



**AEROQUEST INTERNATIONAL LIMITED  
MANAGEMENT'S DISCUSSION & ANALYSIS (MD&A)**

For the three and nine months ended June 30, 2011.

# AEROQUEST INTERNATIONAL LIMITED



## MANAGEMENT'S DISCUSSION & ANALYSIS FOR THE PERIOD ENDING JUNE 30, 2011

*Issued on August 11, 2011*

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 three and nine months ended June 30, 2011 ("Q3-F2011" and "YTD-F2011" respectively) compared with our operating results for the three and nine months ended June 30, 2010 ("Q3-F2010" and "YTD-F2010" respectively). It also compares our balance sheet as at June 30, 2011 to our September 30, 2010 fiscal year-end balance sheet.

The consolidated financial statements presented here are those of the Aeroquest Group of Companies: Aeroquest International Limited (collectively, "the Company"), and its wholly owned subsidiaries Aeroquest Limited, Aeroquest (Aust) Pty Ltd. (collectively doing business as Aeroquest Airborne in Canada and Australia, respectively), Geophex Ltd., Aeroquest Optimal Inc., Mapcon Mapping Limited, Mapcon Mapping Inc. (collectively "Mapcon"), Aeroquest (UK) Limited and AeroKaz LLP with all material inter-company balances having been eliminated on consolidation.

Additional information relating to our company is available on our website at [www.aeroquest.ca](http://www.aeroquest.ca) and on the System for Electronic Document Analysis and Retrieval (SEDAR) at [www.sedar.com](http://www.sedar.com). Unless otherwise noted, all amounts noted in this MD&A are in Canadian dollars.

### **1.1 FORWARD-LOOKING STATEMENTS**

Securities laws encourage companies to disclose forward-looking information so that investors can get a better understanding of a company's future prospects and make informed investment decisions. Certain statements in this MD&A are forward-looking statements or information, collectively "forward-looking statements". We are hereby providing cautionary statements identifying important factors that could cause our actual results to differ materially from those projected in forward-looking statements made in this MD&A. Any statements that express, or involve discussions as to, expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, through the use of words or phrases such as "will likely result", "are expected to", "will continue", "is anticipated", "estimated", "intend", "plan", "projection", "could", "may", "believes", "feel", "targeting", "look forward", "goals", "objective", "outlook" and similar expressions) are not historical facts and may be forward-looking and may involve estimates, assumptions and uncertainties which could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements.

Without limitation, information regarding the volatility of the market for our services, worldwide political stability, factors that could result in significant or prolonged disruption to mining and oil & gas exploration worldwide, domestic and international economic conditions, other political and economic situations and uncertainties, changes in foreign currency exchange rates, the impacts of changes in industry priorities and spending on exploration activities related to our services, major technology changes, timing of product introductions, competition, our ability to replace lost revenue of a customer

significant to an operating division, our ability to attract and retain key employees, and the possibility that such efforts will not have as great an impact on our operating results as is currently anticipated, is forward-looking information. Readers should also refer to our continuous disclosure materials filed with Canadian Securities Regulatory Authorities for additional information with respect to certain risk factors, including our most recent Annual Information Form.

Although we believe that the expectations reflected in such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to have been correct. Important factors that could cause actual results to differ materially from our expectations (“**Cautionary Statements**”), including changes in general economic, market and business conditions, fluctuations in the cost of borrowing, political and economic development, our ability to receive timely regulatory approvals, competitive actions of other companies, the occurrence of unexpected events such as equipment failures and other similar events affecting us or other parties whose operation or assets directly or indirectly affect us, and those risks set forth under the heading “Risks & Uncertainties” below.

All subsequent written and oral forward-looking statements attributable to the Company or persons acting on behalf of the Company are expressly qualified in their entirety by the Cautionary Statements. The forward-looking information contained herein is current only as of the date of this document. New factors emerge from time to time, and it is not possible for management to predict all of such factors and to assess in advance the impact of each such factor on our business or the extent to which any factor or combination of factors may cause actual results to differ materially from those contained in any forward-looking statements. We disclaim any intentions or obligation to update or revise any forward-looking statements or comments as a result of any new information, future event or otherwise unless such disclosure is required by law.

## **1.2 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, cash operating costs, and stock-based compensation expense, 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.

### **CASH OPERATING COSTS**

We define cash operating costs to be those operating expenses in our statement of operations that involve, or will involve, an inflow or outflow of cash. At present, cash operating costs are the sum of general and administrative expenses, and gain or loss on foreign exchange.

## 2 Our Business, Strategy & Outlook

### 2.1 SELECTED COMPARATIVE QUARTERLY FINANCIAL INFORMATION

(Financials in 000's except /share data)

	Fiscal 2011			Fiscal 2010				Fiscal 2009
	Q3-Jun 11	Q2-Mar 11	Q1-Dec 10	Q4-Sep 10	Q3-Jun 10	Q2-Mar 10	Q1-Dec 09	Q4-Sep 09
Revenue	\$ 9,162	\$ 9,750	\$ 12,352	\$ 10,318	\$ 8,632	\$ 5,770	\$ 7,498	\$ 5,099
Operating profit/(loss)	\$ (4,286)	\$ (3,046)	\$ (1,144)	\$ (2,619)	\$ (2,415)	\$ (3,004)	\$ (3,031)	\$ (6,362)
Net income/(loss)	\$ (3,668)	\$ (2,258)	\$ (976)	\$ (2,259)	\$ (1,794)	\$ (2,268)	\$ (2,266)	\$ (4,657)
Weighted average common shares	37,326	37,255	37,085	36,986	36,986	36,944	36,776	33,725
Earnings per share (basic)	\$ (0.10)	\$ (0.06)	\$ (0.03)	\$ (0.06)	\$ (0.05)	\$ (0.06)	\$ (0.06)	\$ (0.14)
Earnings per share (diluted)	\$ (0.10)	\$ (0.06)	\$ (0.03)	\$ (0.06)	\$ (0.05)	\$ (0.06)	\$ (0.06)	\$ (0.13)
Operating cash flow/share	\$ 0.03	\$ (0.05)	\$ 0.05	\$ (0.02)	\$ 0.07	\$ (0.02)	\$ (0.04)	\$ (0.05)
Total assets	\$ 46,183	\$ 48,025	\$ 47,602	\$ 50,563	\$ 49,040	\$ 50,971	\$ 56,162	\$ 57,740
Long term liabilities (excluding future taxes)	\$ 645	\$ 602	\$ 5	\$ 9	\$ 19	\$ 54	\$ 136	\$ 224
Systems available for use at period end *	26	26	26	26	26	28	28	29
Fixed-wing systems	10	9	9	9	9	9	9	10
Helicopter systems	14	15	15	15	15	17	17	17
AeroTEM systems included in above	10	11	11	11	11	13	13	13
Geomatics systems	2	2	2	2	2	2	2	2
Line kilometres flown during period								
Helicopter systems	15,800	38,200	20,100	26,300	27,500	20,100	22,700	5,400
Fixed-wing systems	353,000	314,000	405,000	389,000	286,000	88,000	267,000	351,000
Contract back-log (CAD\$ thousands)								
Helicopter systems	\$ 2,859	\$ 2,300	\$ 1,500	\$ 2,700	\$ 2,700	\$ 1,700	\$ 2,000	\$ 1,100
Fixed-wing systems	\$ 8,800	\$ 9,500	\$ 5,900	\$ 8,000	\$ 8,200	\$ 3,800	\$ 1,600	\$ 2,700
Geomatics	\$ 2,700	\$ 3,600	\$ 3,500	\$ 3,900	\$ 3,600	\$ 4,700	\$ 7,400	\$ 6,700
Other	\$ -	\$ 200	\$ 300	\$ 100	\$ 300	\$ 340	\$ 400	\$ 400
Total Backlog	\$ 14,359	\$ 15,600	\$ 11,200	\$ 14,700	\$ 14,800	\$ 10,540	\$ 11,400	\$ 10,900

