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**Versatile Systems Inc.**  
**Consolidated Financial Statements**  
**December 31, 2010**

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Consolidated Balance Sheets

Consolidated Statements of Operations and Deficit

Consolidated Statements of Comprehensive (Loss) Income

Consolidated Statements of Cash Flows

Notes to Consolidated Financial Statements

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# Versatile Systems Inc.

## Consolidated Balance Sheets

(Unaudited - Prepared by Management)

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Expressed in U.S. dollars

December 31, 2010    June 30, 2010  
(unaudited)

### ASSETS

#### Current Assets

Cash and cash equivalents	\$ 923,825	\$ 1,738,036
Investment in Equus (note 3)	2,407,405	2,203,043
Accounts receivable	10,814,932	10,580,706
Current portion of deferred contract costs	5,509,052	5,793,180
Prepaid expenses	277,956	236,993
Inventory	1,806,109	1,719,477
Future income tax benefits (note 8)	731,006	721,975
	<u>22,470,285</u>	<u>22,993,410</u>

Long-term accounts receivable

318,386

265,612

Deferred contract costs

758,408

598,366

Capital Assets

356,972

519,391

Intangible assets

-

459

Future income tax benefits (note 8)

6,186,924

6,243,875

Goodwill

9,914,350

9,914,350

\$ 40,005,325    \$ 40,535,463

### LIABILITIES

#### Current Liabilities

Line of credit (note 4)	\$ 815,855	\$ 1,353,312
Accounts payable and accrued liabilities	10,008,427	9,955,342
Current portion of deferred revenue	7,264,273	7,432,210
	<u>18,088,555</u>	<u>18,740,864</u>

Deferred Revenue

847,983

710,269

18,936,538

19,451,133

### SHAREHOLDERS' EQUITY

Share Capital (note 5)	54,433,709	54,433,709
Warrants (note 6)	186,367	186,367
Contributed surplus	4,231,539	4,231,539
Deficit	(36,876,185)	(36,965,836)
Accumulated other comprehensive loss	(906,643)	(801,449)
	<u>21,068,787</u>	<u>21,084,330</u>

\$ 40,005,325    \$ 40,535,463

APPROVED BY THE DIRECTORS:

DIRECTOR: *John Hardy*

DIRECTOR: *Fraser Atkinson*

See Notes to Consolidated Financial Statements

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# Versatile Systems Inc.

## Consolidated Statements of Operations and Deficit

(Unaudited - Prepared by Management)

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*Expressed in U.S. dollars*

	Three months ended December 31		Six months ended December 31	
	2010	2009	2010	2009
SALES	\$ 15,460,033	\$ 11,259,292	\$ 24,679,083	\$ 22,875,517
COST OF SALES	12,491,896	8,599,212	19,607,119	17,560,133
	2,968,137	2,660,080	5,071,964	5,315,384
EXPENSES				
Selling and marketing	1,327,878	1,619,075	2,336,445	2,980,776
General and administrative	1,051,897	1,100,145	1,942,347	1,974,493
Research and development	278,909	247,084	471,177	493,754
Non recurring expenses	37,503	28,219	58,171	48,079
Stock-based compensation	-	23,242	-	45,630
Foreign exchange gain	(33,751)	(89,154)	(31,418)	(74,612)
	2,662,436	2,928,611	4,776,722	5,468,120
Earnings (loss) before interest, taxes and amortization	305,701	(268,531)	295,242	(152,736)
Amortization of capital assets	48,108	62,287	119,269	128,911
Amortization of intangible assets	-	90,675	-	181,349
Interest expense	666	10,441	15,636	14,210
Loss (Gain) on sale of capital assets and investments	2,575	(4,952)	2,575	(4,952)
EARNINGS (LOSS) BEFORE INCOME TAXES	254,352	(426,982)	157,762	(472,254)
Current income tax expense	(995)	(1,245)	(1,990)	(2,748)
Future income tax (expense) benefit	(74,392)	347,566	(66,121)	347,566
NET EARNINGS (LOSS)	178,965	(80,661)	89,651	(127,436)
DEFICIT, BEGINNING OF PERIOD	(37,055,150)	(35,775,990)	(36,965,836)	(35,729,215)
DEFICIT, END OF PERIOD	(36,876,185)	(35,856,651)	(36,876,185)	(35,856,651)
EARNINGS (LOSS) PER SHARE (basic and diluted)	\$0.00	(\$0.00)	\$0.00	(\$0.00)

*See Notes to Consolidated Financial Statements*

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## **Versatile Systems Inc.**

