YANGAROO Inc.

Interim Financial Statements

September 30, 2010

(Unaudited)

YANGAROO Inc.
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YOO on the TSX Venture Exchange

YOOIF on the OTCBB

Management Discussion and Analysis
For the Third Quarter Ended September 30, 2010

YANGAROO Inc. ("YANGAROO" or "the company") trades on the TSX Venture Exchange under the symbol YOO (TSX-V: YOO) and in the USA on the OTCBB under the symbol YOOIF. Additional information on the company is available at www.yangaroo.com and www.sedar.com.

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1) Date of MD&A November 23, 2010.

Note Regarding Forward Looking Statements

This document may contain or refer to certain forward-looking statements relating but not limited to YANGAROO's expectations, intentions, plans and beliefs. Forward-looking information can often be identified by forward-looking words such as "anticipate", "believe", "expect", "goal", "plan"," intend", "estimate", "may" and "will" or similar words suggesting future outcomes, or other expectations, beliefs, plans, objectives, assumptions, intentions or statements about future events or performance. Forward-looking information is based on current expectations that involve a number of business risks and uncertainties. Forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from expected results. Potential shareholders and prospective investors should be aware that these statements are subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from those suggested by the forward-looking statements. Shareholders are cautioned not to place undue reliance on forward-looking information. By its nature, forward-looking information involves numerous assumptions, inherent risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and various future events will not occur.

2) Description of Business

YANGAROO Inc. is a technology company that is targeted to become the leading enabler of user-friendly and secure B2B ("business to business") distribution of media via the internet. The principal business objective of YANGAROO is the development and marketing of its patented Digital Media Distribution System ("DMDS") technology solution.

The company's strategy is to use its technology to supplant traditional means of delivering audio and video content on physical media (such as copying to CD, DVD or tapes and delivering via courier) by using the now widely available infrastructure of the high speed internet to enable faster, more secure, less expensive, and environmentally friendly digital content delivery.

DMDS is a web-based delivery system that pioneers secure digital file distribution by incorporating biometrics, encryption and watermarking. DMDS replaces the physical distribution of musical recordings, music video, and advertising to television broadcasters, 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.

DMDS utilizes YANGAROO's patented Biometric Rights Management ("BRM") technology to authenticate the recipient of, and grant specified access rights to, the media being distributed. BRM is a unique combination of biometrics, encryption and digital rights management. This biometric verification system identifies the recipient by his or her user name, password and distinctive personal characteristics. The biometric technology currently deployed in DMDS is keystroke dynamics, which identifies a user by their typing rhythm. BRM technology works to prevent unauthorized access and password sharing by verifying individual recipients, and requires no additional hardware for either the sender or the recipient, providing completely portable and secure access to users.

All of the major Canadian record labels (Universal Music, Warner Music, EMI Music, and Sony Entertainment Canada) used DMDS to become the first in the world to transition to digital delivery of promotional recordings to radio, internally and to other destinations such as consultants, managers, artists, satellite radio, internet radio, media, and reviewers. This recognition helps the company to increase revenue, market its service and build transaction volumes that are required to reach profitability. Obtaining widespread adoption and achieving higher levels of transaction volumes are key to the company's success. Use of DMDS by high profile, influential organizations globally will aid in reaching these goals and has been a focus of the company's recent and planned marketing efforts.

Record labels and artists have been delivering their new music and music videos to radio stations and television broadcasters using traditional physical media methods, and the industry is moving to digital delivery of their media for sales and promotion through other technologies as well as DMDS. The traditional method for music releases requires the pressing of promotional CD's (known in the industry as CD-PRO's) then packaging, labelling, and sending these with related printed materials by mail or courier to radio and other destinations. This is very costly, time consuming, insecure and harmful to the environment.

Similarly, the advantages of DMDS can be obtained for the distribution of television broadcast quality music videos and for both audio and video advertising content. DMDS can put the control of when and to whom ads and videos are distributed directly in the hands of the advertising firm or production house. DMDS can provide significant cost savings, greater efficiencies, direct control, and individual accountability compared to the distribution of ads on CD's, videotape, FTP or satellite based systems. YANGAROO has upgraded DMDS to the next generation 5.0 to enable it to distribute television broadcast quality music videos and TV commercials, as well as provide support for award shows, which offer significant additional market and revenue opportunities for the company.

3) <u>Review of Results of Operations for the Nine Months Ended September 30, 2010</u>

Revenues for the nine months ended September 30, 2010 decreased 8% ($51,000) over revenues for the same period in 2009, primarily as a result of timing differences of $81,000 in recurring award show revenues that were recognized in the first nine months of 2009, but are to be recognized later in 2010 and in early 2011. This treatment is more compatible with International

Financial Reporting Standards. The loss for nine months ended September 30, 2010 was 30% ($564,000) higher compared to the same period in 2009, primarily due to increases in recruiting expense of $236,000, interest expense of $100,000, amortization of intangible assets of $60,000 and stock option expense of $38,000.