\* excluding gamma ray spectrometers

Note: Fiscal 2010 Q1 to Q3 revenue and operating loss figures have been restated to reflect the disposal of the Canadian component of the Optimal Geomatics business that is now disclosed in aggregate as discontinued operations in the financial statements.

### 2.2 AEROQUEST'S BUSINESS

Aeroquest collects and interprets data that reveals information about what is at and beneath the earth's surface. We apply the best available technology in the world-wide search for economic concentrations of mineral and petroleum resources and in the precision-mapping of the earth's surface and objects upon it.

We offer airborne geophysics surveys through Aeroquest Airborne, aerial geomatics surveys through Aeroquest Optimal, and the custom design and construction of geophysical sensors and instruments through Geophex. With over 150 employees and contractors, and a fleet of over two dozen helicopter and fixed-wing survey systems worldwide, we are or are capable of surveying on every continent in the world where exploration activity is underway. Over our history, we have logged over 10 million line kilometers of fixed-wing surveys and over 1 million line kilometers of helicopter surveys – enough to circle the globe over 300 times.

### 2.3 BUSINESS STRATEGY

We refined our strategy in the fourth quarter of 2010. We made changes to our strategy to reflect that our success going forward will depend more on how we deploy all of our assets than on how many new assets we deploy. We will continue to invest in adding new systems and embracing new technologies, but those additions relative to the size of the base are likely to be smaller. We are already well established around the world. We will continue to work to develop our expertise in operating in new

parts of the world, and we will also seek to establish more dominant positions in some key markets.

Below is our current strategy statement:

<b>OBJECTIVE</b>	
<b>to be the most sought after provider of innovative geoscience solutions in our markets</b>	
<b>Strategy</b>	<b>Intent</b>
<b>Invest in innovation</b>	<ul style="list-style-type: none"> <li>• Establish market leading positions in all of our core technologies</li> <li>• Continuously invest in training to develop the experience and expertise of our people</li> </ul>
<b>Expand international operations</b>	<ul style="list-style-type: none"> <li>• Open up markets in Latin America, MENA, and Eurasia, in particular</li> <li>• Allocate labour to take advantage of non-domestic expertise</li> </ul>
<b>Broaden technologies and markets</b>	<ul style="list-style-type: none"> <li>• Identify new technologies that are complementary to our existing technologies to our service delivery model</li> <li>• Develop new applications and open new markets for our products and services point in the year</li> </ul>

For the short term, the Board has directed Management to focus on organic growth in its core operations.

## **2.4 OUTLOOK**

During the quarter, Mr. Roy Graydon CEO, President and a Director, tendered his resignation following his suggestion, and the Board's decision, to shift the Company' business strategy from growth including mergers and acquisitions to organic growth in its core operations. Mr. Bob Motz, CFO of the Company, has been appointed Interim CEO. The Governance Committee of the Board is overseeing the search of a new CEO, taking both internal and external candidates into consideration.

Global spending in both mineral and petroleum exploration continues to improve, as it has each quarter from the lows that occurred in early 2009. Commodity prices are at levels that would normally stimulate ongoing exploration so we remain optimistic for all modes of airborne exploration for the medium and long term. In the short term, the exploration opportunities remain weighted towards fixed-wing activity as the average cost per kilometer to survey using fixed-wing technology is lower than that of helicopter based technology. While we expect helicopter operations to experience a return to growth in order backlog in fiscal 2011, we continue to keep our helicopter business at a downsized level to reflect the current market and are working to maintain breakeven or better positions in each of our regional offices.

The outlook for the aerial geomatics segment remains positive in the long run as government organizations (especially in the United States) are required to replace aging and develop new infrastructure. The pace of new contract awards continue to be slow in the third quarter, a function of the existing uncertainties in general. We expect that this market will continue to be relatively quiet over the next few quarters.

Notwithstanding the optimism for the future, we remain focused on closely managing our costs. With the acquisition of Aeroquest Optimal in 2009 and Mapcon Mapping in Q1 of 2011, we have now integrated a large portion of our United States and Canadian back office operations, eliminated one set of public company costs and rationalized the cost structures between the geophysics and geomatics operations. Throughout the organization, we continue to focus on operational efficiencies and to carefully manage our cash as economic conditions improve.

Looking forward beyond one year, our objective is to use our short term tactics to position ourselves to react quickly as the recovery in our core markets takes hold.

Management is monitoring the recent U.S. debt crisis. It is too early to assess the impact of this crisis on the Company.

