

## Management's Responsibility for Financial Reporting

The accompanying financial statements and related data are the responsibility of management.

Management is responsible for ensuring that the financial statements are prepared in accordance with accounting principles generally accepted in the United States.

The integrity of the financial process is also the responsibility of management. Management maintains systems of internal controls designed to provide reasonable assurance that transactions are authorized, assets are safeguarded, and reliable financial information is produced. Management selects accounting principles and methods that are appropriate to the Company's circumstances, and makes decisions affecting the measurement of transactions in which estimates or judgements are required to determine the amounts reported.

The Audit Committee has responsibility for reviewing the annual financial statements and external auditors' report and recommending the annual financial statements to the Board of Directors for approval.

The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting. The Board has responsibility for reviewing and approving the financial statements.

The external auditors audit the financial statements annually on behalf of the shareholders. The external auditors have free access to management and the Audit Committee.



Kenneth Kirkpatrick  
President and Chief Executive Officer  
March 6, 2006



John Sentjens  
Vice President Finance

## Auditors' Report

To the Shareholders of  
**Offshore Systems International Ltd.**

We have audited the consolidated balance sheets of **Offshore Systems International Ltd.** as at November 30, 2005 and 2004 and the consolidated statements of earnings (loss), stockholders' equity and accumulated deficit and cash flows for each of the years in the two-year period ended November 30, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Offshore Systems International Ltd. as at November 30, 2005 and 2004 and the results of its operations and its cash flows for each of the years in the two-year period ended November 30, 2005 in conformity with United States generally accepted accounting principles.



Chartered Accountants  
Vancouver, Canada  
February 17, 2006

# Consolidated Balance Sheets

(expressed in Canadian dollars)

November 30	2005	2004
<b>ASSETS</b> (note 11)		
<b>Current assets</b>		
Cash and cash equivalents	\$ 9,599,801	\$ 251,037
Restricted cash (note 4)	221,264	–
Accounts receivable (note 6)	11,002,470	9,140,478
Inventory (note 7)	1,094,634	649,427
Prepaid expenses and deposits	624,629	142,752
Deferred income taxes (note 16)	–	780,331
	<b>22,542,798</b>	10,964,025
<b>Plant and equipment</b> (note 8)	<b>1,015,057</b>	938,102
<b>Intangible and other assets</b> (note 9)	<b>732,912</b>	408,611
<b>Goodwill</b> (note 5)	<b>481,014</b>	–
	<b>\$ 24,771,781</b>	\$ 12,310,738
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 10)	\$ 3,919,534	\$ 2,596,362
Income taxes payable	284,833	–
Unearned revenue	530,321	79,865
	<b>4,734,688</b>	2,676,227
<b>Deferred income taxes</b> (note 16)	<b>230,806</b>	–
	<b>4,965,494</b>	2,676,227
<b>Commitments and contingencies</b> (note 14)		
<b>Capital stock</b>		
Authorized (note 12(a))		
Issued and outstanding		
30,262 Class A preference shares – Series A (2004 – 30,262) (note 12(c))	30,262	30,262
nil Class B preference shares – Series 1 (2004 – 57,711) (note 12(d)(i))	–	2,163,621
341,240 Class B preference shares – Series 2 (2004 – nil) (note 12(d)(ii))	11,412,208	–
30,367,309 common shares (2004 – 27,488,074) (note 12(b))	22,832,892	20,047,731
	<b>34,275,362</b>	22,241,614
<b>Warrants</b> (note 12 (e))	<b>5,207,234</b>	661,575
<b>Additional paid in capital</b>	<b>4,743,012</b>	928,169
<b>Accumulated deficit</b>	<b>(24,446,827)</b>	(14,196,847)
<b>Accumulated other comprehensive income</b>	<b>27,506</b>	–
	<b>19,806,287</b>	9,634,511
	<b>\$ 24,771,781</b>	\$ 12,310,738

Approved by the Board of Directors



Raymond Johnston  
Director



Helmut Lobmeier  
Director

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Earnings (Loss)

(expressed in Canadian dollars)

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
<b>Revenue</b>		
Systems and system components	\$ 5,665,590	\$ 4,328,740
Software	3,898,423	5,576,540
Geomatics	3,535,907	2,979,728
Other	327,520	566,295
	<b>13,427,440</b>	<b>13,451,303</b>
<b>Cost of sales</b>	<b>6,932,421</b>	<b>5,669,324</b>
<b>Gross profit</b>	<b>6,495,019</b>	<b>7,781,979</b>
<b>Expenses</b>		
General and administrative	4,763,190	3,330,119
Research and development	2,023,180	2,104,806
Sales and marketing	2,864,282	3,160,359
Depreciation and amortization	300,286	231,033
Interest expense	28,537	2,045
Interest income	(187,751)	(27,707)
Foreign exchange loss	122,310	38,338
Technology Partnerships Canada royalty (note 13)	298,289	124,425
Technology Partnerships Canada contribution (note 13)	(1,337,770)	(1,471,414)
	<b>8,874,553</b>	<b>7,492,004</b>
<b>Net earnings (loss) before income taxes</b>	<b>(2,379,534)</b>	<b>289,975</b>
<b>Income tax expense (recovery)</b> (note 16)		
Deferred income tax expense (recovery)	858,407	(479,446)
Current income tax expense (recovery)	173,253	521,404
	<b>1,031,660</b>	<b>41,958</b>
<b>Net earnings (loss)</b>	<b>\$ (3,411,194)</b>	<b>\$ 248,017</b>
<b>Net earnings loss attributable to common shareholders</b>	<b>\$ (10,249,981)</b>	<b>\$ (58,873)</b>
<b>Earnings (loss) per share</b> (note 12(g))		
Basic	\$ (0.37)	\$ 0.00
Diluted	\$ (0.37)	\$ (0.01)
<b>Weighted average number of common shares outstanding</b> (note 12(g))		
Basic	27,989,832	27,147,246
Diluted	27,989,832	29,856,412
<b>Dividends declared per share</b>		
Class B preference shares – Series 1	\$ 2.76	\$ 4.50
Class B preference shares – Series 2	\$ 4.02	\$ 0.00

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Stockholders' Equity and Accumulated Deficit

(expressed in Canadian dollars)

Years ended November 30	2005		2004	
<b>Class A preference shares</b>				
Balance at the beginning of the year	30,262	\$ 30,262	30,262	\$ 30,262
Balance at the end of the year	30,262	\$ 30,262	30,262	\$ 30,262
<b>Class B preference shares</b>				
Balance at the beginning of the year	57,711	\$ 2,163,621	61,244	\$ 2,169,127
Share issuance costs	-	-	-	(20,115)
Accretion of discount on Class B preference shares – Series 1	-	424,111	-	133,757
Repurchase of Class B preference shares – Series 1	(57,711)	(2,587,732)	-	-
Issue of Class B preference shares – Series 2 – net	390,000	12,503,857	-	-
Beneficial conversion feature on Class B preference shares – Series 2	-	(4,796,649)	-	-
Accretion of beneficial conversion feature on Class B preference shares – Series 2	-	4,796,649	-	-
Accretion of discount on Class B preference shares – Series 2	-	524,283	-	-
Class B preference shares converted	(48,760)	(1,615,932)	(3,533)	(119,148)
Balance at the end of the year	341,240	\$ 11,412,208	57,711	\$ 2,163,621
<b>Common shares</b>				
Balance at the beginning of the year	27,488,074	\$ 20,047,731	26,807,475	\$ 19,516,304
Class B preference shares converted	-	-	160,752	119,148
Class B preference shares – Series 2 converted	2,868,235	2,776,781	-	-
Exercise of stock options	11,000	8,380	519,847	412,279
Balance at the end of the year	30,367,309	\$ 22,832,892	27,488,074	\$ 20,047,731
<b>Warrants</b>				
Balance at the beginning of the year	1,393,301	\$ 661,575	1,393,301	\$ 661,575
Issue of warrants – net of issue costs	12,395,064	4,545,659	-	-
Balance at the end of the year	13,788,365	\$ 5,207,234	1,393,301	\$ 661,575
<b>Additional paid-in capital</b>				
Balance at the beginning of the year	-	\$ 928,169	-	\$ 903,803
Exercise of stock options	-	-	-	(13,800)
Stock-based compensation	-	286,683	-	38,166
Repurchase of Class B preference shares – Series 1	-	(668,785)	-	-
Beneficial conversion feature on Class B preference shares – Series 2	-	4,796,649	-	-
Class B preference shares – Series 2 converted	-	(599,704)	-	-
Balance at the end of the year	-	\$ 4,743,012	-	\$ 928,169
<b>Accumulated deficit</b>				
Balance at the beginning of the year	-	\$ (14,196,847)	-	\$ (14,046,108)
Accretion of discount on Class B preference shares – Series 1	-	(424,111)	-	(133,757)
Dividends on Class B preference shares	-	-	-	(264,999)
Repurchase of Class B preference shares – Series 1	-	370,967	-	-
Accretion of beneficial conversion feature on Class B preference shares – Series 2	-	(4,796,649)	-	-
Accretion of discount on Class B preference shares – Series 2	-	(524,283)	-	-
Class B preference Series 2 converted	-	(561,145)	-	-
Dividends on Class B preference shares – Series 1	-	(62,785)	-	-
Dividends on Class B preference shares – Series 2	-	(840,780)	-	-
Net earnings (loss) for the year	-	(3,411,194)	-	248,017
Balance at the end of the year	-	\$ (24,446,827)	-	\$ (14,196,847)
<b>Accumulated other comprehensive income</b>				
Balance at the beginning of the year	-	\$ -	-	\$ -
Foreign currency translation adjustment	-	27,506	-	-
Balance at the end of the year	-	\$ 27,506	-	\$ -
<b>Total stockholders' equity</b>	-	\$ 19,806,287	-	\$ 9,634,511

