



Offshore Systems International Ltd.

Interim Consolidated Financial Statements (Unaudited)
(Prepared in accordance with United States Generally
Accepted Accounting Principles)

February 28, 2006 and 2005

(expressed in Canadian dollars)

Offshore Systems International Ltd.

U.S. GAAP

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

Consolidated Balance Sheets (unaudited)

(expressed in Canadian dollars)

	February 28 2006	November 30 2005
Assets (note 13)		
Current assets		
Cash and cash equivalents	\$ 1,332,750	\$ 9,599,801
Marketable securities (note 6)	287,950	-
Restricted cash (note 7)	-	221,264
Accounts receivable (note 8)	8,173,796	11,002,470
Inventory (note 9)	1,203,940	1,094,634
Prepaid expenses and deposits	782,514	624,629
	<u>11,780,950</u>	<u>22,542,798</u>
Plant and equipment (note 10)	1,247,027	1,015,057
Intangible and other assets (note 11)	1,069,210	732,912
Goodwill (note 5)	9,147,243	481,014
	<u>\$ 23,244,430</u>	<u>\$ 24,771,781</u>
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities (note 12)	\$ 2,680,087	\$ 3,919,534
Income taxes payable (note 18)	106,797	284,833
Unearned revenue	819,298	530,321
	<u>3,606,182</u>	<u>4,734,688</u>
Deferred income taxes (note 18)	406,164	230,806
	<u>4,012,346</u>	<u>4,965,494</u>
Contingency (note 16)		
Capital stock		
Authorized (note 14(a))		
Issued and outstanding		
30,262 Class A preference shares – Series A (2005– 30,262) (note 14(b))	30,262	30,262
341,240 Class B preference shares – Series 2 (2005– 341,240) (note 14(c))	11,614,713	11,412,208
31,435,284 common shares (2005 – 30,367,309) (note 14(d))	23,697,952	22,832,892
	<u>35,342,927</u>	<u>34,275,362</u>
Warrants (note 14 (e))	5,207,234	5,207,234
Additional paid in capital	4,772,106	4,743,012
Accumulated deficit	(26,143,652)	(24,446,827)
Accumulated other comprehensive income	53,469	27,506
	<u>19,232,084</u>	<u>19,806,287</u>
	<u>\$ 23,244,430</u>	<u>\$ 24,771,781</u>

See accompanying notes to the unaudited consolidated financial statements

Offshore Systems International Ltd.

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Consolidated Statements of Earnings (Loss) (unaudited)
(expressed in Canadian dollars)

	For the three months ended February 28	
	2006	2005
Revenue (note 4(b))		
Marine systems	\$ 1,478,943	\$ 1,952,277
Land and air systems	2,126,731	-
Mapping	616,944	307,586
	<hr/>	<hr/>
	4,222,618	2,259,863
Cost of sales	<hr/>	<hr/>
	2,835,431	1,027,755
Gross profit	<hr/>	<hr/>
	1,387,187	1,232,108
Expenses		
General and administrative	1,552,085	1,036,193
Research and development	625,921	319,232
Sales and marketing	636,438	552,256
Depreciation and amortization	152,215	53,746
Interest expense	6,952	12,716
Interest income	(14,841)	(109)
Foreign exchange loss (gain)	111,895	(73,144)
Technology Partnerships Canada royalty (note 15)	65,645	54,691
Technology Partnerships Canada contribution (note 15)	(243,276)	(265,517)
	<hr/>	<hr/>
	2,893,034	1,690,064
Net loss before income taxes	<hr/>	<hr/>
	(1,505,847)	(457,956)
Income tax recovery (note 18)	<hr/>	<hr/>
	(11,527)	(238,365)
Net loss for the period	<hr/>	<hr/>
	\$ (1,494,320)	\$ (219,591)
Net loss attributable to common shareholders	<hr/>	<hr/>
	\$ (1,696,825)	(296,313)
Loss per share (note 14(g))		
Basic	\$ (0.05)	\$ (0.01)
Diluted	\$ (0.05)	\$ (0.01)
Weighted average number of common shares outstanding (note 14(g))		
Basic	31,269,155	27,488,074
Diluted	31,269,155	27,488,074

See accompanying notes to the unaudited consolidated financial statements

Offshore Systems International Ltd.