### **3 Third Quarter Operating Results**

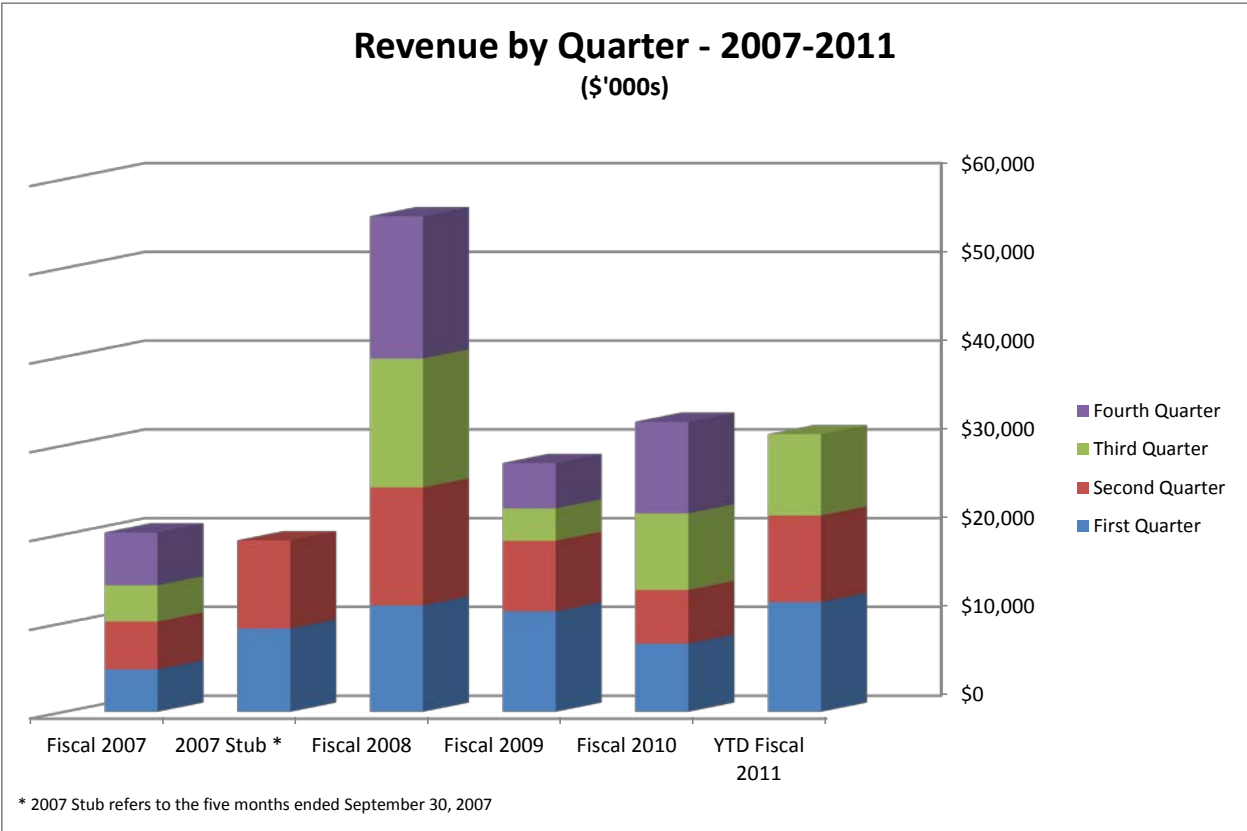
#### **3.1 OVERVIEW AND HIGHLIGHTS**

We report our revenues, cost of sales and margins in the following three business segments:

- Airborne Geophysics – comprising Aeroquest Airborne (Aeroquest Surveys and UTS/Aeroquest, the former UTS Geophysics business);
- Aerial Geomatics – comprising Aeroquest Optimal and Mapcon Mapping; and
- Instruments & Sensors –the Geophex business.

The Airborne Geophysics segment is further divided into fixed-wing and helicopter services to distinguish between these two modes of airborne exploration.

In the third quarter, we continued to see signs of economic recovery trickling down to grassroots exploration activities, especially in fixed-wing activities in the growth markets of Africa and South-East Asia. Grassroots exploration activity continues to improve from levels seen in fiscal 2010. As a result, our Q3-F2011 revenue increased by \$0.6 million (or 6 per cent) to \$9.2 million from \$8.6 million in Q3-F2010. In the Airborne Geophysics segment, helicopter services increased by 14 per cent to \$2.5 million and fixed-wing services increased by 17 per cent to \$4.2 million from their respective levels in Q3-F2010. The Aerial Geomatics segment contributed \$2.3 million in Q3-F2011, approximately equal to the level reported in Q3-F2010. The Instruments & Sensors segment contributed \$0.2 million in revenue for the quarter, a decrease of \$0.4 million to the level reported in Q3-F2010. A more detailed discussion of these variances is provided below.



Gross profit in Q3-F2011 was \$1.7 million or 19 per cent of revenue, a decrease of \$0.1 million from the \$1.8 million, or 21 per cent of revenue reported in Q3-F2010. Margins in airborne geophysics continue to be below the historical levels realized in 2007 and 2008 due to a combination of lower average pricing and lower average productivity. Fixed-wing services continue to experience lower margins due to significant production delays related to logistics and weather in the quarter. Helicopter margins are significantly below Management’s expectations as a result of lower sales having to absorb the fixed-cost component of cost of sales. In addition, geomatics margins remain below our expectations.

The Q3-F2011 net loss was \$3.7 million compared with Q3-F2010 loss of \$1.8 million. The change in net loss is due to several factors working at once, including lower gross profit margin and increased selling, general and administrative expenses. Q3-F2011 selling, general and administrative (“SG&A”) expenses increased by \$1.3 million or 48 per cent from Q3-F2010, reflecting increased activity in operations, as well as severance cost obligations in Q3-F2011 for several senior executives.

The above issues, as well as their year-to-date impact on financial results, are discussed in more detail throughout this MD&A.

Our cash balances decreased to \$2.0 million at the end of Q3-F2011 from \$4.8 million at the end of fiscal 2010 but increased by \$0.4 million from \$1.6 million at the end of the second quarter. Cash flow from operations in Q3-F2011 was \$1.0 million. As discussed below, cash flow from operations before changes in working capital was negative \$1.9 million and changes in non-cash working capital generated \$2.9 million of cash in the quarter. Capital expenditures for the quarter were \$0.6 million compared to \$0.4 million in Q3-F2010.

### 3.2 AIRBORNE FLEET SUMMARY

In this most recent quarter, there were no changes to our airborne fleet. Our active fleet is now comprised of 26 systems; 14 helicopter based and 12 fixed-wing. This includes three Aerial Geomatics systems, one LiDAR system and two aerial digital cameras.

#### AIRBORNE FLEET SUMMARY

	Helicopter	Fixed wing	Total
<b>Geophysics</b>			
<b>AeroTEM</b>	10		10
<b>Impulse/GEM-2A</b>	2		2
<b>Magnetics</b>			
single sensor	1	4	5
multi-sensor	1	3	4
<b>Gravity (+ multi-sensor mag)</b>		2	2
<b>Geomatics</b>		3	3
<b>Total</b>	<b>14</b>	<b>12</b>	<b>26</b>

### 3.3 REVENUE BY GEOGRAPHIC SEGMENT

#### Three Months Ended June 30, 2011

(thousands of Canadian dollars)

	Canada	Australia	USA	RoW	Total	
<b>Airborne Geophysics</b>						
Fixed Wing services	\$ -	\$ 2,755	\$ -	\$ 1,444	\$ 4,199	46%
Helicopter services	867	-	120	1,469	2,456	27%
System sales	-	-	-	-	-	0%
<b>Total Geophysics</b>	<b>867</b>	<b>2,755</b>	<b>120</b>	<b>2,913</b>	<b>6,655</b>	<b>73%</b>
<b>Aerial Geomatics</b>	<b>973</b>		<b>1,281</b>	<b>38</b>	<b>2,292</b>	<b>25%</b>
<b>Instruments &amp; Sensors</b>	<b>52</b>	<b>2</b>	<b>21</b>	<b>139</b>	<b>214</b>	<b>2%</b>
<b>Total Revenue - Aeroquest Group</b>	<b>\$ 1,892</b>	<b>\$ 2,757</b>	<b>\$ 1,422</b>	<b>\$ 3,090</b>	<b>\$ 9,161</b>	<b>100%</b>
	20.7%	30.1%	15.5%	33.7%	100%	

#### Nine Months Ended June 30, 2011

(thousands of Canadian dollars)

