AEROQUEST INTERNATIONAL LIMITED

MANAGEMENT'S DISCUSSION & ANALYSIS

For the period ending January 31, 2007

Management's Discussion and Analysis (MD&A) is intended to help readers understand the dynamics of our business and the key factors underlying our financial results. It explains trends in our financial condition and results of our operations for the quarter and year-to-date ended January 31, 2007 compared with our operating results for the corresponding periods ended January 31, 2006. It also compares our balance sheet as at January 31, 2007 to our balance sheet as at April 30, 2006. This MD&A should be read in conjunction with our audited consolidated financial statements and MD&A for April 30, 2006.

The consolidated financial statements presented here are those of Aeroquest International Limited and its wholly owned subsidiaries Aeroquest Limited and Aeroquest (UK) Limited, with all significant inter-company balances having been eliminated on consolidation.

Additional information relating to our company is available on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

FORWARD-LOOKING STATEMENTS

Securities laws encourage companies to disclose forward-looking information so that investors can get a better understanding of the company's future prospects and make informed investment decisions. Statements that are not historical fact and are based on current expectations, estimates and assumptions are forward-looking statements.

This MD&A contains forward-looking statements about our business. Inherent in these statements are known and unknown risks, uncertainties, and other factors that may cause the results, performance or achievements of our company to differ materially from those expressed or implied by such statements. Such factors include, among others, general economic and business conditions, major technology changes, timing of product introductions, competition and our ability to attract and retain key employees.

NON GAAP FINANCIAL MEASURES

Certain financial measures used in this MD&A do not have any standardized meaning under Canadian generally accepted accounting principles (GAAP). Below is a definition of each of the non-GAAP financial measures used in this MD&A. At the point where each non-GAAP financial measure is first discussed, a table has been provided to reconcile that financial information to the most directly comparable GAAP measure.

EBITDA

Earnings before interest, taxes, depreciation and amortization (EBITDA) is a financial metric used to analyze operating results. We define EBITDA as revenue less cost of sales and operating costs, and we use it as a benchmark of operating performance. We caution you that EBITDA as calculated by us may not be comparable to similarly titled amounts reported by other companies.

OVERVIEW

AEROQUEST'S BUSINESS

We are a world leader in the development and operation of innovative and proprietary airborne geophysical surveying platforms servicing the mineral exploration, oil and gas, and environmental industries. We operate a number of proprietary time-domain, sometimes called transient, electromagnetic (TEM) systems on platforms ranging from 5 metres to 12 metres in diameter, delivered under the trade-name AeroTEM™. We also supply geophysical surveying platforms based on frequency domain electromagnetics (trade-name Impulse™), total field magnetics, magnetic gradient and radiometrics.

SYSTEMS

We operate nine systems on three different platforms, and also own three gamma ray spectrometers. Our most popular and innovative platform is AeroTEM™ and encompasses six of our nine systems.

AeroTEM™

AeroTEM™ is based on time-domain electromagnetics (TEM). TEM systems are referred to as active systems because we energize the earth (using pulsed electric fields) and then measure the earth's response to that energy stimulus. TEM systems are used to identify bodies that are capable of conducting electricity because they measure a property of the earth called conductance. The term "time-domain" distinguishes it from "frequency-domain" and refers to the fact that we measure the response of the earth at various points in time both while we are stimulating the earth (the "on-time") and when our transmitter is shut off (the "off-time").

All the AeroTEM™ systems are based on rigid airframe designs. These rigid systems are the foundation that allows us to take reliable measurements of three different components of the earth's response. We measure the vertical component of the earth's response during the on-time and we can measure both the vertical and horizontal components of the off-time response. We refer to these as Z-on, Z-off and X-off, respectively.

The unique features of our systems allow us to produce very high resolution data with a high signal-to-noise ratio, to do conductance discrimination and to retrieve information on position, orientation, depth and thickness of conductors.

We currently offer three types of AeroTEM™ systems that we designate II, III and IV.

