

Sensio Technologies Inc.

Financial Statements May 31, 2011 and 2010



SENSIO®

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Raymond Chabot Grant Thornton

Independent Auditor's Report

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To the Shareholders of
Sensio Technologies Inc.

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We have audited the accompanying financial statements of Sensio Technologies Inc., which comprise the balance sheets as at May 31, 2011 and 2010 and the statements of earnings and comprehensive income, deficit and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting

policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, these financial statements present fairly, in all material respects, the financial position of Sensio Technologies Inc. as at May 31, 2011 and 2010 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

/S/Raymond Chabot Grant Thornton LLP¹

Montréal
September 21, 2011

¹ Chartered accountant auditor permit no. 18510

Sensio Technologies Inc.

Earnings and Comprehensive Income

Years ended May 31, 2011 and 2010

	2011	2010
	\$	\$
Sales		
Revenues	1,201,857	669,595
Other	51,410	23,773
	<u>1,253,267</u>	<u>693,368</u>
Cost of sales		
Revenues	17,741	152,452
Other	9,988	4,949
	<u>27,729</u>	<u>157,401</u>
Gross profit	<u>1,225,538</u>	<u>535,967</u>
Selling expenses	2,954,231	1,834,632
Research and development expenses	971,191	516,119
Administrative expenses	1,673,529	1,279,443
Stock-based compensation (Note 17)	203,140	96,329
Financial expenses	45,690	30,819
	<u>5,847,781</u>	<u>3,757,342</u>
Interest income on the term deposit	105,145	42,633
Interest income on cash	4,164	4,288
	<u>109,309</u>	<u>46,921</u>
	<u>5,738,472</u>	<u>3,710,421</u>
Net loss and comprehensive income	<u>(4,512,934)</u>	<u>(3,174,454)</u>
Basic and diluted net loss per share (Note 6)	<u>(0.0870)</u>	<u>(0.0670)</u>
Weighted average number of shares outstanding	<u>51,888,742</u>	<u>47,359,876</u>

The accompanying notes are an integral part of the financial statements and Note 4 provides other information on earnings.

Sensio Technologies Inc.**Deficit**

Years ended May 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
	\$	\$
Balance, beginning of year	12,327,309	9,152,855
Net loss	<u>4,512,934</u>	<u>3,174,454</u>
Balance, end of year	<u><u>16,840,243</u></u>	<u><u>12,327,309</u></u>

The accompanying notes are an integral part of the financial statements.

Sensio Technologies Inc.

Cash Flows

Years ended May 31, 2011 and 2010

	2011	2010
	\$	\$
OPERATING ACTIVITIES		
Net loss	(4,512,934)	(3,174,454)
Non-cash items		
Amortization of property, plant and equipment	211,166	177,777
Amortization of intangible assets	244,663	141,271
Amortization of lease inducements	(23,500)	(13,840)
Stock options issued to a consultant (Note 17)	198,306	113,559
Stock-based compensation	203,140	96,329
Unrealized exchange loss on balance of purchase price of rights to use a technology		(6,617)
Implicit interest relating to a term loan and the balance of purchase price of rights to use a technology		9,899
Changes in working capital items (Note 7)	353,510	(316,272)
Cash flows from operating activities	<u>(3,325,649)</u>	<u>(2,972,348)</u>
INVESTING ACTIVITIES		
Term deposit	4,574,388	(9,825,244)
Purchase of assets (Note 8)	(586,000)	
Property, plant and equipment	(408,984)	(46,034)
Intangible assets	(148,231)	(149,793)
Distribution rights	(304,143)	
Cash flows from investing activities	<u>3,127,030</u>	<u>(10,021,071)</u>
FINANCING ACTIVITIES		
Repayment of long-term debt	(153,600)	(164,700)
Issue of equity instruments	404,391	13,946,945
Equity instrument issue expenses		(896,437)
Lease inducements	48,300	
Cash flows from financing activities	<u>299,091</u>	<u>12,885,808</u>
Net increase (decrease) in cash	<u>100,472</u>	<u>(107,611)</u>
Cash, (bank overdraft) beginning of year	<u>(31,247)</u>	<u>76,364</u>
Cash (bank overdraft), end of year	<u>69,225</u>	<u>(31,247)</u>

The accompanying notes are an integral part of the financial statements.

