



AUTOMODULAR CORPORATION

ANNUAL REPORT 2002



*Financial Highlights*

	<b>12 months ended December 31, 2002 (000's)</b>	12 months ended December 31, 2001 (000's)
Sales	\$ 55,919	\$ 52,934
Earnings before income tax	6,755	6,537
Net earnings	4,640	4,344
Net earnings per share	0.25	0.29
Total assets	45,082	48,111
Shareholders' equity	38,520	38,689

*Contents*

Our Business	2
To Our Shareholders	3
Management's Discussion and Analysis	4
Operations Overview	6
Management's Responsibility for Financial Information	7
Auditors' Report	8
Consolidated Balance Sheets	9
Consolidated Statements of Retained Earnings	10
Consolidated Statements of Earnings	10
Consolidated Statements of Cash Flows	11
Notes to Consolidated Financial Statements	12
Investor Information	19
Corporate Information	20

## *Our Business*

---

Our business is the sequencing and sub-assembly of modules of automobile parts for installation in cars and trucks being assembled by our customers. By sequencing, we mean that the sub-assembled modules, such as an instrument panel or a radiator support, arrive at the customer's final assembly plant in precisely the sequence of their final installation in the vehicle, and at precisely the time they are to be installed.

All of our business is contract business. We bid on contracts to sub-assemble particular commodities for particular vehicles at a time prior to the launch of the vehicle design. From the moment the first vehicle rolls down the assembly line until the last one of that particular design, our company ships one of each sub-assembly we are sequencing for that vehicle to the customer for each vehicle being assembled. We receive orders every 5 seconds. We ship completed assemblies typically within 120 minutes of receiving the respective order. We are an integral part of the supply chain and fundamental to the cost-efficient final assembly of vehicles.

Our success is determined by three parameters. We must deliver modules that meet the quality requirements of our customers and of their customers. We must deliver them on time, every time. And, we must deliver them at a cost that makes it more profitable for our customers to use our services than to do the same work themselves.

As a result of the foregoing, our growth comes in lumps. Our contracts are typically for 3 to 5 years. Our growth arises from new contracts.

## *To Our Shareholders*

---

2002 was an excellent year for Automodular Corporation (“Automodular”). Net income was higher in a difficult competitive environment. During the year, Automodular achieved two milestones. One was the completion of QS-9000 certification of all of its facilities, and the other was the acquisition of a company which would not only add to Automodular’s sales and profits, but would also provide synergies for enhancing future growth for the combined operations. This milestone was reached with the acquisition of Tec-Mar Distribution Services, Inc. (“Tec-Mar”), which closed in early 2003.

The Tec-Mar acquisition broadens and strengthens Automodular. It will more than double our annual sales and will make a meaningful contribution to net income and cash flow. More importantly, it brings to Automodular a cadre of competent professionals with deep automotive sequencing experience complementary to our existing staff.

Our combined operations are now poised for enhanced growth. We have the managerial and financial resources to take on increased volumes of business and a reputation in Canada and the United States as a strong and reliable supplier. Our combined operations supply over 15 million modules annually to eight final assembly plants.

Our numbers are impressive. We now employ more than 1,000 personnel. We operate more than 1.5 million square feet of plant. We will supply over \$8 billion of content for over 1.7 million vehicles each year. Every day, hundreds of trucks leave our plants to deliver high-quality modules sequenced to the final car and truck assembly plants we serve. Typically, we ship our modules within 90-120 minutes of receipt of the orders for the components, a truly “Just-in-Time” accomplishment. Each shipment meets tight time windows and exacting quality requirements, providing our customers with increased productivity and reduced final assembly costs.

The automotive business is extremely competitive. Vehicle assembly plants must drive down costs to survive, while delivering the increasingly high quality consumers demand. With final assembly costs typically less than 10% of total vehicle costs, our customers must rely on suppliers’ productivity and diligence to achieve competitive vehicle costs and quality. At Automodular Corporation, we embrace this challenge. We work closely with our customers to find new and innovative ways to reduce costs and to share the benefits with our customers. Our quality goal is simple – zero defects. Our cost goal is similarly simple – to provide the most cost-effective sequencing and sub-assembly services possible.

On behalf of the board of directors.

“Michael F. Blair”

Michael F. Blair  
President

## Management's Discussion and Analysis

The Company and its representatives periodically make written and oral statements, including those contained in the Annual Report and Management's Discussion and Analysis, which may pertain to the Company or the environment in which Automodular operates. These statements should be read in conjunction with the Consolidated Financial Statements and the accompanying notes.

By their nature, forward-looking statements are subject to risks and uncertainties, which could result in actual performance or conditions being materially different from anticipated results. Readers should not place undue reliance on these forward-looking statements when making decisions and should consider the date on which the statements were made. Except as required by applicable securities law, management disclaims any intention or obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

### OVERVIEW

Automodular Corporation is a sequencer and sub-assembler of modules that are installed in cars and trucks assembled by General Motors at plants in Canada and the United States. Following the acquisition of Tec-Mar Distribution Services, Inc. in January 2003, Automodular now operates through three plants in Canada and five in the United States employing more than 1,000 people. The following information does not reflect financial results for Tec-Mar.

### SALES AND NET INCOME

Automodular Corporation's net sales for the year ended December 31, 2002 were \$56 million—an increase of \$3 million, or 6% over the year ended December 31, 2001. Net income was \$4.6 million or \$0.25 per share, versus \$4.3 million or \$0.29 per share in the prior year, owing to more shares outstanding in 2002. Automodular's 2002 income statement ratios compare to 2001 as follows:

	2002	2001
Sales	100.0%	100.0%
Operating income	15.8%	16.7%
Other income	2.3%	3.4%
Depreciation and amortization	6.0%	6.7%
EBIT	12.2%	13.4%
Interest expense	0.1%	1.0%
Income tax	3.8%	4.1%
Net income	8.3%	8.2%

### OPERATING INCOME

Operating income declined from 16.7% of sales to 15.8% of sales as a result of contractual price declines and annual wage rate increases, which could not be fully offset by productivity improvements. Automodular generally shares productivity gains with its customer by reducing prices by an amount equal to two-thirds of cost improvement realized.

