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MCGILL UNIVERSITY







Teknion

Teknion.com

Teknion:  
integrated design.  
infinite possibilities.



Teknion

TeknionFolio

Teknion presents Folio

Folio is the definitive selection of business furniture for the contemporary office from Teknion's diverse, yet integrated, product portfolio. Folio comprises products drawn from several categories unmatched in the contract furnishings industry for design, quality and value, demonstrating that simple, functional furniture can be elegant. **TEKNION:** integrated design. infinite possibilities.







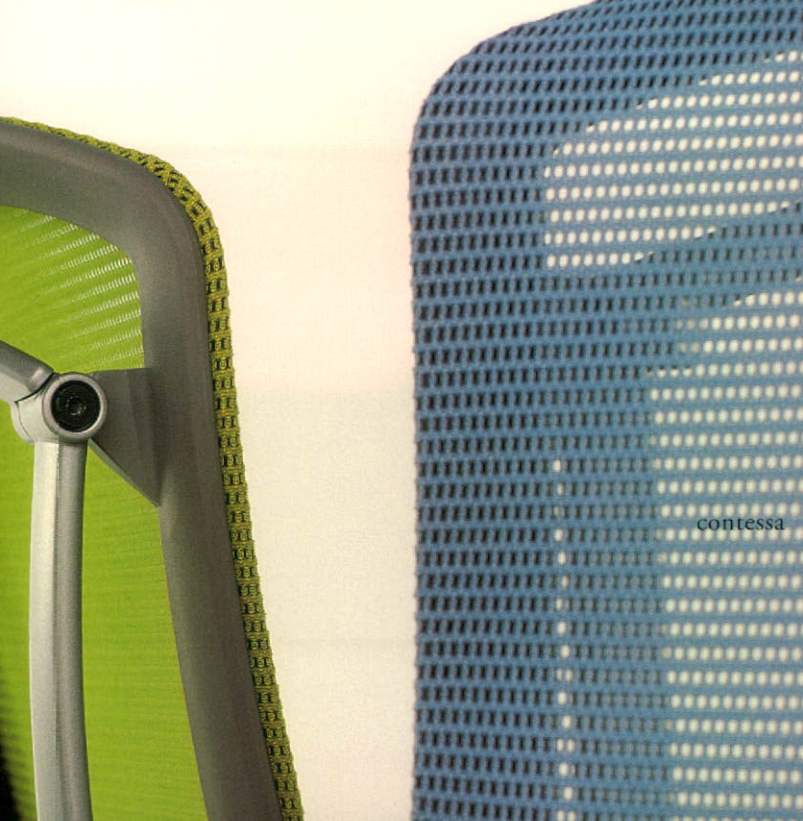
altos











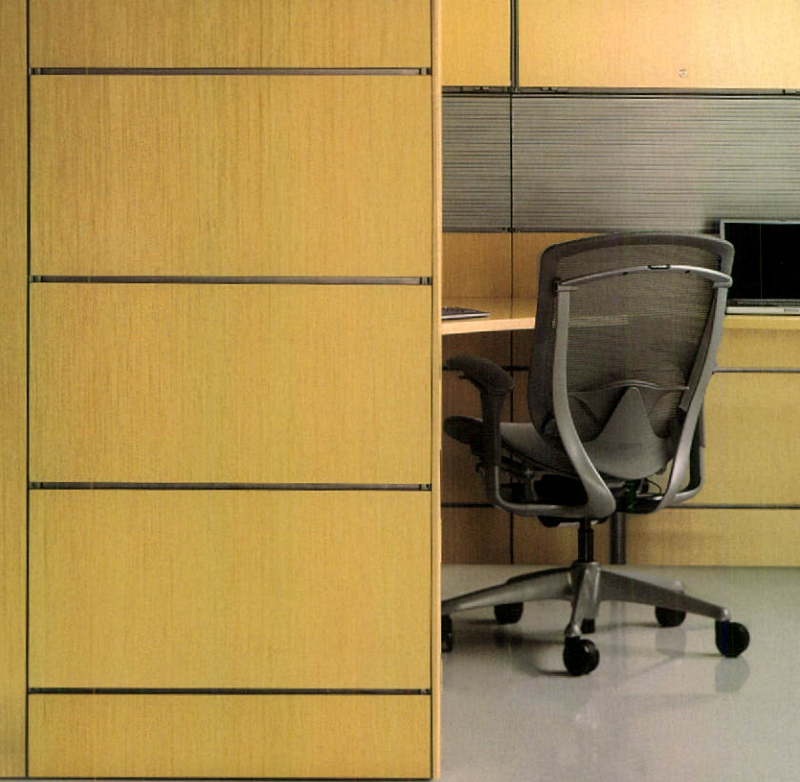
contessa







origami and altos





transit wood







aegis





solitär





nami







transit and xm





xm







ie bench





tux



altos / Altos® is a full-height, architectural wall system that offers a clean, modern aesthetic and incorporates functional design. It combines privacy and elegance to create a unique statement while complementing building interiors.



ie / Designed around the concept of a post-and-beam structure, ie™ is a European-inspired alternative to panel-based furniture. ie provides an architectural framework that defines interior and exterior spaces.



contessa / Contessa refines the qualities of the mesh office chair with its sense of lightness and form-fitting suspension. The chair seat and back are available in a variety of mesh colors, and an extended selection of seat upholstery options is offered.



origami and altos / Origami™ is a modular wood casegoods line whose overlapping and wrapping surfaces are inspired by the art form. The interplay of a variety of finish options makes it possible to customize and express individual creativity.



transit wood / Transit® is a high-performance system that offers freedom from the design limitations inherent in traditional panel systems. Continuous off-modular capability provides superior planning capabilities and expands planning options.



aegis / The Aegis® bench alludes to the rational forms of classic and mid-century modernism. The collection is ideal for application in private offices, reception areas or public lobbies.



solitär / Solitär smoothly incorporates design details that combine such elements as polished wood, leather and metal. Its lightly scaled freestanding pieces are designed to offer a creative alternative to traditional furniture.



nami / The Nami™ stacking chair combines the spare elegance of modern European design with comfort and lightweight agility. Inspired by a cresting wave, Nami's sculpted back and seat have a gentle controlled flex that moves with the body.





transit and xm / Transit includes the xm® collection of worksurfaces that incorporates the design qualities of Teknion's xm product – an elegant aesthetic that draws from classic furniture forms.



xm / Rational in concept, elegant in form, xm is an intelligent response to the new ways that people work. xm is furniture that acts as architecture to define space. It adapts readily to ever-evolving work practices and meets varied planning needs.



ie / ie worksurfaces link in either post-and-beam or freestanding applications to create a Big Table or Bench that are ideal for call centers or touch-down spaces.



tux / Tux seating has crisp, well-tailored lines that convey an impression of quiet elegance and ease. Exposed chrome legs and base lend a fresh modern accent.

**Teknion** is a leading international designer, manufacturer and marketer of office systems and related products for the contract segment of the office furniture industry. We are the market share leader in Canada, with an expanding presence overseas, and over the past decade have been among the fastest growing major office furniture companies in the United States.

## Financial Highlights

November 30 (\$000 except per share amounts)	2005	2004	2003	2002	2001
<b>STATEMENT OF EARNINGS DATA</b>					
Sales	606,183	497,345	502,788	525,800	785,528
EBITDA*	24,093	6,970	(22,591)	(26,374)	77,357
Earnings (loss) from operations	5,411	(15,119)	(49,435)	(54,636)	53,800
Net earnings (loss)	(20,654)	(17,810)	(30,112)	(32,006)	35,829
Earnings (loss) per share (basic)	\$ (0.32)	\$ (0.28)	\$ (0.47)	\$ (0.50)	\$ 0.56

November 30 (\$000)	2005	2004	2003	2002	2001
<b>BALANCE SHEET DATA</b>					
Total assets	394,847	386,053	412,125	463,589	512,940
Net debt**	70,419	53,234	46,867	51,805	54,008
Shareholders' equity	213,442	234,533	256,744	290,139	322,780

\* EBITDA is a non-GAAP financial measure and is defined as earnings before interest, income taxes, depreciation and amortization.

\*\* Net debt is defined as operating loans plus long-term debt less cash.

## Dear fellow shareholders,

2005 was another year of significant accomplishment for Teknion.

We grew our revenues by 22% to \$606 million, compared to sales of \$497 million in 2004. On an exchange rate adjusted basis, our revenues grew by 28% – more than double the industry average of 12% reported by BIFMA, the Business and Institutional Furniture Manufacturers Association.

Our progress was broad-based. In each of our markets – the United States, Canada and International – we grew our revenue in all four quarters of the fiscal year. And in each of our markets, we realized considerable increases: 25% in the United States; 11% in Canada; and 49% in our International division.

Equally important, we achieved substantial improvements in our operations. Earnings from operations before depreciation increased by 250% (to \$25 million) – an \$18 million improvement realized in spite of the challenges posed by currency and commodity prices. These results build on the \$17 million increase in operating earnings achieved in 2004.

We achieved these improvements primarily in three ways.

