YANGAROO Inc.

Unaudited Interim Financial Statements

For the Three Months and Six Months Ended June 30, 2011

(Expressed in Canadian Dollars)

Notice of No Auditor Review of Interim Financial Statements

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements; they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The management of YANGAROO Inc. is responsible for the preparation of the accompanying unaudited interim financial statements. The unaudited interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and are considered by management to present fairly the financial position, operating results and cash flows of the Company.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor. These unaudited financial statements include all adjustments, consisting of normal and recurring items, that management considers necessary for a fair presentation of the financial position, results of operations and cash flows.

"Scott Wambolt"
Scott Wambolt
Chief Executive Officer

"Michael Galloro"
Michael Galloro
Chief Financial Officer

August 18, 2011

YANGAROO Inc.

Unaudited Interim Statement of Financial Position
As at June 30, 2011
(Expressed in Canadian dollars)

	June 30, 2011	December 31 2010
		(Note 14)
Assets		
Current		
Cash and cash equivalents	**$ 1,343,146**	$ 202,604
Accounts receivable	**189,431**	162,752
Prepaid and sundry assets	**177,579**	176,397
	1,710,156	541,753
Property, plant and equipment	**109,224**	140,322
	$1,819,380	$ 682,075
Liabilities		
Current		
Operating line of credit (note 5)	**$ -**	$ 20,000
Trade and other payables (note 6)	**586,897**	833,410
Deferred revenue	**10,630**	33,572
Debentures (note 7)	**4,487,912**	-
	5,085,439	886,982
Debentures (note 7)	**-**	655,202
	5,085,439	1,542,184
Shareholders' Deficiency		
Share capital (note 8)	**23,285,199**	22,338,694
Contributed surplus	**1,703,678**	1,541,896
Warrant capital	**873,455**	761,298
Equity portion of convertible debentures	**-**	29,890
Deficit	**(29,128,391)**	(25,531,887)
	(3,266,059)	(860,109)
	$ 1,819,380	$ 682,075

Going concern (note 1)
Commitment and contingencies (note 10)
Subsequent event (note 13)

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

See accompanying notes, which are an integral part of these financial statements

YANGAROO Inc.

Unaudited Interim Statement of Comprehensive Income
For the period ended June 30
(Expressed in Canadian dollars)

	Six Months Ended June 30		Three Months Ended June 30	
	2011	2010	**2011**	2010
Revenue	**$ 583,775**	$ 381,824	**$ 307,976**	$ 196,534
Expenses				
Salaries and consulting	**1,338,205**	769,486	**644,375**	375,021
Marketing and promotion	**69,918**	100,893	**40,114**	56,217
General and administrative	**295,675**	535,577	**118,722**	302,989
Technology development	**45,623**	49,709	**22,373**	22,843
Settlement of lawsuit	**600,000**	-	**-**	-
Amortization of capital assets	**44,049**	45,474	**18,457**	21,942
Amortization of intangibles	**-**	302,364	**-**	144,845
	2,393,470	1,803,503	**844,041**	923,857
Loss before the undernoted item	**(1,809,695)**	(1,421,679)	**(536,065)**	(727,323)
Other income (expense)				
Interest income	**883**	783	**509**	379
Interest expense	**(197,724)**	(52,008)	**(114,409)**	(52,008)
Financing costs	**(1,399,755)**	-	**(1,399,755)**	-
Debt extinguishment loss	**(190,213)**	-	**(190,213)**	-
	(1,786,809)	(51,225)	**(1,703,868)**	(51,629)
Net loss	**$ (3,596,504)**	$ (1,472,904)	**$ (2,239,933)**	$ (778,952)

Loss per share				
Basic and diluted	**$ (0.03)**	$ (0.02)	**$ (0.02)**	$ (0.01)
Weighted average number of common shares	**118,645,251**	75,517,615	**119,236,319**	75,517,615

See accompanying notes, which are an integral part of these financial statements

YANGAROO Inc.