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Cash Flows

(expressed in Canadian dollars)

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
<b>Cash flows used in operating activities</b>		
Earnings (loss) for the year	\$ (3,411,194)	\$ 248,017
Items not affecting cash		
Depreciation and amortization	493,179	362,564
Loss on disposal of equipment	4,203	
Stock-based compensation	286,683	38,166
Deferred income taxes	846,495	42,192
	<b>(1,780,634)</b>	690,939
Changes in non-cash working capital items		
Accounts receivable	(1,293,518)	(4,518,642)
Inventory	(445,207)	16,076
Prepaid expenses and deposits	(481,877)	287,667
Accounts payable and accrued liabilities	1,271,525	383,735
Income taxes payable	158,293	–
Unearned revenue	423,581	33,958
Rent payable	–	(133,942)
Long term royalties	–	(187,384)
	<b>(367,203)</b>	(4,118,532)
	<b>(2,147,837)</b>	(3,427,593)
<b>Cash flows used in investing activities</b>		
Purchase of Mapcon Mapping Consultants Inc., net of cash acquired (note 5)	(1,236,624)	–
Increase in restricted cash	(221,264)	–
Additions to plant and equipment	(250,870)	(143,515)
Additions to intangibles and other assets	(68,717)	(215,341)
	<b>(1,777,475)</b>	(358,856)
<b>Cash flows from financing activities</b>		
Issue of common shares	8,380	398,479
Issue of Class B preference shares – Series 2 and warrants	19,500,195	–
Class B preference share issue costs	(2,450,679)	(20,115)
Class B preference shares dividends declared and paid	(903,566)	(178,433)
Share repurchases – Class B preference shares – Series 1	(2,885,550)	–
	<b>13,268,780</b>	199,931
Exchange impact on acquired cash balances	5,296	–
<b>Increase (decrease) in cash and cash equivalents</b>	<b>9,348,764</b>	(3,586,518)
<b>Cash and cash equivalents – beginning of year</b>	<b>251,037</b>	3,837,555
<b>Cash and cash equivalents – end of year</b>	<b>\$ 9,599,801</b>	<b>\$ 251,037</b>

See accompanying notes to the consolidated financial statements.  
Refer to note 19 for supplemental cash flow information.

# Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

## 1) Nature of Operations

Offshore Systems International Ltd. ("OSI") designs, develops, and markets software and systems for enhancing situational awareness in command, control, and intelligence applications. The Company's principal product is the proprietary ECPINS® line of electronic chart navigation systems for commercial and military customers. Collectively, OSI and its subsidiaries are referred to as the Company. OSI conducts its operations through three business units. The Company's Navigation Systems business unit develops and produces geographic information display systems and software. The Company's Applications business unit develops situational awareness products for command and control systems. The Company's Mapcon business unit (formally the Geomatics business unit) provides digital land map and electronic nautical chart production services, and produces and distributes electronic nautical chart data.

## 2) Accounting Changes

### a) Changes in accounting policies relating to the adoption of U.S. GAAP

Effective December 1, 2004, the Company elected to report its consolidated financial statements in conformity with U.S. GAAP. The Company continues to report all amounts in Canadian dollars. All accounting policies are the same as described in note 2 to the Company's audited financial statements for the year ended November 30, 2004, which were prepared in accordance with Canadian GAAP filed with the appropriate securities commissions except for the following which have been retroactively adopted to comply with U.S. GAAP:

#### *Stock-based compensation*

The Company grants stock options to employees, officers, directors, and persons providing management or consulting services to the Company pursuant to the stock option plans described in note 12(e). As allowed by Statement of Financial Accounting Standard 123 Accounting for Share-Based Payments, ("SFAS 123") as amended by Statement of Financial Accounting Standard 148, the Company follows the Accounting Principles Board Opinion 25, Accounting for Stock Issued to Employees, ("APB 25") and presents pro forma information required by SFAS 123. APB 25 requires compensation cost for stock-based employee compensation plans to be recognized over the vesting period based on the difference, if any, between the quoted market price of the Company's stock as of the grant date and the amount an employee must pay to acquire the stock.

For stock options granted to non-employees, the Company follows the requirements of SFAS 123 and related interpretations. Costs are measured at the estimated fair value of the consideration received or the estimated fair value of the stock options issued, whichever is more reliably measurable. The value of the stock options issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services.

#### *Beneficial conversion feature and accretion of discount on preference shares issued with attached warrants*

For U.S. GAAP purposes, during the fiscal year 2005, the Company recorded beneficial conversion features of \$4,796,649 on the issuance of Class B preference shares Series 2 (2003 – \$688,785 on the issuance of Class B preference shares Series 1), as a reduction to the net earnings available to common shareholders calculated on the effective conversion price of the preference shares to common shares based on the proceeds allocated to the preference shares. In both cases, the conversion feature of the preference shares vested immediately and the Company recorded the accretion of the full amount of the beneficial conversion feature. For both the Series 1 and Series 2 Class B preference shares, the discount on these shares that resulted from the allocation of the gross proceeds to the Class B preference shares and to the attached warrants is accreted over the five-year life of the warrants. This resulted in an accretion of \$524,283 for the Series 2 and \$424,111 for the Series 1 to accumulated deficit for the year ended November 30, 2005.

Under Canadian GAAP, there is not a requirement to record the beneficial conversion feature and accretion of discount when preference shares are issued with attached warrants.

#### *Derivative financial instruments*

Under Canadian GAAP, there is a requirement for derivatives outside of hedging relationships to be recognized on the balance sheet at fair market value; however for derivatives in hedging relationships, Canadian GAAP does not specify how such derivatives should be recorded. As a result, under Canadian GAAP, in some instances derivatives may not be recorded on the balance sheet. Under U.S. GAAP, it is required that all derivatives be recorded as assets or liabilities, measured at fair value. Derivatives that are not hedges are adjusted to fair value through income. If the derivative is a hedge, depending upon the nature of the hedge, changes in the fair value of the derivative are either offset against the fair value of assets, liabilities or firm commitments through income, or recognized in other comprehensive income until the hedged item is recognized in income. The ineffective portion of a derivative's change in fair value is immediately recognized into income.

# Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

## b) Recent pronouncements

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard 123R, Share-Based Payment, ("SFAS 123R") a revision to SFAS 123. SFAS 123R requires all share-based payments to be recognized in the financial statements based on their values using either a modified-prospective or modified-retrospective transition method. The standard no longer permits pro forma disclosure or prospective recognition. Accordingly, from the date of adoption, December 1, 2005, of the revised standard, the Company will be required to recognize compensation expense for all share-based payments based on grant-date fair value, including those granted, modified or settled prior to September 1, 2005, that were previously disclosed on a pro forma basis. The adoption of SFAS 123R will not have a material impact on the Company's consolidated financial statements.

In December 2004, the FASB issued SFAS No. 153, "Exchange of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions" ("SFAS No. 153"). The amendments made by SFAS No. 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for non-monetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 is to be applied prospectively and is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The adoption of SFAS 153 will not have a material impact on the Company's consolidated financial statements.

## 3) Summary of Significant Accounting Policies

### a) Principles of consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All material intercompany transactions and balances have been eliminated on consolidation.

### b) Foreign currency translation

The operations of the Company's U.S.-based subsidiary are considered integrated (financially and operationally dependent on OSI) and are translated to Canadian dollars using current rates of exchange for monetary assets and liabilities. Historical rates of exchange are used for non-monetary assets and liabilities and average rates for the period are used for revenues and expenses except for amortization, which is translated at exchange rates used in the translation of the related asset accounts. Gains or losses resulting from these translation adjustments are included in income.

Transactions completed in foreign currencies are recorded in Canadian dollars at the rates prevailing at the time of the transactions. Monetary assets and liabilities denominated in foreign currencies are recorded in the consolidated financial statements in equivalent Canadian dollars at the rate of exchange prevailing at the balance sheet date.

The Company purchases foreign exchange forward contracts to hedge sales to customers denominated in U.S. dollars, Australian dollars and euros and the related accounts receivable. Foreign exchange translation gains and losses on foreign currency denominated derivative financial instruments used to hedge anticipated U.S. dollar, Australian dollar, and euro denominated sales are recognized as an adjustment of the revenues when the sale is recorded. The Company does not utilize derivative financial instruments for trading or speculative purposes.

### c) Use of estimates

The preparation of financial statements in conformity with U.S. GAAP requires 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. Actual results could differ from these estimates.

### d) Cash and cash equivalents

Cash and cash equivalents consist of cash and deposit instruments with an initial maturity of three months or less.

### e) Accounts receivable

The Company maintains an allowance for doubtful accounts against its accounts receivable for estimated losses that may arise if any of its customers are unable to make required payments. Management specifically analyzes the age of outstanding customer balances, historical bad debts, customer credit-worthiness and changes in customer payment terms when making estimates of the uncollectability of the Company's accounts receivable. If the Company determines that the financial condition of any of its customers deteriorates, increases in the allowance may be made.

