

Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Financial Statements

March 31, 2013 and 2012

(Unaudited, expressed in thousands of Canadian dollars)

Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Statements of Financial Position

(in thousands of Canadian dollars)

	Note	March 31, 2013 \$	December 31, 2012 \$
Assets			
Current assets:			
Cash		3,159	5,130
Accounts receivable		1,984	3,622
Inventory		149,694	146,710
Prepaid expenses and deposits		5,003	6,715
		159,840	160,177
Deferred tax assets		1,206	1,703
Property and equipment		42,997	43,527
Intangible assets		44,436	44,221
Goodwill		281,861	281,459
		530,340	533,087
Liabilities			
Current liabilities:			
Bank indebtedness		-	3,891
Accounts payable and accrued liabilities		27,598	38,464
Dividends payable to shareholders	4	2,066	2,063
Income tax payable		5,267	2,205
Derivative instrument	11	155	10
		35,086	46,633
Long-term debt		164,160	146,566
Deferred tax liabilities		16,171	22,138
		215,417	215,337
Shareholders' Equity			
Equity attributable to shareholders		314,889	317,658
Equity attributable to non-controlling interest		34	92
		314,923	317,750
		530,340	533,087

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

Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Statements of Changes in Equity

(in thousands of Canadian dollars)

	Attributable to Shareholders of the Company					Total	Non-controlling interest	Total equity
	Share capital	Equity component of convertible debentures	Contributed surplus	Accumulated other comprehensive income	Deficit			
	\$	\$	\$	\$	\$	\$	\$	\$
	(note 6)							
Opening balance – January 1, 2012	181,272	37	174,867	(3,174)	(35,887)	317,115	85	317,200
Net earnings for the period	-	-	-	-	2,300	2,300	106	2,406
Foreign currency translation adjustment	-	-	-	(1,168)	-	(1,168)	-	(1,168)
Comprehensive income for the period	-	-	-	(1,168)	2,300	1,132	106	1,238
Share-based payments	-	-	132	-	-	132	-	132
Exercise of share options	676	-	(36)	-	-	640	-	640
Dividends declared	-	-	-	-	(6,127)	(6,127)	-	(6,127)
Dividend reinvestment plan issuance	453	-	-	-	-	453	-	453
Dividends declared by subsidiaries	-	-	-	-	-	-	(153)	(153)
Transactions with owners	1,129	-	96	-	(6,127)	(4,902)	(153)	(5,055)
Balance – March 31, 2012	182,401	37	174,963	(4,342)	(39,714)	313,345	38	313,383
Opening balance – January 1, 2013	185,696	3,328	174,900	(4,505)	(41,761)	317,658	92	317,750
Net earnings for the period	-	-	-	-	1,426	1,426	31	1,457
Foreign currency translation adjustment	-	-	-	1,345	-	1,345	-	1,345
Comprehensive income for the period	-	-	-	1,345	1,426	2,771	31	2,802
Share-based payments (note 8)	-	-	53	-	-	53	-	53
Exercise of share options	105	-	(11)	-	-	94	-	94
Dividends declared (note 4)	-	-	-	-	(6,195)	(6,195)	-	(6,195)
Dividend reinvestment plan issuance (note 4)	508	-	-	-	-	508	-	508
Dividends declared by subsidiaries	-	-	-	-	-	-	(89)	(89)
Transactions with owners	613	-	42	-	(6,195)	(5,540)	(89)	(5,629)
Balance – March 31, 2013	186,309	3,328	174,942	(3,160)	(46,530)	314,889	34	314,923

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Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Statements of Earnings and Comprehensive Income

Three Months Ended March 31, 2013 and 2012

(in thousands of Canadian dollars)