AeroTEM™ II

The AeroTEM™ II system is based on a platform that is approximately five metres in diameter. This system (with a peak dipole moment of approximately 40,000 Amp•m^2) is typically used in the search for targets that are up to 250 metres in depth. The AeroTEM™ II system, because of its size and base frequency (150 Hz) has been shown to be quite useful in the search for gold and platinum group elements (PGEs), as well as for kimberlites, the host rock of diamonds. The AeroTEM II system is particularly adept at surveying in rugged or mountainous terrain where its smaller diameter and modest weight allow it to be quite maneuverable.

AeroTEM™ III

The AeroTEM™ III system is based on a platform that is approximately 9 metres in diameter. The power level of this system is higher – from 120,000 to up to 180,000 Amp•m^2. The AeroTEM™ III system has been used to search for targets at mid-level depths — up to 400 metres, and is also well suited to work in the oil and gas sector where near surface rocks are often conductive. The range of base frequencies of this system (90 Hz and 150 Hz) also makes it suitable for base metal exploration, particularly nickel, and for oil and gas exploration, especially in the Oil Sands.

AeroTEM™ IV

The AeroTEM™ IV system is based on a platform that is approximately 12 metres in diameter. The power level of this system can range from 140,000 up to 230,000 Amp•m^2. The AeroTEM IV system is well suited to the search for deeper targets, up to 600 metres, and in areas where the rocks are more conductive.

Impulse™

We own and operate a frequency-domain EM system known as the Impulse™ system. It works by transmitting a primary electromagnetic field at discrete frequencies and then measuring the secondary electromagnetic response from the sub-surface at the same frequencies. By transmitting discrete frequencies at two different orientations (one vertical and one horizontal), it is possible to estimate the orientation, position and conductance of the body creating the response.

Magnetic Gradiometer

We own and operate two tri-directional magnetic gradiometers. These are passive systems, as opposed to both AeroTEM™ and Impulse™, which are active systems. Our gradiometers take four measurements of the earth's magnetic field every 0.1 seconds from sensors that are spatially separated by 3 metres. These four measurements can be used to calculate the rate of change of the earth's magnetic field in three orthogonal directions. Because we fly these systems from a helicopter, which can generally fly at lower altitudes and slower speeds, these gradiometers produce very high resolution data when compared to traditional fixed wing applications.

Radiometrics

We also own and operate three gamma ray spectrometers. These passive systems measure the rate of spontaneous radiological decay from rocks up to 60 cm below the earth's surface. In most survey applications, the spectrometer is combined with another of our systems to produce several measurements simultaneously. The most popular combination is gradiometer and spectrometer.

Our goal is to increase the utilization rate of the existing fleet and to continue to add systems as appropriate and as demand dictates, focusing on incorporating our latest advances in electronics and in platform design into each new system. We expect to commission new systems at a rate of approximately one per quarter for the next several quarters. These systems will vary from 6 metres to approximately 15 metres in diameter and all will have transmitters that are more powerful and will be capable of operating at a range of base frequencies from 25 to 150 Hz.

FINANCIAL AND OPERATING SUMMARY

(in thousands of Canadian dollars)

		Q3-07	Q2-07	Q1-07	Q4-06	Q3-06	Q2-06	Q1-06	Q4-05
Revenue	$	**4,425**	$ 5,778	$ 4,227	$ 2,683	$ 1,764	$ 1,867	$ 2,764	$ 2,585
EBITDA	$	**837**	$ 2,027	$ 650	$ 95	$ 124	$ (265)	$ (248)	$ (394)
Net Income	$	**365**	$ 1,101	$ 296	$ (252)	$ (78)	$ (524)	$ (329)	$ (797)
Avg. Common Shares		**15,838**	15,838	15,840	15,840	15,840	15,840	15,840	15,837
EPS	$	**0.02**	$ 0.07	$ 0.02	$ (0.02)	$ (0.00)	$ (0.03)	$ (0.02)	$ (0.05)
Systems available for use at period end		**12**	11	11	7	7	7	8	7
AeroTEM systems		**6**	6	6	4	4	4	5	4
Line kilometres flown during period		**25,600**	45,500	49,000	16,900	12,950	18,700	16,800	24,600
Contracts completed		**18**	21	46	24	15	15	9	10
Contracts in backlog at period end		**12**	11	22	22	7	6	-	2
Contract back-log	$	**3,500**	$ 3,500	$ 4,700	$ 2,600				