**f) Inventory**

Materials and components are stated at the lower of cost and replacement value as determined by the first-in first-out method. Work-in-process and manufactured parts are stated at the cost of materials and direct labour applied to the product and the applicable share of overhead. Finished goods are stated at the lower of cost and net realizable value. The Company assesses the need for inventory write-downs based on its assessment of estimated net realizable value using assumptions about future demand and market conditions. If market conditions differ from those originally estimated by the Company, an additional inventory write-down may be required.

**g) Plant and equipment**

Plant and equipment are recorded at cost. Amortization is provided using the methods indicated below and rates based on the assets' estimated useful lives as follows:

	<b>Method</b>	<b>Percentage</b>
Equipment	Declining balance	20 – 25
Vehicles	Declining balance	30
Furniture and fixtures	Declining balance	20
Leasehold improvements	Straight line	50

An impairment loss is recognized when the undiscounted cash flows expected from use and eventual disposition of the asset are less than the carrying amount of the asset. An impairment charge is recorded to reduce the carrying value of the asset to its fair value.

**h) Intangible and other assets**

Intangible and other assets are recorded at cost. Amortization is provided using the methods indicated below and rates based on the assets' estimated useful lives as follows:

	<b>Method</b>	<b>Percentage</b>
Computer software	Declining balance	33
Licenses and patents	Declining balance	10
Customer relationships	Straight line	10 – 25
Customer contract	Straight line	75

An impairment loss is recognized when the undiscounted cash flows expected from use and eventual disposition of the asset are less than the carrying amount of the asset. An impairment charge is recorded to reduce the carrying value of the asset to its fair value.

**i) Income taxes**

The Company accounts for income taxes using the liability method of tax allocation. Under the liability method, deferred income tax assets and liabilities are determined based on differences between their financial reporting and tax bases and are measured using enacted tax rates and laws expected to be in effect when the differences are expected to reverse. The Company provides a valuation allowance against deferred tax assets to the extent that the Company does not consider them to be more likely than not of being realized.

**j) Revenue recognition**

Revenue from certain projects in the Navigation Systems and Applications segments is recognized using the percentage of completion method of accounting, whereby revenue and profit in the period are based on the ratio of costs incurred to total estimated costs of the project for each segment of the project. Costs include all direct costs including material, labor, and subcontracting costs and certain indirect costs related to contracts. A provision is made for the entire amount of future estimated losses, if any, on contracts in progress.

Revenue from certain projects in the Mapcon segment is recognized using the proportional performance method of accounting, whereby revenue and profit in the period are based on the output completed to total units of work completed of the project for each segment of the project. A provision is made for the entire amount of future estimated losses, if any, on contracts in progress.

Certain other systems and system components revenue, software revenue for the Navigation Systems and Applications segments is recognized at the time of delivery of the system to the customer or the delivery of the software and software locks to the customer if persuasive evidence exists of an agreement with the customer, the price is fixed or determinable, collection is probable, and there are no ongoing obligations of the Company to provide future services with the exception of warranties and maintenance.

## Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

Revenue under bill-and-hold arrangements in the Navigation Systems segment, whereby revenue has been recognized but the goods have not been shipped, is recognized when risks of ownership have been passed on to the customer, there is a signed contract with the customer, the customer has a substantial business purpose for ordering the goods on a bill-and-hold basis, a fixed delivery schedule has been established with the customer, and the Company does not retain any specific performance obligations such that the earnings process is not complete. Goods held under such arrangements are segregated, ready for shipment and not subject to being used to fill other orders. The customers are charged additional fees for storage and other associated costs until shipment occurs.

Revenue from the sale of products by Mapcon is recorded at the time of delivery. Revenue from systems components and other revenues are recorded at the time of delivery or as the services are provided.

Revenue from contracts with multiple deliverables is recognized based on the division of the multiple deliverables into separate units of accounting and arrangement consideration is allocated among separate units based on their relative fair values. Revenue from each unit is recognized in accordance with the applicable policies as described above.

Maintenance and technical support revenues are recognized ratably based on the terms of the respective contract agreements, which is generally one to four years.

### **k) Unbilled revenue**

Unbilled revenue is revenue that has been recognized using the percentage of completion or the proportional performance methods of accounting less amounts billed to the customer in accordance with the milestone terms of the contract. Unbilled revenue is reduced when customers are invoiced and the respective accounts receivable is recorded.

### **l) Unearned revenue**

Unearned revenue is amounts that have been billed to the customer but have not been recognized in revenue.

### **m) Research and development**

Research costs are expensed in the period incurred. Development costs are expensed in the period incurred unless, in the opinion of management, the deferral criteria are satisfied in all material respects, in which case development expenditures are capitalized and amortized over the estimated life of the related products.

### **n) Government assistance**

Government assistance is recorded when there is reasonable assurance that the Company has complied with, and will continue to comply with, all conditions necessary to obtain the government assistance. Government assistance towards current research expenditures is recorded as a reduction of expenses in the consolidated statements of earnings (loss). The liability to repay government assistance is recognized as an expense in the period in which conditions arise that cause the government assistance to be repayable.

### **o) Stock-based compensation**

The Company accounts for stock-based compensation in accordance with the intrinsic value method of the Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees", and has adopted only the disclosure provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", to present the fair value of grants under the Company's existing stock-based compensation plans to employees. APB No. 25 requires compensation cost for stock-based employee compensation plans to be recognized over the vesting period based on the difference, if any, between the quoted market price of the Company's stock as of the grant date and the amount an employee must pay to acquire the stock. All options are granted with an exercise price equal to the market value of the stock on the date of grant. Accordingly, no compensation has been recognized for grants made under the stock option plan.

For stock options granted to non-employees, the Company follows the requirements of SFAS No. 123 and related interpretations. Costs are measured at the estimated fair value of the consideration received or the estimated fair value of the stock options issued, whichever is more reliably measurable. The value of the stock options issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services.

**p) Earnings per share**

Basic earnings per share are computed using the weighted average number of common shares outstanding during the year. The treasury stock method is used for the calculation of diluted earnings per share. Under the treasury stock method, the weighted average number of common shares outstanding for the calculation of diluted earnings per share assumes that the proceeds to be received on the exercise of dilutive stock options and warrants are applied to repurchase common shares at the average market price for the period. Stock options and warrants are dilutive when the average market price of the common shares during the period exceeds the exercise price of the stock options and warrants.

**q) Guarantees**

The Company guarantees that its 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. The Company accrues for known warranty issues if a loss is probable and can be reasonably estimated, and accrues for estimated incurred but unidentified warranty issues based on historical activity. To date, the Company has had no material warranty claims.

**r) Derivative financial instruments**

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

Foreign exchange translation gains and losses on 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, revenue or capital expenditures when the hedged transaction is recorded. Derivatives that are not subject to hedge accounting are recorded on the balance sheet with the changes in fair value being recorded in the statement of earnings each period. For the fiscal year 2005, all derivative financial instruments met the criteria for hedge accounting.

**s) Goodwill**

Acquisitions are accounted for using the purchase method whereby acquired assets and liabilities are recorded at fair value as of the date of acquisition. The excess of purchase price over such fair value is recorded as goodwill. The Company evaluated, on at least an annual basis, the carrying amounts of goodwill to determine whether events or circumstances indicate that such carrying amounts may no longer be recoverable. To accomplish this, the Company compares the fair value of the acquired reporting unit to the carrying amount. If the carrying value of the reporting unit were to exceed its fair value, the Company would perform the second step of the impairment test. In the second step, the Company would compare the fair value of the reporting unit goodwill to the carrying amount and any excess would be written down.

**4) Restricted Cash**

Restricted cash consists of cash pledged with a bank as collateral for bid bonds. The restricted cash is held in an interest-bearing bank account.

**5) Acquisition**

On April 8, 2005, the Company acquired all of the issued and outstanding shares of Mapcon Mapping Consultants Inc. ("Mapcon Mapping") of Salt Lake City, Utah for cash consideration of \$1,347,382 (US\$1,113,907). The acquisition was effective April 1, 2005. Mapcon Mapping is a privately held land mapping company in the U.S. digital and electronic geomatics data production market. The results of Mapcon Mapping's operations have been included in the consolidated financial statements commencing April 1, 2005.

## Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

The following table summarizes the fair value of the assets acquired and liabilities assumed by the Company at April 1, 2005, the date of acquisition. The acquisition was accounted for using the purchase method whereby assets acquired and liabilities assumed were recorded at their fair values at April 1, 2005. The excess of the purchase price over the fair market value was recorded as goodwill. The allocation of the purchase price is preliminary and the final allocation may be subject to refinement in the next four months. The purchase price is subject to certain adjustments related to working capital and the achievement of a minimum level of sales bookings against a specific contract.

<b>Assets</b>	
Current assets	\$ 819,568
Equipment	208,791
Deferred tax assets – current	185,247
Intangible assets	350,784
Goodwill	484,966
<b>Total assets acquired</b>	<b>\$ 2,049,356</b>
<b>Liabilities</b>	
Current liabilities not including deferred tax liabilities	198,166
Deferred tax liabilities – current	271,168
Deferred tax liabilities – long term	73,184
<b>Total liabilities assumed</b>	<b>\$ 542,518</b>
Net assets acquired (cash consideration)	\$ 1,347,382
Direct acquisition costs incurred by the Company	159,456
<b>Total acquisition costs</b>	<b>1,506,838</b>
Less fair value of net identifiable assets acquired	1,021,872
<b>Goodwill</b>	<b>\$ 484,966</b>
<b>Cash of acquired operations</b>	<b>\$ 270,214</b>

The fair values of the assets acquired, including goodwill, and liabilities assumed in the acquisition have been “pushed down” to Mapcon Mapping resulting in foreign currency revaluation at each reporting date.