	Canada	Australia	USA	RoW	Total	
<b>Airborne Geophysics</b>						
Fixed Wing services	\$ 1,130	\$ 7,887	\$ 166	\$ 5,116	\$ 14,299	46%
Helicopter services	4,224	-	307	4,053	8,584	27%
System sales	-	-	-	1,636	1,636	5%
<b>Total Geophysics</b>	<b>5,354</b>	<b>7,887</b>	<b>473</b>	<b>10,805</b>	<b>24,519</b>	<b>78%</b>
<b>Aerial Geomatics</b>	<b>1,199</b>		<b>4,445</b>	<b>38</b>	<b>5,682</b>	<b>18%</b>
<b>Instruments &amp; Sensors</b>	<b>52</b>	<b>416</b>	<b>455</b>	<b>139</b>	<b>1,062</b>	<b>3%</b>
<b>Total Revenue - Aeroquest Group</b>	<b>\$ 6,605</b>	<b>\$ 8,303</b>	<b>\$ 5,373</b>	<b>\$ 10,982</b>	<b>\$ 31,263</b>	<b>100%</b>
	21.1%	26.6%	17.2%	35.1%	100%	

With the ramp up in the exploration services business that we experienced in the later part of 2010, we continue to be active around the globe. As of June 30, 2011, we had positioned helicopter systems in North and South America, Europe, Africa, the Middle East and Australasia. During the same period, we operated fixed-wing units in Australasia, Africa and North and South America.

Changes in the revenue mix between Canada, Australia and the United States reflect normal variations in quarterly activity as we commence and then complete various survey projects around the world. In the quarter, no country (other than those listed) represented more than 10 per cent of revenue.

### 3.4 CONSOLIDATED RESULTS

In Q3-F2011, consolidated revenue was \$9.2 million, up \$0.5 million or 6 per cent over Q3-F2010. In Airborne Geophysics, revenue from helicopter services was \$2.5 million, up \$0.3 million or 14 per cent over Q3-F2010 while revenue from fixed-wing services was \$4.2 million, up \$0.6 million or 17 per cent over Q3-F2010. Revenue from helicopter services increased slightly but continues to reflect the weakness in the market and an increase in competitive activity. Fixed-wing survey services showed an improvement over the levels in Q3-F2010 but remained below our expectations. We had hoped for better results but the fixed-wing operations were negatively impacted due to scheduled and unscheduled aircraft maintenance, weather conditions and permitting delays.

Revenue from Aerial Geomatics was \$2.3 million, approximately equal to revenue reported in Q3-F2010, and revenue from Instruments & Sensors was \$0.2 million in Q3-F2011, a decrease of \$0.4 million over the revenue reported in Q3-F2010.

YTD-F2011 revenue is \$31.3 million, an increase of \$8.9 million or 40 per cent over the \$22.4 million reported in YTD-F2010. Airborne Geophysics revenue is up \$9.4 million or 62 per cent to \$24.5 million, helped by an increase of \$7.7 million in fixed-wing and helicopter services, as well as revenue of \$1.6 million recorded in the first quarter of fiscal 2011 on the sale of an AeroTEM system to a subsidiary of the Chinese government.

Cost of sales was \$7.4 million in Q3-F2011, or 81 per cent of revenue, compared to \$6.8 million or 79 per cent of consolidated revenue in Q3-F2010. Gross margin in Q3-F2011 declined by 2 percentage points to 19 per cent, compared with 21 per cent in Q3-F2010, primarily the result of increased costs in our fixed-wing services.

Aerial Geomatics gross profit in the quarter was 24 per cent, which is an improvement from the margins reported in Q1 and Q2 of fiscal 2011 and Q3 of fiscal 2010. However, the geomatics margins still remain below our expectations. Processing costs of sales are higher than forecasted. The processing component of cost of sales of geomatics is much higher than that of geophysics. With the acquisition on January 31, 2011 of Mapcon Mapping, Management is addressing processing costs through offshore third party processing centres. We expect this acquisition to improve future geomatics margins by optimizing processing between US domestic and offshore processing centres. With the economic slowdown in the U.S., we have also experienced pricing pressure which has impacted our margins.

## CONSOLIDATED RESULTS

(in thousands of Canadian dollars)	Three Months		Change		Nine Months		Change	
	Q3-F11	Q3-F10	\$	%	F2011	F2010	\$	%
<b>Revenue</b>								
Airborne Geophysics								
Fixed Wing	4,199	3,586	613	17%	14,299	8,385	5,914	71%
Helicopter	2,456	2,153	303	14%	8,584	6,772	1,812	27%
System Sales	-	-	-	N/A	1,636	-	1,636	N/A
Total Airborne Geophysics	6,655	5,739	916	16%	24,519	15,157	9,362	62%
Aerial Geomatics	2,292	2,316	(24)	N/A	5,682	6,002	(320)	N/A
Instruments & Sensors	214	591	(377)	(64%)	1,063	1,192	(129)	(11%)
	9,161	8,646	515	6%	31,264	22,351	8,913	40%
<b>Cost of sales</b>								
Airborne Geophysics								
Fixed Wing	3,299	2,739	560	20%	11,354	6,882	4,472	65%
Helicopter	2,234	1,944	290	15%	6,489	5,830	659	11%
System Sales	-	-	-	N/A	613	-	613	N/A
Total Airborne Geophysics	5,533	4,683	850	18%	18,456	12,712	5,131	45%
Aerial Geomatics	1,750	1,895	(145)	N/A	4,620	4,970	(350)	N/A
Instruments & Sensors	149	225	(76)	(34%)	517	444	73	16%
	7,432	6,803	629	9%	23,593	18,126	5,467	30%
<b>Gross profit</b>	1,729	1,843	(114)	(6%)	7,671	4,225	3,446	82%
<b>Gross margin</b>								
<i>Airborne Geophysics</i>								
Fixed Wing	21.4%	23.6%			20.6%	17.9%		
Helicopter	9.0%	9.7%			24.4%	13.9%		
System Sales	N/A	N/A			62.5%	N/A		
Total Airborne Geophysics	16.9%	18.4%			24.7%	16.1%		
Aerial Geomatics	23.6%	18.2%			18.7%	17.2%		
Instruments & Sensors	30.4%	61.9%			51.4%	62.8%		
Gross profit margin %	18.9%	21.3%			24.5%	18.9%		
General & administrative expense	3,941	2,660	1,281	48%	10,470	7,279	3,191	44%
Foreign exchange (gain) loss	12	(121)	133	(110%)	311	60	251	418%
<b>Total cash operating costs</b>	3,953	2,539	1,414	56%	10,781	7,339	3,442	47%
% of revenue	35.0%	22.7%			95.4%	65.6%		
Stock-based compensation expense	158	85	73	86%	371	255	116	45%
EBITDA	(2,382)	(781)	(1,601)	205%	(3,481)	(3,370)	(111)	3%
EBITDA as a % of revenue	(4.3%)	(5.9%)			(6.3%)	(25.3%)		
Depreciation of capital assets	1,043	871	172	20%	2,444	2,626	(182)	(7%)
Amortization of intangible assets	861	828	33	4%	2,550	2,560	(10)	(0%)
<b>Operating profit/(loss)</b>	(4,286)	(2,480)	(1,806)	73%	(8,475)	(8,556)	81	(1%)
Operating profit as a % of revenue	(46.8%)	(28.7%)			(27.1%)	(38.3%)		
Interest and other expense (income)	(130)	(51)	(79)	155%	(265)	(285)	20	(7%)
Provision for income taxes	(488)	(635)	147	(23%)	(1,308)	(2,182)	874	(40%)
Loss from discontinued operations	-	-	-	N/A	-	240	(240)	N/A
<b>Net income</b>	\$ (3,668)	\$ (1,794)	\$ (1,874)	104%	\$ (6,902)	\$ (6,329)	\$ (573)	9%
Earnings per share - basic	\$ (0.10)	\$ (0.05)	\$ (0.05)		\$ (0.18)	\$ (0.17)	\$ (0.01)	

