YANGAROO Inc.

Unaudited Condensed Interim Financial Statements

For the Three and Nine Months Ended September 30, 2012

(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 condensed 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 condensed interim financial statements. The unaudited condensed 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 unaudited condensed interim 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 condensed interim 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.

"Gary Moss"
Gary Moss
Chief Executive Officer

"Michael Galloro"
Michael Galloro
Chief Financial Officer

November 22, 2012

YANGAROO Inc.

Unaudited Condensed Interim Statements of Financial Position
As at
(Expressed in Canadian dollars)

		September 30 2012		December 31 2011 (audited)
Assets				
Current				
Cash and cash equivalents	**$**	**46,222**	$	316,717
Accounts receivable		**623,669**		280,469
Prepaid and sundry assets		**256,676**		230,270
		926,567		827,456
Property and equipment		**86,889**		123,352
	$	**1,013,456**	$	950,808
Liabilities				
Current				
Trade and other payables (note 5)	**$**	**1,064,877**	$	642,664
Accrued interest on debentures (note 6)		**1,105,448**		423,479
Deferred revenue		**2,502**		16,267
Debentures (note 6)		**4,487,912**		4,108,380
Finance lease obligation		**6,849**		6,245
		6,667,588		5,197,035
Finance lease obligation		**8,436**		13,651
		6,676,024		5,210,686
Shareholders' Deficiency				
Share capital (note 7)		**23,445,249**		23,285,199
Warrant capital (note 10)		**315,929**		873,455
Contributed surplus		**2,505,909**		1,726,650
Share proceeds received in advance (note 8)		**50,000**		-
Deficit		**(31,979,655)**		(30,145,182)
		(5,662,568)		(4,259,878)
	$	**1,013,456**	$	950,808

Going concern (note 2(c))
Commitments and contingencies (note 12)
Subsequent event (note 14)

Approved by the Board **"Cliff Hunt"** Director **"Howard Atkinson"** Director

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

YANGAROO Inc.

Unaudited Condensed Interim Statements of Comprehensive Loss
For the period ended September 30
(Expressed in Canadian dollars)

	Nine Months Ended		Three Months Ended	
	2012	**2011**	**2012**	**2011**
Revenue	**$ 1,928,934**	$ 994,135	**$ 752,760**	$ 410,360
Expenses				
Salaries and consulting (note 9)	**1,858,922**	2,069,795	**624,490**	731,590
Marketing and promotion	**145,564**	103,796	**55,543**	33,878
General and administrative	**598,910**	445,896	**260,694**	150,221
Technology development	**45,733**	40,432	**8,975**	(5,191)
Settlement of lawsuit (note 12(c))	**-**	600,000	**-**	-
Depreciation of property and equipment	**51,689**	62,139	**16,577**	18,090
	2,700,818	3,322,058	**966,279**	928,588
Loss from operations	**(771,884)**	(2,327,923)	**(213,519)**	(518,228)
Finance income (expenses)				
Interest income	**611**	2,588	**-**	1,705
Interest expense	**(1,063,200)**	(399,680)	**(240,454)**	(201,956)
Loss on extinguishment of debt	**-**	(1,589,968)	**-**	-
	(1,062,589)	(1,987,060)	**(240,454)**	(200,251)
Net loss and comprehensive loss	**$ (1,834,473)**	$ (4,314,983)	**$ (453,973)**	$ (718,479)

Loss per share (note 11)	**$ (0.01)**	$ (0.04)	**$ (0.003)**	$ (0.01)

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

YANGAROO Inc.

