



# Financial Report FY2010 First Quarter

ended February 28, 2010

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# MANAGEMENT'S DISCUSSION AND ANALYSIS

for the three months ended February 28, 2010

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## **OSI Geospatial Inc.**

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### **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis provides a review of activities, results of operations, and financial condition of OSI Geospatial Inc. for the three months ended February 28, 2010 in comparison with those for the three months ended February 28, 2009. References to "OSI Geospatial", "the Company", "we", "us", and "our" refer to OSI Geospatial Inc. and its subsidiaries, as applicable. The following discussion should be read in conjunction with our unaudited consolidated interim financial statements, including the notes thereto, for the three months ended February 28, 2010, and the audited annual consolidated financial statements for the year ended November 30, 2009 prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). The following discussion should also be read in conjunction with Management's Discussion and Analysis prepared for the year ended November 30, 2009.

All references in this report to financial information, excluding backlog and working capital, concerning OSI Geospatial Inc. are in accordance with Canadian GAAP and all dollar amounts are in Canadian dollars unless otherwise indicated.

This report contains forward-looking statements within the meaning of the Ontario Securities Act including Section 138.4(9) and includes statements regarding the future achievement of corporate objectives, advancement of additional project interests, analysis and development of acquisition opportunities, various project interests and other matters. These statements are neither promises nor guarantees, but involve known and unknown risks and uncertainties that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed in or implied by these forward-looking statements. These risks include risks related to the effects of general economic conditions, changing foreign exchange rates, actions by government authorities, uncertainties associated with contract negotiations, and industry supply, as well as other factors discussed below and those risks which are discussed under the heading "Risks and Uncertainties". Readers should not place undue reliance on any such forward-looking statements, which speak only as of the date they were made. We disclaim any obligation to publicly update or revise any such statements to reflect any change in our expectations or in events, conditions or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those set forth in the forward-looking statements.

ECPINS® and COP-IDS are registered trademarks of Offshore Systems Ltd., an OSI Geospatial company. iGEN™ is a registered trademark of CHI Systems Inc., an OSI Geospatial company. Other Company brand, product and service names are for identification purposes only and may be either trademarks, service marks or registered trademarks of their respective owners. Data subject to change without notice.

Additional information relating to OSI Geospatial, including our Annual Information Form, is filed on SEDAR at [www.sedar.com](http://www.sedar.com) and is also available on the Company's investor web site at [www.osigeospatial.com](http://www.osigeospatial.com).

This management's discussion and analysis is dated April 13, 2010.

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### OVERVIEW

Founded in 1977, the Company is a leader in providing real-time situational awareness solutions. The Company delivers products and services to the large and fast-growing defence and security markets. Our systems address critical issues - namely the need for enhanced real-time situational awareness and network-enabled operations. In the changing face of war where interoperability between forces and allies is critical, OSI Geospatial provides essential tactical, strategic, and operational information to help aid decision making, improve efficiency, and provide real-time access to all available information.

Headquartered in Ottawa, the Company is a globally-focused organization with offices across North America and a sales office in the United Kingdom. The Company became a public company in 1990, and is currently listed on the Toronto Stock Exchange (symbol: OSI).

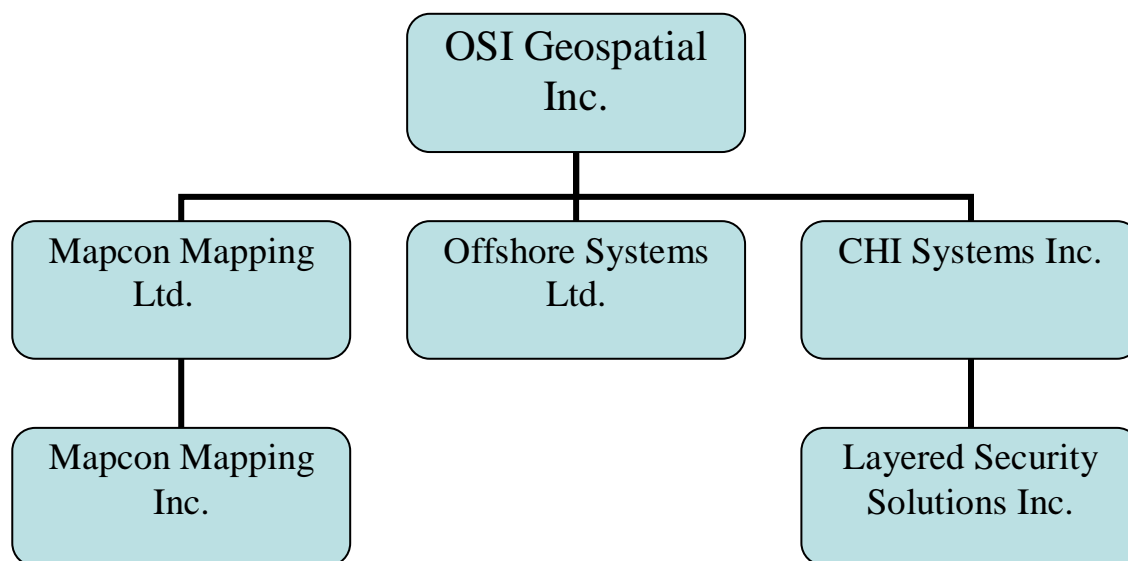
In April 2005, the Company completed the acquisition of all of the outstanding shares of Mapcon Mapping Consultants Inc. ("Mapcon") of Salt Lake City, Utah. Mapcon is a land-mapping company in the U.S. geospatial mapping market.

In December 2005, the Company completed the acquisition of CHI Systems Inc. ("CHI"), a United States defence contractor. CHI had four offices in the United States, and is a supplier of technology and services to the U.S. Department of Defense and key defence prime contractors. With the sale of the Company's rights to its soldier systems intellectual property in February 2010, its San Diego office was transferred to the buyer, Harris Corporation.

CHI has developed C2, training simulation, and cognitive agent applications to support its customers in multiple U.S. military agencies.

In April 2007, the Company, through its subsidiary CHI Systems Inc., acquired the assets of Liddy International Inc. ("Liddy"), a United States defence and security consultancy company, and has established a new subsidiary, Layered Security Solutions Inc. ("LSS"). The Company's LSS subsidiary is primarily focused on developing the U.S. homeland security market.

The Company's current corporate structure is presented in the chart below.



Our mission is to provide integrated navigational and tactical solutions that enhance the operational capabilities, security, and safety for our customers. Our customers include the United States Navy, Army,

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Coast Guard, and Department of Homeland Security; the Canadian Navy and Coast Guard; the UK Royal Navy; and other NATO allies around the world. The Company is leveraging its world-leading technologies, such as ECPINS® and iGEN™, to grow its market share, expand its customer base, and enter into adjacent markets. We will also continue to partner with the world's largest defence and security contractors, such as Lockheed Martin, BAE Systems, Northrop Grumman, L-3 Communications, General Dynamics, and Raytheon. As we successfully integrate our technology into the solution provided by the large defence systems integrators, we will significantly increase our reach into the defence and security markets around the world.

Our Company delivers integrated navigational and tactical solutions that meet naval and maritime security operational requirements. These solutions include our Warship Electronic Chart Display and Information System (ECPINS®-W/S), Tactical Asset Control and Tracking System (T-ACT), Integrated Navigation and Tactical System (INTS), and security risk assessment consulting services. In addition, the Company provides advanced technology research and development engineering services in support of the military and security requirements and mapping services that provide geospatial data production and consulting services.

Real-time situational awareness solutions are critical to mission execution. With the new face of war and the continuing threat of terror, OSI Geospatial's systems and services can provide the solutions that military and security organizations need, including the essential tactical, strategic, and operational information that can be securely shared between forces, allies, and civilians to help ensure interoperability and mission success.

## SELECTED DATA

The following tables contain financial information that is derived from the unaudited interim consolidated financial statements for the three months ended February 28, 2010 and 2009.

<b>Operations:</b>	<b>For the three months ended February 28,</b>	
In thousands of Canadian dollars except share related data	<b>2010</b>	<b>2009</b>
	<b>\$</b>	<b>\$</b>
Revenue	3,444	5,724
Gross profit	1,106	1,719
Gross profit percentage	32%	30%
Net income (loss)	2,082	(697)
Net income (loss) attributable to common shareholders:		
Basic	1,951	(853)
Diluted	2,082	(853)
Earnings (loss) per share:		
Basic	0.04	(0.02)
Diluted	0.04	(0.02)
Weighted average common shares outstanding:		
Basic	48,733,766	46,956,439
Diluted	57,659,553	46,956,439
<u>Dividends declared per share</u>		
Class A Preference Shares – Series A	–	–
Class B Preference Shares – Series 2	\$0.02	\$0.02
Common Shares	–	–

The Company's annual and quarterly operating results are primarily affected by the level, timing and duration of customer orders, relative mix of value added products and services, and fluctuations in material costs. The Company's operating results are also affected by factors such as price competition, manufacturing effectiveness and efficiency, the ability to manage inventory and capital assets effectively, the timing of expenditures in anticipation of increased sales, customer product delivery requirements and shortages of components or labour. Economic factors such as foreign exchange fluctuations, government and corporate spending patterns and regulatory developments may also affect our operating results.

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We depend heavily on government contracts and derive a significant amount of revenue from a few customers, which may result in varying revenue, gross profit, and earnings. Some of our government customers have cyclical purchasing patterns which can also impact our quarterly and annual results.

The decrease in revenue for the three months ended February 28, 2010 as compared to the three months ended February 28, 2009 is largely due to the timing of new contracts that are awarded and the delivery schedules of existing contracts.