The following table presents details of the purchased intangible assets:

	Estimated useful life	Amount
Customer contract	16 months	\$ 157,248
Customer relationships	4 to 10 years	193,536
<b>Total intangible assets</b>		<b>\$ 350,784</b>

The pro forma Offshore Systems International Ltd. consolidated operating results assuming the acquisition of Mapcon Mapping had occurred as of December 1, 2003, are as follows:

Years ended November 30	2005	2004
Revenue	\$ 13,988,950	\$ 14,548,698
Earnings (loss)	\$ (3,007,839)	\$ 397,632
Earnings (loss) per share – basic	\$ (0.35)	\$ 0.00
Earnings (loss) per share – diluted	\$ (0.35)	\$ 0.00

### 6) Accounts Receivable

November 30	2005	2004
Trade	\$ 7,265,224	\$ 4,679,207
Unbilled revenue	2,993,588	4,116,828
Technology Partnerships Canada contribution (note 13)	729,909	257,266
Other	56,072	111,234
Allowance for doubtful accounts	(42,323)	(24,057)
	<b>\$ 11,002,470</b>	<b>\$ 9,140,478</b>

As at November 30, 2005, government contract receivables were \$5,978,619 (2004 – \$4,435,616) and unbilled government contract receivables were \$2,259,275 (2004 – \$3,601,202).

**7) Inventory**

<i>November 30</i>	<b>2005</b>	<b>2004</b>
Materials and components	\$ 1,094,634	\$ 638,127
Finished goods	-	11,300
	<b>\$ 1,094,634</b>	<b>\$ 649,427</b>

**8) Plant and Equipment**

<i>November 30, 2005</i>	<b>Cost</b>	<b>Accumulated amortization</b>	<b>Net amount</b>
Equipment	\$ 4,174,286	\$ 3,235,158	\$ 939,128
Vehicle	10,771	1,240	9,531
Furniture and fixtures	139,946	106,993	32,953
Leasehold improvements	234,175	200,730	33,445
	<b>\$ 4,559,178</b>	<b>\$ 3,544,121</b>	<b>\$ 1,015,057</b>

<i>November 30, 2004</i>	<b>Cost</b>	<b>Accumulated amortization</b>	<b>Net amount</b>
Equipment	\$ 3,905,871	\$ 3,034,306	\$ 871,565
Furniture and fixtures	136,204	99,320	36,884
Leasehold improvements	222,737	193,084	29,653
	<b>\$ 4,264,812</b>	<b>\$ 3,326,710</b>	<b>\$ 938,102</b>

**9) Intangible and Other Assets**

<i>November 30, 2005</i>	<b>Cost</b>	<b>Accumulated amortization</b>	<b>Net amount</b>
Computer software	\$ 1,191,543	\$ 721,273	\$ 470,270
Customer contract	154,395	78,406	75,989
Customer relationships	189,598	19,335	170,263
Licenses and patents	57,267	40,877	16,390
	<b>\$ 1,592,803</b>	<b>\$ 859,891</b>	<b>\$ 732,912</b>

<i>November 30, 2004</i>	<b>Cost</b>	<b>Accumulated amortization</b>	<b>Net amount</b>
Computer software	\$ 936,591	\$ 546,190	\$ 390,401
Licenses and patents	57,267	39,057	18,210
	<b>\$ 993,858</b>	<b>\$ 585,247</b>	<b>\$ 408,611</b>

The estimated aggregate amortization expense for intangible assets for the next five years is as follows:

<i>Years ending November 30</i>	
2006	\$ 261,308
2007	133,942
2008	99,483
2009	65,771
2010	44,954
2011 and after	127,455

# Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

## 10) Accounts Payable and Accrued Liabilities

<i>November 30</i>	2005	2004
Trade	\$ 2,210,994	\$ 1,343,129
Accrued employee compensation	635,638	444,365
Accrued employee benefits and payroll deductions	398,319	128,224
Accrued royalties (note 13)	297,421	311,851
Other accrued liabilities	377,162	282,227
Class B preference shares dividends declared and unpaid	–	86,566
	<b>\$ 3,919,534</b>	<b>\$ 2,596,362</b>

## 11) Credit Facilities

In March 2005, the Company renewed certain credit facilities with a Canadian chartered bank, which consist of an operating line, a foreign exchange forward contract facility and standby letters of credit. The operating line bears interest at the chartered bank's prime lending rate plus 0.5% with interest payable monthly. The prime lending rate at November 30, 2005 was 4.75% (2004 – 4.25%). The standby letters of credit are denominated in U.S. dollars and bear interest at rates between 1% and 2% per annum. Funds drawn on the operating line and the standby letters of credit are repayable on demand. As of November 30, 2005, letters of credit, relating principally to customer contracts, amounting to Australian \$283,886 (2004 – \$283,886) have been issued. The Company utilizes letters of credit to back certain performance obligations with its customers.

The maximum amount(s) available to the Company under the operating line is \$2,000,000 and under the foreign exchange forward contract facility are US\$2,000,000 (2004 -US\$2,000,000) and Australian \$nil (2004 – Australian \$3,678,061). The credit facilities are collateralized by a general assignment of book debts, a general security agreement and general security agreements, from each of Offshore Systems Ltd., Mapcon Mapping Ltd., and Mapcon Mapping Inc. In addition, the Company is required to meet certain covenants as outlined in the credit facilities agreement. As at November 30, 2005, the Company had not drawn on its foreign exchange contract facility.

## 12) Capital Stock

### a) Authorized

100,000,000 Class A preference shares with no par value, issuable in series, of which:

10,000,000 shares are designated Series A voting non-cumulative, retractable, convertible at a ratio of 1:1, 1% preference shares

100,000,000 Class B preference shares with a par value of \$50 each, issuable in series, of which:

10,000,000 shares are designated Series 1 voting, cumulative, convertible shares at a ratio of 1:45.5, 6% preference shares, and

10,000,000 are designated Series 2 voting, cumulative, convertible shares at a ratio of 1:58.82, 7% preference shares

Unlimited Class C preference shares without par value, issuable in series

Unlimited common shares without par value

### b) Issued and outstanding common shares

	2005		2004	
	Number of common shares	Amount	Number of common shares	Amount
<b>Balance – beginning of year</b>	<b>27,488,074</b>	<b>\$ 20,047,731</b>	26,807,475	\$ 19,530,104
<b>Issued during the year:</b>				
Exercise of stock options	11,000	8,380	519,847	398,479
Class B preference shares Series 2 – converted	2,868,235	2,776,781	160,752	119,148
<b>Balance – end of year</b>	<b>30,367,309</b>	<b>\$ 22,832,892</b>	27,488,074	\$ 20,047,731

### c) Class A preference shares

The Company has 30,262 (November 30, 2004 – 30,262) Class A preference shares outstanding that have a nominal value for financial statement purposes. These Class A preference shares are being held in escrow but are no longer subject to any escrow restrictions and may be converted at any time into common shares of the Company, by notice in writing from the holders.

## d) Class B preference shares

	2005		2004	
	Number of Class B preference shares	Amount	Number of Class B preference shares	Amount
<b>Series 1</b>				
<b>Balance – beginning of year</b>	57,711	\$ 2,163,621	61,244	\$ 2,065,420
<b>Issued/redeemed during the year:</b>				
Share issue costs	–	–	–	(20,115)
Class B preference shares converted	–	–	(3,533)	(119,148)
Accretion of discount – Series 1	–	424,111	–	237,464
Repurchased	(57,711)	(2,587,732)	–	–
	–	\$ –	57,711	\$ 2,163,621
<b>Series 2</b>				
<b>Balance – beginning of year</b>	–	–	–	–
<b>Issued/redeemed during the year:</b>				
Issued	390,000	\$ 14,954,731	–	\$ –
Share issue costs	–	(2,450,874)	–	–
Accretion of discount – Series 2	–	524,283	–	–
Converted to common	(48,760)	(1,615,932)	–	–
	341,240	\$ 11,412,208	–	\$ –
<b>Balance Class B – end of year</b>	341,240	\$ 11,412,208	57,711	\$ 2,163,621

## (i) Series 1

The Company completed a private placement on February 13, 2003 consisting of 61,244 units for total gross proceeds of \$3,004,200. Each unit consists of one Class B Series 1 preference share and 22.75 common share purchase warrants exercisable at \$1.10. The preference shares are voting convertible shares at a ratio of 1:45.5 and have a cumulative dividend of 6% per annum. The Company has the right to redeem the preference shares after five years. The share purchase warrants are convertible to common shares at a ratio of 1:1 and expire five years after issue. The private placement incurred share issue costs of \$297,320.