	Note	March 31, 2013 \$	March 31, 2012 \$
Sales		136,302	126,636
Cost of sales		101,384	94,201
Gross margin		34,918	32,435
Operating and administrative expenses		28,426	25,486
Amortization		6,492	6,949
Property and equipment		2,031	1,751
Intangible assets		89	111
		4,372	5,087
Finance costs	3	2,394	1,840
Earnings before income taxes		1,978	3,247
Income tax expense	5	521	841
Net earnings		1,457	2,406
Other comprehensive income (loss)			
Items that may be reclassified subsequently to net earnings:			
Currency translation difference on foreign subsidiaries		1,345	(1,168)
Comprehensive income		2,802	1,238
Net earnings attributable to			
Owners of the parent		1,426	2,300
Non-controlling interest		31	106
		1,457	2,406
Comprehensive income attributable to			
Owners of the parent		2,771	1,132
Non-controlling interest		31	106
		2,802	1,238
Earnings per share			
Basic	7	0.06	0.10
Diluted	7	0.06	0.10

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

Liquor Stores N.A. Ltd.**Condensed Interim Consolidated Statements of Cash Flow****Three Months Ended March 31, 2013 and 2012***(in thousands of Canadian dollars)*

	Note	March 31, 2013 \$	March 31, 2012 \$
Cash provided by (used in)			
Operating activities:			
Net earnings for the period		1,457	2,406
Adjustments to reconcile net income to net cash flows from operating activities:			
Amortization of property and equipment		2,031	1,751
Amortization of intangible assets		89	111
Amortization of financing charges	3	82	110
Non-cash interest on convertible debentures	3	250	435
Fair value adjustment on derivative instrument	11	145	(590)
Deferred income tax		(5,445)	(1,383)
Share-based payments		53	132
Cash provided by operating activities before changes in non-cash working capital		(1,338)	2,972
Net change in non-cash working capital items		(6,966)	(4,077)
		(8,304)	(1,105)
Investing activities:			
Purchase of property and equipment		(1,370)	(970)
Purchase of intangible assets		(71)	(60)
		(1,441)	(1,030)
Financing activities:			
Proceeds (repayment) of bank indebtedness		(3,892)	2,223
Proceeds from long-term debt		17,262	5,103
Dividends paid	4	(5,690)	(5,670)
Proceeds received on exercise of stock-options		94	640
Dividends paid to non-controlling interest by subsidiaries		(89)	(153)
		7,685	2,143
Foreign exchange gain on cash held in foreign currency		89	10
Increase (decrease) in cash		(1,971)	18
Cash - Beginning of quarter		5,130	1,707
Cash - End of quarter		3,159	1,725

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

Liquor Stores N.A. Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

March 31, 2013 and 2012

(in thousands of Canadian dollars)

1 Nature of the business

Liquor Stores N.A. Ltd. (the “Company”) was incorporated under the Canada Business Corporations Act. The address of the Company’s registered office is 300, 10508 – 82 Avenue, Edmonton, Alberta. The Company’s common shares and convertible unsecured subordinated debentures trade on the Toronto Stock Exchange (the “TSX”) under the symbols “LIQ” and “LIQ.DB.A”.

The Company’s principal activity is the retailing of wines, beers and spirits. As at March 31, 2013, the Company operated 248 (2012 - 240) retail liquor stores, of which 180 (2012 - 174) were in Alberta, 36 (2012 - 35) were in British Columbia, 20 (2012 - 20) were in Alaska and 12 (2012 - 11) were in Kentucky. Of the stores operated, 206 (2012 - 205) were acquired and 42 (2012 - 35) were developed by the Company.

These condensed interim consolidated financial statements (the “financial statements”) were approved and authorized for issuance by the Board of Directors on May 6, 2013.

2 Basis of preparation and significant accounting policies

These condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34, Interim Financial Reporting and do not include all of the information required for full annual financial statements. Accordingly, these condensed interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto, for the year ended December 31, 2012.

The preparation of condensed interim consolidated financial statements requires management to make judgements, estimates, and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates. In preparing these interim financial statements, the significant judgements made by management in applying the Company’s accounting policies and the key sources of estimation uncertainty were the same as those that applied to the consolidated financial statements as at and for the year ended December 31, 2012.