THIRD QUARTER 2007 OPERATING RESULTS

OVERVIEW

In the third quarter of 2007, we continued to see tangible and significant results from the re-positioning and restructuring activities that we began in the second half of our 2006 fiscal year. Our quarterly revenue and net earnings are up substantially over the same period last year, continuing the pace set in earlier quarters.

Our gross margin dropped slightly in the quarter over year to date principally related to our entry into the Mexican market. In the third quarter we deployed two AeroTEM™ systems to Mexico and incurred some one time costs such as transportation and the training of field crew and helicopter pilots. We continued to generate positive cash flows for the quarter and year to date.

We remain very satisfied with our current activity level. We completed 18 contracts in the third quarter and flew over 25,000 line kilometers. Just as important, our level of contracts in progress and our backlog remains very healthy. As expected, we have seen some contraction of our backlog as we enter the winter month's, a traditionally slow season for exploration in North America, but we have secured contracts that should allow us to continue surveying continuously through the winter.

REVENUE

In the third quarter of 2007, our total revenue was $4.43 million, up $2.66 million, or 151 per cent compared to the same quarter last year. Revenue in our business is a function of the number of systems we have available to fly and the average utilization of those systems. In the third quarter, we had nine systems available for at least a portion of the quarter, of which six were AeroTEM™.

Our revenue is characterized by a relatively small number of large contracts, so the presence or absence of one or two contracts can have a meaningful impact on our sales level in a given quarter. In addition, the amount we charge for a survey is a function of the type of survey performed, and this amount can vary significantly. In particular, we charge more for surveys using the AeroTEM™ platforms than we do for surveys on other platforms.

Revenue & Gross Profit

(in thousands of Canadian dollars)	Three Months Ended		Year-to-Date		Change from prior year		Change from YTD	
	31-Jan-07	31-Jan-06	31-Jan-07	31-Jan-06				
Revenue	**4,425**	1,764	14,430	6,429	2,661	151%	8,001	124%
Cost of sales	**2,685**	825	7,838	4,034	1,860	225%	3,804	94%
Gross profit	**1,740**	939	6,592	2,395	801	85%	4,197	175%
Gross profit margin %	**39.3%**	53.2%	45.7%	37.3%		(13.9%)		8.4%

Cost of sales was $2.68 million in the third quarter of 2007, or approximately 61 per cent of revenue. This compares to $0.82 million in the same quarter last year representing 47 per cent of revenue in that quarter.

A higher sales level results in some economies of scale, as some of our Cost of sales are fixed. Flying more line kms allows us to spread the fixed cost of production, operations, processing and interpretation personnel over a larger revenue base. In addition, longer surveys generally have lower fixed costs as a percentage of revenue. In the quarter, the average length of our surveys was approximately 2,200 kms.

The increase in cost of sales as a percentage of revenue translated into a lower gross profit and a lower gross profit margin percentage in the quarter. Gross profit was $1.74 million or 39 per cent of revenue in the third quarter compared to $0.94 million or 53 per cent in the same quarter last year. Gross profit for the third quarter of 2006 was unusually high as a result of a one-time benefit in the quarter. Year to date gross profit of $6.59 million, or 46% of revenue is an 8 per cent improvement over last year to date of $2.39 million or 37 per cent of revenue.

We will continue to focus on our margins for the remainder of 2007, and expect them to return to the 45% range in the fourth quarter of the year as some of the Q3 effects are non-recurring in nature.

OPERATING COSTS

Overall, third quarter operating costs were $1.17 million, up from $1.05 million in the same quarter last year, an increase of $0.12 million or 12%. This increase is primarily attributed to an increase in general and administrative costs necessary to support the current business level. Research and development expenditures are down $0.08 million or 46% over the same quarter last year continuing the trend from the second half of fiscal 2006 to better balance the research and development activities within the context of the Company's ability to afford the expenditures.