Unaudited Condensed Interim Statements of Changes in Equity
For the period ended September 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, 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	-	-	188,084	-	-	-	188,084
Equity portion of convertible debenture	-	-	-	69,693	-	-	69,693
Debt extinguishment	-	-	43,682	(99,583)	-	-	(55,901)
Loss for the period	-	-	-	-	-	(4,314,983)	(4,314,983)
Balance at September 30, 2011	23,285,199	873,455	1,773,662	-	-	(29,846,870)	(3,914,554)
Share-based payments	-	-	(47,012)	-	-	-	(47,012)
Loss for the period	-	-	-	-	-	(298,312)	(298,312)
Balance at December 31, 2011	23,285,199	873,455	1,726,650	-	-	(30,145,182)	(4,259,878)
					-		
Private placement (notes 7&8)	160,050	151,264	-	-	50,000	-	361,314
Expiry of warrants (note 10)	-	(708,790)	708,790	-	-	-	-
Share-based payments (note 9)	-	-	70,469	-	-	-	70,469
Loss for the period	-	-	-	-	-	(1,834,473)	(1,834,473)
Balance at September 30, 2012	**$ 23,445,249**	**$ 315,929**	**$ 2,505,909**	**$ -**	**$ 50,000**	**$ (31,979,655)**	**$ (5,662,568)**

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

YANGAROO Inc.

Unaudited Condensed Interim Statements of Cash Flows
For the nine months ended September 30
(Expressed in Canadian dollars)

	2012	2011
Cash flow from operating activities		
Cash flow used in operating activities:		
Net loss for the period	**$ (1,834,473)**	$ (4,314,983)
Items not affecting cash:		
Depreciation of property and equipment	**51,689**	62,139
Bad debt expense	**7,536**	-
Share-based payments	**70,469**	188,084
Accretion interest	**379,532**	134,822
Accrued interest on debentures	**681,969**	219,908
Loss of extinguishment of debt	**-**	1,589,968
Debentures issued for interest payment	**-**	44,911
Changes in non-cash operating working capital:		
Accounts receivable	**(350,736)**	(147,153)
Prepaid and sundry assets	**(26,406)**	28,754
Trade and other payables	**422,213**	(499,400)
Deferred revenue	**(13,765)**	(26,057)
Net cash used in operating activities	**(611,972)**	(2,719,007)
Cash flow from investing activities		
Acquisition of property and equipment	**(15,226)**	(40,643)
Net cash used in investing activities	**(15,226)**	(40,643)
Cash flow from financing activities		
Proceeds from issuance of common shares, net of issuance costs	**311,314**	-
Proceeds from issuance of debentures, net of issuance costs	**-**	3,135,462
Share subscription proceeds received in advance	**50,000**	-
Operating loan	**-**	(20,000)
Payment of finance lease obligation	**(4,611)**	-
Net cash received from financing activities	**356,703**	3,115,462
Net increase / (decrease) in cash and cash equivalents	**(270,495)**	355,812
Cash and cash equivalents at January 1	**316,717**	202,604
Cash and cash equivalents at September 30	**$ 46,222**	$ 558,416

Cash interest paid	**$ 2,328**	$ 729

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

1. Nature of Operations

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

YANGAROO Inc. 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 address of the Company's corporate office and principal place of business is 18 Mowat Avenue, Toronto, Ontario M6K 3E8.

2. Basis of Preparation

(a) Basis of Compliance

These unaudited condensed interim financial statements were prepared using the same accounting policies and methods as those used in the Company's audited financial statements for the year ended December 31, 2011. These unaudited condensed interim financial statements are in compliance with International Accounting Standard (IAS) 34, *Interim Financial Reporting.* Accordingly, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB), have been omitted. The preparation of these unaudited condensed interim financial statements in accordance with IAS 34 requires the use of certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements have been set out in note 3 of the Company's audited annual financial statements for the year ended December 31, 2011.

These unaudited condensed interim financial statements have been prepared on a historical cost basis. These statements should be read in conjunction with the audited financial statements for the year ended December 31, 2011. These statements were approved by the Board of Directors on November 22, 2012.

2. Basis of Preparation (continued)

(b) Basis of Measurement

The condensed unaudited interim financial statements are presented in Canadian dollars, which is also the Company's functional currency. The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies. The areas involving a higher degree of judgment of complexity, or areas where assumptions and estimates are significant to the condensed unaudited interim financial statements, are disclosed in the following notes:

(i) Share-based payments

Share-based payments which include stock options granted to employees, officers and directors and warrants to the extent that they are not measured at the fair value of the services received are based on the fair value at the date of the award. These share-based payments are valued using Black-Scholes option pricing model. The assumptions used on the inputs to the model are provided in the audited financial statements for the year ended December 31, 2011.