### OTHER INCOME

Other income declined by 1.1% of sales, reflecting lower securities gains. Automodular no longer maintains an investment portfolio, and does not expect material amounts of other income in future years.

### DEPRECIATION AND AMORTIZATION

Depreciation and amortization declined from 6.7% of sales in 2001 to 6.0% of sales in 2002. These expenses are expected to rise in 2003 owing to higher capitalized expenditures in 2002 than in 2001. The higher capitalized expenditures arose in part from the move from two Pickering locations to the newly constructed Whitby plant, which took place in January 2002.

### EARNINGS BEFORE INTEREST AND TAX

2002 EBIT of 12.2% was down slightly from 13.4% in 2001. Lower depreciation and amortization expense did not fully offset lower margin ratios.

**INTEREST EXPENSE**

Automodular eliminated bank indebtedness during 2002, resulting in lower interest charges. Automodular borrowed approximately \$17.5 million in early 2003 to fund the Tec-Mar acquisition, and expects commensurately higher interest charges in 2003.

**INCOME TAXES**

Income tax ratios fell in 2002 as a result of lower tax rates and a larger mix of non-taxable gains included in other income. Automodular expects 2003 income tax rates to be slightly lower than 2002 on operating income, but anticipates no material amounts of non-taxable gains.

**NET INCOME**

Net income as a percentage of sales grew to 8.3% in 2002 from 8.2% in 2001. For 2003, Automodular expects this ratio to decline as a result of the consolidation of the lower-margin Tec-Mar acquisition and the absence of any material amounts of non-operating income. On a pro forma basis, net income as a percentage of sales would have been 5.5% in 2002 had Tec-Mar been consolidated throughout that year.

**LIQUIDITY AND CAPITAL RESOURCES**

\$11.0 million cash was generated from operating activities in the current fiscal period compared to \$4.7 million in 2001, largely as a result of improved management of non-cash working capital. At year end, the Corporation had \$18 million cash or equivalent on hand. However, the Tec-Mar acquisition in early 2003 consumed approximately \$36.8 million cash, funded by the usage of available cash and a \$17.5 million term loan. The Corporation also has a \$5 million operating line and believes it has sufficient liquidity to meet all plans and programs contemplated for 2003, while continuing to pay regular quarterly dividends.

**CAPITAL EXPANSION**

In the current period, the Company expended \$3.2 million on capital and other assets, compared to \$1.9 million in the prior period. The increased capital outlays reflect the capitalized costs arising from the consolidation of two Pickering plants in the new Whitby plant in January 2002.

**DIVIDENDS**

Dividends paid in the current year were \$5.3 million compared with \$6.8 million in the prior period. The Directors of Automodular approved a policy of paying regular quarterly dividends and set the current rate at \$0.28 annually. Automodular's operations are expected to generate sufficient cash flow to fund this dividend while meeting all operating requirements and the terms of the Corporation's banking agreements.

**EQUITY**

Shareholders' equity remained unchanged at \$39 million, reflecting the Corporation's dividend policy.

**OUTLOOK**

The automotive parts industry faces lower volumes in 2003. The Tec-Mar acquisition broadens and strengthens Automodular as it will more than double our annual sales and will make a meaningful contribution to net income and cash flow despite the industry slowdown. The Company's balance sheet reflects management's judgment on the valuation of the assets, and management feels the Company is poised for further growth through expansion of its automotive parts sub-assembly and sequencing operations and other opportunistic acquisitions in the automotive sector. The capital requirements for any expansion will be met initially through internally generated funds and selectively through issuance of additional shares.

As set out in Note 15 to the Corporation's financial statements, the Corporation has prepared a pro forma income statement as though the Tec-Mar acquisition had taken place January 1, 2002. This analysis provides a benchmark for investors to analyze the impact of this acquisition. The pro forma shows Automodular would have earned \$6.5 million or \$0.35 per share on sales of \$120 million in 2002 had Tec-Mar been included. Management believes the combined operations in 2003 will be more profitable than the pro forma 2002 results, tempered somewhat by the soft automotive market environment.

## Operations Overview

---

### **AUTOMODULAR ASSEMBLIES INC. ("AAI")**

Sales for the consolidated Automotive Division in 2002 were \$56 million, compared to \$53 million in 2001. Sales for both years include U.S. operations expressed in Canadian dollars.

In 2002, Canadian operations provided sequenced and sub-assembled components for 868,000 Canadian-built vehicles, compared with 782,000 vehicles the prior year. New Castle, Delaware serviced 99,000 vehicles versus 103,000 in 2001. 2002 was very active, with short-term shutdowns that impacted the New Castle operation being offset by substantial truck and car plant overtime, as well as the introduction of third shift production at GM Oshawa Car Plant 1. The third shift necessitated the hiring and training of 65 additional staff and was accomplished in the third quarter.

The consolidation project, which resulted in AAI's move into its 183,000 square foot facility in Whitby, started up fully operational on January 2, 2002. It was impressively executed and continues to meet expectations.

Major operating initiatives during the year in both Canada and New Castle were focused on productivity improvements and the resultant gain-sharing with our major customer. In New Castle, a successful productivity review was undertaken on the cockpit assembly operations, and plans are to continue the process through the remaining assembly operations. In Canada, an even larger productivity review utilizing General Motors "Global Manufacturing System" is underway at our Whitby facility. The GMS principles focus on people involvement, standardization, built-in quality, shortened lead times and continuous improvement. We intend to continue this process throughout the entire operation. We are confident this major initiative will result in AAI becoming a world class sub-assembler/sequencer to General Motors.