Operating Costs

(in thousands of Canadian dollars)	Three Months Ended 31-Jan-07	31-Jan-06	Year-to-Date 31-Jan-07	31-Jan-06	Change from prior year		Change from YTD	
Research & development expense	**98**	182	413	749	(84)	(46%)	(336)	(45%)
General & adminstrative expense	**805**	633	2,520	1,999	172	27%	521	26%
Depreciation & amortization expense	**270**	231	759	712	39	17%	47	7%
Stock option expense	**-**	-	145	37	-		108	292%
Total operating costs	**1,173**	1,046	3,837	3,497	127	12%	340	10%
% of Revenue	**26.5%**	59.3%	26.6%	54.4%		(32.8%)		(27.8%)

OPERATING PROFIT (LOSS)

EBITDA

EBITDA for the third quarter 2007 was $0.84 million, an increase of $0.72 million over the same quarter last year. As a percentage of revenue, EBITDA was down in the quarter compared to year to date primarily due to some one time costs related to the entry into the Mexican market.

EBITDA & Operating Profit (Loss)

(in thousands of Canadian dollars)	Three Months Ended 31-Jan-07	31-Jan-06	Year-to-Date 31-Jan-07	31-Jan-06	Change from prior year		Change from YTD	
Operating profit (loss)	**567**	(108)	2,755	(1,102)	675	625%	3,857	350%
Depreciation & amortization	**270**	231	759	712	39	17%	47	7%
EBITDA	**837**	123	3,514	(390)	714	580%	3,904	1001%
Writedown of discontinued project	**-**	-	-	73	-		(73)	(100%)
Contract cancellation costs	**68**	-	68	268	68		(200)	(75%)
EBITDA after unusual items	**769**	123	**3,446**	(658)	646	525%	4,104	624%
EBITDA as a % of Revenue	19%	7%	24%	(6%)		271%		401%

Our operating profit was $0.57 million in the third quarter, an improvement of $0.68 million, or 625 per cent from the operating loss of $0.11 million in the same quarter last year.

Depreciation and amortization charges totaled $0.27 million, a 17 per cent increase from the same quarter last year. Depreciation and amortization has generally been rising as we build and deploy more AeroTEM systems. We expect this growth to continue although the rate of growth will slow over the next several quarters.

NET INCOME (LOSS)

As a result of the above factors, we recorded a net profit in the quarter of $0.37 million, or $0.02 per share, compared with a net loss of $0.08 million or $(0.00) per share in the same quarter last year.

Net Income (Loss)

(in thousands of Canadian dollars)	Three Months Ended 31-Jan-07	31-Jan-06	Year-to-Date 31-Jan-07	31-Jan-06	Change from prior year		Change from YTD	
Operating profit (loss)	**567**	(108)	2,755	(1,102)	675	625%	3,857	350%
Other costs (income)	**(31)**	(8)	(66)	(35)	(23)	(288%)	(31)	(89%)
Contract cancellation costs	**68**	-	68	268	68		(200)	(75%)
Write down of discontinued project	**-**	-	-	73	-		(73)	(100%)
Provision for income taxes (recovery)	**165**	(21)	991	(477)	186	886%	1,468	308%
Net income (loss)	**365**	(79)	1,762	(931)	444	562%	2,693	289%
Earnings per share - basic	**$ 0.02**	$ (0.00)	$ 0.11	$ (0.06)	$ 0.02	600%	$ 0.17	283%

Cash Flow

Cash Flow from Operating Activities

Before changes in non-cash working capital, operating cash flow provided $0.64 million in the third quarter of 2007 a change of $0.48 million from the third quarter of 2006. Operating cash flow improved because of the increased sales activity and the Company's efforts to reduce development activity to a level that is supported by the current business.