Sensio Technologies Inc.

Balance Sheets

May 31, 2011 and 2010

	2011	2010
	\$	\$
ASSETS		
Current assets		
Cash	69,225	
Term deposit, 0.75% (1.27% in 2010), maturing in May 2012	6,026,507	10,600,895
Accounts receivable (Note 9)	440,894	436,315
Inventories (Note 10)	163,558	127,354
Prepaid expenses	15,182	32,919
	<u>6,715,366</u>	<u>11,197,483</u>
Property, plant and equipment (Note 11)	639,381	392,533
Intangible assets (Note 12)	671,905	328,969
Goodwill	316,905	
Security deposit (Note 13)	12,373	12,373
Distribution rights	304,143	
	<u>8,660,073</u>	<u>11,931,358</u>
LIABILITIES		
Current liabilities		
Bank overdraft		31,247
Accounts payable and accrued liabilities	1,024,106	452,247
Instalments on long-term debt (Note 14)		129,600
	<u>1,024,106</u>	<u>613,094</u>
Lease inducements (Note 15)	73,240	48,440
	<u>1,097,346</u>	<u>661,534</u>
SHAREHOLDERS' EQUITY		
Capital stock (Note 16)	22,265,520	21,588,734
Contributed surplus (Notes 16, 17 and 18)	2,137,450	2,008,399
Deficit	(16,840,243)	(12,327,309)
	<u>7,562,727</u>	<u>11,269,824</u>
	<u>8,660,073</u>	<u>11,931,358</u>

The accompanying notes are an integral part of the financial statements.

On behalf of the Board,

/S/ Nicholas Routhier

Director

/S/ Yvan Goineau

Director

Sensio Technologies Inc.

Notes to Financial Statements

May 31, 2011 and 2010

1 - GOVERNING STATUTES AND NATURE OF OPERATIONS

The Company, incorporated under Part IA of the Companies Act (Québec), develops and markets stereoscopic technologies for the electronic consumer, digital broadcasting and digital cinema markets.

2 - ACCOUNTING CHANGES

Recently adopted standards

Business combinations

In January 2009, the CICA published Section 1582, "Business Combinations", replacing Section 1581 which bears the same title.

Section 1582's objective is to improve the relevance, reliability and comparability of information relating to a business combination and to its effects on the financial statements of the reporting entity.

Section 1582 is applicable to business combinations where the acquisition date occurs in a financial year beginning on or after January 1, 2011. Since June 1, 2010, the Company has adopted section 1582 by anticipation. Consequently, the acquisition of Algolith's assets described in Note 8 was accounted for in accordance with the requirements of Section 1582.

3 - SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The financial statements are prepared using the historical cost method, except for certain financial instruments that are recognized at fair value. No information on fair value is presented when the carrying amount corresponds to a reasonable approximation of the fair value.

Accounting estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements and notes to financial statements. The principal estimates include the allowance for doubtful accounts, the allowance for the research and development tax credit receivable, and the useful lives of property, plant and equipment and intangible assets and their recoverable value and the fair value of goodwill. These estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future. Actual results may differ from these estimates.

Financial assets and liabilities

On initial recognition, all financial assets and liabilities are measured and recognized at their fair value, except for financial assets and liabilities resulting from certain related party transactions.

Sensio Technologies Inc.

Notes to Financial Statements

May 31, 2011 and 2010

3 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Subsequently, financial assets and liabilities are measured and recognized as follows:

Held-for-trading financial assets

Cash is classified as held-for-trading financial assets and is measured at its fair value.

Loans and receivables

Trade and other accounts receivable are classified as loans and receivables. They are measured at amortized cost, which is generally the recognized amount, less any allowance for doubtful accounts, if any.