The gross proceeds of \$3,004,200 were allocated between the preference shares and warrants based on their relative fair value at the date of issuance. The \$2,342,625 fair value of the preference shares has been estimated based on the fair value of the underlying common shares. The \$661,575 fair value of the warrants has been estimated using the Black-Scholes option pricing model. Assumptions used in the pricing model included: (i) risk free interest rate of 2.7%, (ii) expected volatility of 66%, (iii) an estimated life of five years and (iv) an expected dividend rate of 0%. During the fiscal year 2003, the Company has recorded a beneficial conversion feature of \$668,785 in dividends calculated on the effective conversion price of the preference shares to common shares based on the proceeds allocated to the preference shares. The conversion feature of the preference shares vested immediately and the Company recorded the accretion of the full amount of the beneficial conversion feature. The preference share discount that resulted from the allocation of the gross proceeds is accreted over the five-year life of the warrants.

On April 11, 2005, 57,711 Class B Series 1 preference shares were repurchased by the Company at their par value of \$50 per share for aggregate cash consideration of \$2,885,550. The unamortized discount in the amount of \$390,672 as of the repurchase date was amortized and accreted to the Class B Series 1 preference shares and the beneficial conversion feature of \$668,785 was deducted from additional paid in capital. The repurchase resulted in a decrease of \$370,967 to deficit. As a result of the repurchase of all remaining preference B Series 1 shares, the remaining un-accreted balance of the discount has been accreted to accumulated deficit in the amount of \$424,111 for fiscal 2005 (2004 – \$133,757). During fiscal 2004, 3,533 Class B Series 1 preference shares were converted into common shares.

## (ii) Series 2

On April 11, 2005, the Company completed a private placement consisting of 19,500 units for total gross proceeds of \$19,500,195. The issue price was \$1,000.01 per unit. Each unit consist of 20 voting Class B preference shares Series 2 ("Preference Shares") and 588 share purchase warrants ("Warrants"). The Preference Shares entitle the holders to receive a fixed preferential cumulative 7% dividend payable semi-annually. Each Preference Share is convertible at the option of the holder at any time into 58.8235 of the Company's common shares, calculated by dividing the issue price of \$50.00 for each Preference Share by the conversion price of \$0.85. Each Warrant entitles the holder to purchase one of the Company's common shares at the exercise price of \$0.85 for a period of five years. Fees for advisory, investment banking and legal and other professional services in connection with this private placement were paid in the amount of \$2,418,363 and 929,064 Warrants were issued to an investment bank and related party (note 15) in connection with the private placement. The fair value of the finder's fee Warrants was estimated to be \$0.47 per warrant, using the Black-Scholes option pricing model, and has been recognized as a share issue cost.

## Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

The gross proceeds of \$19,500,195 were allocated between the Preference Shares and Warrants based on their relative fair value at the date of issuance. The \$20,161,770 fair value of the Preference Shares has been estimated based on the fair value of the underlying common shares. The \$5,207,039 fair value of the Warrants has been estimated using the Black-Scholes option pricing model. Assumptions used in the pricing model included: (i) risk free interest rate of 2.88%, (ii) expected volatility of 59%, (iii) an estimated life of five years and (iv) an expected dividend rate of 0%. The Company has recorded a beneficial conversion feature of \$4,796,649 as a reduction to the net earnings available to common shareholders calculated on the effective conversion price of the Preference Shares to common shares based on the proceeds allocated to the Preference Shares. The conversion feature of the Preference Shares vested immediately and the Company recorded the accretion of the full amount of the beneficial conversion feature. The Preference Share discount that resulted from the allocation of the gross proceeds is accreted over the five-year life of the Warrants. This resulted in an accretion of \$524,283 to accumulated deficit for year ended November 30, 2005.

Each Preference Share entitles the holder to one vote either in person or by proxy at any general meeting of the shareholders of the Company. The Company has the right to require the shareholders of the preference shares to convert each such share into 58.8235 common shares if (i) at any time after 13 months following the issuance of the preference shares, the closing trade price of the Company's common shares exceeds \$2.13 for at least 20 consecutive trading days, or (ii) at any time, the Company completes a firm public underwritten offering of its common shares for more than \$40,000,000 at a price per common share greater than \$1.70. The Preference Shares are redeemable at the option of the Company at any time after the third anniversary of the issuance date for an amount equal to the original issuance price plus a premium of 20% of the original issue price. The Preference Shares are not subject to any right of redemption at the option of the holder.

During the fiscal year 2005, 48,760 Preference Shares were converted into 2,868,235 common shares with an aggregate fair market value of \$2,776,782. The Preference Shares were reduced by, \$1,615,932, the carrying value of the shares converted, and the beneficial conversion feature attributed to the converted shares resulted in a deduction of \$599,704 from additional paid in capital. The conversion resulted in an increase of \$561,145 to deficit.

### e) Warrants

	2005		2004	
	Number of warrants	Amount	Number of warrants	Amount
<b>Balance – beginning of year</b>	<b>1,393,301</b>	<b>\$ 661,575</b>	1,393,301	\$ 661,575
<b>Issued/redeemed during the year:</b>				
Issued	12,395,064	4,545,659	–	–
<b>Balance – end of year</b>	<b>13,788,365</b>	<b>\$ 5,207,234</b>	1,393,301	\$ 661,575

### f) Stock option plans

The Company has established three stock option plans under which stock options to purchase common shares may be granted to directors, officers and employees of the Company and to any other person or Company permitted by the applicable regulatory authorities to purchase unissued common shares. The number of common shares authorized for grant under the Company's stock option plans is 10,930,732, of which 4,364,494 are available for future granting. The exercise price of stock options granted pursuant to the plans may not be less than the market price of the common shares at the time of grant. The plans provide that stock options may be granted with vesting periods and expiry dates at the discretion of the board of directors. Stock options granted to directors and management vest over periods ranging from immediately to five years and options granted to employees vest one year after the date granted.

A summary of the status of the Company's stock option plans at November 30 is as follows:

	2005		2004	
	Number of shares	Weighted average exercise price	Number of shares	Weighted average exercise price
Outstanding – beginning of year	2,254,047	\$ 1.11	2,890,046	\$ 1.02
Granted	3,054,666	0.92	496,750	1.12
Exercised	(11,000)	0.76	(519,847)	0.42
Forfeited	(18,384)	0.93	(22,725)	0.74
Surrendered	(632,784)	1.02	-	0.00
Expired	(972,128)	1.14	(590,177)	1.06
<b>Outstanding – end of year</b>	<b>3,674,417</b>	<b>\$ 0.96</b>	2,254,047	\$ 1.11
<b>Exercisable – end of year</b>	<b>3,378,417</b>	<b>\$ 0.95</b>	2,108,047	\$ 1.10

A summary of the Company's stock options outstanding and exercisable at November 30, 2005 is as follows:

Range of exercise prices	Number outstanding at November 30, 2005	Options outstanding		Options exercisable	
		Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at November 30, 2005	Weighted average exercise price
\$0.75 – \$1.12	3,101,416	4.19 years	\$ 0.92	2,951,416	\$ 0.92
\$1.13 – \$1.41	573,001	1.26 years	1.14	427,001	1.15
\$0.75 – \$1.41	3,674,417	3.73 years	\$ 0.96	3,378,417	\$ 0.95

A summary of the Company's stock options outstanding and exercisable at November 30, 2004 is as follows:

Range of exercise prices	Number outstanding at November 30, 2004	Options outstanding		Options exercisable	
		Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at November 30, 2004	Weighted average exercise price
\$0.75 – \$1.12	1,026,047	1.08 years	\$ 1.01	1,026,047	\$ 1.01
\$1.13 – \$1.41	1,228,000	1.12 years	1.18	1,082,000	1.19
\$0.75 – \$1.41	2,254,047	1.10 years	\$ 1.11	2,108,047	\$ 1.10

#### Stock-based compensation

For the year ended November 30, 2005, the Company incurred non-cash stock-based compensation expense of \$286,683, related to 900,000 stock options granted to third parties (\$38,166 and 45,000 stock options for the year ended November 30, 2004). The expense was included in general and administrative costs and was recorded in additional paid-in capital.

The fair value of stock options was estimated using the Black-Scholes option pricing model using the following weighted average assumptions by grant year:

	2005	2004
Risk-free interest rate	2.87%	2.24%
Volatility	49%	58%
Estimated average option lives	3.2 years	3.0 years
Dividend yield	0.0%	0.0%

#### Pro forma Disclosure

The Company applies the intrinsic value method for employee stock options granted as prescribed in APB No. 25. Had compensation cost been determined using the fair value approach set forth in SFAS No. 123, the Company's earnings (loss) for the year and earnings (loss) per share would have been in accordance with the pro forma amounts indicated below:

Years ended November 30	2005	2004
Net earnings for the year – as reported	\$ (3,411,194)	\$ 248,017
Stock-based employee compensation expense	(1,014,117)	(133,276)
Pro forma net earnings (loss) for the year	\$ (4,425,311)	\$ 114,741
Pro forma net earnings (loss) attributable to common shareholders	\$ (11,264,098)	\$ (192,149)
Basic earnings (loss) per share – as reported	\$ (0.37)	\$ 0.00
Diluted earnings (loss) per share – as reported	\$ (0.37)	\$ (0.01)
Pro forma basic and diluted earnings (loss) per share	\$ (0.40)	\$ (0.01)

The fair value of stock options was estimated using the Black-Scholes option pricing model using the following weighted average assumptions by grant year:

	2005	2004
Risk-free interest rate	3.0%	2.2%
Volatility	54%	58%
Estimated average option lives	4.2 years	3.0 years
Dividend yield	0.0%	0.0%

## Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

### Shareholder rights plan

On April 18, 2001, the Board of Directors of the Company adopted a shareholder rights plan (the "Rights Plan"). The Rights Plan was approved by the Toronto Stock Exchange in accordance with its policies. On March 12, 2004, the Board of Directors carried a resolution regarding the continued existence of the Rights Plan, subject to receipt of shareholder approval, for an additional three year period. The continued existence of the Rights Plan was approved by the shareholders of the Company by ordinary resolution at the annual general meeting of the Company held on April 22, 2004.