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Consolidated Statements of Stockholders' Equity and Accumulated Deficit (unaudited)
(expressed in Canadian dollars)

For the three months ended February 28

2006

2005

Class A preference shares

Balance at the beginning of the period	30,262	\$	30,262	30,262	\$	30,262
Balance at the end of the period	30,262	\$	30,262	30,262	\$	30,262

Class B preference shares

Balance at the beginning of the period	341,240	\$	11,412,208	57,711	\$	2,163,622
Accretion of discount on Class B preference shares						
– Series 1	-		-	-		33,439
Accretion of discount on Class B preference shares						
– Series 2	-		202,505	-		-
Balance at the end of the period	341,240	\$	11,614,713	57,711	\$	2,197,061

Common shares

Balance at the beginning of the period	30,367,309	\$	22,832,892	27,488,074	\$	20,033,931
Shares Issued to CHI Systems shareholders (note 5)	1,067,975		865,060	-		-
Balance at the end of the period	31,435,284	\$	23,697,952	27,488,074	\$	20,033,931

Warrants

Balance at the beginning of the period	13,788,365	\$	5,207,234	1,393,301	\$	661,575
Balance at the end of the period	13,788,365	\$	5,207,234	1,393,301	\$	661,575

Additional paid-in capital

Balance at the beginning of the period		\$	4,743,012		\$	941,968
Stock-based compensation			29,094			2,524
Balance at the end of the period		\$	4,772,106		\$	944,492

Accumulated deficit

Balance at the beginning of the period		\$	(24,446,827)		\$	(14,196,847)
Accretion of discount on Class B preference shares –						
Series 1			-			(33,439)
Accretion of discount on Class B preference shares –						
Series 2			(202,505)			-
Net earnings (loss) for the period			(1,494,320)			(219,591)
Balance at the end of the period		\$	(26,143,652)		\$	(14,449,877)

Accumulated other comprehensive income

Foreign currency translation adjustment						
Mapcon Mapping						
Balance at the beginning of the period		\$	27,506		\$	-
Adjustment for the period			5,535			-
Balance at the end of the period			33,041			-
CHI Systems						
Balance at the beginning of the period			-			-
Adjustment for the period			20,428			-
Balance at the end of the period			20,428			-
Balance at the end of the period		\$	53,469		\$	-
Total stockholders' equity		\$	19,232,084		\$	9,417,444

See accompanying notes to the unaudited consolidated financial statements

Offshore Systems International Ltd.
Consolidated Statements of Cash Flows (unaudited)
(expressed in Canadian dollars)

U.S. GAAP

	For the three months ended February 28	
	2006	2005
Cash flows provided by operating activities		
Loss for the period	\$ (1,494,320)	\$ (219,591)
Items not affecting cash		
Depreciation and amortization	215,959	84,670
Stock-based compensation	29,094	2,524
Deferred income taxes	(14,906)	(238,365)
Changes in non-cash working capital items		
Accounts receivable	4,246,059	980,286
Inventory	(109,306)	(213,127)
Prepaid expenses and deposits	82,913	(297,321)
Accounts payable and accrued liabilities	(2,078,656)	(765,414)
Income taxes payable	(167,413)	-
Unearned revenue	288,978	(5,520)
	<u>998,402</u>	<u>(671,858)</u>
Cash flows provided by (used in) financing activities		
Proceeds from operating line of credit	-	548,394
Class B preference share dividend paid	-	(86,566)
	<u>-</u>	<u>461,828</u>
Cash flows used in investing activities		
Purchase of CHI Systems, net of acquired cash	(9,143,191)	-
Increase in marketable securities	(287,950)	-
Decrease in restricted cash	221,264	-
Additions to plant and equipment	(55,128)	(27,424)
Additions to intangible and other assets	(46,282)	(13,583)
Additions to goodwill on acquisition of Mapcon Mapping	(264)	-
	<u>(9,311,551)</u>	<u>(41,007)</u>
Effect of exchange rate changes on cash and cash equivalents	<u>46,098</u>	<u>-</u>
Decrease in cash and cash equivalents	(8,267,051)	(251,037)
Cash and cash equivalents – beginning of period	9,599,801	251,037
Cash and cash equivalents – end of period	\$ 1,332,750	\$ -