The lower gross profit in the three months ended February 28, 2010 as compared to the three months ended February 28, 2009 is due to the decrease in revenue in all operating units, the mix of revenue and the level of fixed costs included in cost of sales across all operating units.

The higher gross profit percentage is the result of less revenue derived from projects that included third party systems and labour. Projects that include third party systems and labour have less favourable margins than those that do not.

Fluctuations in gross profit are influenced by the proportion of engineering labour, third-party systems or third-party labour or portions of all three required for a project, and a high proportion of these factors can result in increased cost of sales and therefore lower gross profit. Certain contracts awarded may require the inclusion of engineering labour, third-party systems or third-party labour. In order to maintain competitiveness on these contracts, we may elect to reduce our usual margins on the third-party components.

The Company's sales strategy's focuses on markets such as military command and control, homeland security, and maritime defence that to date experienced curtailments in budgets and delays in spending. These changes have impacted the Company's customers and as a result, the Company experienced delays in the execution of current projects, awarding of new contracts and releasing of competitive request for proposals; and reductions in the values of some sales opportunities which the Company has been pursuing.

<b>Financial Position:</b>	<b>At February 28, 2010</b>	<b>At November 30, 2009</b>
In thousands of Canadian dollars		
	\$	\$
Working capital <sup>(1)</sup>	5,508	3,446
Current assets	9,661	8,750
Long-term assets	7,018	7,009
Total assets	16,679	15,759
Current liabilities	4,153	5,304
Long-term liabilities	447	492
Total liabilities	4,600	5,796
Shareholders' equity	12,079	9,963

(1) Working capital is defined as current assets less current liabilities. Working capital does not have a standardized meaning or comparable measure under generally accepted accounting principles and may not be comparable to similar measures presented by other companies.

On February 1, 2010, the Company's U.S. Systems Operations signed a contract valued at U.S. \$6.5 million with Harris Corporation ("Harris"). Under the terms of this contract, OSI Geospatial sold all of its rights to its soldier systems intellectual property and transferred its San Diego-based employees, office and associated equipment, furniture and fixtures to Harris. This intellectual property is a non-core asset that is not aligned with the Company's maritime strategy. The net proceeds after corporate income taxes were approximately U.S. \$5.5 million. The net proceeds provided additional working capital for the Company.

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### RESULTS OF OPERATIONS – Three months ended February 28, 2010 as compared to three months ended February 28, 2009

#### Overall Performance

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars, except for share related data			
Net income (loss) before income taxes	\$ 4,041	\$ (844)	\$ 4,885
Net income (loss)	\$ 2,082	\$ (697)	\$ 4,632
Net income (loss) attributable to common shareholders:			
Basic	\$ 1,951	\$ (853)	\$ 4,657
Diluted	\$ 2,082	\$ (853)	\$ 2,935
Earnings (loss) per share:			
Basic	\$ 0.04	\$ (0.02)	\$ 0.06
Diluted	\$ 0.04	\$ (0.02)	\$ 0.06

The higher net income reported for the three months ended February 28, 2010 compared to February 28, 2009 was largely driven by the gain on sale of intellectual property.

#### Backlog

Firm backlog consists of firm, fixed, or signed orders issued and executable subsequent to the balance sheet date. Firm backlog as at February 28, 2010 was at \$40 million compared to \$53 million at February 28, 2009. Of the \$40 million firm backlog, \$8 million is expected to be executed in fiscal 2010 and \$32 million is expected to be executed in fiscal year 2011 and beyond.

Firm backlog is a non-GAAP measure. This measure does not have a standardized meaning or comparable GAAP measure and is likely not comparable to similar measures presented by other companies and cannot be reconciled to any GAAP measurements. The Company discloses this non-GAAP measure as we believe it provides more insight into our performance specifically regarding revenue available for periods subsequent to February 28, 2010.

The timing of major contracts awarded can significantly impact our firm backlog position and revenue. Historically, major contracts awarded have taken up to three years to finalize. The contracting process involves lengthy discussions and negotiations with several groups of people within the prospective customer's organization. We have continually pursued, and will continue to pursue, major contracts with lengthy sales cycles, and as a result, there could be large variations in backlog and revenue from quarter to quarter.

Multi-year contracts with government agencies have a termination-for-convenience clause because governments approve budget expenditures on an annual basis. This allows contracts to be terminated by the contracting government agency should future budget funding not be approved. In International Systems operations and U.S. Systems operations, the termination-for-convenience clause has not been exercised by any of our customers.

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### Revenue

Three months ended	February 28, 2010	% of total revenue	February 28, 2009	% of total revenue	2010 to 2009
In thousands of Canadian dollars					
<b>Maritime navigation and tactical solutions</b>	\$ 1,406	41	\$ 3,522	62	\$ (2,116)
<b>Advanced technology research and development</b>	1,924	56	1,943	34	(19)
<b>Mapping</b>	114	3	259	4	(145)
	<u>\$ 3,444</u>	<u>100</u>	<u>\$ 5,724</u>	<u>100</u>	<u>\$ (2,280)</u>

Our core revenue stream is derived from three sources: maritime navigation and tactical solutions, advanced technology research and development, and mapping. In maritime navigation and tactical solutions, our principal developed product, ECPINS®, delivers the majority of the maritime navigation and tactical solutions revenue. We also derive revenue from the delivery of the ECPINS® software component of our system product. Maritime navigation and tactical solutions delivered 41% and 62% of the revenue for the three months ended February 28, 2010 and February 28, 2009, respectively. Advanced technology research and development through our U.S. Systems operations delivered 56% and 34% of the revenue for the three months ended February 28, 2010 and February 29, 2009, respectively.

Our results are primarily affected by the level, timing, and duration of customer orders and customer product delivery requirements. The main customers for our products and services in the three months ended February 28, 2010 were the U.S. Army, Royal Navy of the U.K., and the U.S. Defense Advanced Research Projects Agency (DARPA). Revenue from these customers accounted for 47% of the consolidated revenue. The main customers for our products and services in the three months ended February 28, 2009 were the Royal Australian Navy, the U.S. Coast Guard, the U.S. Army and the Royal Navy of the U.K. Revenue from these customers accounted for 55% of the consolidated revenue.

### Revenue by Segment

Three months ended	February 28, 2010	% of total revenue	February 28, 2009	% of total revenue	2010 to 2009
In thousands of Canadian dollars					
<b>International Systems operations</b>	\$ 1,215	35	\$ 1,997	35	\$ (782)
<b>U.S. Systems operations</b>	2,115	62	3,468	61	(1,353)
<b>Mapping operations</b>	114	3	259	4	(145)
	<u>\$ 3,444</u>	<u>100</u>	<u>\$ 5,724</u>	<u>100</u>	<u>\$ (2,280)</u>

Revenue from the International Systems operations for the three months ended February 28, 2010 decreased 39% due to delays in the project execution of signed contracts and in the signing of new contracts and contract options.

Revenue from the U.S. Systems operations for the three months ended February 28, 2010 decreased over the same period from the prior year by 39%. The decrease is mainly due to the timing of new contracts awarded and the delivery schedules of existing contracts.

Revenue from the Mapping operations for the three months ended February 28, 2010 decreased over the same period from the prior year by 56% due to the timing of new contracts awarded and the delivery schedules of existing contracts. Revenue from Mapping operations is normally low during the first quarter as the revenue generating activities are largely influenced by weather.

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We continue to invest significant corporate, sales, and marketing resources in identifying and pursuing new opportunities and contracts, both in our existing customer base and with new prospective customers.

### Gross Profit

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Gross profit</b>	<b>\$ 1,106</b>	<b>\$ 1,719</b>	<b>\$ (613)</b>
<b>Gross profit percentage</b>	<b>32%</b>	<b>30%</b>	<b>2%</b>

Gross profit decreased by 36% in the three months ended February 28, 2010 compared to the three months ended February 28, 2009 and the gross profit percentage was 2% higher period-over-period. The decreased gross profit compared to the prior period is mainly due to lower revenues in the current quarter.

The increase in gross profit percentage compared to the prior period is the result of less revenue derived from projects that included third party system and labour. Projects that include third party systems and labour have less favourable margins than those that do not.

### Gross Profit by Segment

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Gross profit:</b>			
<b>International Systems operations</b>	<b>\$ 644</b>	<b>\$ 1,141</b>	<b>\$ (497)</b>
<b>U.S. Systems operations</b>	<b>549</b>	<b>584</b>	<b>(35)</b>
<b>Mapping operations</b>	<b>(87)</b>	<b>(6)</b>	<b>(81)</b>
<b>Consolidated operations</b>	<b>\$ 1,106</b>	<b>\$ 1,719</b>	<b>\$ (613)</b>
<b>Gross profit percentage:</b>			
<b>International Systems operations</b>	<b>53%</b>	<b>57%</b>	<b>(4%)</b>
<b>U.S. Systems operations</b>	<b>26%</b>	<b>17%</b>	<b>9%</b>
<b>Mapping operations</b>	<b>(76%)</b>	<b>-%</b>	<b>(76%)</b>
<b>Consolidated operations</b>	<b>32%</b>	<b>30%</b>	<b>2%</b>

Gross profit from the International Systems operations decreased 44% and gross profit percentage was 4% lower when compared to the prior period. The decrease in gross profit for the first quarter of 2010 is the result of lower revenues in the International Systems operations. The lower gross profit margin is the result of lower software sales and higher systems and services sales compared to the prior period.

Gross profit from the U.S. Systems operations for the three months ended February 28, 2010 decreased 6% and gross profit percentage was 9% higher when compared to February 28, 2009. The increase in gross profit rate is due to a lesser proportion of low margin equipment revenues when compared to the same period last year.