Cash Flow from Operating Activities

(in thousands of Canadian dollars)	Three Months Ended 31-Jan-07	31-Jan-06	Year-to-Date 31-Jan-07	31-Jan-06	Change from prior year		Change from YTD	
Net income (loss)	**365**	(79)	1,762	(931)	444	562%	2,693	289%
Depreciation & amortization	**270**	231	759	713	39	17%	46	6%
Stock option expense	**-**	-	145	37	-		108	292%
Future income taxes	**-**	-	23	-	-		23	
Writedown of development costs	**-**	-	-	73	-		(73)	(100%)
Operating cash flow	**635**	152	2,689	(108)	483	318%	2,797	2590%
Change in non-cash working capital	**63**	320	(315)	370	(257)	(80%)	(685)	(185%)
Cash flow from operating activities	**698**	472	2,374	262	226	48%	2,112	806%

Changes in non-cash working capital generated $0.06 million increasing cash flow from operating activities to $0.70 million in the quarter, as compared to $0.47 million in the same quarter last year. The change in non-cash working capital came as a result of a significant increase in sales level. We continue to see improvements in working capital management as we continue to reduce the level of accounts receivable in relation to revenue.

Cash Flow from Investing Activities

Overall, investment activities in the third quarter used $0.25 million of cash. This compares to the third quarter of last year when investing activities used cash of $0.09 million.

Cash Flow from Investing Activities

(in thousands of Canadian dollars)	Three Months Ended **31-Jan-07**	31-Jan-06	Year-to-Date 31-Jan-07	31-Jan-06	Change from prior year		Change from YTD	
Acquisition of capital assets	**(257)**	(85)	(1,041)	(766)	(172)	(202%)	(275)	(36%)
Change in loan receivable	**2**	-	19	3	2		16	533%
Decline in value of long term investment	**-**	-	-	-	-		-	
Cash flow from investing activities	**(255)**	(85)	(1,022)	(763)	(170)	(200%)	(259)	(34%)
Capital expenditures as a % of revenue	6%	5%	7%	12%				

Acquisition of capital assets consumed $0.26 million, or 6 per cent of revenue, as compared to $0.09 million, or 5 per cent of revenue in the same quarter last year. We are targeting to keep ongoing capital expenditures at or less than 10 per cent of revenue. Capital investments were, and will be, made primarily to expand the fleet of AeroTEM systems.

CASH FLOW FROM FINANCING ACTIVITIES

In the quarter, financing activities were not significant and primarily relate to the effects of our Normal Course Issuer Bid. In the third quarter, we purchased a total of 500 shares for cancellation at an average price of $0.69.

Cash Flow from Financing Activities

(in thousands of Canadian dollars)	Three Months Ended **31-Jan-07**	31-Jan-06	Year-to-Date 31-Jan-07	31-Jan-06	Change from prior year		Change from YTD	
Repayment of long term debt	**-**	(1)	-	(6)	1	100%	6	100%
Shares cancelled from NCIB	**(0)**	-	(3)	-	(0)		(3)	
Issuance of Common Shares	**-**	-	1	-	-		1	
Cash flow from financing activities	**(0)**	(1)	(2)	(6)	0	(50%)	4	67%

LIQUIDITY AND CAPITAL RESOURCES

Our liquidity, as measured by cash balances, has increased by $1.35 million from the start of the fiscal year and $1.33 million from the end of the third quarter 2006. A large portion of this change is due to a reduction in discretionary spending and improvements in the management of working capital.

Cash and short-term investments are generally invested in liquid Canadian dollar or U.S. dollar denominated securities with maturities no greater than ninety days.

FINANCIAL POSITION

At January 31, 2007, we had current assets of $7.74 million and current liabilities of $3.30 million. Net working capital was $4.44 million, an increase from the $2.80 million at April 30, 2006.

This $1.65 million change from the year-end is primarily due to management efforts to improve working capital.