See accompanying notes to the unaudited consolidated financial statements

Offshore Systems International Ltd.

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Notes to the Consolidated Financial Statements (unaudited)

February 28, 2006 and February 28, 2005

(expressed in Canadian dollars)

1) Basis of Presentation

These unaudited interim consolidated financial statements have been prepared by management and include the accounts of Offshore Systems International Ltd. ("OSI") and its subsidiaries, collectively referred to as the Company. These unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") and all amounts herein have been expressed in Canadian dollars unless otherwise noted. These unaudited interim consolidated financial statements do not include all the information and footnote disclosures required for compliance with U.S. GAAP for annual financial statements applied on a consistent basis. These unaudited interim consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and notes thereto. These unaudited interim consolidated financial statements conform in all material respects with Canadian generally accepted accounting principles ("Canadian GAAP"), except as disclosed in note 21.

The preparation of these unaudited interim consolidated financial statements and the accompanying notes requires management to make estimates and assumptions that affect the amounts reported. In the opinion of management, these unaudited interim consolidated financial statements reflect all adjustments necessary to state fairly the results for the periods presented. Actual results could vary from these estimates and the operating results for the interim period presented are not necessarily indicative of the results expected for the full year.

2) Nature of Operations

OSI designs, develops, and markets software and systems for enhancing situational awareness in command, control, and intelligence applications. OSI'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 – International Systems Operations, U.S. Systems Operations and Mapping. The Company's International Systems and U.S. Systems business units develop and produce geographic information display systems and software for the marine navigation, and command and control markets, and situational awareness products for land-based and aeronautical command and control markets. The Company's Mapping 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.

3) Adoption of Accounting Policies

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard 123R, Share-Based Payment, ("SFAS 123(R)") a revision to SFAS 123. SFAS 123(R) requires all share-based payments to be recognized in the financial statements based on their fair values using either a modified-prospective or modified-retrospective transition method.

Prior to December 1, 2005, the Company's stock-based employee compensation plans were accounted for under the recognition and measurement provisions of Accounting Principles Board Opinion ("APBO") No. 25, "Accounting for Stock Issued to Employees" ("APBO 25") and related Interpretations, as permitted by FASB Statement No. 123, "Accounting for Stock-Based Compensation ("SFAS 123)". The Company did not recognize stock-based compensation costs in its statement of operations for periods prior to December 1, 2005, as all options granted had an exercise price equal to the market value of the underlying common stock on the date of the grant.

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(expressed in Canadian dollars)

Effective December 1, 2005, the Company adopted the fair value recognition provisions of SFAS No. 123(R), using the modified-prospective-transition method. Under this transition method, stock-based compensation cost recognized in the first three months of 2006 includes (a) compensation costs for all unvested stock-based awards based on the grant-date fair value, including those granted, modified or settled prior to September 1, 2005, that were previously disclosed on a pro forma basis, and (b) compensation cost for all stock-based awards granted subsequent to December 1, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R).

As a result of adopting SFAS 123(R) on December 1, 2005, the Company's loss from operations, loss before income taxes and net loss for the period ended February 28, 2006 increased by \$7,970.