### Consolidated Statements of Comprehensive (Loss) Income

(Unaudited - Prepared by Management)

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*Expressed in U.S. dollars*

	Three Months ended December 31		Six Months ended December 31	
	2010	2009	2010	2009
Net earnings (loss)	178,965	(80,661)	89,651	(127,436)
Other comprehensive (loss) income				
Net change in fair value of available-for-sale investments	141,415	-	(105,194)	-
Comprehensive (loss) income	<u>320,380</u>	<u>(80,661)</u>	<u>(15,543)</u>	<u>(127,436)</u>

*See Notes to Consolidated Financial Statements*

# Versatile Systems Inc.

## Consolidated Statements of Cash Flows

(Unaudited - Prepared by Management)

*Expressed in U.S. dollars*

	Three Months ended December 31		Six Months ended December 31	
	2010	2009	2010	2009
<b>OPERATING ACTIVITIES</b>				
Net earnings (loss)	\$ 178,965	\$ (80,661)	\$ 89,651	\$ (127,436)
Items not affecting cash				
Amortization of capital and intangible assets	63,597	170,862	137,849	348,987
Stock-based compensation	-	23,242	-	45,630
Loss (Gain) on sale of capital assets and investments	2,575	(4,952)	2,575	(4,952)
Unrealized foreign exchange gain	(20,886)	(38,209)	(20,391)	(42,539)
Future income tax expense (benefit)	74,392	(347,566)	66,121	(347,566)
Cash flow used in operations before other items	298,643	(277,284)	275,805	(127,876)
Net change in non-cash operating balance sheet items	(415,708)	41,236	(267,647)	(2,157,242)
	(117,065)	(236,048)	8,158	(2,285,118)
<b>INVESTING ACTIVITIES</b>				
Short term investments	(309,556)	(567,558)	(309,556)	(2,300,835)
Proceeds from disposition of capital assets	30,174	7,701	103,268	7,701
Additions to capital assets	(38,799)	(21,414)	(78,624)	(37,266)
	(318,181)	(581,271)	(284,912)	(2,330,400)
<b>FINANCING ACTIVITIES</b>				
Proceeds from issuance of shares	-	3,876,257	-	3,876,257
Share issue costs	-	(26,291)	-	(26,291)
Proceeds from (repayment of) line of credit	(104,426)	(503,051)	(537,457)	2,558,445
	(104,426)	3,346,915	(537,457)	6,408,411
Increase (decrease) in cash and cash equivalents	(539,672)	2,529,596	(814,211)	1,792,893
CASH and cash equivalents, beginning of period	1,463,497	1,265,827	1,738,036	2,002,530
CASH and cash equivalents, end of period	\$ 923,825	\$ 3,795,423	\$ 923,825	\$ 3,795,423
<b>Supplementary information</b>				
Cash paid for interest expense	\$ 4,929	\$ 14,130	\$ 16,993	\$ 14,672
Cash paid for income taxes	1,050	1,455	2,469	2,963

*See Notes to Consolidated Financial Statements*

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# Versatile Systems Inc.

## Notes to Consolidated Financial Statements

### For the period ended December 31, 2010

(Unaudited - Prepared by Management)

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#### 1. Consolidated financial statement presentation:

These unaudited interim consolidated financial statements at December 31, 2010 and the consolidated statements of operations and deficit, comprehensive income (loss) and cash flows for the periods ended December 31, 2010 and 2009, have been prepared in accordance with Canadian generally accepted accounting principles. These unaudited interim financial statements do not include all the disclosures required for annual audited financial statements and should be read in conjunction with the Company's annual audited consolidated financial statements and notes therein for the year ended June 30, 2010.

The results of operations for the periods ended December 31, 2010 are not necessarily indicative of the results for the full year ending June 30, 2011. All amounts herein, including the comparative figures, have been expressed in United States dollars unless otherwise

The financial statements as at and for the period ended December 31, 2010 have not been reviewed or audited by the Company's auditor.

#### 2. Accounting Policies

The accounting policies applied in these interim financial statements are consistent with those applied in the Annual financial statements.

#### 3. Investment in Equus

The Investment in Equus consists of 962,962 shares of Equus Total Return, Inc. which is a public company trading on the NYSE under the symbol EQS. The share price as at December 31, 2010 was \$2.50 so the unrealized gain for the quarter was \$141,415 and the cumulative unrealized loss was \$624,864.