Gross profit from the Mapping operations for the three months ended February 28, 2010 decreased 135% and gross profit percentage dropped 76% when compared to the prior period. Gross profit was negatively impacted by the level of fixed costs included in cost of sales. It is also driven by season as the revenue

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generating activities are mostly influenced by weather. The gross profit percentage of any given mapping project is largely influenced by two factors:

1. the proportion of production services that are performed in-house versus subcontracted to either specialized production service companies in North America or offshore production companies in India or China; and
2. the customer's primary driver, being either price or quality.

Projects where the Company can rely heavily on offshore production will typically have higher gross margin percentages than those that include a large component of specialized or in-house services. Projects where the primary customer driver is quality will generally have higher margins than projects where the primary driver is price.

### Operating Expenses

Three months ended	February 28, 2010	% of total revenue	February 28, 2009	% of total revenue	2010 to 2009
In thousands of Canadian dollars					
<b>General and administrative</b>	\$ 1,267	37%	\$ 1,209	21%	\$ 58
<b>Engineering</b>	176	5%	301	5%	(125)
<b>Sales and marketing</b>	665	19%	813	14%	(148)

**General and administrative** ("G&A") expenses consist mainly of salaries and benefits of management and administrative personnel, professional fees, public company expenses, related facility costs, and other general administrative expenses.

G&A increased 5% for three months ended February 28, 2010 compared to the previous year's first quarter. The slight increase was because of stock-based compensation expense recognized for stock options granted in the current period.

**Engineering** expenses consist mainly of salaries and benefits of software and hardware engineering personnel, facilities expenses, and related expenses. The Company expenses research and development-related costs in the period incurred unless, in the opinion of management, certain development costs meet the deferral criteria under Canadian GAAP, in which case development expenditures are capitalized and amortized over the estimated lives of the related products.

Engineering costs decreased 42% for the three months ended February 28, 2010, compared to the three months ended February 28, 2009. The decrease is mainly related to reduction in staff levels. We believe that in order to maintain our technological leadership, we must continue to develop existing products and introduce innovative new products that challenge and redefine the industry standards.

**Sales and marketing** ("S&M") expenses consist primarily of compensation of sales and marketing personnel, as well as expenses associated with advertising, trade shows, facilities, and other expenses related to the sales and marketing of our products and services.

S&M expenses decreased by 18% for three months ended February 28, 2010 compared to the three months ended February 28, 2009. The decrease is primarily due to staff reduction, lower commissions and a reduction in discretionary spending. We believe our current level of S&M staff continues to allow us to pursue business development activities relating to our expansion efforts targeting new and existing customers in the military agencies of Canada, the U.S., European NATO, and other allies of Canada, and national and international commercial marine transportation companies. To increase our profile and our products, and to broaden our customer base in international markets, we have established marketing agreements with

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companies local to the targeted regions. Some of these activities will not result in closing orders during the current year but may yield orders in subsequent fiscal years.

### Amortization

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Amortization</b>	<b>\$ 87</b>	<b>\$ 113</b>	<b>\$ (26)</b>

Total amortization decreased by 23% on the three months ended February 28, 2010 as compared to the three months ended February 28, 2009. For the three months ended February 28, 2010 and February 28, 2009, a portion of the amortization, \$37,000 and \$48,000, respectively, was included in cost of sales for equipment used in revenue-generating activities.

### Interest expense

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Interest expense</b>	<b>\$ 38</b>	<b>\$ 31</b>	<b>\$ 7</b>

Interest expense increased by 23% in the three months ended February 28, 2010 as compared to the three months ended February 28, 2009. The increase is mainly due to higher interest rates for the new credit facilities. With the cash proceeds from the sale of intellectual property, the Company did not utilize its credit facilities for the entire quarter ended February 28, 2010.

### Foreign exchange

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Foreign exchange loss (gain)</b>	<b>\$ (10)</b>	<b>\$ -</b>	<b>\$ 10</b>

The Company's Canadian subsidiaries, whose functional currency is the Canadian dollar, are exposed to foreign exchange gain and loss due to exchange rate movements of the U.S. dollar, the Australian dollar, the Euro and the UK pound. The Company minimized the exposure to foreign exchange fluctuations through the use of foreign exchange forward contracts.

### Technology Partnerships Canada royalty

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Royalty</b>	<b>\$ 69</b>	<b>\$ 96</b>	<b>\$ (27)</b>

The Company entered into two agreements with Technology Partnerships Canada ("TPC") whereby TPC granted financial assistance for the purpose of funding research and development activities which were completed on March 31, 2007. The contributions we received were based on the eligible expenditures incurred.

As part of the agreement entered into on November 15, 1999 with TPC, we are required to pay a royalty of 3% on annual gross revenue in our subsidiary Offshore Systems Ltd. for the period December 1, 1999 to November 30, 2008. In addition, as part of the agreement entered into on April 26, 2004, we are required to

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pay a royalty of 1.4% on annual gross revenue in our subsidiary Offshore Systems for the period from January 1, 2006 to December 31, 2008 and a royalty of 2.5% on annual gross revenue for the period from January 1, 2009 to December 31, 2013.

Although we believe that our submissions for TPC funding meet the terms and conditions of the TPC agreements, the final determination is subject to audit by government authorities in the ordinary course of business.

### Gain on sale of intellectual property

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
Gain on sale of intellectual property	\$ 5,227	\$ -	\$ 5,227

On February 1, 2010, the Company's U.S. Systems Operations signed a contract valued at U.S. \$6.5 million with Harris Corporation ("Harris"). Under the terms of this contract, OSI Geospatial sold all of its rights to its soldier systems intellectual property and transferred its San Diego-based employees, office and associated equipment, furniture and fixtures to Harris. This intellectual property is a non-core asset that is not aligned with the Company's maritime strategy. The net proceeds after corporate income taxes were approximately U.S. \$5.5 million.

### Income Taxes

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
Future income tax expense (recovery)	\$ 888	\$ (152)	\$ 1,040
Current income tax expense	1,071	5	1,066
	<u>1,959</u>	<u>(147)</u>	<u>2,106</u>

Based on the information available at the time of the issue of the interim financial statements for the three months ended February 28, 2010, we estimated that we would not have sufficient taxable earnings in Canada in future periods to utilize a portion of our \$4.8 million Canadian non-capital losses carried forward, \$13.2 million scientific research and experimental development costs, and other Canadian tax balances.

We have recognized a future tax expense for the three months ended February 28, 2010 related to temporary timing differences between accounting income and income for tax purposes in our U.S. subsidiaries. The future tax expense is mainly a result of reversal of future tax assets recognized in prior period for timing differences as these differences were utilized in the current quarter resulting from the sale of intellectual property. At February 28, 2010, we have current future tax asset of \$180,000 and non-current future tax asset of \$80,000 as we believe that it is more likely than not that these differences will be realized in future fiscal years. In accordance with Canadian GAAP, we have provided a valuation allowance against future tax assets where realization did not meet the requirements of "more likely than not" under the liability method of tax allocation. We continue to evaluate our taxable position quarterly and consider factors such as estimated taxable income, the history of losses for tax purposes, and the growth of the Company, among others.

We recognized current income tax expense for the three months ended February 28, 2010 mainly due to taxable income earned from the sale of intellectual property.

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### LIQUIDITY AND CAPITAL RESOURCES - February 28, 2010 compared to November 30, 2009

In thousands of Canadian dollars	February 28, 2010	November 30, 2009	2010 to 2009
<b>Current assets</b>	\$ 9,661	\$ 8,750	\$ 911
<b>Current liabilities</b>	4,153	5,304	(1,151)
<b>Working capital <sup>(1)</sup></b>	<b>5,508</b>	<b>3,446</b>	<b>2,062</b>

<sup>(1)</sup> Working capital is defined as current assets less current liabilities. Working capital does not have a standardized meaning or comparable measure under generally accepted accounting principles and may not be comparable to similar measures presented by other companies.

We strive to maintain cash-contributing profitable operations that provide an adequate liquidity and capital resource base for growth. We believe that cash flow from operating activities, together with lines of credit borrowings available under our credit facilities, will be sufficient to fund currently anticipated working capital, planned capital spending, and debt service requirements for the next 12 months.

At February 28, 2010, our current assets increased primarily due to an increase in cash as a result of the sale of intellectual property during the quarter. Our working capital has increased mainly due to the increase in cash, decrease in accounts payable and accrued liabilities offset by a decrease in accounts receivable and the current portion of future tax assets. Accounts receivable decreased due to lower revenues in the first quarter of 2010 compared to the fourth quarter of 2009 and due to collection of significant receivables. Accounts payable and accrued liabilities decreased due to payment of specific project costs related to receivable that were collected during the same period. Current portion of future tax assets decreased due to utilization of future tax assets to offset the taxable income generated mainly from the sale of intellectual property.

We have credit facilities consisting of accounts receivable factoring arrangements and forward exchange contract facilities. The credit facilities permit us to borrow funds directly for general corporate purposes. At February 28, 2010, we had borrowings of \$74,000 against our U.S. accounts receivable factoring facility. We have an accounts receivable factoring facility with a Canadian financial institution with a maximum limit of \$2.0 million and a variable limit with a U.S. financial institution that is based on the outstanding accounts receivable of the U.S. operations. During the three months ended February 28, 2010, we utilized these facilities which increased interest expense for the period. We utilize our forward exchange contract facility to reduce our exposure to exchange rate movements.

In December 2008, we declared and paid the semi-annual dividends earned from June to November 2008 in the amount of Canadian \$0.0175 per share to the Class B Series 2 preference shareholders. In July 2009, we declared and paid the partial semi-annual dividends earned from December 2008 to May 2009 in the amount of Canadian \$0.0175 per share to the Class B Series 2 preference shareholders. In January 2010, we declared and paid a partial semi-annual dividend earned from June to November 2009 in the amount of Canadian \$0.0175 per share on the Class B Series 2 preference shareholders. The partial dividends were paid in accordance with the Company's Articles of Incorporation and to preserve our financial resources in light of the current market conditions. The Company will be assessing its financial resources on a regular basis to determine when we can increase or reinstate the dividends.

