
Versatile Mobile Systems (Canada) Inc.
SCHEDULE C
Management Discussion and Analysis
Year Ended June 30, 2003

The company is primarily engaged in software development and sales of computer software, hardware and systems integration services related to wired and wireless mobile business solutions.

Review of operations

Revenue for the year ended June 30, 2003 was \$20,596,215 compared to \$16,033,453 in 2002, an increase of 28.5%. The loss for the year was \$2,739,753 (\$0.03 per share) compared to a loss of \$20,022,397 (\$0.27 per share) for 2002, which included a loss from discontinued operations of \$11,224,852 (\$0.15 per share), a decrease of 86.3%.

For the year, the EBITDA loss (loss before interest expense, taxes, depreciation, amortization, write-down of capital assets and write-down of goodwill) was \$2,204,177. This compares to an EBITDA loss for fiscal 2002 of \$4,961,596 which was made up of \$3,706,516 from operations and \$1,255,080 from discontinued operations. These EBITDA amounts are provided by management as a complement to the financial results reported in accordance with GAAP in order to provide investors additional information concerning the company's use of cash in its operations.

In adopting CICA Handbook Section 3062, Goodwill and Other Intangible Assets issued in August, 2001, the company was required to assess whether the intangible assets previously identified as part of the acquisition of the U.S. operations met the new definition of intangible assets. In performing this assessment, the company determined that the acquired workforce and developed technology no longer met the criteria of an intangible asset. As such, the company reclassified a net balance of \$2,222,498 from intangible assets to goodwill.

Also in adopting CICA Handbook Section 3062, the company is required to evaluate the carrying value of goodwill for impairment annually, or more frequently if events or changes in circumstances indicate that the asset may be impaired. During the year, the company performed an assessment of the carrying value of goodwill and found that no impairment charge was required for the year.

Revenues increased by \$4,562,762 or 28.5% in the year over the previous year. The increase relates to the completion of several projects during the year, as well as increased orders from both the existing customer base and new customers. The most significant project completed was the Books are Fun Project, which resulted in a decrease in

deferred revenue as the Company was able to recognize as revenue invoiced amounts related to the Books are Fun Project, that was deferred in the prior year.

Cost of sales amounted to \$14,838,352 or 72.0% of sales for the year as compared to \$9,700,814 or 60.5% of sales in the previous year. The increase in the cost of sales percentage compared to last year can be attributed to the fact that sales in the current year were primarily related to lower margin hardware and peripheral sales as well as systems integration services. Further there has been an increase in competitive pressure in our market resulting in lower than expected gross margins.

General and administrative expenses for the year amounted to \$3,567,837 compared to \$3,681,009 last year. Professional fees, investor relations and communication costs were lower in the year. The reduction was partially offset by an increase in the allowance for doubtful accounts. Costs for salaries and remuneration for the year were approximately the same as last year.

Research and development expense for the year amounted to \$1,675,837 compared to \$3,114,258 for last year. Costs decreased as research and development work for several major initiatives was completed at the end of last year, which resulted in significant staff reductions. During the year the Company had many new product initiatives, along with feature improvements to current product lines. New products released during the year included:

- VM Dex for the Pocket PC™ operating system,
- VM Pre-Sales for the Pocket PC™ operating system,
- VM Delivery for the Pocket PC™ operating system,
- DEX In A Box, and
- Planogram

The significant expense item in this category is salary and benefit costs, which amounted to \$1,190,367 compared to \$2,984,576 last year.

Selling and marketing expense for the year amounted to \$2,732,892 compared to \$3,109,486 last year. The decrease from last year is attributable to lower advertising and promotion costs, travel expense and lower staffing levels as a result of the company refocusing its sales activities on fewer but larger customers. Selling and marketing expenses in the upcoming year have been budgeted to increase to support new sales initiatives.

Fourth Quarter

Revenue for the three months ended June 30, 2003 was \$4,295,177 compared to \$3,318,732 for the same period last year an increase of 29.4%. The loss for the quarter was \$772,940 (\$0.01 per share) compared to a loss of \$4,406,428 (\$0.06 per share) for the same period last year which included a loss from discontinued operations of \$735,983 (\$0.01 per share), a decrease of 82.5%.

For the quarter, the EBITDA loss (loss before interest expense, taxes, depreciation, amortization, write-down of capital assets and write-down of goodwill) was \$550,278. This compares to an EBITDA loss for the same quarter last year of \$2,537,889, which was made up of \$2,016,123 from operations and \$521,766 from discontinued operations. These EBITDA amounts are provided by management as a complement to the financial results reported in accordance with GAAP in order to provide investors additional information concerning the company's use of cash in its operations.