Cash & Working Capital Changes

(in thousands of Canadian dollars)	31-Jan-07	30-Apr-06	Change from year end	
Cash	**$3,861**	$2,511	$1,350	54%
Non-cash current assets	**3,882**	2,672	1,210	45%
Current assets	**7,743**	5,183	2,560	49%
Less: Current liabilities	**3,301**	2,387	914	38%
Net working capital	**$4,442**	$2,796	$1,646	59%
Current ratio	**2.3**	2.2	0.2	8%

TRANSACTIONS WITH RELATED PARTIES

During the period, we paid $90 thousand to companies owned by certain directors for management consulting services. These transactions are in the normal course of operations and are measured at the exchange value (the amount of consideration established and agreed to by the related parties), which approximates the arm's length equivalent value for services performed.

SHARE CAPITAL

As at the date of this report we had 15,837,773 Common Shares issued and outstanding.

As at the date of this report, Common Share stock options held by directors, officers, employees, consultants and brokers are as follows:

	Number of options	Exercise price		Expiry date
Fully vested & exercisable options held by directors,	40,000	$	2.00	October 28, 2009
officers, employees and consultants under the	202,500	$	0.50	October 28, 2009
Company's Stock Option Plan	30,000	$	0.50	March 1, 2010
	30,000	$	0.50	June 30, 2010
	15,000	$	2.00	June 30, 2010
	280,000	$	0.50	February 9, 2011
	50,000	$	0.50	March 28, 2011
	642,500	$	0.60	June 30, 2011
	30,000	$	0.75	October 3, 2011
	45,000	$	0.75	October 13, 2011
	15,000	$	0.75	October 16, 2011
Total vested & exercisable under Stock Option Plan	1,380,000	$	0.62	

A restricted stock unit plan was established in the second quarter and in the month of October a total of 120,000 shares were granted to employees at a price of $0.75 per share. According to the plan, vesting occurs over a period of three years with one-third vesting in each of the three years on the anniversary date of the grant. No expense has been recorded in the quarter.

In the second quarter the company received approval from the TSX for a normal course issuer bid whereby the company has been given the right to purchase up to 500,000 of its own common shares on the open market for cancellation. At January 31, 2007 the Company had purchased a total of 5,000 common shares of Aeroquest International Limited for cancellation. The share capital value and outstanding shares have been adjusted to reflect this cancellation.

INTERNAL CONTROLS AND DISCLOSURE CONTROLS AND PROCEDURES

We maintain a system of internal controls over financial reporting designed to safeguard assets and ensure that financial information is reliable. We also undertake ongoing evaluations of the effectiveness of our internal controls over financial reporting and, where appropriate, implement enhancements. We also file annual and quarterly certifications in accordance with Multilateral Instrument 52-109 certifying that our CEO and CFO have reviewed our financial statements and MD&A to ensure that they do not contain an untrue fact or omit a material fact, and that they present fairly the financial position, results of operation and cash flows of our company.

We also maintain a system of disclosure controls and procedures designed to ensure the reliability completeness and timeliness of the information we disclose in all of our public disclosure documents, including this MD&A. These controls are designed to ensure that information required to be disclosed by Aeroquest is recorded, processed, summarized and reported on a timely basis, as required by law, and is accumulated and communicated to Aeroquest's senior management and board of directors to allow timely decisions on required disclosure. In addition, our Audit Committee and Board of Directors provide an oversight role with respect to all public disclosure and review all financial statements, press releases and MD&A, including this one. Our annual and quarterly certifications also confirm that disclosure controls exist, that we have evaluated their effectiveness and that we have reported to you our conclusions about their effectiveness, especially during the period covered by this MD&A.

As of January 31, 2007, the Company's Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures and internal control over financial reporting and determined that they were effective.

CRITICAL ACCOUNTING POLICIES

Nature of Business

Aeroquest International Limited (formerly PICorp.) was incorporated by Certificate of Incorporation issued pursuant to the provisions of the General Corporation Law of the State of Delaware on September 21, 2001. On April 29, 2004, the Company was continued under the ABCA and on October 27, 2004 continued under the OBCA in conjunction with the Qualifying Transaction. The Company is a public company trading on the TSX Venture Exchange.