First, we executed our sales and marketing strategies, launching new product programs, and working with our dealers to grow our revenue in all of our markets. Second, we continued to carefully manage our selling, general and administrative expenditures, reducing our SG&A expense as a percentage of sales, to its lowest level since 1999. And last, we increased our manufacturing efficiency, implementing two facility consolidations while supporting a substantial increase in sales volume.

We also continued to actively extend the depth and breadth of our product range to leverage our distribution and provide our customers with an even more comprehensive offering of innovative, integrated, design-driven office furniture. We launched the **ie** office system in the U.S. market. Designed and developed in Europe, **ie** offers an alternative to traditional panel formats. Its post-and-beam structure acts as an architectural framework, delivering unlimited planning possibilities. We are extremely pleased with the reception that **ie** has received in the market.

We also continued to broaden our customer base, building on the successes of the past couple of years, particularly in the U.S. government, health and educational areas, and exceeding our sales objectives in those sectors.

The U.S. market remains our largest opportunity. On a source currency basis, U.S. sales increased in fiscal 2005 by 32%. Revenues throughout the company accelerated towards the end of 2005, and sales of \$173 million in the fourth quarter were the strongest in almost five years.

**LOOKING AHEAD**

Our primary economic challenge is the impact of the U.S./Canadian dollar exchange rate on our bottom line. The continuing weakness of the U.S. dollar reinforces the need for us to continue to achieve operating improvements.

Overall, however, we are encouraged by the buoyant activity that we are seeing in all our markets, and as a result, we are confident that we can continue to grow our business in 2006.

The operating environment continues to be strong. Industry shipments grew by 9% in January, marking the 24th consecutive month of positive year-over-year comparisons, and BIFMA forecasts industry growth of 8% in 2006.

We are well-positioned to capitalize on the continued recovery in demand for contract office furniture. Our expanding product offering continues to build on one of Teknion's key competitive strengths – integrated design that delivers infinite possibilities to our customers. Our international presence remains strong and we continue to selectively look for opportunities where we can leverage our product and service strengths. In August we officially opened a showroom in Bangalore, India, which we expect will achieve a meaningful role in our overall international business. In the United States, our largest market, we continue to gain share. And in Canada, we are the leader in the contract furniture business, a tribute to our extensive dealer base and long-standing customer relationships.

The significant improvement in our operating earnings in 2005 – and in particular our strong fourth-quarter results – demonstrates the positive impact of our strategies in the market and the effectiveness of our cost reduction and efficiency initiatives. We are pleased with the initial results of our efforts, and encouraged by the prospects for even more success. We intend to build on these initiatives in 2006 and beyond.

On behalf of our entire management team, we would like to thank our employees for their hard work and commitment, the members of our Board of Directors for their guidance and leadership, and our customers, dealers and shareholders for their continued support.



**DAVID FELDBERG**  
President and Chief Executive Officer



**SAUL FELDBERG**  
Chairman of the Board



## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management's discussion and analysis of the financial condition and results of operations for Teknion Corporation ("Teknion" or the "Company") for the years ended November 30, 2005 and 2004, should be read in conjunction with the Company's consolidated financial statements and the notes to those statements. In addition, the Company's continuous disclosure filings are available at [www.sedar.com](http://www.sedar.com).

### OVERVIEW

Teknion is an international designer, manufacturer and marketer of office systems and related products such as seating, storage, filing and tables. The Company's primary product offering is office systems, which accounted for a majority of the Company's sales in fiscal 2005. The Company's operations include approximately 2.5 million square feet of vertically integrated manufacturing space, sales and marketing operations, and showrooms located in major markets around the world. The Company's products are sold through authorized dealers.

From 1994 through 2000 the Company grew at a compound annual growth rate in excess of 40%. Over this period, Teknion consistently outperformed the overall contract office furniture industry as measured by the Business and Institutional Furniture Manufacturers Association (BIFMA). Teknion attributes its superior track record of growth over this period to its ability to introduce new and innovative products, expand into new geographic markets and increase market share.

Beginning in mid-2001 and continuing throughout fiscal 2003, the contract office furniture industry experienced an unprecedented decline in demand. The estimated total annual production of office furniture in the U.S. declined from approximately U.S. \$13 billion in 2000 to U.S. \$8.4 billion in fiscal 2003. In late fiscal 2003, the rate of decline subsided, and in fiscal 2004, the industry grew to U.S. \$8.8 billion. During fiscal 2005 the industry continued to grow, reaching U.S. \$10 billion.

Given the significant change in market conditions since 2001, the Company has successfully improved its cost structure. Manufacturing space has been consolidated, selling, general and administrative costs have been significantly reduced, and the Company's Malaysian and U.K. operations have been restructured. These activities, coupled with the Company's continued focus on improving manufacturing efficiency and reducing input costs, have had a significant positive impact. However, the high prices of commodities, including steel, fuel and its derivatives, and further weakening of the U.S. dollar have mitigated, to a considerable extent, the benefit of the Company's initiatives. In addition to focusing on its cost structure, Teknion has continued to introduce innovative award-winning office products. The Company considers that this strategy is not only key to growth but will result in a more sustainable revenue base during changing economic conditions. New product highlights in 2005 included the Almanac line of customizable, high-capacity workstation and freestanding storage, the Universal Overhead Storage Cabinet with its curved profile and refined front door mechanism, and the Lyft collection of thin panels and screens that allows users to cost effectively enhance existing panel systems by introducing new ways of planning their workspaces. Also, Teknion expanded its environmentally friendly fabric offering with the introduction of Mardi Gras and Martini Eco Intelligent® polyester seating fabrics incorporating a new manufacturing process that does not generate pollutants.

## RESULTS OF OPERATIONS

## Annual

Years ended November 30,  
(000 except per share amounts)

	2005	2004	2003
Sales	\$ 606,183	\$ 497,345	\$ 502,788
Gross margin	\$ 165,894	\$ 140,637	\$ 137,878
Gross margin (% of sales)	27.4%	28.3%	27.4%
Earnings (loss) before income taxes	\$ 494	\$ (18,301)	\$ (52,824)
Net loss	\$ (20,654)	\$ (17,810)	\$ (30,112)
Loss per share (basic and diluted)	\$ (0.32)	\$ (0.28)	\$ (0.47)
Total assets	\$ 394,847	\$ 386,053	\$ 412,125
Long-term debt	\$ 16,087	\$ 18,424	\$ 22,428
Multiple voting shares	39,920	39,920	39,955
Subordinate voting shares	24,196	24,181	24,132

## Quarterly

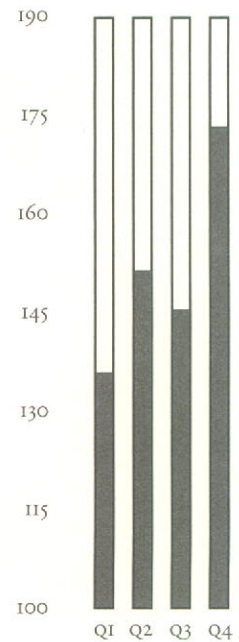
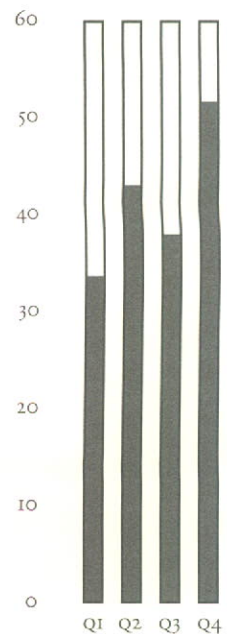
Fiscal 2005  
(000 except per share amounts)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Sales	\$ 135,859	\$ 151,584	\$ 145,605	\$ 173,135	\$ 606,183
Gross margin	\$ 33,645	\$ 42,817	\$ 37,778	\$ 51,654	\$ 165,894
Gross margin (% of sales)	24.8%	28.2%	25.9%	29.8%	27.4%
Earnings (loss) before income taxes	\$ (6,095)	\$ 448	\$ (3,022)	\$ 9,163	\$ 494
Net earnings (loss)	\$ (6,323)	\$ 234	\$ (3,246)	\$ (11,319)	\$ (20,654)
Loss per share (basic and diluted)	\$ (0.10)	\$ (0.00)	\$ (0.05)	\$ (0.17)	\$ (0.32)

## Quarterly

Fiscal 2004  
(000 except per share amounts)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Sales	\$ 114,339	\$ 126,392	\$ 118,626	\$ 137,988	\$ 497,345
Gross margin	\$ 31,170	\$ 38,534	\$ 31,652	\$ 39,281	\$ 140,637
Gross margin (% of sales)	27.3%	30.5%	26.7%	28.5%	28.3%
Earnings (loss) before income taxes	\$ (8,155)	\$ 353	\$ (8,784)	\$ (1,715)	\$ (18,301)
Net earnings (loss)	\$ (4,082)	\$ 1,416	\$ (5,235)	\$ (9,909)	\$ (17,810)
Earnings (loss) per share (basic and diluted)	\$ (0.06)	\$ 0.02	\$ (0.08)	\$ (0.16)	\$ (0.28)

2005  
QUARTERLY SALES  
(in thousands of dollars)2005  
QUARTERLY GROSS  
MARGIN  
(in thousands of dollars)



The fluctuation in quarterly results is largely a function of sales volume and product mix. In addition, during fiscal 2005, the Company incurred costs to exit two facilities and combine these operations into existing premises. Furthermore, in order to improve manufacturing capacity, a product line was moved from one facility to another. In total approximately \$3.3 million was incurred relating to facility exit and moving costs. By quarter these expenses were recorded as follows: first quarter \$1.0 million, second quarter \$1.4 million, third quarter \$250 thousand and fourth quarter \$630 thousand. In the fourth quarter of 2005, another factor that affected the operating results was favorable realty tax assessments relating to certain facilities, increasing earnings before income taxes by \$2.1 million and gross margin by 1% of sales. In addition, fourth quarter 2005 sales of \$173.1 million resulted in considerably improved earnings before income taxes as the Company benefited from positive operating leverage on sales that were significantly above the Company's estimated current break-even sales level. The improvement of approximately \$18.8 million for the year in earnings before income taxes is particularly significant as it was achieved notwithstanding the negative impact of the weakening of the U.S. dollar. With respect to the net loss in the fourth quarter of fiscal 2005 and 2004, an adjustment to the Company's valuation allowance for future tax assets was recorded, totaling \$20.3 million and \$8.1 million respectively, and is discussed below under the heading Income Taxes.