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Management's Discussion and Analysis  
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### Cash Flows

Three months ended	February 28, 2010	February 28, 2009	2010 to 2009
In thousands of Canadian dollars			
<b>Cash flows provided by (used in):</b>			
Operating activities	\$ (1,489)	\$ 136	\$ (1,625)
Investing activities	4,771	(50)	4,821
Financing activities	(787)	(83)	(704)
Effect of foreign exchange on cash	42	3	39

Cash flows used in operating activities for the three months ended February 28, 2010 were the result of the net income for the three months ended February 28, 2010 which was increased by amortization, stock-based compensation and a decrease in accounts receivable offset by a decrease in accounts payable and accrued liabilities and the gain on disposal of intellectual property.

Cash flows provided by investing activities for the three months ended February 28, 2010 were primarily due to disposal of intellectual property.

Cash flows used in financing activities for the three months ended February 28, 2010 were the result of a repayment of bank indebtedness, factored advance payable and capital lease obligations.

As a result of the above mentioned changes, the credit facilities utilization decreased by \$764,000 for the three months ended February 28, 2010.

In order to reduce the impact of exchange rate fluctuations, we use the forward exchange contract facility to mitigate any foreign exchange gain or loss that might occur. We use the forward exchange contract facility only for known or reasonably certain future foreign currency transactions. At February 28, 2010 we had entered into forward exchange contracts in the amount of U.S. \$51,000, £292,000 and €220,000.

There can be no assurance that we will have adequate financial resources, financing, or cash flows to support the Company into the future.

### CONTRACTUAL OBLIGATIONS

The following table provides a summary of the contractual obligations and the payments due for each of the next five years and thereafter.

Payments due by period	Total	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years
In thousands of Canadian dollars					
Facility leases	\$ 2,967	\$ 761	\$ 1,156	\$ 510	\$ 540
Capital equipment leases	113	61	52	-	-
Operating equipment leases	43	31	12	-	-
<b>Total contractual obligations</b>	<b>\$ 3,123</b>	<b>\$ 853</b>	<b>\$ 1,220</b>	<b>\$ 510</b>	<b>\$ 540</b>

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### **OFF BALANCE SHEET ARRANGEMENTS**

#### Guarantees

The Company has entered into a guarantee agreement for one of the Company's subsidiaries, CHI. The Company has guaranteed CHI's accounts receivable factoring facility with a U.S. financial institution. At February 28, 2010, the carrying amount of CHI's factored advances payable was U.S. \$71,000 (November 30, 2009 – U.S. \$227,000).

We warrant that our software and hardware products will operate substantially in conformity with product documentation and that the physical media will be free from defect. The specific terms and conditions of the warranties are generally one year but may vary depending on the country in which the products are sold. We accrue for known warranty issues if a loss is probable and can be reasonably estimated, and accrue for estimated incurred but unidentified warranty issues based on historical activity. To date, we have had no material warranty claims.

### **TRANSACTIONS WITH RELATED PARTIES**

The Company had no related party transactions during the periods reported.

### **CRITICAL ACCOUNTING ESTIMATES**

The preparation of financial statements in conformity with Canadian GAAP requires the Company's management to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses for the years reported. Significant areas requiring the use of estimates include valuation of goodwill and intangible assets, future income tax assets, and revenue recognition. Management reviews its estimates based on management's best knowledge of current events and actions that the Company may undertake in the future. Actual results could differ from these estimates.

The Company's critical accounting policies are those that it believes are the most important in determining its financial condition and results, and requires significant subjective judgement by management. The Company considers an accounting estimate to be critical if the estimate requires management to make assumptions about matters that were highly uncertain at the time the estimate was made, if different estimates could have been reasonably used or if changes in the estimate would have a material impact on the Company's financial condition or results of operations are likely to occur from period to period.

#### *Valuation of goodwill and intangible assets impairment*

In November 2009, the Company performed impairment tests for goodwill and intangible assets with indefinite useful lives, and determined that goodwill was impaired. This resulted in a non-cash impairment charge of \$4.5 million that was recorded in the consolidated financial statements for the year ended November 30, 2009. In November 2008, the Company determined that these assets were not impaired. The impairment test involves considerable use of judgment, and requires management to make estimates and assumptions. The fair values of the reporting units are derived from certain valuation models, which consider various factors such as cost of capital, discount rates, the Company's stock price, future earnings, and earnings multiples. Changes in estimates and assumptions can affect the reported value of goodwill and intangible assets with indefinite useful lives.

#### *Future income tax assets*

The Company is required to determine if the "more likely than not" test under the liability method of accounting for income taxes is met in order to include in income the potential tax benefits relating to increases in future income tax assets. The valuation of income tax assets involves considerable use of judgment and

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requires management to make estimates and assumptions. Estimates and assumptions include projected earnings, projected growth, projected taxable income and tax planning strategies. Changes in estimates and assumptions can affect the reported value of net future tax assets.

### Revenue recognition

The Company generates a portion of International Systems revenues from long-term fixed fee contracts to render specific consulting and software modification services. Revenues from long-term contracts are recognized using the percentage of completion method based on labour costs incurred relative to total estimated labour costs. The long-term nature of contracts involves considerable use of judgment and estimates in determining total revenues, total labour costs and percentage of completion. There are numerous factors to consider, including variances in the contract deliverables, scheduling, labour costs and productivity. The Company has developed methods and systems to provide dependable expenditure estimates for its long-term contracts.

## PROPOSED TRANSACTIONS

We are not currently engaged in any proposed transactions.

## SELECTED QUARTERLY DATA (UNAUDITED)

In thousands of Canadian dollars

For the three months ended	February 28, 2010	November 30, 2009	August 31, 2009	May 31, 2009
Revenue	\$ 3,444	\$ 4,743	\$ 6,212	\$ 6,315
Gross profit	1,155	1,435	2,362	1,934
Gross profit percentage	34%	30%	38%	31%
Net income (loss)	2,082	(5,713)	(263)	(1,038)
Net income (loss) attributable to common shareholders				
Basic	1,951	(5,860)	(410)	(1,192)
Diluted	2,082	(5,860)	(410)	(1,192)
Earnings (loss) per share:				
Basic	0.04	(0.12)	(0.01)	(0.02)
Diluted	0.04	(0.12)	(0.01)	(0.02)

For the three months ended	February 28, 2009	November 30, 2008	August 31, 2008	May 31, 2008
Revenue	\$ 5,724	\$ 8,146	\$ 6,327	\$ 6,574
Gross profit	1,719	3,332	2,243	2,025
Gross profit percentage	30%	41%	36%	31%
Net income (loss)	(697)	1,029	(682)	(1,174)
Net income (loss) attributable to common shareholders				
Basic	(853)	873	(838)	(1,330)
Diluted	(853)	873	(838)	(1,330)
Earnings (loss) per share:				
Basic	(0.02)	0.02	(0.02)	(0.03)
Diluted	(0.02)	0.02	(0.02)	(0.03)

## **OSI Geospatial Inc.**

Management's Discussion and Analysis  
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### **CRITICAL ACCOUNTING POLICIES**

These items are substantially unchanged as discussed in the Company's MD&A for the year ended November 30, 2009 as contained in our 2009 Annual Report filed on SEDAR at [www.sedar.com](http://www.sedar.com).

### **RECENT ACCOUNTING PRONOUNCEMENTS**

The following recent pronouncements issued by the CICA will be monitored by the Company:

The CICA has issued CICA Handbook Section 1582, *Business Combinations*, which replaces CICA Handbook Section 1581, *Business Combinations*. This Section establishes standards for the recognition, measurement, presentation, and disclosure of business combinations. This Section applies to annual and interim financial statements relating to fiscal years beginning on or after January 1, 2011. Accordingly, the Company will adopt the new section for its fiscal year beginning December 1, 2011. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

The CICA has issued CICA Handbook Section 1601, *Consolidated Financial Statements*, and CICA Handbook Section 1602, *Non-controlling Interests*, which replace CICA Handbook Section 1600, *Consolidated Financial Statements*. CICA Handbook Section 1601 establishes standards for the preparation of consolidated financial statements, and CICA Handbook Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements. These sections apply to annual and interim financial statements relating to fiscal years beginning on or after January 1, 2011. Accordingly, the Company will adopt the new Sections for its fiscal year beginning December 1, 2011. The Company does not expect that the adoption of these new Sections will have a material impact on its consolidated financial statements.

The Canadian Accounting Standards Board has confirmed that the use of International Financial Reporting Standards ("IFRS") will be required commencing 2011 for publicly-accountable, profit-oriented enterprises. IFRS will be replacing current Canadian GAAP followed by the Company. The Company will be required to begin reporting under IFRS for its fiscal year ended November 30, 2012, and will be required to provide information that conforms to IFRS for the comparative periods presented. The Company is currently evaluating the impact of adopting IFRS.

The CICA has issued EIC 175, *Multiple Deliverable Revenue Arrangements*, which addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting. This abstract also addresses how arrangement consideration should be measured and allocated to the separate units of accounting in the arrangement. EIC 175 applies to revenue arrangements with multiple deliverables entered into or materially modified in the first annual fiscal period beginning on or after January 1, 2011. Accordingly, the Company will adopt the new sections for its fiscal year beginning December 1, 2011. The Company does not expect that the adoption of this standard will have a material impact on its consolidated financial statements.

### **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

#### **Foreign Exchange Forward Contracts**

Derivative financial instruments are utilized by the Company in the management of its foreign currency exposure to reduce its exposure to fluctuations in foreign exchange on certain committed and anticipated transactions. The Company formally documents the relationships between derivative financial instruments and hedged items, as well as the risk management objective and strategy. The Company assesses, on an

## OSI Geospatial Inc.

Management's Discussion and Analysis  
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ongoing basis, whether the derivative financial instruments continue to be effective in offsetting changes in fair values or cash flows of the hedged transactions.

Changes in fair value of foreign currency denominated derivative financial instruments used to hedge anticipated or committed foreign currency exposures are recognized as an adjustment to the related operating costs or revenue when the hedged transaction is recorded. Derivatives are not subject to hedge accounting and are recorded on the consolidated balance sheets with the changes in fair value being recorded in the consolidated statement of operations each period.

The Company purchases foreign exchange forward contracts to mitigate the exposure to sales and the related accounts receivable to customers denominated in U.S. dollars, UK pounds, Australian dollars and Euros.

At February 28, 2010, we had entered into the following foreign exchange forward contracts, which were not treated as hedges in accordance with CICA Section 3865:

<i>Sell</i>	<i>Exchange rate in relation to CAD</i>	<i>Value date</i>
GBP 292,000	1.6849 to 1.7503	April 5, 2010 to May 28, 2010
EURO 220,000	1.4713 to 1.5704	April 5, 2010 to May 28, 2010
USD 51,000	1.0600	April 5, 2010

### DISCLOSURE OF OUTSTANDING SHARE DATA

As at April 13, 2010, we had 51,602,083 issued and outstanding common shares and 3,384,083 outstanding stock options. As at April 13, 2010, we also had 30,262 issued and outstanding class A preference shares and 100,829 issued and outstanding class B preference shares series 2 convertible into common shares at conversion ratios of 1:1 and 1:58.82353, respectively, which represents 5,961,380 common shares.

### DISCLOSURE CONTROLS AND PROCEDURES

Management, including the Chief Executive Officer and the Chief Financial Officer, is responsible for establishing and maintaining disclosure controls and procedures as defined in National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings*. Management, as at the end of the period covered by this interim filing, designed disclosure controls and procedures to provide reasonable, but not absolute, assurance that (i) material information relating to the issuer is made known to management by others, particularly during the period in which the interim filings were being prepared; and (ii) information required to be disclosed by the issuer in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

Disclosure controls and procedures provide only a reasonable level of assurance that they are effective. Accordingly, they may not detect that all disclosure requirements have not been met. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

## **OSI Geospatial Inc.**

Management's Discussion and Analysis  
For the three months ended February 28, 2010 and 2009  
(expressed in Canadian dollars)

### **INTERNAL CONTROL OVER FINANCIAL REPORTING**

Management, including the Chief Executive Officer and the Chief Financial Officer, is responsible for establishing and maintaining internal control over financial reporting as defined in National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings*. Management, as at the end of the period covered by this interim filing, designed internal control over financial reporting to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. The control framework management used to design the issuer's internal control over financial reporting is that established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management did not identify material weaknesses relating to the design of internal controls over financial reporting existing at the end of the period covered by this interim filing.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the design of internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Chief Executive Officer and the Chief Financial Officer have evaluated the effectiveness of the Company's internal control over financial reporting and have determined that the Company's internal control over financial reporting was effective as of November 30, 2009.

### **CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING**

There were no changes in the Company's internal control over financial reporting that occurred since the beginning of the Company's first quarter to the date of this document that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

### **RISKS AND UNCERTAINTIES**

The primary risks and uncertainties that affect and may affect us and our business, financial condition and results of operations are substantially unchanged as discussed in the Company's MD&A for the year ended November 30, 2009 as contained in our 2009 Annual Report filed on SEDAR at [www.sedar.com](http://www.sedar.com).



## **OSI Geospatial Inc.**

**Interim Consolidated Financial Statements (Unaudited)  
Three Months Ended February 28, 2010 and 2009  
(expressed in Canadian dollars)**

(Prepared in accordance with Canadian Generally Accepted Accounting Principles)

# OSI Geospatial Inc.

(Incorporated under the laws of the Province of British Columbia, Canada)

## Interim Consolidated Balance Sheets (Unaudited)

In thousands of Canadian dollars	February 28, 2010	November 30, 2009
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 2,852	\$ 315
Restricted cash	263	-
Accounts receivable and unbilled revenue	4,832	5,880
Inventory (note 5)	1,053	1,139
Prepaid expenses and deposits	480	375
Current portion of future income tax asset	181	1,041
	9,661	8,750
<b>Restricted cash</b>	373	-
<b>Deferred development costs</b>	546	653
<b>Future income tax asset</b>	80	113
<b>Equipment and furnishings</b>	1,334	1,473
<b>Intangible and other assets</b>	380	446
<b>Goodwill</b>	4,305	4,324
	\$ 16,679	\$ 15,759
<b>Liabilities</b>		
<b>Current liabilities</b>		
Bank indebtedness	\$ -	\$ 599
Factored advances payable (note 4)	74	240
Accounts payable and accrued liabilities	2,637	3,806
Income taxes payable	1,068	-
Unearned revenue	279	550
Current portion of deferred rent	41	41
Current portion of capital lease obligation	54	68
	4,153	5,304
<b>Deferred rent</b>	249	260
<b>Capital lease obligation</b>	48	54
<b>Unearned revenue</b>	150	178
	4,600	5,796
<b>Contingency (note 10)</b>		
<b>Shareholders' Equity</b>		
Issued and outstanding		
Class A, Series A preference shares	30	30
Class B, Series 2 preference shares (note 6a)	3,237	5,383
Common shares (note 6a)	30,769	29,876
	34,036	35,289
<b>Warrants (note 6b)</b>	4,546	4,546
<b>Contributed surplus (note 6a)</b>	4,603	3,322
<b>Accumulated deficit</b>	(29,759)	(31,838)
<b>Accumulated other comprehensive loss</b>	(1,347)	(1,356)
	12,079	9,963
	\$ 16,679	\$ 15,759

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

# OSI Geospatial Inc.

## Interim Consolidated Statements of Income (Loss) and Deficit (Unaudited)

In thousands of Canadian dollars, except share related data	Three months ended February 28,	
	2010	2009
<b>Revenue</b>		
Maritime navigation and tactical solutions	\$ 1,406	\$ 3,522
Advanced technology research and development	1,924	1,943
Mapping	114	259
	<hr/>	<hr/>
	3,444	5,724
<b>Cost of sales</b>	<hr/>	<hr/>
	2,338	4,005
<b>Gross profit</b>	<hr/>	<hr/>
	1,106	1,719
<b>Expenses (income)</b>		
General and administrative	1,267	1,209
Sales and marketing	665	813
Engineering	176	301
Amortization	87	113
Interest expense	38	31
Foreign exchange gain	(10)	-
Technology Partnerships Canada royalty	69	96
	<hr/>	<hr/>
	2,292	2,563
<b>Net loss before other items</b>	<hr/>	<hr/>
	(1,186)	(844)
Gain on sale of intellectual property (note 11)	5,227	-
<b>Net income (loss) before income taxes</b>	<hr/>	<hr/>
	4,041	(844)
Future income tax (recovery)	888	(152)
Current income tax expense	1,071	5
<b>Income tax expense (recovery)</b>	<hr/>	<hr/>
	1,959	(147)
<b>Net income (loss)</b>	<hr/>	<hr/>
	2,082	(697)
Accumulated deficit, beginning of period	(31,838)	(24,121)
Dividends on Class B preference shares	(3)	(3)
<b>Accumulated deficit, end of period</b>	<hr/>	<hr/>
	\$ (29,759)	\$ (24,821)
<b>Net income (loss) attributable to common shareholders</b> (note 6d)		
Basic	\$ 1,951	\$ (853)
Diluted	2,082	(853)
<b>Earnings (loss) per share</b> (note 6d):		
Basic	\$ 0.04	\$ (0.02)
Diluted	0.04	(0.02)
<b>Weighted average number of common shares outstanding</b> (note 6d):		
Basic	48,733,766	46,956,439
Diluted	57,659,553	46,956,439

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

## OSI Geospatial Inc.

### Interim Consolidated Statements of Comprehensive Income (Loss) (Unaudited)

In thousands of Canadian dollars	<b>Three months ended February 28,</b>	
	<b>2010</b>	<b>2009</b>
<b>Net income (loss)</b>	\$ 2,082	\$ (697)
<b>Other comprehensive income, net of taxes</b>		
Unrealized gain on translation of self-sustaining foreign operations	9	361
<b>Comprehensive income (loss)</b>	<u>\$ 2,091</u>	<u>\$ (336)</u>

## OSI Geospatial Inc.

### Interim Consolidated Statements of Accumulated Other Comprehensive Income (Loss) (Unaudited)

In thousands of Canadian dollars	<b>Three months ended February 28,</b>	<b>Year ended November 30,</b>
	<b>2010</b>	<b>2009</b>
Accumulated other comprehensive income (loss), beginning of the period	\$ (1,356)	\$ 631
Unrealized gain (loss) on translating financial statements of self-sustaining foreign operations	9	(1,987)
<b>Accumulated other comprehensive loss, end of period</b>	<u>\$ (1,347)</u>	<u>\$ (1,356)</u>