EBITDA (Earnings before interest, taxes, depreciation and amortization) for the nine months ended September 30, 2010, calculated as the loss for the period before amortization, interest income and interest expense, decreased by 27% ($398,000) over the same period in 2009. EBITDA is a non-GAAP measure that does not have any standardized meaning prescribed by GAAP and is therefore unlikely to be comparable to similar measures presented by other companies. The company provides this information at the request of investors and it is commonly used throughout the investment industry as a measure of performance. The nearest GAAP measure to EBITDA is the loss for the year. Interest expense was included in the composition of EBITDA for the period because convertible debentures issued by company during the period accrued interest. The following table is a reconciliation of EBITDA to the loss for the nine month periods ended September 30:

$	2010	2009
Loss for the period	(2,444,938)	(1,881,298)
Less: Interest earned	(2,854)	(10,044)
Add: Interest expense	99,756	-
Amortization of capital assets	64,240	65,653
Amortization of intangible assets	433,346	373,264
EBITDA	(1,850,450)	(1,452,515)

Total expenses increased 16% ($406,000) for the nine months ended September 30, 2010 compared to the same period in 2009. Increases in general and administrative expense of 43% ($274,000), salaries and consulting of 6% ($67,000) and amortization of intangible assets of 16% ($60,000) were the main contributors to the higher total expenses.

The increase in amortization expense of intangible assets of $60,000 (16%) was largely a result of the commencement of amortization of deferred development costs for the investment in DMDS 5.0. A reduction in interest income of $7,000 (72%), due to lower investment balances added to the increase in the loss.

The increase in salaries and consulting expense was primarily due to increases in this expense in the general and administration department of 13% ($67,000) for the nine months ended September 30, 2010 compared to the same period in 2009. This increase was mainly attributable to the addition of the new CEO, plus the new US advertising department's initial personnel expenses of $34,000, The salaries and consulting expense for the technology department was higher by 6% ($13,000) and for the operations department this expense rose 13% ($19,000), reflecting increased staffing to support a greater number of customers and usage of DMDS. These increases were partly offset by the decrease in salaries and consulting for the sales and marketing department, which were 20% ($66,000) lower compared to the same nine month period in 2009.

Stock based compensation of $60,000 was included in the salaries and consulting expense for the nine months ended September 30, 2010, an increase of $38,000 (182%) from the same period in 2009, largely reflecting the value assigned to option grants to new employees.

General and administrative expense increased 43% ($274,000) for the nine months ended September 30, 2010, primarily due to recruiting expenses of $236,000 incurred in the period for the hiring of new executives, which were nil in the same period in 2009. The company does not expect that recruiting expenses will continue to be incurred at this level in subsequent periods. General and administrative expense includes expenses related to the protection of the company's Canadian and U.S. intellectual property rights, which were $235,000 in nine months ended September 30, 2010 compared to $236,000 for the same period in 2009. Expenditures related to enforcing the company's intellectual property rights are a non-recurring operating expense, as it is expected that these will not be necessary once the matters under litigation are resolved. These expenditures are essential to maintain 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.

Total expenditures on technology development were $553,000 in the nine months ended September 30, 2010. Of these expenditures, $57,000 was expensed as technology development, $236,000 was included in salaries and consulting expense and $260,000 was capitalized as deferred development costs. Technology development expense for the nine month period in 2010 was essentially unchanged from the same period in 2009. The company met the deferral criteria for development costs under generally accepted accounting principles as the company is generating increasing revenues from the products and technology it has developed. Amortization expense for deferred development costs in the amount of $355,000 was recognized in the first nine months of 2010, an increase of $59,000 (20%) compared to the same period in 2009.

Marketing and promotion expense for the nine months ended September 30, 2010 was $6,000 (4%) higher than for the same period in 2009 primarily because of increased advertising and sponsorship expenses.

DMDS is designed to save time and money compared to traditional physical means of distributing media such as sending CD's and videotapes by couriers. Users of these traditional methods are accustomed to these methods and must be convinced to change to using DMDS. The company's products are technology innovations and the revenues these generate are subject to the risks and uncertainties associated with the rate of adoption of new technology by the targeted markets and the creation of new market verticals, such as for television advertising delivery, music video delivery and award shows. Competitors for these markets may emerge with alternative technology solutions. Inflation was not a significant risk to the company's prices or costs during the period.

During the first quarter of 2010, the 52nd GRAMMY® Awards telecast took place at Staples Center in Los Angeles on January 31, 2010. The Recording Academy® successfully utilized DMDS to distribute music submitted for the 52nd GRAMMY Awards consideration to the more than 12,000 voting members of The Academy throughout the U.S. Submitted music was digitally ingested into DMDS and The Academy used the system to securely distribute the music to voting members, allowing them to stream the music online for review.

In March 2010 the company entered into multi-year agreements with the Western Canadian Music Alliance (WCMA), the organization which presents BreakOut West, and with Music BC, the organization administering The Peak Performance Project, a seven-year, $5.29 million artist development program funded by Jim Pattison Broadcasting's 100.5 The PEAK Vancouver.

In April 2010 the company completed the private placement of 818 Units at $1,000 per Unit for gross proceeds of $818,000. Each Unit consists of $1,000 principal amount of Convertible Debentures and 7,500 Warrants. 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. The Warrants are exercisable until March 22, 2012, with each whole Warrant entitling the holder to purchase one common share at $0.10.