The Company’s operations are seasonal in nature. Accordingly, sales will vary by quarter based on consumer spending behaviour. The Company is able to adjust certain variable costs in response to seasonal revenue patterns; however, costs such as occupancy are fixed, causing the Company to report a higher level of earnings in the third and fourth quarters. This business seasonality results in quarterly performance that is not necessarily indicative of the year’s performance.

The accounting policies applied by the Company in these interim financial statements are the same as those applied by the Company in its consolidated financial statements as at and for the year ended December 31, 2012, except as described below.

Changes in Accounting Policies

The Company has adopted the following new and revised standards, along with any consequential amendments, effective January 1, 2013. These changes were made in accordance with the applicable transitional provisions.

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March 31, 2013 and 2012

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International Financial Reporting Standard (“IFRS”) 13, *Fair Value Measurement* provides a single IFRS framework for measuring fair value. The standard defines fair value and sets out a fair value hierarchy that categorizes inputs used in valuation techniques into three levels: (1) quoted prices in active markets for identical assets or liabilities that can be accessed at the measurement date, (2) inputs other than quoted market prices included within level 1 that are either directly or indirectly observable and (3) unobservable inputs. The standard also outlines required disclosures regarding fair value measurements. This standard was adopted prospectively and did not require any measurement adjustments or adjustments to the valuation techniques employed by the Company to measure fair value.

Amendments to IAS 1, *Presentation of Financial Statements – Items of Other Comprehensive Income* addresses requirements for entities to group items presented in other comprehensive income based on whether they can potentially be reclassified to profit or loss subsequently. These changes did not result in any changes to other comprehensive income or comprehensive income.

IAS 28, *Investments in Associates and Joint Ventures* (as amended in 2011) applies to entities that have joint control or significant influence over an investee. The standard sets out the requirements for applying the equity method to investments in joint ventures and associates. Adoption of this standard did not result in any changes in the Company’s accounting policies.

IFRS 10, *Consolidated Financial Statements* replaces the guidance on control and consolidation in IAS 27 – Consolidated and Separate Financial Statements and SIC-12 – Consolidation, Special Purpose Entities and establishes exemptions for eligible investment entities from consolidating subsidiaries, measuring those investments at their fair value instead. The Company has determined that the adoption of IFRS 10 does not result in any change in the consolidation of any of its subsidiaries and investees.

3 Finance costs

Finance costs comprise the following:

	Three months ended March 31,	
	2013	2012
	\$	\$
Interest expense		
Bank indebtedness	108	308
Long-term debt ⁽ⁱ⁾	915	690
Convertible debenture ⁽ⁱⁱ⁾	1,237	1,411
Change in fair value of interest rate swap	145	(590)
Net loss (gain) on foreign exchange from financing activities	(11)	21
	2,394	1,840

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- i) Included in interest expense on long-term debt was amortization of deferred financing costs of \$82 (2012 - \$110).
- ii) Interest expense on the convertible debentures of \$1,237 (2012 - \$1,411) represents coupon interest of \$987 (2012 - \$976) and \$250 (2012 - \$435) pertaining to the impact of capitalized transaction costs and the accretion of the debt using the effective interest rate method.

4 Dividends

Dividends are determined in accordance with the Board of Directors periodic review of Company performance. During the three months ended March 31, 2013, the Company declared monthly dividends of \$0.09 per share or \$6,195 (2012 - \$0.09 per share or \$6,127). Dividends of \$6,192 (2012 - \$6,123) were paid during the period, of which \$508 (2012 - \$453) was paid in shares pursuant to the Company's dividend reinvestment plan. Dividends of \$2,066 were payable as at March 31, 2013 (2012 - \$2,046). Dividends are paid mid-month following the month of declaration.

Dividends were declared on April 15, 2013 in the amount of \$0.09 per common share and were paid to the holders of common shares as at the close of the record dates of April 30, 2013.

5 Income tax

Income tax is recognized based on management's estimate of the weighted average annual effective tax rate expected for the full financial year. The estimated average annual effective tax rate for 2013 is 26% (the effective tax rate for the year ended December 31, 2012 was 26%).

Income tax expense for the three months ended March 31, 2013 was \$564 (2012 - \$841), which includes current income tax expense of \$5,965, (2012 - \$2,224) and a deferred income tax recovery of \$5,401 (2012 - \$1,383).