4) Accounting Changes

a) Recent pronouncements

In May 2005 the Financial Accounting Standards Board issued Statement No. 154, Accounting Changes and Error Corrections. This Statement replaces APB Opinion No. 20, Accounting Changes, and FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, and changes the requirements for the accounting for and reporting of a change in accounting principle. This Statement applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. The adoption of SFAS 154 will not have a material impact on the Company's consolidated financial statements.

In February 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 155, Accounting for Certain Hybrid Financial Instruments. This Statement amends FASB Statements No. 133, Accounting for Derivative Instruments and Hedging Activities, and No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. This Statement resolves issues addressed in Statement 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets. The adoption of SFAS 155 will not have a material impact on the Company's consolidated financial statements.

In March 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 156, Accounting for Servicing of Financial Assets. This Statement amends FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, with respect to the accounting for separately recognized servicing assets and servicing liabilities. The adoption of SFAS 156 will not have a material impact on the Company's consolidated financial statements.

b) Change in revenue and reporting segments

Beginning in the first quarter of 2006, the Company will report consolidated revenue as Marine systems, Land and air systems, and Mapping. These were previously reported as Software, Geomatics, Systems and software components, and Other. Segmented results will now be reported as International Systems operations, U.S. Systems operations, and Mapping. These were previously reported as Navigation systems, Applications, and Geomatics. Navigation systems and Applications are now combined as International Systems and Geomatics has been renamed as Mapping. Prior period revenue has been restated to conform to the new reporting categories.

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Notes to the Consolidated Financial Statements (unaudited)
February 28, 2006 and February 28, 2005
(expressed in Canadian dollars)

5) Acquisitions

a) CHI Systems Inc.

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. The results of CHI's operations have been included in the consolidated financial statements commencing December 14, 2005.

The following table summarizes the fair value of the assets acquired and liabilities assumed by the Company at December 14, 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 December 14, 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 nine months.

Assets	
Current assets	\$ 2,373,595
Plant and equipment	259,257
Intangible and other assets	432,413
Goodwill	8,684,157
Total assets acquired	\$ 11,749,422
Liabilities	
Current liabilities not including deferred tax liabilities	824,793
Deferred tax liabilities	190,055
Total liabilities assumed	\$ 1,014,848
Net assets acquired (cash and common share consideration)	\$ 10,250,162
Direct acquisition costs incurred by the Company	484,412
Total acquisition costs	10,734,574
Less fair value of net identifiable assets acquired	2,050,417
Goodwill	\$ 8,684,157
Cash of acquired operations	\$ 722,999

The fair value of the assets acquired, including goodwill, and liabilities assumed in the acquisition have been "pushed down" to CHI Systems resulting in foreign currency revaluation at each reporting date.

The following table presents details of the purchased intangible assets:

	Estimated useful life	Amount
Patents	5 years	\$ 149,903
Customer contracts	2 to 24 months	155,669
Customer relationships	1 to 3 years	126,841
Total intangible assets		\$ 432,413

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February 28, 2006 and February 28, 2005

(expressed in Canadian dollars)

The pro forma Offshore Systems International consolidated operating results assuming the acquisition of CHI Systems had occurred as of December 1, 2004 are as follows:

	For the three months ended February 28	
	2006	2005
Revenue	\$ 4,665,147	\$ 5,518,225
Loss	\$ (1,464,857)	\$ (311,606)
Loss per share – basic	\$ (0.05)	\$ (0.01)
Loss per share – diluted	\$ (0.05)	\$ (0.01)

b) Mapcon Mapping Consultants Inc.

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 production market. The results of Mapcon Mapping's operations have been included in the consolidated financial statements commencing April 1, 2005.

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.

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

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Notes to the Consolidated Financial Statements (unaudited)

February 28, 2006 and February 28, 2005

(expressed in Canadian dollars)

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
Total intangible assets		<u>\$ 350,784</u>

6) Marketable Securities

Marketable securities consist of municipal obligations carried at fair value and classified as available for sale.