Unaudited Interim Statement of Changes in Equity
For the period ended June 30
(Expressed in Canadian dollars)

	Share capital	Warrants	Contributed surplus	Equity portion of convertible debentures	Share subscription proceeds received in advance	Deficit	**Total**
Balance at January 1, 2010	$ 21,043,889	$ 31,883	$ 1,425,436	$ -	$ -	$ (20,441,390)	**$ 2,059,818**
Issuance of common shares	-	-	-	-	519,000	-	**519,000**
Issuance of warrants	-	55,982	-	-	-	-	**55,982**
Share-based payments	-	-	42,074	-	-	-	**42,072**
Equity portion of convertible debenture	-	-	-	30,500	-	-	**30,500**
Loss for the period	-	-	-	-	-	(1,472,904)	**(1,472,904)**
Balance at June 30, 2010	21,043,889	87,865	1,467,510	30,500	519,000	(21,914,294)	**1,234,470**
Balance at January 1, 2011	22,338,694	761,298	1,541,896	29,890	-	(25,531,887)	**(860,109)**
Issuance of common shares	946,505	-	-	-	-	-	**946,505**
Issuance of warrants	-	112,157	-	-	-	-	**112,157**
Share-based payments	-	-	118,100	-	-	-	**118,100**
Equity portion of convertible debenture	-	-	-	69,693	-	-	**69,693**
Debt extinguishment	-	-	43,682	(99,583)	-	-	**(55,901)**
Loss for the period	-	-	-	-	-	(3,596,504)	**(3,596,504)**
Balance at June 30, 2011	$ 23,285,199	$ 873,455	$ 1,703,678	$ -	$ -	$ (29,128,391)	**$ (3,266,059)**

See accompanying notes, which are an integral part of these financial statements

YANGAROO Inc.

Unaudited Interim Statement of Cash Flows
For the period ended June 30
(Expressed in Canadian dollars)

	Six Months Ended June 30	
	2011	2010
Cash flow from operating activities		
Net comprehensive loss for the period	**$ (3,596,504)**	$ (1,472,904)
Adjustment for:		
Amortization	**44,049**	347,838
Accretion interest	**134,822**	26,078
Financing costs	**1,399,755**	-
Debt extinguishment loss	**190,213**	-
Share-based payments	**118,100**	42,074
Change in accounts receivable	**(27,018)**	24,815
Change in prepaid and sundry assets	**(844)**	(9,406)
Change in trade and other payables	**(201,601)**	238,556
Change in deferred revenue	**(22,941)**	1,043
Net cash used in operating activities	**(1,961,969)**	(801,906)
Cash flow from investing activities		
Acquisition of property, plant and equipment	**(12,951)**	(15,862)
Investment in patents	**-**	(83)
Investment in technology (net of tax credit)	**-**	(199,785)
Net cash used in investing activities	**(12,951)**	(215,730)
Cash flow from financing		
Proceeds from the issuance of debentures, net of issuance costs	**3,135,462**	669,753
Share subscription proceeds received in advance	**-**	519,000
Operating loan	**(20,000)**	(5,000)
Net cash received from financing activities	**3,115,462**	1,183,753
Net increase / (decrease) in cash and cash equivalents	**1,140,542**	166,117
Cash and cash equivalents at January 1	**202,604**	259,603
Cash and cash equivalents at June 30	**$ 1,343,146**	$ 425,720

See accompanying notes, which are an integral part of these financial statements

1. Incorporation and Nature of Operations

YANGAROO Inc. (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. YANGAROO trades on the TSX Venture Exchange (TSX-V) under the symbol YOO and in the U.S. under TCBB: YOOIF. The head office, principal and registered address of the Company is located at 18 Mowat Avenue, Toronto, ON M6K 3E8.

YANGAROO Inc. 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. 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.

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 in fiscal 2011. These proceeds are used to fund operations of the Company.

