YANGAROO INC.

ANNUAL REPORT 2010

Dear shareholders,

2010 was a year of change at Yangaroo. As you may know, I joined the team in Q3 (June) 2010 and the Yangaroo team and I have been hard at work on our profitable growth strategy ever since.

The introduction of DMDS 5.0 and the addition of SD and HD video distribution capabilities gave us the opportunity to expand our value proposition to our existing customer base and it also provided us the ability to move into the much larger video advertising content distribution market.

We invested Q3 and Q4 of 2010 in building our capabilities and skill sets to enable us to build our distribution footprint with television networks, cable operators and television stations in the U.S. This distribution footprint gives us the network destinations that become attractive to content owners seeking to distribute their content faster, more efficiently and less expensively. We have seen a rapid adoption of DMDS at most of the larger high value destinations we targeted. Our destination network build out is at the tipping point and we expect to profit from this in 2011.

Our efforts were rewarded as revenue for the fourth quarter of 2010 was 44% higher than the revenue for the same period of 2009 and revenue for the fiscal year of 2010 was 3% higher than the revenue in fiscal 2009. The increase in revenue is a result of greater use of DMDS for music video delivery by the major labels and the independent sector. Revenue is expected to continue to increase as billable US music audio and video deliveries grow, independent sector usage increases, and billable advertising delivery volumes rise.

Total operating expenses for the year ended December 31, 2010 increased by 16% compared to the same period in fiscal 2009, primarily due to recruiting costs and management changes, the addition of a new advertising division and debenture interest. In the fourth quarter of 2010, management continued its cost cutting initiative through reducing costs and increasing productivity by consolidating offices. The Company also reduced its expenditures on consultants by terminating or suspending certain engagements and restructuring compensation terms with existing consultants and employees to more closely link compensation to results. The benefits of the Company's cost cutting measures will be reflected fully in fiscal 2011.

As part of the Company's annual review for indications of impairment, it determined there to be a reduction in value of $1,543,575 in its long lived asset group, which includes patents, investment in technology and deferred development costs. The Company believes that its cost savings initiative and the recent restructuring of management will enhance the Company's economic future.

Recent period highlights include a multi-year agreement with Viacom's BET Networks to use YANGAROO's Digital Media Distribution System (DMDS) technology for delivery of all artist and music-related audiovisual content to BET properties, an agreement with the Academy of Country Music to power online review and professional member voting for the 46th Annual Academy of Country Music Awards and receiving the grant of Canada patent number 2,349,797 titled "*Biometric Rights Management System*". YANGAROO named advertising industry veteran Anthony G. Miller to the board of directors and appointed former advertising executive Karen Dealy to President of U.S. Advertising Operations.

In the fourth quarter we made great strides in expanding our reach beyond the music industry to the advertising industry. The revenue growth in Q4 is just the beginning. With music video revenues continuing to grow, and the advertising rollout well underway, we expect revenue growth to continue and accelerate.

We will continue to execute our profitable growth strategy and expect to see the full impact of our initiatives in 2011.

Scott Wambolt
Chief Executive Officer

YANGAROO INC. **Date: April 11, 2011**
December 31, 2010
Management's Discussion and Analysis ("MD&A")

Introduction

Unless the context suggests otherwise, references to "YANGAROO", "the Company" or similar terms refer to YANGAROO Inc.

This MD&A is a discussion and review of operations, current financial position and outlook for YANGAROO and should be read in conjunction with the financial statements and related notes for the year ended December 31, 2010. Amounts are reported in Canadian dollars based upon the financial statements prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

Forward Looking Information

This MD&A contains "forward-looking information" which may include, but is not limited to, statements with respect to the future financial or operating performance of the Company, its mineral project, the future price of resources, the estimation of resources, the realization of resource estimates, the timing and amount of estimated future production, costs of production, capital, operating and exploration expenditures, costs and timing of development, costs and timing of future exploration, requirements for additional capital, government regulations, environmental risks, reclamation expenses, title disputes or claims and limitations of insurance coverage. Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates", or "believes" or variations (including negative variations) of such words and phrases, or state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved.

Forward-looking statements are based on the opinions and estimates of management as of the date such statements are made and are based on assumptions. They involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company and/or its subsidiary to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Such factors include, among others, general business, economic, competitive, political and social uncertainties; the actual results of current exploration activities; actual results of reclamation activities; conclusions of economic evaluations; changes in project parameters as plans continue to be refined; future prices of resources; possible variations recovery rates; failure of plant, equipment or processes to operate as anticipated; accidents, labour disputes and other risks of the industry; political instability; delays in obtaining governmental approvals or financing or in the completion of development or construction activities, as well as those factors discussed in the section entitled "Risk Factors" in this MD&A. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results to differ from those anticipated, estimated or intended. Forward-looking statements contained herein are made as of the date of this MD&A and the Company disclaims any obligation to update any forward-looking statements, whether as a result of new information, future events or result, except as may be required by applicable securities laws. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements.

Description of Business

YANGAROO's patented Digital Media Distribution System (DMDS) is a leading secure B2B digital delivery solution for the music and advertising industries. DMDS is a Web-based delivery system that pioneers secure digital file distribution by incorporating biometrics, high-value encryption and watermarking. DMDS replaces the physical distribution of audio and video content for music, music videos, and advertising to television, radio, media, retailers, award shows and other authorized recipients with more accountable, effective, and far less costly digital delivery of broadcast quality media via the Internet.

Named one of Canada’s Top 100 Tech Companies for 2009 by Canadian Business, YANGAROO has offices in Toronto, New York, Dallas, and Los Angeles.

Results of Operations

Revenue

Revenue for the year ended December 31, 2010 increased 3% over the prior year. The change is due to increased usage in music video delivery and new contracts with major labels for awards management. A significant portion of the Company’s revenue is derived from music audio delivery.

Revenue for the fourth quarter of 2010 was $252,939, 44% higher than the revenue for the fourth quarter of 2009. Revenues increased as a result of greater use of DMDS for music video delivery by existing music industry customers and billings to new customers, both in the independent sector and with the major labels. Revenue is expected to continue to increase as billable US music audio and video deliveries grow, independent sector usage increases, and billable advertising delivery volumes rise.

Operating Expenses

Total Operating expenses for the year ended December 31, 2010 increased by 16% compared to the same period in fiscal 2009 to $4,183,000 (2009 - $3,608,000). The main contributors of the change are the increase in general and administrative expense of 30% ($310,000) and an increase in salaries and consulting of 12% ($209,000) over the prior year.

Management continued to cut operating costs in the fourth quarter of 2010. In the period, management sought to reduce costs and increase productivity by consolidating offices. The office in Richmond Hill was closed and the headquarters was moved to the Mowat Street office in Toronto. The Company also reduced its expenditures on consultants by terminating or suspending some engagements while also structuring compensation terms with existing consultants that more closely link compensation to results. The benefits of the Company's cost cutting measures will be reflected in fiscal 2011.

(i) Salaries and Consulting

The increase in salaries and consulting expense is primarily due to the addition of the new CEO and the US advertising department. The US advertising department incurred personnel expenses of $167,000 in fiscal 2010. The administration department incurred a 26% ($176,000) increase in salaries and consulting expenses over the prior year which is due to the addition of personnel. Operations department incurred a 7% ($14,000) increase over the prior year. The increase is due to hiring staff to support a greater number of customers and usage of DMDS.