The objectives of the Rights Plan are to ensure, to the extent possible, that all shareholders of the Company are treated equally and fairly in connection with any take-over offer for the Company. Take-over offers may not always result in shareholders receiving equal or fair treatment or full value for their investment. In addition, current Canadian securities legislation only requires a take-over offer to remain open for 21 days. The Board believes that this period may be insufficient for the shareholders to evaluate a bid, or for the Board to pursue alternatives that could maximize shareholder value and to make informed recommendations to shareholders.

The Rights Plan is designed to discourage discriminatory or unfair take-over offers for the Company and gives the board time, if appropriate, to pursue alternatives to maximize shareholder value in the event of an unsolicited take-over bid for the Company. The Rights Plan will encourage an offeror to proceed by way of a permitted bid or to approach the Board of Directors with a view to negotiation by creating the potential for substantial dilution of the offeror's position. The permitted bid provisions of the Rights Plan are designed to ensure that, in any take-over bid, all shareholders are treated equally, receive the maximum value for their investment and are given adequate time to properly assess the take-over bid on a fully informed basis.

### g) Earnings per share

Years ended November 30	2005	2004
<b>Basic earnings (loss) per share</b>		
Net earnings (loss)	\$ (3,411,194)	\$ 248,017
Less: Accretion of discount on Class B preference shares Series 1	(424,111)	(133,757)
Accretion of beneficial conversion feature on Class B preference shares Series 2	(4,796,649)	–
Accretion of discount on Class B preference shares Series 2	(524,283)	–
Class B preference share dividends Series 1	(62,785)	(173,133)
Class B preference share dividends Series 2	(840,780)	–
Excess of conversion consideration over carrying value of Class B preference shares Series 2 and beneficial conversion feature.	(561,146)	–
Add: Excess of carrying value of Class B preference shares Series 1 and beneficial conversion feature over repurchase consideration paid.	370,967	–
<b>Loss available to common shareholders</b>	<b>\$ (10,249,981)</b>	<b>\$ (58,392)</b>
Weighted average number of common shares outstanding	27,989,832	27,147,246
<b>Basic earnings (loss) per share</b>	<b>\$ (0.37)</b>	<b>\$ (0.00)</b>

Years ended November 30	2005	2004
<b>Diluted earnings (loss) per share</b>		
Net earnings (loss)	\$ (3,411,194)	\$ 248,017
Less: Accretion of discount on Class B preference shares Series 1	(424,111)	(565,078)
Accretion of beneficial conversion feature on Class B preference shares Series 2	(4,796,649)	–
Accretion of discount on Class B preference shares Series 2	(524,283)	–
Class B preference share dividends Series 1	(62,785)	–
Class B preference share dividends Series 2	(840,780)	–
Excess of conversion consideration over carrying value of Class B preference shares Series 2 and beneficial conversion feature.	(561,146)	–
Add: Excess of carrying value of Class B preference shares Series 1 and beneficial conversion feature over repurchase consideration paid.	370,967	–
<b>Loss available to common shareholders</b>	<b>\$ (10,249,981)</b>	<b>\$ (317,061)</b>
Weighted average number of common shares outstanding	27,989,832	27,230,561
Dilutive effect of Class A preference shares – Series A <sup>(1)</sup>	–	–
Dilutive effect of Class B preference shares – Series 1	–	2,625,851
Dilutive effect of Class B preference shares – Series 2 <sup>(2)</sup>	–	–
Dilutive effect of warrants <sup>(1)</sup>	–	–
Dilutive effect of stock options <sup>(1)</sup>	–	–
<b>Adjusted weighted average number of common shares outstanding</b>	<b>27,989,832</b>	<b>29,856,412</b>
<b>Diluted loss per share</b>	<b>\$ (0.37)</b>	<b>\$ (0.01)</b>

(1) The Class A preference shares – Series A, the outstanding warrants and stock options were anti-dilutive for the purposes of calculating diluted earnings per share for the years ended November 30, 2005 and 2004.

(2) The Class B preference shares – Series 2 were anti-dilutive for the purposes of calculating diluted earnings per share for the year ended November 30, 2005.

#### h) Normal course issuer bid

In January 2003, the Company received approval for a normal course issuer bid that entitles the Company to repurchase up to 1,300,000 common shares for cancellation between January 16, 2003 and January 15, 2004. The purchases are made on the open market. During the period January 16, 2003 to November 30, 2003 the Company purchased 455,000 of its common shares on the open market under the normal course issuer bid at an average cost of \$1.11 per share for an aggregate consideration of \$505,681. The premium on the purchase and cancellation of the common shares under the normal course issuer bid was \$187,181 and was charged to the deficit. No common shares were purchased under the normal course issuer bid during the period December 1, 2003 to January 15, 2004.

#### 13) Technology Partnerships Canada

On April 26, 2004, the Company entered into an agreement with Technology Partnerships Canada ("TPC") whereby TPC granted financial assistance to the Company for the purpose of funding research and development activities to be completed on or before March 31, 2007. The maximum eligible contribution by TPC is \$3,768,391. For the year ended November 30, 2005, the Company has claimed for \$1,466,054 of assistance under the agreement (2004 – \$1,471,414). Accounts receivable at November 30, 2005 includes \$729,909 of amounts receivable from TPC in connection with these claims (2004 – \$257,266).

In addition, the Company is required to pay a royalty of 1.4% on annual gross revenue in the Navigation Systems and Applications segment for the period January 1, 2006 to December 31, 2008 and a royalty of 2.5% on annual gross revenue in the Navigation Systems and Applications segment for the period January 1, 2009 to December 31, 2013. Royalty payments will continue until the cumulative royalties paid or payable to December 31, 2013 are at least \$6,079,176 or until December 31, 2017. No amounts for royalty payments in connection with this agreement have been recorded in the financial statements.

On November 15, 1999, the Company entered into an agreement with TPC whereby TPC granted financial assistance to the Company for the purpose of funding research and development activities to be completed on or before March 31, 2003. Under the agreement with TPC, the Company was eligible to receive contributions to a maximum of \$4,000,177 over the period from December 23, 1998 to March 31, 2003. As of March 31, 2003, the Company has received the maximum allowed under the agreement. There are no amounts recorded in accounts receivable with respect to these claims (2004 – nil).

In addition, the Company is required to pay a royalty of 3% on annual gross revenue in the Navigation Systems and Applications segment for the period December 1, 1999 to November 30, 2008. The Company has paid royalties of \$1,241,154 to date (2004 – \$929,303) and has accrued royalties of \$297,421 at November 30, 2005 (November 30, 2004 – \$311,851). Royalty payments will continue until the cumulative royalties paid or payable to November 30, 2008 are at least \$7,810,230 or until November 30, 2014.

Although the Company believes that its submissions for TPC funding meet the terms and conditions of the TPC agreements, the final determination may be subject to audit by government authorities in the ordinary course of business.

During the year ended November 30, 2005, the Company was subject to a three audits by government authorities. The results of the cost audit did not have a financial impact on the Company's results. The results of the compliance audit required a repayment of contributions received of \$128,284 recognized in the current fiscal year as a reduction in TPC contributions. The royalty audit is currently in process. The Company has no reason to believe that the audit will have a material impact on the Company's financial results.

TPC royalties paid and accrued are as follows:

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
Royalties paid	\$ 311,851	\$ 183,392
Accrued royalties – current	\$ 297,421	\$ 311,851

If the Company causes an event of default, as defined in the agreement, TPC can suspend or terminate any obligation to contribute to the costs of the project or require the Company to repay all or part of the contributions made, together with interest, from the date of demand.

# Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

## 14) Commitments and Contingencies

The Company has entered into operating leases for its office premises in Canada and for certain equipment. Minimum lease payments required under the remaining terms of the leases are as follows:

<i>Years ending November 30</i>		
2006	\$	324,426
2007		232,431
2008		56,896
2009		52,498
2010		18,470
	\$	684,723

For the fiscal year ended November 30, 2005, the Company paid basic rent of \$256,705 (2004 – \$256,705). In addition to basic rent, the Company is required to pay a portion of certain costs and property taxes for the above commitments. In 2005, the Company paid \$120,365 (2004 – \$90,229) for these costs.

In July 2002, two of the Company's subsidiaries, Offshore Systems Ltd. and OSI Geomatics Ltd., and four employees became subject to a lawsuit for an undisclosed amount by Triathlon Ltd., a subsidiary of MacDonald, Dettwiler and Associates Ltd., related to use of confidential information and breach of fiduciary duty. No amount has been accrued at November 30, 2005 in respect of these claims because the potential liability for the claims and the amount of damages, if any, cannot be reasonably estimated.

## 15) Related Party Transactions

On April 11, 2005, Brinton Coxe, a director of the Company, assisted the Company in structuring and arranging the private placement financing (note 12(d)(ii)). In consideration for his services, the Company paid him compensation of \$815,908 and 350,000 common share purchase warrants. Mr. Coxe has also participated in the financing by purchasing 100 units personally. Mr. Coxe was paid an additional \$145,940 for professional services provided during the year and to be provided to April 2006. For the year ended November 30, 2005, \$116,447 was charged to expenses.