The interim financial statements of the Company for the three and six month period ended June 30, 2011 were approved by the Board of Directors on August 18, 2011.

2. Basis of Preparation

(a) Statement of Compliance

These interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and in accordance with International Accounting Standards ("IAS") 34, "Interim Financial Reporting". These unaudited interim financial statements are for part of the period covered by the Company's first annual financial statements prepared under IFRS. The interim financial statements do not include all of the information required for full annual financial statements, and should be read in conjunction with the unaudited consolidated interim financial statements for the three months ended March 31, 2011, as they follow the same accounting policies and methods of application, unless otherwise indicated.

The Company adopted IFRS in accordance with IFRS 1 First-time Adoption of International Financial Reporting Standards ("IFRS 1") with a transition date to IFRS of January 1, 2010. Consequently, the comparative figures for 2010 and the Company's statement of financial position as at January 1, 2010 have been restated from accounting principles generally accepted in Canada ("Canadian GAAP") to comply with IFRS.

2. Basis of Preparation (continued)

(b) Basis of Measurement

The Company's interim financial statements have been prepared on the historical cost basis. Where there are assets and liabilities calculated on a different basis, this fact is disclosed in the relevant accounting policy.

(c) Functional and presentation currency

These financial statements are presented in Canadian dollars, which is the Company's functional currency.

(d) Use of estimates and judgements

The preparation of the financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the interim financial statements are noted below with further details of the assumptions in the following notes:

(i) Share-based payments

Charges for share-based payments are based on the fair value at the date of the award. The shares are valued using Black-Scholes; inputs to the model include assumptions on share price volatility, discount rates and expected life outstanding.

(ii) Income taxes

Tax interpretations, regulations and legislation in the jurisdiction in which the Company operates are subject to change. As such, income taxes are subject to measurement uncertainty. Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realised from future taxable earnings.

3. Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these interim financial statements as at and for the three and six months ended June 30, 2011, unless otherwise indicated.

(a) Property, plant and equipment

Amortization is calculated as the cost of the asset less its residual value.

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the assets.

The estimated useful lives for the current and comparative periods are 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

This most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset.

Estimates for amortization methods, useful lives and residual values are reviewed at each reporting period-end and adjusted if appropriate.

(b) Share based payments

The grant date fair value of options awarded to employees, directors, and service providers is measured using the Black-Scholes option pricing model and recognised in the statement comprehensive income, with corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of options that vest. Upon exercise of the option, consideration received, together with the amount previously recognised in contributed surplus, is recorded as an increase to share capital.

(c) Contingent liability

A contingent liability is a possible obligation that arises from past events and of which the existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company; or a present obligation that arises from past events (and therefore exists), but is not recognized because it is not probable that a transfer or use of assets, provision of services or any other transfer of economic benefits will be required to settle the obligation, or the amount of the obligation cannot be estimated reliably.

3. Significant Accounting Policies (continued)

(d) New standards and interpretations not yet adopted

The Company has reviewed new and revised accounting pronouncements that have been issued but are not yet effective and determined that the following may have an impact on the Company:

- Earnings per share (replacement of IAS 3)
- First-time adoption of IFRS (amendment of IFRS 1)
- Group cash-settled share-based payment transactions (amendment of IFRS 2)
- Management commentary
- IFRS 9, “Financial Instruments”

As of January 1, 2013, the Company will be required to adopt IFRS 9, “Financial Instruments”, which is the result of the first phase of the IASB’s project to replace IAS 39, “Financial Instruments: Recognition and Measurement”. The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortisation cost and fair value. The extent of the impact has not been determined.

Issued but not effective would be:

- Financial statement presentation (amendment to IAS 1)
- Leases (replacement of IAS 17)
- Liabilities and equity (replacement of IAS 32) and
- Revenue recognition (replacement of IAS 11 and IAS 18)

4. Determination of Fair Value

A number of the Company’s accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Cash and cash equivalents, trade and other receivables, trade and other payables, and loans and borrowings.

