SMART ONLINE INC
Form DEF 14C
April 27, 2012

UNITED STATES SECURITIES
AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

SCHEDULE 14C INFORMATION
Information Statement Pursuant to Section 14(c) of the Securities Exchange Act of 1934 (Amendment No.)

Check the appropriate box:

o Preliminary Information Statement

o Confidential, for Use of the Commission Only (as permitted by Rule 14c- 5(d)(2))

þ Definitive Information Statement

SMART ONLINE, INC.
(Name of Registrant as Specified in Its Charter)

Payment of Filing Fee (Check the appropriate box):

þ No fee required

o Fee computed on table below per Exchange Act Rules 14c-5(g) and 0-11.

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SMART ONLINE, INC.
4505 Emperor Boulevard
Suite 320
Durham, North Carolina 27703

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

TO BE HELD JUNE 13, 2012

You are cordially invited to attend the Annual Meeting of Stockholders of Smart Online, Inc., which will be held on Wednesday, June 13, 2012, at 9:00 a.m. local time, in the Board Room at the offices of the corporation at 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703. Stockholders will be asked to consider and vote upon the following matters at the meeting, which are described in the accompanying information statement:

1. The election of four directors, each to serve for a term of one year or until his successor shall have been duly elected and qualified;

2. The ratification of the appointment of Cherry, Bekaert & Holland, L.L.P. as the independent registered public accounting firm of the Company for the fiscal year ending December 31, 2012; and

3. The transaction of such other business as may be properly brought before the meeting.

Stockholders of record at the close of business on April 27, 2012 are entitled to notice of and to vote at the annual meeting and any and all adjournments or postponements thereof.

We are not soliciting proxies for this annual meeting. However, all stockholders are welcome to attend the meeting and vote in person.

By Order of the Board of Directors

/s/ Dror Zoreff
Dror Zoreff
Chairman of the Board

Durham, North Carolina

SMART ONLINE, INC.

2012 ANNUAL MEETING OF STOCKHOLDERS

9:00A.M. EST, JUNE 13, 2012

INFORMATION STATEMENT

WE ARE NOT ASKING YOU FOR A PROXY AND YOU ARE
REQUESTED NOT TO SEND US A PROXY

This Information Statement contains information related to the Company's 2012 annual meeting of stockholders to be held at the Company's corporate offices, 4505 Emperor Boulevard Suite 320, Durham North Carolina 27703 at 9:00 A.M., Eastern Standard Time, on June 13, 2012 and at any adjournments or postponements thereof. The approximate date that this Information Statement, the preceding Notice of Annual Meeting and the Company's Annual Report to Stockholders for the fiscal year ended December 31, 2011, or the Annual Report are first being made available to stockholders is April 30, 2012. We are making this Information Statement available to our stockholders for use at the annual meeting. You should review this Information Statement in conjunction with the Company's Annual Report.

GENERAL INFORMATION

Meeting Information

The annual meeting of stockholders of Smart Online, Inc. or Smart Online, the Company, we, our or us will be held at the Company's corporate offices 4505 Emperor Boulevard, Suite 320, Durham, NC 27703 beginning at 9:00 A.M., Eastern Standard Time, on June 13, 2012.

The proposals scheduled to be voted on are (1) to elect four (4) directors for one-year terms; and (2) to ratify the appointment of Cherry, Bekaert & Holland, L.L.P., or Cherry Bekaert, as the independent registered public accountant for the fiscal year ending December 31, 2012. Our Board of Directors, or the Board, recommends that you vote "FOR" each of the nominees to the Board described in Proposal No. 1 and "FOR" the ratification of the selection of Cherry Bekaert as our independent registered public accounting firm for the fiscal year ended December 31, 2012, as described in Proposal No. 2.

Who May Vote

You are entitled to vote in person at the annual meeting if you owned shares of our common stock as of the close of business (5:00 p.m.) on April 27, 2012, the record date of the annual meeting. On the record date, 18,352,542 shares of our common stock were issued and outstanding and held by 198 holders of record. Holders on the record date of our common stock which is (1) held directly in your name as the stockholder of record or (2) held for you as the beneficial owner through a stockbroker, bank or other nominee, are entitled to one vote per share at the annual meeting. You may vote by ballot or grant a proxy to another person to vote in your place.

WE ARE NOT ASKING YOU FOR A PROXY AND YOU ARE REQUESTED NOT TO SEND US A PROXY

How To Vote

Holders of record may vote in person at the meeting by ballot or grant a proxy to another person to vote in your place. If your shares are not held of record in your name, you must obtain a proxy from the record holder, usually a broker or other nominee, in order to vote in person at the meeting.

Quorum

The presence at the annual meeting, in person or by proxy, of the holders of a majority of the shares of our common stock outstanding on the record date will constitute a quorum. Abstentions are counted as present for the purpose of determining the presence of a quorum. A broker who holds shares in nominee or "street name" for a customer who is the beneficial owner of those shares may be prohibited from voting those shares in person on any proposal to be voted on at the annual meeting without specific instructions from such customer with respect to such proposal.

Votes Needed

Proposal 1: Election of Directors. The affirmative vote of a plurality of the votes cast at the annual meeting is required for the election of each of the four director nominees. You may vote "for" one or more director nominees or you may withhold your vote as to one or more director nominees. A properly executed ballot or proxy marked "withhold" as to the election of one or more director nominees will not be counted with respect to the director or directors indicated, although it will be counted for purposes of determining whether there is a quorum. Stockholders do not have the right to cumulate their votes for directors. No New York Stock Exchange (NYSE) member broker who is the record holder of shares on behalf of a beneficial owner (the customer) can vote shares at the meeting for the election of directors unless the broker receives instructions from the beneficial owner. These "broker non-votes" will not impact the results of the election, but will be counted for purposes of determining whether there is a quorum.

Proposal 2: Ratification of the Appointment of the Independent Registered Public Accounting Firm. The affirmative "FOR" vote of the holders of a majority of all shares casting votes in person or by proxy at the annual meeting is required to ratify the appointment of Cherry Bekaert, as our independent registered public accounting firm for the fiscal year ending December 31, 2012. A properly executed ballot marked "abstain" with respect to this proposal will not be counted, although it will be counted for purposes of determining whether there is a quorum. Abstentions will have the same effect as a vote against this proposal. NYSE member brokers have discretion to vote on behalf of beneficial owners with respect to this proposal; as a result, there will be no "broker non-votes" on this item.

As of the record date, our directors and executive officers and their affiliates owned and were entitled to vote approximately 18,352,542 shares of our common stock. All of these persons have indicated they and their affiliates will vote their shares in favor of the four director nominees and the ratification of the appointment of Cherry Bekaert.

Other Matters

The Board does not know of any other matter that will be presented for your consideration at the annual meeting other than the two proposals described herein.

PROPOSAL NO. 1

ELECTION OF DIRECTORS

At the annual meeting, four nominees will be elected as directors. Our Board currently consists of four members, all of whom are standing for re-election at the annual meeting. The directors elected at the annual meeting will serve until the next annual meeting of stockholders and until their respective successors are duly elected and qualified.

Our Board , based on the recommendation of the nominating and governance committee, has nominated each of Shlomo Elia, Amir Elbaz, Dror Zoreff and Robert M. Brinson, Jr. to stand for re-election at the annual meeting.

The bylaws of the Company provide that the number of directors on the Board will be no more than nine. We had three directors at the beginning of fiscal year 2011. In September 2011, we expanded the size of the Board to 4 directors and nominated our fourth director. We will also elect four directors for fiscal year 2012. The four nominees that receive the most votes will be appointed to serve on our Board for the next year. You cannot vote for a greater number of persons than the number of nominees named. All four of the persons nominated for election to the Board at the annual meeting are currently serving as directors of the Company. The Company is not aware of any nominee who will be unable or will decline to serve as a director. If a nominee becomes unable or declines to serve, votes may be cast for a substitute nominee, if any, designated by the Board. The term of office of each person elected as a director will continue until the later of the next annual meeting of stockholders or until such time as his or her successor has been duly elected and qualified, or until his prior death, resignation or removal.

The following table lists the nominees for election and information about each.

Name	Age	Principal Occupation and Background
Shlomo Elia	69	Director. Mr. Elia has served on the Company’s Board since November 2006 and was originally recommended for appointment to the Board by Atlas Capital, SA, Atlas or Atlas Capital, one of the Company’s stockholders and lenders. Mr. Elia is the founder and a Director of 3Pen Ltd., 3Pen, a private holding company focusing on business opportunities in Internet infrastructure and telecommunications. Prior to founding 3Pen in 1999, Mr. Elia held several senior positions in the Israeli Defense Forces, I.D.F., including the post of the Military Governor of the West-Bank (1982-1984) and Commander of the Liaison Unit for South Lebanon (1984-1985). During his service, among other activities, General Elia was engaged for a year as a Research Fellow in the Institute of International Strategic Affairs at U.C.L.A. Since his retirement from the I.D.F., he has been involved in communication projects in Nigeria and West Africa and construction projects in Romania. Among his civilian activities, Mr. Elia was Chairman of the National Tourist Board and currently is Chairman of 3Pen Technologies Ltd. and co-chairman of the Israeli Soldiers Welfare Association. Mr. Elia holds a B.A. degree in Modern History of the Middle-East from Tel Aviv University. We believe Mr. Elia’s international business expertise and significant management experience will provide constructive insight and perspective to our Board and management.
Amir Elbaz	35	Director. Mr. Elbaz has served on the Company’s Board since January 2010. Mr. Elbaz currently serves as Chief Executive Officer of two companies in the technology and media sectors. Mr. Elbaz also advises technology and renewable energy companies on business strategy, restructuring and business development initiatives. Mr. Elbaz served as the

Executive Vice President & Chief Financial Officer of Lithium Technology Corporation until November 2008. Mr. Elbaz joined LTC in 2006 to oversee finances and marketing, as well as business development. Prior to joining LTC, Mr. Elbaz served as a Senior Associate of Arch Hill Capital NV, a Dutch venture firm, from 2005-2006. During 2004 and most of 2005 Mr. Elbaz served as Vice President of Corporate Finance at Yorkville Advisors, where Mr. Elbaz sourced, structured and managed investments in more than a dozen public and private companies. Prior to joining Yorkville Advisors, Mr. Elbaz served for several years as an analyst with the Economic Department in the Procurement Mission of the Israeli Ministry of Defense in New York City. In that capacity, Mr. Elbaz co-headed multi-million dollar negotiations with first tier technology companies, and was in charge of the financial aspects of the day-to-day operations. Mr. Elbaz holds a B.A. degree from the University of Haifa, Israel, and an MBA in Finance & Investments from Bernard Baruch College, CUNY, New York. Following his MBA graduation, Mr. Elbaz was elected to the International Honorary Finance Society of Beta Gamma Sigma.

We believe Mr. Elbaz's significant experience in the technology sector, coupled with his extensive financial and economic background provide invaluable insight with respect to our business and technologies.

Dror Zoreff	66	Director. Mr. Zoreff has served on the Company's Board since April 2008. Since May 2009, he has served as Chairman of the Board, and since November 2009, he has served as Interim President and Chief Executive Officer. Since 2008, he has served as the President and CEO of Donor Management Services, Inc., a New York-based company that provides major donors, corporations, and foundations a unique set of tools and services to ensure their charitable gifts are properly used and achieve the desired impact. From 1999 to 2008, Mr. Zoreff served as Consultant to the President and CEO of United Retail Group Inc., a specialty retailer of plus size women's fashions. From 1997 to 1999, he was Vice President of International Operations at Russ Berrie, Inc., a designer, importer, marketer, and distributor of gift and infant and juvenile consumer products. Prior to 1997, Mr. Zoreff held positions with The College of Judea & Samaria, Glenoit Industries Ltd, and the Jewish Agency for Israel. Mr. Zoreff holds a B.A. degree in Business Administration from Manchester University and an M.A. degree in Business Administration from Tel Aviv University. We believe Mr. Zoreff's extensive marketing and management experience, in addition to his knowledge of the international marketplace, contributes to the strategic composition of the Board.
Robert M. Brinson, Jr.	48	Director. Mr. Brinson has served on the Company's Board since September 14, 2011. From 2005 until 2007, Mr. Brinson was a board member and Chief Technology Officer of IntelliScience Corporation, a developer of intelligent multi-modal image analysis systems and software. In 2007, Mr. Brinson became a board member and Chief Technology Officer of IP Tank, LLC. Mr. Brinson is currently the Chief Visionary Officer of Apokalyyis, Inc., a developer of consultative technology solutions and serves as Chief Technology Officer of Concept Connections and Affirm ID, LLC. Mr. Brinson serves on the boards of directors of Apokalyyis, Inc. and iissee, LLC, a company specializing in local search solutions. He is also a self-employed technology consultant. In addition to his service as a Board member, Mr. Brinson provided technology and management consulting services to the Company during 2011 and continues to provide those services during 2012. We believe Mr. Brinson's extensive technology, innovation and management experience contributes to the strategic composition of the Board.

Our Board unanimously recommends that you vote "FOR" the election of each of the director nominees named above.

Executive Officers

The names of the Company's current executive officers are listed in our Annual Report on Form 10-K. The Company's executive officers are appointed by its Board to hold office until their successors are appointed.

Name	Age	Position
Dror Zoreff	66	Chairman of the Board, Interim President and Chief Executive Officer
Thaddeus J. Shalek	62	Chief Financial Officer

Information regarding Mr. Zoreff is described above under "Nominees for Election as Directors".

Thaddeus J. Shalek, Chief Financial Officer.

Chief Financial Officer since August 2009. Mr. Shalek was the CFO of Lindell Investments, Inc., a closely held national real estate development company in Tampa, Florida from June 2006 until April 2008, the CEO and CFO of Vertical Health Solutions, Inc., Oldsmar, Florida form October 2004 to June 2006 and the owner and president of Shalek & Associates, CPA's Inc., a Certified Public Accounting firm in Cleveland, Ohio providing accounting, tax and consulting services to small and medium sized businesses from 1984 through December 2004. Mr. Shalek worked as an auditor and tax manager with Coopers & Lybrand (now PricewaterhouseCoopers) and currently teaches accounting and entrepreneurial finance, on a part-time basis, at the University of North Carolina at Greensboro. He was an adjunct instructor of business, accounting and taxation at Cuyahoga Community College of Cleveland, Ohio. Mr. Shalek earned his BSBA from John Carroll University, Cleveland, Ohio and his MBA from The University of Tampa. Mr. Shalek has served on numerous charitable and business boards throughout his career.

Code of Ethics

The Company has adopted a Code of Ethics applicable to its executives, including the principal executive officer, principal financial officer, and principal accounting officer, as defined by applicable rules of the Securities and Exchange Commission, or SEC. It is publicly available on the Company's website at www.smartonline.com. If the Company makes any amendments to the Code of Ethics other than technical, administrative, or other non-substantive amendments, or grants any waivers, including implicit waivers, from a provision of the Code of Ethics to the Company's Chief Executive Officer, Chief Financial Officer, or certain other finance executives, the Company will disclose the nature of the amendment or waiver, its effective date, and to whom it applies on the Company's website at www.smartonline.com.

Board Composition and Independence of Directors

The size of the Board is currently fixed at four members. Four persons have been nominated for election at the annual meeting. The Board believes that the current number of directors is appropriate at this time.

The Company's stock is currently quoted on the OTC Bulletin Board, or OTCBB. The OTCBB does not have rules regarding director independence. Accordingly, we determined that the NASDAQ Stock Market, or Nasdaq, independence requirements are an appropriate standard to determine director independence because these requirements are stricter than the current OTCBB's requirements. Additionally, we adopted these stricter standards to strengthen our corporate governance and improve internal controls.

Nasdaq listing requirements mandate that a majority of the members of a listed company's board of directors be "independent directors" as defined under Nasdaq Stock Market Rule 5605. Although not currently required, the Board has determined that three of the present directors — Messrs. Elia, Elbaz and Brinson — are "independent directors" within the meaning of Nasdaq Marketplace Rules. Messrs. Elia, Elbaz and Brinson are standing for re-election. Therefore, assuming all four nominees are elected at the annual meeting, the Board will have a majority of "independent directors" after the annual meeting.

Dror Zoreff currently serves as both Interim President and Chief Executive Officer and Chairman of the Board. Mr. Zoreff was appointed Interim President and Chief Executive Officer of the Company in November 2009, and has been a director since April 2008. The Board believes that combining the positions of Chairman and CEO is the most appropriate for the Company at this time, given that Mr. Zoreff continues to serve as CEO in an interim capacity. Having one person as Chairman and CEO has provided unified leadership and direction to the Company and minimized disruption to the business over the past two fiscal years, which have been a time of frequent management turnover, and strengthens the ability of the CEO to develop and implement strategic initiatives and respond efficiently in crisis situations. The Company currently has no lead independent director.