In April 2010 the company signed a multi-year contract with MTV Networks (MTVN), a division of Viacom International Inc. (NYSE: VIA, VIA.B), which is one of the world's leading creators of entertainment content. MTVN's portfolio spans more than 150 television channels and 300 digital media properties in over 160 countries worldwide, and includes music video channels MTV, MTV2, VH1, VH1 Classic, VH1 Soul, and Country Music Television (CMT) and CMT Pure (see www.mtvnetworks.com). "By implementing YANGAROO's cutting-edge DMDS 5.0 platform, we hope to enhance the efficiency and cost-effectiveness of our music video delivery process while significantly reducing its environmental impact," said Emilienne Gray, Sr. Vice President, MTV360 & VH1 Music Programming and Strategy.

The company successfully completed the first commercial delivery of a broadcast quality music video to MTV Networks and other destinations on May 27, 2010 via DMDS. The music video for the song "21@12" by the band Hot Hot Heat was uploaded to DMDS by DVS, a video production and duplication company in Los Angeles.

In May 2010 the company announced the integration of DMDS with Telestream's TrafficManager™, which automates the way television advertising spots move within a TV station. Using Telestream's FlipFactory automation engine, TrafficManager integrates directly with the DMDS Manager and Website, automatically detecting spots when they are delivered via DMDS.

Following the grant of its U.S. patent #7,529,712 in May 2009, the company filed a claim for patent infringement in United States Federal District Court in Wisconsin requesting that the court issue an injunction against Destiny Media Technologies Inc. (OTC:DSNY) as well as Destiny Software Productions, Inc., and MPE Distribution, Inc. ("Destiny") to cease the use of their system in the United States. In September 2009 a Federal Court in Wisconsin ruled in YANGAROO'S favour on a Motion to Dismiss brought by Defendant Destiny. In June 2010, the U.S. District Court for the Eastern District of Wisconsin granted Destiny summary judgment of non-infringement, finding that the Defendant's allegedly infringing conduct is beyond the territorial reach of the United States Patent Law on the grounds that its servers were located outside the United States and that the patented claim is one of distributing content, not manufacturing the content. The company is currently appealing that ruling. The Court awarded the Defendant court costs in the amount of $1,831. The Defendant filed a motion with the Court requesting attorney fees in the amount of $172,759, which the Company opposed and the Court denied. In its submissions to the court Destiny stated that music uploaded to its system from the U.S. goes through its servers in Canada before being sent back into the United States. YANGAROO has an outstanding patent infringement claim for $15 million against Destiny in Canada for any infringing acts occurring in Canada.

In June 2010 DMDS was chosen to power the "2010 MTV Video Music Awards" the world's leading music video award show broadcast in approximately 160 countries with a potential audience of more than 1.2 billion viewers. The VMAs will utilize DMDS to distribute nominated music videos submitted for VMA consideration to the voting members throughout the U.S

In June 2010 Scott R. Wambolt joined the company as Chief Executive Officer and was appointed to the Board of Directors. Scott Wambolt has had a dynamic, results-charged career highlighted by success in driving revenues, market share, profitability, and shareholder value. Prior to joining YANGAROO, Wambolt served as the Senior Vice President, Channel Strategies and Revenues at Bell Mobility where he headed the 2,500+ person sales force to drive over $4 billion in revenues and $1.4 billion in EBITDA. Previously, Wambolt served as Senior Vice President, Sales at Yellow Pages Group. As a member of the team that led the leveraged/management buyout of the Yellow Pages Group from Bell Canada, Scott contributed to taking the business public in August 2003 delivering nearly $1 billion in incremental shareholder value in approximately one year. Scott also spent seven years at Dell Computer Corp, in various General Management roles in North America, the UK and Europe serving the SMB, Large Corporate and the Consumer segments. Wambolt received his MBA from the University of Toronto's Rotman School of Management and his BA in Law from Carleton University. "I see this as a tremendous value creation opportunity," said Scott Wambolt, CEO, YANGAROO Inc. "YANGAROO has developed world class technology and intellectual property, established relationships with powerful and influential partners, and has a dedicated, solid team. I am excited to help take the company to the next level and significantly increase shareholder value."

The company announced in June that DMDS had delivered the following authorized music videos for major Canadian record labels by top name recording artists, including Beyoncé, Adam Lambert, Katy Perry, Shakira, Sarah McLachlan, Drake, Bruce Springsteen, Barenaked Ladies, Avril Lavigne, AC/DC, Christina Aguilera, John Mayer, Charlotte Gainsbourg feat. Beck, and others. These videos were delivered to broadcasters that include MuchMusic, MTV Canada, Musique Plus, etalk, Entertainment Tonight Canada, Sun TV, AUX TV, and many others. "We used DMDS to deliver the Katy Perry, Kylie Minogue, Barenaked Ladies videos and others, and could not be happier with the results," said Rob Chubey, VP National Promotion EMI Records Canada. "DMDS gets the video to air much quicker, plus we're saving money - which is always a good thing."