The fair value of cash and cash equivalents, trade and other receivables, trade and other payables and loans and borrowings is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At June 30, 2011, December 31, 2010 and January 1, 2010, the fair value of these balances approximated their carrying value due to their short term to maturity, or in the case of the line of credit, the fair value approximates its carrying value as it bears interest at floating rates.

(Expressed in Canadian dollars)

4. Determination of Fair Value (continued)

(b) The fair value of stock options and warrants are measured using a Black-Scholes, option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option and warrant holder behaviour) and the risk-free interest rate (based on government bonds).

The following tables provide fair value measurement information for financial assets and liabilities as of June 30, 2011 and December 31, 2010. The carrying value of cash and cash equivalents, trade and other receivables, trade and other payables and loans and borrowings included in the interim financial position approximate fair value due to the short term nature of those instruments or the indexed rate of interest on the long-term debt. These assets and liabilities except cash and cash equivalents are not included in the following tables.

			Fair value measurements using		
June 30, 2011	Carrying amount	Fair value	Quoted prices in active market (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Financial assets					
Cash and cash equivalents	$ 1,343,146	$ 1,343,146	$1,343,146	$ -	$ -

			Fair value measurements using		
December 31, 2010	Carrying amount	Fair value	Quoted prices in active market (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Financial assets					
Cash and cash equivalents	$ 202,604	$ 202,604	$ 202,604	$ -	$ -
Financial liabilities					
Loans and borrowings	$ 20,000	$ 20,000	$ -	$ -	$ 20,000

Level 1 fair value measurements are based on unadjusted quoted market prices. Cash and cash equivalents have been classified as level 1.

Level 2 fair value measurements are based on valuation models and techniques where the significant inputs are derived from quoted indices.

Level 3 fair value measurements are those with inputs for the asset or liability that are not based on observable market data.

(Expressed in Canadian dollars)

5. 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. At the quarter ended June 30, 2011, the Company had a balance outstanding of $ Nil (December 31, 2010 - $20,000) on this line of credit.

6. Trade and Other Payables

		June 30, 2011		December 31, 2010
Trade payables	**$**	**352,065**	$	520,417
Non-trade payables and accrued expenses		**234,832**		312,993
	$	**586,897**	$	833,410

7. Debenture

On June 23, 2011, the Company issued $2,500,000 principal amount of senior secured 18% non-convertible debentures (the “New Debenture). In addition, with the prior requisite approval of the debenture holders, the Company amended its previously issued $818,000 principal amount 12% convertible debentures maturing March 31, 2012 (the “March 2012 Debentures”) and $1,125,000 principal amount convertible debentures maturing July 31, 2012 to reflect the terms of the New Debentures (the “July 2012 Debentures” and together with the March 2012 Debentures, the “Amended Debentures”). $44,911 of interest that accrued on the March 2012 Debentures was added to the principal amount of the amended March 2012 Debentures.

Pursuant to their terms, the New Debentures and the Amended Debentures (collectively, the “Debentures”) are, among other things, non-convertible and repayable upon demand, after the first anniversary of their issuance, subject to the requisite determination of the holders of the outstanding Debentures to make demand for repayment. In addition, in the event of an asset sale in excess of $3,000,000, the Company would be required to offer to repurchase a minimum of 50% of the outstanding Debentures, plus all accrued and unpaid interest due, at a price equal to 100%. Debenture holders would also have a right of first refusal to participate in future offerings by the Company, subject to the satisfaction of certain conditions. In turn, the Company may redeem the Debentures in the event that it has first raised a minimum of $4 million of “net new cash”, which would include the proceeds raised from the issuance of the New Debentures but would exclude, among other things, the proceeds from the repayment of any debentures that, in turn, are used to fund the purchase of new securities of the Company.

In accordance with the rules of the TSX Venture Exchange, the Company also issued an aggregate of 13,521,504 “Bonus” common shares to purchasers of the New Debentures and holders of the previously issued debentures.