In Airborne Geophysics, gross margin in helicopter services was 9 per cent in Q3-F2011, as compared to 10 per cent in the Q3-F2010. Helicopter margins in Q3-F2011 and Q3-F2010 are significantly below Management's expectations as a result of lower sales having to absorb the fixed cost component of cost of sales.

Gross margin in Airborne Geophysics fixed-wing services was \$0.9 million, or 21 per cent of revenue in the current quarter as compared to 24 per cent in Q3-F2010. As previously stated, we had a number of factors that impacted productivity in Q3-F2011 and we expect margins to improve in subsequent quarters as productivity improves.

YTD-F2011 gross profit was \$7.7 million or 25 per cent of revenue, an increase of \$3.5 million from the \$4.2 million (and 19 per cent of revenue) reported in YTD-F2010. The impact of the previously noted system sale as well as improved airborne geophysics productivity served to improve overall margins when compared to YTD-F2010.

### **3.5 CASH OPERATING COSTS**

Cash operating costs in Q3-F2011 totaled \$4.0 million, an increase of \$1.3 million, or 48 per cent from the \$2.7 million reported in Q3-F2010. This increase is partially due to increased costs in Airborne Geophysics. As we have indicated in prior MD&A, in 2010 we had downsized our operations to address the economic slowdown. We are now taking measures to increase staffing to reflect current volumes of business. Also, we did recognize approximately \$0.7 million in severance cost obligations in Q3-F2011 related to management changes in our Corporate office.

### **3.6 OPERATING PROFIT AND EBITDA**

In Q3-F2011, we recognized a one-time expense of \$0.2 million related to fair value of a five year extension of certain employee stock options that were scheduled to expire in 2011. This extension was approved by the shareholders of the Company at its Annual General Meeting on February 10, 2011.

EBITDA in Q3-F2011, was negative \$2.4 million, an increase of \$1.6 million over the negative EBITDA of \$0.8 million reported in Q3-F2010. The major component of this additional cost was the \$1.3 million increase in SG&A.

Depreciation and amortization charges totaled \$1.9 million in Q3-F2011, up \$0.2 million from the depreciation and amortization reported in Q3-F2010 reflecting the slower pace of capital asset acquisition in the last two fiscal years.

As a result, operating loss before discontinued operations in Q3-F2011, was \$4.3 million compared to the operating loss of \$2.5 million reported in Q3-F2010.

During the second quarter of F2010, we sold a division of our Aerial Geomatics segment based in Vancouver, BC to a third party. As a result, results of these operations have been separated out and disclosed as a loss from discontinued operations in Q3-F2010. Loss from discontinued operations during this period was \$0.2 million.

### 3.7 NET LOSS

Net loss for Q3-F2011 was \$3.7 million, or \$0.10 per share compared to net loss of \$1.8 million, or \$0.05 per share in Q3-F2010.

Our provision for recovery of income taxes for Q3-F2011 was \$0.5 million, a decrease of \$0.1 million compared to an income tax recovery of \$0.6 million in Q3-F2010. The percentage rate decline is primarily due to different tax rates in foreign jurisdictions combined with several jurisdictions reporting taxable income and others still reporting losses for tax purposes.

### 4 Liquidity and Capital Resources

Our cash balances declined by \$2.8 million from \$4.8 million at September 30, 2010 to \$2.0 million at June 30, 2011. Much of this decline is due to three factors:

- 1) Cash flow from operations – which generated \$0.7 million of cash (cash flow from operations consumed \$2.6 million of cash whereas changes in non-cash working capital generated \$3.3 million of cash);
- 2) Acquisition of Mapcon Mapping – which consumed \$1.4 million; and
- 3) Capital expenditures which consumed \$1.9 million of cash.

#### CASH & WORKING CAPITAL CHANGES

(in thousands of Canadian dollars)	Three Months			Nine Months		
	Q3-F11	Q3-F10	Change	F2011	F2010	Change
<b>Operating activities</b>						
<b>Net Income/(Loss)</b>	\$ (3,668)	\$ (1,794)	\$ (1,874)	\$ (6,903)	\$ (6,328)	\$ (575)
<b>Non-cash operating items</b>						
Depreciation/Amortization	1,904	1,699	205	4,995	5,186	(191)
Future taxes	(307)	(123)	(184)	(1,052)	(629)	(423)
Loss/(Gain) on disposal of capital assets	-	(18)	18	6	(376)	382
Stock based compensation	158	85	73	371	254	117
<b>Operating cash before change in non-cash working capital</b>	<b>(1,913)</b>	<b>(151)</b>	<b>(1,762)</b>	<b>(2,583)</b>	<b>(1,893)</b>	<b>(690)</b>
Change in non-cash working capital	2,918	2,703	215	3,282	2,277	1,005
<b>Cash flow from operations</b>	<b>1,005</b>	<b>2,552</b>	<b>(1,547)</b>	<b>699</b>	<b>384</b>	<b>315</b>
<b>Investing activities</b>						
Capital asset purchases	(582)	(368)	(214)	(1,920)	(839)	(1,081)
Proceeds from disposal of capital assets	-	17	(17)	-	510	(510)
Long term investments acquired	-	-	-	-	90	(90)
Cash cost of acquisition	-	-	-	(1,384)	-	(1,384)
<b>Cash flow from investing</b>	<b>(582)</b>	<b>(351)</b>	<b>(231)</b>	<b>(3,304)</b>	<b>(239)</b>	<b>(3,065)</b>
<b>Financing Activities</b>						
Capital lease payments	(31)	(122)	91	(195)	(474)	279
Proceeds from issuance of shares	8	-	8	75	25	50
<b>Cash flow from financing</b>	<b>(23)</b>	<b>(122)</b>	<b>99</b>	<b>(120)</b>	<b>(449)</b>	<b>329</b>
Net change in cash for the period	400	2,079	(1,679)	(2,725)	(304)	(2,421)
Cash - beginning of period	1,632	3,583	(1,951)	4,757	6,145	(1,388)
<b>Cash - end of period</b>	<b>\$ 2,032</b>	<b>\$ 5,662</b>	<b>\$ (3,630)</b>	<b>\$ 2,032</b>	<b>\$ 5,841</b>	<b>\$ (3,809)</b>

Cash and short-term investments are currently invested in liquid Canadian dollar, Australian dollar or U.S. dollar denominated bank guaranteed securities with maturities no greater than three months.