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

# OSI Geospatial Inc.

## Interim Consolidated Statements of Cash Flows (Unaudited)

In thousands of Canadian dollars	Three months ended February 28,	
	2010	2009
<b>Cash flows from (used in) operating activities</b>		
Net income (loss) for the period	\$ 2,082	\$ (697)
Items not affecting cash		
Amortization	124	161
Gain on disposal of intellectual property	(5,227)	-
Stock-based compensation	28	-
Future income taxes	888	(152)
	<u>(2,105)</u>	<u>(688)</u>
Changes in non-cash operating working capital items		
Accounts receivable	1,036	2,014
Inventory	86	356
Prepaid expenses and deposits	(103)	(220)
Accounts payable and accrued liabilities	(1,164)	(1,331)
Income taxes payable	1,070	5
Deferred rent	(10)	(10)
Unearned revenue	(299)	10
	<u>616</u>	<u>824</u>
	<u>(1,489)</u>	<u>136</u>
<b>Cash flows from (used in) investing activities</b>		
Increase in restricted cash	(638)	-
Development costs deferred	(25)	(18)
Additions to equipment and furnishings	(10)	(30)
Additions to intangibles and other assets	-	(2)
Proceeds from disposal of intellectual property and related tangible assets, net of costs to dispose	5,444	-
	<u>4,771</u>	<u>(50)</u>
<b>Cash flows used in financing activities</b>		
Repayment of bank indebtedness	(599)	(66)
Factored advances payable	(165)	-
Repayment of capital lease obligation	(20)	(14)
Class B preference share dividends declared and paid	(3)	(3)
	<u>(787)</u>	<u>(83)</u>
<b>Effect of foreign exchange on cash balances</b>	<u>42</u>	<u>(3)</u>
<b>Increase in cash and cash equivalents</b>	<u>2,537</u>	<u>-</u>
<b>Cash and cash equivalents – beginning of period</b>	<u>315</u>	<u>-</u>
<b>Cash and cash equivalents – end of period</b>	<u>\$ 2,852</u>	<u>\$ -</u>
Supplemental cash flow information:		
Cash interest paid	\$ (43)	\$ (30)
Cash income taxes paid	(1)	-

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

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited)

Three Months Ended February 28, 2010 and 2009

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### 1 Basis of presentation

These unaudited interim consolidated financial statements have been prepared by management and include the accounts of OSI Geospatial Inc. and its subsidiaries, collectively referred to as OSI Geospatial or the Company. These unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") and all amounts have been expressed in Canadian dollars unless otherwise noted.

These unaudited interim consolidated financial statements have been prepared using the same accounting policies used in the preparation of the audited annual consolidated financial statements for the year ended November 30, 2009.

These unaudited interim consolidated financial statements do not include all the information and footnote disclosures required by Canadian GAAP for annual audited consolidated financial statements. These unaudited interim consolidated financial statements should be read in conjunction with the Company's audited annual consolidated financial statements.

The preparation of these unaudited interim consolidated financial statements requires management to make estimates and assumptions that affect the amounts reported. Actual results could vary from these estimates and the operating results for the interim periods presented are not necessarily indicative of the results expected for the full year.

These unaudited interim consolidated financial statements are prepared on a going-concern basis, which assumes that the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. Certain conditions and uncertainties cast doubt about the validity of this assumption. The Company has a history of recurring losses and has an accumulated deficit of \$30 million. In October 2009, the Company replaced its U.S. line of credit with an accounts receivable factoring arrangement to support its U.S. working capital requirements. In January 2010, the Company replaced its Canadian line of credit with an accounts receivable factoring arrangement to support its Canadian working capital requirements. As per note 11, on February 1, 2010, the Company sold its soldier systems intellectual property for U.S. \$6.5 million. The net proceeds after corporate income taxes are approximately U.S. \$5.5 million with approximately U.S. \$5.0 million paid in February 2010 and the balance to be paid in fiscal 2011. The net proceeds provided additional working capital for the Company. The Company expects that its level of working capital should be sufficient to fund future operations for a period greater than twelve months.

The ability of the Company to continue as a going concern and meet its commitments and ongoing operating expenses is dependent on achieving profitable operations, and/or obtaining necessary levels of financing. There is no assurance that the Company will be successful in achieving these goals.

These unaudited interim consolidated financial statements do not include any adjustments to the carrying value of assets and liabilities, and changes to balance sheet classifications that might be necessary should the Company not continue as a going concern and these adjustments and reclassifications could be material.

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

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### 2 Accounting Changes

#### Recent pronouncements

The following recent pronouncements issued by the Canadian Institute of Chartered Accountants (CICA) will be monitored by the Company:

The CICA has issued CICA Handbook Section 1582, *Business Combinations*, which replaces CICA Handbook Section 1581, *Business Combinations*. This Section establishes standards for the recognition, measurement, presentation and disclosure of business combinations. This Section applies to annual and interim financial statements relating to fiscal years beginning on or after January 1, 2011. Accordingly, the Company plans to adopt the new Section for its fiscal year beginning December 1, 2011. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

The CICA has issued CICA Handbook Section 1601, *Consolidated Financial Statements*, and CICA Handbook Section 1602, *Non-controlling Interests*, which replace CICA Handbook Section 1600, *Consolidated Financial Statements*. CICA Handbook Section 1601 establishes standards for the preparation of consolidated financial statements and CICA Handbook Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements. These Sections apply to annual and interim financial statements relating to fiscal years beginning on or after January 1, 2011. Accordingly, the Company plans to adopt the new Section for its fiscal year beginning December 1, 2011. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

The CICA has issued EIC 175, *Multiple Deliverable Revenue Arrangements*, which addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting. This abstract also addresses how arrangement consideration should be measured and allocated to the separate units of accounting in the arrangement. EIC 175 applies to revenue arrangements with multiple deliverables entered into or materially modified in the first annual fiscal period beginning on or after January 1, 2011. Accordingly, the Company plans to adopt the new Section for its fiscal year beginning December 1, 2011. The Company does not expect that the adoption of this standard will have a material impact on its consolidated financial statements.

The Canadian Accounting Standards Board has confirmed that the use of International Financial Reporting Standards ("IFRS") will be required commencing 2011 for publicly accountable, profit oriented enterprises. IFRS will be replacing current Canadian GAAP followed by the Company. The Company will be required to begin reporting under IFRS for its fiscal year ended November 30, 2012 and will be required to provide information that conforms to IFRS for the comparative periods presented. The Company is currently evaluating the impact of adopting IFRS.

### 3 Nature of operations

OSI Geospatial delivers integrated navigation and tactical solutions that meet naval and maritime security operational requirements. These solutions include our Warship Electronic Chart Display and Information System (ECPINS®-W/S), Tactical Asset Control and Tracking System (TACTS), Integrated Navigation and Tactical System (INTS) and security risk assessment consulting services. In addition, OSI Geospatial provides advanced technology research and development engineering services in support of the military and security requirements and mapping services that provide geospatial data production and consulting services. OSI Geospatial conducts its operations through three business units – International Systems, U.S. Systems and Mapping.

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

### 4 Credit facilities

In January 2010, the Company moved its Canadian credit facilities to another Canadian financial institution. The financing agreement consists of accounts receivable factoring arrangements.

At February 28, 2010, the Company had total borrowing capacity under its Canadian accounts receivable factoring arrangement of \$2.0 million. Under the terms of the factoring agreement, the Company may be requested to repay any amounts owing plus applicable interest. The fees charged under this agreement are a) discount equal to discount percentage as set forth in the applicable schedule; b) 18.25% interest on any receivables that are required to be repurchased, payable from the designated due date until payment is made; and c) per diem equal to discount factor as set forth in the applicable schedule for any receivable not collected, payable from the designated due date until full payment of receivable is received. The financial institution is not entitled to both the interest and the per diem on any given day in respect of the same receivable. The credit facility is secured by a general assignment of accounts covering substantially all of the Company's present and future Canadian accounts receivable, claims and interests. This arrangement is being recorded as a financing from the factoring company and factoring costs are being charged to operations as incurred. At February 28, 2010, the amount advanced under this facility was \$nil (November 30, 2009 – \$nil).

In October 2009, the Company's subsidiary, CHI Systems Inc. ("CHI"), entered into accounts receivable factoring arrangements with a U.S. financial institution. Under the terms of the factoring agreement, CHI shall repurchase the accounts that remain unpaid because of certain events as specified in the agreement. Fees charged under this agreement are a servicing fee of 0.275% for the first 15 days, 0.293% after 15 days and a daily discount fee of 0.0132%. The daily discount fee is the prime rate as published in *The Wall Street Journal* on the purchase date plus 1.5% per annum. This arrangement is being recorded as a financing from the factoring company and factoring costs are being charged to operations as incurred. The facility is secured by a security agreement covering substantially all of CHI's present and future property and interests. At February 28, 2010, the amount advanced under this facility was \$74,000 (November 30, 2009 – \$240,000).

The Company has a foreign exchange facility with a Canadian chartered bank whereby it can enter into forward foreign exchange contracts. The maximum facility is based on a bank formula for deemed risk and is calculated using recent volatility in the currency of the contract as well as the length of the contract. At February 28, 2010, the foreign exchange facility would enable the Company to enter into U.S. dollar denominated forward foreign exchange contracts for approximately \$9 million (November 30, 2009 - \$9 million). This facility is insured through insurance solutions provided by Export Development Canada. As at February 28, 2010, the Company has drawn on its forward foreign exchange contract facility in the amount of \$894,000 (November 30, 2009 - \$918,000). A foreign exchange gain on these contracts of \$56,000 and a foreign exchange loss of \$8,000 was recognized at February 28, 2010 and November 30, 2009, respectively.

### 5 Inventory

In thousands of Canadian dollars

	February 28, 2010	November 30, 2009
Materials and components	\$ 825	\$ 806
Work-in-process	45	150
Finished goods	183	183
	<u>\$ 1,053</u>	<u>\$ 1,139</u>

The cost of inventories recognized as expense and included in cost of sales for the three months ended February 28, 2010 was \$100,000 (three months ended February 28, 2009 - \$848,000).