The 12% increase of salaries and consulting expense was offset by a decrease of the expense in sales and marketing department by 25% ($113,000). The reduction in the sales and marketing department was due to the reconstruction of the sales team. As well, the technology development decreased its salaries and consulting expense by 10% ($36,000). This change is due to the completion of a majority of the development of DMDS.

Stock based compensation of $90,000 is also included in the salaries and consulting expense for the fiscal year ended December 31, 2010. Stock-based compensation increased by $50,000 (124%) from fiscal year ended December 31, 2009. A significant portion of the increase reflects the value assigned to option grants to new employees and an executive.

(ii) General and Administrative

The increase in general and administrative expense for fiscal year end December 31, 2010 is primarily due to recruiting expenses of $236,000 (2009 - $0) for the Chief Executive Officer and the President US Advertising Operations. The Company does not expect to incur recruiting expenses in fiscal 2011.

General and administrative expense also includes expenses related to the defence of the Company's Canadian and American intellectual property rights. The Company incurred costs of $378,000 for the fiscal year of 2010 (2009 - $480,000); a decrease of 21%. The cost of enforcing the Company's intellectual property rights are a non-recurring operating expense. It is expected that these costs will not be necessary once the matters under litigation are resolved. This expenditure is essential in maintaining the value of the company's intellectual property by protecting it from unauthorized replication. If the company is not successful in these actions it will not prevent the company from continuing with its business.

(iii)Research and Development

Total expenditure on technology development was $692,000 for fiscal year ended December 31, 2010. Deferred development costs for the fiscal year of 2010 decreased by $191,000 (14%) in comparison to fiscal year of 2009 and technology development expense increased by $5,000 (8%). The company met the deferral criteria for development costs under Canadian generally accepted accounting principles as the company is generating increasing revenues from the products and technology it has developed.

As part of the Company's annual review for indications of impairment, the Company chose the discounted cash flow approach to determine the fair value of the long lived asset group which includes patents, investment in technology and deferred development costs. Based on this selection, the Company determined there to be a reduction in value in its long lived asset group as the estimated fair value no longer supports the net book value. The impairment is premised upon management's assessment in accordance with GAAP while considering other internal and external factors, such as lower than anticipated sales in music for the fiscal year ended December 31, 2010 and revised growth estimates in music for fiscal 2011. As well, the Company's considered its impending transition to International Financial Reporting Standards ("IFRS") standards. A charge of $1,543,575 relates to the impairment of the intangible assets.

(iv) Sales and Marketing

Marketing and promotion expense for the fiscal year ended December 31, 2010 increase by less than 1% over the prior year.

Selected Financial Information and Management Discussion and Analysis

Summary of Quarterly Results

The following table sets out selected unaudited financial information, presented in Canadian dollars and prepared in accordance with Canadian generally accepted accounting principles ("GAAP") for each of the last eight quarters ended up to and including December 31, 2010. The information contained herein is drawn from interim financial statements of the Company for each of the aforementioned quarters.

	2010 Q4	**2010 Q3**	**2010 Q2**	**2010 Q1**
Working capital	$ (345,229)	$ 590,111	$ 4,698	$ 28,889
Sales	$ 252,939	$ 171,729	$ 196,534	$ 185,290
Expenses	$ 2,871,635	$ 1,153,016	$ 973,885	$ 871,590
Loss for the period	$ 2,618,696	$ 981,287	$ 777,351	$ 686,300
Loss per share (basic & diluted)	$ 0.02	$ 0.01	$ 0.01	$ 0.01

	2009 Q4	**2009 Q3**	**2009 Q2**	**2009 Q1**
Working capital	$ 88,588	$ 851,395	$ 1,375,824	$ 2,119,430
Sales	$ 175,613	$ 218,211	$ 204,842	$ 181,386
Expenses	$ 1,111,065	$ 763,837	$ 930,492	$ 791,407
Loss for the period	$ 935,452	$ 545,626	$ 725,650	$ 610,021
Loss per share (basic & diluted)	$ 0.01	$ 0.01	$ 0.01	$ 0.01

Revenue has increased due to increased use of DMDS by the music industry and music award shows. The trend in the losses over the period reflects the development of DMDS 5.0 nearing completion through 2009 and the commencement of amortization of deferred development costs in subsequent quarters. The increase in loss in the fourth quarter of 2009 was primarily the result of several months of work for the protection of the company's Canadian and U.S. patent rights being billed in the quarter. The second, third and fourth quarters of 2010 includes interest expense for convertible debentures that were issued in the first half of 2010. The figures in the second and third quarter 2010 include a one-time recruiting expense.

Liquidity, Capital Resources and Financings

At December 31, 2010, the Company has cash and cash equivalents balance of $203,000 and a negative working capital of $345,229.

The company will continue to invest funds in building its business to achieve key market and growth targets. The company's operations are not yet generating positive cash flow, so in future the company will need to source additional funds in order to fulfil its business objectives. While the company believes it will be able to secure sufficient funding to carry out its business plans, insufficient capital will affect its ability to pursue its marketing and business development strategies.

Subsequent to the year ended December 31, 2010, the Company issued convertible debenture through a private placement and generated gross proceeds of $1,125,000. The debentures are convertible into common shares at $0.10 per share.

Outstanding Share Data

The following securities were outstanding as at December 31, 2010:

Common shares	118,047,615
Stock options	7,335,000
Warrants	30,713,000
Convertible debentures	8,180,000

Off Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements.

Critical Accounting Estimates

The preparation of the Company's financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the financial results of the Company. Such estimates and assumptions affect the carrying value of assets, impact decisions as to when exploration and development costs should be capitalized or expensed, and estimate for asset retirement obligations and reclamation costs.

Other significant estimates made by the Company include factors affecting valuations of stock based compensation. The Company regularly reviews its estimates and assumptions, however, actual results could differ from these estimates and these differences could be material.

Recent Accounting Pronouncements Issued and Not Yet Applied

Business Combinations

In January 2009, the CICA issued Sections 1582 – Business Combinations, 1601 – Consolidated Financial Statements and 1602 – Non-controlling Interests which replaces CICA Sections 1581 – Business Combinations and 1600 - Consolidated Financial Statements. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1582 is applicable for the Company's business combinations with acquisition dates on or after January 1, 2011. Early adoption of this Section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company's interim and annual consolidated financial statements for its fiscal year beginning July 1, 2011. Early adoption of this Section is permitted. If the Company chooses to early adopt any one of these Sections, the other two Sections must also be adopted at the same time. The Company has not yet determined the impact of the adoption of these standards on its financial statements.

International Financial Reporting Standards

In February 2008, the Accounting Standards Board announced that 2011 is the changeover date for publicly listed companies to use International Financial Reporting Standards ("IFRS"), replacing Canadian GAAP. As of January 1, 2011, the Company will have the option of reporting under Accounting Standards for Canadian Private Enterprises or IFRS. The Company has decided to follow IFRS. The changeover date of January 1, 2010 will require the restatement for comparative purposes of amounts reported by the Company for the year ending December 31, 2010.