In August 2010 the company announced that it had appointed former senior DG FastChannel (NASDAQ: DGIT) executive and advertising industry veteran Karen Dealy as President of U.S.

Advertising Operations. She will work closely with the YANGAROO team on launching the new advertising delivery division. DMDS offers the advertising community a fast, secure and cost-effective way to deliver HD and SD video as well as audio advertisements to broadcasters. Advertising executives can work directly with DMDS or a DMDS Certified Sender, such as a dub house or production house, to deliver ready-to-air ads to broadcasters. Karen Dealy was previously the Senior Vice President of Affiliate Marketing for DG FastChannel Inc. In her new role, she will be responsible for the development and growth of the new division and will report to YANGAROO's Chief Executive Officer, Scott Wambolt. Karen Dealy brings over 25 years of sales and marketing experience across multiple sectors, including digital technology services, broadcast cable and network media, and advertising. During her seven years with DG FastChannel, Inc., as a member of the executive management team, she successfully deployed new digital technology and content delivery strategies while driving adoption for the electronic distribution of media content across the broadcast platform, and consolidated the sales and marketing team to move revenue from a hardware to a software based model. Prior to joining DG FastChannel, Ms. Dealy served as the Senior Vice President of Affiliate Marketing at Premiere Radio Networks, a subsidiary of Clear Channel Communications. She has also held senior management positions at AMFM Radio Networks, and ABC Radio Networks. Ms. Dealy received her MBA from the Simmons School of Management, as part of a special ABC-sponsored executive management program. She received her Bachelor of Arts degree from Texas Tech University in advertising and marketing.

Also in August 2010 the company closed an over-subscribed private placement of 2,126.5 Units for gross proceeds of $2,126,500. Each Unit consists of 20,000 common shares and 10,000 common share purchase warrants at an issue price of $1,000 per Unit. The Warrants are exercisable until January 31, 2012, with each whole Warrant entitling the holder to purchase one common share at $0.10.

During September 2010 Anthony G. Miller, former Chairman Emeritus of MacLaren McCann, joined the company's board of directors. His five decades of experience in the advertising field is expected to be an invaluable asset to the company as it builds its advertising delivery division. Until January 2007, Anthony Miller was Chairman Emeritus of MacLaren McCann, one of Canada's leading advertising and marketing communications companies. He previously served as Vice Chairman of the global parent, McCann Worldgroup, based in New York, and has held a number of senior positions in advertising agencies in both the United States and Canada for more than 40 years. Miller is a former chairman of the Canadian Institute of Communication and Advertising, a past chairman of the Young Presidents Organization (Ontario), and a member of the Chief Executive Organization. He also serves on the board of Care Canada.

In November 2010 the company signed an agreement with the Academy of Country Music (ACM) to use DMDS to power online review and professional member voting for the forthcoming 46th Annual Academy of Country Music Awards to be held in the spring of 2011. The Academy will employ the DMDS Awards solution to securely distribute ballots in digital formats to its voting members. Through DMDS, members will be able to review materials online and vote electronically at a time that is most convenient for them. Each year, the Academy presents awards honoring country music's top talent and the industry's hottest emerging talent.

The 46th Annual Academy of Country Music Awards will be broadcast live on the CBS Television Network.

Also in November 2010, the company announced a multi-year agreement with BET Networks, a subsidiary of Viacom International Inc. (NYSE: VIA.B). Under this agreement, BET Networks and YANGAROO will work to have all artist and music-related audiovisual content delivered to BET properties - including the primary BET channel, BET Digital Networks, BET.com, BET International, BET Gospel and BET Hip Hop - using DMDS, as well as integrate DMDS with BET Network's internal workflow. BET Networks will actively promote and recommend to the entertainment industry to utilize DMDS to send content digitally to BET Networks. BET Networks is the leading provider of quality entertainment, music, news and public affairs television programming for the African-American audience in the U.S. The primary BET channel reaches more than 90 million households and can be seen in the United States, Canada, the Caribbean, the United Kingdom and sub-Saharan Africa.

In the third quarter of 2010 the company received the grant of Canada patent number 2,349,797 titled "*Biometric Rights Management System*" by the Canadian Intellectual Property Office (CIPO). The Biometric Rights Management System ("BRM") patent relates to YANGAROO's innovative use of biometric security measures to provide secure online distribution of digital media. The BRM patent will be in effect until June 2021. The utilization of BRM in DMDS provides a secure, user-friendly and portable way to link media access rights to an individual through their unique traits, rather than to a machine or an easily shared password. This feature provides DMDS customers with the most advanced solution available today. This BRM patent augments YANGAROO'S intellectual property portfolio, which includes the related United States patent number 7,003,670 titled "*Biometric Rights Management System*", United States patent number 7,529,712 titled "*Content Distribution System and Method*" and Canadian patent number 2,407,774 titled "*Content Distribution System and Method*". YANGAROO also has pending U.S. continuation patent application number 12/398,238 titled "*Content Distribution System and Method*" and U.S. patent application number 11/854,289 titled "*Media File Distribution System and Method*".

4) <u>Review of Operations for the Third Quarter Ended September 30, 2010</u>

Revenues for the third quarter ended September 30, 2010 decreased by 21% ($46,000) over revenues for the third quarter of 2009, primarily as a result of timing differences of $47,000 in recurring award show revenues that were recognized in the third quarter of 2009, but are to be recognized later in 2010 and in early 2011.

The loss for the third quarter of 2010 increased 80% ($436,000) compared to the third quarter of 2009. This increase was primarily due to increases in general and administrative expense of $233,000 (174%), salaries and consulting expense of $136,000 (36%), and interest expense of $48,000 on convertible debentures that were issued in the first half of 2010.

The increase in general and administrative expense for the third quarter ended September 30, 2010 was primarily due to recruiting expenses of $144,000 incurred in the period, which were nil in the same period in 2009. The company does not expect that recruiting expenses will continue to be incurred at this level in subsequent periods. General and administrative expense includes expenses related to the protection of the company's Canadian and U.S. intellectual property rights, which increased $35,000 (198%) in the third quarter ended September 30, 2010 compared to the same period in 2009. Other legal and accounting expenses increased by $24,000 (86%) in the quarter.

The increase in salaries and consulting expenses for the third quarter of 2010 was mainly a result of an increase in this expense in the general and administration department of $109,000 (72%), stemming from the addition of the new CEO and increased directors fees, plus the new US advertising department's initial personnel expenses of $34,000. Equity based compensation of $27,000 was included in the salaries and consulting expense for the third quarter of 2010, an increase of $18,000 (216%) from the same period in 2009.

EBITDA (Earnings before interest, taxes, depreciation and amortization) for the third quarter of 2010, calculated as the loss for the quarter before amortization, interest income and interest expense, decreased 115% ($420,000) compared to the third quarter of 2009. EBITDA is a non-GAAP measure that does not have any standardized meaning prescribed by GAAP and is therefore unlikely to be comparable to similar measures presented by other companies. The company provides this information at the request of investors and it is commonly used throughout the investment industry as a measure of performance. The nearest GAAP measure to EBITDA is the loss for the year. Interest expense was included in the composition of EBITDA for the period because convertible debentures issued by company during the period accrued interest. The following table is a reconciliation of EBITDA to the loss for the quarter ended September 30:

$	2010	2009
Loss for the period	(981,287)	(545,626)
Less: Interest earned	(2,071)	(945)
Add: Interest expense	47,748	-
Amortization of capital assets	18,766	22,370
Amortization of intangible assets	130,982	158,205
EBITDA	(785,862)	(365,996)

Marketing and promotion expense for the third quarter of 2010 was 44% ($21,000) higher compared to the same period in 2009 due to increased advertising and sponsorship expenses.

Total expenditures on technology development were $135,000 in the third quarter of 2010. Of these expenditures, $7,000 was expensed as technology development, $67,000 was included in salaries and consulting expense and $61,000 was capitalized as deferred development costs. Technology development expense for the third quarter of 2010 decreased $17,000 (70%) from the same period in 2009 primarily due to recognition of an investment tax credit of $17,000 in the third quarter of 2009. The company met the deferral criteria for development costs under generally accepted accounting principles as the company is generating increasing revenues from the product and technology it has developed.

5) Summary of Quarterly Results

The following table sets out quarterly results of the Corporation for the eight quarters prior to the effective date of this report. The information contained herein is drawn from the interim and annual financial statements of the Corporation.

Fiscal Year: **2010** **2009**

($)	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4 2008
Sales	171,729	196,534	185,290	175,613	218,211	204,842	181,386	138,023
Loss for the period	981,287	777,351	686,300	935,452	545,626	725,650	610,021	760,455
Loss per share (basic & diluted)	.01	.01	.01	.01	.01	.01	.01	.01

The revenues over the eight quarters show the results of increased use of DMDS by the music industry and music award shows. The trend in the losses over the eight quarters 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 quarter of 2010 includes $52,000 in interest expense for convertible debentures that were issued in the first half of 2010. The figures for the third quarter of 2010 show the effect of a timing difference in award show revenue recognition, recruiting expenses and interest on convertible debentures.

6) Liquidity and Capital Resources

Cash and cash equivalents at September 30, 2010 were $1,103,000 compared to $260,000 as at the December 31, 2009 fiscal year end. The main reason for this change was the cash flow from financing activities, which increased $2,606,000 in the first nine months of 2010 over the same period in 2009. Cash used in operating activities was $286,000 (16%) lower for the first nine months of 2010 compared to the same period in 2009. During the period the company invested $260,000 in deferred development costs and $45,000 in property plant and equipment.

During the first half of 2010 the company raised $818,000 gross proceeds from an issue of convertible debentures. See note 3 to the accompanying financial statements for a description of this transaction.

In August 2010 the company closed a private placement of 2,126.5 Units for gross proceeds of $2,126,500. Each Unit consists of 20,000 common shares and 10,000 common share purchase warrants at an issue price of $1,000 per Unit. The Warrants are exercisable until January 31, 2012, with each whole Warrant entitling the holder to purchase one common share at $0.10. See note 4 of the accompanying financial statements for a description of this transaction.

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, if it does not secure adequate funds it might not be able to pursue its marketing and business development strategies.

7) <u>Share Capital</u>

At September 30, 2010 YANGAROO had 118,047,615 common shares, 7,410,000 options, and 30,713,000 warrants outstanding. At December 31, 2009 the company had 75,517,615 common shares and 3,595,000 options and 750,000 warrants outstanding. The increase in the number of shares and warrants outstanding is due to the issuances of convertible debentures and Units described above. 1,250,000 of the company's outstanding common shares are not tradable currently as these are subject to the litigation described in note 8(b) of the financial statements.

8) <u>Disclosure Controls and Procedures, and Internal Control Over Financial Reporting</u>

The accompanying financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. 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, 2009, and have evaluated the design of the Company's ICFRs for the period ended December 31, 2009; 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, 2009; 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 itself 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 (formerly DMCT, 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.

9) <u>Off Balance Sheet Arrangements</u>

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

10) <u>International Financial Reporting Standards</u>

In February 2008, the Canadian Accounting Standards Board confirmed that publicly accountable entities would be required to adopt International Financial Reporting Standards ("IFRS"). The Company must prepare its interim and annual financial statements in accordance with IFRS for periods beginning on January 1, 2011. The Company has assigned responsibility for IFRS adoption and is currently studying the impacts of IFRS on the Company's accounting policies, information systems, internal controls over financial reporting and contractual arrangements and covenants.

The company has developed a three phase plan to adopt IFRS by January 1, 2011:

(i) This first phase involves the identification of differences between IFRS and existing Canadian GAAP, and an assessment of their applicability and the expected impact on the company.

The Audit Committee and management of the Company engaged the company's auditors to conduct an IFRS impact assessment in October 2010. The initial assessment of the process indicates that the most significant areas of difference applicable to the Company include treatment of stock-based compensation, intangible assets and the more extensive presentation and disclosure requirements under IFRS.

(ii) The second 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.

(iii) The final phase involves the actual implementation of IFRS standards. This phase will involve the finalization of IFRS conversion impacts, approval and implementation of accounting policies, implementation and testing of new processes, systems and controls, and the execution of detailed training where required.

As at the date of writing, the first phase of the company's IFRS plan was complete and Phase two was in progress. Phase three is expected to be completed by March 31, 2011.

Based on the impact assessment conducted to date the company expects the adoption of IFRS will:

- result in the use of the cost model for valuation of intangible assets, which is not expected to materially affect the reported values of capital or intangible assets or their amortization;
- have a manageable impact on internal reporting systems and processes;
- require more extensive presentation and disclosure requirements under IFRS, including note disclosure of management compensation;
- not materially affect the expense value assigned to options and warrants;
- not affect the classification of interest expense on the statement of cash flows;
- not affect the treatment of income taxes; and
- not materially affect the categories of expenses presented on the statement of operations.

YANGAROO Inc.

Interim Financial Statements

(unaudited)

September 30, 2010

NOTICE TO READER

The accompanying unaudited interim financial statements have been prepared by the company's management and the company's independent auditors have not performed a review of these financial statements.

Collins Barrow Toronto LLP

Licensed Public Accountants
Chartered Accountants

YANGAROO Inc.
Balance Sheet
As at September 30, 2010
(unaudited - see Notice to Reader)

	September 30, 2010	December 31, 2009 (audited)
Assets		
Current		
Cash and cash equivalents	**$ 1,103,314**	$ 259,603
Accounts receivable	**239,087**	193,581
Prepaid and sundry assets	**145,576**	196,204
	1,487,977	649,388
Property, plant and equipment	**113,948**	133,345
Patents	**133,499**	138,438
Investment in technology	**284,117**	356,209
Deferred development costs	**1,248,582**	1,343,238
	$ 3,268,123	$ 2,620,618
Liabilities		
Current		
Line of credit	**$ -**	$ 5,000
Accounts payable and accrued liabilities	**848,036**	538,666
Deferred revenue	**49,830**	17,134
	897,866	560,800
Convertible debentures (Note 3)	**632,355**	-
	1,530,221	560,800
Shareholders' Equity		
Capital stock (Note 4)	**22,346,946**	21,043,889
Contributed surplus (Note 6)	**1,473,465**	1,413,871
Warrants capital (Note 7)	**761,754**	31,883
Equity portion of convertible debentures (Note 3)	**30,500**	-
Deficit	**(22,874,763)**	(20,429,825)
	1,737,902	2,059,818
	$ 3,268,123	$ 2,620,618

Going Concern (Note 1)

Commitments and Contingencies (Note 8)

Approved by the Board "Scott Wambolt" Director (Signed) "John Heaven" Director (Signed)

See accompanying notes

YANGAROO Inc.
Interim Statement of Operations and Deficit
Period Ended September 30
(unaudited - see Notice to Reader)

	Nine Months Ended September 30		Three Months Ended September 30	
	2010	2009	**2010**	2009
Revenue	**$ 553,553**	$ 604,439	**$ 171,729**	$ 218,211
Expenses				
Salaries and consulting	**1,274,239**	1,207,693	**514,006**	378,083
Marketing and promotion	**169,878**	163,798	**68,985**	47,741
General and administrative	**902,930**	629,282	**367,353**	133,949
Technology development	**56,956**	56,181	**7,247**	24,434
Amortization of intangibles	**433,346**	373,264	**130,982**	158,205
Amortization of capital assets	**64,240**	65,563	**18,766**	22,370
	2,901,589	2,495,781	**1,107,339**	764,782
Loss before the undernoted item	**(2,348,036)**	(1,891,342)	**(935,610)**	(546,571)
Other income (expenses)				
Interest income	**2,854**	10,044	**2,071**	945
Interest expense	**(99,756)**	-	**(47,748)**	-
	(96,902)	10,044	**(45,677)**	945
Net loss	**(2,444,938)**	(1,881,298)	**(981,287)**	(545,626)
Deficit, beginning of period	**(20,429,825)**	(17,613,074)	**(21,893,476)**	(18,948,746)
Deficit, end of period	**$(22,874,763)**	$(19,494,372)	**$(22,874,763)**	$(19,494,372)
Loss per share				
Basic and diluted	**$ (0.03)**	$ (0.02)	**$ (0.01)**	$ (0.01)
Weighted average number of common shares outstanding				
Basic and diluted	**80,970,179**	75,517,615	**91,697,506**	75,517,615

See accompanying notes

YANGAROO Inc.
Statement of Cash Flows
Period Ended September 30
(unaudited - see Notice to Reader)

	Nine Months Ended September 30		Three Months Ended September 30	
	2010	2009	**2010**	2009
Cash provided by (used in)				
Operations				
Net loss	**$ (2,444,938)**	$ (1,881,298)	**$ (981,287)**	$ (545,626)
Items not affecting cash				
Amortization	**497,586**	438,827	**149,748**	180,575
Stock-based compensation	**59,594**	21,112	**26,773**	8,464
Gain on disposal of capital assets	**-**	(762)	-	(496)
Accretion interest	**49,084**	-	**23,006**	-
Warrants issued	**20,625**	-	**20,625**	-
	(1,818,049)	(1,422,121)	**(761,135)**	(357,083)
Net changes in non-cash working capital				
Accounts receivable	**(45,506)**	(128,970)	**(70,321)**	29,627
Prepaids and sundry assets	**50,628**	(33,368)	**60,034**	36,987
Accounts payable and accrued liabilities	**309,371**	(173,845)	**70,815**	(98,721)
Deferred revenue	**32,696**	1,779	**31,653**	(3,295)
	(1,470,860)	(1,756,525)	**(668,954)**	(392,485)
Investing				
Purchase of capital assets	**(44,843)**	(52,722)	**(28,981)**	(19,307)
Patents	**(1,395)**	(40,144)	**(1,312)**	(23,480)
Deferred development costs	**(260,265)**	(414,623)	**(60,480)**	(125,309)
Proceeds from disposition of property, plant and equipment	**-**	1,129	-	750
	(306,503)	**(506,360)**	**(90,773)**	**(167,346)**
Financing				
Issuance of convertible debentures, net of issue costs	**669,753**	-	**-**	-
Line of credit (repayment)	**(5,000)**	15,000	-	10,000
Issuance of common shares, net of issue costs	**1,956,321**	-	**1,437,321**	-
	2,621,074	**15,000**	**1,437,321**	**10,000**
Net change in cash	**843,711**	(2,247,885)	**677,594**	(549,831)
Cash, beginning of period	**259,603**	3,030,099	**425,720**	1,332,045
Cash, end of period	**$ 1,103,314**	$ 782,214	**$ 1,103,314**	$ 782,214

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 was 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 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 during the nine months ended September 30, 2010, the Company raised gross proceeds of $818,000 (see Note 3) by way of convertible debentures. In addition, the Company has raised gross proceeds of $2,126,500 by way of private placement. These financings are expected to fund the Company through the end of the fiscal year.

2. SIGNIFICANT ACCOUNTING POLICIES

The interim financial statements are prepared in accordance with Canadian generally accepted accounting principles and follow the same accounting policies and methods of their application as the most recent audited financial statements for the year ended December 31, 2009, except for the additional significant accounting policy disclosed below. These financial statements should be read in conjunction with those audited financial statements.

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.

3. CONVERTIBLE DEBENTURES

On March 22, 2010, the Company raised by way of convertible debentures (the "Debentures") 663 Units at $1,000 per Unit for gross proceeds of $663,000. 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.

3. CONVERTIBLE DEBENTURES (Cont'd)

On April 12, 2010 the Company raised an additional $155,000 by issuing 155 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 $68,581. 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 $39,189 was recorded as the equity portion of convertible debentures and $29,392 was allocated to the warrants. The Company incurred costs of $148,247 and issued agent warrants with a value of $33,106 (see Note 5) in connection with issuing the convertible debt. Of the total costs, $166,148 has been allocated to the liability component, $8,689 has been allocated to the equity component and $6,516 was allocated to warrants. The discount on the debt results in an effective interest rate on the liability of approximately 32.48%.

4. CAPITAL STOCK

Authorized

an unlimited number of common shares.