The acquisition of Tec-Mar Distribution Services, Inc. in January 2003, increases our staff levels to over 1,000 employees in eight plants, serving eight General Motors assembly plants (representing one-third of GM North American production). It provides exciting opportunities from an operating viewpoint. Because of the many operating similarities, management can perform best practices reviews and adopt the most efficient and quality-effective methods. Another significant benefit is in the area of customer relations. Tec-Mar has a large Tier 1 customer base and new relationships allow AAI to expand its contacts and assist efforts to seek more complex sub-assembly contracts.

AAI management continues to concentrate on quality initiatives and maintaining QS-9000 standards. We have been audited at all locations and continue to meet and exceed customer supplier metrics.

## *Management's Responsibility for Financial Information*

---

The accompanying consolidated financial statements and all information contained in this report were prepared by and are the responsibility of management. The statements were prepared in accordance with Canadian generally accepted accounting principles and include management's best judgments and estimates. Where alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances. Financial information presented elsewhere in this report is consistent with that in the financial statements.

The company maintains a system of internal controls which provides management with reasonable assurance that financial information is relevant, reliable and accurate, and that the company's assets are properly accounted for and adequately safeguarded.

The consolidated financial statements have been audited by the independent external auditors appointed by the shareholders, Smith, Nixon & Co. LLP. In that capacity they have examined and reported on the consolidated financial statements for the years ended December 31, 2002 and 2001. The Audit Committee of the Board of Directors has reviewed the consolidated financial statements with management and the external auditors and has recommended their approval by the Board of Directors.

"Michael F. Blair"

Michael F. Blair  
President  
Toronto, Ontario  
February 21, 2003

## Auditors' Report

---

### TO THE SHAREHOLDERS OF AUTOMODULAR CORPORATION

We have audited the consolidated balance sheets of Automodular Corporation as at December 31, 2002 and 2001 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

**TORONTO, ONTARIO**

February 21, 2003

*Smith, Nipon & Co. LLP*

**CHARTERED ACCOUNTANTS**

# Consolidated Balance Sheets

as at December 31, 2002 and 2001

	2002	2001 <i>Restated</i>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash	\$ 18,310,248	\$ 19,462,922
Investments (trading value \$442,992; 2001 – \$277,209)	273,299	273,570
Receivables ( <i>Note 2</i> )	2,504,039	5,203,677
Prepaid expenses	2,288,571	1,875,852
Income taxes receivable	1,108,142	64,197
Current portion of loans receivable ( <i>Note 3</i> )	–	450,715
	<u>24,484,299</u>	<u>27,330,933</u>
<b>LONG-TERM INVESTMENTS</b>	283,268	417,344
<b>LOANS RECEIVABLE</b> ( <i>Note 3</i> )	–	31,765
<b>FUTURE INCOME TAXES</b> ( <i>Note 10</i> )	–	481,770
<b>CAPITAL ASSETS</b> ( <i>Note 4</i> )	6,663,247	7,661,851
<b>OTHER ASSETS</b> ( <i>Note 5</i> )	13,651,635	12,187,432
	<u>\$ 45,082,449</u>	<u>\$ 48,111,095</u>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued liabilities	\$ 5,812,215	\$ 4,249,691
Current portion of long-term liabilities ( <i>Note 7</i> )	–	3,092,800
	<u>5,812,215</u>	<u>7,342,491</u>
<b>FUTURE INCOME TAXES</b> ( <i>Note 10</i> )	749,909	–
<b>ACCRUED PENSION COST</b> ( <i>Note 12</i> )	–	88,700
<b>LONG-TERM LIABILITIES</b> ( <i>Note 7</i> )	–	1,991,000
	<u>6,562,124</u>	<u>9,422,191</u>
Contingencies and Commitments ( <i>Note 13</i> )		
<b>SHAREHOLDERS' EQUITY</b>		
<b>CAPITAL STOCK</b> ( <i>Note 8</i> )	39,613,186	39,148,986
<b>DEFICIT</b>	(1,092,861)	(460,082)
	<u>38,520,325</u>	<u>38,688,904</u>
	<u>\$ 45,082,449</u>	<u>\$ 48,111,095</u>

Signed on behalf of the Board

“Michael F. Blair”

Director

“Alan R. Marchment”

Director

## Consolidated Statements of Retained Earnings

Years ended December 31, 2002 and 2001

	2002	2001 <i>RESTATED</i>
<b>BALANCE – BEGINNING OF YEAR</b>	\$ (460,082)	\$ 1,972,979
Net earnings for the year	4,639,910	4,344,281
Cash dividends	(5,272,689)	(6,777,342)
<b>BALANCE – END OF YEAR</b>	<u>\$ (1,092,861)</u>	<u>\$ (460,082)</u>

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

## Consolidated Statements of Earnings

Years ended December 31, 2002 and 2001

	2002	2001 <i>RESTATED</i>
<b>SALES</b>	\$ 55,919,009	\$ 52,933,898
<b>COST OF SALES AND OTHER EXPENSES</b>	47,063,614	44,104,277
<b>EARNINGS FROM OPERATIONS BEFORE THE FOLLOWING</b>	<u>8,855,395</u>	<u>8,829,621</u>
Amortization	3,351,959	3,546,669
Interest expense	42,452	552,185
Other income ( <i>Note 9</i> )	(1,294,506)	(1,805,830)
	<u>2,099,905</u>	<u>2,293,024</u>
<b>EARNINGS BEFORE INCOME TAXES</b>	6,755,490	6,536,597
<b>INCOME TAXES</b> ( <i>Note 10</i> )	<u>2,115,580</u>	<u>2,192,316</u>
<b>NET EARNINGS FOR THE YEAR</b>	<u>\$ 4,639,910</u>	<u>\$ 4,344,281</u>
<b>Earnings per share</b>		
Basic	<u>\$ 0.25</u>	<u>\$ 0.29</u>
Fully diluted	<u>\$ 0.25</u>	<u>\$ 0.29</u>
Weighted average common shares outstanding	11,829,359	11,162,764
Exchangeable Class X shares ( <i>Note 8 (e)</i> )	7,000,000	3,720,548
Basic weighted average common shares outstanding	<u>18,829,359</u>	<u>14,883,312</u>
Basic weighted average common shares outstanding	18,829,359	14,883,312
Incremental shares from stock options and warrants	106,647	155,805
Fully diluted weighted average common shares outstanding	<u>18,936,006</u>	<u>15,039,117</u>