GEOGRAPHIC SALES  
(as percentages of total sales)



## Sales

### Sales by Geographic Region

Teknion's sales represented by geographic region are set forth below.

(000)						
Years ended November 30,	2005	%	2004	%	2003	%
Canada	\$ 204,731	33.8	\$ 184,751	37.1	\$ 197,211	39.2
United States	341,667	56.3	272,438	54.8	263,853	52.5
International	59,785	9.9	40,156	8.1	41,724	8.3
Total	\$ 606,183	100	\$ 497,345	100	\$ 502,788	100

Sales for the year ended November 30, 2005, were \$606.2 million, an increase of 21.9% compared to the prior year. Despite significant sales growth, reported sales were negatively impacted by the decline in value of the U.S. dollar relative to the Canadian dollar and would have increased by approximately 28% in fiscal 2005 if the relative value of the currencies had remained the same as the prior year.

Sales in fiscal 2004 were \$497.3 million as compared to \$502.8 million in 2003, a decline of 1%. The decrease in sales in fiscal 2004 reflects the impact of the decline in value of the U.S. dollar. Sales would have increased by approximately 5% if the relative value of the currencies had not changed.

### Canada

Canadian sales grew 10.8% in fiscal 2005 as compared to a decline of 6.3% in 2004 over 2003. The growth in 2005 resulted from increased activity in small and mid-sized commercial projects and reflects both the underlying strength of the Canadian economy and Teknion's ability to maintain its leading position.

On a quarterly basis Canadian sales were as follows: first quarter \$45.7 million, second quarter \$60.1 million, third quarter \$42.0 million and fourth quarter \$56.9 million. The second quarter is typically the strongest quarter in the year for the Canadian market, while the third quarter is typically the weakest. These trends were repeated in fiscal 2005. The year ended with strong fourth quarter sales, 35.4% higher than the third quarter and 18.2% higher than the fourth quarter of the prior year.

#### United States

The following table reflects U.S. sales in U.S. dollars:

(000)			
Years ended November 30	2005	2004	2003
U.S. Sales	<b>U.S. \$273,178</b>	U.S. \$207,448	U.S. \$184,330

Sales in the U.S. increased 25.4% in Canadian dollars to \$341.7 million; however, when measured in U.S. dollars, the increase was 31.7%. Teknion continued to gain market share in the U.S. as growth exceeded the 12.4% growth rate of the industry overall as reported by BIFMA for fiscal 2005. In fiscal 2004, in source currency the Company also exceeded industry growth, increasing by 12.5% as compared to 4.5% for the industry as reported by BIFMA. The success of Teknion's strategy to broaden its customer base to the government and health and education sectors continued to fuel growth. In addition, the introduction in 2005 of a "quick ship" program for small orders also helped, particularly in the third and fourth quarters. These initiatives, coupled with strong commercial project activity and focused market strategies, resulted in an outstanding year in this market.

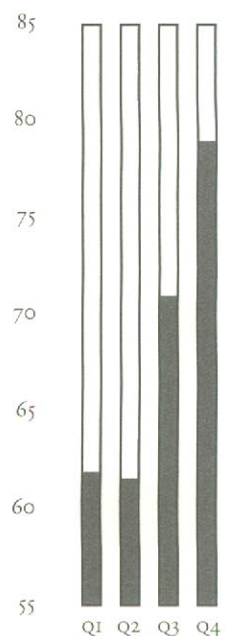
On a quarterly basis U.S. sales in Canadian dollars were as follows: first quarter \$79.2 million, second quarter \$78.9 million, third quarter \$87.8 million and fourth quarter \$95.8 million. U.S. quarterly sales are driven by the timing of large projects and therefore quarterly trends are less predictable than the Canadian market. Fourth quarter sales showed continued strength, increasing 23.3% in source currency over the prior year and exceeding industry growth reported by BIFMA of 12.4%.

#### International

International sales increased 48.9% to \$59.8 million. This increase reflects a significant improvement over 2004, which showed a modest decrease over 2003. International sales benefited from a number of large projects in the strong economies of the Middle East, Asia and Latin America. The Company believes that its international markets will continue to be strong and therefore Teknion's strategy includes initiatives to increase its presence in these markets. For example, during 2005 Teknion opened a showroom and sales office in Bangalore, India, to capture business in India's rapidly growing economy. On a quarterly basis sales climbed throughout the year as follows: first quarter \$11.0 million, second quarter \$12.6 million, third quarter \$15.8 million and fourth quarter \$20.4 million. The sequential quarterly increases reflect the growing number of large projects through the year. The fourth quarter was particularly strong as a result of a large project in the Middle East.

Sales in the U.S., measured in U.S. dollars, increased by 31.7%.

2005  
QUARTERLY U.S. SALES  
(in millions of U.S. dollars)



As a percentage of sales, SG&A expenses are at their lowest level in five years.

**Gross Margin**

Gross margin as a percentage of sales in 2005 was 27.4% as compared to 28.3% in 2004. Although Teknion has been successful in reducing its cost structure since 2001 as outlined on page 4 under the heading Overview, the positive impact of these initiatives has been offset to a considerable extent as a result of the negative impact of the decline in the value of the U.S. dollar relative to the Canadian dollar and the increase in the price of certain commodities. The Company estimates that the decline in value of the U.S. dollar relative to the Canadian dollar reduced gross margin in 2005 by 1.4%. In 2004, both the decline in the value of the U.S. dollar relative to the Canadian dollar and the increase in the price of commodities were significant and negatively impacted gross margin by 4.2% as compared to 2003. The Company continues to focus on increasing efficiencies and reducing costs to offset the impact of higher costs and foreign exchange. In addition, on August 1, 2005, the Company introduced a price increase averaging 3.7% across its product lines.

**Selling, General and Administrative Expenses**

Selling, general and administrative ("SG&A") expenses were \$140.4 million, 23.2% of sales, compared to \$133.5 million, 26.8% of sales in 2004 (29.5% of sales in 2003). In 2005, SG&A expenses included exit and moving costs totaling \$2.4 million. As a percentage of sales, SG&A expenses are at their lowest level in five years, reflecting both the benefit of the Company's cost reduction initiatives and the increase in sales. The Company continues to closely monitor SG&A expenses and, as a percentage of sales, SG&A is expected to remain at current levels in 2006.

**Depreciation and Amortization Expense ("Depreciation")**

Depreciation was \$20.1 million compared to \$22.4 million in 2004 and \$27.0 million in 2003. Depreciation has been declining primarily due to the lower level of capital spending and because of the corresponding reduction in the Company's depreciable assets. Refer to Note 4 in the consolidated financial statements. For 2006, depreciation is expected to remain at the 2005 level.

**Restructuring Costs**

In 2005, the Company did not incur restructuring costs; however, in 2004, the Company recorded a recovery of restructuring costs totaling \$739 thousand as compared to an expense of \$12.1 million in 2003. The recovery recorded in fiscal 2004 occurred primarily because estimated facility exit costs were less than those anticipated and expensed in fiscal 2003. The restructuring costs recorded in 2003 of \$12.1 million related to the Company's manufacturing operations in Malaysia and the U.K.



In Malaysia, prior to the restructuring, manufacturing was being carried out in two facilities, Klang and Tangkak. Given the decline in annual sales in this operation, the Company had significant excess capacity and was incurring losses. In addition, many administrative support activities were being duplicated. Accordingly, the Company decided to consolidate the operations into one facility. The restructuring costs for Malaysia totaled \$2.6 million and were related to inventory obsolescence, fixed asset write-offs, employee severance payments and relocation costs.

In the U.K., the office furniture industry declined by 35% in 2003. As a result, the Company outsourced manufacturing operations, reduced staff levels and consolidated sales offices. The restructuring costs for the U.K. totaled \$9.5 million and related to inventory obsolescence, fixed asset write-offs, loans to a distributor, facility exit costs and employee severance payments. The restructuring of the Malaysian and U.K. facilities was completed in fiscal 2003.