7) 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. There was no restricted cash at February 28, 2006.

8) Accounts Receivable

	February 28 2006	November 30 2005
Trade	\$ 5,057,722	\$ 7,265,224
Unbilled revenue	2,796,075	2,993,588
Technology Partnerships Canada contribution (note 15)	266,401	729,909
Other	67,916	56,072
Allowance for doubtful accounts	(14,318)	(42,323)
	<u>\$ 8,173,796</u>	<u>\$ 11,002,470</u>

9) Inventory

	February 28 2006	November 30 2005
Materials and components	\$ 1,170,941	\$ 1,094,634
Finished Goods	32,999	-
	<u>\$ 1,203,940</u>	<u>\$ 1,094,634</u>

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Notes to the Consolidated Financial Statements (unaudited)

February 28, 2006 and February 28, 2005

(expressed in Canadian dollars)

10) Plant and Equipment

February 28, 2006			
	Cost	Accumulated amortization	Net amount
Equipment	\$ 5,058,430	4,037,483	\$ 1,020,947
Vehicle	10,627	1,720	8,907
Furniture and fixtures	654,550	505,625	148,925
Leasehold improvements	335,625	267,377	68,248
	<u>\$ 6,059,232</u>	<u>4,812,205</u>	<u>\$ 1,247,027</u>

November 30, 2005			
	Cost	Accumulated amortization	Net amount
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
	<u>\$ 4,559,178</u>	<u>\$ 3,544,121</u>	<u>\$ 1,015,057</u>

11) Intangible and Other Assets

February 28, 2006			
	Cost	Accumulated amortization	Net amount
Computer software	\$ 1,235,530	\$ 762,200	\$ 473,330
Customer contracts	305,403	137,856	167,547
Customer relationships	311,128	49,329	261,800
Licenses and patents	249,235	82,701	166,534
	<u>\$ 2,101,296</u>	<u>\$ 1,032,086</u>	<u>\$ 1,069,210</u>

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

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Notes to the Consolidated Financial Statements (unaudited)

February 28, 2006 and February 28, 2005

(expressed in Canadian dollars)

12) Accounts Payable and Accrued Liabilities

	February 28, 2006	November 30, 2005
Trade	\$ 1,004,659	2,210,994
Accrued employee compensation	999,430	635,638
Accrued employee benefits and payroll deductions	43,249	398,319
Accrued royalties (note 15)	66,744	297,421
Other accrued liabilities	566,005	377,162
	<u>\$ 2,680,087</u>	<u>\$ 3,919,534</u>

13) 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 February 28, 2006 was 5.25% (2005 – 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 February 28, 2006, letters of credit, relating principally to customer contracts, amounting to U.S. \$nil (2005 – \$nil) and to Australian \$nil (2005 – \$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 (2005 – US\$2,000,000) and Australian \$nil (2005 – Australian \$2,750,000). 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 February 28, 2006, the Company had not drawn on its foreign exchange contract facility.

14) 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) Class A preference shares

The Company has 30,262 (November 30, 2005 – 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.

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February 28, 2006 and February 28, 2005

(expressed in Canadian dollars)

c) Class B preference shares

	For the three months ended February 28, 2006		For the year ended November 30, 2005	
	Number of Class B preference shares	Amount	Number of Class B preference shares	Amount
Balance – beginning of period	341,240	\$ 11,412,208	368,640	\$ 12,118,306
Accretion of discount – Series 2	-	202,505	-	219,661
Converted to common shares	-	-	(27,400)	(925,759)
Balance – end of period	341,240	\$ 11,614,713	341,240	\$ 11,412,208

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.

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.