The conversion requirement from GAAP to IFRS raises both financial and non-financial issues. The Company has commenced the development of an IFRS implementation plan to prepare for this transition. The plan consists of three phases which are diagnostic, design and planning, and implementation.

The Company is currently near completion of the second phase. This phase includes the detailed review, documentation and selection of accounting policy choices relating to each IFRS standard. This phase will also include assessing the impact of the conversion on business activities, including the effect on information technology and data systems, income tax, internal controls over financial reporting, and disclosure controls. In this phase, accounting policies will be finalized, first-time adoption exemptions and exceptions will be considered, and draft financial statements and note disclosures will be prepared. The Company is in the preliminary stages of phase three of the process. YANGAROO plans on implementing IFRS standards during the second quarter of fiscal 2011.

Financial Instruments and Other Instruments

The Company's financial instruments consist of cash and cash equivalents, other receivables, deposit, note receivable, and accounts payable and accrued liabilities.

Management does not believe these financial instruments expose the Company to any significant interest, currency or credit risks. The fair market values of cash and cash equivalents, other receivable, deposit, note receivable, and accounts payables and accrued liabilities approximate their carrying values.

Financial Risk Factors

The Company is exposed to a variety of risks, including, but not limited to the risks set out below. The Company considers these risks the most significant to potential investors, but not all of the risks associated with an investment in securities of YANGAROO.

- Financial risks
  - Fluctuations in currency exchange rates
  - Interest rate risk
  - Credit risk
  - Cash flows and additional funding requirements
  - Global financial conditions
  - Uncertainty of additional financing

- Operational risks
  - Dependent on the internet as a medium for business and communication
  - The lack of a defined market for our product
  - Online commerce security
  - The ability to generate revenue and control operating costs
  - Lack of profitability
  - Contingencies

- Non-Financial Risks
  - Management of growth
  - Competition risks
  - Availability and dependence on management and outside advisors
  - Fluctuations in currency exchange rates
  - Heavily relying on upper management
  - The global economy
  - Price and public volatility of public stock
  - Dividends
  - Dilution
  - Adoption of new accounting standards under IFRS for the years beginning on or after January 1, 2011

Disclosure Controls and Procedures

The accompanying financial statements have been prepared by management in accordance with GAAP. For quarterly reporting periods and annual reporting periods, the Company's financial statements are approved by the Board of Directors upon recommendation by the Audit Committee. The integrity and objectivity of these financial statements are the responsibility of management. In addition, management is responsible for all other information in this report and for ensuring that this information is consistent, where appropriate, with the information contained in the financial statements.

In support of this responsibility, management maintains a system of internal controls to provide reasonable assurance as to the reliability of financial information and the safeguarding of assets. In particular, the CEO and CFO are responsible for establishing and maintaining disclosure controls and procedures ("DC&Ps") and internal controls over financial reporting ("ICFRs") for the Company, and we have:

(a) designed such DC&Ps, or caused them to be designed under our supervision, to provide reasonable assurance that material information is made known to us during the period in which the annual filings are being prepared; and

(b) designed such ICFRs, or caused them to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP; and

(c) evaluated the design and effectiveness of the Company's DC&Ps as of the period ended December 31, 2010, and have evaluated the design of the Company's ICFRs for the period ended December 31, 2010; and

(d) have concluded that a material design weakness in the ICFRs may exist in terms of the inadequate segregation of certain duties, which is typical of development stage companies with limited staff; mitigating factors, including dual-payment authorization policies and transparent internal financial transaction reporting processes, serve to minimize the risk that such design weakness could result in a material misstatement of results for the period ended December 31, 2010; and

(e) have concluded that, other than the item described above in sub-point (d), there are no additional material design weaknesses in the DC&Ps or ICFRs, and that the effectiveness of the DC&Ps is sufficient to expect the prevention or detection of material misstatements of results.

The financial statements include amounts that are based on the best estimates and judgments of management. The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and internal control. The Board of Directors exercises this responsibility principally through the Audit Committee. The Audit Committee consists of three directors not involved in the daily operations of the Company. The Audit Committee meets with management and the external auditors to satisfy themselves that management's responsibilities are properly discharged and to review the financial statements prior to their presentation to the Board of Directors for approval.

The external auditors, Collins Barrow Toronto LLP audit the annual statements, in accordance with Canadian generally accepted auditing standards, and provide a report of their findings to the Audit Committee. The external auditors have free and full access to the Audit Committee with respect to their findings concerning the fairness of financial reporting and the adequacy of internal controls.

YANGAROO Inc.

Financial Statements

For the Years Ended December 31, 2010 and 2009

Collins Barrow
Chartered Accountants

Collins Barrow Toronto LLP
20 Eglinton Avenue West
Suite 2100, P.O. Box 2014
Toronto, Ontario
M4R 1K8 Canada

T. 416.480.0160
F. 416.480.2646

www.collinsbarrow.com

INDEPENDENT AUDITORS' REPORT

To the Shareholders of YANGAROO Inc.

We have audited the accompanying financial statements of YANGAROO Inc. which comprise the balance sheets as at December 31, 2010 and December 31, 2009 and the consolidated statements of operations, deficit and cash flows for the years then ended and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of YANGAROO Inc. as at December 31, 2010 and December 31, 2009, and its financial performance and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 1 in the financial statements which indicates that the Company has material uncertainties that may cast significant doubt about the Company's ability to continue as a going concern.

Collins Barrow Toronto LLP

Licensed Public Accountants
Chartered Accountants
April 11, 2010
Toronto, Ontario

YANGAROO Inc.
Balance Sheets
As at December 31, 2010 and 2009

	2010	2009
Assets		
Current		
Cash and cash equivalents	**$ 202,604**	$ 259,603
Accounts receivable	**162,752**	193,581
Prepaid and sundry assets	**176,397**	196,204
	541,753	649,388
Capital assets (Note 3)	**140,322**	133,345
Patents (Note 4)	**-**	138,438
Investment in technology (Note 5)	**-**	356,209
Deferred development costs (Note 6)	**-**	1,343,238
	$ 682,075	$ 2,620,618
Liabilities		
Current		
Line of credit (Note 7)	**$ 20,000**	$ 5,000
Accounts payable and accrued liabilities	**833,410**	538,666
Deferred revenue	**33,572**	17,134
	886,982	560,800
Convertible debentures (Note 8)	**655,202**	-
	1,542,184	560,800
Shareholders' Deficiency		
Capital stock (Note 9)	**22,338,694**	21,043,889
Contributed surplus (Note 11)	**1,503,468**	1,413,871
Warrants capital (Note 12)	**761,298**	31,883
Equity portion of convertible debentures (Note 8)	**29,890**	-
Deficit	**(25,493,459)**	(20,429,825)
	(860,109)	2,059,818
	$ 682,075	$ 2,620,618

Going Concern (Note 1)
Commitments and Contingencies (Note 16)
Subsequent Event (Note 19)

Approved by the Board **"Cliff Hunt"** Director **"Scott Wambolt"** Director

YANGAROO Inc.
Statements of Operations and Deficit
Years Ended December 31, 2010 and 2009