#### **4.1 OPERATING ACTIVITIES**

In Q3-F2011, cash flow from operations before changes in working capital consumed \$1.9 million of cash in the quarter. Changes in non-cash working capital resulted in \$2.9 million of cash. In Q3-F2010, operating cash flow before changes in working capital consumed \$0.1 million of cash and net changes in non-cash working capital generated \$2.7 million in cash.

#### **4.2 INVESTING ACTIVITIES**

Investment activities in Q3-F2011 consumed \$0.6 million of cash representing capital expenditures made in the quarter of \$0.6 million. Q3-F2010's capital expenditures were \$0.4 million.

#### **4.3 FINANCING ACTIVITIES**

The financing activities in Q3-F2011 were less than \$0.1 million and represented capital lease payments offset by cash generated from exercise of employee stock options.

#### **4.4 CASH**

Our cash balances declined in Q3-F2011 by \$2.8 million from the end of fiscal 2010. This decline is primarily the result of the combination of cash used in capital expenditures of \$1.9 million and \$1.4 million cash used of the acquisition of Mapcon offset by cash flow from operations (after changes in working capital) of \$0.7 million.

We are continuing to actively manage our working capital wherever possible to ensure that cash is appropriately invested in our business operations.

#### **4.5 CAPITAL RESOURCES**

We have a credit facility in place for our Canadian operations. At September 30, 2010, \$0.1 million was drawn on this facility representing an overdraft in our United States dollar balances in Canada. This amount was repaid in early October, 2010 and remains undrawn as of the end of Q3-F2011.

We believe that cash, cash flow from operations and unused operating facilities will be sufficient to fund our working capital requirements and debt service costs (if applicable) for the near future.

#### **4.6 SUMMARY FINANCIAL POSITION**

As of June 30, 2011, we had current assets of \$10.0 million and current liabilities of \$8.5 million. Net working capital was \$1.5 million, a decrease of \$4.5 million from September 30, 2010.

## SUMMARY CASH & WORKING CAPITAL

(in thousands of Canadian dollars)	30-Jun-11	30-Sep-10	Change from prior year-end	
<b>Cash</b>	<b>\$2,032</b>	\$4,757	(\$2,725)	-57.3%
Non-cash current assets	<b>7,986</b>	8,454	(468)	-5.5%
<b>Current assets</b>	<b>10,018</b>	13,211	(3,193)	-24.2%
Less: Current liabilities	<b>8,480</b>	7,139	1,341	18.8%
<b>Net working capital</b>	<b>\$1,538</b>	\$6,072	(\$4,534)	-74.7%
Current ratio	<b>1.2</b>	1.9		-36.2%

### 4.7 Acquisition of Mapcon Mapping

On January 31, 2011, we completed the acquisition of the Mapcon Mapping group of companies from OSI Geospatial Inc. Mapcon provides LiDAR, photogrammetry and related geomatic services to customers in the North American marketplace. Mapcon consists of two entities: a Canadian sales, operations and project management team located in Burnaby, BC; and a United States sales team located in Salt Lake City, Utah. Mapcon generated approximately \$4 million of revenue in its last fiscal year prior to acquisition.

The total purchase price net of cash acquired was \$1.38 million. The acquisition has been accounted for under the purchase method of accounting and has been included in the balance sheet of the Company on March 31, 2011. The details of the consideration given and the fair value of net assets acquired, in Canadian dollars, are as follows:

Net Assets Acquired at Fair Values ('000s):

Cash	\$ 18
Accounts receivable	863
Work in progress	1,191
Prepays	11
Capital assets	270
Accounts payable and accrued liabilities	(948)
Deferred revenue	(3)
<b>Total net assets acquired, net of cash</b>	<b>\$ 1,384</b>

Consideration provided was all paid in cash.

We believe that the acquisition is positive to the Company as Mapcon's customers do not overlap with that of Aeroquest Optimal (Mapcon is primarily Canada and Western USA whereas Optimal is Eastern USA and government). As well, Mapcon provides a unique opportunity to integrate processing operations as their processing is primarily done overseas.

## **5 Risks and Uncertainties**

### **5.1 Foreign Currency Exchange Risk**

We record transactions and prepare our financial statements in Canadian dollars. For Q3-F2011, we maintained operations in Canada, Australia, and the United States with business conducted in other countries as well. International operations are considered financially and operationally self-sustaining. Accordingly, the assets and liabilities of our foreign subsidiaries are translated into Canadian dollars at period end exchange rates. Revenue and expense items of our foreign subsidiaries are translated into Canadian dollars at monthly exchange rates.

Significant portions of our contract survey expenditures are denominated in the same currency as our revenue on these contract surveys and therefore, a natural hedge exists for much of this exposure. However, a net exposure exists for Australian and United States dollars cash flows that can affect results as the Canadian dollar exchange rate changes in relation to these currencies.

Other comprehensive income includes a currency translation adjustment related to our net investment in self-sustaining subsidiaries.

While our foreign exchange policy does permit active hedging of any portion of our net foreign currency cash flow beyond the natural hedges identified and discussed above, no active hedges were employed in the quarter or the year. As a result, we did not employ any financial derivative products.

### **5.2 INTEREST RATE RISK**

At the end of Q2-F2011 we purchased a digital mapping camera for our geomatics operations. The vendor agreed to finance \$0.7 million payable over four years. The interest rate is United States Wall Street Journal prime rate plus 2 per cent. Accordingly, the company is exposed to volatility in the United States prime rate in the future.

Other than the financing noted above, interest rate volatility had minimal impact on our operations only to the extent that the interest rate received on our cash balances was negatively affected by the overall decline in interest rates in the Canada, Australia and the United States.

### **5.3 LITIGATION**

We are involved in various claims and litigation arising in the normal course of business. While the outcome of these matters is uncertain and there can be no assurance that such matters will be resolved in our favour, we do not currently believe that the outcome of adverse decisions in any pending or threatened proceedings related to those or other matters or amount which may be required to pay by reason thereof would have a material adverse impact on our financial position, results of operations or liquidity.

## **6 Off-Balance Sheet Arrangements**

We have not entered into any off balance sheet arrangements, other than previously disclosed, that have, or are reasonably likely to have, an impact on the current or future results of operations or the financial condition of our company.