#### **Interest Expense**

Net interest expense increased in fiscal 2005 to \$3.5 million from \$2.9 million in fiscal 2004. Both average interest rates and debt levels were higher in fiscal 2005, compared to 2004.

#### **Loss on Disposal of Property, Plant and Equipment**

The loss on disposal of property, plant and equipment assets totaling \$1.4 million included \$600 thousand related to the facilities the Company exited during the year, which are described under the heading Quarterly Results.

#### **Earnings before Income Taxes**

The Company reported earnings before income taxes of \$494 thousand in fiscal 2005 as compared to a loss before income taxes of \$18.3 million in fiscal 2004 and a loss of \$52.8 million in 2003. Although industry revenues are still 33% below the levels of 2000, a recovery of the office furniture industry has occurred. The Company has achieved strong sales growth; and its cost reduction and manufacturing efficiency initiatives have resulted in significant operating improvements. However, the continued weakening of the U.S. dollar relative to the Canadian dollar reinforces the need to make further operating improvements. The Company continues to focus on streamlining all aspects of its business while executing strategies to increase its market share.

#### **Income Taxes**

The Company's income tax expense for the year was \$21.1 million (2004 – recovery of \$491 thousand) of which \$20.3 million (2004 – \$8.1 million) relates to an income tax valuation allowance recorded to reduce to nil the carrying value of the net future tax assets shown on the consolidated balance sheet. The income tax valuation allowance is discussed in more detail on page 13 under the heading Critical Accounting Estimates.

The Company reported earnings before income taxes of \$494 thousand in fiscal 2005 as compared to a loss before income taxes of \$18.3 million in fiscal 2004.

Cash flow from operations, before working capital changes, increased to \$21.4 million in 2005 from \$1.5 million in 2004.

#### LIQUIDITY AND CAPITAL RESOURCES

(000)

Years ended November 30,	2005	2004	2003
Cash from (used in) operations before non-cash working capital changes	\$ 21,417	\$ 1,546	\$ (8,895)
Cash from (used in) operations after non-cash working capital changes	\$ (1,243)	\$ 1,508	\$ 13,288
Non-cash working capital <sup>(1)</sup>	\$ 82,561	\$ 60,212	\$ 62,903
Capital expenditures	\$ 16,504	\$ 7,329	\$ 9,407
Net debt to equity	0.33:1	0.23:1	0.18:1

<sup>(1)</sup> Non-cash working capital is defined as current assets less current liabilities before cash, future income taxes, operating loans and the current portion of long-term debt. The term non-cash working capital is a non-GAAP financial measure and does not necessarily have a standardized meaning amongst issuers. The Company believes that non-cash working capital is a useful figure because it measures the effectiveness of the Company's accounts receivable collection, inventory management and supplier payment practices.

As a result of the significant improvement in the Company's operating results, cash flow from operations, before working capital changes, increased to \$21.4 million in 2005 from \$1.5 million in 2004. Fiscal 2004 also compared favorably to fiscal 2003 when the Company used \$8.9 million in cash.

Sales in the fourth quarter of 2005 were \$173.1 million compared to \$138.0 million in the prior year period. As a result, working capital in 2005 compared to 2004 increased by \$22.3 million to support these higher sales levels. Specifically as compared to 2004 accounts receivable increased to \$125.5 million from \$94.5 million; inventories increased to \$52.2 million from \$48.4 million; and accounts payable and accrued liabilities increased to \$98.4 million from \$86.2 million. The above-noted increases result in similar working capital management statistics as compared to 2004. Days outstanding for accounts receivable were 65 as at November 30, 2005, compared to 62 at November 30, 2004. Further, the number of days of production inventory declined to 43 at November 30, 2005, from 47 at November 30, 2004.

Capital spending in 2005 totaled \$15.7 million (net of proceeds on disposal of property, plant and equipment) compared to \$7.2 million in 2004. For 2006, the Company expects capital spending to approximate \$25 million and will be primarily directed to: tooling for new products; manufacturing equipment to both improve efficiency and increase capacity; and replacement of computer hardware. The Company has sufficient available manufacturing capacity in most product areas.

At November 30, 2005, the Company's net debt was \$70.4 million compared to \$53.2 million at November 30, 2004. The Company defines net debt as operating loans plus long-term debt, less cash. The balance sheet remains strong with a net debt-to-equity ratio of 0.33:1. At November 30, 2005, the Company utilized \$63.1 million of its \$105.1 million operating lines of credit with the majority of its credit lines bearing interest at the banks' prime rate minus 0.25% per annum.

As noted under Sales by Geographic Region, more than half of the Company's sales are U.S.-based and are billed and collected in U.S. dollars. In addition, approximately half of international sales are transacted in U.S. dollars. Accordingly, the Company is exposed to changes in the value of the U.S. dollar compared to the Canadian dollar. The Company's current policy is to hedge a portion of its U.S. dollar exposure, based on forecast U.S. dollar revenues, by entering into foreign exchange contracts. As well, the Company has an inherent or "natural" hedge, which at current sales levels, covers more than half of its U.S. dollar sales. This natural hedge derives principally from the purchase of products and material in U.S. dollars, and from the cost of running the Company's U.S. operations. As at November 30, 2005, the Company held foreign exchange contracts maturing within 13 months for the sale of U.S. \$88.0 million at a weighted average rate of exchange of \$1.22 (see Note 11 to the annual consolidated financial statements). Foreign exchange contracts settled during 2005 resulted in increasing reported sales and increasing the income before income tax by \$8.4 million.

The following table summarizes the Company's contractual obligations:

(000)	Total	Less than 1 year	1-3 years	4-5 years	After 5 years
Long-term debt	\$ 17,798	\$ 1,711	\$ 2,235	\$ 1,647	\$ 12,205
Operating leases	49,785	13,305	18,388	8,709	9,383
Total contractual obligations	\$ 67,583	\$ 15,016	\$ 20,623	\$ 10,356	\$ 21,588

#### RELATED PARTY TRANSACTIONS

Transactions with related parties were as follows:

(000)	2005	2004	2003
Sales	\$ 11,006	\$ 9,238	\$ 13,290
Purchases	57,215	45,245	47,876
Lease payments	6,499	8,469	8,275
Other purchases	983	272	233

Substantially all related party transactions occurred with an indirect shareholder, Global Upholstery Co. Limited and entities controlled, related or significantly influenced by it (collectively "Global").



Transactions between the Company and Global occur at prices that are either in accordance with written agreements between the Company and Global or in accordance with regular market prices. Management believes that the prices and terms at which all transactions are conducted with Global are competitive with prices and terms for comparable arm's-length transactions. The Corporate Governance Committee of the Board of Directors is responsible for and reviews, monitors and establishes all policies for related party transactions.

**Purchases from Global**

Global manufactures the Boulevard and Descor lines, both of which are targeted to the mid-priced segment of the contract furniture market. Boulevard and Descor are sold in the U.S. by Teknion pursuant to an exclusive distribution agreement with Global.

The Global Group Israel Limited Partnership ("Global Israel") is a supplier of certain products to Teknion for the European market, and for its own account is the exclusive manufacturer and distributor of Teknion products in Israel, the Czech Republic, the Slovak Republic, Bulgaria, Turkey, Cyprus and Egypt, collectively the "Territory." Global Israel has agreed not to sell or permit a sale of Teknion products outside the Territory other than to Teknion.

Global maintains a government-certified testing laboratory for purposes of testing newly developed and customized products, and components used in the manufacturing of products. The Company uses the facility and pays Global for use of this testing facility.

**Sales to Global**

Global currently purchases components and products manufactured by the Company.

**Sales to Related Party Dealers**

Two of the Company's subsidiaries have third-party minority shareholders. These shareholders have direct or indirect interests in office furniture dealers that sell and distribute the Company's products. Management believes that the prices at which product is purchased by these related parties from the Company are competitive.

**Leases from Global**

The Company leases properties from Global. These properties are used for general manufacturing and office purposes.

**CRITICAL ACCOUNTING ESTIMATES**

The preparation of the Company's financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amount of revenue and expenses during the reporting period.

The most significant accounting estimates included in the consolidated financial statements are: goodwill valued at \$30.9 million and unchanged from 2004 and 2003; and the valuation of net future tax assets.

The Company assesses the realization of these future tax assets to determine whether an income tax valuation allowance is required. The main factors that are considered include:

- cumulative losses in recent years;
- the carryforward period associated with the future tax assets;
- net earnings/loss by tax jurisdiction; and
- future earnings potential determined through the use of internal forecasts and available external market research.

Based on the above-noted factors, during fiscal 2005, a valuation allowance of \$20.3 million was recorded (2004 – \$8.1 million). Accordingly, the Company has reduced its net future tax asset on its consolidated balance sheet to nil (2004 – \$20.3 million). Therefore, the income tax expense included on the Company's consolidated statement of earnings included an additional expense of \$20.3 million relating to the valuation allowance. In 2004, the Company increased its net future tax assets by \$4.1 million.