	2010	2009
Revenue	**$ 806,492**	$ 780,051
Expenses		
Salaries and consulting	**1,889,550**	1,680,707
Marketing and promotion	**210,024**	209,501
General and administrative	**1,356,684**	1,047,145
Technology development	**59,809**	55,305
Amortization of intangibles	**579,126**	526,295
Amortization of capital assets	**87,804**	88,923
	4,182,997	3,607,876
Loss before the undernoted items and income taxes	**(3,376,505)**	(2,827,825)
Other income (expenses)		
Interest income	**4,327**	11,074
Interest expense	**(147,881)**	-
Impairment of intangible assets (Note 4)	**(1,543,575)**	-
	(1,687,129)	11,074
Net loss	**(5,063,634)**	(2,816,751)
Deficit, beginning of year	**(20,429,825)**	(17,613,074)
Deficit, end of year	**$(25,493,459)**	$(20,429,825)

Loss per share (Note 14)		
Basic and diluted	**$ (0.06)**	$ (0.04)

See accompanying notes

YANGAROO Inc.
Statements of Cash Flows
Years Ended December 31, 2010 and 2009

	2010	2009
Cash provided by (used in)		
Operations		
Net loss	**$ (5,063,634)**	$ (2,816,751)
Items not affecting cash		
Amortization	**666,930**	615,218
Accretion interest	**70,865**	-
Loss (gain) on disposal of capital assets	**-**	(762)
Stock-based compensation	**89,597**	40,059
Warrants issued for services/compensation	**20,625**	31,883
Impairment of intangible assets	**1,543,575**	-
	(2,672,042)	(2,130,353)
Net changes in non-cash working capital		
Accounts receivable	**30,829**	(35,783)
Prepaids and sundry assets	**19,807**	(70,401)
Accounts payable and accrued liabilities	**294,745**	95,213
Deferred revenue	**16,438**	2,145
	(2,310,223)	(2,139,179)
Investing		
Purchase of capital assets	**(94,781)**	(56,499)
Proceeds from sale of capital assets	**-**	1,129
Patents	**(1,395)**	(40,374)
Deferred development costs	**(283,422)**	(540,573)
	(379,598)	(636,317)
Financing		
Issuance of convertible debentures, net of issue costs	**669,753**	-
Line of credit	**15,000**	5,000
Issuance of common shares, net of issue costs	**1,948,069**	-
	2,632,822	5,000
Net change in cash	**(56,999)**	(2,770,496)
Cash, beginning of year	**259,603**	3,030,099
Cash, end of year	**$ 202,604**	$ 259,603

Supplemental Disclosure		
Cash	**$ 200,348**	$ 257,352
Cash equivalents	**2,256**	2,251
Total cash and cash equivalents	**$ 202,604**	$ 259,603

See accompanying notes

1. GOING CONCERN

YANGAROO Inc. (the "Company") is a technology company that is targeted to become the leading enabler of user friendly and secure business to business distribution of media via the Internet. The Company's patented Digital Media Distribution System (DMDS) is a leading secure B2B digital delivery solution for the music and advertising industries. DMDS is a Web-based delivery system that pioneers secure digital file distribution by incorporating biometrics, high-value encryption and watermarking. DMDS replaces the physical distribution of audio and video content for music, music videos, and advertising to television, radio, media, retailers, award shows and other authorized recipients with more accountable, effective, and far less costly digital delivery of broadcast quality media via the Internet.

The Company is a publicly listed company incorporated on July 28, 1999 under the laws of Ontario as Musicrypt.com Inc. and changed to its present name on July 17, 2007. The Company trades on the TSX Venture Exchange (TSX-V) under the symbol YOO and in the U.S. under TCBB: YOOIF.

The Company will have to raise additional capital to fund operations until such point that revenues from their technology are able to fund operations. If the Company is not able to raise sufficient capital then there is the risk that the Company will not be able to realize the value of its assets and discharge its liabilities. These financial statements do not give effect to adjustments that would be necessary to the carrying values and classification of assets and liabilities should the going concern assumption not be appropriate. To date the Company has been successful raising capital and in fiscal 2010 the Company raised gross proceeds of $818,000 by way of convertible debentures and $2,126,500 by way of private placement. These proceeds were used to fund operations of the Company. As well, subsequent to the year end (Note 19), the Company raised gross proceeds of $1,125,000 by way of convertible debentures, however there is no assurance the Company will be able to raise sufficient funds in the future.

2. SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles within the framework of the significant accounting policies summarized below.

Financial Instruments

All financial instruments are recorded initially at fair value. In subsequent periods, all financial instruments are measured based on the classification adopted for the financial instrument: held to maturity, loans and receivables, held for trading, available for sale or other liability.

Financial Assets

Held for trading assets are subsequently measured at fair value with the change in the fair value recognized in net income during the period.

Held to maturity assets are subsequently measured at amortized cost using the effective interest rate method.

Loans and receivables are subsequently measured at amortized cost using the effective interest rate method.

Available for sale assets are subsequently measured at fair value with the changes in fair value recorded in other comprehensive income, except for equity instruments without a quoted market price which are measured at cost.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Financial Liabilities

Held for trading liabilities are subsequently measured at fair value with the change in the fair value recognized in net income during the period.

Other liabilities are subsequently measured at amortized cost using the effective interest rate method.

The Company has classified its financial instruments as follows:

Financial Instrument	Classification
Cash and cash equivalents	Held for trading
Accounts receivable	Loans and receivables
Line of credit	Other liabilities
Accounts payable and accrued liabilities	Other liabilities
Convertible debentures	Other liabilities

The Company's financial instruments measured at fair value on the balance sheet consist of cash and cash equivalents and are measured at level 1 of the fair value hierarchy. There are three levels of the fair value hierarchy as follows:

Level 1: Values based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2: Values based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

Level 3: Values based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

Comprehensive Income

Comprehensive income measures net earnings for the period plus other comprehensive income. Other comprehensive income consists of changes to unrealized gains and losses on available for sale financial assets, changes to unrealized gains and losses on the effective portion of cash flow hedges and changes to foreign currency translation adjustments of self-sustaining foreign operations during the period. Amounts reported as other comprehensive income are accumulated in a separate component of shareholders' equity as Accumulated Other Comprehensive Income. To date there has not been any other comprehensive income and accordingly, a statement of other comprehensive income has not been presented.

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenue and expenses during the year. Actual results could differ from those estimates.

Significant areas requiring the use of management estimates relate to the determination of the useful lives of long-lived assets for amortization purposes, valuation of convertible debentures, valuation of stock based payments and warrants, the fair values of financial instruments and impairment, if any, of long-lived assets.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Cash and Cash Equivalents

Cash and cash equivalents include bank deposits and highly liquid money market investments such as bankers' acceptance notes, treasury bills and guaranteed investment certificates.

Capital Assets

Capital assets are recorded at cost less accumulated amortization. Amortization is calculated on a straight-line basis over the estimated useful lives of the assets as follows:

Office furniture and equipment	- 5 years
Computer equipment	- 3 years
Computer software	- 3 years
Leasehold improvements	- over the term of the lease
Website and other technology	- 3 years

Patents

Costs to obtain patents are capitalized and are amortized to operations on a straight-line basis over the underlying term of the patents, which is 20 years, commencing upon the registration of the patent. The patents relate to the use of the technology under license described in Note 5 and the asset described in Note 6.