On April 8, 2005, Gerald Shields, a related party by virtue of the provision of legal services to the Company by two laws firm in which he has an interest (Mr. Shields having moved from his former firm to his current firm in July, 2005) was elected to the Company's Board of Directors. Fees paid to these two law firms for services Mr. Shields provided to the Company during the fiscal year 2005 totalled \$199,196.

## 16) Income Taxes

The Company is subject to Canadian federal and British Columbia provincial taxes in Canada. The Company is also subject to federal income taxes in the U.S and state taxes in Utah.

Earnings before income taxes consisted of the following:

<i>Years ended November 30</i>	2005	2004
Canadian income (loss)	\$ (2,758,720)	\$ 10,709
U.S. income	379,186	145,990
	\$ (2,379,534)	\$ 156,699

Income tax expense consisted of the following:

<i>Years ended November 30</i>	2005	2004
Canadian income tax expense	\$ 861,413	\$ –
U.S. income tax expense	170,247	41,958
	\$ 1,031,660	\$ 41,958

The Company has non-capital losses for Canadian income tax purposes of approximately \$5,084,445, which are available for carry forward to reduce future years' taxable income. These income tax losses expire as follows:

*Years ending November 30*

2006	\$	2,345,461
2007		–
2008		–
2009		169,005
2010		–
2011		–
2012		–
2013		–
2014		475,348
2015		2,094,631

The Company also has investment tax credits for Canadian income tax purposes of approximately \$1,088,090, which can be used to offset future income taxes otherwise payable and expire as follows:

*Years ending November 30*

2006	\$	130,114
2007		–
2008		–
2009		–
2010		–
2011		146,453
2012		191,931
2013		199,522
2014		191,801
2015		228,269

The Company has capital losses for Canadian income tax purposes of approximately \$354,466, which are available for carry forward to reduce future years' income from capital gains. These capital losses carry forward indefinitely.

The Company has un-deducted scientific research and experimental development expenses for Canadian income tax purposes of approximately \$5,225,417, which are available for carry forward to reduce future years' income for tax purposes. These expenses carry forward indefinitely.

The net deferred tax asset consists of the following:

<i>November 30</i>	2005	2004
<b>Deferred tax assets</b>		
Non-capital loss carry-forwards and net operating losses	\$ 1,734,812	\$ 1,191,426
Net capital loss carry-forwards	60,472	63,130
Scientific research and experimental development costs	1,782,912	1,701,004
Investment tax credits	837,487	680,793
Plant and equipment	982,312	895,457
Other	667,435	91,420
	6,065,430	4,623,230
Valuation allowance	(6,065,430)	(3,842,899)
<b>Deferred tax asset</b>	\$ –	\$ 780,331

The net deferred tax liabilities consists of the following:

<i>November 30</i>	2005	2004
<b>Deferred tax liabilities</b>		
Change in tax accounting method	\$ 97,093	\$ –
Intangible assets	91,502	–
Plant and equipment	50,211	–
<b>Deferred tax liabilities</b>	\$ 238,806	\$ –

## Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

The Company increased its valuation allowance against deferred income tax assets to reflect the amount of the future tax benefit that was more likely than not to be realized. A valuation allowance continues to be provided against deferred income tax assets for which the more likely than not criteria of future realization has not been met. Although the Company believes that its tax estimates are reasonable, the ultimate tax determination involves significant judgment that could become subject to audit by tax authorities in the ordinary course of business.

A reconciliation of the combined Canadian federal and provincial income tax rate with the Company's effective income tax rate is as follows:

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
Expected statutory rate	<b>35.00%</b>	35.79%
Expected provision for income taxes	<b>\$ (832,718)</b>	\$ 103,782
Change in tax rates applied in valuation allowance	<b>151,049</b>	1,199
Change in valuation allowance	<b>2,222,531</b>	84,827
Foreign tax differentials	<b>(3,014)</b>	(8,453)
Temporary differences related to share issues costs and other items arising during the year not included in accounting income	<b>(767,981)</b>	(189,402)
Part VI.1 Tax	<b>101,693</b>	–
Non-deductible expenses and other	<b>160,100</b>	50,005
Income tax expense	<b>\$ 1,031,660</b>	\$ 41,958

### 17) Segmented Information

The Company's reportable segments are as outlined below. Accounting policies used by these segments are the same as those described in the significant accounting policies as disclosed in note 3. The Company defines reportable segments as components of the Company about which separate financial information is available and which is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

<i>Year ended November 30, 2005</i>	<b>Navigation Systems</b>	<b>Applications</b>	<b>Mapcon</b>	<b>Total</b>
Revenue	<b>\$ 9,508,060</b>	<b>\$ 369,347</b>	<b>\$ 3,550,033</b>	<b>\$ 13,427,440</b>
Gross profit	<b>4,923,550</b>	<b>357,290</b>	<b>1,214,179</b>	<b>6,495,019</b>
Technology Partnerships Canada – net	<b>(1,039,481)</b>	<b>–</b>	<b>–</b>	<b>(1,039,481)</b>
Interest expense	<b>25,882</b>	<b>–</b>	<b>2,655</b>	<b>28,537</b>
Income tax expense	<b>405,331</b>	<b>455,224</b>	<b>171,105</b>	<b>1,031,660</b>
Net earnings (loss)	<b>(1,068,596)</b>	<b>(1,200,131)</b>	<b>(1,142,467)</b>	<b>(3,411,194)</b>
Plant and equipment expenditures	<b>198,950</b>	<b>–</b>	<b>51,920</b>	<b>250,870</b>
Intangibles and other asset expenditures	<b>26,634</b>	<b>1,214</b>	<b>40,869</b>	<b>68,717</b>
Depreciation and amortization	<b>222,368</b>	<b>4,298</b>	<b>266,513</b>	<b>493,179</b>

<i>Year ended November 30, 2004</i>	<b>Navigation Systems</b>	<b>Applications</b>	<b>Mapcon</b>	<b>Total</b>
Revenue	<b>\$ 10,232,671</b>	<b>\$ 191,279</b>	<b>\$ 3,027,353</b>	<b>\$ 13,451,303</b>
Gross profit	<b>6,561,870</b>	<b>171,518</b>	<b>1,048,591</b>	<b>7,781,979</b>
Technology Partnerships Canada – net	<b>(1,184,932)</b>	<b>(162,057)</b>	<b>–</b>	<b>(1,346,989)</b>
Interest expense	<b>1,902</b>	<b>–</b>	<b>143</b>	<b>2,045</b>
Income tax expense	<b>22,760</b>	<b>–</b>	<b>19,198</b>	<b>41,958</b>
Net earnings (loss)	<b>1,239,069</b>	<b>(972,476)</b>	<b>(18,576)</b>	<b>248,017</b>
Plant and equipment expenditures	<b>106,954</b>	<b>16,140</b>	<b>20,421</b>	<b>143,515</b>
Intangibles and other asset expenditures	<b>30,516</b>	<b>3,995</b>	<b>180,830</b>	<b>215,341</b>
Depreciation and amortization	<b>233,128</b>	<b>2,778</b>	<b>126,658</b>	<b>362,564</b>

Total assets employed:

<i>November 30</i>	<b>Navigation Systems</b>	<b>Applications</b>	<b>Mapcon</b>	<b>Total</b>
2005	\$ 20,502,483	\$ 102,669	\$ 4,166,629	\$ 24,771,781
2004	10,562,064	17,357	1,731,317	12,310,738

The Applications business unit began operations effective fiscal year 2004.

Segment revenues by category for the year ended November 30, 2005 are as follows:

	<b>Navigation Systems</b>	<b>Applications</b>	<b>Mapcon</b>	<b>Total</b>
Systems and system components	5,665,590	-	\$ -	\$ 5,665,590
Software	3,529,076	369,347	-	3,898,423
Geomatics	-	-	3,535,907	3,535,907
Other	313,394	-	14,126	327,520
<b>Total</b>	<b>\$ 9,508,060</b>	<b>\$ 369,347</b>	<b>\$ 3,550,033</b>	<b>\$ 13,427,440</b>

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

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
Europe	\$ 4,939,931	\$ 4,332,392
United States	2,907,793	2,872,860
Canada	2,914,744	1,427,288
Australia/New Zealand	2,593,635	4,818,763
Other	71,337	-
<b>Total</b>	<b>\$ 13,427,440</b>	<b>\$ 13,451,303</b>

Approximately 40% of revenue for the year ended November 30, 2005 (2004 – 58%) is derived from the three largest customers at 22%, 10% and 8%, respectively (2004 – 26%, 24%, 8%).

The three largest customers for 2005 were the Royal Navy of the United Kingdom, Royal Australian Navy and the Canadian Navy. The three largest customers for 2004 were the Royal Australian Navy, the Royal Navy of the United Kingdom and the U.S. Coast Guard.

Geographically, plant and equipment are reported based on location.

<i>November 30</i>	<b>2005</b>	<b>2004</b>
Canada	\$ 954,418	\$ 938,102
United States	60,639	-
	<b>\$ 1,015,057</b>	<b>\$ 938,102</b>

## 18) Financial Instruments

### Fluctuations in foreign currency exchange rates

The Company enters into transactions denominated in U.S. dollars, Australian dollars and euros and as such its revenue, expenses, monetary assets and liabilities will be affected by fluctuations in the various currencies relative to its functional currency, the Canadian dollar.