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d) Issued and outstanding common shares

	For the three months ended February 28, 2006		For the year ended November 30, 2005	
	Number of common shares	Amount	Number of common shares	Amount
Balance – beginning of period	30,367,309	\$ 22,832,892	28,745,536	\$ 21,330,449
Issued during the period:				
Shares issued (note 5(a))	1,067,975	865,060	-	-
Exercise of stock options	-	-	10,000	7,500
Class B preference shares – Series 2 converted	-	-	1,611,773	1,494,943
Balance – end of period	31,435,284	\$ 23,697,952	30,367,309	\$ 22,832,892

e) Warrants

	For the three months ended February 28, 2006		For the year ended November 30, 2005	
	Number of warrants	Amount	Number of warrants	Amount
Balance – beginning of period	13,788,365	\$ 5,207,234	13,788,365	\$ 5,206,844
Balance – end of period	13,788,365	\$ 5,207,234	13,788,365	\$ 5,207,234

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 stock options granted to employees vest one year after the date granted.

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A summary of the status of the Company's stock option plans at February 28, 2006 is as follows:

	Number of shares	Weighted average exercise price
Outstanding - beginning of period	3,674,417	\$ 0.96
Granted	25,000	0.87
Forfeited	(129,000)	0.92
Expired	(33,333)	1.20
Outstanding - end of period	3,537,084	\$ 0.96
Exercisable – end of period	3,341,084	\$ 0.95

A summary of the Company's stock options outstanding and exercisable at February 28, 2006 is as follows:

Range of exercise prices	Stock options outstanding			Stock options exercisable	
	Number outstanding at February 28, 2006	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at February 28, 2006	Weighted average exercise price
\$0.75 – \$1.12	2,997,416	3.86 years	\$0.92	2,947,416	\$0.92
\$1.13 – \$1.20	539,668	1.08 years	\$1.14	393,668	\$1.14
\$0.75 – \$1.20	3,537,084	3.44 years	\$0.96	3,341,084	\$0.95

Stock-based compensation

For the three months ended February 28, 2006, the Company incurred non-cash stock-based compensation expense of \$29,094, related to total of 332,250 stock options granted to the end of February 28, 2006. (three months ended February 28, 2005 - \$2,524). The expense was included in general and administrative costs and was recorded in additional paid-in capital. Of the \$29,094, \$10,708 relates to the 25,000 stock options granted during the quarter ended February 28, 2006.

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

	2006	2005
Risk-free interest rate	2.98%	2.20%
Volatility	54%	58%
Estimated average stock option lives	5 years	3 years
Dividend yield	0.0%	0.0%

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.

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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) Loss per share

	For the three months ended February 28	
	2006	2005
Net loss for the period	\$ (1,494,320)	\$ (219,591)
Less: Class B preference share dividends	-	76,722
Accretion of discount on Class B preference shares - Series 2	(202,505)	-
Loss available to common shareholders	\$ (1,696,825)	\$ (296,313)
Weighted average number of common shares outstanding	31,269,155	27,488,074
Basic loss per share	\$ (0.05)	\$ (0.01)

Diluted loss per share

Net loss for the period	\$ (1,494,320)	\$ (219,591)
Less: Class B preference share dividends	-	76,722
Accretion of discount on Class B preference shares - Series 2	(202,505)	-
Loss available to common shareholders	\$ (1,696,825)	\$ (296,313)
Weighted average number of common shares outstanding	31,269,155	27,488,074
Diluted loss per share	\$ (0.05)	\$ (0.01)

15) 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 three months ended February 28, 2006, the Company claimed \$257,862 under the agreement. Accounts receivable at February 28, 2006 include \$266,401 of amounts receivable from TPC in connection with these claims (November 2005 - \$729,909).

The Company is required to pay a royalty of 3% on annual gross revenue the Company's subsidiary, Offshore

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Systems Ltd., for the period December 1, 1999 to November 30, 2008. The Company has paid royalties of \$1,306,799 to February 28, 2006 (to November 30, 2005 - \$1,241,154) and has accrued royalties of \$47,067 for the three months ended February 28, 2006 (three months ended February 28, 2005 - \$53,823). 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.