**NEW CICA REPORTING REQUIREMENTS**

Effective December 1, 2004, the Company retroactively adopted CICA Handbook Section 3110, Asset Retirement Obligations. The standard addresses the recognition, measurement and disclosure of liabilities for asset retirement obligations and the associated asset retirement costs. The standard applies to legal obligations associated with the retirement of a tangible long-lived asset that resulted from acquisition, construction, development or from normal operations. The standard requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The fair value is added to the carrying amount of the associated asset and expensed using a systematic and rational method over the estimated useful life of the related asset. The impact on the consolidated financial statements for the period ended November 30, 2005, and the prior year comparative is negligible.

The CICA issued Accounting Guideline No. 15, Consolidation of Variable Interest Entities ("AcG-15"), which establishes criteria to identify variable interest entities ("VIEs") and the primary beneficiary of such entities. Entities that qualify as VIEs must be consolidated by their primary beneficiary. Effective December 1, 2004, the Company adopted AcG-15 and concluded that there were no interests to be consolidated.

#### **DISCLOSURE CONTROLS AND PROCEDURES**

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the CEO and CFO, on a timely basis so that appropriate decisions can be made regarding public disclosure. An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures was conducted as of November 30, 2005. Based on this evaluation, the CEO and CFO have concluded that our disclosure controls and procedures, as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings, are effective to ensure that information required to be disclosed in reports that we file under Canadian securities legislation is reported within the time periods required.

#### **RISKS AND UNCERTAINTIES**

Factors that could cause actual results to differ from expectations include, but are not limited to, fluctuations in the Company's operating results due to product demand arising from competitive and general economic and business conditions in the Company's North American and international markets and operations; significant fluctuations in exchange rates for currencies in which the Company does business; changes in the cost of raw materials; the ability to maintain the proprietary nature of the Company's intellectual property in the design and manufacturing of its products; changes in the size and timing of customers' order patterns; changes in the Company's markets, including technology change, changes in customer requirements, frequent new product introductions by competitors and emerging standards; the Company's dependence on key personnel; the Company's dependence on key commitments from significant dealers and distributors; the Company's dependence on its suppliers; potential liabilities arising from product defects; and environmental matters.

#### **OUTLOOK**

Management continues to believe that, over the long term, the worldwide business environment will increasingly require that organizations and institutions utilize costly office space more effectively and improve the working environment to increase employee productivity. The Company also believes that these factors, combined with increased commercial construction and capital spending, as well as the growing use of technology and the increasing awareness of workplace health and safety, will allow long-term growth in the contract office furniture industry to exceed growth in GDP.



The Company believes that the positive trend of growing customer demand reflected in the BIFMA statistics throughout 2005 bodes well for the office furniture industry. Industry observers agree that the industry will continue to grow in 2006.

The Company remains confident that its focused growth strategies, combined with its comprehensive product lines, innovative designs and extensive dealer network, will enable the Company to capitalize on renewed demand in its markets as business conditions improve. In addition, new sales and marketing programs are broadening the Company's customer base into market segments in the U.S. where the Company did not previously have a strong presence, including the health, education and government sectors.

The Company's strategies for future growth and improvement to its operating results are to: continue to develop its sales and marketing initiatives to expand its presence and market share, focusing on market segments where the Company previously did not have a strong presence; leverage the strength and economies of scale resulting from the vertical integration and recent modernization of its manufacturing facilities and processes; maintain its focus on design and innovation to ensure it can respond quickly with new and enhanced products to meet the needs of its customers; continue its focus on cost improvement and efficiency; and make prudent acquisitions that meet the Company's long-term strategic objectives.

As a result of these strategies and an anticipated improvement in the market for the Company's products, management expects to generate improved financial performance in fiscal 2006 compared to fiscal 2005.

#### **FORWARD-LOOKING STATEMENTS**

This management discussion and analysis of the financial condition and results of operations contains forward-looking statements with respect to the Company's future prospects. These statements involve certain risks and uncertainties as outlined above under the heading Risks and Uncertainties that could cause the Company's financial results to differ materially from stated expectations. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

## AUDITORS' REPORT TO SHAREHOLDERS

We have audited the consolidated balance sheets of Teknion Corporation as at November 30, 2005 and 2004 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at November 30, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

A stylized, handwritten signature in black ink that reads "KPMG LLP". The signature is written in a cursive, flowing style with a long horizontal line extending from the end of the "P" in "KPMG".

**CHARTERED ACCOUNTANTS**

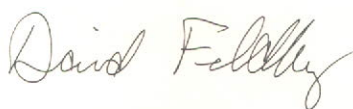
Toronto, Canada  
January 31, 2006

## MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

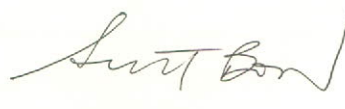
The accompanying financial statements and information included in this Annual Report have been prepared by the management of Teknion Corporation in accordance with Canadian generally accepted accounting principles, and include amounts based on management's informed judgments and estimates. Management is responsible for the integrity and objectivity of these financial statements. To fulfill this responsibility, Teknion maintains an appropriate system of internal control, policies and procedures to reasonably ensure that its reporting practices and accounting and administrative procedures provide reliable and accurate financial information, and that assets are adequately safeguarded. The financial information presented elsewhere in this Annual Report is consistent with that in the financial statements in all material respects.

KPMG LLP, the auditors appointed by the shareholders of Teknion, have examined the financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to shareholders their opinion on the financial statements. Their report as the Company's auditors is set forth herein.

The financial statements have been further reviewed and approved by the Board of Directors and its Audit Committee. This Committee meets regularly with management and the auditors, who have full and free access to the Audit Committee.



**DAVID FELDBERG**  
President and Chief Executive Officer  
January 31, 2006



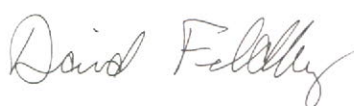
**SCOTT BOND**  
Chief Financial Officer and Secretary  
January 31, 2006



## CONSOLIDATED BALANCE SHEETS

November 30 (in thousands of dollars)	2005	2004
<b>ASSETS</b>		
Current assets:		
Cash	\$ 10,435	\$ 11,154
Accounts receivable (NOTE 2(A))	125,505	94,497
Inventory	52,215	48,393
Prepaid expenses and other deposits	4,189	4,454
Future income taxes (NOTE 3)	1,203	1,283
	193,547	159,781
Future income taxes (NOTE 3)	—	18,985
Property, plant and equipment (NOTE 4)	170,426	176,073
Loan receivable	—	340
Goodwill	30,874	30,874
	\$ 394,847	\$ 386,053
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Operating loans (NOTE 5)	\$ 63,056	\$ 43,907
Accounts payable and accrued liabilities (NOTE 2(A))	98,377	86,168
Income taxes payable	920	380
Due to affiliated companies (NOTE 2(B))	51	584
Current portion of long-term debt (NOTE 6)	1,711	2,057
	164,115	133,096
Long-term debt (NOTE 6)	16,087	18,424
Future income taxes (NOTE 3)	1,203	—
Shareholders' equity:		
Share capital (NOTE 7)	107,005	106,928
Retained earnings	116,486	137,140
Contributed surplus (NOTE 7(C))	94	37
Currency translation adjustment	(10,143)	(9,572)
	213,442	234,533
Commitments (NOTE 9)		
	\$ 394,847	\$ 386,053

See accompanying notes to consolidated financial statements.



ON BEHALF OF THE BOARD:

DAVID FELDBERG  
Director



GEORGE S. TAYLOR  
Director

**CONSOLIDATED STATEMENTS OF EARNINGS**

Years ended November 30 (in thousands of dollars, except per share amounts)	2005	2004
Sales	\$ 606,183	\$ 497,345
Cost of sales	440,289	356,708
Gross margin	165,894	140,637
Expenses:		
Selling, general and administrative (NOTE 1(F))	140,396	133,459
Depreciation and amortization	20,087	22,406
Restructuring costs recovered (NOTE 13)	—	(739)
Loss on disposal of investment	—	630
	160,483	155,756
Earnings (loss) from operations	5,411	(15,119)
Interest expense, net (NOTE 6)	3,512	2,865
Loss on disposal of property, plant and equipment	1,405	317
Earnings (loss) before income taxes	494	(18,301)
Income taxes (recovery) (NOTE 3):		
Current	880	3,629
Future	20,268	(4,120)
	21,148	(491)
Loss for the year	\$ (20,654)	\$ (17,810)
Loss per share (NOTE 8):		
Basic and diluted	\$ (0.32)	\$ (0.28)

**CONSOLIDATED STATEMENTS OF RETAINED EARNINGS**

Years ended November 30 (in thousands of dollars)	2005	2004
Retained earnings, beginning of year	\$ 137,140	\$ 154,950
Loss for the year	(20,654)	(17,810)
Retained earnings, end of year	\$ 116,486	\$ 137,140

*See accompanying notes to consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended November 30 (in thousands of dollars)	2005	2004
Cash provided by (used in):		
<b>OPERATIONS</b>		
Loss for the year	\$ (20,654)	\$ (17,810)
Items not affecting cash:		
Depreciation and amortization	20,087	22,406
Future income taxes	20,268	(4,120)
Loss on disposal of property, plant and equipment	1,405	317
Foreign exchange loss	254	825
Amortization of stock-based compensation	57	37
Loss on disposal of investment	—	630
Restructuring costs recovered (NOTE 13)	—	(739)
	21,417	1,546
Change in non-cash operating working capital	(22,660)	(38)
	(1,243)	1,508
<b>FINANCING</b>		
Operating loans	19,149	13,593
Repayment of long-term debt	(2,474)	(2,124)
Issue of share capital	77	77
	16,752	11,546
<b>INVESTMENTS</b>		
Purchase of property, plant and equipment	(16,504)	(7,329)
Proceeds on disposal of property, plant and equipment	825	130
	(15,679)	(7,199)
Foreign exchange loss on cash held in foreign currencies	(549)	(2,706)
Increase (decrease) in cash	(719)	3,149
Cash, beginning of year	11,154	8,005
Cash, end of year	\$ 10,435	\$ 11,154

Supplemental cash flow information (NOTE 12)

See accompanying notes to consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts in thousands of dollars) Years ended November 30, 2005 and 2004

Teknion Corporation is incorporated under the *Business Corporations Act* (Ontario) and its primary business activity is the design, manufacture and sale of office furniture.