#### 4. Bank Line of Credit

The Company has a credit line facility for up to \$5,800,000, which is limited to 70% of eligible accounts receivable of certain U.S. subsidiaries from a U.S. based financial institution. At December 31, 2010 this amounted to \$5,800,000. The line of credit bears interest at the prime rate of lending as published in the Wall Street Journal and is secured with a first charge on the assets of these U.S. subsidiaries.

#### 5. Share Capital

Authorized

Unlimited common shares without par value

Issued and outstanding

Issued and outstanding - June 30, 2010

Issued during the period

Balance - December 31, 2010

	Number of shares	Amount
Issued and outstanding - June 30, 2010	157,285,643	\$ 54,433,709
Issued during the period	-	-
Balance - December 31, 2010	157,285,643	\$ 54,433,709

**Versatile Systems Inc.**  
**Notes to Consolidated Financial Statements**  
**For the period ended December 31, 2010**

(Unaudited - Prepared by Management)

**6. Warrants**

Issued and outstanding:

Expiry date	Exercise Price CDN\$	Number of Warrants	Cost
March 31, 2011	\$ 0.569	1,411,808	\$ 63,309
April 16, 2011	\$ 0.6636	583,770	81,058
January 22, 2012	\$ 0.30	600,000	42,000
Balance - December 31, 2010		<u>2,595,578</u>	<u>\$ 186,367</u>

**7. Stock Options**

	Number of Stock Options	Weighted average exercise price CDN\$
Balance - June 30, 2010	7,901,000	\$ 0.45
Granted during the period	-	
Forfeited during the period	(225,000)	\$ 0.10
Expired during the period	(3,125,000)	\$ 0.94
Balance - December 31, 2010	<u>4,551,000</u>	<u>\$ 0.12</u>

During the second quarter 1,610,000 stock options expired and during the first quarter 1,515,000 stock options expired and 225,000 stock options were forfeited.

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**Notes to Consolidated Financial Statements**  
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(Unaudited - Prepared by Management)

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**8. Income taxes**

Canadian GAAP requires a valuation allowance to be recorded against any future tax asset to the extent that it is more likely than not that the future income tax asset will not be realized. This is also the Company's stated accounting policy.

	<u>December 31, 2010</u>	<u>June 30, 2010</u>
	(unaudited)	
Future income tax assets		
Tax losses and deductions	\$ 8,990,499	\$ 8,929,483
Capital assets	1,078,107	1,063,918
Share issuance costs	123,435	115,754
Other	347,103	338,000
	<hr/>	<hr/>
Future income tax assets	10,539,144	10,447,155
Valuation allowance	(2,865,564)	(2,725,655)
	<hr/>	<hr/>
Net Future income tax asset	7,673,580	7,721,500
Future income tax liabilities - Goodwill	(755,650)	(755,650)
	<hr/>	<hr/>
Net Future income tax asset	6,917,930	6,965,850
Less current portion	(731,006)	(721,975)
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Non-current portion of net future income tax asset	\$ 6,186,924	\$ 6,243,875

During the three months ended December 31, 2010 the Company recorded a future income tax expense of \$74,392 related to the recognition of future income tax assets compared to a future income tax benefit of \$347,566 for the comparable period last year.

# Versatile Systems Inc.

## Notes to Consolidated Financial Statements

### For the period ended December 31, 2010

(Unaudited - Prepared by Management)

#### 9. Segmented Information

The Company's only reportable segment is the development and sales of computer software, hardware and system integration services.

The Company's assets and sales by geographic area are as follows:

	December 31 2010 (unaudited)	June 30 2010	Three months ended December 31	
			2010 (unaudited)	2009 (unaudited)
	Capital assets, intangible assets and goodwill	Capital assets, intangible assets and goodwill	Revenue	Revenue
<i>U.S. companies</i>				
United States	\$ 10,267,025	\$ 10,431,566	\$ 15,112,456	\$ 10,949,663
Canada			81,507	138,802
Netherlands			10,460	16,579
France			37,120	32,390
United Kingdom			30,000	16,884
Australia			12,050	
Other			9,852	32,906
<i>UK and Canadian companies</i>				
United Kingdom	4,297	2,634	166,588	72,068
Canada	-	-	-	-
	10,271,322	10,434,200	15,460,033	11,259,292

During the three months ended December 31, 2010 the Company generated revenue of \$2,785,710 (2009 - \$1,804,020) from Comcast Cable representing 18.0% (2009 - 16.0%) of the revenue for that period.

During the three months ended December 31, 2010 the Company purchased products and services from one vendor for \$5,564,358 (2009 - \$3,551,944) representing 44.5% (2009 - 41.0%) of the cost of sales.