The Company's wholly owned subsidiary, Aeroquest Limited is incorporated under the laws of Ontario. The Company's wholly owned subsidiary, Aeroquest (UK) Limited is incorporated under the laws of England and Wales. Both are engaged in the operation of providing airborne geophysical services to the mining, oil & gas, environmental and geologic engineering industries as well as government agencies worldwide.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Aeroquest Limited and Aeroquest (UK) Limited. All significant inter company transactions and balances have been eliminated on consolidation.

Use of Estimates

These financial statements have been prepared in accordance with generally accepted accounting principles in Canada. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates as additional information becomes available in the future. The financial statements have, in management's opinion, been properly prepared using careful judgment within reasonable limits of materiality and within the framework of the accounting policies summarized below.

Revenue Recognition

Revenue is recognized when fieldwork is substantially complete, the contract revenue is fixed and determinable and collectibility is reasonably assured. Contracts range for less than a one year period. Costs related to contracts for which field work is incomplete at year end are classified as contracts in process whereas customer deposits received in advance for these contracts in process are classified as deferred revenue.

Revenue on sale of equipment is recognized when the equipment is delivered to the customer, the amount is fixed and determinable and collectibility is reasonably assured. The related cost of the equipment is recognized in cost of sales.

Financial Instruments

Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from its financial instruments. The fair value of financial instruments approximate their carrying values, unless otherwise noted.

Foreign Currency Translation

Foreign currency accounts are translated into Canadian dollars as follows:

- At the transaction date, each asset, liability, revenue and expense is translated into Canadian dollars by the use of the exchange rate in effect at that date.
- At the period end date, monetary assets and liabilities are translated into Canadian dollars by using the exchange rate in effect at that date.

The resulting foreign exchange gains and losses are included in income in the current period.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand and short-term investments readily convertible to cash with original maturities of 90 days or less.

Long-term Investments

Long-term investments are carried at cost unless an impairment in value exists that is other than temporary, in which case the long-term investment is written down to fair market value.

Capital Assets

Capital assets are stated at cost less accumulated amortization. Cost is net of related investment tax credits and government grants. Amortization based on the estimated useful life of the asset is calculated as follows:

Airborne and geophysical equipment	- 30% diminishing balance
Automotive equipment	- 30% diminishing balance
Data processing equipment	- 30% diminishing balance
Office equipment	- 20% diminishing balance
Leasehold improvements	- shorter of estimated economic life or lease term

Intellectual Property

Intellectual property is recorded at cost and amortized on a straight line basis over 3 years. The value of the intellectual property is regularly evaluated by reviewing the returns of the related business, taking into account the risk associated with the investment. Any impairment of permanent nature in the value of the intellectual property is written off against earnings.

Long-lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which carrying amounts of the assets exceed the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less cost to sell.

Research and Development

All research costs are charged to operations in the year of expenditure. Development costs are only capitalized if they meet the criteria for capitalization and are amortized over the period of the expected life. Development costs are written off when there is no longer expectation of future benefits.

Income Taxes

The Company follows the liability method of tax allocation in accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities, and measured using the substantively enacted tax rates and laws expected to be in effect when the differences are realized.

Stock-based Compensation

The Company has adopted the recommendations of the CICA with respect to stock-based compensation and other stock-based payments. These standards require that direct awards of stock, liabilities incurred or other compensation arrangements that are based on the price of common stock, be measured at fair value at each reporting date, with the change in fair value reported in the statement of operations.

The Company uses the fair value based method of accounting for all its stock-based compensation. Accordingly, the fair value method of accounting is applied for stock options granted to directors, officers, employees and consultants whereby the weighted average fair value of options granted is measured as of the earlier of the period the options are vested or the performance is complete and are recognized in the financial statements in accordance with the nature of the services or the assets received. When the awards are exercised, share capital is credited by the sum of the consideration paid together with the related portion previously credited to contributed surplus.

The fair value method of accounting is applied for restricted stock units granted to directors, officers, employees and consultants whereby the weighted average fair value of restricted stock units granted is measured from the grant date and accrued in the financial statements over the vesting period of 1/3 per year over the three year period. When the awards are fully vested, share capital is credited by the sum of the consideration together with the related portion previously credited to contributed surplus.