The securities issued and issuable pursuant to the transaction are subject to a hold period expiring October 24, 2011.

(Expressed in Canadian dollars)

8. Share Capital

Authorized an unlimited number of common shares

Issued and outstanding:

	Number of shares	Value
Balance at January 1, 2010 and June 30, 2010	75,517,615	$ 21,043,889
Issuance of common shares	42,530,000	1,294,805
Balance at December 31, 2010 and March 31, 2011	118,047,615	22,338,694
Issuance of “Bonus” common shares to purchasers of the newly issued debentures and holders of the previously issued convertible debentures.	13,521,504	946,505
Balance at June 30, 2011	131,569,119	$ 23,285,199

9. Stock Options and Warrants

(a) Stock Options

The Company had the following stock options outstanding at June 30, 2011:

Number of options	Exercise price	Expiry date
40,000	$0.20	August 16, 2011
95,000	$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
75,000	$0.13	November 27, 2012
100,000	$0.14	January 9, 2013
250,000	$0.22	April 18, 2013
360,000	$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
500,000	$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
1,735,000	$0.10	February 11, 2016
8,925,000	$0.12	Weighted-average exercise price

(Expressed in Canadian dollars)

9. Stock Options and Warrants (continued)

(b) Warrants

The Company had the following warrants outstanding at June 30, 2011:

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
600,000	(vii)	$0.10	February 11, 2013
2,066,000	(viii)	$0.10	June 23, 2013
33,379,000			

(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 will become exercisable after various phases of digital media workflow solution are 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.

(vii) 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 129%; (III) a risk free interest rate of 1.90% and (IV) an expected life of 2 years.

(viii) These warrants were issued to agents in connection with the issuance of 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 121%; (III) a risk free rate of 1.45%; and (IV) an expected life of 2 years.

10. 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. 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 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 motions and any follow up questions.

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.

10. Commitments and Contingencies (continued)

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.

On June 24, 2011, the Company and its competitor resolved all litigation between the two parties. In consideration of the settlement, the Company agreed to pay its competitor a lump sum amount totalling $600,000 and granted the competitor certain intellectual property rights relating to the two patents held by the Company that were the subject matter of the dispute. As part of the settlement, neither party will pursue legal fees, court costs or royalties pursuant to the above mentioned disputes. The payment was made in the period.

11. Capital Risk Management

The Company includes equity, comprised of issued capital stock, warrant capital, contributed surplus 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 three month period ended June 30, 2011.

12. 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.

(Expressed in Canadian dollars)

12. Financial Risk Management (continued)

(a) Market risk:

(i) Currency risk:

The Company operates internationally and is exposed to foreign exchange risk from various currencies, primarily United States dollars and Australian 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 June 30, 2011 are as follows:

	USD$	AUD$
Accounts receivable	$ 64,500	$ 5,700
Accounts payable and accrued liabilities	$ 174,000	$ -

(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 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 June 30, 2011, approximately 29% (December 31, 2010 - 27%) of accounts receivable and 17% (December 31, 2010 - 24%) of revenue are from two customers (2010 - two customers).

12. Financial Risk Management (continued)

(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 June 30, 2011, the Company has trade and other payables of approximately $587,000 due within 12 months and has cash and cash equivalents and accounts receivable of $1,533,000 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, amounts receivable, accounts payable and accrued liabilities approximate fair values due to the relatively short term maturities of these instruments.

13. Subsequent Events

Subsequent to June 30, 2011, the Board of Directors approved the granting of stock options totalling 2,879,761. The options were granted to particular members of management, officers and directors.

14. Reconciliation from Canadian GAAP to IFRS

The Company's accounting policies under IFRS differ from those followed under previous GAAP. These accounting policies have been applied for the six months ended June 30, 2011, as well as to the opening statement of financial position on the transition date, January 1, 2010, the comparative information for the three months ended June 30, 2010 and the comparative information for the year ended December 31, 2010.