Financial position

Working capital at June 30, 2003 was \$1,157,591 versus \$3,961,949 at June 30, 2002. Cash and cash equivalents at June 30, 2003 amounted to \$1,152,287. The ability of the Company to continue operations on an ongoing basis will be dependent on its ability to generate sales, maintain its margins and control operating expenses. The company has cash on hand and accounts receivable sufficient for the company to meet all of its current obligations as they become due.

Cash required for continuing operations and non-cash working capital for the year was \$1,712,084 compared to \$4,259,981 in the previous year. Cash required for capital expenditures in the year amounted to \$114,994 and \$5,600 was realized from the sale of fixed assets. In addition, capital lease obligations were reduced by \$36,195.

The decrease in deferred revenue in the year is primarily related to the company being able to recognize as revenue invoiced amounts related to the Books are Fun project that was deferred in the prior year as required by generally accepted accounting principles. The invoiced amounts were recognized as revenue as the company completed all of its contractual obligations.

As a result of the completed transaction referred to above, there was a significant reduction in both accounts receivable of \$3,202,538 and accounts payable of \$1,480,547. These changes can be mainly attributed to the collection of monies owing and the payment of amounts due in relation to the Books are Fun project which were outstanding at June 30, 2002.

A significant amount of inventory at June 30, 2002 was related to the Books are Fun project. As a result of the completed transaction referred to above, inventory hardware invoiced and held by the company at the customer's request in the prior year was transferred to the customer. As a result, inventory decreased \$2,944,109 from \$4,038,803 at June 30, 2002 to \$1,094,694 at June 30, 2003. The company also completed the implementation of a new inventory management system and an extensive review of its inventory and recorded an inventory provision of \$171,000, which is recorded in the cost of sales.

The acquired business of EvolutionB was discontinued in the prior year as at June 30, 2002. During the current year, the company disposed of the remaining assets of EvolutionB and took a write-down on capital assets of \$95,276. Also during the year, the

company vacated the premises subleased by EvolutionB. At June 30, 2003 the discontinued operations had assets of \$1,430 and liabilities of \$282,527.

Share Capital

During the year, there were no changes in share capital.

During the year, 150,000 warrants expired.

Stock Options

On April 17, 2003, the Company granted employee, director and officer incentive stock options to acquire a total of 3,475,000 common shares of the Company vesting from 4 months up to 28 months and exercisable for a period of up to 4 years at a price of \$ 0.10 per share, which have been filed with the TSX Venture Exchange.

During the year, 1,859,000 stock options were forfeited or expired (2002 – 1,129,000) and no stock options were exercised (2002 – 7,500).

Foreign Exchange

Foreign exchange rates for the U.S. dollar fell during the year as the Canadian dollar strengthened. The closing rate was 1.3475 at June 30, 2003 compared to 1.5162 at June 30, 2002. The average rate for fiscal 2003 was 1.5129 compared to 1.5688 for fiscal 2002. The significant change in the rates had an impact on the current year's financial statements as most of the company's operations are in the U.S., which operates its business in U.S. dollars, which are translated into Canadian dollars at the prevailing rate. The substantial change in the foreign exchange rate occurred in the fourth quarter and had a negative impact on the net monetary position and the results for the fourth quarter.

Related Party Transactions

Related party transactions are disclosed in Note 13 in the audited financial statements.

Management Changes

On October 29, 2002, Robert Polychron was appointed the President of the U.S. subsidiary.

On February 22, 2003, Fraser Atkinson, C.A. was appointed Chief Financial Officer of the Company.

On April 17, 2003, Malcolm F. Clay, B.A., FCA was appointed to the Board of Directors of the company.

Investor relations

During the year Russ Millward was engaged at a total cost of \$71,928. As of March 31, 2003, John Hardy, CEO and Fraser Atkinson, CFO assumed the investor relations function.

Forward-Looking Statements

This document may contain forward-looking statements relating to Versatile Mobile Systems' operations or to the environment in which it operates, which are based on Versatile Mobile Systems' operations, estimates, forecasts and projections. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict or are beyond Versatile Mobile Systems' control. A number of important factors including those set forth in other public filings could cause actual outcomes and results to differ materially from those expressed in these forward looking statements. Consequently readers should not place any undue reliance on such forward-looking statements. In addition, these forward looking statements relate to the date on which they are made. Versatile Mobile Systems disclaims any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise.