(63,408)**	$	(83,128)
Dividends on exchangeable preferred shares		**(10,200)**		(10,200)
Net loss attributable to common shareholders	**$**	**(73,608)**	$	(93,328)

The weighted average number of shares outstanding used in the computation of loss per share for the period ended September 30, 2012 was 62,230,562 (June 30, 2012 – 54,639,943). Outstanding stock options, warrants, and agent unit options have not been considered in the computation of diluted loss per share as the result is anti-dilutive.

16. SUPPLEMENTAL CASH FLOW INFORMATION

		Three Months Ended September 30, 2012		Three Months Ended September 30, 2011
Cash paid for:				
Interest	**$**	**8,897**	$	13,554
Income taxes		**–**		–
Non-cash investing and financing activities:				
Capital lease obligations recognized for assets under capital lease	**$**	**42,815**	**$**	**–**
Common shares issued for services		**–**		**–**

(Unaudited; Expressed in Canadian Dollars)

17. RELATED PARTY TRANSACTIONS AND BALANCES

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:

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

		Three Months Ended September 30, 2012		Three Months Ended September 30, 2012
Management fees (Notes 17(a) and (b))	**$**	**(60,000)**	$	(72,500)
Directors fees (Note 17(c))		**(9,000)**		(6,000)
Share-based payments (Note 17(c))		**(30,857)**		-
	$	**(99,857)**	$	(78,500)

(a) During the period ended September 30, 2012, the Company incurred management fees of $nil to the CEO of the Company (2011 – $26,250) and $30,000 to a company controlled by the CEO (2011 – $10,000). As at September 30, 2012, the Company owed $44,680 to the CEO and a company controlled by the CEO (2011 – $44,527), which is non-interest bearing, unsecured and due on demand.

(b) During the period ended September 30, 2012, the Company incurred management fees of $nil to the COO of the Company (2011 – $36,250) and $30,000 to a company controlled by the COO (2011 – $nil). As at September 30, 2012, the Company owed $65,875 to the COO and a company controlled by the COO (2011 – $45,050), which is non-interest bearing, unsecured and due on demand.

(c) During the period ended September 30, 2012, the Company granted nil and vested 500,000 stock options to directors and officers and key employees and incurred director fees of $9,000 to the independent directors of the Company (2011 – $6,000). As at September 30, 2012, the Company owed $50,000 to the independent directors (2011 – $89,000), which is non-interest bearing, unsecured and due on demand.

(d) During the period ended September 30, 2012, the Company paid consulting fees of $1,500 to a company controlled by an independent director of the Company (2011 – $4,500).

(e) During the period ended September 30, 2012, the Company incurred accounting fees of $25,000 to a company controlled by the CFO of the Company (2011 – $31,250). As at September 30, 2012, the Company owed $52,160 to this company (2011 - $35,692), which is non-interest bearing, unsecured and due on demand.

(f) During the period ended September 30, 2012, the Company incurred salaries and wages expense of $13,627 relatives of directors and officers of the Company (2011 – $34,583). As at September 30, 2012, the Company owed $16,346 to relatives of directors of the Company (2011 - $3,255), which is non-interest bearing, unsecured and due on demand.

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.

18. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS

(a) Fair Values of Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable, restricted term deposits, other assets, bank indebtedness, accounts payable, dividend payable, interest payable on convertible debentures, and due to related parties are reasonable estimates of fair values due to the relatively short periods to maturity and the commercial terms of these instruments. The carrying values of long-term debt, finance lease obligations and convertible debentures at September 30, 2012 are considered to be reasonable estimates of fair value based on current market rates for similar financial instruments.

(b) Fair Value Measurements

Certain of the Company's financial assets and liabilities are measured at fair value on a recurring basis and classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Certain non-financial assets and liabilities may also be measured at fair value on a non-recurring basis. There are three levels of the fair value hierarchy that prioritize the inputs to valuation techniques used to measure fair value, with Level 1 inputs having the highest priority. The levels and the valuation techniques used to value our financial assets and liabilities are described below:

Level 1 - Quoted Prices in Active Markets for Identical Assets
Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Cash equivalents, restricted term deposits and bank indebtedness, when applicable, are valued using quoted market prices. Accordingly, these items are included in Level 1 of the fair value hierarchy.

Level 2 - Significant Other Observable Inputs
Quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Derivative instruments are included in Level 2 of the fair value hierarchy as they are valued using pricing models or discounted cash flow models. These models require a variety of inputs, including, but not limited to, contractual terms, market prices, forward price curves, yield curves, and credit spreads. These inputs are obtained from or corroborated with the market where possible.

Level 3 - Significant Unobservable Inputs
Unobservable (supported by little or no market activity) prices.

(Unaudited; Expressed in Canadian Dollars)

18. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)

(b) Fair Value Measurements (continued)

Financial assets and liabilities measured at fair value on a recurring basis were presented on the Company's consolidated balance sheet as of September 30, 2012 as follows:

	Fair Value Measurements Using			
	Quoted Prices in Active Markets For Identical Instruments (Level 1) $	**Significant Other Observable Inputs (Level 2) $**	**Significant Unobservable Inputs (Level 3) $**	**Balance as Of September 30, 2012 $**
Assets:				
Cash and cash equivalents	27,494	–	–	27,494
Restricted term deposits	100,000	–	–	100,000
Liabilities:				
Bank indebtedness	98,545	–	–	98,545

(c) Financial Risks

(i) Credit Risk

Credit risk arises from the non-performance by counterparties of contractual financial obligations. The Company maintains substantially all of its cash and cash equivalents and term deposits classified as other assets in the balance sheet with major financial institutions. Deposits held with these institutions may exceed the amount of insurance provided on such deposits. As at September 30, 2012, the Company has significant accounts receivable from one major customer totalling $578,352 (June 30, 2012 - $299,105). The Company manages credit risk for trade and other receivables through established credit monitoring activities. As at September 30, 2012, the Company's maximum exposure to credit risk is the carrying value of cash and cash equivalents, accounts receivable and restricted term deposits.

The Company's concentration of, and past due, accounts receivable are summarized as follows:

	September 30, 2012		June 30, 2012	
	Over 90 days	**Total**	Over 90 days	Total
Provincial Liquor Boards	**$ -**	**$ 902,059**	$ -	$ 888,296
Total	**$ -**	**$ 902,059**	$ -	$ 888,296

(Unaudited; Expressed in Canadian Dollars)

18. FINANCIAL INSTRUMENTS, FAIR VALUE MEASUREMENTS AND FINANCIAL RISKS (continued)

(c) Financial Risks (continued)

(i) Credit Risk (continued)

The Company has a concentration of credit risk because a majority of its accounts receivable are from provincial liquor boards, under provincially regulated industry sale and payment terms. The Company is not exposed to significant credit risk as payment in full is typically collected by provincial liquor boards at the time of sale and receivables are with government agencies. While substantially all of the Company's accounts receivable are from provincial government liquor authorities, the timing of receipts of large balances may vary significantly from period to period.

(ii) Liquidity Risk

Liquidity risk arises from the Company's general and capital financing needs. The Company continuously monitors and reviews both actual and forecasted cash flows, and also matches the maturity profile of financial assets and liabilities, when feasible.

Contractual undiscounted cash flow requirements for financial liabilities as at September 30, 2012 are as follows:

	Less Than 1 Year $	Years 2 and 3 $	Years 4 and 5 $	More Than 5 Years $	Total $
Bank indebtedness	**98,545**	–	–	–	98,545
Accounts payable and accrued liabilities	**1,404,412**	–	–	–	1,404,412
Dividend payable	**193,800**	–	–	–	193,800
Interest payable on convertible debentures	**37,038**	–	–	–	37,038
Long-term debt	**842,100**	207,750	3,250	–	1,053,100
Finance lease obligations	**22,378**	67,404	12,970	–	102,752
Convertible debentures	**740,750**	–	–	–	740,750
	3,339,023	275,154	16,220	–	3,630,397

As at September 30, 2012, the Company had a working capital deficiency of $1,619,397.