Risk Oversight

While our management is responsible for assessing and managing risks to the Company, the Board takes an active role, as a whole and also at the committee level, in overseeing the material risks facing the Company, including operational, financial, legal and regulatory and strategic and reputational risks. Risks are considered in virtually every business decision and as part of the Company's overall business strategy. Our board committees also regularly engage in risk assessment as a part of their regular function. The Audit Committee discusses with management the Company's major financial risk exposures and the steps management has taken to monitor and control such exposures. The Compensation Committee is responsible for overseeing the management of risks relating to the Company's executive compensation plans and arrangements. The Corporate Governance and Nominating Committee manages risks associated with corporate governance, including risks associated with the independence of the board and reviews risks associated with potential conflicts of interest affecting directors and executive officers of the Company. While each committee is responsible for evaluating certain risks and overseeing the management of such risks, our entire Board is regularly informed through committee reports about such risks. The Board regularly engages in discussion of financial, legal, technological, economic and other risks. Because overseeing risk is an ongoing process that is inherent in the Company’s strategic decisions, our Board discusses risk throughout the year at other meetings in relation to specific proposed actions. Additionally, our Board exercises its risk oversight function in approving new product research and development projects, large marketing engagements, the annual budget and quarterly forecasts and in reviewing the Company’s long-range strategic and financial plans with management.

Attendance at Meetings

The Board held five meetings during the fiscal year ended December 31, 2011 Each incumbent director attended or participated in at least 75% of the aggregate of (1) the number of meetings of the Board held in fiscal year 2011 during the period he served as a director and (2) the number of meetings of committees on which he served that were held during the period of his service.

The Company expects all directors to attend each annual meeting of stockholders, absent good reason. Three directors attended the annual meeting of stockholders in 2011.

Standing Committees

The Company's Board has three standing committees: the Audit Committee, the Compensation Committee, and the Corporate Governance and Nominating Committee. Copies of the charters of these committees, as they may be amended from time to time, are available on the Company's website at www.smartonline.com.

Audit Committee. The Audit Committee is composed of Mr. Elbaz and Mr. Elia. Mr. Elbaz serves as Chairman of the Audit Committee. The Company's Board has determined that Mr. Elbaz and Mr. Elia are each an "independent director" as that term is defined by Nasdaq Stock Market Rule 5605 and SEC rules, and they each meet the special independence requirements applicable to audit committee members. All members have past financial experience resulting in their financial sophistication as would be required by Nasdaq Marketplace Rules and SEC rules. The Board has determined that Mr. Elbaz meets the definition of "audit committee financial expert" as that term is defined in Item 407(d)(5)(ii) of Regulation S-K. The Company's securities are quoted on the OTCBB and are not listed on a national securities exchange. Therefore, neither the SEC rules nor the Nasdaq Marketplace Rules regarding audit committees are applicable to the Company's Board.

The Audit Committee was established by the Board for the purpose of assisting it in fulfilling its responsibilities with respect to its oversight of (1) the quality and integrity of the Company's financial statements, (2) compliance with legal and regulatory requirements, (3) the independent registered public accounting firm's qualifications and independence, and (4) the performance of the Company's internal audit function and independent registered public accounting firm. The Audit Committee is also responsible for the preparation of reports required to be included in the Company's annual proxy or information statement or other documents from time to time required with respect to the Audit Committee's functions. The Audit Committee met four times during 2011.

Compensation Committee. The Compensation Committee is composed of Mr. Elia and Mr. Elbaz. Mr. Elia serves as Chairman of the Compensation Committee. The Company's Board has determined that Mr. Elia and Mr. Elbaz are "independent directors" within the meaning of the Nasdaq Marketplace Rules.

The Compensation Committee was established by the Company's Board for the purpose of assisting it in discharging its duties with respect to (1) the formulation, implementation, review, and modification of the compensation of the Company's officers and directors and (2) the preparation of the annual report on executive compensation for inclusion in the Company's annual proxy or information statement, if required. The Compensation Committee's duties include, among other things, setting the compensation for officers and directors, making recommendations to the Board with respect to incentive compensation plans and equity-based compensation plans, approving grants of stock options and other awards under the Company's 2004 Equity Compensation Plan, and administering the Company's defined benefit and defined contribution plans, if any.

In fulfilling its responsibilities, the Compensation Committee is entitled to delegate any or all of its responsibilities to a subcommittee of the Compensation Committee, to the extent consistent with applicable law, the Company's certificate of incorporation, bylaws, corporate governance guidelines, and rules of any exchange or market on which the securities of the Company are then traded if compliance with such rules is required to begin or continue trading.

As part of its review and establishment of the performance criteria and compensation of officers and directors of the Company, the Compensation Committee must separately meet at least annually with the Company's Chief Executive Officer, the principal human resources executive and compliance officer, and with any other corporate officers as the Compensation Committee deems appropriate. However, the Compensation Committee must also meet regularly without such officers present, and in all cases such officers must not be present at the meetings at which their performance and compensation is being discussed and determined. The Compensation Committee must consult with the Chief Executive Officer regarding compensation of the other officers of the Company. The Compensation

Committee has not engaged any compensation consultant to determine or recommend the amount or form of executive and director compensation. The Compensation Committee met one time during 2011.

Corporate Governance and Nominating Committee and Procedures for Director Nominations. The Corporate Governance and Nominating Committee is composed of Mr. Elbaz and Mr. Zoreff. Mr. Zoreff serves as Chairman of the Corporate Governance and Nominating Committee. The Company's Board has determined that Mr. Elbaz is an "independent director" within the meaning of the Nasdaq Marketplace Rules. Mr. Zoreff is not an "independent director" within the meaning of the Nasdaq Marketplace Rules

The Corporate Governance and Nominating Committee was established by the Board for the purpose of assisting it in discharging its duties with respect to (1) the identification of individuals qualified to become directors and the selection or recommendation of candidates for directorships to be filled by the Board or the stockholders, and (2) the development, maintenance, and recommendation of a set of corporate governance principles applicable to the Company, and the periodic review of such principles. The Corporate Governance and Nominating Committee met one time during 2011.

The Corporate Governance and Nominating Committee is responsible for identifying and selecting or recommending qualified candidates for membership on the Board. In identifying candidates, the Committee takes into account such factors as it considers appropriate, which may include (a) knowledge in the technology industry generally, and Software-as-a-Service specifically, (b) experience in the areas of accounting and finance, (c) mature business judgment, (d) the candidate's management, leadership, and business strategy experience, (e) the candidate's ability to manage a crisis, and (f) the candidate's knowledge of proper corporate governance.

The Corporate Governance and Nominating Committee is responsible for evaluating suggestions concerning possible candidates for election to the Board submitted to the Company, including those submitted by Board members (including self-nominations) and stockholders. All candidates, including those submitted by stockholders, will be evaluated by the Corporate Governance and Nominating Committee on the same basis as other candidates using the Board membership criteria described above and in accordance with applicable procedures. The Corporate Governance and Nominating Committee believes that the minimum qualifications for serving as a Company director are that a candidate demonstrate, by significant accomplishment in his or her field, an ability to make a meaningful contribution to the Board's oversight of the Company's business and affairs and have an impeccable record and reputation for honest and ethical conduct in his or her professional and personal activities. Qualifications for consideration as a director nominee may vary according to the particular areas of expertise being sought as a complement to the existing Board composition.

Once candidates have been identified, the Corporate Governance and Nominating Committee will determine whether such candidates meet the minimum qualifications for director nominees and will recommend qualified nominees to the Board. In accordance with the Company's bylaws, proposed nominees must tender, prior to nomination, an irrevocable, conditional letter of resignation that would be effective upon such person being charged with a felony or equivalent offense under the laws of any jurisdiction. The full Board will then approve qualified nominees for appointment or election to the Board.

While the Corporate Governance and Nominating Committee currently has no policy with respect to which it considers diversity in identifying nominees for director, one of our directors has a strong technical background that is relevant to our industry; another of our directors has a background in accounting, finance, and management. We believe that the backgrounds and skills of our directors bring a diverse range of experience, opinion and perspectives to the Board. Details of each nominee's strengths are identified in the biographical presentation under PROPOSAL NO.1, ELECTION OF DIRECTORS, above.

Any stockholder desiring to present a nomination for consideration by the Corporate Governance and Nominating Committee prior to the 2013 Annual Meeting of Stockholders must do so in accordance with the Company's bylaws. See "Stockholder Proposals for the 2013 Annual Meeting" below.

Section 16(a) Beneficial Ownership Reporting Compliance

The members of the Company's Board, its executive officers, and persons who hold more than 10% of its outstanding common stock are subject to the reporting requirements of Section 16(a) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, which requires them to file reports with respect to their ownership of the Company's common stock and their transactions in such common stock. Based upon the Company's review of the Section 16(a) reports in its records for fiscal year 2011 transactions in the Company's common stock, the Company believes that all reporting requirements under Section 16(a) for fiscal year 2011 were met in a timely manner by its directors, executive officers, and greater than 10% beneficial owners.

Certain Relationships and Related Transactions

On December 6, 2010, the Company entered into (i) a $6,500,000 Promissory Note, or the IDB Note, as borrower, and (ii) a Letter Agreement for the $6,500,000 Term Loan Facility, or the Letter Agreement, each with Israel Discount Bank of New York, or IDB as lender ((i) and (ii), the IDB Credit Facility.

The IDB Credit Facility is secured by two irrevocable standby letters of credit issued by UBS Switzerland in favor of IDB in the aggregate amount of $6,500,000, or collectively, the SBLC, each issued with Atlas as account party. Atlas and the Company anticipate finalizing in the near future the terms of the Company's reimbursement of Atlas for any future drawdowns on the SBLC. The advances drawn on the IDB Credit Facility must be repaid on the earlier of (a) May 31, 2012 or (b) 180 days prior to the expiration date of the SBLC. Interest on each advance under the IDB Credit Facility accrues, at the Company's election, at either LIBOR plus 300 basis points or IDB's prime rate plus 100 basis points, provided that the rate of interest for each advance shall never be less than four percent. Interest accrued on each advance is due quarterly and payable in arrears on the last day of each of February, May, August and November during the term of the IDB Credit Facility, commencing on the last day of February 2011. All required interest payments were made on a timely basis during 2011. As of December 31, 2011, the Company drew $5,000,000 of the total Term Loan Facility. All interest payments have been made on a timely basis. We are currently working with IDB to extend our IDB Credit Facility for an additional one-year period with terms similar to those currently in place. We believe that we will be successful in our efforts.

Atlas is a beneficial owner of 10% or more of the common stock of the Company, and the holder of a majority of the aggregate outstanding principal amount of the convertible secured subordinated notes, as amended, or the Notes under the Convertible Secured Subordinated Note Purchase Agreement, dated November 14, 2007, as amended, or the Note Purchase Agreement, between the Company and the convertible noteholders, under which the Company is entitled to elect to sell to the convertible noteholders, and the convertible noteholders are obligated to buy, Notes. The terms of the Note Purchase Agreement and the Notes are described in "Sale of Convertible Notes to Certain Affiliates" below.

Sale Leaseback of Company Equipment with Noteholders. On September 4, 2009, the Company entered into a sale-leaseback agreement with the current holders of the Notes. The noteholders paid a market rate cost of $200,000 through the reduction of current outstanding debt under such Notes in exchange for all of the Company's office furniture, equipment and computers. The noteholders then leased all furniture, equipment and computers back to the Company over a ten (10) year period. The purchase price of $200,000 represented the fair market value of the equipment based on an independent appraisal of the equipment by Dynamic Office Services and Coastal Computers, which are not affiliated with the Company.

Sale of Convertible Notes to Certain Affiliates. As of April 27, 2012, the Company had $16.9 million aggregate principal amount of Notes due November 14, 2013 outstanding, after the $200,000 reduction of such current outstanding debt on account of the sale-leaseback described in above. As of such date, Atlas held Notes in the aggregate principal amount of $13.575 million. The Notes sold to Atlas during 2011 are as follows:

Date of Purchase	Amount of Convertible Note	Interest Rate	Original Maturity Date
February 7, 2011	$ 250,000	8 %	11/14/2013
March 4, 2011	$ 325,000	8 %	11/14/2013
April 6, 2011	$ 400,000	8 %	11/14/2013
September 6, 2011	$ 500,000	8 %	11/14/2013
October 11, 2011	$ 300,000	8 %	11/14/2013
November 7, 2011	$ 300,000	8 %	11/14/2013

On the maturity date, earlier of the maturity date of November 14, 2013 or a merger or acquisition or other transaction pursuant to which our existing stockholders hold less than 50% of the surviving entity, or the sale of all or substantially all of our assets, or similar transaction, or event of default, each noteholder in its sole discretion shall have the option to:

convert the principal then outstanding on its Notes into shares of our common stock , or
receive immediate repayment in cash of the Notes, including any accrued and unpaid interest.

If a noteholder elects to convert its notes under the circumstances, the conversion price will be the lowest "applicable conversion price" determined for each Note. The "applicable conversion price" for each Note shall be calculated by multiplying 120% by the lowest of

the average of the high and low prices of the Company's common stock on the OTCBB averaged over the five trading days prior to the closing date of the issuance of such Note,

if the Company's common stock is not traded on the Over-The-Counter market, the closing price of the common stock reported on the Nasdaq National Market or the principal exchange on which the common stock is listed, averaged over the five trading days prior to the closing date of the issuance of such Note, or

the closing price of the Company's common stock on the OTCBB, the Nasdaq National Market, or the principal exchange on which the common stock is listed, as applicable, on the trading day immediately preceding the date such Note is converted.

We are obligated to pay interest on the Notes at an annualized rate of 8% payable in quarterly installments commencing three months after the purchase date of the Notes. We are not permitted to prepay the Notes without approval of the holders of at least a majority of the principal amount of the Notes then outstanding.

Payment of the Notes will be automatically accelerated if we enter voluntary or involuntary bankruptcy or insolvency proceedings.

The noteholders of the Notes include, among others, Atlas, an affiliate that originally recommended Shlomo Elia, one of our current directors, for appointment to the Board. The noteholders have designated Doron Roethler as bond representative to act as their agent. So long as the Notes are outstanding, the Company has agreed that it will not take certain actions without approval of the bond representative. Crystal Management Ltd., which owns $750,000 aggregate principal amount of Notes, is owned by Doron Roethler, the former Chairman of the Board and former Interim Chief Executive Officer and who currently serves as the noteholders' bond representative.

If we propose to file a registration statement to register any of our common stock under the Securities Act in connection with the public offering of such securities solely for cash, subject to certain limitations, we must give each noteholder who has converted its Notes into common stock the opportunity to include such shares of converted common stock in the registration. We have agreed to bear the expenses for any of these registrations, exclusive of any stock transfer taxes, underwriting discounts, and commissions.

EXECUTIVE COMPENSATION

Summary of Cash and Certain Other Compensation

The following table shows the annual and long-term compensation, for the fiscal years indicated, of the individual who served as the Company's Chief Executive Officer and Chief Financial Officer (together, referred to as "the named executive officers" during fiscal years 2010 and 2011.

Summary Compensation Table

Name and Principal Position	Year	Salary ($)	Option Awards ($)(1)		All Other Compensation ($)	Total ($)
Dror Zoreff	2010		$ 34,200	(3)	$ 60,000	$ 94,200
Interim President and	2011				$ 60,000	$ 60,000
Chief Executive Officer (2)						
Thaddeus J. Shalek	2010	$ 109,200	16,500	(5)	$ 2,101	$ 127,801
Chief Financial Officer (4)	2011	$ 109,200	$ 0	(5)	$ 2,184	$ 111,384

(1) Amounts do not reflect compensation actually received by the named executive officer. Instead, the amounts represent the amount of compensation cost recognized in fiscal years 2010 and 2011, as applicable, in accordance with United States Generally Accepted Accounting Principles or US GAAP, disregarding any adjustments for forfeiture assumptions. For a discussion of the assumptions used to value these awards, see Note 2 to the Company's consolidated financial statements included in its Annual Report on Form 10-K.