## 7 Share Capital

### 7.1 Stock Option Plan

At June 30, 2011, we had 37,325,940 Common Shares issued and outstanding and as at the same date the Common Share stock options held by directors, officers, and employees were as follows:

	Number of options	Exercise price	Expiry date
Issued options held by directors, officers and employees under the Company Stock Option Plan	250,000	\$ 0.50	February 9, 2016
	312,500	\$ 0.60	June 30, 2016
	15,000	\$ 0.75	October 13, 2016
	64,000	\$ 2.34	September 30, 2012
	50,000	\$ 1.70	July 16, 2013
	280,666	\$ 0.42	January 18, 2014
	339,000	\$ 0.45	August 4, 2014
	120,000	\$ 0.55	October 20, 2014
	450,000	\$ 0.63	May 11, 2015
	25,000	\$ 0.62	September 27, 2015
	50,000	\$ 0.85	December 14, 2015
	30,000	\$ 0.92	February 10, 2016
	180,000	\$ 0.62	June 9, 2016
	Total outstanding	2,166,166	\$ 0.58
Total exercisable	1,680,165	\$ 0.59	

### 7.2 Restricted Stock Unit Plan

At March 31, 2011 there were 51,665 RSU's outstanding. No RSU's were granted, vested or converted into Common Shares in either Q3-F2011, Q3-F2010, or F2010.

### 7.3 Short Form Prospectus

During the quarter, the Company reported that it elected not to proceed with its previously announced best efforts offering of units (each comprised of a common share and a half-warrant) and withdrew the short form prospectus filed with regulatory authorities in Canada.

## 8 Internal Controls and Disclosure Controls & 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 National (formerly 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.

NI 52-109 also contains the requirements that we, on an annual basis:

- evaluate the effectiveness of Internal Controls over Financial Reporting ('ICFR');
- evaluate the effectiveness of Disclosure Controls & Procedures ('DC&P')
- use a control framework in the design of our ICFR and such framework must be disclosed; and
- disclose all material weaknesses, their financial impact (actual or potential), and plans or actions to remediate such weaknesses.

During the 2010 fiscal year, we engaged external advisors to assess the impact of these changes on our current evaluation of ICFR and disclosure control and procedures. Our Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of our disclosure controls and procedures and internal control over financial reporting, and determined that they were effective as of September 30, 2010 and March 31, 2011.

## **9 Critical Accounting Policies and Estimates**

Here and in our Consolidated Financial Statements (including the Notes) we have identified the accounting policies and estimates that are critical to the understanding of our business and the results of our operations.

### **9.1 ACCOUNTING POLICY CHANGES**

In January 2009, the CICA issued Section 1582 "Business Combinations", Section 1601 "Consolidated Financial Statements and Section 1602 "Non-controlling Interests" to replace Section 1581 "Business Combinations" and Section 1600 "Consolidated Financial Statements". Prospective application of these standards are effective for fiscal years beginning on or after January 1, 2011, with early adoption permitted. This new Section 1582 effectively harmonizes the business combinations standard under Canadian GAAP with International Financial Reporting Standards ("IFRS"). The new Section 1582 revises guidance on the determination of the carrying amount of the assets acquired and liabilities assumed, goodwill and accounting for non-controlling interests at the time of a business combination. New Section 1601 together with Section 1602 establish standards for the preparation of consolidated financial statements.

Please also refer to commentary on IFRS noted at 9.4 below.

## **9.2 FOREIGN ACCOUNTING STANDARDS**

The results of operations of our subsidiary UTS Geophysics Pty Ltd. are prepared in accordance with Australian equivalents to International Financial Reporting Standards (AIFRS) and then adjusted to Canadian GAAP standards for consolidation. Our Geophex Ltd. subsidiary results are reported under United States GAAP and are adjusted to Canadian GAAP standards for consolidation.

## **9.3 USE OF ESTIMATES**

In the preparation of our financial statements we are required to make some estimates of the fair value of certain transactions, or the likely impact of certain events on our results of operations. The following is a summary of the areas that require the most significant use of estimates:

### *BAD DEBT EXPENSE*

We are required, each reporting period, to make an estimate of the likelihood that we will collect all of the accounts receivable owed to us. This requires that we exercise some judgment about the timing and likelihood of payment on accounts that have become past due and record a provision for those accounts where there is significant risk of collection. We review all outstanding accounts receivable on at least a monthly basis to establish whether or not any action is required.

Included in June 30, 2011 accounts receivable is an amount of approximately \$800,000 from a customer resident in Libya. Included in the \$800,000 is \$128,000 that was in transit at a United Kingdom bank. Subsequent to the end of Q3-F2011, we received permission from the Canadian government to collect all monies owed. The \$128,000 has since been paid. While some uncertainty exists regarding the general political unrest in Libya, we have ongoing contact with the customer and continue to work with them to arrange for collection of the remaining balance. As a result, we have determined that no allowance for doubtful accounts is necessary at this time.

### *FOREIGN CURRENCY TRANSLATION*

We record revenue in Canadian, Australian, and United States dollars, as well as in Euros and, at times, other currencies. Changes in the exchange rates between currencies may create a change in the revenue, or profit on a survey between the time we record revenue and the time we disburse for costs. In addition, we translate all amounts into Canadian dollars for the purposes of financial reporting.

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 monthly average exchange rate.
- 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.

### *GOODWILL AND INTANGIBLE ASSETS*

Goodwill represents the difference between the price paid and the fair value attributed to tangible and

intangible assets upon the acquisition of businesses. Goodwill is not amortized but tested for impairment annually or more frequently if changes in circumstances indicate a potential impairment. The impairment test first consists of a comparison of the fair value of the reporting unit to which goodwill is assigned with its carrying amount. When the carrying amount of a reporting unit exceeds its fair value, the fair value of the reporting unit's goodwill is compared with its carrying amount to measure the amount of the impairment loss, if any. Any impairment loss is charged to earnings in the period in which the loss is incurred. We use a combination of the discounted cash flow method and the market value method to determine the fair value of reporting units.

Intangible assets are amortized over the useful life of the underlying asset. No amortization is recorded where the asset has an infinite life or is not determinable. Any intangible assets not subject to amortization are tested annually for any impairment. 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 undiscounted 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.

Amortization is recorded on a straight line basis over the estimated useful life of the assets. Customer relationships and technology are amortized over seven years, sales backlog is amortized over one year and any trade names are not amortized until a decision is made to end trade name at which time the amortization will take place over the remaining expected life of the trade name.

#### *INCENTIVE COMPENSATION*

We have Incentive Plans of which most employees are members. One such Incentive Plan establishes Target and Stretch performance levels against which the performance of the Company and its senior managers are measured. Each quarter we accrue an amount equal to one quarter of the estimated Incentive Plan payout, based on the Company meeting its Target performance levels. The actual amount paid could be different from the amounts estimated in interim periods requiring an adjustment, usually in the fourth quarter of the year.

The fair value of stock-based compensation is estimated using a Black-Scholes option pricing methodology. The principal assumptions required for the Black-Scholes methodology are assumptions about the expected life of the options, and the expected volatility and dividend policy of the underlying stock over the expected life of the options.

## **9.4 INTERNATIONAL FINANCIAL REPORTING STANDARDS ('IFRS')**

### **Background, project structure and project progress**

In March 2006, the CICA released its plan to adopt International Financial Reporting Standards. ("IFRS") After a five year transitional period, at the end of 2011, Canadian GAAP will cease to exist as a separate basis of financial reporting for public companies.