# Consolidated Statements of Cash Flows

Years ended December 31, 2002 and 2001

	2002	2001 <i>RESTATED</i>
<b>CASH PROVIDED BY (USED IN)</b>		
<b>OPERATIONS</b>		
Net earnings for the year	\$ 4,639,910	\$ 4,344,281
Items not involving current cash flows <i>(Note 11)</i>	3,594,967	3,134,650
Net change in non-cash working capital <i>(Note 11)</i>	2,805,769	(2,738,032)
	<u>11,040,646</u>	<u>4,740,899</u>
<b>INVESTING ACTIVITIES</b>		
Purchase of capital and other assets	(3,162,882)	(1,897,113)
Proceeds on disposal of capital and other assets	1,012,989	52,710
Funding of pension plan	(1,577,400)	-
Proceeds on disposal of long-term investments	990,915	1,782,147
Repayment on long-term receivable	-	107,696
Repayment of loans receivable	422,297	202,358
	<u>(2,314,081)</u>	<u>247,798</u>
<b>FINANCING ACTIVITIES</b>		
Issue of common shares	464,200	992,800
Issue of Class X shares by a subsidiary <i>(Note 8(e))</i>	-	20,847,948
Repayment of bank indebtedness	-	(2,000,000)
Repayment of long-term liabilities	(5,070,750)	(3,535,200)
Cash dividends paid	(5,272,689)	(6,777,342)
	<u>(9,879,239)</u>	<u>9,528,206</u>
<b>CHANGE IN CASH</b>	(1,152,674)	14,516,903
<b>CASH – BEGINNING OF YEAR</b>	19,462,922	4,946,019
<b>CASH – END OF YEAR</b>	<u>\$ 18,310,248</u>	<u>\$ 19,462,922</u>

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Principles of Consolidation

The consolidated financial statements include the accounts of Automodular Corporation and its wholly owned subsidiaries (the "Company") and have been prepared following Canadian generally accepted accounting principles.

### Use of Estimates

The preparation of consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

### Financial Instruments and Risk Management

The carrying value of cash, short-term investments, receivables, income taxes receivable, accounts payable and accrued liabilities are considered to be representative of their respective values due to their short-term nature.

The fair value of long-term financial instruments approximate carrying values since actual rates approximate market rates.

### Investments

Short-term investments are recorded as current assets and are carried at the lower of cost or trading value.

Long-term investments in which the Company has significant influence but not control, are accounted for by the equity method. Other long-term investments are carried at cost less any write-downs for impairments that are other than temporary.

### Capital Assets

Capital assets are stated at cost and are amortized on the diminishing balance method at annual rates ranging from 20% to 40%. Open projects are assets not currently available for use and will be reclassified to their appropriate classification upon project completion.

### Acquisition Costs

Acquisition costs are capitalized and amortized on a straight-line basis over 5 years.

### Deferred Contract Costs

Costs incurred in establishing new production lines and facilities which require substantial time to reach commercial production capability are capitalized. In addition, contract costs incurred which provide a future benefit over the life of the contract are capitalized. Amortization of these costs is provided over the remaining life of the contract, commencing on the date commercial production is achieved.

### Goodwill

Goodwill represents the excess of the purchase price of the Company's interest in subsidiary entities over the fair value of the underlying net identifiable tangible and intangible assets arising on acquisition.

Commencing January 1, 2002 the Company adopted the Canadian Institute of Chartered Accountants (CICA) new recommendations under Handbook Section 3062 "Goodwill and Other Intangible Assets" and Handbook Section 1581 "Business Combinations" which were issued in 2001.

The new standards require non-amortization of existing and future goodwill and intangible assets that meet the criteria for indefinite life. Since goodwill is no longer amortized, the Company must determine at least once annually whether the fair value of the existing goodwill and intangible assets has been permanently impaired. Any permanent impairments are then recorded as a separate charge against earnings and a reduction of the carrying value of goodwill and intangible assets. Upon adoption of the new Sections, the Company evaluated the carrying value of its goodwill and intangible assets and determined that no write-down was necessary.

If the Company had retroactively adopted the accounting policy change of not amortizing goodwill, net earnings for the year ended December 31, 2001 would have been increased by \$382,484. Basic and diluted earnings per share would have increased by \$0.03 to \$0.32 per share from \$0.29 per share.

### Pension Plans

The Company has both defined contribution and defined benefit pension plans. The costs of defined contribution pension plans, representing the Company's required contribution, and the costs of defined benefit pension plans, determined based on the actuarial present value of future expected benefits attributed to the period, are charged to earnings in the period. Adjustments arising from plan amendments, experience gains and losses and changes in actuarial assumptions are amortized to earnings over the expected average remaining service lives of the respective employees.

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## Foreign Exchange

Monetary assets and liabilities are translated at the rate of exchange in effect at the balance sheet date. Other assets and liabilities and revenue and expense transactions are translated at the actual rates of exchange in effect at the time of the transaction. In 2001, exchange gains and losses were included in income except for currency translation adjustments relative to long-term monetary items with a fixed and ascertainable life which were deferred and amortized on a straight-line basis over the life of the item.

In August 2001, the CICA amended Handbook Section 1650 "Foreign Currency Translation" (the "Section") to eliminate the deferral and amortization of foreign currency translation gains and losses on long-term monetary items, effective January 1, 2002. As required by the amended Section, the Company has retroactively restated all comparative information. As a result, the Company reduced other assets by \$242,070 with a corresponding increase in opening deficit as of January 1, 2002. The Company's earnings for the year ended December 31, 2001 has been decreased by \$286,870 (\$0.02 per share) and retained earnings as at January 1, 2001 was increased by \$44,800.