(ii) Impairment of intangible assets

The Company assesses the carrying value of long-lived assets each reporting period to determine whether any indication of impairment exists. The calculation of recoverable amount requires the use of estimates and assumptions such as discount rates and operational performance of the Company.

(c) Going Concern

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.

At September 30, 2012, the Company had negative working capital of $5,741,021 and deficit of $31,979,655. To date the Company has been successful raising capital. During the second quarter, the Company secured a private placement of equity units of a minimum of $1,250,000 and up to a maximum of $2,000,000. On August 31, 2012, the Company announced that the first phase of the private placement was closed, raising an aggregate gross proceeds of approximately $344,000, in respect of which 6,875,652 units were subscribed for at a price of $0.05 per unit.

The Company also fulfilled its obligations pursuant to the approval of the Debenture holders and amended all of the existing debentures, by extending the timeline for repayment for an additional 36 months, and reducing the interest rate payable on the outstanding indebtedness from 18% to 14% on October 3, 2012. The interest will accrue throughout the amended term and is payable with the redemption of the principal portion of the debenture (note 14).

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2. Basis of Preparation (continued)

(c) Going Concern (continued)

As of October 3, 2012, the Company closed its Private Placement and raised aggregate gross proceeds of $1,268,783 between Phase 1 and Phase 2. Common shares for the gross proceeds of $343,783 were issued on September 7, 2012 and common shares for the remaining amount, $925,000 was issued on October 3, 201 (note 14).

3. Significant Accounting Policies

The unaudited condensed interim financial statements are prepared in accordance with IFRS and follow the same accounting policies and methods of their application as the most recent audited financial statements for the year ended December 31, 2011. These unaudited condensed financial statements should be read in conjunction with those audited financial statements.

New standards and interpretations not yet adopted

The following accounting standards, amendments and interpretations have been issued but are not yet effective for the Company. Management is currently assessing the impact of the new standards on the Company's accounting policies and financial statement presentation.

- IFRS 7 *Financial Instruments: Disclosure* was amended by the IASB in December 2011 to provide additional information about offsetting of financial assets and financial liabilities. Additional disclosures will be required to enable users of financial statements to evaluate the effect or potential effect of netting arrangements on the entity's financial position. The amendments are effective for annual periods beginning on or after January 1, 2013.

- IFRS 9 *Financial Instruments* was issued by the IASB in October 2010 and will replace IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for annual periods beginning on or after January 1, 2015.

- IFRS 10 *Consolidated Financial Statements* was issued by the IASB in May 2011. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 replaces the consolidation requirements in SIC-12 *Consolidation—Special Purpose Entities* and IAS 27 *Consolidated and Separate Financial Statements* and is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

3. Significant Accounting Policies (continued)

- IFRS 11 *Joint Arrangements* was issued by the IASB in May 2011. IFRS 11 provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form. The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities. IFRS 11 supersedes IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly Controlled Entities - Non-Monetary Contributions by Venturers*, and is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

- IFRS 12 *Disclosure of Interests in Other Entities* was issued by the IASB in May 2011. IFRS 12 is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. IFRS 12 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

- IFRS 13 *Fair Value Measurement* was issued by the IASB in May 2011. IFRS 13 establishes new guidance on fair value measurement and disclosure requirements for IFRSs and US generally accepted accounting principles (GAAP). The guidance, set out in IFRS 13 and an update to Topic 820 in the FASB's Accounting Standards Codification (formerly referred to as SFAS 157), completes a major project of the boards' joint work to improve IFRSs and US GAAP and to bring about their convergence. The standard is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

- IAS 1 *Presentation of Financial Statements* was amended by the IASB in June 2011 in order to align the presentation of items in other comprehensive income with US GAAP standards. Items in other comprehensive income will be required to be presented in two categories: items that will be reclassified into profit or loss and those that will not be reclassified. The flexibility to present a statement of comprehensive income as one statement or two separate statements of profit and loss and other comprehensive income remains unchanged. The amendments to IAS 1 are effective for annual periods beginning on or after July 1, 2012.