### 1. SIGNIFICANT ACCOUNTING POLICIES:

#### (a) Basis of presentation:

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles.

The consolidated financial statements include the accounts of Teknion Corporation and all of its subsidiaries ("Teknion" or the "Company"). All significant intercompany transactions have been eliminated on consolidation.

#### (b) Revenue recognition:

The Company recognizes revenue when products are shipped and the customer takes ownership and assumes risk of loss, persuasive evidence of an arrangement exists and the sales price is fixed or determinable.

#### (c) Inventory:

Inventory is valued at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis.

#### (d) Property, plant and equipment:

Property, plant and equipment are recorded at cost and depreciated on a declining-balance basis at the following annual rates:

Buildings	5%
Computer hardware	20%
Computer software	20%
Manufacturing equipment	10%
Office equipment	20%
Tools and dies	10%

Showrooms are depreciated on a straight-line basis over four years.

Leasehold improvements are amortized on a straight-line basis over the term of the lease.

Patents and trademarks are amortized on a straight-line basis over 10 years.

#### (e) Goodwill and other intangible assets:

Goodwill represents the difference between the purchase price and the related underlying net asset values resulting from business acquisitions. The Company reviews the carrying value of goodwill to an estimate of its fair value annually. Due to the integrated nature of the Company's operations and lack of differing economic characteristics among the Company's subsidiaries, the entire Company was determined to be one single reporting unit. The quoted market price of the Company's stock on the impairment testing date is the basis for determining the fair value of the Company's reporting unit. If the fair value of the Company's one reporting unit exceeds its carrying amount, further evaluation is not necessary. However, if the fair value of the reporting unit is less than its carrying amount, further evaluation is required to compare the implied fair value of the reporting unit's goodwill to its carrying amount to determine whether a write-down of goodwill is required. Intangible assets with determinable lives continue to be amortized over their estimated useful lives and are tested for impairment at least annually by comparing their book values with the undiscounted cash flow expected to be received from their use. The Company determined that no impairment existed in the carrying value of the goodwill in its reporting unit as at November 30, 2005 and 2004.



**(f) Translation of foreign currency:**

Foreign operations are classified as self-sustaining or integrated.

**(i) Self-sustaining foreign operations:**

All assets and liabilities are translated into Canadian dollars at exchange rates in effect at year-end. Revenue and expenses are translated at the average rates of exchange for the year. The resulting net gains or losses are recorded as a currency translation adjustment in shareholders' equity. Cash flows are translated at the rate at the time of the cash flows.

**(ii) Integrated foreign operations and accounts in foreign currencies:**

Integrated foreign operations and accounts in foreign currencies have been translated into Canadian dollars using the temporal method. Under this method, consolidated balance sheet monetary items are translated at the rates of exchange in effect at year-end and non-monetary items are translated at historical exchange rates. Revenue and expenses (other than depreciation and amortization, which are translated at the same rates as the related property, plant and equipment) are translated at the rates in effect on the transaction dates or at the average rates of exchange for the year. The resulting gains or losses are included in the consolidated statements of earnings.

Included in selling, general and administrative expenses are foreign exchange losses of \$0.3 million (2004 – \$0.5 million).

**(g) Income taxes:**

The Company uses the asset and liability method of accounting for the tax effect of temporary differences between the carrying amount and the tax basis of the Company's assets and liabilities. Temporary differences arise when the realization of an asset or the settlement of a liability would give rise to either an increase or decrease in the Company's income taxes payable for the year or a later period.

Future income taxes are recorded at the income tax rates that are expected to apply when the future tax liability is settled or the future income tax asset is realized. Future tax assets are recognized to the extent that realization of these assets is more likely than not. Income tax expense consists of the income taxes payable for the year and the change during the year in future income tax assets and liabilities.

**(h) Earnings per share:**

Basic earnings per share are computed by dividing net earnings by the weighted average shares outstanding during the year. Diluted earnings per share are computed similar to basic earnings per share except that the weighted average shares outstanding are increased to include additional shares from the assumed exercise of stock options, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options were exercised and that the proceeds from such exercises were used to acquire shares of common stock at the average market price during the year.

**(i) Stock-based compensation plans:**

The Company has a stock-based compensation plan, which is described in Note 7. The Company accounts for all stock-based payments to non-employees, and employee awards that are direct awards of stock granted on or after December 1, 2003 under the fair value-based method, and accounts for all stock-based employee awards that call for settlement in cash or other assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments under that method.

Effective December 1, 2003, the Company elected early adoption, on a prospective basis, of the new recommendations issued by The Canadian Institute of Chartered Accountants ("CICA") related to physically settled stock options. Stock options that were granted before fiscal 2004 have been accounted for as a capital transaction when exercised and no compensation cost has been recognized.

Under the fair value-based method, compensation cost for physically settled stock options and direct awards of stock is measured at fair value at the grant date, while compensation cost for awards that call for settlement in cash or other assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments, is measured at the ultimate settlement amount. Compensation cost is recognized in earnings on a straight-line basis over the relevant vesting period. The counterpart is recognized in contributed surplus. Upon exercise of a stock option, share capital is recorded at the sum of the proceeds received and the related amount of contributed surplus.

**(j) Guarantees:**

The Company is required to disclose significant information on guarantees it has provided, without regard to whether it will have to make any payments under the guarantees and in addition to the accounting required by Contingencies, CICA Section 3290. As of the years ended November 30, 2005 and 2004, there were no significant guarantees entered into by the Company that would require any additional financial statement note disclosure.

In certain situations, the Company provides performance bonds to ensure installations are carried out in accordance with the agreement. If either the contractor or the Company do not comply with the terms of the agreement, the Company would be liable for payments under the terms of the performance bond. The Company has not experienced a loss to date and future losses are not anticipated; therefore, no liability has been recorded in the financial statements. The amount of performance bonds outstanding at year-end is not significant.

**(k) Derivative financial instruments:**

Derivative financial instruments are utilized by the Company in the management of its foreign currency exposures. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Gains and losses on foreign exchange contracts identified as a hedge of future transactions are deferred and recognized in income when the underlying hedged transaction is recognized.

**(l) Shipping and handling:**

Amounts billed to clients for shipping and handling of products are recognized as sales in the consolidated statements of earnings. Costs incurred by the Company for shipping and handling are included in cost of sales.



**(m) Impairment of long-lived assets:**

Long-lived assets, including property, plant and equipment and purchased intangibles subject to depreciation and amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The asset and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

**(n) Use of estimates:**

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the years. Significant items subject to such estimates and assumptions include the carrying amount of property, plant and equipment; intangibles and goodwill; valuation allowances for receivables; inventories; future income taxes; and valuation of derivative financial instruments. Actual results could differ from those estimates.

**(o) Asset retirement obligations:**

Effective December 1, 2004, the Company adopted the amendments to the new CICA Handbook Section 3110, Asset Retirement Obligations. This recommendation requires the recognition of the fair value of a future asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that results from the acquisition, construction, development and or normal use of the assets. The Company concurrently recognizes a corresponding increase in the carrying amount of the related long-lived asset that is depreciated over the life of the asset. The fair value of the asset retirement obligation is estimated using the expected cash flow approach that reflects a range of possible outcomes discounted at a credit-adjusted risk-free interest rate. Subsequent to the initial measurement, the asset retirement obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. Changes in the obligation due to the passage of time are recognized in income as an operating expense using the interest method. Changes in the obligation due to changes in estimated cash flows are recognized as an adjustment of the carrying amount of the related long-lived asset that is depreciated over the remaining life of the asset. During the year ended November 30, 2005, the Company determined there were no significant future asset retirement obligations.

**(p) Variable interest entities:**

The CICA issued Accounting Guideline No. 15, Consolidation of Variable Interest Entities ("AcG-15"), which establishes criteria to identify variable interest entities ("VIEs") and the primary beneficiary of such entities. Entities that qualify as VIEs must be consolidated by their primary beneficiary. Effective December 1, 2004, the Company adopted AcG-15 and concluded that there were no interests to be consolidated.