Investment in Technology

The investment in technology consists of consideration paid for the acquisition of licenses to use technology. Such costs are amortized to operations on a straight-line basis over the remaining term of the license. In 2007, the Company signed a license agreement expiring on June 28, 2013 as disclosed in Note 16(a).

Research and Development Costs

Research costs are charged to operations when incurred. Development costs are expensed in the year incurred unless they meet the criteria under Canadian generally accepted accounting principles for deferral and amortization. Amortization commences with the successful commercial production or use of the product or process. These costs are being amortized over a period of four years from commencement of commercial use.

Investment Tax Credits ("ITCs") earned as a result of incurring Scientific Research and Experimental Development ("SRED") expenditures are recorded as a reduction of the related current period expense, the related deferred development costs or related capital assets. Management records ITC's when there is reasonable assurance of collection. Included in prepaid and sundry assets as at December 31, 2010, management has recorded approximately $83,900 relating to ITC's of which approximately $62,300 has been recorded as a reduction to deferred development costs and $21,600 has been recorded as a reduction to technology development expense.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Impairment of Long-lived Assets

Long-lived assets with finite useful lives consist of capital assets, patents, deferred development costs and investment in technology. Long-lived assets are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. When the carrying value is not recoverable from future cash flows on an undiscounted basis and the carrying value exceeds the assets' fair value, an impairment loss is recorded for the excess of carrying value over fair value.

Convertible Debentures

The Company accounts for its convertible debentures in accordance with the substance of the contractual arrangement on initial recognition. Therefore, as a result of the conversion feature of the debentures, the Company's convertible instruments have been segregated between debt and equity based on the fair value of the debt components. The difference between the estimated fair value of the debt at issuance and the face amount is reflected as "Equity portion of convertible debt" in shareholders' equity and as a discount in that amount to the liability portion of the debenture. This discount is being accreted to the principal face amount as additional interest expense over the term of the liability using the effective interest rate method.

Share Issuance Costs

Costs incurred in connection with the issuance of capital stock are netted against the proceeds received.

Accounting for Stock-Based Compensation and Other Stock-Based Payments

The Company applies a fair value based method of accounting to all stock based payments. Accordingly, stock based payments are measured at the fair value of the consideration received or the fair value of the equity instruments issued or liabilities incurred, whichever is more reliably measurable. Stock based compensation is charged to operations over the vesting period and the offset is credited to contributed surplus. Consideration received upon the exercise of stock options is credited to share capital and the related contributed surplus is transferred to share capital.

Revenue Recognition

The Company's revenue is derived through the secure distribution of media via its patented Digital Media Distribution System. The Company recognizes revenue at the time persuasive evidence of an agreement exists, price is fixed and determinable, the distribution of the media has occurred and collectability is reasonably assured. The Company defers revenue which has been billed but for which services have not yet been performed.

Loss Per Share

Basic loss per share is calculated based on the weighted average number of shares outstanding. The treasury stock method is used to compute the dilutive effect of options, warrants and similar instruments.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Income Taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on temporary differences between financial reporting and tax bases of assets and liabilities, as well as for the benefit of losses available to be carried forward to future years for tax purposes. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Future income tax assets are recorded in the financial statements if realization is considered more likely than not.

Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at rates of exchange at each transaction date. Revenue and expenses are translated at the rate of exchange at each transaction date. Gains or losses on translation are included in income.

Recent Accounting Pronouncements Issued and Not Yet Applied

(a) Canadian public companies will be required to prepare their financial statements in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), for financial years beginning on or after January 1, 2011 ("Changeover Date"). Effective January 1, 2011, the Company will adopt IFRS as the basis for preparing its consolidated financial statements. The Company will issue its financial results for the quarter ended March 31, 2011 prepared on an IFRS basis and provide comparative data on an IFRS basis as required.

(b) The CICA has recently issued CICA Handbook section 1582, Business Combinations, section 1601, Consolidated Financial Statements, and section 1602, Non Controlling Interests. These new sections replace the currently existing standards in CICA Handbook section 1581, Business Combinations, and section 1600, Consolidated Financial Statements. These new standards are effective for fiscal periods beginning on or after January 1, 2011, however, early adoption is permitted. Once adopted, these standards will be harmonized with international financial reporting standards.

Section 1582 amends the standards for measurement, presentation and disclosure of a business combination. A number of changes are specified, including an expanded definition of a business, a requirement to measure all business acquisitions at fair value, a requirement to measure non controlling interests at fair value, and a requirement to recognize acquisition related costs as expenses.

These standards will require a change in the measurement and presentation of non-controlling interest. As a result of these changes, net earnings will include 100% of the subsidiary's results and non controlling interest will be presented as part of shareholders' equity on the balance sheet.

The Company is currently assessing the impact of these new accounting standards on its financial statements.

3. CAPITAL ASSETS

December 31, 2010	**Cost**	**Accumulated Amortization**	**Net**
Office furniture and equipment	**$ 38,564**	**$ 26,643**	**$ 11,921**
Computer equipment	**401,325**	**342,605**	**58,720**
Computer software	**103,883**	**43,847**	**60,036**
Leasehold improvements	**14,791**	**9,844**	**4,947**
Website and other technology	**18,176**	**13,478**	**4,698**
	$ 576,739	**$ 436,417**	**$ 140,322**

December 31, 2009	Cost	Accumulated Amortization	Net
Office furniture and equipment	$ 32,824	$ 23,270	$ 9,554
Computer equipment	362,775	283,086	79,689
Computer software	56,588	23,797	32,791
Leasehold improvements	14,791	7,017	7,774
Website and other technology	14,980	11,443	3,537
	$ 481,958	$ 348,613	$ 133,345

4. PATENTS

	2010	2009
Balance at beginning of year	**$ 138,438**	$ 105,855
Additions	**1,395**	40,374
Less: Amortization	**(8,424)**	(7,791)
Less: Impairment [(a)]	**(131,409)**	-
Balance at end of year	**$ -**	$ 138,438

As at December 31, 2010 the total cost of the patents is $NIL (2009 - $154,173) and the accumulated amortization is $NIL (2009 - $15,735).

(a) As part of its annual review for indications of impairment, the company determined there to be an impairment of the long-lived assets group, which includes patents, investment in technology and deferred development costs. The impairment is premised upon management's assessment in accordance with GAAP while considering other internal and external factors, such as lower than anticipated sales in music for the fiscal year ended December 31, 2010 and revised growth estimates in music for fiscal 2011. The Company chose the discounted cash flow approach to determine the fair value of the long-lived assets group. The estimated fair value of the long-lived assets no longer supports the net book value of the assets.

5. INVESTMENT IN TECHNOLOGY

		2010		2009
Balance at beginning of year	$	**356,209**	$	452,330
Less: Amortization		**(96,122)**		(96,121)
Less: Impairment (Note 4(a))		**(260,087)**		-
Balance at end of year	$	**-**	$	356,209

As at December 31, 2010 the total cost of the investment in technology is $NIL (2009 - $1,189,217) and the accumulated amortization is $NIL (2009 - $833,009). The Company has entered into a license agreement relating to the investment in technology (see Note 16(a)).