(2) Mr. Zoreff has served as the Chairman of the Board since May 2009, and as the Company's Interim President and Chief Executive Officer since November 2009. As Chairman of the Board, Mr. Zoreff receives $5,000 per month, $60,000 per year for his services. The compensation to Mr. Zoreff in 2010 includes $34,200 in Option Awards paid for service as Chairman of the Board and service as the Company's Interim President and Chief Executive Officer. Mr. Zoreff was not granted Option Awards in 2011. He did not otherwise receive a salary in fiscal years 2010 and 2011.

(3) On March 26, 2010, Mr. Zoreff was granted a nonqualified stock option to purchase 30,000 shares of common stock of the Company, subject to vesting at the rate of twenty-five percent (25%) for each quarter after the date of grant. The stock option is now fully exercisable.

(4) Mr. Shalek served as the Company's Interim Chief Financial Officer from August 2009, until September 2010, at which time he was promoted to Chief Financial Officer of the Company.

(5) On October 21, 2010, Mr. Shalek was granted a nonqualified stock option to purchase 15,000 shares of common stock of the Company, subject to vesting at the rate of twenty-five percent (25%) on each anniversary date, beginning on January 1, 2011. As of December 31, 2011 only twenty-five percent (25%) of the options were vested.

Outstanding Equity Awards

The following table provides information about outstanding equity awards held by the named executive officers as of December 31, 2011.

Outstanding Equity Awards at 2011 Fiscal Year-End

Name	Options Awards Number of securities underlying unexercised options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option exercise price ($/Sh)	Option expiration date
Dror Zoreff	15,000	—	$ 3.25	9/19/2018
	30,000		$ 1.14	3/25/2020
Thaddeus J. Shalek	15,000	11,250	$ 1.10	10/20/2020

(1) Market value of shares that have not vested is based on $1.20 share (the closing price of the Company's common stock as quoted on the OTCBB on December 31, 2011).

Termination and Change in Control Arrangements

The Company currently has no arrangements with any of its named executive officers with respect to payments in connection with a termination of their employment or a change in control of the Company.

Compensation of Directors

The following table summarizes the compensation paid to non-employee directors for the fiscal year ended December 31, 2011

2011 Director Compensation

Name	Fees Earned or Paid in Cash ($)	Stock Awards ($)(1)(2)	Option Awards ($) (1)(3)	All Other Compensation ($)	Total ($)
Shlomo Elia	$ -	$ 11,000		$ -	$ 11,000
Amir Elbaz	$ 18,000		$ -	$ -	$ 18,000
Robert M. Brinson, Jr. (4)	$ 5,250		$ 27,000	$ 44,970	$ 77,220

(1) Amounts represent the amount of compensation cost recognized in fiscal 2011 in accordance with US GAAP, disregarding any adjustments for forfeiture assumptions. For a discussion of the assumptions used to value these awards, see Note 2 to the Company's consolidated financial statements included in its Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

(2) At December 31, 2011, the aggregate number of shares of restricted stock underlying stock awards held by each non-employee director was as follows: Mr. Elia – 40,000.

(3) At December 31, 2011, the aggregate number of shares of common stock underlying option awards held by each non-employee director was as follows: Mr. Zoreff – 45,000, Mr. Elbaz — 20,000 and Mr. Brinson – 20,000.

(4) Robert M. Brinson, Jr. was appointed as a director effective September 14, 2011. Mr. Brinson continues to provide technical and management consulting services to the Company and is paid $10,500 per month. During 2011, he was paid a total of $44,970 in such fees in addition to director fees of $5,250.

Restricted Stock Agreements. The restricted stock agreements with Mr. Elia provide that upon a "Change in Control," the lapsing of restrictions on their restricted stock shall accelerate so as to lapse as to all of such shares on the date of such event.

A "Change in Control" shall be deemed to have occurred on the earliest of the following dates:

(i) the date on which any "person" (as such term is used in Sections 13(d) and 14(d) of the Exchange Act), other than: (A) the Company; (B) a trustee or other fiduciary holding securities under an employee benefit plan of the Company; (c) a corporation owned, directly or indirectly, by the stockholders of the Company in substantially the same proportions as their ownership of stock of the Company; or (D) the existing holders of capital stock of the Company as of the effective date hereof or their respective affiliates, is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing more than fifty percent (50%) of the combined voting power of the Company's then outstanding securities; or

(ii) on the condition that the transaction is consummated, the date the shareholders of the Company approve a definitive agreement or plan for: (A) a merger, share exchange, consolidation or reorganization involving the Company and any other corporation or other entity as a result of which securities representing more than fifty percent (50%) of the combined voting power of the Company or of the surviving or resulting corporation or entity are held in the aggregate by persons different than the persons holding those securities (including their affiliates) immediately prior to such transaction; or (B) an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets.

From April 1, 2009 until March 26, 2010, the Board had in place a compensation policy, or the April 2009 Policy, under which each non-management member of the Board was entitled to a fee of $1,500 per month. No additional monetary compensation would be received for committee service or for service as the Chairman of the Board or Chairman of the Audit Committee. However, additional monetary compensation could be awarded at the Chairman of the Board's discretion for any director incurring overnight travel to attend Board meetings or other functions for the benefit of the Company. In addition, the number of shares underlying equity award grants was set at either 40,000 shares (60,000 shares for a non-management director who was appointed the Chairman of the Board) for stock option grants or 20,000 shares (30,000 shares for a non-management director who is appointed the Chairman of the Board) for restricted stock awards.

Effective March 26, 2010, the Company's Board adopted a revised compensation policy, or the Revised Policy. Under the Revised Policy, each non-management member of the Board remained entitled to a fee of $1,500 per month. No additional monetary compensation would be received for committee service or for service as the Chairman of the Board or Chairman of the Audit Committee. However, additional monetary compensation may be awarded at the Chairman of the Board's discretion for any director incurring overnight travel to attend Board meetings or other functions for the benefit of the Company. In addition, the number of shares underlying equity award grants was decreased to either 20,000 shares (30,000 shares for a non-management director who is appointed the Chairman of the Board) for stock option grants or 10,000 shares (15,000 shares for a non-management director who is appointed the Chairman of the Board) for restricted stock awards.

On October 21, 2010, the Board granted 10,000 shares of restricted stock to Shlomo Elia, the transfer restrictions on which lapse quarterly in 25% increments, commencing January 1, 2011. The restricted stock was provided to Mr. Elia on March 31, 2011.

On September 14, 2011, the Board granted Robert M. Brinson, Jr. non-qualified stock options to acquire up to 20,000 shares of common stock at an exercise price of $1.35 per share, representing fair market value on the date of grant. The options vest quarterly in 25% increments, commencing September 14, 2011.

Equity Compensation Plans

The following table provides information, as of December 31, 2011, regarding the Company’s compensation plans (including individual compensation arrangements) under which the Company is authorized to issue equity securities.

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Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights(1) (a)	Weighted average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))(1) (c)
Equity compensation plans approved by security holders	301,900(2)	$ 2.24	4,240,604(3)
Equity compensation plans not approved by security holders	—	—	—
Total	301,900		4,240,604

(1) Refers to shares of the Company's common stock.

(2) Consists of shares issuable upon exercise of outstanding options under the Company's 2004 Equity Compensation Plan.

(3) All of the shares remaining for future issuance under the 2004 Equity Compensation Plan are available for issuance as options or restricted stock awards.

OWNERSHIP OF SECURITIES

Principal Stockholders and Share Ownership by Management

The following table sets forth information regarding beneficial ownership of the Company's common stock as of April 14, 2012 by (i) each person who is known by the Company to beneficially own more than 5% of its common stock; (ii) each person who served as a named executive officer of the Company in fiscal year 2011,, (iii) each person serving as a director or nominated for election as a director, and (iv) all current executive officers and directors as a group. Except as otherwise indicated by footnote, to the Company's knowledge, the persons named in the table below have sole voting and investment power with respect to all shares of common stock shown as beneficially owned by them.

Beneficial Owner Name and Address(1)	Amount and Nature of Beneficial Ownership(2)	Percent of Class
Atlas Capital SA(3) 118 Rue du Rhone CH-1204 Geneva, Switzerland	7,330,269	40.0%
Doron Roethler(4) c/o S. Roethler 134 Aluf David Street Ramat Gan 52236 Israel	2,418,353	13.2%
Shlomo Elia(5)	52,500	*
Dror Zoreff	45,000	*
Amir Elbaz	20,000	*
Robert M. Brinson, Jr.	20,000	*
Thaddeus Shalek	15,000	*
All officers and directors as a group (5 persons)(6)	152,500	0.82%

* Less than 1%.

(1) Unless otherwise noted, all addresses are in care of the Company at 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703.

(2) Based upon 18,352,542 shares of common stock outstanding on April 14, 2012. The number and percentage of shares beneficially owned is determined in accordance with Rule 13d-3 of the Exchange Act, and the information is not necessarily indicative of beneficial ownership for any other purpose. Under such rule, beneficial ownership includes any shares as to which the person has sole or shared voting power or investment power and also any shares that the person has the right to acquire within 60 days of April 14, 2012 through the exercise of any stock options or other rights. Any shares that a person has the right to acquire within 60 days are deemed to be outstanding for the purpose of computing the percentage ownership of such person but are not deemed outstanding for the purpose of computing the percentage ownership of any other person.

(3) Atlas Capital SA is primarily controlled by Mr. Avy Lugassy, Director.

(4) Includes (i) 1,323,619 shares owned by Greenleaf Ventures Ltd., a British Virgin Islands company, (ii) 421,791 shares owned by Crystal Management Ltd., a company registered in Anguilla, (entities controlled by Mr. Roethler) and (iii) 672,943 shares of common stock owned directly by Doron Roethler, of which 3,750 shares are held pursuant to a restricted stock award as to which restrictions had not lapsed as of April 14, 2012.

(5) Includes 10,000 shares held pursuant to a restricted stock award as to which all restrictions had not lapsed as of April 14, 2012.

(6) For all current executive officers and directors as a group, includes a total of 100,000 shares subject to options exercisable within 60 days of April 14, 2012 and 2,500 shares held pursuant to restricted stock awards as to which restrictions had not lapsed as of April 14, 2012.

Arrangements That May Result in a Change in Control

As described in detail under “Certain Relationships and Related Transactions” above, Atlas has certain relationships with the Company that, under certain circumstances, could result in Atlas obtaining a majority of the Company’s outstanding common stock in the future. As of April 12, 2012, Atlas held 7,330,269 shares of the Company’s common stock, which represents approximately 40% of the number of shares issued and outstanding, and continues to purchase the Company’s common stock from time to time. As of April 12, 2012, Atlas holds $13,575,000 aggregate principal amount of the Company’s Notes due November 14, 2013, which are convertible into the Company’s common stock on the earlier of November 14, 2013, certain change in control events, or an event of default. If the notes were converted at the conversion price applicable to the Notes as of April 14, 2012, Atlas would receive approximately 12,220,000 shares upon conversion of the Notes.

Report of the Audit Committee

The role of the Audit Committee is to assist the Board in its oversight of the quality and integrity of the Company’s financial statements, compliance with legal and regulatory requirements, qualification and independence of the Company’s independent registered public accounting firm, and performance of internal control over financial reporting. The full responsibilities of the Audit Committee are described in a written charter adopted by the Board, a copy of which is posted on the Company’s website at www.smartonline.com. The management of the Company is responsible for the preparation, presentation and integrity of the Company’s financial statements, the Company’s accounting and financial reporting principles, internal controls and procedures designed to assure compliance with accounting standards and applicable laws and regulations. The independent registered public accounting firm are responsible for auditing the Company’s financial statements and expressing an opinion as to their conformity with US GAAP.

In the performance of its oversight function, the Audit Committee has reviewed and discussed with management and the independent registered public accounting firm the audited financial statements as of and for the year ended December 31, 2011. The Audit Committee has also discussed with the independent registered public accounting firm the matters required to be discussed by Statement on Auditing Standards No. 114, as amended (AICPA, Professional Standards, Vol. 1. AU section 380), as adopted by the Public Company Accounting Oversight Board. In addition, the Audit Committee has received the written disclosures and the letter from the independent registered public accounting firm required by applicable requirements of the Public Company Accounting Oversight Board regarding the independent registered public accounting firm's communications with the Audit Committee concerning independence, and has discussed with the independent registered public accounting firm's independence.

The members of the Audit Committee in carrying out their duties are not engaged in the practice of accounting and do not act as auditors. Members of the Audit Committee rely without independent verification on the information provided to them and on the representations made by management and the independent auditors. Accordingly, the Audit Committee's oversight does not provide an independent basis to determine that management has maintained appropriate accounting and financial reporting principles or appropriate internal controls and procedures designed to assure compliance with accounting standards and applicable laws and regulations. The Audit Committee's considerations and discussions referred to above do not assure that the audit of the Company's financial statements has been carried out in accordance with US GAAP, that the financial statements are presented in accordance with US GAAP or that the Company's independent registered public accounting firm are in fact independent.

Based upon the review and discussions described in this report, and subject to the limitations on the role and responsibilities of the Audit Committee referred to above and in the Audit Committee Charter, the Audit Committee recommended to the Board that the audited financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for filing with the SEC.

THE AUDIT COMMITTEE

Amir Elbaz, Chairman
Shlomo Elia
April 30, 2012

Principal Accountant

Cherry Bekaert's report on the financial statements of the Company for each of the fiscal years ended December 31, 2010 and December 31, 2011 did not contain any adverse opinion or disclaimer of opinion, and was not qualified or modified as to uncertainty, audit scope, or accounting principles, except that the reports on the financial statements of the Company for each of the fiscal years ended December 31, 2010 and December 31, 2011 contained an explanatory paragraph expressing substantial doubt about the Company's ability to continue as a going concern.

During the fiscal years ended December 31, 2010 and 2011, neither the Company nor anyone on the Company's behalf consulted with Cherry Bekaert regarding (i) either the application of accounting principles to a specific transaction, either completed or proposed, or the type of audit opinion that might be rendered on the Company's financial statements, and Cherry Bekaert did not provide any written report or oral advice to the Company that Cherry Bekaert concluded was an important factor considered by the Company in reaching a decision as to the accounting, auditing, or financial reporting issue; or (ii) any matter that was either the subject of a "disagreement" (as defined in Item 304(a)(1)(iv) of Regulation S-K) or a "reportable event" (as defined in Item 304(a)(1)(v) of Regulation S-K).

Principal Independent Registered Public Accounting Firm Fees and Services

Audit Fees. Aggregate fees billed in 2010 and 2011 for audit services, consisting of the audit of the Company's 2009 and 2010 annual consolidated financial statements, including the reviews of the Company's Quarterly Reports on Form 10-Q filed during 2010, and assistance to the Company with its response to SEC comment letters, were approximately $204,400. Aggregate fees billed in 2010 and 2011for audit services, consisting of the audit of the Company's 2010 annual consolidated financial statements, including the reviews of the Company's Quarterly Reports on Form 10-Q filed during 2011, were approximately $74,600.

Audit-Related Fees. There were no audit-related fees billed by the principal accountant in fiscal years 2010 and 2011.

Tax Fees. The principal independent registered public accounting firm did not provide professional services related to tax compliance, tax advice, and tax planning during fiscal years 2010 and 2011.

All Other Fees. The Company was billed fees of $6,500 for technical accounting and tax research by the principal independent registered public accounting firm in fiscal year 2011 and $0 in 2010.

All audit and permissible non-audit services provided by the Company's independent registered public accounting firm, as well as the fees for such services, must be pre-approved by the Audit Committee. The Audit Committee may delegate to one or more designated members of the Audit Committee the authority to pre-approve audit and permissible non-audit services, provided such pre-approval decisions are reported to the full Audit Committee at a later time. Any pre-approval is generally for the current fiscal year, and any pre-approval is detailed as to the particular service or category of services. All audit and non-audit services provided by the Company's independent registered public accounting firm during fiscal years 2010 and 2011 were pre-approved by or on behalf of the Audit Committee.

PROPOSAL NO. 2 — RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Cherry Bekaert has acted as our independent registered public accounting firm to audit the consolidated financial statements of the Company for the fiscal year ended December 31, 2011. Cherry Bekaert has served the Company as its independent registered public accounting firm and independent auditors since April 2009. Representatives of Cherry Bekaert are not expected to be present at the Meeting, but will be available to respond to appropriate questions and make any necessary statements, if required, at the meeting via conference call.

Although the appointment of Cherry Bekaert as independent independent registered public accounting firm is not required to be submitted to a vote by stockholders, the Board believes it appropriate, as a matter of policy, to request that the stockholders ratify the appointment. If stockholder ratification (by the affirmative vote of a majority of the shares of common stock present in person or represented by proxy at the Meeting) is not received, the Audit Committee of the Board will reconsider the appointment. Even if the selection of Cherry Bekaert is ratified, the Audit Committee of the Board may, in its discretion, appoint a different firm at any time during the year if the Audit Committee feels that such a change would be in the best interests of the Company and its stockholders.