The adjustments arising from the application of IFRS to amounts on the statement of financial position on the transition date and on transactions prior to that date, were recognized as an adjustment to the Company's opening deficit on the statement of financial position when appropriate.,

On transition to IFRS on January 1, 2010 the Company used certain exemptions allowed under, IFRS 1 "First Time Adoption of International Reporting Standards". The exemptions used were:

Fair value or revaluation as deemed cost – IFRS 1 allows the Company to measure certain assets of property, plant and equipment at fair value at the Transition Date or revalue amounts previously determined under GAAP. The Company has elected to use the carrying value as determined under IFRS as the deemed costs as January 31, 2011.

Share based compensation – IFRS1 allows an entity an exemption on IFRS 2, "Share-Based Payments" to equity instruments which vested before the Company's transition date to IFRS. The Company has elected to apply IFRS 2 only to stock options that remain unvested at transition date.

The adoption of IFRS did not significantly affect our cash flows compared to GAAP. There were no changes to over all cash flows.

(Expressed in Canadian dollars)

14. Reconciliation from Canadian GAAP to IFRS (continued)

Statement of Financial Position

At June 30, 2010	Canadian GAAP	Effect of transition to IFRS	IFRS
Assets			
Current assets			
Accounts receivable	$ 168,766	$ -	$ 168,766
Prepaid and sundry assets	205,610	-	205,610
Cash and cash equivalents	425,720	-	425,720
	800,096	-	800,096
Non-current assets			
Property, plant and equipment	103,733	-	103,733
Patents	134,283	-	134,283
Investment in Technology	308,148	-	308,148
Deferred Development Costs	1,292,957	-	1,292,957
	1,839,121	-	1,839,121
	$ 2,639,217	$ -	$ 2,639,217
Liabilities			
Current liabilities			
Trade and other payables	$ 777,221	$ -	$ 777,221
Deferred revenue	18,177	-	18,177
	795,398	-	795,398
Non-current liabilities			
Convertible debentures	609,349	-	609,349
	1,404,747	-	1,404,747
Shareholders' Deficiency			
Share capital issued and outstanding	21,043,889	-	21,043,889
Warrants issued and outstanding	87,865	-	87,865
Equity portion of convertible debentures	30,500	-	30,500
Reserves: contributed surplus	1,446,692	20,818	1,467,510
Share subscription proceeds received in advance	519,000	-	519,000
Retained earnings (deficit)	(21,893,476)	(20,818)	(21,914,294)
	1,234,470	-	1,234,470
	$ 2,639,217	$ -	$ 2,639,217

(Expressed in Canadian dollars)

14. Reconciliation from Canadian GAAP to IFRS (continued)

Statement of Comprehensive Income

	Six Months Ended June 30, 2010			Three Months Ended June 30, 2010		
	Canadian GAAP	Effect of transition to IFRS	IFRS	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue	$ 381,824	$ -	$ 381,824	$ 196,534	$ -	$ 196,534
Expenses						
Salaries and consulting	760,233	9,253	769,486	373,420	1,601	375,021
Marketing and promotion	100,893	-	100,893	56,217	-	56,217
General and administrative	535,577	-	535,577	302,989	-	302,989
Technology development	49,709	-	49,709	22,843	-	22,843
Amortization of intangibles	302,364	-	302,364	144,845	-	144,845
Amortization of property, plant and equipment	45,474	-	45,474	21,942	-	21,942
	1,794,250	9,253	1,803,503	922,256	1,601	923,857
	(1,412,426)	(9,253)	(1,421,679)	(725,722)	(1,601)	(727,323)
Finance income (expenses)						
Interest income	783	-	783	379	-	379
Interest expense	(52,008)		(52,008)	(52,008)		(52,008)
	(51,225)		(51,225)	(51,629)		(51,629)
Net loss and comprehensive loss	$ (1,463,651)	$ (9,253)	$ (1,472,904)	$ (777,351)	$ (1,601)	$ (778,952)