Issued and outstanding

	Number of Shares	Value
Balance, January 1, 2010	**75,517,615**	**$ 21,043,889**
Issued for cash [(a)]	42,530,000	1,876,361
Less: Proceeds allocated to warrants [(a)]	-	(573,304)
Balance, September 30, 2010	**118,047,615**	**$ 22,346,946**

(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 $250,139 have been netted against the proceeds. Included in share issuance costs is $79,960 representing the value of 2,055,000 warrants issued to agents in connection with the private placement.

5. STOCK OPTIONS AND WARRANTS

(a) Stock Options

The Company had the following stock options outstanding at September 30, 2010:

Number of Options	Exercise Price	Expiry Date
75,000	$ 0.25	November 22, 2010
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	$ 0.07	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
7,410,000		

(b) Warrants

The Company had the following warrants outstanding at September 30, 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 (see Note 3).

(ii) These warrants were issued to agents in connection with the issuance of convertible debentures (see Note 3). 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 1.6% and (IV) an expected life of 2 years.

5. STOCK OPTIONS AND WARRANTS (Cont'd)

(b) Warrants (Cont'd)

(iii) These warrants were issued for services related to digital media workflow solutions. The warrants will become exercisable after various phases of digital media workflow solution are completed. During the period ended September 30, 2010, the remaining 375,000 warrants became exercisable.

(iv) These warrants were issued as part of the convertible debenture financing that closed on April 12, 2010 (see Note 3).

(v) These warrants were issued as part of the private placement of units disclosed in Note 4(a). 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 disclosed in Note 4(a). 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.

6. CONTRIBUTED SURPLUS

	September 30, 2010	December 31, 2009 (audited)
Contributed surplus beginning of year	**$ 1,413,871**	$ 868,384
Expiry of warrants	**-**	505,428
Stock-based compensation expense	**59,594**	40,059
	$ 1,473,465	$ 1,413,871

7. WARRANT CAPITAL

	September 30, 2010	December 31, 2009 (audited)
Warrant capital beginning of year	**$ 31,883**	$ 505,428
Value of warrants issued in the year	**20,625**	31,883
Value of agent warrants issued in the period (Notes 3, 4 and 5)	**33,106**	-
Value allocated to warrants issued in conjunction with convertible debentures, net of issuance costs (Note 3)	**22,876**	-
Value allocated to warrants issued in conjunction with private placement (Note 4)	**573,304**	-
Value of agent warrants issued in the period (Note 4)	**79,960**	-
Value of warrants expired in the year	**-**	(505,428)
	$ 761,754	$ 31,883

8. 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 Digital Media Distribution System ("DMDS"). 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.

8. COMMITMENTS AND CONTINGENCIES (Cont'd)

(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 counter claim seeking $15 million in damages for infringement from the competitor and its partners. Examinations for discovery were conducted in 2007 into 2008 followed by motion appearances before the Court seeking orders compelling answers to questions refused. The Company was successful in obtaining a number of rulings in its favour including a ruling requiring the competitor to produce its software source code on a strict confidential basis for review by the Company's experts. The second round of examinations for discovery are complete, and are pending further answers due December 17, 2010 and any follow up questions to be completed by March 15, 2011. A pre-trial conference is to be filed no later than December 31, 2010.

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. On June 4, 2010, the competitor brought a summary judgement motion in respect of the Company's counterclaim. The motion was heard on October 27, 2010 wherein the judge reserved and has yet to issue his order.

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 2,407,774, 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. The Defendants filed a motion for summary judgment claiming that because certain steps of their method are performed outside of the United States, the Company's claim should be dismissed. On June 7, 2010, the U.S. District Court for the Eastern District of Wisconsin granted the competitor summary judgment of non-infringement, finding that the Defendant's allegedly infringing conduct is beyond the territorial reach of the United States Patent Law on the grounds that its servers were located outside the United States and that the patented claim is one of distributing content, not manufacturing the content. The Company is currently appealing that ruling. The Court awarded the Defendant court costs in the amount of $1,831. The Defendant filed a motion with the Court requesting attorney fees in the amount of $172,759 which the court has denied.

8. COMMITMENTS AND CONTINGENCIES(Cont'd)

(c) Patent Infringement (Cont'd)

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

9. CAPITAL RISK MANAGEMENT

The Company includes equity, comprised of issued capital stock, warrant capital, contributed surplus, equity component of convertible debentures, share subscription proceeds received in advance 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 period ended September 30, 2010.

10. 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 September 30, 2010 are as follows:

		USD$
Accounts receivable	$	71,000
Accounts payable and accrued liabilities	$	129,000

10. FINANCIAL RISK MANAGEMENT (Cont'd)

(a) Market Risk: (Cont'd)

(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 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 September 30, 2010, approximately 24% (December 31, 2009 - 22%) of accounts receivable and 26% (December 31, 2009 - 23%) of revenue are from two customers.

(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 September 30, 2010, the Company has accounts payable and accrued liabilities of $848,036 due within 12 months and has cash and cash equivalents and accounts receivable of $1,342,401 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.

DMDS

Digital Media Distribution System