The Board recommends stockholders vote FOR ratification of Cherry Bekaert as the Company's independent registered public accounting firm for the fiscal year ending December 31, 2012.

OTHER MATTERS

Other Business

Other than the election of directors and the ratification of the appointment of independent registered public accounting firm for the Company, as described in this information statement, the Board presently knows of no other business to be conducted at the 2012 Annual Meeting of Stockholders. The Company has not received any notice from a stockholder desiring to present a proposal for consideration at the meeting, including any director nomination. Should any other business properly come before the meeting, stockholders may vote their shares in their discretion.

Stockholder Proposals for the 2013 Annual Meeting

Stockholder proposals can be eligible for inclusion in our 2013 proxy or information statement. Any such stockholder proposals must be submitted, along with proof of ownership of our stock in accordance with Rule 14a-8(b)(2) under the Exchange Act, to our principal executive offices, in care of our Corporate Secretary, Smart Online, Inc., 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703. Failure to deliver a proposal by this means may result in it not being deemed timely received. We must receive each such stockholder proposal no later than December 31, 2012 for it to be considered for inclusion in our 2013 proxy statement. We strongly encourage any stockholder interested in submitting a proposal to contact our Corporate Secretary in advance of this deadline to discuss the proposal, and stockholders may want to consult knowledgeable counsel with regard to the detailed requirements of applicable securities laws. Submitting a stockholder proposal does not guarantee that we will include it in our proxy statement. The Board will review all stockholder proposals.

Alternatively, if a stockholder does not want to submit a proposal for the 2013 annual meeting in our proxy statement under Rule 14a-8 under the Exchange Act, or intends to nominate a person as a candidate for election to the Board, the stockholder may submit the proposal or nomination not earlier than ninety (90) days or later than sixty (60) days prior to the first anniversary of the date of the 2012 Meeting, unless the date of the 2013 annual meeting is advanced by more than thirty (30) days or delayed by more than sixty (60) days from the anniversary of the 2012 Meeting (other than by adjournment), in which case such proposal or nomination must be submitted no earlier than ninety (90) days prior to the 2012 annual meeting and not later than (a) sixty (60) days prior to such annual meeting or (b) the tenth (10th) day following the calendar day on which public announcement of the date of such meeting is first made by the Company.

For our 2013 annual meeting, we must receive such proposals and nominations no earlier than March 15, 2013 and no later than April 14, 2013. If the date of the 2013 annual meeting is advanced by more than thirty (30) days or delayed by more than sixty (60) days from the anniversary of the 2011 Meeting (other than by adjournment), the stockholder must submit any such proposal or nomination no earlier than the close of business on the ninetieth (90th) day prior to the 2013 annual meeting and no later than the close of business on the later of the sixtieth (60th) day prior to the 2013 annual meeting or the tenth (10th) day following the day on which public announcement of the date of such meeting is first made. The stockholder's submission must include certain specified information concerning the proposal or nominee, as the case may be, and information as to the stockholder's ownership of our stock. We will not entertain any proposals or nominations at the annual meeting that do not meet these requirements.

If the stockholder does not also comply with the requirements of Rule 14a-4(c)(2) under the Exchange Act, we may exercise discretionary voting authority under proxies that we solicit, if any, to vote in accordance with our best judgment on any such stockholder proposal or nomination. To make a submission, stockholders should contact our Corporate Secretary via mail directed to Corporate Secretary, 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703. We strongly encourage stockholders to seek advice from knowledgeable counsel before submitting a proposal or a nomination.

Stockholder Communications with Directors

The Board, as a matter of policy, desires to facilitate communications between stockholders and directors to assist the Board in fulfilling its responsibilities to all stockholders. To that end, the Board has established a process for use by stockholders who desire to bring matters to the Board's attention. The process is intended to provide stockholders one means of communicating with directors and is not intended to be exclusive.

Any stockholder who desires to send a communication to members of the Board may submit it either by e-mail addressed to Corporate.Secretary@smartonline.com, or by mail addressed to the attention of Thaddeus Shalek at Smart Online, Inc., 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703. All such communications should include the mailing address, telephone number, and e-mail address, if any, of the person submitting the communication. All communications properly submitted under these procedures, except those deemed inappropriate as noted below, will be delivered to all members of the Board periodically, generally in advance of each regularly scheduled Board meeting. The Board has directed that the Secretary not forward communications that (a) are not reasonably related to the business of the Company, (b) concern individual grievances or other interests that are personal to the stockholder submitting the communication and that cannot reasonably be construed to present a matter of concern to stockholders generally, or (c) under community standards, contain offensive, scurrilous, or abusive content or advocate engaging in illegal activities. If the Secretary, in his or her judgment, deems a communication inappropriate under the foregoing criteria, it will be returned to the person who submitted it together with a brief explanation of the reason why it has been deemed inappropriate for delivery.

Availability of Report on Form 10-K

A copy of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 (without exhibits), including financial statements, is available at www.smartonline.com and www.iproxydirect.com/SOLN. A copy will be furnished without charge to any stockholder whose proxy is solicited hereby upon written request directed to the attention of Thaddeus Shalek, Smart Online, Inc., 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703. Copies of information is also available through the following resource:

PHONE: Call toll free 1-866-752-8683	FAX: Send this card to 202-521-3464	INTERNET: https://www.iproxydirect.com/SOLN and follow the on-screen instructions.	EMAIL: proxy@iproxydirect.com. Include your Control ID in your email.

Stockholders Sharing the Same Last Name and Address

Only one Annual Report and proxy statement may be delivered to multiple stockholders sharing an address unless the Company has received contrary instructions from one or more of the stockholders. The Company will deliver promptly upon written or oral request a separate copy of the Annual Report and proxy statement to a stockholder at a shared address to which a single copy of the documents was delivered. Requests for additional copies should be directed to the Secretary by e-mail addressed to Corporate.Secretary@smartonline.com, by mail addressed to the attention of Thaddeus Shalek at Smart Online, Inc., 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703, or by telephone at (919) 765-5000. Stockholders sharing an address and currently receiving a single copy may contact the Secretary as described above to request that multiple copies be delivered in future years. Stockholders sharing an address and currently receiving multiple copies may request delivery of a single copy in future years by contacting the Secretary as described above.

Principal Executive Offices and Annual Meeting Location

The Company's principal executive offices are located at 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703, and the main telephone number at that location is (919) 765-5000. The 2012 Annual Meeting of Stockholders will be held in the Board Room at the Company's principal executive offices on Wednesday, June 13, 2012, at 9:00 a.m. local time. Requests for directions to the meeting location may be directed to Thaddeus Shalek by telephone at (919) 765-5000 or by e-mail at Corporate.Secretary@smartonline.com.

Dated: April 30, 2012

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0em; font-size:10pt; font-family:Times New Roman">**Operating margin**
[(1)] **26.2%** 27.3% (1.1pts) **18.8%** 23.3% (4.5pts)

(1) See definitions and discussion under Non-IFRS and additional GAAP measures.

The Wireless division added 46,659 RGUs in the **third quarter** of fiscal 2018 as compared to 19,974 RGUs gained in the third quarter of fiscal 2017. The increase in the customer base reflects continued customer demand for data-centric service plans and the ongoing execution of our Wireless growth strategy to improve the network and customer experience.

Revenue highlights include:

Revenue of $237 million for the **third quarter** of fiscal 2018 was up $83 million or 53.9% over the third quarter of fiscal 2017. The increase in revenue was driven primarily by year-over-year growth in both handset and service revenue. Service revenue grew as a result of increased postpaid RGUs, and improved ARPU of $39.84 as compared to $37.05 in the third quarter of fiscal 2017.

As **compared to the second quarter** of fiscal 2018, the current quarter revenue decreased $53 million or 18.3% and ARPU increased by $1.41 or 3.7% (ARPU of $38.43 in the second quarter of fiscal 2018).

Operating income before restructuring costs and amortization highlights include:

Operating income before restructuring costs and amortization of $62 million for the **third quarter** of fiscal 2018 improved by $20 million or 47.6% over the third quarter of fiscal 2017. The improvements were driven primarily by increased subscribers and a credit of approximately $13 million for a retroactive domestic roaming rate adjustment received in the quarter offset partially by higher distribution and handset costs associated with the loading of new customers.

As **compared to the second quarter** of fiscal 2018, operating income before restructuring costs and amortization for the current quarter increased $26 million or 72.2%.

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Shaw Communications Inc.

Capital expenditures and equipment costs

	Three months ended May 31,			Nine months ended May 31,		
(millions of Canadian dollars)	**2018**	2017	Change %	**2018**	2017	Change %
Wireline						
New housing development	31	27	14.8	88	74	18.9
Success-based	57	77	(26.0)	220	219	0.5
Upgrades and enhancements	112	102	9.8	309	275	12.4
Replacement	10	6	66.7	23	19	21.1
Building and other	15	20	(25.0)	52	64	(18.8)
Total as per Note 4 to the unaudited interim consolidated financial statements	**225**	232	(3.0)	**692**	651	6.3
Wireless						
Total as per Note 4 to the unaudited interim consolidated financial statements	**68**	58	17.2	**241**	176	36.9
Consolidated total as per Note 4 to the unaudited interim consolidated financial statements	**293**	290	1.0	**933**	827	12.8

In the **third quarter** of fiscal 2018, capital investment was $293 million, a $3 million or 1% increase over the comparable period in fiscal 2017, driven by higher planned capital expenditures of $10 million in the Wireless division, $10 million in Wireline growth and upgrades related to residential and business customers and $1 million in Wireline network infrastructure and broadband capacity expansion partially offset by lower capital expenditures of $20 million in success-based equipment.

Wireline highlights include:

Success-based capital for the quarter of $57 million was $20 million lower than in the third quarter of fiscal 2017. The decrease was driven primarily by lower Video and Internet activations in the quarter.

Investment in new housing development was $31 million, a $4 million or 15% increase over the comparable period, driven by residential and commercial customer network growth and acquisition.

Wireless highlights include:

Capital investment of $68 million in the third quarter was related primarily to continued investment in network infrastructure, specifically the deployment of 700 MHz spectrum and the completion of the refarming of AWS-1 spectrum as well as back office system upgrades.

Discontinued operations

Shaw Tracking

On May 31, 2017, the Company entered an agreement to sell a group of assets comprising the operations of Shaw Tracking, a fleet tracking operation reported within the Company s Business Network Services segment. The Company determined that the assets and liabilities of the Shaw Tracking business met the criteria to be classified as a disposal group held for sale. Accordingly, the assets and liabilities of the Shaw Tracking business were classified in the consolidated statement of financial position at August 31, 2017 as current assets held for sale or current liabilities held for sale, respectively, as the sale of these assets and liabilities was expected to be completed within one year. In addition, the operating results and operating cash flows of the business are presented as discontinued operations separate from the Company s continuing operations. The transaction closed on September 15, 2017.

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(millions of Canadian dollars)	Three months ended May 31, **2018**	2017	Nine months ended May 31, **2018**	2017
Revenue		8	**1**	24
Operating, general and administrative expenses				
Employee salaries and benefits		2		5
Purchases of goods and services		5	**1**	14
		7	1	19
Amortization		(1)		(3)
Impairment of goodwill/disposal group		32		32
Loss from discontinued operations before tax		(30)		(24)
Income taxes				2
Loss from discontinued operations, net of tax, before divestiture		(30)		(26)
Loss on divestiture, net of tax			**(6)**	
Loss from discontinued operations, net of tax		(30)	**(6)**	(26)

ViaWest, Inc.

In the fourth quarter of fiscal 2017, the Company entered into an agreement to sell 100% of its wholly owned subsidiary ViaWest, Inc. (ViaWest) for proceeds of approximately USD $1.68 billion. Accordingly, the operating results and operating cash flows for the previously reported Business Infrastructure Services segment relating to ViaWest are presented as discontinued operations separate from the Company s continuing operations. The remaining operations of the previously reported Business Infrastructure Services segment and their results are now included within the Wireline segment.

(millions of Canadian dollars)	Three months ended May 31, **2018**	2017	Nine months ended May 31, **2018**	2017
Revenue		94		274
Eliminations[(1)]				(1)
		94		273
Operating, general and administrative expenses				
Employee salaries and benefits		23		67
Purchases of goods and services		33		99

	56	166
Eliminations[1]		(1)
	38	106
Amortization	34	98
Interest on long-term debt	9	27
Amortization of transaction costs	1	2
Loss from discontinued operations before tax	(6)	(21)
Income taxes	(5)	(9)
Loss from discontinued operations, net of tax	(1)	(12)

(1) Eliminations relate to intercompany transactions between continuing and discontinued operations. The costs are included in continuing operations as they continue to be incurred subsequent to the disposition.

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Supplementary quarterly financial information

Quarter	Revenue	Operating income before restructuring costs and amortization [1]	Net income (loss) from continuing operations attributable to equity shareholders	Net income (loss) attributable to equity shareholders	Net income (loss) [2]	Basic and Diluted earnings (loss) per share from continuing operations	Basic and Diluted earnings (loss) per share
(millions of Canadian dollars except per share amounts)							
2018							
Third	1,300	547	(91)	(91)	(91)	(0.18)	(0.18)
Second	1,355	501	(164)	(164)	(164)	(0.33)	(0.33)
First	1,249	481	120	114	114	0.23	0.22
2017							
Fourth	1,244	479	149	481	481	0.30	0.97
Third	1,216	511	164	133	133	0.33	0.27
Second	1,206	503	150	147	147	0.30	0.30
First	1,216	504	93	89	89	0.19	0.18
2016							
Fourth	1,212	514	145	154	154	0.29	0.31

(1) See definition and discussion under Non-IFRS and additional GAAP measures.

(2) Net income attributable to both equity shareholders and non-controlling interests

In the third quarter of fiscal 2018, net income increased $73 million compared to the second quarter of fiscal 2018 mainly due a decrease in current quarter restructuring costs of $404 million and an increase in operating income before restructuring costs and amortization. The increase was partially offset by an impairment charge of $284 million related to the Company s investment in Corus Entertainment Inc. and higher income taxes.

In the second quarter of fiscal 2018, net income decreased $278 million compared to the first quarter of fiscal 2018 mainly due to $417 million of restructuring costs recorded during the quarter related to the Company s TBT initiative and composed primarily of the costs associated with the VDP. See Other income and expense items for further details on non-operating items.

In the first quarter of fiscal 2018, net income decreased $367 million compared to the fourth quarter of fiscal 2017 mainly due to the $330 million gain on divestiture, net of tax, of ViaWest, as well as an $11 million non-operating provision recovery in the prior quarter.

In the fourth quarter of fiscal 2017, net income increased $348 million compared to the third quarter of fiscal 2017 mainly due to the gain on divestiture, net of tax, of ViaWest, and lower current quarter restructuring costs. The increase was partially offset by a decrease in operating income before restructuring costs and amortization, higher amortization, lower equity income from our investment in Corus and higher income taxes. Net other costs and revenue changed primarily due to a $14 million decrease in income from an equity accounted associate and an $11 million provision reversal related to the wind down of shomi in the quarter.

In the third quarter of fiscal 2017, net income decreased $14 million compared to the second quarter of fiscal 2017 mainly due to current quarter restructuring costs and losses on discontinued operations, net of tax, as well as increased amortization. The decrease was partially offset by an increase in operating income before restructuring costs and amortization and lower income taxes. Net other costs and revenue changed primarily due to a $16 million increase in income from an equity accounted associate and a $15 million provision reversal related to the wind down of shomi in the quarter.

In the second quarter of fiscal 2017, net income increased $58 million compared to the first quarter of fiscal 2017 mainly due to a non-recurring provision related to the wind down of shomi operations

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recorded in the first quarter, partially offset by an increase in amortization and income taxes. Also contributing to the increased net income were lower restructuring costs, partially offset by lower equity income from our investment in Corus. Net other costs and revenue changed primarily due to a provision of $107 million recorded in the prior quarter relating to shomi operations partially offset by a $17 million decrease in income from an equity accounted associate in the quarter.

In the first quarter of fiscal 2017, net income decreased $65 million compared to the fourth quarter of fiscal 2016 mainly due to a non-recurring provision related to the wind down of shomi operations included in net other costs and revenue for the current quarter. Also contributing to the decreased net income was lower operating income before restructuring costs and amortization, higher restructuring charges and lower income from discontinued operations, partially offset by lower income taxes. Net other costs and revenue changed primarily due to a $107 million impairment of the Company s joint venture investment in shomi and a $27 million increase in income from an equity accounted associate in the quarter.