## Income Taxes

The Company uses the liability method of tax allocation for accounting for income taxes. Under the liability method of tax allocation, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

## Adoption of New Accounting Standard for Earnings per Share

During 2001, the Company adopted the new CICA recommendations for the calculation of earnings per share. Under the new accounting policy, the calculation of diluted earnings per share requires the use of the treasury method and assumes any option or warrant proceeds would be used to purchase common shares at the average market price during the period.

## Stock-Based Compensation

In December 2001, the CICA issued Handbook Section 3870 "Stock-Based Compensation and Other Stock-Based Payments." Effective for the Company's fiscal year beginning January 1, 2002, the new Section requires the use of a fair-value based approach of accounting for certain specified stock-based awards. For all other employee stock-based awards, the Section encourages but does not require that a fair-value based approach be used.

The Company records no expense when it issues options. Accordingly, the Section requires that the Company disclose pro forma net earnings and earnings per share data as if the fair-value based approach were used for options granted in 2002.

## 2. RECEIVABLES

	2002	2001
Trade	\$ 2,483,081	\$ 4,885,207
Other	20,958	318,470
	<u>\$ 2,504,039</u>	<u>\$ 5,203,677</u>

The Company, in the normal course of business, is exposed to credit risk from its customers—all of which are in the automotive industry. These accounts receivable are subject to normal industry credit risks. As at December 31, 2002, 91% (2001 – 91%) of trade receivables were due from General Motors Corporation.

The Company has long-term contracts with General Motors Corporation. Substantially all of its sales are made to General Motors Corporation.

## 3. LOANS RECEIVABLE

The Company has made interest-bearing and interest-free loans to an officer and senior employees in connection with the employee stock purchase plan. All stock purchase loans must be repaid within ten years of inception or earlier at the option of the Company upon the termination, retirement or death of a plan member.

	2002	2001
Interest-free loans to senior employees, repayable from dividends in respect of the shares. As at December 31, 2001 the loans were secured by 7,958 common shares of the Company having a trading value of \$31,036. During 2002, \$1,407 was repaid and the balance of \$30,358 was cancelled.	\$ –	\$ 31,765
Interest-bearing loan to an officer with interest equal to the dividends paid in respect of the shares. As at December 2001 the loan was secured by 100,000 common shares of the Company having a trading value of \$390,000. During 2002, \$420,890 was repaid and the balance of \$29,825 was cancelled.	–	450,715
	–	482,480
Deduct: Current portion	–	450,715
	<u>\$ –</u>	<u>\$ 31,765</u>

During 2002, \$422,297 (2001 – \$202,358) was repaid on the interest-free loans.

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## 4. CAPITAL ASSETS

	2002			2001
	Cost	Accumulated Amortization	Net	Net
Land, buildings and leasehold improvements	\$ 5,428,112	\$ 2,360,588	\$ 3,067,524	\$ 3,271,161
Manufacturing equipment	5,710,733	3,903,571	1,807,162	1,894,115
Other equipment and furniture	2,460,438	1,478,683	981,755	1,040,097
Open projects	806,806	-	806,806	1,456,478
	<u>\$ 14,406,089</u>	<u>\$ 7,742,842</u>	<u>\$ 6,663,247</u>	<u>\$ 7,661,851</u>

## 5. OTHER ASSETS

	2002			2001
	Cost	Accumulated Amortization	Net	Net
Goodwill	\$ 23,474,542	\$ 14,060,353	\$ 9,414,189	\$ 9,414,189
Acquisition costs	266,147	266,147	-	48,795
Deferred contract costs	8,271,073	5,355,427	2,915,646	2,724,448
Pension fund asset (Note 12)	1,321,800	-	1,321,800	-
	<u>\$ 33,333,562</u>	<u>\$ 19,681,927</u>	<u>\$ 13,651,635</u>	<u>\$ 12,187,432</u>

## 6. CREDIT FACILITIES

The Company has available to it a revolving credit facility with a limit of \$2,000,000. It is secured by the Company's present and future assets, properties and undertakings. Interest is calculated at the bank's prime rate of interest plus ¾%. The effective interest rate at December 31, 2002 was 5.25% (2001 - 4.75%).

## 7. LONG-TERM LIABILITIES

	2002	2001
Non-revolving term credit facility, repayable in quarterly principal instalments of \$500,000, with a final payment of \$1,500,000 on March 31, 2002, bearing interest at the bank's prime rate of interest plus ¾%. The effective interest rate at December 31, 2001 was 4.75%. The credit facility was repaid during the year.	\$ -	\$ 1,500,000
US\$ non-revolving term credit facility, repayable in quarterly principal instalments of \$398,200 (US\$ 250,000) with a final principal payment of \$1,592,800 (US\$ 1,000,000) due on June 30, 2003, bearing interest at LIBOR plus 1.75%. The interest rate at December 31, 2001 was 3.98%. The credit facility was repaid during the year.	-	3,583,800
	-	5,083,800
Deduct: Current portion	-	3,092,800
	<u>\$ -</u>	<u>\$ 1,991,000</u>

Interest expense on long-term liabilities amounted to \$42,452 (2001 - \$494,537).

## 8. CAPITAL STOCK

### (a) Authorized

Unlimited number of common shares.

### (b) Issued - Common Shares

	Number of Shares	Amount
Balance - December 31, 2000	10,605,566	\$ 16,780,538
Share options exercised	392,000	992,800
Share exchange (Note 8(c))	698,667	-
Balance - December 31, 2001	11,696,233	17,773,338
Share options exercised	173,000	464,200
Balance - December 31, 2002	<u>11,869,233</u>	<u>\$ 18,237,538</u>

### Class X shares issued by a subsidiary (Note 8(e))

	Number of Shares	Amount
Balance - December 31, 2000	-	\$ -
Issued during 2001	1,504,365	21,375,648
Balance - December 31, 2001 and 2002	<u>1,504,365</u>	<u>\$ 21,375,648</u>
<b>Total</b>		<u>\$ 39,613,186</u>

### (c) Share Exchange

In 2001, the Company acquired the remaining 13% interest in its subsidiary from related parties in exchange for the issuance of 698,667 common shares of the Company. The transaction was recorded at the carrying value of the investment.