The Company uses foreign exchange forward contracts to hedge transactions denominated in US dollars, Australian dollars and euros. The purpose of the Company's hedging activities is to reduce the level of exposure to exchange rate movements. At November 30, 2005, the Company had foreign exchange forward contracts maturing in the following year to sell US\$nil (2004 – US\$851,196), Australian \$nil (2004 – Australian \$3,678,061), and €nil (2004 – €383,310).

The fair value of derivative instruments generally reflects the estimated amounts that the Company would receive or pay to settle the contracts at November 30, 2005. The fair value of the above derivative financial instruments was an unrecorded liability of \$nil at November 30, 2005 (2004 – \$42,303).

# Notes to the Consolidated Financial Statements

November 30, 2005 and 2004 (expressed in Canadian dollars)

## 19) Supplemental Cash Flow Information

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
Cash paid during the year for interest	\$ 28,453	\$ 2,045
Cash paid during the year for income taxes	\$ 5,751	\$ 12,916

## 20) Reconciliation of Generally Accepted Accounting Principles

The Company prepares its unaudited interim consolidated financial statements in accordance with U.S. generally accepted accounting principles which, as applied in these unaudited interim consolidated financial statements, conform in all material respects to Canadian GAAP, except for the differences below as follows:

- (a) Under Canadian GAAP, for stock option awards granted by the Company after December 1, 2003, the Company is required to recognize compensation when stock options are granted to employees and directors under stock option plans with no cash settlement feature based on the fair value method. As permitted by the standard, the Company had applied this change prospectively for new awards granted on or after December 1, 2003. Under U.S. GAAP, the Company accounts for stock based compensation to employees and directors in accordance with the intrinsic value method of the Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees."
- (b) Under Canadian GAAP, there is not a requirement to record the beneficial conversion feature and accretion of discount when preference shares are issued with attached warrants. For U.S. GAAP purposes, during the fiscal years 2003 and 2005 the Company recorded beneficial conversion features of \$668,785 and \$4,796,649, respectively on the issuance of Class B preference shares Series 1 and 2, respectively as a reduction to the net earnings available to common shareholders calculated on the effective conversion price of the preference shares to common shares based on the proceeds allocated to the preference shares. In both cases, the conversion feature of the preference shares vested immediately and the Company recorded the accretion of the full amount of the beneficial conversion feature. For both the Series 1 and Series 2 Class B preference shares, the discount on these shares that resulted from the allocation of the gross proceeds to the Class B preference shares and to the attached warrants is accreted over the five-year life of the warrants. This resulted in an accretion of \$424,111 and \$524,283, respectively to deficit for the year ended November 30, 2005.
- (c) Under Canadian GAAP, there is a requirement for derivatives outside of hedging relationships to be recognized on the balance sheet at fair market value, however for derivatives in hedging relationships, Canadian GAAP does not specify how such derivatives should be recorded. As a result, under Canadian GAAP in some instances derivatives may not be recorded on the balance sheet. Under U.S. GAAP it is required that all derivatives be recorded as assets or liabilities, measured at fair value. Derivatives that are not hedges are adjusted to fair value through income. If the derivative is a hedge, depending upon the nature of the hedge, changes in the fair value of the derivative are either offset against the fair value of assets, liabilities or firm commitments through income, or recognized in other comprehensive income until the hedged item is recognized in income. The ineffective portion of a derivative's change in fair value is immediately recognized into income. With respect to the ineffective portion of derivative's changes in fair value, the Company did not have a foreign exchange gain or loss amounts for the year ended November 30, 2005, under U.S. GAAP which has not been recorded under Canadian GAAP.
- (d) Under Canadian GAAP, the Company was not required to record stock-based compensation for stock options granted to third parties prior to December 1, 2001. Under U.S. GAAP, the Company is required to record stock-based compensation for stock options granted to third parties based on the fair value method as required by SFAS 123 retroactive for all prior periods. As a result, these stock-based compensation transactions result in differences when compared to the same balances as previously reported under Canadian GAAP.
- (e) For Canadian GAAP financial statement purposes, the Company's 30,262 (November 30, 2004 – 30,262) Class A preference shares have been presented at a nominal value. For U.S. GAAP financial statement purposes, these shares have been presented at a value of \$30,362.
- (f) For Canadian GAAP financial statement purposes, the Company has recorded a cumulative translation adjustment of \$11,975 which is a separate component of shareholders' equity. For U.S. GAAP purposes changes in the cumulative translation adjustment are included as a component of accumulated other comprehensive income.

(g) If Canadian GAAP were followed:

i) the effect on the Consolidated Statements of Earnings would be:

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
Earnings (loss) for the period, U.S. GAAP	\$ (3,411,194)	\$ 248,017
Adjustment for stock-based compensation (a),(d)	(1,014,117)	(133,276)
Adjustment for loss on derivative (c)	-	-
Earnings (loss) for the period, Canadian GAAP	\$ (4,425,311)	\$ 114,741
Basic earnings (loss) per common share, Canadian GAAP	\$ (0.16)	\$ 0.00
Diluted earnings (loss) per common share, Canadian GAAP	\$ (0.16)	\$ 0.00
Weighted average number of common shares – basic, Canadian GAAP	27,989,832	27,230,561
Weighted average number of common shares – diluted, Canadian GAAP	27,989,832	29,856,412

ii) Balance Sheet items which would differ under Canadian GAAP are as follows:

<i>November 30</i>	<b>2005</b>	<b>2004</b>
Common shares (d)	\$ 21,811,286	\$ 19,026,125
Class A preference shares – Series A (e)	-	-
Class B preference shares – Series 1 (b)	-	1,926,157
Class B preference shares – Series 2 (b)	10,912,177	-
Warrants (b)	5,207,039	661,575
Additional paid in capital (a), (d)	299,929	214,492
Accumulated deficit (a), (b), (c), (d)	(18,481,837)	(12,193,838)
Cumulative translation adjustment (f)	27,506	-

(h) Pro forma information – Stock based compensation

The following pro forma financial information as required by The Canadian Institute of Chartered Accountants (“CICA”) Handbook section 3870, Stock-based Compensation and Other Stock-based Payments, presents the earnings had the Company recognized stock-based compensation using a fair value method for all stock awards granted, modified or settled prior to December 1, 2003:

<i>Years ended November 30</i>	<b>2005</b>	<b>2004</b>
Earnings (loss) for the period, Canadian GAAP	\$ (4,425,311)	\$ 114,741
Add: Stock-based compensation cost	1,300,800	171,442
Less: Pro forma stock-based compensation cost	(1,319,700)	(196,642)
Pro forma income (loss)	\$ (4,444,211)	\$ 89,541
Pro forma basic earnings (loss) per share	\$ (0.16)	\$ 0.00
Pro forma diluted earnings (loss) per share	\$ (0.16)	\$ 0.00
Weighted average number of common shares – basic	27,989,832	27,230,561
Weighted average number of common shares – diluted	27,989,832	29,856,412

The fair value of the stock options was estimated using the Black-Scholes option pricing model using the following weighted average assumptions by grant year:

	<b>2005</b>	<b>2004</b>
Risk-free interest rate	3.0%	2.2%
Volatility	54%	58%
Estimated average option lives	4.2 years	3.0 years
Dividend yield	0.0%	0.0%

## Notes to the Consolidated Financial Statements

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### 21) Other Information

The following presents the conversion of the Company's comparative financial information from Canadian GAAP to U.S. GAAP and presents a comparison for amounts which differ between Canadian GAAP and U.S. GAAP:

#### a) Balance sheet at November 30, 2004:

	As previously reported under Canadian GAAP	As currently reported under US GAAP
<b>Shareholders' equity</b>		
<b>Capital stock</b>		
Issued and outstanding		
30,262 Class A preference shares – Series A	\$ –	\$ 30,262
57,711 Class B preference shares – Series 1	1,926,157	2,163,621
27,488,074 common shares	19,026,125	20,047,731
	\$ 20,952,282	\$ 22,241,614
<b>Additional paid in capital</b>	\$ 214,492	\$ 928,169
<b>Accumulated deficit</b>	\$ (12,193,838)	\$ (14,196,847)

#### b) Statement of earnings and accumulated deficit for the year ended November 30, 2004

	As previously reported under Canadian GAAP	As currently reported under U.S. GAAP
<b>Accumulated deficit – beginning of year</b>	\$ (12,043,580)	\$ (14,046,108)
<b>Class B preference share dividend paid</b>	\$ (264,999)	\$ (264,999)
<b>Class B preference share dividend accreted</b>	\$ –	\$ (133,757)
<b>Accumulated deficit – end of year</b>	\$ (12,193,838)	\$ (14,196,847)

### 22) Subsequent Events

On December 14, 2005, the Company acquired CHI Systems Inc., a United States defense contracting company. CHI Systems has multiple offices in the United States and is a supplier of technology and services to the U.S. Department of Defense and key defense prime contractors. Under the terms of the agreement, the Company paid approximately \$10,250,162 (approximately US\$9,000,000) for 100% of the outstanding shares of CHI Systems, of which approximately \$9,385,000 (approximately US\$8,101,780) was paid in cash with the balance paid by the issuance of 1,067,975 common shares of the Company.