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

### 6 Capital stock

#### a) Class B series 2 preference shares and common shares

During the three months ended February 28, 2010, 66,861 Class B series 2 preference shares (2009 – nil) were converted into 3,932,999 common shares. Accordingly, the Class B series 2 preference shares were reduced by \$2,146,000, the carrying value of the shares converted. The common shares were increased by \$893,000 and the contributed surplus was increased by \$1,253,000.

#### b) Warrants

On July 31, 2009, 2,780,000 common share purchase warrants, which were valued at \$352,000 using the Black-Scholes option pricing model, expired. Accordingly, the Company has reduced warrants by \$352,000 with a corresponding increase to contributed surplus.

#### c) Stock option plans

A summary of the outstanding and exercisable options of the Company's stock option plan at February 28, 2010 is as follows:

In Canadian dollars		
	Number of shares	Weighted average exercise price
Outstanding at November 30, 2009	4,153,166	\$ 0.65
Granted	525,000	0.23
Forfeited	(380,750)	0.48
Surrendered	(510,333)	0.91
Outstanding at February 28, 2010	3,787,083	\$ 0.57
Exercisable at February 28, 2010	3,003,739	\$ 0.67

#### Stock-based compensation

For the three months ended February 28, 2010, the Company incurred non-cash stock-based compensation expense of \$28,000 (three months ended February 28, 2009 - \$nil) related to 525,000 stock options granted during the quarter ended February 28, 2010 and 1,275,000 stock options granted during the year ended November 30, 2009. Of the stock options granted during the quarter ended February 28, 2010, 175,000 vested immediately, 175,000 will vest over one year and 175,000 will vest over two years from the grant date. Of the stock options granted during the year ended November 30, 2009, 809,000 vested immediately, 233,000 will vest over one year and 233,000 will vest over two years from the grant date. The expense was included in general and administrative costs and the offsetting amount was recorded in contributed surplus. The weighted average fair value of the stock options at grant date is \$0.12 per stock option (2009 - \$0.07).

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

### d) Earnings (loss) per share

In thousands of Canadian dollars, except share related data	For the three months ended February 28,	
<b>Earnings (loss) per share – basic</b>	<b>2010</b>	<b>2009</b>
Net income (loss) for the period	\$ 2,082	\$ (697)
Less:		
Class B Series 2 preference share dividends (*A)	(131)	(156)
Net income (loss) available to common shareholders	\$ 1,951	\$ (853)
Weighted average number of common shares outstanding – basic	48,733,766	46,956,439
Earnings (loss) per share – basic	\$ 0.04	\$ (0.02)

(\*A) Dividends of \$131,000 (2009 - \$156,000) are included which represents the dividends earned by the shareholders of Class B Series 2 cumulative preference shares. As at February 28, 2010, there were \$1,351,000 (November 30, 2009 - \$1,219,000) of dividends in arrears for the Class B Series 2 cumulative preference shares.

In thousands of Canadian dollars, except share related data	For the three months ended February 28,	
<b>Earnings (loss) per share – diluted</b>	<b>2010</b>	<b>2009</b>
Net income (loss) for the period	\$ 2,082	\$ (697)
Less:		
Class B Series 2 preference share dividends (*A)	-	(156)
Net income (loss) available to common shareholders	\$ 2,082	\$ (853)
Weighted average number of common shares outstanding	48,733,766	46,956,439
Dilutive effect of Class A, Series A preference shares (*C)	30,262	-
Dilutive effect of Class B, Series 2 preference shares (*C)	8,799,431	-
Dilutive effect of warrants (*B) (*C)	-	-
Dilutive effect of stock options (*B) (*C)	96,094	-
Adjusted weighted average number of common shares outstanding – diluted	57,659,553	46,956,439
Earnings (loss) per share – diluted	\$ 0.04	\$ (0.02)

(\*A) Dividends of \$nil (2009 - \$156,000) are included which represents the dividends earned by the shareholders of Class B Series 2 cumulative preference shares. As at February 28, 2010, there were \$1,351,000 (November 30, 2009 - \$1,219,000) of dividends in arrears for the Class B Series 2 cumulative preference shares.

(\*B) The outstanding warrants and some stock options that were outstanding at February 28, 2010 were not included in the calculation of diluted earnings per share because the exercise price of warrants and stock options were greater than the average market price of the common shares.

(\*C) The outstanding preferred shares, warrants and stock options were anti-dilutive for the purposes of calculating diluted loss per share for the three months ended February 28, 2009.

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

If all preferred shares were converted, and all warrants and options were exercised, there would be a total of 73,746,610 common shares outstanding at February 28, 2010 (November 30, 2009 – 76,093,696). As a result of the exercise of all warrants and options, the Company would receive cash of \$12.7 million (November 30, 2009 - \$13.2 million).

### 7 Financial instruments

The Company has exposure to the following risks from its use of financial instruments: credit, market and liquidity risks. The Company reviews its risk management framework on a quarterly basis and makes adjustments as necessary.

#### Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises principally from the Company's cash and cash equivalents, accounts receivable and its foreign exchange contracts. The Company provides credit to its customers in the normal course of its operations. The Company's credit risk review includes performing credit evaluations of the financial condition of significant customers. The Company's customers are for the most part national and international government clients and large public customers. A significant portion of the Company's accounts receivable is from long-time customers and at February 28, 2010, 84% (November 30, 2009 – 62%) of its accounts receivable was with national and international government clients and 4% (November 30, 2009 – 20%) of its accounts receivable was with large international public companies. Due to the low risk nature of the government clients and a history of excellent collections, provisions for doubtful accounts are made on a customer-by-customer basis, based on ongoing customer discussions.

The Company is exposed to non-performance by counterparties to foreign currency forward contracts. These counterparties are major financial institutions and to date, no such counterparty has failed to meet its financial obligations to the Company. Management does not believe there is a significant risk of non-performance by these counterparties because the positions with and the credit rating of these counterparties are monitored.

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

In thousands of Canadian dollars

	<b>February 28, 2010</b>	<b>November 30, 2009</b>
Cash and cash equivalents	\$ 2,852	\$ 315
Restricted cash	636	-
Trade accounts receivable	2,474	2,607
Unbilled revenue	2,124	3,164
Other	244	119
Allowance for doubtful accounts	(10)	(10)
	<b>\$ 8,320</b>	<b>\$ 6,195</b>

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

The aging of the trade accounts receivable at the reporting date was:

In thousands of Canadian dollars

	February 28, 2010	November 30, 2009
Current	\$ 2,054	\$ 2,401
Past due (61 – 90 days)	52	33
Past due greater than 90 days	368	173
	<u>\$ 2,474</u>	<u>\$ 2,607</u>

Based on historic default rates, the Company believes that there are minimal requirements for an allowance for doubtful accounts.

### Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, will affect the Company's income or the value of its holding of financial instruments.

#### *Foreign exchange risk*

The Company operates internationally, giving rise to exposure to market risks from changes in foreign exchange rates. The Company is exposed to foreign currency fluctuations mainly on its accounts receivable and future cash flows related to contracts denominated in a foreign currency. The Company's foreign exchange risk management includes the use of foreign currency forward contracts to fix the exchange rates on certain foreign currency exposures. The Company's objective is to manage and control exposures and secure the Company's profitability on existing contracts and, therefore, the Company's policy is to hedge the majority of its foreign currency exposure. The Company does not utilize derivative financial instruments for trading or speculative purposes. The Company formally documents all relationships between derivative financial 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 firm contractually related commitments on projects.

The Company did not designate its foreign exchange forward contracts as a hedge of underlying assets, liabilities, firm commitments or anticipated transactions in accordance with CICA Handbook Section 3865, *Hedges*, and accordingly, did not use hedge accounting. As a result of this, the foreign exchange forward contracts are recorded on the consolidated balance sheet at fair value in other receivables when the contracts are in a gain position and in other accrued liabilities when the contracts are in a loss position. The fair value of the foreign exchange forward contracts was a recorded asset in other receivables of \$56,000 at February 28, 2010 and was a recorded liability in accounts payable and accrued liabilities of \$8,000 at November 30, 2009. Changes in fair value of these contracts are recognized as gains or losses in the consolidated statement of operations.

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

The forward foreign exchange contracts primarily require the Company to sell certain foreign currencies for Canadian dollars at contractual rates. The Company had the following forward foreign exchange contracts:

In thousands of dollars				February 28, 2010	
Type	Notional	Currency	Maturity	Equivalent to Canadian Dollars	Fair Value
Sell	192	GBP	April 2010	336	\$ 29
Sell	51	USD	April 2010	54	-
Sell	120	EURO	April 2010	188	16
Sell	100	GBP	May 2010	168	8
Sell	100	EURO	May 2010	147	3
					<u>\$ 56</u>

In thousands of dollars				November 30, 2009	
Type	Notional	Currency	Maturity	Equivalent to Canadian Dollars	Fair Value
Sell	200	GBP	April 2010	350	\$ -
Sell	120	USD	April 2010	127	-
Sell	163	EURO	February 2010	253	(6)
Sell	120	EURO	April 2010	188	(2)
					<u>\$ (8)</u>

A 10% strengthening (weakening) of the Canadian dollar against each of the Great Britain pound, the U. S. dollar, the Euro and the Australian dollar would have decreased (increased) earnings from operations at February 28, 2010 by a total of \$15,000 (November 30, 2009 – \$5,000). A 10% strengthening (weakening) of the Canadian dollar against the U.S. dollar would have decreased (increased) the reporting currency earnings from U.S. operations for the three months ended February 28, 2010 by a total of \$473,000 (the year ended November 30, 2009 – \$51,000). A 10% strengthening (weakening) of the Canadian dollar against the U.S. dollar would impact the reporting currency balance sheet values at February 28, 2010 with an offsetting loss (gain) of approximately \$832,000 (November 30, 2009 – \$1,183,000) to other comprehensive income.