4. Operating Line of Credit

The Company has available an operating line of credit of $20,000. 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 period ended September 30, 2012, the Company had a balance outstanding of $ Nil (December 31, 2011 - $Nil) on this line of credit.

(Expressed in Canadian dollars)

5. Trade and Other Payables

	September 30 2012	December 31 2011
Trade payables	**$ 595,463**	$ 294,647
Non-trade payables	**469,414**	348,017
	$ 1,064,877	$ 642,664

6. Debenture

On June 23, 2011, the Company issued $2,500,000 principal amount of senior secured 18% non-convertible debentures (the "New Debenture). As well on June 23 2011, 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. 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. The non-convertible debentures are secured by all tangible and intangible assets 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. Market value of $0.07 per share was used to value the "Bonus" common shares for an aggregate value of $946,505.

The securities issued and issuable pursuant to the transaction were subject to a hold period that expired on October 24, 2011.

The Company incurred cash financing costs of $374,969, "Bonus" common shares of $946,505 and 2,066,000 warrants with a fair value of $78,281 (note 10) in connection with the transaction. These costs were allocated between the New Debentures and the previously issued convertible debentures on a pro rata basis resulting in $606,011 of these costs being included in the loss on extinguishment of debentures and $793,744 recorded against the carrying value of the New Debentures. The New

(Expressed in Canadian dollars)

6. Debenture (continued)

Debentures are being accreted to its face value at a weighted average effective interest rate of 39.72%. The amendment to the debentures was accounted for as an extinguishment of the previously issued convertible debentures as they had yet to mature when the terms were modified on June 23, 2011. Also, the terms between current debentures and the previously issued convertible debentures are considered to be substantially different. Accordingly, the Company recorded a loss on the extinguishment of debentures of $796,224 inclusive of the financing costs outlined above in the statement of comprehensive loss for the year-ended December 31, 2011.

On October 3, 2012, the Company also fulfilled its obligations pursuant to the approval of the Debenture holders and amended all of the existing debentures, by extending the timeline for repayment for an additional 36 months, and reducing the interest rate payable on the outstanding indebtedness from 18% to 14%. The interest will accrue throughout the amended term and is payable with the redemption of the principal portion of the debenture (note 14).

7. Share Capital

The Company is authorized to issue an unlimited number of common shares.

The following is a summary of changes in common share capital from January 1, 2011 to September 30, 2012:

	Number of shares	**Value**
Balance at January 1, 2011	118,047,615	$ 22,338,694
Issuance of “Bonus” common shares on June 23, 2011 [a]	13,521,504	946,505
Balance at December 31, 2011	131,569,119	23,285,199
Issued for cash on September 7, 2012 [b]	6,875,652	160,050
Balance at September 30, 2012	**138,444,771**	**$ 23,445,249**

(a) The Company issued 13,521,504 units of “Bonus” common shares to purchasers of the debentures issued on June 23, 2011 and holders of the previously issued convertible debentures (note 6).

(b) The Company issued 6,875,652 units for gross proceeds of $343,783 by way of a private placement. Each unit consists of one common share at a price of $0.05 per unit and one warrant entitling the holder to purchase one additional common share at $0.10. Share issuance costs of $32,469 have been netted against the proceeds and $151,264 has been allocated to warrants (notes 8 & 10).

8. Share Issuance and Proceeds Received in Advance

On April 16, 2012, the Company announced a private placement of a minimum of $1,250,000 and up to a maximum of $2,000,000 in units. Each unit consists of one common share in the capital stock of the Company and one warrant, entitling the subscriber to purchase an additional share at $0.10 per share within 36 months of closing. The Company will issue the units at $0.05 per unit, resulting in the issue of a minimum of 25,000,000 shares and up to a maximum of 40,000,000 shares upon closing, non-diluted. This financing is a partially brokered private placement and the Company currently has commitments for the minimum amount of the raise.

The Company received approval from the Debenture holders to amend all of the existing debentures, by extending the timeline for repayment for an additional 36 months, and reducing the interest rate payable on the outstanding indebtedness from 18% to 14%.

The Company will pay a cash commission and advisory fees to Fraser Mackenzie Limited on their portion of the raised proceeds, and will pay a finder's fee to certain other parties that assisted in the private placement.