In addition, the Company is required to pay a royalty of 1.4% on annual gross revenue in the Company's subsidiary, Offshore Systems Ltd., for the period January 1, 2006 to December 31, 2008 and a royalty of 2.5% on annual gross revenue in the Company's subsidiary, Offshore Systems Ltd., for the period January 1, 2009 to December 31, 2013. The company has accrued royalties of \$18,578 for the three months ended February 28, 2006 (three months ended February 28, 2005 - \$nil). 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.

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 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 year ended November 30, 2005 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:

	For the three months ended February 28	
	2006	2005
Royalties paid	\$ 296,322	\$ 311,851
Accrued royalties – current	\$ 65,645	\$ 54,691

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.

16) Contingency

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 February 28, 2006 in respect of these claims because the potential liability for the claims and the amount of damages, if any, cannot be reasonably estimated.

17) Related Party Transactions

On April 11, 2005, E. Brinton Coxe, a director of the Company, assisted the Company in structuring and arranging the private placement financing (note 14(c)). 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 ended November 30, 2005 and to be provided to April 2006. For the three months ended February 28, 2006 \$24,189 was charged to expenses.

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On April 8, 2005, Gerald J. Shields, a related party by virtue of the provision of legal services to the Company by a law firm in which he has an interest was elected to the Company's Board of Directors. Fees paid to this law firm for services Mr. Shields provided to the Company during the three months ended February 28, 2006 totaled \$116,160.

18) Income Taxes

The Company is subject to income taxes in Canada and the United States and the use of estimates is required in determining the company's provision for income taxes. Although the Company believes its tax estimates are reasonable, the ultimate tax determination involves significant judgement that could become subject to audit by tax authorities in the ordinary course of business.

The effective rate used to record income tax expense for the three months ended February 28, 2006 differed from the Canadian federal and provincial combined statutory tax rate primarily due to the change in valuation allowance to reflect those future tax benefits that were more likely than not to be realized and, also, items not deductible for income tax purposes. The change in effective tax rate from 2005 to 2006 was due primarily to the effect of the change in valuation allowance.

At February 28, 2006, the Company adjusted its valuation allowance against deferred 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 those deferred tax assets for which there is uncertainty of future realization.

Earnings before income taxes consisted of the following:

	For the three months ended February 28	
	2006	2005
Income tax recovery	\$ (11,527)	\$ (238,365)
Effective tax rate	0.0%	52.0%

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19) 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 of the Company's audited consolidated annual financial statements for the year ended November 30, 2005 prepared in accordance with U.S. GAAP. 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.

Three months ended February 28, 2006

	International Systems Operations	U.S. Systems Operations	Mapcon	Corporate & Public Company Costs	Total
Revenue	\$ 1,478,943	\$ 2,126,731	\$ 616,944	\$ -	\$ 4,222,618
Gross profit	783,144	486,560	117,483	-	1,387,187
Technology Partnerships Canada - net	177,631	-	-	-	177,631
Interest expense	-	-	-	6,952	6,952
Income tax recovery	-	(3,885)	(7,642)	-	(11,527)
Net loss	(452,644)	(22,153)	(330,455)	(689,068)	(1,494,320)
Plant and equipment expenditures	18,229	6,724	27,729	2,446	55,128
Intangibles and other asset expenditures	37,603	12,266	(3,587)	-	46,282
Depreciation and amortization	54,627	82,718	78,614	-	215,959

Three months ended February 28, 2005

	International Systems Operations	U.S. Systems Operations	Mapcon	Corporate & Public Company Costs	Total
Revenue	\$ 1,952,283	\$ -	\$ 307,580	\$ -	\$ 2,259,863
Gross profit	1,208,100	-	24,008	-	1,232,108
Technology Partnerships Canada - net	210,826	-	-	-	210,826
Interest expense	5,623	-	1,485	5,608	12,716
Income tax recovery	(214,110)	-	(24,255)	-	(238,365)
Net earnings (loss)	587,378	-	(142,894)	(664,075)	(219,591)
Plant and equipment expenditures	27,424	-	-	-	27,424
Intangibles and other asset expenditures	11,561	-	2,022	-	13,583
Depreciation and amortization	51,988	-	30,702	1,980	84,670