6. DEFERRED DEVELOPMENT COSTS

		2010		2009
Opening balance	$	**1,343,238**	$	1,300,433
Additions		**283,422**		465,188
Less: Amortization		**(474,580)**		(422,383)
Less: Impairment (Note 4(a))		**(1,152,080)**		-
Ending balance	$	**-**	$	1,343,238

Costs associated with the development of the Company's various digital media distribution systems ("DMDS") versions have been recorded as a deferred development costs. When a product begins to generate revenues, management ceases to defer the associated costs and begins to amortize the asset over the estimated benefit period of four years. As at December 31, 2010, the total cost of the deferred development is $NIL (2009 - $2,465,075) and the accumulated amortization is $NIL (2009 - $1,121,837).

7. OPERATING LINE OF CREDIT

The Company has available an operating line of credit of $25,000. Borrowings under the operating line of credit are due on demand and bear interest at prime plus 2.5% per annum and are secured by a general security agreement. As at December 31, 2010, the Company had drawn $20,000 (2009 - $5,000) on this line of credit.

8. CONVERTIBLE DEBENTURES

On March 22, 2010, the Company raised by way of convertible debentures (the "Debentures") 668 Units at $1,000 per Unit for gross proceeds of $668,000. The Debentures mature on March 31, 2012, have interest payable semi-annually at 12% per annum, are secured by a general security agreement over the assets of the Company and are convertible into common shares of the Company at $0.10 per share. In addition, each unit includes 7,500 warrants exercisable until March 22, 2012, with each whole Warrant entitling the holder to purchase one common share at $0.10. The Company granted the agents non-transferable warrants to acquire 508,000 common shares of the Company at $0.10 per share unit March 22, 2012.

On April 12, 2010 the Company raised an additional $150,000 by issuing 150 Units at $1,000 per Unit. These Debentures also mature on March 31, 2012 and have the same features as the previously issued Units.

The difference between the estimated fair value of the debt and the face amount was $67,211. To determine the value ascribed to the equity component and the warrants, the Company valued each component individually and then applied the relative fair value method of allocating the proceeds to each component. Both the fair value of the equity component of the convertible debentures and the warrants were estimated at the date of grant using the Black-Scholes model with the following weighted average assumptions: (a) dividend yield of 0%; (b) expected volatility of 157%; (c) a risk free interest rate of 1.6% and (d) an expected life of 2 years.

Based on the results, $38,405 was recorded as the equity portion of convertible debentures and $28,806 was allocated to the warrants. The Company incurred costs of $148,247 and issued agent warrants with a value of $33,106 (see Note 10) in connection with issuing the convertible debt. Of the total costs, $166,451 has been allocated to the liability component, $8,515 has been allocated to the equity component and $6,386 was allocated to warrants. The discount on the debt results in an effective interest rate on the liability of approximately 32.50%.

9. CAPITAL STOCK

Authorized

an unlimited number of common shares.

Issued and outstanding

	Number of Shares	Value
Balance, January 1, 2009 and 2010	75,517,615	**$ 21,043,889**
Issued for cash [(a)]	42,530,000	**1,868,109**
Less: proceeds allocated to warrants[(a)]	-	**(573,304)**
Balance, December 31, 2010	118,047,615	**$ 22,338,694**

(a) The Company issued 2,126.50 units for gross proceeds of $2,126,500 by way of a private placement. Each unit consists of 20,000 common shares and 10,000 common share purchase warrants. Share issuance costs of $258,389 have been netted against the proceeds. Included in share issuance costs is $79,960; which represents the value of 2,055,000 warrants issued to agents in connection with the private placement.

10. STOCK OPTIONS AND WARRANTS

(a) Stock Options

The Company has an Incentive Stock Option Plan (the "Plan"). The Plan provides for options to be granted to the benefit of employees, directors and third parties. The maximum number of shares allocated to and made available to be issued under the Plan is 7,551,761. In 2007, the board of directors adopted a new option pricing model such that the exercise price of options granted under the Stock Option Plan is priced as the greater of the three months weighted average trading price prior to the grant and the closing trading price for the common shares for the last trading day prior to the grant. The term of any option granted shall not exceed the maximum permitted time period under applicable regulations. Unless otherwise provided in the Stock Option Plan, the options shall be cumulatively exercisable in instalments over the option period at a rate to be fixed by the Board of Directors. The Company will not provide financial assistance to any optionee in connection with the exercise of options.

The Company had issued stock options to acquire common shares as follows:

	2010		2009	
	Number of Options	**Weighted Average Exercise Price**	Number of Options	Weighted Average Exercise Price
Outstanding, beginning of year	**3,595,000**	**$ 0.25**	3,769,000	$ 0.35
Granted	**5,200,000**	**$ 0.10**	750,000	$ 0.11
Cancelled	**(150,000)**	**$ 0.11**	(224,000)	$ 0.32
Forfeited	**(200,000)**	**$ 0.33**	-	$ -
Expired	**(1,110,000)**	**$ 0.42**	(700,000)	$ 0.57
Outstanding, end of year	**7,335,000**	**$ 0.12**	3,595,000	$ 0.25
Exercisable	**2,147,500**	**$ 0.18**	2,804,500	$ 0.30

10. STOCK OPTIONS AND WARRANTS (Cont'd)

(a) Stock Options (Cont'd)

The Company had the following stock options outstanding at December 31, 2010:

Number of Options	Exercise Price	Expiry Date
65,000	$ 0.20	August 16, 2011
120,000	$ 0.24	November 21, 2011
10,000	$ 0.35	April 12, 2012
340,000	$ 0.32	May 24, 2012
50,000	$ 0.27	June 25, 2012
120,000	$ 0.24	August 15, 2012
100,000	$ 0.13	November 27, 2012
100,000	$ 0.14	January 9, 2013
250,000	$ 0.22	April 18, 2013
410,000	$ 0.10	November 19, 2013
25,000	$ 0.13	April 17, 2014
25,000	$ 0.13	April 17, 2014
25,000	$ 0.10	August 19, 2014
520,000	$ 0.11	November 18, 2014
400,000	$ 0.10	April 20, 2015
3,775,000	$ 0.10	June 15, 2015
1,000,000	$ 0.10	August 23, 2015
7,335,000		

(b) Warrants

The Company had issued warrants to acquire common shares as follows:

	2010		2009	
	Number of Warrants	**Weighted Average Exercise Price**	Number of Warrants	Weighted Average Exercise Price
Outstanding, beginning of year	**750,000**	**$ 0.10**	2,800,000	$ 0.25
Issued	**29,963,000**	**$ 0.10**	750,000	$ 0.10
Expired	**-**	**$ -**	(2,800,000)	$ 0.25
Outstanding, end of year	**30,713,000**	**$ 0.10**	750,000	$ 0.10
Exercisable	**30,713,000**	**$ 0.10**	375,000	$ 0.10

10. STOCK OPTIONS AND WARRANTS (Cont'd)

(b) Warrants (Cont'd)

The Company had the following warrants outstanding at December 31, 2010:

Number of Warrants	Exercise Price	Expiry Date
4,972,500 (i)	$ 0.10	March 22, 2012
508,000 (ii)	$ 0.10	March 22, 2012
750,000 (iii)	$ 0.10	August 24, 2014
1,162,500 (iv)	$ 0.10	March 22, 2012
21,265,000 (v)	$ 0.10	January 31, 2012
2,055,000 (vi)	$ 0.10	August 27, 2012
30,713,000		

(i) These warrants were issued as part of the convertible debenture financing that closed on March 22, 2010.