The net proceeds from the private placement will be used for general working capital. The proposed financing has been submitted to the TSX Venture Exchange ("TSX-V") for conditional approval, and is subject to TSX-V final approval.

As at September 30, 2012, the Company has collected $393,783, of which $343,783 was included for the first phrase of the above mentioned financing which was closed on September 7, 2012. The remaining $50,000 was included for the second phase of the above mentioned financing which was closed subsequent to the quarter end.

9. Share-Based Payments

The Company has an Incentive Stock Option Plan (the "Plan"). The Plan provides for options to be granted to the benefit of employees, directors and third parties. The maximum number of shares allocated to and made available to be issued under the Plan is 11,804,761. In 2007, the board of directors adopted a new option pricing policy such that the exercise price of options granted under the Stock Option Plan is priced as the greater of the three months weighted average trading price prior to the grant and the closing trading price for the common shares for the last trading day prior to the grant. The term of any option granted shall not exceed the maximum permitted time period under applicable regulations. Unless otherwise provided in the Stock Option Plan, the options shall be cumulatively exercisable in installments over the option period at a rate to be fixed by the Board of Directors. Certain options become exercisable upon achieving predetermined performance milestones and are specific to the respective employee's agreement. The Company will not provide financial assistance to any optionee in connection with the exercise of options.

(Expressed in Canadian dollars)

9. Share-Based Payments (continued)

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

Issuance date		Weighted average exercise price	Outstanding options	Vested options	Weighted average remaining life (years)
Balance at January 1, 2011	$	0.12	7,335,000	2,147,500	3.89
Granted		0.10	4,614,761		
Cancelled		0.10	(27,000)		
Forfeited		0.15	(145,000)		
Expired		0.20	(40,000)		
Balance at September 30, 2011	$	0.11	11,737,761	3,631,310	3.78
Forfeited		0.12	(103,000)		
Expired		0.24	(95,000)		
Balance at December 31, 2011	$	0.11	11,539,761	3,553,310	3.57
Cancelled		0.10	(3,915,035)		
Forfeited		0.10	(1,054,468)		
Expired		0.30	(520,000)		
Balance at September 30, 2012	**$**	**0.11**	**6,050,258**	**3,960,513**	**2.96**

For the nine months ended September 30, 2012, the fair value of the options granted was $Nil (September 30, 2011 - $275,134).

The Company had the following stock options outstanding at September 30, 2012:

Number of options	Number of non-vested options	Number of vested options	Exercise price	Expiry date
75,000	-	75,000	$0.13	November 27, 2012
100,000	-	100,000	$0.14	January 9, 2013
250,000	-	250,000	$0.22	April 18, 2013
360,000	-	360,000	$0.10	November 19, 2013
25,000	-	25,000	$0.10	August 19, 2014
450,000	-	450,000	$0.11	November 18, 2014
400,000	-	400,000	$0.10	April 20, 2015
1,000,000	666,667	333,333	$0.10	August 23, 2015
1,480,000	850,000	630,000	$0.10	February 11, 2016
1,910,258	573,078	1,337,180	$0.10	August 18, 2016
6,050,258	2,089,745	3,960,513	$0.11	Weighted-average exercise price of vested options

(Expressed in Canadian dollars)

9. Share-Based Payments (continued)

The estimated fair value of the options is expensed over the vesting period. The fair value of the compensation and contributed surplus relating to the stock options for the nine months ended September 30, 2012 was $70,469 (September 30, 2011 - $188,084). The fair value of all the Company's stock options was estimated using the Black-Scholes option pricing model.