During the first quarter of 2013, the Company received a notice of assessment and demand for payment from the State of Alaska Department of Revenue denying certain deductions from taxable income claimed in the 2008 through 2011 taxation years. The assessed tax, along with associated penalties and interest, totals approximately US\$855. Management is contesting the assessments and believes the Company's tax positions are well founded and that these assessments are unlikely to stand, and accordingly no provision has been recorded in the financial statements. The Company and its tax and legal advisors are currently preparing its appeal, which will be filed with the State of Alaska Department of Revenue prior to the deadline to do so (mid-May 2013). The assessed amounts are not required to be paid while the appeal is pending.

6 Share capital

- a) Authorized:

An unlimited number of voting common shares are authorized to be issued.

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(in thousands of Canadian dollars)

b) Issued and outstanding:

	#	\$
Balance – January 1, 2012	22,665,902	181,272
Exercised share options	41,250	640
Transfer from contributed surplus for share options exercised	-	36
Shares issued under dividend reinvestment plan	28,924	453
Balance – March 31, 2012	22,736,076	182,401
Balance – January 1, 2013	22,924,591	185,696
Exercised stock options	6,750	94
Transfer from contributed surplus for share options exercised	-	11
Shares issued under dividend reinvestment plan	27,551	508
Balance – March 31, 2013	22,958,892	186,309

7 Earnings per share

	Three months ended March 31,	
	2013	2012
	\$	\$
Net earnings attributable to owners of the parent	1,426	2,300
	2013	2012
	#	#
Weighted average number of common shares outstanding – Basic	22,938,643	22,682,213
Effect of dilutive securities		
Equity-settled share-based payment awards	43,904	17,693
Weighted average number of common shares outstanding - Diluted	22,982,547	22,699,906
	2013	2012
	\$	\$
Basic earnings per share	0.06	0.10
Diluted earnings per share	0.06	0.10

For the three months ended March 31, 2013, potential shares issuable in exchange for 267,750 (2012 – 543,750) equity-settled share options have been included in the diluted earnings per share calculation. Due to their anti-dilutive effect, the potential shares issuable in exchange for convertible debentures were not included in the diluted earnings per share calculation for the three months ended March 31, 2013 and March 31, 2012.

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8 Share-based payments

On March 28, 2013, the Company adopted a new incentive award plan comprised of restricted awards and performance awards for employees of the Company. Restricted awards are subject to service conditions and performance awards are subject to both service conditions and corporate performance measures. Restricted awards and performance awards issued under the incentive award plan are granted at the discretion of the Company's Board of Directors.

Incentive award plan units vest over three years, one third of each of the first, second and third anniversaries of the grant date and are settled in cash calculated based on the volume weighted average share price of the Company for the five days immediately preceding the vesting date. Incentive Awards are accounted for as an employee benefit, the liability for which is revalued at each balance sheet date using the weighted average price of the Company's shares for the immediately preceding five days.

During the period ended March 31, 2013, the company granted 10,649 restricted share units with a value of \$192, and recognized \$1 in compensation expense (2012 - \$nil). No performance share units were awarded during the period.

9 Related party transactions

The following transactions were carried out with related parties:

Operating and administrative expenses

	Three months ended March 31,	
	2013	2012
	\$	\$
Professional fees ⁽ⁱ⁾	38	51
Rent expense ⁽ⁱⁱ⁾	117	146
	155	197

⁽ⁱ⁾ A Director of the Company is a partner in a law firm to which the Company incurred professional fees for legal services.

⁽ⁱⁱ⁾ The Company paid rent to entities controlled by a Director of the Company.

These operating and administrative expenses are incurred in the normal course of business at terms similar to those applicable to unrelated parties.

There was \$2 included in accounts payable and accrued liabilities (December 31, 2012 - \$nil) relating to these transactions.