(ii) These warrants were issued to agents in connection with the issuance of convertible debentures. The fair value of the warrants issued were estimated at the date of grant using the Black Scholes model with the following weighted average assumptions: (I) dividend yield of 0%; (II) expected volatility of 157%; (III) a risk free interest rate of 1.61% and (IV) an expected life of 2 years.

(iii) These warrants were issued for services related to digital media workflow solutions. The warrants are now exercisable as various phases of digital media workflow solution have been completed.

(iv) These warrants were issued as part of the convertible debenture financing that closed on April 12, 2010.

(v) These warrants were issued as part of the private placement of units. The fair value of the warrants issued were estimated at the date of grant using the Black Scholes model with the following weighted average assumptions: (I) dividend yield of 0%; (II) expected volatility of 129%; (III) a risk free interest rate of 1.25% and (IV) an expected life of 1.43 years.

(vi) These warrants were issued to agents in connection with the private placement of units. The fair value of the warrants issued were estimated at the date of grant using the Black Scholes model with the following weighted average assumptions: (I) dividend yield of 0%; (II) expected volatility of 153%; (III) a risk free interest rate of 1.25% and (IV) an expected life of 2 years.

11. CONTRIBUTED SURPLUS

	2010	2009
Contributed surplus beginning of year	**$ 1,413,871**	$ 868,384
Expiry of warrants	**-**	505,428
Stock-based compensation expense (Note 13)	**89,597**	40,059
	$ 1,503,468	$ 1,413,871

12. WARRANT CAPITAL

		2010		2009
Warrant capital beginning of year	**$**	**31,883**	$	505,428
Value of warrants expired in the year		**-**		(505,428)
Value of warrants issued in the year		**729,415**		31,883
	$	**761,298**	$	31,883

13. STOCK-BASED COMPENSATION

The total stock compensation expense relating to options recognized in the year was $89,597 (2009 - $40,059).

The fair value of each option granted in the year ended December 31, 2010 has been estimated at the date of grant or the date when it became measurable using the Black-Scholes option pricing model with the following weighted-average assumptions: (a) dividend yield of 0% (2009 - 0%); (b) expected volatility of 130% (2009 - 129%); (c) risk-free interest rate of 2.64% (2009 - 2.59%) and; (d) expected life of 5 years (2009 - 5 years). The Company has assumed no forfeiture rate (except on performance based options) as adjustments for actual forfeitures are made in the period they occur. The weighted average grant date fair values of options issued in the year ended December 31, 2010 was $0.10 (2009 - $0.11).

14. LOSS PER SHARE

Loss per share has been calculated based on the weighted average number of common shares outstanding during the year, of 90,315,725 (2009 - 75,517,615).

For the above-mentioned years, the Company had securities outstanding which could potentially dilute basic earnings per share in the future, but were excluded from the computation of dilutive net loss per share in the periods presented, as their effect would have been anti-dilutive. Such outstanding securities consist of the following:

	2010	2009
Options	**7,335,000**	3,595,000
Warrants	**30,713,000**	750,000
Convertible debt	**8,180,000**	-

15. INCOME TAXES

(a) Income Tax Expense

The following table reconciles income taxes calculated at combined Canadian federal/ provincial tax rates with the income tax expense in these financial statements:

	2010	2009
Loss before income taxes	**$ (5,063,634)**	$ (2,816,751)
Statutory rate	**31.0%**	33.0%
Expected income tax recovery	**$ (1,569,727)**	$ (929,528)
Amounts not deductible for tax and other	**58,200**	24,148
Change in valuation allowance	**957,700**	217,600
Change in expected tax rate and other	**213,527**	550,780
Expiration of non-capital losses	**442,200**	137,000
Share issuance costs incurred	**(101,900)**	-
Income tax expense	**$ -**	$ -

(b) Future Income Taxes

The temporary differences that give rise to future income tax assets and future income tax liabilities are presented below:

	2010	2009
Amounts related to tax loss and credit carryforwards	**$ 4,957,800**	$ 4,679,300
Share issuance costs	**109,700**	109,400
Capital and intangible assets	**777,500**	98,600
Net future tax asset	**5,845,000**	4,887,300
Less: Valuation allowance	**(5,845,000)**	(4,887,300)
	$ -	$ -

The Company has ITCs of approximately $450,000 and unused expenditures of approximately $1,416,000 related to scientific research and experimental development costs. The Company also has non-capital losses of approximately $16,799,000 available to apply against future taxable income. If not utilized, the non-capital losses will expire as follows:

2014	$ 2,630,000
2015	1,389,000
2026	1,861,000
2027	2,618,000
2028	2,885,000
2029	2,425,000
2030	2,991,000
	$ 16,799,000

The potential tax benefit relating to these losses has not been reflected in these financial statements.

16. COMMITMENTS AND CONTINGENCIES

(a) Technology License Agreement

Pursuant to a licensing agreement dated June 28, 2007, the Company was granted a non-exclusive license to integrate a patented biometric technology (the "Intellectual Property") with their DMDS (Notes 5 and 6). The initial term of the License is for six years, automatically renewing for successive terms of one year after the initial five-year term and may be terminated by either party upon 180 days notice prior to the renewal date of the agreement. The Company must pay an additional annual maintenance fee based on the number of annual users, which at the Company's current usage results in a fee of $5,400 per year.

(b) Litigation

On November 14, 2000, the Company filed a claim against a former employee and shareholder, and related shareholders, seeking a rescission of their 1,250,000 common shares and damages in the amount of $100,000. A counterclaim was brought against the Company by these defendants for various relief including damages of approximately $850,000, a declaration that the defendants are shareholders and orders that they be bought out or the Company be wound up. In May 2001, the Company successfully defeated a motion by the defendants that sought interim costs and security for costs. The Company was awarded its costs for this motion. The Company continues to vigorously defend the action. The outcome is not determinable and therefore no provision is recorded.

In the ordinary course of business activities, the Company may be contingently liable for litigation and claims with customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the accounts where required.

(c) Patent Infringement

On July 25, 2005, the Company sent a letter to a competitor and its partners demanding that they cease infringement of the Company's Content Distribution System and Method patent number 2,407,774 in Canada. On March 7, 2006, the competitor filed a claim with the Federal Court of Canada requesting a ruling that the technology of the competitor and its partners does not infringe on this patent and that the patent was invalid. In June 2006, the Company filed with the Federal Court a statement of defence and counterclaim seeking $15 million in damages for infringement from the competitor and its partners. A pre-trial conference was held on March 8, 2011 and a pre-trial order issued on March 17, 2011 requesting a trial date for a period of 25 days and, among other things, setting a schedule for expert reports and judicial mediation.

In May 2007, the competitor sued the company for defamation and interference with their business claiming $25 million in damages. Management is of the opinion that the suit is a meritless attempt to deflect attention from the company's patent infringement claim against the competitor. The Company has filed a statement of defence and counterclaim with the Federal court for $25 million in damages from the competitor for defamation and interference with the Company's business. The competitor moved for summary judgment on the entire counterclaim but was unsuccessful on several grounds. The Company has put the competitor on notice of its own summary judgment motion in respect of the competitor's claim.