10. Warrants

	Number of warrants		Amount		Weighted average exercise price
Balance at January 1, 2011	30,713,000	$	761,298	$	0.10
Warrants issued	2,666,000		112,157		0.10
Balance at September 30, 2011 and December 31, 2011	33,379,000	$	873,455	$	0.10
Warrants issued	6,875,652		151,264		0.10
Warrants expired	(29,963,000)		(708,790)		0.10
Balance at September 30, 2012	**10,291,652**	**$**	**315,929**	**$**	**0.10**

The Company had the following warrants outstanding and exercisable at September 30, 2012:

Number of warrants		Exercise price	Expiry date
750,000	(i)	$0.10	August 24,2014
600,000	(ii)	$0.10	February 11, 2013
2,066,000	(iii)	$0.10	June 23, 2013
6,875,652	(iv)	$0.10	September 7, 2015
10,291,652			

(i) These warrants were issued for services related to digital media workflow solutions. The warrants became exercisable after various phases of digital media workflow solution were completed.

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

(iii) 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.

(Expressed in Canadian dollars)

10. Warrants (continued)

(iv) These warrants were issued as part of the private placement of units (note 7). 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 119%; (III) a risk free rate of 1.25%; and (IV) an expected life of 3 years.

Warrants issued to agents and related to financings were not measured at the fair value of the services received as the fair value of such services was not reliably measurable.

11. Loss per Share

	Nine Months Ended		Three Months Ended	
	Sept 30 2012	**Sept 30 2011**	**Sept 30 2012**	**Sept 30 2011**
Numerator:				
Net loss and comprehensive loss for the period	**$ (1,834,473)**	$ (4,314,983)	**$ (453,973)**	$ (718,479)
Denominator:				
Weighted average number of common shares	**132,171,366**	123,000,547	**133,362,767**	131,569,119
Basic and diluted loss per share	**$ (0.01)**	$ (0.04)	**$ (0.003)**	$ (0.01)

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

	September 30 2012	**September 30 2011**
Share based payments:		
Vested	3,960,513	3,631,310
Non-vested:	2,089,745	8,106,451
Stock options	6,050,258	11,737,761
Warrants	10,291,652	33,379,000

12. 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 condensed interim costs and security for costs. The Company was awarded its costs for this motion. The Company continues to defend the action. The amount cannot be estimated reliably, 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) Settlement of Patent Infringement

On June 24, 2011, the Company resolved all litigation with a competitor that had been ongoing since 2005. In consideration of the settlement, the Company agreed to pay its competitor a lump sum amount totalling $600,000. As part of the settlement, the Company retained the patents and the rights 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 well, neither party will pursue legal fees, court costs or royalties pursuant to the above mentioned disputes. The payment was made in the three month period ended March 31, 2011.

(Expressed in Canadian dollars)

12. Commitments and Contingencies (continued)

(c) Settlement of Patent Infringement (continued)

The following is an account of the patent infringement litigation:

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 were completed, and were 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.

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.

(d) Leases

Total future annual lease payments for premises are as follows:

2012	$20,704
2013	82,818
2014	82,818
2015	82,818
2016	82,818
2017	62,114
	$414,090

13. Capital Risk Management

The Company includes equity; comprised of share capital, warrant capital, contributed surplus, share 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 three and nine months ended September 30, 2012.

14. Subsequent Event

On October 3, 2012, the Company announced that the second and final phase of the Private Placement had closed, raising aggregate gross proceeds of $1,268,783 between Phase 1 and Phase 2, with $375,000 invested by company insiders. Phase 2 raised proceeds of $925,000, in respect of which 18,500,000 units were subscribed for at a price of $0.05 per Unit. Each unit consists of one common share and one warrant, entitling the holder to purchase one additional common share of the Company at $0.10 and expiring on October 3, 2015. All securities issued in connection with Phase 2 will be subject to a four-month hold period. Phase 2 is subject to final approval from the TSX Venture Exchange. Fraser Mackenzie Limited acted as the agent for the Private Placement and will receive in consideration for its services a cash commission and advisory fees equal to approximately $99,500 and will be issued 738,000 warrants entitling them to purchase 738,000 common shares at an exercise price of $0.10 per share, for a period of two years from the closing date of Phase 2. As a result of closing the Private Placement and achieving the minimum threshold of $1,250,000, the existing debenture holders of the Company have consented to the amending of their existing debenture agreements. The key amendments include lowering the interest rate from 18% to 14% and extending the repayment date of the existing debentures for an additional three years, all as of the closing date of the Private Placement. The interest will accrue throughout the amended term and is payable with the redemption of the principal portion of the debenture.