We will issue consolidated financial statements in accordance with IFRS as issued by the International Accounting Standards Board (“IASB”) for the year ended September 30, 2012, with comparative information.

### **Preliminary Impact Assessment**

We have completed a diagnostic study of the conversion of its consolidated financial statements to IFRS, with the assistance of external consultants. The study identified the principal differences between the Company’s records using existing Canadian GAAP and IFRS standards, and evaluated the impact on the business processes information systems, developing an implementation program determine the full impact on the business.

The results of this assessment identified:

- Preliminary analysis of all Canadian GAAP to IFRS differences and IFRS 1 First time adoption elections and resulting prioritization of high, medium and low impact areas of focus for the Company based on potential impact;
- Preliminary resource requirements;
- Preliminary training requirements; and
- A preliminary IFRS Transition Plan (details outlined below).

### **IFRS Transition Plan**

We have formalized the IFRS Transition Plan. The following are elements of the plan that are currently in place:

- An established project structure and governance practices;
- Detailed timetable with milestones and deliverables;
- Identification and allocation of resources (combination of internal and external);
- Development and execution of a training program;
- Detailed analysis of all Canadian GAAP to IFRS differences;
- Detailed analysis and selection of all IFRS 1 elections; and
- Assessment of impact on data systems, internal controls over financial reporting, and business activities, such as financing and compensation arrangements.

We have completed the detailed assessment phase for all standards that affect the transition to IFRS. We are currently in the implementation phase on many of the IFRS issues including construction of full financial statements.

### **Potential accounting changes as a result of transition to IFRS**

We have implemented a detailed review of the potential impact of International Financial Reporting Standards, IFRS, on our accounting policies, knowledge of staff and computerized system requirements. Outlined below is a very brief summary of select IFRS that may impact our company, its differences from Canadian Generally Accepted Accounting Principles (“GAAP”) and their potential impact. The list is not comprehensive and does not include all of the differences from GAAP for the standards noted. Also, the list does not include all the standards that may require changes for the transition to IFRS. Some of the standards not presented in the table could have a significant impact on our consolidated financial statements.

**Property Plant & Equipment ('PP&E')** – IAS 16 Property Plant and Equipment requires that each part of PP&E that has a cost significant in relation to the overall cost of the item should be depreciated separately. We have reviewed componentization of PP&E and do not expect any material adjustments upon transition to IFRS.

**Share Based Payments** – Under IFRS 2 *Share-based payments*, stock options with graded vesting must be accounted for as separate awards. In addition, forfeitures must be estimated when the stock options are issued.

We have decided to apply the IFRS 1 election available, meaning only equity instruments in respect of share-based payment transactions that are outstanding at transition date will be accounted for under IFRS 2.

We have conducted a review of its share-based payment transactions outstanding at the transition date and have determined that there will be no significant impact on transition date. The Company currently accounts for awards with graded vesting features as separate awards and there is no material difference anticipated by applying a forfeiture rate to share-based payment transactions. We expect to reassess this conclusion for any fiscal 2011 transactions.

**Foreign Exchange Translation** - We sell products to customers in foreign currencies and purchases services and raw materials from suppliers invoiced in foreign currencies. An analysis was undertaken to determine what the functional currency is under IFRS for each subsidiary.

This analysis has determined that there will be no change to the functional currency for any of our subsidiaries under IFRS. We have also elected to apply the IFRS 1 election to allow it to not calculate the translation difference in relation to certain exchange gains and losses recognized in other comprehensive income. As a result of the election the cumulative translation balance for all the foreign operations is set at zero at the date of transition. We will continue to monitor this conclusion to ensure that no adjustment is required.

**Revenue** - IFRS 1 does not contain any special exemptions for revenue for first-time adoption. All accounting policies related to revenue were assessed against the appropriate standard including IAS 18, *Revenue* for compliance.

The results indicated that there will be no significant change to the recognition or classification policy for revenue under IFRS.

**Business Combinations** – we have elected not to restate business combinations prior to the transition date, as permitted under IFRS 1. Any business combinations that occur prior to October 1, 2011 will be accounted for under Canadian Institute Chartered Accountants (“CICA”) Accounting Handbook Section 1582 Business Combinations, which mirrors IFRS 3 Business Combinations.

**Presentation & Disclosure** - IFRS requires significantly more disclosure than GAAP for certain standards. In some cases, IFRS also requires different presentation on the balance sheet and income statement.

After review of the standards noted above and other differences from GAAP, we do not expect any significant impact of IFRS on its financial statements. However, we continue to reassess its evaluations and accounting policy choices and have the ability to adjust or modify conclusions up to the release of our first IFRS statements.

We have completed its analysis of IFRS issues including evaluation of any IFRS 1 exemptions. The project is now in the process of documenting accounting policies under IFRS, creating additional note disclosures and developing a full set of IFRS statements. Note that consistent with many other entities transitioning to IFRS the Company will revisit its evaluations and accounting policy choices up to and including the date of the release of its first IFRS statements.

The IASB has several projects slated for completion in 2011. We originally anticipated that these may significantly impact the transition to IFRS and our financial statements. We have monitored release of new standards and have opted against early adopting; therefore there will be no impact for the first IFRS financial statements. We continue to monitor the IASB's progress on future projects and their impact on our ongoing IFRS reporting.

### **Impact on Information Systems and Technology**

It is anticipated that the adoption of IFRS will have some impact on information systems requirements. We are assessing, through discussion with external consultants, the need for systems upgrades or modifications to ensure an efficient conversion to IFRS. The main drivers for systems changes include:

- Additional information required as a result of enhanced note disclosures;
- Tracking of IFRS to GAAP differences during the transition; and
- Tracking sufficient level of details within the accounting records to allow management to maintain adherence with IFRS going forward.

As the conversion to IFRS progresses, additional information will need to be maintained. The impact on systems and existing processes is still being evaluated. These changes are expected to be manageable and will be prioritized as part of the project.

### **Impact on Reporting and Internal Controls**

In accordance with the Company's approach to certification of internal controls required under Canadian Securities Administrators' National Instrument 52-109, all entity-level, information technology, disclosure and business process controls will require updating and testing to reflect changes arising from the conversion to IFRS. Where material changes are identified, these changes will be mapped and tested to ensure that no material control deficiencies exist as a result of the Corporation's conversion to IFRS. Adjustments to internal controls in response to the conversion to IFRS have been scheduled. The additional controls are not expected to be significant but will continue to be evaluated as the conversion continues.

### **Training**

We have begun training for finance personnel with respect to IFRS. In addition, training has commenced for senior management and audit committee members. The Company will continue to monitor and evaluate the need for training as a result of the IFRS conversion.

### **Impact on Business**

We have reviewed the impact IFRS will have on business practices. Given our expectation that there will be no material differences, we do not expect there to be a significant impact on contractual or business relationships. However, we will monitor new accounting standards issued by the IASB to determine any future impact on the business.