16. COMMITMENTS AND CONTINGENCIES (Cont'd)

(c) Patent Infringement (Cont'd)

On June 22, 2007, the Company filed a claim against a customer of the above competitor, requesting a declaration that the Company's Canadian patent, Content Distribution System and Method patent number 2,407,774 is valid and infringed by the use of the competitors technology and is seeking $2 million in damages. In November 2007, a defence and counterclaim was filed seeking a declaration that the use of the competitor's technology does not infringe the patent and the patent is valid.

Management believes that the above claims against the Company are meritless as a result of the Company having a valid patent, Content Distribution System and Method patent number 2,404,774, registered in Canada. In addition, in May 2009, the Company received a grant from the United States Patent and Trademark Office for US patent #7,529,712 titled Content Distribution System and Method. The Company also filed a patent infringement claim in May 2009 in the United States requesting that the court issue a permanent injunction prohibiting use of the competitor's system in the United States and payment of damages and legal costs. In August 2009 a Federal Court in Wisconsin ruled in the Company's favour on a motion to dismiss that was brought by the competitor and the claim proceeded. The Defendants thereafter brought a motion for summary judgment claiming that because certain steps of their method are performed outside of the United States, Yangaroo's claim should be dismissed. The motion was successful in the first instance and the Company's appeal dismissed.

The outcome of the above claims is not determinable and therefore, no provision is recorded.

(d) Leases

Total future minimum annual lease payments for premises and equipment are as follows:

2011	$	98,234
2012		52,075
	$	**150,309**

17. CAPITAL RISK MANAGEMENT

The Company includes equity, comprised of issued capital stock, warrant capital, contributed surplus, equity component of convertible debentures and deficit, in the definition of capital.

The Company's primary objective with respect to its capital management is to ensure that it has sufficient cash resources to further develop and market its digital media distribution systems, and to maintain its ongoing operations. To secure the additional capital necessary to pursue these plans, the Company may attempt to raise additional funds through the issuance of equity and warrants, debt or by securing strategic partners.

The Company is not subject to externally imposed capital requirements and there has been no change with respect to the overall capital risk management strategy during the year ended December 31, 2010.

18. FINANCIAL RISK MANAGEMENT

The Company is exposed to a variety of financial risks by virtue of its activities: market risk (including currency risk and interest rate risk), credit risk and liquidity risk. The overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on financial performance.

Risk management is carried out by management under policies approved by the Board of Directors. Management is charged with the responsibility of establishing controls and procedures to ensure that financial risks are mitigated in accordance with the approved policies.

(a) Market Risk:

(i) Currency risk:

The Company operates internationally and is exposed to foreign exchange risk from various currencies, primarily United States dollars. Foreign exchange risk arises from purchase transactions as well as recognized financial assets and liabilities denominated in foreign currencies.

Balances in foreign currencies at December 31, 2010 are as follows:

	USD$
Accounts receivable	$ 27,000
Accounts payable and accrued liabilities	$ 233,000

(ii) Interest rate risk:

Interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Financial assets and financial liabilities with variable interest rates expose the Company to cash flow interest rate risk. The Company's cash earns interest at market rates and its line of credit incurs interest at market rates.

The Company is exposed to price interest rate risk on its convertible debt as they bear interest at a fixed rate.

The Company manages its interest rate risk by maximizing the interest income earned on excess funds while maintaining the liquidity necessary to conduct operations on a day-to-day basis. Fluctuations in market rates of interest do not have a significant impact on the Company's results of operations.

(b) Credit Risk:

The Company is subject to risk of non-payment of accounts receivable. The Company mitigates this risk by monitoring the credit worthiness of its customers and by offering an ecommerce service to smaller customers. As at December 31, 2010, approximately 27% (December 31, 2009 - 22%) of accounts receivable and 24% (December 31, 2009 - 23%) of revenue are from two customers (2009 - two customers).

18. FINANCIAL RISK MANAGEMENT (Cont'd)

(c) Liquidity Risk:

Liquidity risk is the risk that the Company will not be able to meet its obligations as they fall due. The Company manages its liquidity risk by forecasting cash flows from operations and anticipated investing and financing activities. Senior management is also actively involved in the review and approval of planned expenditures.

As at December 31, 2010, the Company has accounts payable and accrued liabilities of $833,410 due within 12 months and has cash and cash equivalents and accounts receivable of $365,356 to meet its current obligations. As disclosed in Note 1, the Company will have to raise additional capital to fund further development of their product and operations.

The carrying values of cash and cash equivalents, accounts receivable, line of credit, and accounts payable and accrued liabilities approximate fair values due to the relatively short term maturities of these instruments. The fair value of the convertible debentures approximate carrying value due to the effective interest rates implicit in the debt.

19. SUBSEQUENT EVENT

Subsequent to the year end the Company raised by way of convertible debentures 1,125 Units at $1,000 per Unit for gross proceeds of $1,125,000. The Debentures mature on July 31, 2012, have interest payable semi-annually at 15% per annum, are secured by a general security agreement over the assets of the Company and are convertible into common shares of the Company at $0.10 per share. The Company paid the agents $60,000 and granted them non-transferable options to acquire 600,000 common shares of the Company at $0.10 per share until February 11, 2013.

CORPORATE INFORMATION

Address
YANGAROO Inc.
18 Mowat Avenue
Toronto, Ontario, Canada M6K 3E8
Phone: 416-534-0607 Fax: 416-534-9427
Website: www.yangaroo.com

Board of Directors

Clifford G. Hunt	*Chairman*
Scott R. Wambolt	*Chief Executive Officer*
Howard Atkinson	*Member of Audit Committee and Compensation Committee*
Justin D. C. LaFayette	*Member of Audit Committee and Compensation Committee*
Anthony Miller	*Member of Audit Committee and Compensation Committee*
Gary Moss	*Member of Audit Committee and Compensation Committee*

Officers

Scott R. Wambolt	*Chief Executive Officer*
Clifford G. Hunt	*Chairman & Chief Operating Officer*
Michael Galloro	*Acting Chief Financial Officer*
Richard Klosa	*Chief Technology Officer*
Karen R. Dealy	*President, US Advertising Operations*

Stock Exchange Listing *TSX Venture Exchange: Stock Symbol YOO*
TSX Venture Exchange
3rd Floor, 130 King Street West
Toronto, Ontario, Canada M5X 1J2
Phone: 416-365-2200 or Toll Free 1-877-421-2369 Fax: 416-365-2224
Website: www.tsx.com

Registrar and Transfer Agent
Equity Financial Trust Company
200 University Avenue, Suite 400
Toronto, Ontario, Canada M5H 4H1
Phone: 416-361-0930 Fax: 416-361-0470

Auditors
Collins Barrow Toronto LLP
11 King Street West, Suite 700
Toronto, Ontario, Canada M5H 4C7
Phone: 416-480-0160 Fax: 416-480-2646

Legal Counsel
Baker & McKenzie LLP
Brookfield Place
181 Bay Street, Suite 2100
P.O. Box 874
Toronto, Ontario, Canada M5J 2T3
Phone: 416-863-1221 Fax: 416-863-6275

DMDS Digital Media Distribution System