Total assets employed:

	International Systems Operations	U.S. Systems Operations	Mapcon	Total
As at February 28, 2006	\$ 8,028,382	11,648,300	3,567,748	\$ 23,244,430
As at November 30, 2005	20,605,152	-	4,166,629	24,771,781

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Segment revenues by category for the three months ended February 28 are as follows:

	Three months ended February 28, 2006			
	International Systems Operations	U.S. Systems Operations	Mapcon	Total
Marine systems	\$ 1,478,943	-	-	\$ 1,478,943
Land and air systems	-	2,126,731	-	2,126,731
Mapping	-	-	616,944	616,944
Total	\$ 1,478,943	2,126,731	616,944	\$ 4,222,618

	Three months ended February 28, 2005			
	International Systems Operations	U.S. Systems Operations	Mapcon	Total
Marine systems	\$ 1,952,277	-	-	\$ 1,952,277
Land and air systems	-	-	-	-
Mapping	-	-	307,586	307,586
Total	\$ 1,952,277	-	307,586	\$ 2,259,863

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

	Three months ended February 28	
	2006	2005
Europe	\$ 195,600	\$ 1,627,000
Australia/New Zealand	440,605	311,894
United States	2,650,294	200,713
Canada	936,119	120,256
Total	\$ 4,222,618	\$ 2,559,863

Geographically, plant and equipment are reported based on location.

	February 28 2006	November 30 2005
Canada	\$ 948,890	\$ 954,418
United States	298,137	60,639
Total	\$ 1,247,027	\$ 1,015,057

20) Financial Instruments**Fluctuations in foreign currency exchange rates**

The Company enters into transactions denominated in Canadian dollars, U.S. dollars, Australian dollars, British Pounds, Danish kroners 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 U.S. 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 February 28, 2006, the Company had foreign exchange forward contracts maturing in the following year to sell US \$nil (2005 - \$nil), Australian \$nil (2005 - Australian \$2,750,000), and €nil (2005 -€nil).

The fair value of derivative instruments generally reflects the estimated amounts that the Company would receive or pay to settle the contracts at February 28, 2006. The fair value of the above derivative financial instruments was an unrecorded liability of \$nil at February 28, 2006 (November 30, 2005 - \$nil).

21) 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 no 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 \$ nil and \$202,505, respectively, to deficit for the three months ended February 28, 2006 (for the quarter ended February 28, 2005 - \$nil and \$33,439).

(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

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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 three months ended February 28, 2006 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, 2005 - 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 \$53,469 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 (Loss) would be:

	Three months ended February 28	
	2006	2005
Loss for the period, U.S. GAAP	\$ (1,494,320)	\$ (219,591)
Adjustment for stock-based compensation (a),(d)	-	(23,645)
Loss for the period, Canadian GAAP	\$ (1,494,320)	\$ (243,236)
Basic loss per common share, Canadian GAAP	\$ (0.05)	\$ (0.01)
Diluted loss per common share, Canadian GAAP	\$ (0.05)	\$ (0.01)
Weighted average number of common shares - basic, Canadian GAAP	31,269,155	27,488,074
Weighted average number of common shares - diluted, Canadian GAAP	31,269,155	27,488,074

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

	February 28	November 30
	2006	2005
Common shares (d)	22,676,346	21,811,286
Class B preference shares – Series 2 (b)	10,226,350	10,912,177
Additional paid in capital (a), (b)	454,125	299,929
Accumulated deficit (a), (b), (c), (d)	(19,415,702)	(18,481,837)
Cumulative translation adjustment (f)	\$ 53,469	\$ 27,506