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## (d) Warrants

As at December 31, 2002, 100,000 warrants, exercisable by December 31, 2003, which entitle the holder to purchase one common share of the Company at a price of \$6.00 per share per warrant, were outstanding.

## (e) Class X shares

During 2001, a subsidiary of the Company issued 1,504,365 Class X shares, for gross proceeds of \$22,400,000 which are exchangeable into 7,000,000 common shares of the Company. Costs of \$1,552,052 associated with the share issue and a future tax benefit of \$527,700 were netted against the gross proceeds of \$22,400,000. The shares participate in the earnings and dividends of the Company as though they were common shares of the Company and accordingly are included in the calculation of weighted average common shares outstanding.

## (f) Options

Under the Company's stock purchase plan, the board of directors is entitled to grant to designated directors, officers and employees of the Company or any subsidiary thereof, the right to purchase unissued common shares of the Company. The options are granted at a price not less than the fair value of the shares on the date of the grant. All options granted prior to December 31, 2000 vested immediately upon the grant date.

During 2001, all options granted vest evenly over a period of five years except for 100,000 options granted which vest evenly over three years. 20,000 options expired during the year ended December 31, 2001.

During 2002, all options granted vest evenly over a period of five years except for 50,000 options granted which vest evenly over two years and 30,000 options which vest evenly over four years. 24,000 options expired during the year ended December 31, 2002.

As at December 31, 2002, options outstanding to certain directors, officers and employees for the purchase of common shares were as follows:

Date of Grant	Number	Exercise Price	Expiry Date
January 27, 1999	45,000	\$ 3.50	January 27, 2004
October 26, 1999	135,000	\$ 4.50	October 26, 2004
October 25, 2001	272,000	\$ 3.85	October 25, 2006
November 16, 2001	18,000	\$ 4.16	November 16, 2006
October 24, 2002	216,000	\$ 4.00	October 24, 2007
	<u>686,000</u>		

The Company records no expense when it issues options. Had the Company elected to recognize the cost of its stock-based compensation based on the estimated fair value of stock options granted, the Company's results would have been as follows:

Fair value of options granted in 2002	\$ 71,554
Compensation expense for 2002	\$ 6,898
Pro forma net earnings	\$ 4,633,012

Pro forma basic and fully diluted earnings per common share remain unchanged.

The fair value of stock options granted is estimated using the Black-Scholes option pricing model on the date of grant with the following weighted average assumptions:

Stock price at grant date	\$ 4.00
Exercise price	\$ 4.00
Average life of options (years)	3.6
Expected stock price volatility	20%
Expected dividend yield	7.00%
Risk-free interest rate	3.93%

## 9. OTHER INCOME

	2002	2001
Interest, dividends and other	\$ 437,079	\$ 372,730
Gain on disposal of long-term investments	856,839	1,559,272
Gain on disposal of current investments	588	2,648
Share of loss in equity investment	-	(128,820)
	<u>\$ 1,294,506</u>	<u>\$ 1,805,830</u>

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## 10. INCOME TAXES

(a) The future income tax asset (liability) is comprised of the following temporary differences:

	2002	2001
Capital and other assets	\$ (1,301,188)	\$ (356,783)
Reserves and other temporary differences	551,279	610,580
Income tax losses	-	227,973
	<u>\$ (749,909)</u>	<u>\$ 481,770</u>

(b) The Company has capital losses of approximately \$7,400,000 for income tax purposes which may be carried forward indefinitely to reduce future taxable capital gains. The potential benefit of these capital losses has not been recognized in these financial statements.

(c) The major factors that cause variations from the Company's combined federal and provincial statutory Canadian income tax rates of 38.62% (2001 - 42.12%) were the following:

	2002	2001
Earnings before income taxes	<u>\$ 6,755,490</u>	<u>\$ 6,536,597</u>
Expected income tax expense at statutory rates	\$ 2,608,970	\$ 2,753,215
Increase (decrease) resulting from:		
Non-deductible/non-taxable items	153,139	552,727
Tax rate differential on US operations	17,423	(91,874)
Manufacturing and processing deduction	(280,018)	(369,278)
Non-taxable portion of capital gains	(194,577)	(2,281,652)
Taxes resulting from Dominion Citrus reorganization	-	3,878,811
Capital losses previously unrecognized	(194,577)	(2,281,651)
Other	5,220	32,018
	<u>\$ 2,115,580</u>	<u>\$ 2,192,316</u>

(d) Provision

The details of the income tax provision are as follows:

	2002	2001
Current provision	\$ 837,303	\$ 1,867,677
Future provision	1,278,277	324,639
	<u>\$ 2,115,580</u>	<u>\$ 2,192,316</u>

## 11. CASH FLOW INFORMATION

(a) Items not involving current cash flows

	2002	2001 <i>Restated</i>
Amortization	\$ 3,351,959	\$ 3,546,669
(Gain) loss on disposal of capital assets	(345,865)	213,765
Future income taxes	1,231,679	425,543
Gain on disposal of long-term investments	(856,839)	(1,559,272)
Cancellation of loans receivable	60,183	-
Foreign exchange	(13,050)	290,425
Share of loss in equity investment	-	128,820
Accrued pension cost	166,900	88,700
	<u>\$ 3,594,967</u>	<u>\$ 3,134,650</u>

(b) Net change in non-cash working capital

	2002	2001
Investments	\$ 271	\$ 884,525
Receivables	2,699,638	146,708
Prepaid expenses	(412,719)	(671,108)
Accounts payable and accrued liabilities	1,562,524	(1,822,300)
Income taxes	(1,043,945)	(1,275,857)
	<u>\$ 2,805,769</u>	<u>\$ (2,738,032)</u>

(c) Supplemental information

	2002	2001
Interest paid	\$ 71,388	\$ 624,527
Income taxes paid	\$ 1,881,248	\$ 3,143,534

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## 12. PENSION PLANS

The Company has defined contribution plans in place for the employees of its subsidiaries. Contributions to these plans are based on specified percentages of salaries. During 2001, the Company initiated a defined benefit pension plan for the Company's president. The pension benefit for this plan is based on earnings and years of service.