(iii) Interest Rate Price Risk

Certain of the Company's long-term debt instruments, finance lease obligations and convertible debentures are subject to interest rate price risk as they carry fixed rates of interest. The Company's interest rate risk management policy is to purchase highly liquid investments with a term to maturity of three months or less on the date of purchase, when the instrument is not required as security for another financial obligation.

(iv) Interest Rate Cash Flow Risk

Certain of the Company's long-term debt instruments and bank indebtedness are subject to interest rate cash flow risk as they carry variable rates of interest. A plus or minus 1% change in market interest rates would not have a significant effect on the Company's loss and comprehensive loss for the year.

(Unaudited; Expressed in Canadian Dollars)

19. COMMITMENTS AND CONTINGENCIES

(a) The Company's future minimum operating lease payments for premises and vehicles for the next five years are as follows:

Fiscal Year		**Amount**
2013	$	219,850
2014		271,555
2015		251,754
2016		243,127
2017		256,720
	$	1,243,006

(b) As at September 30, 2012, the Company had issued a general excise bond of $55,000 in favour of the Minister of National Revenue of Canada.

(c) The Company has a bank operating line of credit with a limit of $100,000 which bears interest at prime, matures on October 16, 2012 and extended automatically on a quarterly basis, and is secured by a term deposit of $100,000 (see Note 7).

20. CAPITAL MANAGEMENT

The Company manages its capital structure in order to ensure sufficient resources are available to meet operational requirements. The Company is required to maintain term deposits of $100,000 (June 30, 2012 - $100,000) related to its bank line of credit (see Note 7). There are no other externally imposed capital requirements.

The Company seeks to manage capital to provide adequate funding for its operations while minimizing dilution for its existing shareholders. The Company's principal source of funds is from the issuance of common shares and warrants.

Management considers its shareholders' equity, long-term debt, finance lease obligations and convertible debentures as capital, which consists of the following:

		September 30, 2012		**June 30, 2012**
Long-term debt	**$**	**1,057,711**	$	1,071,719
Finance lease obligations		**90,628**		61,122
Convertible debentures		**716,419**		668,841
Shareholders' equity		**2,972,089**		3,335,839
	$	**4,836,847**	$	5,137,521

21. MAJOR CUSTOMER

During the period ended September 30, 2012, the Company had sales of $1,004,638 (2012 - $909,925) to the Manitoba Liquor Control Commission which accounted for 43% of its gross revenues (2011 - 41%).

22. SUBSEQUENT EVENT

a) Expiration of warrants

On November 4, 2012, 10, 402,500 warrants exercisable at $0.15 per share expired unexercised.

On November 4, 2012, 1,673,100 agent unit warrants exercisable at $0.08 per share expired unexercised.

b) Redemption of convertible debentures

On November 2, 2012, the Company announced that on November 5, 2012 (the “Redemption Date”), the Company will redeem its convertible debentures (the “Convertible Debentures”) maturing on November 5, 2012. The aggregate principal amount (the “Principal Amount”) of the Convertible Debentures currently outstanding is $531,000.00.

On the Redemption Date, the Company will redeem the whole of the Principal Amount of the Convertible Debentures by issuing fully paid and non-assessable common shares (the “Common Shares”) in the capital of the Company, at a price equal to $0.15 per Common Share (the “Redemption”). The Company is entitled to redeem the Convertible Debentures without any action required on the part of holders (the “Holders”) of the Convertible Debentures, including the surrender of any certificates. On the Redemption Date, the Company will allot and issue, as fully paid and non-assessable shares of the Company, an aggregate of 3,540,000 Common Shares to the Holders.

The securities issued pursuant to the Redemption will be subject to a hold period of four months and one day from the date of issue in compliance with applicable securities laws and the rules of the TSX Venture Exchange.