**2. RELATED PARTY TRANSACTIONS AND BALANCES:**

(a) Substantially all related party transactions occurred with an indirect shareholder, Global Upholstery Co. Limited ("Global"), and entities controlled or significantly influenced by Global.

Transactions between the Company and Global occur at prices that are in accordance with written agreements between the Company and Global. Management believes that the prices and terms at which transactions are conducted with Global are competitive with prices and terms for comparable arm's-length transactions. The Corporate Governance Committee is responsible for and reviews, monitors and establishes all policies for related party transactions.

Related party amounts included in accounts receivable and accounts payable and accrued liabilities are as follows:

	2005	2004
Accounts receivable	\$ 4,589	\$ 4,025
Accounts payable and accrued liabilities	12,275	9,928

Transactions with related parties are as follows:

	2005	2004
Sales	\$ 11,006	\$ 9,238
Purchases	57,215	45,245
Other	7,482	8,741

(b) The amounts due to/from companies controlled or significantly influenced by the controlling shareholders are unsecured, non-interest bearing and payable on demand.

**3. INCOME TAXES:**

Income taxes have been determined in accordance with the legislation prevailing in Canada and the applicable foreign jurisdictions. The effective income tax rate differs from the basic Canadian combined federal and provincial tax rates as follows:

	2005	2004
Earnings (loss) before income taxes	\$ 494	\$ (18,301)
Combined statutory tax rate	41.6%	41.6%
Computed income taxes (recovery)	\$ 205	\$ (7,613)
Increase (decrease) resulting from:		
Canadian federal and provincial rate reductions	268	1,915
International rate differences	(766)	(3,548)
Increase to valuation allowance	21,291	8,108
Corporate minimum taxes	456	417
Other differences	(306)	230
	\$ 21,148	\$ (491)

The tax effects of temporary differences that give rise to significant portions of the future tax assets and future tax liabilities at November 30 are presented below:

	2005	2004
Future tax assets:		
Accounts receivable	\$ 191	\$ 772
Accounts payable and accrued liabilities	1,012	511
	1,203	1,283
Non-capital loss carryforward	54,851	54,286
Valuation allowance	(34,137)	(12,846)
	20,714	41,440
	21,917	42,723
Future tax liabilities:		
Property, plant and equipment – differences in accounting and tax net book values	(21,917)	(22,455)
Net future tax asset	\$ –	\$ 20,268

Future tax benefits for operating loss and tax credit carryforwards are recognized to the extent that realization of these benefits is considered certain. At November 30, 2005, it was not certain whether the future benefit of operating losses and tax credit carryforwards would be realized and, therefore, the net future tax asset has been reduced to nil.

At November 30, 2005, the Company has the following amounts available to reduce future years' income for tax purposes.

Unused tax losses expiring:	
2009	\$ 14,224
2010	33,111
2014	32,948
2015	6,262
2023	28,229
2024	4,302
Indefinite	15,056
	\$ 134,132

At November 30, 2005, the Company had undeducted scientific research and experimental development expenses of \$2.9 million that can be carried forward indefinitely.

## 4. PROPERTY, PLANT AND EQUIPMENT:

2005	Cost	Accumulated depreciation and amortization	Net book value
Land	\$ 8,693	\$ –	\$ 8,693
Buildings	61,570	13,098	48,472
Computer hardware	29,426	21,822	7,604
Computer software	18,755	12,697	6,058
Manufacturing equipment, office equipment and showrooms	132,148	71,838	60,310
Tools and dies	45,181	17,919	27,262
Leasehold improvements	34,540	24,181	10,359
Patents and trademarks	3,855	2,187	1,668
	<b>\$ 334,168</b>	<b>\$ 163,742</b>	<b>\$ 170,426</b>

2004	Cost	Accumulated depreciation and amortization	Net book value
Land	\$ 8,682	\$ –	\$ 8,682
Buildings	61,099	10,848	50,251
Computer hardware	28,512	20,158	8,354
Computer software	18,746	11,702	7,044
Manufacturing equipment, office equipment and showrooms	128,888	66,402	62,486
Tools and dies	42,825	15,945	26,880
Leasehold improvements	32,655	22,058	10,597
Patents and trademarks	3,658	1,879	1,779
	<b>\$ 325,065</b>	<b>\$ 148,992</b>	<b>\$ 176,073</b>



**5. OPERATING LOANS:**

During the year, the Company refinanced its primary operating facility. The facility provides available lines of credit based on the value of assets up to a maximum of \$100 million.

At November 30, 2005, Teknion had available secured operating lines of credit of up to \$105.1 million (2004 – \$87.2 million). Borrowings under these lines of credit bear interest at varying rates ranging from the banks' prime rate minus 0.25% to plus 2.00% per annum. The Company and certain of its subsidiaries have entered into general security agreements and undertaken an assignment of certain assets to secure bank borrowings.

**6. LONG-TERM DEBT:**

	2005	2004
U.S. \$12.7 million (2004 – U.S. \$13.2 million) mortgage loan, bearing interest at 1.5% over the five-year treasury rate, payable in monthly instalments of \$0.038 million plus interest, secured by a first mortgage lien on real estate of the Company's New Jersey U.S. subsidiary (net book value – U.S. \$16.2 million; 2004 – U.S. \$17.2 million), due October 2012	\$ 14,768	\$ 15,603
U.S. \$1.15 million (2004 – U.S. \$1.5 million) 1998 industrial revenue bonds, bearing interest at the variable seven-day market rate plus 1.5%, principal repayments made monthly to March 1, 2018, secured by a second mortgage on real estate and a charge over book debts of the Company's Minnesota U.S. subsidiary	1,348	1,826
5.4 million (2004 – 8.2 million) Malaysian ringgit term loan, bearing interest at 7%, payable in monthly instalments of 0.10 million Malaysian ringgit, secured by a charge over land, buildings and all assets of the Company's Malaysian subsidiary, due May 2009	1,682	2,591
Various loans with blended monthly repayments, bearing interest at various rates to a maximum of 8.1%	–	461
	17,798	20,481
Less current portion	1,711	2,057
	\$ 16,087	\$ 18,424



Annual principal repayments on long-term debt are due as follows:

2006	\$ 1,711
2007	1,304
2008	931
2009	826
2010	821
Thereafter	12,205
	<u>\$ 17,798</u>

Interest expensed on long-term debt was \$1,046 in 2005 (2004 – \$1,293).

#### 7. SHARE CAPITAL:

	2005	2004
Authorized:		
Unlimited Class A preference shares, non-voting		
Unlimited Class B preference shares, non-voting		
39,919,846 multiple voting shares (2004 – 39,919,846)		
Unlimited subordinate voting shares		
Issued:		
39,919,846 multiple voting shares (2004 – 39,919,846)	\$ 5,051	\$ 5,051
24,196,285 subordinate voting shares (2004 – 24,181,410)	101,954	101,877
	<u>\$ 107,005</u>	<u>\$ 106,928</u>

##### (a) Class A and Class B preference shares:

Class A and Class B preference shares are issuable in series, with other attributes to be determined at the time of issue. The Class A preference shares will rank prior to the Class B preference shares and both will rank prior to the multiple voting shares and subordinate voting shares as to dividends and as to distributions in the event of liquidation, dissolution or winding up of the Company.

**(b) Multiple voting shares and subordinate voting shares:**

During fiscal 2005, no shareholders converted multiple voting shares (2004 – 34,800) on a one-for-one basis to subordinate voting shares. In 2005, 14,875 subordinate voting shares were issued for cash consideration of \$77,350 on the exercise of stock options. In fiscal 2004, 14,800 shares were issued for cash consideration of \$76,960 on the exercise of stock options.

The multiple and subordinate voting shares rank equally on a share-for-share basis as to dividends and as to distributions in the event of liquidation, dissolution or winding up of the Company. The multiple voting shares carry 10 votes per share and are convertible into subordinate voting shares on a one-for-one basis at the option of the holder. The subordinate voting shares carry one vote per share.

**(c) Stock option plan:**

The Company's stock option plan is for directors, officers, employees and affiliates of the Company. The stock option plan is administered by a committee of the Board of Directors of the Company. The price at the date of grant cannot be less than the market price at issue of the subordinate voting shares on any stock exchange on which the subordinate voting shares are listed. The options have a maximum term of 10 years and are non-assignable, except in certain limited circumstances. The vesting periods of options granted under the stock option plan range from four to five years, as determined by a committee of the Board of Directors of the Company at the time the options are granted. The Board of Directors of the Company may, from time to time, amend or revise the terms of the stock option plan, subject to applicable law and the rules of any stock exchange on which the subordinate voting shares are listed, or may discontinue the stock option plan at any time. The maximum number of subordinate voting shares, which may be issued pursuant to the stock option plan, is 6,072,190 subordinate voting shares.

In 2005, the Company did not grant stock options (2004 – 75,000 options were granted at an exercise price of \$5.35). The compensation expense recorded in the year ended November 30, 2005, in respect of stock options granted on or after December 1, 2003, was \$56,900 (2004 – \$37,100) based on a four-year vesting period. The counterpart is recorded as contributed surplus. Any consideration paid by employees on exercise of stock options is credited to share capital. The fair value of each option granted has been estimated at the date of grant using the Black-Scholes option pricing model as detailed in the table below.