	2002	2001
Total pension expense is comprised as follows:		
Defined benefit plan		
Service costs (benefits earned during the year)	\$ 67,700	\$ 29,000
Interest costs on accrued benefit obligation	53,700	23,900
Expected return on plan assets	(27,600)	-
Amortization of transitional obligation	71,600	35,800
Amortization of net actuarial loss	1,500	-
	<u>166,900</u>	<u>88,700</u>
Defined contribution plans	639,474	451,395
<b>Total pension expense</b>	<b><u>\$ 806,374</u></b>	<b><u>\$ 540,095</u></b>
Pension fund asset is comprised as follows:		
Market value of plan assets at beginning of year	\$ -	\$ -
Employer contributions	1,577,400	-
Actual return on plan assets	13,100	-
Market value of plan assets at end of year	<u>1,590,500</u>	<u>-</u>
Accrued benefit obligation is comprised as follows:		
Obligation at beginning of year	754,700	-
Past service obligation upon initiation of plan	-	679,800
Service costs (benefits earned during the year)	67,700	29,000
Interest costs on accrued benefit obligation	53,700	23,900
Actuarial loss on accrued benefit obligation	36,000	22,000
Accumulated benefit obligation at the end of the year	<u>912,100</u>	<u>754,700</u>
Funded status at end of year	678,400	(754,700)
Items not recognized in earnings:		
Unrealized transitional obligation	572,400	644,000
Unrecognized actuarial losses	71,000	22,000
<b>Pension fund asset (liability)</b>	<b><u>\$ 1,321,800</u></b>	<b><u>\$ (88,700)</u></b>

An actuarial valuation was performed in December 2002. The significant actuarial assumptions used for the valuation of the Corporation's accrued benefit obligation and pension expense for the year are as follows: Discount rate - 6.0%, an assumed rate of salary escalation of 4%, an estimated remaining service lifetime of 8 years and an expected rate of return on plan assets of 7% per annum for the next 5 years and 8% thereafter.

## 13. CONTINGENCIES AND COMMITMENTS

### (a) Operating Leases

The future minimum lease commitments under operating leases are:

2003	\$ 3,277,708
2004	1,422,637
2005	1,283,411
2006	1,121,981
2007	1,072,159
Thereafter	4,842,638
	<u>\$ 13,020,534</u>

### (b) General

In the ordinary course of business activities, the Company is a plaintiff and has been named as defendant in certain litigation and other claims. Management believes that the resolution of such litigation and claims will not have a material adverse effect on the consolidated position of the Company.

## 14. SEGMENTED INFORMATION

### Geographic Information

	2002		2001	
	Sales	Capital Assets and Goodwill	Sales	Capital Assets and Goodwill
Canada	\$ 41,062,640	\$ 14,472,288	\$ 37,414,835	\$ 15,092,741
United States	14,856,369	1,605,148	15,519,063	1,983,299
	<u>\$ 55,919,009</u>	<u>\$ 16,077,436</u>	<u>\$ 52,933,898</u>	<u>\$ 17,076,040</u>

# Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001

## 15. SUBSEQUENT EVENT

On January 10, 2003, a subsidiary of the Company entered into an agreement to acquire 100% of the issued and outstanding shares of Tec-Mar Distribution Services, Inc. ("Tec-Mar") located in Michigan. The transaction closed January 31, 2003. The purchase will be accounted for using the purchase method with results of operations consolidated from February 1, 2003 onwards.

The purchase price was USD\$24,278,695 (CDN\$38,302,069) which was based upon USD\$18,000,000 plus the excess of adjusted working capital over USD\$6,400,000, which was USD\$6,278,695 and is subject to post-closing adjustments. The purchase price will be increased by 50% of any Tec-Mar EBITDA (as defined in the agreement) that exceeds USD\$4,500,000 in each of the four years from 2003 through 2006 inclusive. If Tec-Mar EBITDA falls below USD\$4,500,000 in any year such deficit will be deducted from the next year EBITDA.

The following pro-forma information reflects the results of the acquisition as though the transaction occurred on January 1, 2002 for income statement purposes and December 31, 2002 for balance sheet purposes.

### BALANCE SHEET

	Automodular Corporation (000's)	Unaudited Tec-Mar (000's)	Adjustments (000's)	Combined (000's)
Current assets	\$ 24,484	\$ 23,460	\$ (21,006)	\$ 26,938
Long-term investments	283	-	-	283
Capital assets	6,663	4,732	-	11,395
Other assets	13,652	-	15,483	29,135
	<u>\$ 45,082</u>	<u>\$ 28,192</u>	<u>\$ (5,523)</u>	<u>\$ 67,751</u>
Current liabilities	\$ 5,812	\$ 4,604	\$ 3,500	\$ 13,916
Long-term debt	-	-	14,000	14,000
Notes payable	-	303	-	303
Future income taxes	750	262	-	1,012
Shareholders' equity	38,520	23,023	(23,023)	38,520
	<u>\$ 45,082</u>	<u>\$ 28,192</u>	<u>\$ (5,523)</u>	<u>\$ 67,751</u>

The purchase price was paid in cash on closing and was funded by a CDN\$17,500,000 non-revolving term credit facility, a US\$5,000,000 (CDN\$7,888,000) bridge credit facility and cash of CDN\$12,914,069. The non-revolving term credit facility bears interest at the bank's prime rate plus 0.75%. It is repayable in quarterly principal payments of CDN\$875,000 with a final payment of CDN\$7,875,000 due on September 30, 2005. The Company also has available to it a revolving term credit facility of CDN\$5,000,000 which bears interest at the bank's prime rate plus 0.75%. This facility replaces the CDN\$2,000,000 facility described in Note 6.