In the fourth quarter of fiscal 2016 net income decreased $550 million compared to the third quarter of fiscal 2016 mainly due to lower income from discontinued operations, net of tax, relating primarily to the gain on the divestiture of the former Media division recorded in the third quarter, decreased operating income before restructuring costs and amortization, and higher income taxes. Partly offsetting the decrease in net income were decreases in net other costs and revenue and restructuring costs. Net other costs and revenue changed primarily due to non-recurring charges recorded in the third quarter, including a $54 million impairment of the Company s joint venture investment in shomi, a $20 million write-down of a private portfolio investment, $12 million in acquisition related costs and a $10 million loss from an equity accounted associate.

Other income and expense items

Restructuring costs

Restructuring costs generally include severance, employee related costs and other costs directly associated with a restructuring program. For the three-month period ended May 31, 2018, the category included an additional $13 million in restructuring charges related to the Company s TBT initiative for a total of $430 million in the nine-month period ended May 31, 2018. As a first step in the TBT, the VDP was offered to eligible employees in the second quarter of fiscal 2018. The outcome of the program had approximately 3,300 Shaw employees accepting the VDP package, representing approximately 25% of all employees. The costs related to this program make up the majority of the restructuring costs recorded in the year to date; however, in the third quarter of fiscal 2018, further organizational changes in the execution of TBT resulted in additional restructuring costs. See Introduction for further details on the TBT and the VDP.

Amortization

	Three months ended May 31,		Nine months ended May 31,	
(millions of Canadian dollars)	**2018**	2017	**2018**	2017

			Change %			Change %
Amortization revenue (expense)						
Deferred equipment revenue	**7**	9	(22.2)	**24**	29	(17.2)
Deferred equipment costs	**(27)**	(30)	(10.0)	**(85)**	(92)	(7.6)
Property, plant and equipment, intangibles and other	**(229)**	(218)	5.1	**(695)**	(634)	9.6

Amortization of property, plant and equipment, intangibles and other increased 5.1% and 9.6% for the three and nine months ended May 31, 2018 over the comparable periods due to amortization of new expenditures exceeding the amortization of assets that became fully amortized during the period.

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Amortization of financing costs and interest expense

	Three months ended May 31,			Nine months ended May 31,		
(millions of Canadian dollars)	**2018**	2017	Change %	**2018**	2017	Change %
Amortization of financing costs long-term debt		1	(100.0)	**2**	2	
Interest expense	**60**	66	(9.1)	**184**	201	(8.5)

Interest expense for the three and nine-month periods ended May 31, 2018 was lower than the comparable periods due to lower average outstanding debt balances in the current year. (See note 9 of the unaudited interim consolidated financial statements for further detail.)

Equity income (loss) of an associate or joint venture

For the three and nine-month periods ended May 31, 2018 the Company recorded equity losses of $259 million and $213 million, respectively, related to its interest in Corus, compared to equity income of $26 million and $62 million for the comparable periods. The decrease substantially reflects a $284 million impairment from the Company s investment in Corus Entertainment Inc. recorded in the third quarter of fiscal 2018.

Other gains/losses

This category generally includes realized and unrealized foreign exchange gains and losses on U.S. dollar denominated current assets and liabilities, gains and losses on disposal of property, plant and equipment and minor investments, and the Company s share of the operations of Burrard Landing Lot 2 Holdings Partnership. For the prior year nine-month period ended May 31, 2017, the category included a $92 million provision in respect of the Company s investment in shomi, which discontinued operations in fiscal 2017.

Income taxes

Income taxes are higher in the quarter compared to the third quarter of fiscal 2017 mainly due to the increase in net income and the change in applicable tax rates that occurred during the third quarter of fiscal 2017.

Financial position

Total assets were $14.1 billion at May 31, 2018 compared to $14.4 billion at August 31, 2017. The following is a discussion of significant changes in the consolidated statement of financial position since August 31, 2017.

Current assets decreased $200 million due to decreases in cash of $213 million, accounts receivable of $40 million, and assets held for sale of $61 million partially offset by increases in other current assets of $101 million and inventories of $13 million. Cash decreased as the cash outlay for investing activities and financing activities exceeded the funds provided by operations. Accounts receivable decreased primarily due to the receipt of a commodity tax refund relating to the purchase of spectrum licenses made by Freedom Mobile in fiscal 2017. Assets held for sale as at August 31, 2017 included the assets of the Shaw Tracking business, which was sold on September 15, 2017.

Other current assets increased over the period mainly due to a significant increase in Wireless subscribers participating in both the Company s MyTab plan, a discretionary wireless handset discount

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plan and MyTab Boost, a plan that allows our customers to pay less for their handset upfront if they pay a predetermined incremental charge on a monthly basis. The significant growth in handset sales was primarily related to the introduction of the iPhone to the Company s handset lineup in the second quarter of fiscal 2018 and is also contributing to the increased inventory balance.

Investments and other assets decreased by $270 million primarily due to an impairment charge of $284 million partially offset by equity income and other comprehensive income of associates both related to the Company s investment in Corus. The Company assessed its investment in Corus for indicators of impairment, which included a significant and sustained decrease in the share price as well as the recording by Corus of an impairment charge against their goodwill and broadcast license intangibles, and found that there was evidence that impairment had occurred. The Company compared the recoverable amount to the carrying value and determined that an impairment charge of $284 million was required. The recoverable amount was determined based on the value in use of the investment.

Property, plant and equipment increased $173 million due to capital investments in excess of amortization.

Current liabilities increased $24 million during the period primarily due to an increase in provisions of $181 million, partially offset by decreases in accounts payable and accrued liabilities of $85 million, income taxes payable of $39 million, and liabilities held for sale of $39 million. The increase in current provisions was mainly due to the restructuring costs related to TBT. In connection with the VDP, the Company recorded $430 million in restructuring charges primarily related to severance and other related costs, of which $110 million has been paid, $184 million is included in current provisions and $140 million is included in long-term provisions. Income taxes payable decreased due to normal course tax installment payments (net of refunds), offset by the current period provision. Accounts payable and accruals decreased due to the timing of payment and fluctuations in various payables including capital expenditures and network fees. Liabilities held for sale as at August 31, 2017 included the liabilities of the Shaw Tracking business, which was sold on September 15, 2017.

Long-term debt increased $12 million due to an increase in the Burrard Landing Lot 2 Holdings Partnership mortgage. The additional loan matures on November 1, 2024 and bears interest at 4.14% compounded semi-annually.

Other long-term liabilities decreased $83 million during the quarter primarily due to a remeasurement of the Company s defined benefit plan related to the effect of experience adjustments due to changes in demographic assumptions. The cost and related accrued benefit obligation of the Company s non-registered pension plans are determined using actuarial valuations. The actuarial valuations involve estimates and actuarial assumptions including discount rates and rate of compensation increase (financial assumptions) as well as mortality rates and retirement rates (demographic assumptions). Due to the long-term nature of the non-registered pension plans, such estimates are subject to significant uncertainty. Remeasurements related to the effect of experience adjustments arise when the non-registered pension plans experience differs from the experience expected using the actuarial assumptions, such as mortality and retirement rates.

Shareholders equity decreased $325 million mainly due to a decrease in retained earnings of $594 million partially offset by an increase in share capital of $194 million and accumulated other comprehensive income of $77 million. Share capital increased due to the issuance of 7,336,928 Class B non-voting participating shares (Class B Non-Voting Shares) under the Company s option plan and Dividend Reinvestment Plan (DRIP). Retained earnings decreased due to dividends of $454 million and a current year loss of $141 million. Accumulated other comprehensive loss decreased due to the re-measurement recorded on employee benefit plans and a change in unrealized fair value of derivatives.

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As at June 15, 2018, there were 481,817,814 Class B Non-Voting Shares, 10,012,393 Series A Shares, 1,987,607 Series B Shares and 22,420,064 Class A Shares issued and outstanding. As at June 15, 2018, 9,783,005 Class B Non-Voting Shares were issuable on exercise of outstanding options. Shaw is traded on the Toronto and New York stock exchanges and is included in the S&P/TSX 60 Index (Trading Symbols: TSX SJR.B, SJR.PR.A, SJR.PR.B, NYSE SJR, and TSXV SJR.A). For more information, please visit www.shaw.ca.

Liquidity and capital resources

In the nine-month period ended May 31, 2018, the Company generated $378 million of free cash flow. Shaw used its free cash flow along with proceeds on issuance of Class B Non-Voting Shares of $31 million, proceeds from the sale of the Shaw Tracking business of $18 million, and cash on hand to pay common share dividends of $286 million, and fund the net working capital change of $233 million.

As at May 31, 2018, the Company had $294 million of cash on hand and its $1.5 billion fully undrawn bank credit facility. The facility can be used for working capital and general corporate purposes.

As at May 31, 2018, the net debt leverage ratio for the Company is 2.0x, which is up slightly from 1.9x as at August 31, 2017. Having regard to prevailing competitive, operational and capital market conditions, the Board of Directors has determined that having this ratio in the range of 2.0 to 2.5x would be optimal leverage for the Company in the current environment. Should the ratio fall below this, other than on a temporary basis, the Board may choose to recapitalize back into this optimal range. The Board may also determine to increase the Company s debt above these levels to finance specific strategic opportunities such as a significant acquisition or repurchase of Class B Non-Voting Participating Shares in the event that pricing levels were to drop precipitously.

The Company calculates net debt leverage ratio as follows[1]:

(millions of Canadian dollars)	**May 31, 2018**	**August 31, 2017**
Current portion of Long-Term Debt	**1**	2
Long-Term Debt	**4,310**	4,298
50% of Outstanding Preferred Shares	**147**	147
Cash	**(294)**	(507)
(A) Net Debt[2]	**4,164**	3,940
Operating income before restructuring costs and amortization	**2,008**	1,997
Corus Dividends	**92**	88
(B) Adjusted operating income before restructuring costs and amortization[2]	**2,100**	2,085

(A/B) Net debt leverage ratio	**2.0x**	1.9x

(1) The following contains a description of the Company s use of non-IFRS financial measures, provides a reconciliation to the nearest IFRS measure or provides a reference to such reconciliation.
(2) These financial measures do not have standard definitions prescribed by IFRS and therefore may not be comparable to similar measures disclosed by other companies and have not been presented as an alternative to liquidity prescribed by IFRS.

The Company issued Class B Non-Voting Shares from treasury under its DRIP which resulted in cash savings and incremental Class B Non-Voting Shares of $53 million and $159 million, during the three and nine month periods ending May 31, 2018, respectively.

Shaw s credit facilities are subject to customary covenants which include maintaining minimum or maximum financial ratios.

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	Covenant Limit
Shaw Credit Facilities	
Total Debt to Operating Cash Flow [1] Ratio	< 5.00:1
Operating Cash Flow [1] to Fixed Charges [2] Ratio	> 2.00:1

(1) Operating Cash Flow, for the purposes of the covenants, is calculated as net earnings before interest expense, depreciation, amortization and current and deferred income taxes, excluding profit or loss from investments accounted for on an equity basis, for the most recently completed fiscal quarter multiplied by four, plus cash dividends and other cash distributions received in the most recently completed four fiscal quarters from investments accounted for on an equity basis.

(2) Fixed Charges are defined as the aggregate interest expense for the most recently completed fiscal quarter multiplied by four.

As at May 31, 2018, Shaw is in compliance with these covenants and based on current business plans, the Company is not aware of any condition or event that would give rise to non-compliance with the covenants over the life of the borrowings.

Based on the aforementioned financing activities, available credit facilities and forecasted free cash flow, the Company expects to have sufficient liquidity to fund operations, obligations, working capital requirements, including maturing debt, during the upcoming fiscal year. On a longer-term basis, Shaw expects to generate free cash flow and have borrowing capacity sufficient to finance foreseeable future business plans and refinance maturing debt.

Subsequent to quarter-end, on June 19, 2018, the Company established an accounts receivable securitization program with a Canadian financial institution which allows it to sell certain trade receivables into the program. As at June 28, 2018, the proceeds of the sales were committed up to a maximum of $100 million (with $40 million currently drawn under the program). The Company continues to service and retain substantially all of the risks and rewards relating to the trade receivables sold, and therefore, the trade receivables will remain recognized on the Company s Consolidated Statement of Financial Position and the funding received will be recorded as a current liability (revolving floating rate loans) secured by the trade receivables. The buyer s interest in the accounts receivable ranks ahead of the Company s interest and the program restricts it from using the trade receivables as collateral for any other purpose. The buyer of the trade receivable has no claim on any of our other assets.

Cash Flow from Operations

Operating Activities

	Three months ended May 31,			Nine months ended May 31,		
(millions of Canadian dollars)	**2018**	2017	Change %	**2018**	2017	Change %
Funds flow from continuing operations	**459**	362	26.8	**817**	1,148	(28.8)

Net change in non-cash balances related to operations	**(112)**	41	(>100.0)	**100**	(72)	>100.0
Operating activities of discontinued operations		35	(100.0)	**(2)**	69	(>100.0)
	347	438	(20.8)	**915**	1,145	(20.1)

For the three months ended May 31, 2018, funds flow from operating activities increased over the comparable period in fiscal 2017 primarily due to higher funds flow from continuing operations, which was partially offset by an increase in net change in non-cash balances related to operations. The net change in non-cash balances related to operations fluctuated over the comparative period due to changes in accounts receivable and other current asset balances, and the timing of payment of current income taxes payable and accounts payable and accrued liabilities.

<u>Investing Activities</u>

	Three months ended May 31,			Nine months ended May 31,		
(millions of Canadian dollars)	**2018**	2017	Decrease	**2018**	2017	Decrease
Cash flow used in investing activities	**(236)**	(395)	159	**(876)**	(1,040)	164

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For the three months ended May 31, 2018, the cash used in investing activities decreased over the comparable period in fiscal 2018 due primarily to lower investing activities of discontinued operations, as well as higher cash dividends received from an equity-accounted associate as compared to the prior year. This was slightly offset by higher cash outlays for inventory, capital and intangible expenditures during the three months ended May 31, 2018.

Financing Activities

The changes in financing activities during the comparative periods were as follows:

	Three months ended May 31,		Nine months ended May 31,	
(millions of Canadian dollars)	**2018**	2017	**2018**	2017
Bank loans net borrowings			**10**	
Bank facility arrangement costs		(1)		(4)
Repay 5.70% Senior unsecured notes		(400)		(400)
Senior notes issuance costs				(1)
Freedom Mobile finance lease obligations	**(1)**		**(1)**	(1)
Issuance of 3.80% Senior unsecured notes				300
Dividends	**(98)**	(98)	**(292)**	(292)
Issuance of Class B Non-Voting Shares	**4**	7	**31**	37
Financing activities of discontinued operations		4		26
	(95)	(488)	**(252)**	(335)

Capital Resources

There has been no material change in the Company s capital resources, including commitments for capital expenditures, between August 31, 2017 and May 31, 2018.

Accounting standards

The MD&A included in the Company s August 31, 2017 Annual Report outlined critical accounting policies, including key estimates and assumptions that management has made under these policies, and how they affect the amounts reported in the Consolidated Financial Statements. The MD&A also describes significant accounting policies where alternatives exist. See Critical Accounting Policies and Estimates in the Company s Management Discussion and Analysis for the year ended August 31, 2017. The condensed interim consolidated financial statements follow the same accounting policies and methods of application as the most recent annual consolidated financial statements except as described below.

Standards and amendments to standards issued but not yet effective

The Company has not yet adopted certain standards and amendments that have been issued but are not yet effective. The following pronouncements are being assessed to determine their impact on the Company s results and financial position.

IFRS 15 *Revenue from Contracts with Customers*, was issued in May 2014 and replaces IAS 11 *Construction Contracts*, IAS 18 *Revenue*, IFRIC 13 *Customer Loyalty Programs*, IFRIC 15 *Agreements for the Construction of Real Estate*, IFRIC 18 *Transfers of Assets from Customers* and SIC-31 *Revenue Barter Transactions Involving Advertising Services*. The new standard requires revenue to be recognized in a manner that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration expected to be received in exchange for those goods or services. The principles are to be applied in the following five steps: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine

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the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation.