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

	Risk-free rate of return	Volatility factor	Expected life of options	Options granted	Fair value per option granted
2005	—	—	—	—	—
2004	4.66%	39%	10 years	75,000	\$ 3.04

The following is a summary of the number of subordinate voting shares issuable pursuant to outstanding stock options:

	2005		2004	
	Number of shares	Weighted average price	Number of shares	Weighted average price
Options outstanding, beginning of year	4,038,790	\$ 10.47	4,534,115	\$ 10.55
Exercise of options	(14,875)	5.20	(14,800)	5.20
Options cancelled	(197,170)	11.46	(555,525)	10.55
Grant of additional options	—	—	75,000	5.35
Options outstanding, end of year	3,826,745	10.44	4,038,790	10.47

	2005		2004	
Weighted average subscription price of outstanding options	\$ 10.44		\$ 10.47	
Number of options exercisable at November 30	3,272,451		2,945,040	
Weighted average subscription price of outstanding exercisable options	\$ 11.06		\$ 11.30	

The range of subscription prices for options granted and exercised were as follows:

	2005		2004	
	High	Low	High	Low
Grant of options	\$ —	\$ —	\$ 5.35	\$ 5.35
Exercise of options	6.70	6.25	7.60	7.25

Range of exercise prices	Total options outstanding			Total options exercisable	
	Number outstanding, November 30, 2005	Weighted average remaining contractual life (years)	Weighted average exercise price	Number exercisable, November 30, 2005	Weighted average exercise price
\$ 5.20—\$ 8.99	755,825	7.67	\$ 5.28	364,625	\$ 5.31
\$ 9.00—\$ 12.99	2,284,920	3.32	10.92	2,121,826	10.95
\$13.00—\$16.00	749,000	5.01	13.75	749,000	13.75
\$16.01—\$21.20	37,000	5.11	19.39	37,000	19.39
	3,826,745	4.50	\$ 10.44	3,272,451	\$ 11.06

**(d) Deferred share units:**

During 2005, the Company established a plan to grant Deferred Share Units ("DSUs") to its non-management directors. Under this plan, the directors may elect to receive a portion of their annual compensation package in DSUs. A DSU is a unit equivalent in value to one common share of the Company based on the 20-day average trading price of the Company's common shares on the Toronto Stock Exchange (the "Weighted Average Price") immediately prior to the date on which the value of the DSU is determined. DSUs may be redeemed following termination of Board service, and prior to the end of the year following departure from the Board based on the Weighted Average Price at the time of redemption.

As of the date of the grant, the fair value of the DSUs outstanding, being the fair market value of the Company's common shares at that date, are expensed in the period and a liability is recorded on the Company's consolidated balance sheet. The value of the DSU liability is adjusted to reflect changes in the market value of the Company's common shares. The expense for fiscal 2005 related to DSUs granted to the directors for services rendered was \$30,000.

**8. LOSS PER SHARE:**

The following table sets forth the computation of basic and diluted loss per share:

	2005	2004
Numerator for basic and diluted loss per share – loss for the year	\$ (20,654)	\$ (17,810)
Denominator for basic and diluted loss per share – weighted average shares	64,107,352	64,091,354
Basic and diluted loss per share	\$ (0.32)	\$ (0.28)

**9. COMMITMENTS:**

The minimum annual lease payments under long-term operating leases for premises and equipment for the next five fiscal years and thereafter are as follows:

2006	\$ 13,305
2007	10,320
2008	8,068
2009	5,072
2010	3,637
Thereafter	9,383
	\$ 49,785



**10. SEGMENTED INFORMATION:**

## Industry:

The Company is considered to operate in one operating segment, that being the design, manufacture and marketing of office systems and related office furniture products.

Geographic:	2005	2004
Sales (based on location of customer):		
Canada	\$ 204,731	\$ 184,751
United States	341,667	272,438
International	59,785	40,156
	<b>\$ 606,183</b>	<b>\$ 497,345</b>
Total assets:		
Canada	\$ 224,548	\$ 229,331
United States	128,738	118,947
International	41,561	37,775
	<b>\$ 394,847</b>	<b>\$ 386,053</b>
Property, plant and equipment:		
Canada	\$ 119,651	\$ 121,833
United States	37,913	40,554
International	12,862	13,686
	<b>\$ 170,426</b>	<b>\$ 176,073</b>
Goodwill:		
Canada	\$ 10,124	\$ 10,124
United States	18,807	18,807
International	1,943	1,943
	<b>\$ 30,874</b>	<b>\$ 30,874</b>

**11. FINANCIAL INSTRUMENTS:**

Teknion operates internationally, which gives rise to a risk that earnings and cash flows may be adversely affected by fluctuations in foreign exchange rates. Foreign exchange contracts are used by the Company to manage foreign exchange risk. The Company does not enter into foreign exchange contracts for speculative purposes.

**(a) Foreign exchange contracts:**

Teknion enters into foreign exchange contracts to limit its exposure to foreign exchange fluctuations on future revenue and expenditure streams. At November 30, 2005, the Company had outstanding foreign exchange contracts representing a commitment to sell U.S. \$88.0 million at an average rate of exchange of \$1.223 (2004 – U.S. \$75.0 million at an average rate of exchange of \$1.33). The fair value of these contracts was \$4.7 million in favour of the Company at November 30, 2005 (2004 – \$8.4 million in favour of the Company). These contracts mature within 13 months (2004 – 12 months).



**(b) Fair values of other financial instruments:**

Teknion has evaluated the fair values of its other financial instruments based on the current interest rate environment, related market values and current pricing of financial instruments with comparable terms. The carrying amounts of cash, accounts receivable, operating loans, accounts payable and accrued liabilities, and due from/to affiliates approximate fair values due to the short-term nature of these instruments. Long-term debt approximates market value as the interest rate charged on this amount is comparable to the current borrowing rate of the Company.

**(c) Credit risk:**

The Company, in the normal course of business, is exposed to credit risk from its customers. In addition, Teknion is also exposed to credit risk from the potential default by any of its counterparties on its foreign exchange forward contracts. The Company controls this credit risk by dealing with counterparties that are major financial institutions and which the Company anticipates will satisfy their obligations under the contracts.

**12. SUPPLEMENTAL CASH FLOW INFORMATION:**

	2005	2004
Income taxes paid	\$ 2,208	\$ 2,295
Income taxes received	1,119	402
Interest paid	4,041	3,541
Interest received	271	240

**13. RESTRUCTURING COSTS:**

Substantially all of the restructuring activity was completed in 2003. During 2004, an accrual of \$739,000 was reversed. No further charges or recoveries occurred in 2005.

The following is a summary of the restructuring accrual activity during fiscal 2005 and 2004:

	Severance costs	Facility exit and other related costs	Total
Accrual balance, November 30, 2003	\$ 303	\$ 2,361	\$ 2,664
Restructuring charges	—	(739)	(739)
Cash payments	(237)	(1,465)	(1,702)
Accrual balance, November 30, 2004	66	157	223
Cash payments	(66)	(157)	(223)
Accrual balance, November 30, 2005	\$ —	\$ —	\$ —

**14. COMPARATIVE FIGURES:**

Certain 2004 comparative figures have been reclassified to conform with the financial statement presentation adopted in 2005.

## CORPORATE INFORMATION

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### STOCK LISTING

The Toronto Stock Exchange  
Ticker Symbol: TKN

### AUDITORS

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Toronto, Canada

### ANNUAL MEETING

Tuesday, May 16, 2006  
10:00 a.m. (eastern standard time)  
Design Exchange  
234 Bay Street  
Toronto Dominion Centre  
Toronto, Ontario  
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**David Feldberg**

President and Chief Executive Officer  
Teknion Corporation

**Saul Feldberg**

Chairman, President and Chief Executive Officer  
Global Upholstery Co. Limited

**Allen Karp**

Corporate Director

**Stephen Miner**

Chairman, Teknion LLC

**David Sanchez**

Vice President, Global Supply Chain and  
Chief Financial Officer  
McCain Foods Limited

**Christi Strauss**

President, General Mills Canada Corporation

**George Taylor**

Consultant

### EXECUTIVE OFFICERS

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President and Chief Executive Officer

**Scott Bond**

Senior Vice President, Chief Financial Officer  
and Secretary

**Steven Cohen**

Senior Vice President, Corporate Development

**John Comacchio**

Senior Vice President and Chief Information Officer

**Frank Delfino**

Senior Vice President and  
President, Canadian and International Markets

**Ian Madell**

Senior Vice President, Marketing and  
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**Stephen Silver**

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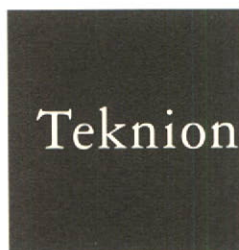
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Teknion's commitment to sustainability practices is reflected in our design, manufacturing, and daily operations. These initiatives drive our growth and innovation, strengthen client relationships, are good for business and, of course, the environment. We are committed to continually learning from and evaluating our results to achieve our goal of total sustainability.