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10 Supplementary disclosure of cash flow information

Changes in non-cash working capital items comprise the following:

	2013	2012
	\$	\$
Accounts receivable	1,647	(284)
Inventory	(2,104)	1,878
Prepaid expenses and deposits	1,732	364
Accounts payable and accrued liabilities	(11,301)	(8,243)
Income tax payable	3,060	2,208
	(6,966)	(4,077)

Interest and income taxes paid are included in cash flows from operating activities in the Statement of Cash Flows.

	2013	2012
	\$	\$
Interest paid	1,917	998
Income taxes paid	2,904	-

11 Fair value of financial instruments

- a) Financial instruments measured at fair value

Fair value hierarchy

Financial instruments recognized on the balance sheet at fair value are classified in a hierarchy based on the significance of the estimates used in their measurement, as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 – Inputs for the asset or liability that are not based on observable market data.

The only instrument recognized at fair value is the interest rate swap, which is a level 2 measurement. There have been no transfers of instruments between levels in the hierarchy.

The fair values of interest rate swaps are calculated as the net present value of the future cash flows expected to arise on the variable and fixed legs, determined using observable yield curves at each measurement date.

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b) Financial instruments measured at other than fair value

Financial assets that are valued at other than fair value on the consolidated statements of financial position include cash and accounts receivable. The carrying value less impairment provision of trade receivables approximates fair value at March 31, 2013 and March 31, 2012 due to the short-term nature of the instruments.

Financial liabilities that are valued at other than fair value are comprised of bank indebtedness, accounts payable and accrued liabilities, dividends payable to shareholders, and long-term debt.

The carrying value of trade payables and dividends payable approximates their fair value due to the short-term nature of the instruments. The carrying value of bank indebtedness and long-term debt approximates the fair value, as the interest rate affecting these instruments is at a variable market rate. Debentures with a carrying value of \$67,500 have a fair value of \$72,225, determined based on market trading values at the balance sheet date.

12 Operating segments

The Company has two reportable segments: Canadian Operations and US Operations. Segmentation is based on differences in the regulatory environments of Canada and the US and reflects the basis on which management measures performance and makes decisions regarding the allocation of resources. Both segments operate retail liquor stores in their respective jurisdictions.

Financial information regarding the results of each reportable segment is included below. Performance is measured based on operating margin, which is defined as earnings before amortization, finance costs and income tax expense (recovery), as included in the internal management reports that are reviewed regularly by the Company's Interim Chief Executive Officer (the Company's chief operating decision maker) and follow the organization, management and reporting structure of the Company. Operating margin is one of the primary benchmarks used by management to evaluate the performance of its operating segments. A reconciliation of operating margin to earnings before income taxes, an earnings measure used in the Company's Consolidated Statement of Earnings and Comprehensive Income, has been included in the table below.

Operating margin is not an earnings measure recognized by IFRS and does not have a standardized meaning prescribed by IFRS. Therefore, operating margin may not be comparable to similar measures presented by other issuers. Investors are cautioned that operating margin should not be construed as an alternative to earnings before income tax as determined in accordance with IFRS, as an indicator of performance or as an alternative to cash flows from operating, investing and financing activities as a measure of liquidity and cash flows.

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(in thousands of Canadian dollars)

	March 31, 2013		
	Canadian Operations \$	US Operations \$	Consolidated \$
Sales to external customers	104,025	32,277	136,302
Operating margin	5,338	1,154	6,492
Property and equipment amortization			2,031
Intangible asset amortization			89
Finance costs			2,394
Earnings before income taxes			1,978
Other information			
Expenditures for additions to			
Property and equipment	952	354	1,306
Intangible assets	66	5	71
Total assets at December 31, 2012	451,496	78,844	530,340
	March 31, 2012		
	Canadian Operations \$	US Operations \$	Consolidated \$
Sales to external customers	95,140	31,496	126,636
Operating margin	5,561	1,388	6,949
Property and equipment amortization			1,751
Intangible asset amortization			111
Finance costs			1,840
Earnings before income taxes			3,247
Other information			
Expenditures for additions to			
Property and equipment	605	365	970
Intangibles	57	3	60
Total assets at March 31, 2012	429,239	71,525	500,674