The application of IFRS 15 will impact the Company s reported results, including the classification and timing of revenue recognition and the treatment of costs incurred to obtain contracts with customers. IFRS 15 requires the estimation of total consideration to be received over the contract term at contract inception, and the allocation of that consideration to performance obligations in the contract, typically based on the relative stand-alone selling price of each obligation. IFRS 15 also requires that incremental costs to obtain a contract with a customer (for example, commissions) be capitalized and amortized into operating expenses over time. The Company currently expenses such costs as incurred.

The Company s financial position will also be impacted by the adoption of IFRS 15, with new contract asset and contract liability categories recognized to reflect differences between the timing of revenue recognition and the actual billing of those goods and services to customers. While similar differences are recognized currently, IFRS 15 introduces additional requirements and disclosures specific to contracts with customers.

Shaw continues to evaluate the impacts of IFRS 15 and preparations are underway for the adoption of the new standard. Initial planning and scoping efforts were conducted during fiscal 2017, with ongoing development of the required accounting policies, significant judgments and estimates, processes, information systems and internal controls expected to continue throughout the Company s 2018 fiscal year. In connection with these development efforts, the Company has undertaken a significant historical data gathering initiative to identify and account for multi-year contracts with customers at the date of adoption. We are implementing a new system to enable us to comply with the requirements of IFRS 15 on a contract-by-contract basis, including appropriately allocating revenue between different performance obligations for certain revenue streams. System configuration and data validation have commenced, which we expect will continue throughout the course of fiscal 2018. At this stage in the Company s IFRS 15 implementation process, it is not possible to make reasonable quantitative estimates of the effects of the new standard. We will disclose the estimated financial impacts of IFRS 15 in our 2018 annual report.

The new standard is effective for annual periods beginning on or after January 1, 2018, which for the Company will be the annual period commencing September 1, 2018 and must be applied either retrospectively or on a modified retrospective basis for all contracts that are not complete as at that date. We intend to make a policy choice to restate each prior period presented and recognize the cumulative effect of initially applying IFRS 15 as an adjustment to the opening balance of equity at the beginning of the earliest period presented, subject to certain practical expedients we anticipate we will adopt.

IFRS 16 *Leases* requires entities to recognize lease assets and lease obligations on the balance sheet. For lessees, IFRS 16 removes the classification of leases as either operating leases or finance leases, effectively treating all leases as finance leases. Certain short-term leases (less than 12 months) and leases of low-value are exempt from the requirements and may continue to be treated as operating leases. Lessors will continue with a dual lease classification model. Classification will determine how and when a lessor will recognize lease revenue, and what assets would be recorded.

As the Company has significant contractual obligations currently being recognized as operating leases, we anticipate that the application of IFRS 16 will result in a material increase to both assets and liabilities and material changes to the timing of the recognition of expenses associated with the lease arrangements although at this stage in the Company s IFRS 16 implementation process, it is not possible to make reasonable quantitative estimates of the effects of the new standard. We have a team engaged to ensuring our compliance with IFRS 16. Our current estimate of the time and effort

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necessary to develop and implement the accounting policies, estimates and processes (including incremental requirements of our information technology systems) we will need to have in place to comply with the new standard will continue through the course of fiscal 2018.

The standard may be applied retroactively or using a modified retrospective approach for annual periods commencing January 1, 2019, which for the Company will be the annual period commencing September 1, 2019, with early adoption permitted if IFRS 15 *Revenue from Contracts with Customers* has been adopted. The Company will evaluate the adoption approach in conjunction with its assessment of the expected impacts of adoption.

Change in accounting policy

In September 2017, the IFRS Interpretations Committee (the Committee) published a summary of its agenda decision regarding accounting for interest and penalties related to income taxes, which is not specifically addressed by IFRS Standards. Although the Committee decided not to add this issue to its standard-setting agenda, the Committee noted if an entity considers a particular amount payable or receivable for interest and penalties to be an income tax, then the entity applies IAS 12 *Income Taxes* to that amount. If an entity does not apply IAS 12 to a particular amount payable or receivable for interest and penalties, it applies IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. As such, the Company retrospectively changed its accounting policy for the accounting of interest and penalties related to income taxes to be in line with the Committee decision. The change of accounting policy did not have a significant impact on the previously reported consolidated financial statements.

Related party transactions

The Company s transactions with related parties are discussed in its Management s Discussion and Analysis for the year ended August 31, 2017 under Related Party Transactions and under Note 27 of the Consolidated Financial Statements of the Company for the year ended August 31, 2017. There has been no material change in the Company s transactions with related parties between August 31, 2017 and May 31, 2018.

Financial instruments

There has been no material change in the Company s risk management practices with respect to financial instruments between August 31, 2017 and May 31, 2018. See Known Events, Trends, Risks and Uncertainties Interest Rates, Foreign Exchange Rates and Capital Markets in the Company s Management s Discussion and Analysis for the year ended August 31, 2017 and the section entitled Risk Management under Note 28 of the Consolidated Financial Statements of the Company for the year ended August 31, 2017.

Risks and uncertainties

In the second quarter, the Company introduced TBT, a multi-year initiative designed to reinvent Shaw s operating model to better meet the changing tastes and expectations of consumers and businesses by reducing staff, optimizing the use of resources, and maintaining and ultimately improving customer service. Three key elements of TBT are to: 1) shift customer interactions to digital platforms; 2) drive more self-install and self-serve; and, 3) streamline the organization that builds and services our network. As part of the TBT initiative, the Company also plans to reduce input costs, consolidate functions, and

Shaw Communications Inc.

streamline processes, which is expected to create operational improvements across the business allowing it to evolve into a more efficient organization.

There is an overall risk that the TBT initiative may not be completed in a timely and cost-effective manner to yield the expected results and benefits or result in a leaner, more integrated and agile company with improved efficiencies and execution to better meet its consumers needs and expectations (including the products and services offered to its customers). Specifically, there is a risk that the Company may not be able to: (i) establish and continue to upgrade a digital platform that will effectively engage customers digitally; (ii) successfully adopt a digital platform that will yield the expected results and benefits, including maintaining the quality of customer service, protecting the security of customer information, and coordinating the delivery of product and service offerings; (iii) deploy programs that will result in customers using the self-serve functions and electing to self-install the Company s products and services; and (iv) consolidate and streamline the functions and processes of the divisions responsible for building and servicing its networks. The realization of any of these risks may have a material adverse effect on Shaw, its operations and/or financial results.

As a first step in the TBT, the VDP was offered to eligible employees. The outcome of the program had approximately 3,300 Shaw employees accepting the VDP package representing approximately 25% of all employees. As part of the program design, the majority of customer-facing employees (i.e., Customer Care, Retail, Sales) were not eligible to participate in the VDP. A large portion of employees who elected to participate in the VDP are in functions that will be addressed through the aforementioned key elements of the TBT and Shaw has control over the timing of employee departures across the Company through an actively managed, orderly transition over the next 18 months. In select functions, the Company determined that some employees will transition over a 24-month period, an extension from the 18-month period initially expected. Approximately 1,200 employees will be exiting before the end of fiscal 2018. For a detailed discussion of the restructuring charge, anticipated annual cost reduction, and VDP related cost reductions in fiscal 2018, see Introduction.

With approximately 3,300 employees accepting the VDP package, there is a risk that the Company may not be able to: (i) complete the employee exits with minimal impact on business operations within the anticipated timeframes and for the budgeted amounts, (ii) replace or outsource the functions performed by certain key employees that have accepted the VDP package in a manner that aligns with customer expectations which may have a material adverse effect on the Company s business operations, (iii) continue to operate the business in the normal course, and maintain or improve customer services, (iv) maintain employee morale as a result of the organizational changes, staff and cost reductions; (v) ensure that the staff reductions will reduce costs, and achieve the financial goals, cost competitiveness and profitability required to be attractive to investors. In addition, there can be no assurance that restructuring costs of the VDP will be limited to the budgeted amounts or that the expected annualized cost reductions from the VDP (including reductions in operating and capital expenditures), and the VDP related cost reductions in fiscal 2018 will be realized within the expected time frames or at all. The realization of any of these risks may have a material adverse effect on Shaw, its operations and/or financial results.

Other significant risks and uncertainties affecting the Company and its business are discussed in the Company s MD&A for the fiscal year ended August 31, 2017 under Known Events, Trends, Risks and Uncertainties.

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Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(unaudited)

(millions of Canadian dollars)	**May 31, 2018**	August 31, 2017
ASSETS		
Current		
Cash	**294**	507
Accounts receivable	**246**	286
Inventories	**122**	109
Other current assets *[note 5]*	**256**	155
Assets held for sale *[note 3]*		61
	918	1,118
Investments and other assets *[notes 14 and 15]*	**667**	937
Property, plant and equipment	**4,517**	4,344
Other long-term assets *[note 14]*	**297**	255
Deferred income tax assets	**4**	4
Intangibles	**7,450**	7,435
Goodwill	**280**	280
	14,133	14,373
LIABILITIES AND SHAREHOLDERS EQUITY		
Current		
Accounts payable and accrued liabilities	**828**	913
Provisions *[note 6]*	**257**	76
Income taxes payable	**112**	151
Unearned revenue	**218**	211
Current portion of long-term debt *[notes 9 and 14]*	**1**	2
Liabilities held for sale *[note 3]*		39
	1,416	1,392
Long-term debt *[notes 9 and 14]*	**4,310**	4,298
Other long-term liabilities *[notes 7 and 16]*	**31**	114
Provisions *[note 6]*	**211**	67
Deferred credits	**466**	490
Deferred income tax liabilities	**1,870**	1,858
	8,304	8,219
Shareholders equity *[notes 10 and 12]*		
Common and preferred shareholders	**5,828**	6,153

Non-controlling interests in subsidiaries	**1**	1
	5,829	6,154
	14,133	14,373

See accompanying notes.

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Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF INCOME (LOSS)

(unaudited)

	Three months ended May 31,		Nine months ended May 31,	
(millions of Canadian dollars)	**2018**	2017	**2018**	2017
Revenue *[note 4]*	**1,300**	1,216	**3,904**	3,638
Operating, general and administrative expenses *[note 8]*	**(753)**	(705)	**(2,375)**	(2,120)
Restructuring costs *[notes 6 and 8]*	**(13)**	(43)	**(430)**	(54)
Amortization:				
Deferred equipment revenue	**7**	9	**24**	29
Deferred equipment costs	**(27)**	(30)	**(85)**	(92)
Property, plant and equipment, intangibles and other	**(229)**	(218)	**(695)**	(634)
Operating income from continuing operations	**285**	229	**343**	767
Amortization of financing costs long-term debt		(1)	**(2)**	(2)
Interest expense	**(60)**	(66)	**(184)**	(201)
Equity income of an associate or joint venture *[note 15]*	**(259)**	26	**(213)**	62
Other gains (losses)	**1**	19	**3**	(91)
Income (loss) from continuing operations before income taxes	**(33)**	207	**(53)**	535
Current income tax expense *[note 4]*	**18**	41	**96**	109
Deferred income tax expense (recovery)	**40**	2	**(14)**	18
Net income (loss) from continuing operations	**(91)**	164	**(135)**	408
Loss from discontinued operations, net of tax *[note 3]*		(31)	**(6)**	(38)
Net income (loss)	**(91)**	133	**(141)**	370
Net income (loss) from continuing operations attributable to:				
Equity shareholders	**(91)**	164	**(135)**	408
Loss from discontinued operations attributable to:				
Equity shareholders		(31)	**(6)**	(38)
		(31)	**(6)**	(38)
Basic earnings (loss) per share *[note 11]*				
Continuing operations	**(0.18)**	0.33	**(0.28)**	0.82
Discontinued operations		(0.06)	**(0.01)**	(0.08)

	(0.18)	0.27	**(0.29)**	0.74
Diluted earnings (loss) per share *[note 11]*				
Continuing operations	**(0.18)**	0.33	**(0.28)**	0.82
Discontinued operations		(0.06)	**(0.01)**	(0.08)
	(0.18)	0.27	**(0.29)**	0.74

See accompanying notes.

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Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited)

(millions of Canadian dollars)	Three months ended May 31, **2018**	2017	Nine months ended May 31, **2018**	2017
Net income (loss)	**(91)**	133	**(141)**	370
Other comprehensive income (loss) *[note 12]*				
Items that may subsequently be reclassified to income:				
Continuing operations:				
Change in unrealized fair value of derivatives designated as cash flow hedges	**1**	1	**4**	2
Adjustment for hedged items recognized in the period	**1**	(1)	**3**	(2)
Share of other comprehensive income (loss) of associates	**2**	(3)	**7**	7
Discontinued operations:				
Exchange differences on translation of a foreign operation		14		28
Exchange differences on translation of US denominated debt hedging a foreign operation		(6)		(12)
	4	5	**14**	23
Items that will not subsequently be reclassified to income:				
Remeasurements on employee benefit plans:				
Continuing operations		(17)	**63**	
	4	(12)	**77**	23
Comprehensive income (loss)	**(87)**	121	**(64)**	393
Comprehensive income (loss) attributable to:				
Equity shareholders	**(87)**	121	**(64)**	393

See accompanying notes.

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Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

(unaudited)

Nine months ended May 31, 2018

	Attributable to equity shareholders						
[millions of Canadian dollars]	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Total	Equity attributable to non-controlling interests	Total equity
Balance as at September 1, 2017	**4,090**	**30**	**2,164**	**(131)**	**6,153**	**1**	**6,154**
Net loss			**(141)**		**(141)**		**(141)**
Other comprehensive income				**77**	**77**		**77**
Comprehensive income (loss)			**(141)**	**77**	**(64)**		**(64)**
Dividends			**(294)**		**(294)**		**(294)**
Dividend reinvestment plan	**159**		**(159)**				
Shares issued under stock option plan	**35**	**(4)**			**31**		**31**
Share-based compensation		**2**			**2**		**2**
Balance as at May 31, 2018	**4,284**	**28**	**1,570**	**(54)**	**5,828**	**1**	**5,829**

Nine months ended May 31, 2017

	Attributable to equity shareholders						
[millions of Canadian dollars]	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Total	Equity attributable to non-controlling interests	Total equity
Balance as at September 1, 2016	3,799	42	1,908	(52)	5,697	1	5,698
Net income			370		370		370
Other comprehensive income				23	23		23
Comprehensive income			370	23	393		393
Dividends			(296)		(296)		(296)
Dividend reinvestment plan	149		(149)				
Shares issued under stock option plan	45	(7)			38		38
Share-based compensation		3			3		3

Balance as at May 31, 2017	3,993	38	1,833	(29)	5,835	1	5,836

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Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(millions of Canadian dollars)	Three months ended May 31, **2018**	2017	Nine months ended May 31, **2018**	2017
OPERATING ACTIVITIES				
Funds flow from continuing operations *[note 13]*	**459**	362	**817**	1,148
Net change in non-cash balances related to continuing operations	**(112)**	41	**100**	(72)
Operating activities of discontinued operations		35	**(2)**	69
	347	438	**915**	1,145
INVESTING ACTIVITIES				
Additions to property, plant and equipment *[note 4]*	**(231)**	(251)	**(833)**	(736)
Additions to equipment costs (net) *[note 4]*	**(11)**	(21)	**(37)**	(58)
Additions to other intangibles *[note 4]*	**(29)**	(27)	**(84)**	(72)
Net additions to inventories	**11**	(14)	**(14)**	(30)
Proceeds on sale of discontinued operations *[note 3]*			**18**	
Net additions to investments and other assets	**23**	(31)	**65**	(50)
Proceeds on disposal of property, plant and equipment	**1**		**9**	
Investing activities of discontinued operations		(51)		(94)
	(236)	(395)	**(876)**	(1,040)
FINANCING ACTIVITIES				
Increase in long-term debt			**10**	300
Debt repayments *[note 9]*	**(1)**	(400)	**(1)**	(402)
Bank facility arrangement costs		(1)		(4)
Issue of Class B Non-Voting Shares *[note 10]*	**4**	7	**31**	37
Dividends paid on Class A Shares and Class B Non-Voting Shares	**(96)**	(96)	**(286)**	(286)
Dividends paid on Preferred Shares	**(2)**	(2)	**(6)**	(6)
Financing activities of discontinued operations		4		26
	(95)	(488)	**(252)**	(335)
Increase (decrease) in cash	**16**	(445)	**(213)**	(230)
Cash, beginning of the period	**278**	620	**507**	405
Cash of continuing operations, end of the period	**294**	175	**294**	175

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Shaw Communications Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

May 31, 2018 and 2017

[all amounts in millions of Canadian dollars, except share and per share amounts]

1. CORPORATE INFORMATION

Shaw Communications Inc. (the Company) is a diversified Canadian connectivity company whose core operating business is providing: Cable telecommunications, Satellite video services and data networking to residential customers, businesses and public-sector entities (Wireline); and wireless services for voice and data communications (Wireless). The Company s shares are listed on the Toronto Stock Exchange (TSX), TSX Venture Exchange and New York Stock Exchange.

2. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

Statement of compliance

These condensed interim consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) and in compliance with International Accounting Standard (IAS) 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board (IASB).

The condensed interim consolidated financial statements of the Company for the three and nine months ended May 31, 2018 were approved by the Audit Committee and authorized for issue on June 27, 2018.

Basis of presentation

These condensed interim consolidated financial statements have been prepared primarily under the historical cost convention except as detailed in the significant accounting policies disclosed in the Company s consolidated financial statements for the year ended August 31, 2017 and are expressed in millions of Canadian dollars unless otherwise indicated. The condensed interim consolidated statements of income are presented using the nature classification for expenses.

Certain comparative figures have been reclassified to conform to the current period s presentation.

The notes presented in these condensed interim consolidated financial statements include only significant events and transactions occurring since the Company s last fiscal year end and are not fully inclusive of all matters required to be disclosed by IFRS in the Company s annual consolidated financial statements. As a result, these condensed interim consolidated financial statements should be read in conjunction with the Company s consolidated financial statements for the year ended August 31, 2017.

The condensed interim consolidated financial statements follow the same accounting policies and methods of application as the most recent annual consolidated financial statements except as noted below.

Standards and amendments to standards issued but not yet effective

The Company has not yet adopted certain standards and amendments that have been issued but are not yet effective. The following pronouncements are being assessed to determine their impact on the Company s results and financial position.

IFRS 15 *Revenue from Contracts with Customers,* was issued in May 2014 and replaces IAS 11 *Construction Contracts,* IAS 18 *Revenue,* IFRIC 13 *Customer Loyalty Programs,* IFRIC 15 *Agreements for the Construction of Real Estate*, IFRIC 18 *Transfers of Assets from Customers* and SIC-31 *Revenue Barter Transactions Involving Advertising Services*. The new standard requires revenue to be recognized in a manner that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration expected to be received in exchange for those goods or services. The principles are to be applied in the following five steps: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the

Shaw Communications Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation.

The application of IFRS 15 will impact the Company s reported results, including the classification and timing of revenue recognition and the treatment of costs incurred to obtain contracts with customers. IFRS 15 requires the estimation of total consideration to be received over the contract term at contract inception, and the allocation of that consideration to performance obligations in the contract, typically based on the relative stand-alone selling price of each obligation. IFRS 15 also requires that incremental costs to obtain a contract with a customer (for example, commissions) be capitalized and amortized into operating expenses over time. The Company currently expenses such costs as incurred.

The Company s financial position will also be impacted by the adoption of IFRS 15, with new contract asset and contract liability categories recognized to reflect differences between the timing of revenue recognition and the actual billing of those goods and services to customers. While similar differences are recognized currently, IFRS 15 introduces additional requirements and disclosures specific to contracts with customers.

Shaw continues to evaluate the impacts of IFRS 15 and preparations are underway for the adoption of the new standard. Initial planning and scoping efforts were conducted during fiscal 2017, with ongoing development of the required accounting policies, significant judgments and estimates, processes, information systems and internal controls expected to continue throughout the Company s 2018 fiscal year. In connection with these development efforts, the Company has undertaken a significant historical data gathering initiative to identify and account for multi-year contracts with customers at the date of adoption. We are implementing a new system to enable us to comply with the requirements of IFRS 15 on a contract-by-contract basis, including appropriately allocating revenue between different performance obligations for certain revenue streams. System configuration and data validation have commenced, which we expect will continue throughout the course of fiscal 2018. At this stage in the Company s IFRS 15 implementation process, it is not possible to make reasonable quantitative estimates of the effects of the new standard. We will disclose the estimated financial impacts of IFRS 15 in our 2018 annual report.

The new standard is effective for annual periods beginning on or after January 1, 2018, which for the Company will be the annual period commencing September 1, 2018 and must be applied either retrospectively or on a modified retrospective basis for all contracts that are not complete as at that date. We intend to make a policy choice to restate each period presented and recognize the cumulative effect of initially applying IFRS 15 as an adjustment to the opening balance of equity at the beginning of the earliest period presented, subject to certain practical expedients we anticipate we will adopt.

IFRS 16 *Leases* requires entities to recognize lease assets and lease obligations on the balance sheet. For lessees, IFRS 16 removes the classification of leases as either operating leases or finance leases, effectively treating all leases as finance leases. Certain short-term leases (less than 12 months) and leases of low-value are exempt from the requirements and may continue to be treated as operating leases. Lessors will continue with a dual lease classification model. Classification will determine how and when a lessor will recognize lease revenue, and what assets would be recorded.

As the Company has significant contractual obligations currently being recognized as operating leases, we anticipate that the application of IFRS 16 will result in a material increase to both assets and liabilities and material changes to the timing of the recognition of expenses associated with the lease arrangements although at this stage in the Company s IFRS 16 implementation process, it is not possible to make reasonable quantitative estimates of the effects of the new standard. We have a team engaged to ensuring our compliance with IFRS 16. Our current estimate of the time and effort necessary to develop and implement the accounting policies, estimates and processes (including incremental requirements of our

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Shaw Communications Inc.

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information technology systems) we will need to have in place to comply with the new standard will continue through the course of fiscal 2018.

The standard may be applied retroactively or using a modified retrospective approach for annual periods commencing January 1, 2019, which for the Company will be the annual period commencing September 1, 2019, with early adoption permitted if IFRS 15 *Revenue from Contracts with Customers* has been adopted. The Company will evaluate the adoption approach in conjunction with its assessment of the expected impacts of adoption.

Discontinued operations

The Company reports financial results for discontinued operations separately from continuing operations to distinguish the financial impact of disposal transactions from ongoing operations. Discontinued operations reporting occurs when the disposal of a component or a group of components of the Company represents a strategic shift that will have a major impact on the Company s operations and financial results, and where the operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the Company.

The results of discontinued operations are excluded from both continuing operations and business segment information in the condensed interim consolidated financial statements and the notes to the condensed interim consolidated financial statements, unless otherwise noted, and are presented net of tax in the statement of income for the current and comparative periods. Refer to Note 3 Discontinued Operations for further information regarding the Company s discontinued operations.

Change in accounting policy

In September 2017, the IFRS Interpretations Committee (the Committee) published a summary of its agenda decision regarding accounting for interest and penalties related to income taxes, which is not specifically addressed by IFRS Standards. Although the Committee decided not to add this issue to its standard-setting agenda, the Committee noted if an entity considers a particular amount payable or receivable for interest and penalties to be an income tax, then the entity applies IAS 12 *Income Taxes* to that amount. If an entity does not apply IAS 12 to a particular amount payable or receivable for interest and penalties, it applies IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. As such, the Company retrospectively changed its accounting policy for the accounting of interest and penalties related to income taxes to be in line with the Committee decision. The change of accounting policy did not have a significant impact on the previously reported consolidated financial statements.

3. DISCONTINUED OPERATIONS

Shaw Tracking

In the third quarter of fiscal 2017, the Company entered into an agreement to sell a group of assets comprising the operations of Shaw Tracking, a fleet tracking operation reported within the Company s Wireline segment, for proceeds of approximately USD $20, net of working capital adjustments. Accordingly, the operating results and operating cash flows of the Tracking business are presented as discontinued operations separate from the Company s continuing operations.

The transaction closed on September 15, 2017 and the Company recognized a loss on the divestiture within income from discontinued operations as follows:

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Shaw Communications Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

May 31, 2018 and 2017

[all amounts in millions of Canadian dollars, except share and per share amounts]

	May 31, 2018
Proceeds on disposal, net of transaction costs of $nil	**18**
Net assets disposed	**(22)**
	(4)
Income taxes	**2**
Loss on divestiture, net of tax	**(6)**

The assets and liabilities disposed of were as follows:

	$
Accounts receivable	**6**
Inventories	**5**
Other current assets	**1**
Other long-term assets	**25**
Goodwill	**24**
	61
Accounts payable and accrued liabilities	**8**
Deferred credits	**33**
Deferred income tax liabilities	**(2)**
	22

A reconciliation of the major classes of line items related to Shaw Tracking constituting income from discontinued operations, net of tax, as presented in the consolidated statements of income is as follows:

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Revenue		8	**1**	24

Operating, general and administrative expenses			
Employee salaries and benefits	2		5
Purchases of goods and services	5	**1**	14
	7	**1**	19
Amortization	(1)		(3)
Impairment of goodwill/disposal group	32		32
Loss from discontinued operations before tax	(30)		(24)
Income taxes			2
Loss from discontinued operations, net of tax, before divestiture	(30)		(26)
Loss on divestiture, net of tax		**(6)**	
Loss from discontinued operations, net of tax	(30)	**(6)**	(26)

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Shaw Communications Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

May 31, 2018 and 2017

[all amounts in millions of Canadian dollars, except share and per share amounts]

ViaWest

In the fourth quarter of fiscal 2017, the Company entered into an agreement to sell 100% of its wholly owned subsidiary ViaWest, Inc. (ViaWest) for proceeds of approximately USD $1.68 billion. Accordingly, the operating results and operating cash flows for the previously reported Business Infrastructure Services segment are presented as discontinued operations separate from the Company s continuing operations. Prior period financial information has been reclassified to present the Business Infrastructure Services division of the Company as a discontinued operation.

A reconciliation of the major classes of line items related to ViaWest constituting income from discontinued operations, net of tax, as presented in the consolidated statements of income is as follows:

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Revenue		94		274
Eliminations[1]				(1)
		94		273
Operating, general and administrative expenses				
Employee salaries and benefits		23		67
Purchases of goods and services		33		99
		56		166
Eliminations[1]				(1)
		38		106
Amortization		34		98
Interest on long-term debt		9		27
Amortization of transaction costs		1		2
Loss from discontinued operations before tax		(6)		(21)
Income taxes		(5)		(9)
Loss from discontinued operations, net of tax		(1)		(12)

(2) Eliminations relate to intercompany transactions between continuing and discontinued operations. The costs are included in continuing operations as they continue to be incurred subsequent to the disposition.

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Shaw Communications Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

May 31, 2018 and 2017

[all amounts in millions of Canadian dollars, except share and per share amounts]

4. BUSINESS SEGMENT INFORMATION

The Company s chief operating decision makers are the CEO, President and CFO and they review the operating performance of the Company by segments which comprise of Wireline and Wireless. The chief operating decision makers utilize operating income before restructuring costs and amortization for each segment as a key measure in making operating decisions and assessing performance. As a result of the restructuring undertaken in 2017, the Company reorganized and integrated its management structure, previously separated in the Consumer and Business Network Services segments, into a combined Wireline segment, as costs were becoming increasingly inseparable between these segments. There was no change to the Wireless operating segment.

The Wireline segment provides Cable telecommunications services including Video, Internet, Wi-Fi, Phone, Satellite Video and data networking through a national fibre-optic backbone network to Canadian consumers, North American businesses and public-sector entities. The Wireless segment provides wireless services for voice and data communications serving customers in Ontario, British Columbia and Alberta.

The previously reported Business Infrastructure Services segment was comprised primarily of the ViaWest operations and as a result, the majority of this segment is now reported in discontinued operations. The remaining operations and their results are now included within the Wireline segment.

Both of the Company s reportable segments are substantially located in Canada. Information on operations by segment is as follows:

Operating information

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Revenue				
Wireline	**1,064**	1,063	**3,205**	3,207
Wireless				
Service	**155**	122	**428**	355
Equipment and other	**82**	32	**274**	78
	237	154	**702**	433

	1,301	1,217	**3,907**	3,640
Intersegment eliminations	**(1)**	(1)	**(3)**	(2)
	1,300	1,216	**3,904**	3,638
Operating income before restructuring costs and Amortization				
Wireline	**485**	469	**1,397**	1,417
Wireless	**62**	42	**132**	101
	547	511	**1,529**	1,518
Restructuring costs	**(13)**	(43)	**(430)**	(54)
Amortization	**(249)**	(239)	**(756)**	(697)
Operating income	**285**	229	**343**	767
Current taxes				
Operating	**29**	52	**116**	133
Other/non-operating	**(11)**	(11)	**(20)**	(24)
	18	41	**96**	109

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Shaw Communications Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

May 31, 2018 and 2017

[all amounts in millions of Canadian dollars, except share and per share amounts]

Capital expenditures

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Capital expenditures accrual basis				
Wireline	**213**	209	**652**	588
Wireless	**68**	58	**241**	176
	281	267	**893**	764
Equipment costs (net of revenue)				
Wireline	**12**	23	**41**	63
Capital expenditures and equipment costs (net)				
Wireline	**225**	232	**692**	651
Wireless	**68**	58	**241**	176
	293	290	**933**	827
Reconciliation to Consolidated Statements of Cash Flows				
Additions to property, plant and equipment	**231**	251	**833**	736
Additions to equipment costs (net)	**11**	21	**37**	58
Additions to other intangibles	**29**	27	**84**	72
Total of capital expenditures and equipment costs (net) per Consolidated Statements of Cash Flows	**271**	299	**954**	866
Increase/decrease in working capital and other liabilities related to capital expenditures	**22**	(11)	**(15)**	(44)
Decrease in customer equipment financing receivables	**1**	2	**3**	5
Less: Proceeds on disposal of property, plant and equipment	**(1)**		**(9)**	
	293	290	**933**	827

Total capital expenditures and equipment costs (net) reported by segments	

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5. OTHER CURRENT ASSETS

	May 31, 2018	August 31, 2017
	$	$
Prepaid expenses	106	99
Wireless handset receivables[1]	150	56
	256	155

(1) As described in the revenue and expenses accounting policy detailed in the significant accounting policies disclosed in the Company s consolidated financial statements for the year ended August 31, 2017, these amounts relate to the current portion of wireless handset discounts receivable.

6. PROVISIONS

	Asset retirement obligations	**Restructuring**	**Other**	**Total**
	$	**$**	**$**	**$**
Balance as at September 1, 2017	60	7[1]	76	143
Additions	**2**	**430** [2]	**19**	**451**
Accretion	**1**			**1**
Reversal			**(7)**	**(7)**
Payments		**(113)**	**(7)**	**(120)**
Balance as at May 31, 2018	**63**	**324**	**81**	**468**
Current		7	69	76
Long-term	60		7	67
Balance as at September 1, 2017	60	7	76	143

Current		**184**	**73**	**257**
Long-term	**63**	**140**	**8**	**211**
Balance as at May 31, 2018	**63**	**324**	**81**	**468**

(1) During fiscal 2017, the Company restructured certain operations within the Wireline segment and announced a realignment to integrate certain Consumer/Business operations and Freedom Mobile. The majority of the remaining costs are expected to be paid in the current year.

(2) During the second quarter of fiscal 2018, the Company offered a voluntary departure program to a group of eligible employees and in the third quarter made additional changes to its organizational structure as part of a total business transformation initiative. In connection with the restructuring, the Company recorded $430 primarily related to severance and employee related costs in respect of the approximate 3,300 affected employees. A total of $110 has been paid in fiscal 2018. The remaining costs are expected to be paid out within the next 32 months.

7. OTHER LONG-TERM LIABILITIES

	May 31, 2018	August 31, 2017
	$	$
Pension liabilities *[note 16]*	**22**	99
Post retirement liabilities	**7**	5
Other	**2**	10
	31	114

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8. OPERATING, GENERAL AND ADMINISTRATIVE EXPENSES AND RESTRUCTURING COSTS

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Employee salaries and benefits	**188**	244	**993**	656
Purchase of goods and services	**578**	504	**1,812**	1,518
	766	748	**2,805**	2,174

9. LONG-TERM DEBT

	May 31, 2018			August 31, 2017		
	Long-term debt at amortized cost $	**Adjustment for finance costs $**	**Long-term debt repayable at maturity $**	Long-term debt at amortized cost $	Adjustment for finance costs $	Long-term debt repayable at maturity $
Corporate						
Cdn fixed rate senior notes-						
5.65% due October 1, 2019	**1,248**	**2**	**1,250**	1,247	3	1,250
5.50% due December 7, 2020	**499**	**1**	**500**	498	2	500
3.15% due February 19, 2021	**298**	**2**	**300**	298	2	300
4.35% due January 31, 2024	**498**	**2**	**500**	498	2	500
3.80% due March 1, 2027	**298**	**2**	**300**	298	2	300
6.75% due November 9, 2039	**1,419**	**31**	**1,450**	1,419	31	1,450
	4,260	**40**	**4,300**	4,258	42	4,300
Other						
Freedom Mobile - other	**1**		**1**	2		2
Burrard Landing Lot 2 Holdings Partnership[1]	**50**		**50**	40		40

Total consolidated debt	**4,311**	**40**	**4,351**	4,300	42	4,342
Less current portion [2]	**1**	**1**	**2**	2		2
	4,310	**39**	**4,349**	4,298	42	4,340

[1] In February 2018, the Partnership refinanced its debt. The Partnership received an additional mortgage loan of $30 and used the proceeds to loan excess funds to each of its partners, of which the Company received $10. The additional loan matures on November 1, 2024 and bears interest at 4.14% compounded semi-annually.