### *Interest rate risk*

The Company is exposed to interest rate risk on its operating line of credit. A 1% increase (decrease) in the interest rate would have resulted in \$1,000 increase (decrease) in the loss of the Company for this quarter.

### **Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity risk is to ensure that it will always have sufficient liquidity to meet liabilities when due. The Company has an accounts receivable factoring credit facility of \$2.0 million in Canada and a variable limit in the U.S. that is based on the outstanding accounts receivable of the U.S. operations. At February 28, 2010, the Company utilized \$nil (November 30, 2009 – \$nil) and U.S. \$71,000 (November 30, 2009 – U.S. \$227,000). As at November 30, 2009, the Company has operating line of credit facility of \$1 million in Canada and utilized \$860,000. All of the Company's financial liabilities, other than capital lease obligations, have contractual maturities of less than 45 days.

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited)

Three Months Ended February 28, 2010 and 2009

The table below analyzes the following liabilities which will settle as indicated based on the remaining periods at February 28, 2010 to the contractual maturity date. The amounts disclosed in this table are the contractual undiscounted cash flows. Balances within twelve months equal the carrying balance as the impact of discounting is not significant.

<b>Payments due by period</b>	<b>Total</b>	<b>Less than 1 year</b>	<b>1 to 3 years</b>	<b>4 to 5 years</b>	<b>After 5 years</b>
In thousands of Canadian dollars					
Facility leases	\$ 2,967	\$ 761	\$ 1,156	\$ 510	\$ 540
Capital equipment leases	113	61	52	-	-
Operating equipment leases	43	31	12	-	-
<b>Total contractual obligations</b>	<b>\$ 3,123</b>	<b>\$ 853</b>	<b>\$ 1,220</b>	<b>\$ 510</b>	<b>\$ 540</b>

### Fair values

#### a) Establishing fair value

The Company's financial instruments consist of cash, bank indebtedness, accounts receivable, accounts payable and accrued liabilities, factored advances payable, capital lease obligations, and foreign exchange contracts. The carrying value of cash and cash equivalents, bank indebtedness, accounts receivable, accounts payable and accrued liabilities, and factored advances payable approximates their fair value due to the immediate or short-term maturity of these financial instruments.

The fair values of the Company's forward foreign exchange contracts are based on the current market values of similar contracts with the same remaining duration as if the contracts had been entered into on February 28, 2010 and November 30, 2009.

The carrying amounts of each of the financial instruments are:

In thousands of Canadian dollars

	<b>February 28, 2010</b>	<b>November 30, 2009</b>
Held-for-trading		
Cash	\$ 2,852	\$ 315
Restricted cash	636	-
Forward contracts	56	(8)
Loans and receivables		
Trade accounts receivable	2,474	2,607
Other liabilities		
Bank indebtedness	-	(599)
Factored advances payable	(74)	(240)
Accounts payable and accrued liabilities	(2,637)	(3,806)
Capital lease obligation	(102)	(122)

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

### b) Fair-value hierarchy

Financial instruments recorded at fair value on the consolidated balance sheet are classified using the fair-value hierarchy that reflects the significance of the inputs used in making the measurements. The fair-value hierarchy has the following levels:

Level 1 – valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and

Level 3 – valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair-value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The following table presents the fair value of the financial instruments that are carried at fair value classified using the fair-value hierarchy described above:

In thousands of Canadian dollars	February 28, 2010			
	Level 1	Level 2	Level 3	Total
Financial assets				
Forward foreign exchange contracts	\$ -	\$ 56	\$ -	\$ 56
Total financial assets	\$ -	\$ 56	\$ -	\$ 56
In thousands of Canadian dollars	November 30, 2009			
	Level 1	Level 2	Level 3	Total
Financial liabilities				
Forward foreign exchange contracts	\$ -	\$ (8)	\$ -	\$ (8)
Total financial liabilities	\$ -	\$ (8)	\$ -	\$ (8)

## 8 Capital structure management

The Company's objective is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Company reviews on a semi-annual basis whether any dividends should be paid.

The Company monitors capital on a basis consistent with others in the industry based on total debt to shareholders' equity. Management defines capital as the Company's total shareholders' equity, excluding accumulated other comprehensive income and total debt, is defined as bank indebtedness and capital lease obligations.

There were no changes in the Company's approach to capital management during the period. Neither the Company nor any of its subsidiaries is subject to externally imposed capital requirements other than disclosed in note 4.

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

In thousands of Canadian dollars

	February 28, 2010	November 30, 2009
Bank indebtedness	\$ -	\$ 599
Factored advances payable	74	240
Capital lease obligation	101	122
Total debt	<u>\$ 175</u>	<u>\$ 961</u>
Total equity	12,079	9,963
Less accumulated other comprehensive loss	1,347	1,356
Net equity	<u>\$ 13,426</u>	<u>\$ 11,319</u>

### 9 Segmented information

The Company operates in four segments: International Systems Operations, U.S. Systems Operations, Mapping Operations and Corporate and public company costs. Operating segments are identified as components of the Company for which separate discrete financial information is available for evaluation by the chief operating decision maker regarding how to allocate resources and assess performance. The Company's chief operating decision maker is the Chief Executive Officer.

The Company's reportable segments are as outlined below which are defined by their primary type of service offerings. Information about the Company's reportable segments is as follows:

In thousands of Canadian dollars

Three Months Ended February 28, 2010

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
Revenue	\$ 1,215	\$ 2,115	\$ 114	\$ -	\$ 3,444
Gross profit	644	549	(87)	-	1,106
Technology Partnerships Canada – net	69	-	-	-	69
Interest expense	7	5	-	26	38
Income tax expense (recovery)	-	1,959	-	-	1,959
Amortization	46	48	24	6	124
Net income (loss)	(220)	3,060	(295)	(463)	2,082
Equipment and furnishings expenditures	-	10	-	-	10
Intangible expenditures	-	-	-	-	-

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

In thousands of Canadian dollars

Three Months Ended February 28, 2009

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
Revenue	\$ 1,997	\$ 3,468	\$ 259	\$ -	\$ 5,724
Gross profit	1,141	584	(6)	-	1,719
Technology Partnerships Canada – net	96	-	-	-	96
Interest expense	1	16	-	14	31
Income tax expense (recovery)	-	(152)	-	5	(147)
Amortization	54	64	36	7	161
Net income (loss)	99	115	(283)	(628)	(697)
Equipment and furnishings expenditures	1	22	2	5	30
Intangible expenditures	-	2	-	-	2

In thousands of Canadian dollars

Total assets employed	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
As at February 28, 2010	\$ 4,587	\$ 8,691	\$ 1,740	\$ 1,661	\$ 16,679
As at November 30, 2009	\$ 4,636	\$ 8,448	\$ 2,439	\$ 236	\$ 15,759

Geographically, revenues reported are based on the location of the Company's customers as follows:

In thousands of Canadian dollars

Three months ended February 28,

	2010	2009
United States	\$ 2,191	\$ 3,526
Australia	254	1,213
United Kingdom	412	512
Netherlands	122	-
Canada	96	358
New Zealand	64	63
Other	305	52
Total	\$ 3,444	\$ 5,724

# OSI Geospatial Inc.

## Notes to the Interim Consolidated Financial Statements (Unaudited) Three Months Ended February 28, 2010 and 2009

Geographically, equipment and furnishings and intangible and other assets are reported based on location. At February 28, 2010 and November 30, 2009, all of the Company's equipment and furnishings and intangible and other assets were located in Canada and the U.S. as follows:

In thousands of Canadian dollars		February 28, 2010		
	Canada	U.S.	Total	
Equipment and furnishings	\$ 1,162	\$ 172	\$ 1,334	
Intangible and other assets	155	225	380	
Goodwill	-	4,305	4,305	
Total	<u>\$ 1,317</u>	<u>\$ 4,702</u>	<u>\$ 6,019</u>	

In thousands of Canadian dollars		November 30, 2009		
	Canada	U.S.	Total	
Equipment and furnishings	\$ 1,215	\$ 258	\$ 1,473	
Intangible and other assets	168	278	446	
Goodwill	-	4,324	4,324	
Total	<u>\$ 1,383</u>	<u>\$ 4,860</u>	<u>\$ 6,243</u>	

### 10 Contingency

In January 2010, a claim for breach of contract and wrongful dismissal was filed against the Company by a former employee of the Company. The Company believes the claim is without merit and the Company has filed a counterclaim for breach of fiduciary obligations as an officer of the Company and contractual obligations under the former employee's Employment Agreement. The final outcome with respect to this claim and counterclaim cannot be predicted with certainty and no amount has been accrued in the financial statements.

### 11 Sale of soldier systems intellectual property

On February 1, 2010, the Company's U.S. Systems Operations signed a contract valued at U.S. \$6.5 million with Harris Corporation ("Harris"). Under the terms of this contract, OSI Geospatial sold all of its rights to its soldier systems intellectual property and transferred its San Diego-based employees, office and associated equipment, furniture and fixtures to Harris. This intellectual property is a non-core asset that is not aligned with the Company's maritime strategy. The net proceeds after corporate income taxes were approximately U.S. \$5.5 million.

Pursuant to the terms of the contract with Harris, U.S. \$500,000 was held in escrow on behalf of the Company for the purposes of, among other things, funding the payment of any indemnification obligations of the Company. 50% of the escrow fund will be released on the first year anniversary of the closing date and the other 50% will be released upon the expiration of the escrow period in September 2011. The escrow fund is included in restricted cash in the interim consolidated balance sheet.