The adjustments above reflect the impact of the acquisition on the Company's consolidated financial statements. An outside party has been retained to analyze the purchase price excess and identify and quantify the breakdown between intangible assets and goodwill. Any intangible assets with a fixed lifetime will be amortized over the period of future benefit. No provision for such amortization has been recorded in the pro-forma income statement since the amount cannot be estimated at this time.

### INCOME STATEMENT

	Automodular Corporation (000's)	Unaudited Tec-Mar (000's)	Adjustments (000's)	Combined (000's)
Sales	\$ 55,919	\$ 63,776	\$ -	\$ 119,695
Cost of sales and other expenses	47,064	58,164	-	105,228
Earnings from operations before the following	8,855	5,612	-	14,467
Amortization	3,352	1,154	-	4,506
Interest expense	42	135	800	977
Other income	(1,294)	(349)	303	(1,340)
	<u>2,100</u>	<u>940</u>	<u>1,103</u>	<u>4,143</u>
Earnings before income taxes	6,755	4,672	(1,103)	10,324
Income taxes	2,115	2,080	(397)	3,798
Net earnings for the year	<u>\$ 4,640</u>	<u>\$ 2,592</u>	<u>\$ (706)</u>	<u>\$ 6,526</u>

# Investor Information

Years ended December 31, 2002 and 2001

## COMPARATIVE DATA

	Dec. 31 2002	Dec. 31 2001	Dec. 31 2000	Dec. 31 1999	Dec. 31 1998
<b>Operations (\$000's)</b>					
Sales	55,919	52,934	49,698	39,604	61,081
Earnings from continuing operations	4,640	4,344	2,105	5,019	(11,984)
Net earnings	4,640	4,344	3,431	5,711	(10,188)
Cash flow from operations	11,041	4,741	9,063	3,202	(708)
<b>Financial (\$000's)</b>					
Total assets	45,082	48,111	38,351	37,021	32,022
Long-term debt	0	1,991	4,874	3,500	10,096
Retained earnings (deficit) (end of year)	(1,093)	(460)	1,928	3,660	(7,885)
Shareholders' equity	38,520	38,689	18,709	20,440	15,394
Return on average shareholders' equity (%)	12.0	15.1	17.5	31.9	-
<b>Per share (\$)</b>					
Earnings before discontinued operations	0.25	0.29	0.20	0.50	(1.25)
Net earnings	0.25	0.29	0.32	0.57	(1.06)
Weighted average number of shares outstanding (000's)	18,829	14,883	10,606	10,009	9,619

## QUARTERLY DATA

	2002				2001 (Restated)			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Sales (\$000's)	14,485	13,574	14,236	13,624	14,022	12,461	13,220	13,231
Depreciation and amortization	808	855	843	846	836	910	911	890
Net earnings	434	1,296	1,201	1,709	1,199	1,396	914	835

## COMMON SHARE PRICES

### Calendar year

	The Toronto Stock Exchange		
	High \$	Low \$	Volume (000's)
<b>2002</b>			
Fourth Quarter	4.50	3.80	175
Third Quarter	5.00	3.90	263
Second Quarter	5.73	4.80	288
First Quarter	5.26	3.85	581
<b>2001</b>			
Fourth Quarter	4.35	3.10	624
Third Quarter	4.45	3.50	370
Second Quarter	4.95	3.00	462
First Quarter	4.00	2.90	36

## DIVIDENDS

The Board of Directors has approved a dividend policy whereby the Corporation pays regular quarterly dividends at a rate of \$0.07 per common share. The quarterly rate of dividends will be reviewed annually.

## INVESTOR RELATIONS

Institutional investors, brokers, security analysts and others desiring financial information about Automodular should contact:

Winston R. Ash

Vice President Finance and Secretary

Automodular Corporation

Tel: (905)665-0060 x112

Fax: (905)665-8560

e-mail: invest@automodular.net

## Corporate Information

### HEAD OFFICE

200 Montecorte Street  
Whitby, Ontario  
L1N 9V8  
Tel: (905)665-0060  
Fax: (905)665-8560  
<http://www.automodular.com>  
[invest@automodular.net](mailto:invest@automodular.net)

### SUBSIDIARY OFFICES

Automodular Assemblies Inc.  
200 Montecorte Street  
Whitby, Ontario  
L1N 9V8  
Tel: (905)665-0060  
Fax: (905)665-8560

Automodular Assemblies (DE) Inc.  
700 Centerpointe Boulevard  
New Castle, Delaware  
19720 U.S.A.  
Tel: (302)328-5464  
Fax: (302)328-5646

### AUDITORS

Smith, Nixon & Co. LLP  
Toronto

### PRINCIPAL BANKERS

The Bank of Nova Scotia

### SOLICITORS

Sheldon • Huxtable, Toronto

### TRANSFER AGENT AND REGISTRAR

Computershare Trust Company  
of Canada  
Investor Services  
(416)981-9500  
Fax: (416)981-9800  
[www.computershare.com](http://www.computershare.com)

### DIRECTORS

Russell M. Baranowski  
President  
Automodular Assemblies Inc.

Michael F. Blair  
President

Andrew Brenton  
Managing Partner  
Scotia Merchant Capital

Garth Davis  
Partner  
Scotia Merchant Capital

T. Daniel Flood  
Entrepreneur

Henry Knowles  
Business and Financial Consultant

R. Peter McLaughlin  
President  
Greenbriar Holdings Limited

Alan R. Marchment  
Chairman  
Wiltshire Group Limited

James Rodgers  
President  
Cames Consulting Inc.

Rae Wallin  
President  
N-Viro Systems Canada Inc.

### OFFICERS

Winston R. Ash  
Vice President Finance  
and Secretary

Michael F. Blair  
President

Diane Erlingher  
Assistant Secretary

## Annual Meeting

The Annual Meeting of Shareholders will be held in the City Hall Room of The Sheraton Centre  
123 Queen Street West, Toronto, Ontario on Wednesday, May 7, 2003 at 10:00 a.m.

All shareholders are encouraged to attend.