[2] Current portion of long-term debt includes amounts due within one year in respect of Freedom Mobile s finance lease obligations.

10. SHARE CAPITAL

Changes in share capital during the nine months ended May 31, 2018 are as follows:

	Class A Shares		**Class B Non-Voting Shares**		**Series A Preferred Shares**		**Series B Preferred Shares**	
	Number	$	Number	$	Number	$	Number	$
August 31, 2017	22,420,064	2	474,350,861	3,795	10,012,393	245	1,987,607	48
Issued upon stock option plan exercises			1,302,690	35				
Issued pursuant to dividend reinvestment plan			6,034,238	159				
May 31, 2018	**22,420,064**	**2**	**481,687,789**	**3,989**	**10,012,393**	**245**	**1,987,607**	**48**

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11. EARNINGS (LOSS) PER SHARE

Earnings (loss) per share calculations are as follows:

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Numerator for basic and diluted earnings per share ($)				
Net income (loss) from continuing operations	**(91)**	164	**(135)**	408
Deduct: dividends on Preferred Shares	**(2)**	(2)	**(6)**	(6)
Net income (loss) attributable to common shareholders from continuing operations	**(93)**	162	**(141)**	402
Net loss from discontinued operations		(31)	**(6)**	(38)
Net loss from discontinued operations attributable to common shareholders		(31)	**(6)**	(38)
Net income (loss) attributable to common shareholders	**(93)**	131	**(147)**	364
Denominator (millions of shares)				
Weighted average number of Class A Shares and Class B Non-Voting Shares for basic earnings per share	**503**	492	**500**	490
Effect of dilutive securities [(1)]	**1**	1	**1**	1
Weighted average number of Class A Shares and Class B Non-Voting Shares for diluted earnings per share	**504**	493	**501**	491
Basic earnings (loss) per share ($)				
Continuing operations	**(0.18)**	0.33	**(0.28)**	0.82
Discontinued operations		(0.06)	**(0.01)**	(0.08)

Attributable to common shareholders	**(0.18)**	0.27	**(0.29)**	0.74
Diluted earnings (loss) per share ($)				
Continuing operations	**(0.18)**	0.33	**(0.28)**	0.82
Discontinued operations		(0.06)	**(0.01)**	(0.08)
Attributable to common shareholders	**(0.18)**	0.27	**(0.29)**	0.74

(1) The earnings per share calculation does not take into consideration the potential dilutive effect of certain stock options since their impact is anti-dilutive. For the three and nine months ended May 31, 2018, 5,800,939 (2017 1,158,659) and 4,200,298 (2017 3,566,228) options were excluded from the diluted earnings per share calculation, respectively.

12. OTHER COMPREHENSIVE INCOME AND ACCUMULATED OTHER COMPREHENSIVE LOSS

Components of other comprehensive income and the related income tax effects for the nine months ended May 31, 2018 are as follows:

	Amount $	Income taxes $	Net $
Items that may subsequently be reclassified to income			
Continuing operations:			
Change in unrealized fair value of derivatives designated as cash flow hedges	**6**	**(2)**	**4**
Adjustment for hedged items recognized in the period	**4**	**(1)**	**3**
Share of other comprehensive income of associates	**7**		**7**
	17	**(3)**	**14**
Items that will not be subsequently be reclassified to income			
Remeasurements on employee benefit plans:			
Continuing operations	**85**	**(22)**	**63**
	102	**(25)**	**77**

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Components of other comprehensive income and the related income tax effects for the three months ended May 31, 2018 are as follows:

	Amount $	Income taxes $	Net $
Items that may subsequently be reclassified to income			
Continuing operations:			
Change in unrealized fair value of derivatives designated as cash flow hedges	**2**	**(1)**	**1**
Adjustment for hedged items recognized in the period	**1**		**1**
Share of other comprehensive income of associates	**2**		**2**
	5	**(1)**	**4**

Components of other comprehensive income and the related income tax effects for the nine months ended May 31, 2017 are as follows:

	Amount $	Income taxes $	Net $
Items that may subsequently be reclassified to income			
Change in unrealized fair value of derivatives designated as cash flow hedges	3	(1)	2
Adjustment for hedged items recognized in the period	(3)	1	(2)
Share of other comprehensive income of associates	7		7
Exchange differences on translation of a foreign operation	28		28
Exchange differences on translation of US denominated debt hedging a foreign operation	(12)		(12)
	23		23

Components of other comprehensive loss and the related income tax effects for the three months ended May 31, 2017 are as follows:

	Amount $	**Income taxes $**	**Net $**
Items that may subsequently be reclassified to income			
Change in unrealized fair value of derivatives designated as cash flow hedges	2	(1)	1
Adjustment for hedged items recognized in the period	(2)	1	(1)
Share of other comprehensive income of associates	(3)		(3)
Exchange differences on translation of a foreign operation	14		14
Exchange differences on translation of US denominated debt hedging a foreign operation	(6)		(6)
	5		5
Items that will not be subsequently be reclassified to income			
Remeasurements on employee benefit plans:			
Continuing operations	(23)	6	(17)
	(18)	6	(12)

Accumulated other comprehensive loss is comprised of the following:

	May 31, 2018 $	August 31, 2017 $
Items that may subsequently be reclassified to income		
Continuing operations:		
Change in unrealized fair value of derivatives designated as cash flow hedges	**(1)**	(8)
Share of other comprehensive income of associates	**15**	8
Items that will not be subsequently reclassified to income		
Remeasurements on employee benefit plans:		
Continuing operations	**(68)**	(131)
	(54)	(131)

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13. STATEMENTS OF CASH FLOWS

Disclosures with respect to the Consolidated Statements of Cash Flows are as follows:

(i) Funds flow from continuing operations

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Net income (loss) from continuing operations	**(91)**	164	**(135)**	408
Adjustments to reconcile net income (loss) to funds flow from operations:				
Amortization	**249**	240	**758**	698
Deferred income tax expense	**40**	2	**(14)**	18
Share-based compensation		1	**2**	3
Defined benefit pension plans	**4**	4	**12**	8
Accretion of long-term liabilities and provisions	**(1)**		**(2)**	(1)
Equity (income) loss of an associate or joint venture	**259**	(26)	**213**	(62)
Provision for investment loss		(15)		96
Other	**(1)**	(8)	**(17)**	(20)
Funds flow from continuing operations	**459**	362	**817**	1,148

(ii) Interest and income taxes paid and interest received and classified as operating activities are as follows:

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Interest paid	**90**	96	**207**	250
Income taxes paid (net of refunds)	**(28)**	15	**136**	204
Interest received	**1**		**3**	

(iii) Non-cash transactions:

The Consolidated Statements of Cash Flows exclude the following non-cash transactions:

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Issuance of Class B Non-Voting Shares:				
Dividend reinvestment plan	**53**	50	**159**	149

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14. FAIR VALUE

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Financial instruments

The fair value of financial instruments has been determined as follows:

(i) Current assets and current liabilities
The fair value of financial instruments included in current assets and current liabilities approximates their carrying value due to their short-term nature.

(ii) Investments and other assets and other long-term assets
The fair value of publicly traded investments is determined by quoted market prices. Investments in private entities which do not have quoted market prices in an active market and whose fair value cannot be readily measured are carried at cost. No published market exists for such investments. These equity investments have been made as they are considered to have the potential to provide future benefit to the Company and accordingly, the Company has no current intention to dispose of these investments in the near term. The fair value of long-term receivables approximates their carrying value as they are recorded at the net present values of their future cash flows, using an appropriate discount rate.

(iii) Long-term debt

The carrying value of long-term debt is at amortized cost based on the initial fair value as determined at the time of issuance or at the time of a business acquisition. The fair value of publicly traded notes is based upon current trading values. The fair value of finance lease obligations is determined by discounting future cash flows using a rate for loans with similar terms, conditions and maturity dates. The carrying value of bank credit facilities approximates fair value as the debt bears interest at rates that fluctuate with market values. Other notes and debentures are valued based upon current trading values for similar instruments.

(iv) Other long-term liabilities

The fair value of contingent consideration arising from a business acquisition is determined by calculating the present value of the probability weighted assessment of the likelihood that revenue targets will be met and the estimated timing of such payments.

(v) Derivative financial instruments

The fair value of US currency forward purchase contracts is determined by an estimated credit-adjusted mark-to-market valuation using observable forward exchange rates at the end of reporting periods and contract forward rates.

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The carrying values and estimated fair values of long-term debt and a contingent liability are as follows:

	May 31, 2018		August 31, 2017	
	Carrying value $	**Estimated fair value $**	Carrying value $	Estimated fair value $
Liabilities				
Long-term debt (including current portion) [1]	**4,311**	**4,819**	4,300	4,901

[1] Level 2 fair value determined by valuation techniques using inputs based on observable market data, either directly or indirectly, other than quoted prices.

15. INVESTMENTS AND OTHER ASSETS

Corus Entertainment Inc.

In connection with the sale of the Media division to Corus in 2016, the Company received 71,364,853 Corus Class B non-voting participating shares (the Corus B Consideration Shares) representing approximately 37% of Corus total issued equity of Class A and Class B shares. The Company agreed to retain approximately one third of its Corus B Consideration Shares for 12 months post-closing, a second one third for 18 months post-closing and the final one third for 24 months post-closing. The Company also agreed to have its Corus B Consideration Shares participate in Corus dividend reinvestment plan while subject to these retention periods until September 1, 2017. For the three and nine months ended May 31, 2018, the Company received dividends of $23 (2017 $22) and $69 (2017 $65) from Corus, of which $nil (2017 $20) and $nil (2017 $61) were reinvested in additional Corus Class B shares, respectively. At May 31, 2018, the Company owned 80,630,383 (2017 79,119,000) Corus Class B shares having a trading value of $501 (2017 $1,056) and representing 38% (2017 39%) of Corus total issued equity of Class A and Class B shares. The Company s weighted average ownership of Corus for the months ended May 31, 2018 was 39% (2017 39%). As of September 1, 2017, the Company s Corus B Consideration Shares no longer participate in Corus dividend reinvestment plan.

Summary financial information for Corus and reconciliation with the carrying amount of the investment in the unaudited interim condensed consolidated balance sheets is as follows:

	May 31, 2018	August 31, 2017
Current assets	**572**	525
Non-current assets	**4,414**	5,543
Current liabilities	**(605)**	(604)
Non-current liabilities	**(2,732)**	(2,864)
Net assets	**1,649**	2,600
Less: non-controlling interests	**(157)**	(159)
	1,492	2,441
Carrying amount of the investment less accumulated impairment losses	**622**	897

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Summarized statement of earnings of Corus:

	Three months ended May 31,		Nine months ended May 31,	
	2018	2017	**2018**	2017
Revenue	**441**	462	**1,268**	1,298
Net income (loss) attributable to:				
Shareholders	**(936)**	67	**(818)**	163
Non-controlling interest	**7**	9	**20**	25
	(929)	76	**(798)**	188
Other comprehensive income (loss), attributable to shareholders	**5**	(7)	**18**	20
Comprehensive income (loss)	**(924)**	69	**(780)**	208
Equity income from associates, excluding goodwill impairment	**25**	26	**71**	62
Impairment of investment in associate[1]	**(284)**		**(284)**	
Equity income from associates[2]	**(259)**	26	**(213)**	62
Other comprehensive income (loss) from equity accounted associates[2]	**2**	(3)	**7**	7
	(257)	23	**(206)**	69

(1) The Company assessed its investment in Corus for indicators of impairment, which included a significant and sustained decrease in the share price as well as the recording by Corus of an impairment charge against their goodwill and broadcast license intangibles, and found that there was evidence that impairment had occurred. The Company compared the recoverable amount to the carrying value and determined that an impairment charge of $284 million was required. The recoverable amount was determined based on the value in use of the investment.

(2) The Company s share of income and other comprehensive income reflect the weighted average proportion of Corus net income and other comprehensive income attributable to shareholders for the three and nine months

periods ended May 31, 2018 and 2017.

16. EMPLOYEE BENEFIT PLANS

Defined benefit pension plans

The Company has two non-registered retirement plans for designated executives and senior executives. The following is a summary of the accrued benefit liabilities recognized in the statement of financial position.

	May 31, 2018 **$**	**August 31, 2017** **$**
Non-registered plans		
Accrued benefit obligation	**455**	532
Fair value of plan assets	**433**	433
Accrued benefit liabilities and deficit	**22**	99

The plans expose the Company to a number of risks, of which the most significant are as follows:

(i) Volatility in market conditions: The accrued benefit obligations are calculated using discount rates with reference to bond yields closely matching the term of the estimated cash flows while many of the assets are invested in other types of assets. If plan assets underperform these yields, this will result in a deficit. Changing market conditions in conjunction with discount rate volatility will result in volatility of the accrued benefit liabilities. To minimize some of the investment risk, the Company has established long-term funding targets where the time horizon and risk tolerance are specified.

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(ii) Selection of accounting assumptions: The calculation of the accrued benefit obligations involves projecting future cash flows of the plans over a long-time frame. This means that assumptions used can have a material impact on the statements of financial position and comprehensive income because in practice, future experience of the plans may not be in line with the selected assumptions.

Non-registered pension plans

The Company provides a supplemental executive retirement plan (SERP) for certain of its senior executives. Benefits under this plan are based on the employees length of service and their highest three-year average rate of eligible pensionable earnings during their years of service. In 2012, the Company closed the plan to new participants and amended the plan to freeze base salary levels at August 31, 2012 for purposes of determining eligible pensionable earnings. Employees are not required to contribute to this plan.

The Company provides an executive retirement plan (ERP) for certain executives not covered by the SERP. Benefits under this plan are comprised of defined contribution and defined benefit components and are based on the employees length of service as well as final average earnings during their years of service. Employees are not required to contribute to this plan.

The table below shows the change in benefit obligation and funding status and the fair value of plan assets.

	SERP $	ERP $	Total $
Accrued benefit obligation, as at September 1, 2017	518	14	532
Current service cost	**4**	**4**	**8**
Remeasurements:			
Effect of experience adjustments(1)	**(85)**		**(85)**
Accrued benefit obligation, as at May 31, 2018	**437**	**18**	**455**
Fair value of plan assets, as at September 1, 2017	**420**	**13**	**433**
Employer contributions			
Fair value of plan assets, as at May 31, 2018	**420**	**13**	**433**
Accrued benefit liability and plan deficit, as at May 31, 2018	**17**	**5**	**22**

(1) In the second quarter of the fiscal year, a remeasurement related to the effect of experience adjustments of $85 was recognized to reflect the decrease in the accrued benefit obligation due to demographic experience in the quarter.

The cost and related accrued benefit obligation of the Company s non-registered pension plans are determined using actuarial valuations. The actuarial valuations involve estimates and actuarial assumptions including discount rates and rate of compensation increase (financial assumptions) as well as mortality rates and retirement rates (demographic assumptions). Due to the long-term nature of the non-registered pension plans, such estimates are subject to significant uncertainty. Remeasurements related to the effect of experience adjustments arise when the non-registered pension plans experience differs from the experience expected using the actuarial assumptions.

17. SUBSEQUENT EVENT

On June 19, 2018 the Company established an accounts receivable securitization program with a Canadian financial institution which will allow it to sell certain trade receivables into the program up to a maximum of $100. The Company will continue to service and retain substantially all of the risks and rewards relating to the trade receivables sold, and therefore, the trade receivables will remain recognized on the Company s Consolidated Statement of Financial Position and the funding received will be recorded as a current liability (revolving floating rate loans) secured by the trade receivables. The buyer s interest in the accounts receivable ranks ahead of the Company s interest and the program restricts it from using the trade receivables as collateral for any other purpose. The buyer of the trade receivables has no claim on any of the Company s other assets. Sale proceeds in respect of the new securitization program of approximately $40 were received on June 19, 2018.

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