Available-for-sale financial assets

The term deposit and interest on the term deposit receivable are classified as available-for-sale financial assets and measured at their fair value. Related unrealized gains or losses are recognized in other comprehensive income until these gains or losses are realized or a decline in value of the financial asset is other than temporary.

Other financial liabilities

The bank overdraft, accounts payable and accrued liabilities, and the long-term debt are classified as other financial liabilities and are measured at amortized cost using the effective interest method. Interest on other financial liabilities is calculated using the effective interest method and is presented in earnings under Financial expenses.

Embedded derivatives

Embedded derivatives that are not closely related to the host contract must be separated and classified as held-for-trading financial instruments. They are then measured at fair value; changes in fair value are recognized in earnings and transaction costs from these embedded derivatives are recognized in earnings as administrative expenses. As at May 31, 2011 and 2010, the Company has no hybrid instrument including an embedded derivative that should be separated from the host contract.

Revenue recognition

Revenue is recognized when persuasive evidence of an arrangement exists, the price to the buyer is fixed or determinable, delivery has occurred and collection is reasonably assured.

Certain contracts include multiple elements or deliverables. The accounting policies for contracts including multiple elements require the Company to allocate the value of the contract among the various elements of the contract based on the fair value of each element and recognize the revenue for each element when revenue recognition criteria are met. To determine the fair value of each element, the Company uses a variety of factors such as the price charged for an element when it is sold separately and any other information considered to be relevant by management.

Amounts billed or received that do not satisfy revenue recognition criteria are recorded as deferred revenue.

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

3 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income from the sale of creative services which is included in other revenue is recognized using the percentage-of-completion method. Under this method, income including profits is recognized proportionately with the degree of completion of the work. The Company uses the efforts expended method to calculate the degree of completion of the work based on hours incurred at the date of the financial statements compared to total estimated hours. Work in process is valued taking into account the hours worked to be invoiced and the disbursements made for customers including the estimated profits. Losses are recorded once an estimate of total costs indicates a loss.

Interest income is calculated based on the number of days the investment was held during the year and calculated using the effective interest method.

Inventory valuation

Inventory is valued at the lower of cost and net realizable value. Cost is determined by the average cost method.

The cost of inventories includes all acquisition costs and other costs incurred to bring the inventories in their present condition.

The net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs necessary to make the sale.

Any write-down of inventory to bring it to its net realizable value and all inventory losses are recognized as expenses for the year in which the write-down or loss occurred. The amount of any reversal of write-down of inventory resulting from an increase in the net realizable value is recognized as a reduction in the amount of inventory recognized as expenses for the year in which the reversal occurred.

Property, plant and equipment and intangible assets

Property, plant and equipment and intangible assets are recorded at cost and amortized over their estimated useful lives according to the straight-line method and following periods:

	<u>Periods</u>
Computer equipment	3 years
Office furniture, machinery and equipment	5 years
Leasehold improvements	Lease term of 7 years
Patents	5 years
Rights to use a technology	5 years
Web site	3 years
Software	3 years

Sensio Technologies Inc.

Notes to Financial Statements

May 31, 2011 and 2010

3 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment of long-lived assets

Property, plant and equipment and intangible assets subject to amortization are tested for recoverability when events or changes in circumstances indicate that their carrying amount may not be recoverable. The carrying amount of a long-lived asset is not recoverable when it exceeds the sum of the undiscounted cash flows expected from its use and eventual disposal. In such a case, an impairment loss must be recognized and is equivalent to the excess of the carrying amount of a long-lived asset over its fair value.

Goodwill

Goodwill is the excess of the cost of an acquired company over the net of the amounts assigned to acquired and the liabilities assumed. Goodwill is not amortized. It is tested for impairment annually or more frequently if events or changes in situation indicate that it may have depreciated. Goodwill is linked to a business unit and possible depreciation is detected by comparing the carrying amount with its fair value. If any potential impairment is identified, it is quantified by comparing the carrying amount of goodwill to its fair value. The fair value of a reporting unit is calculated using discounted cash flows.

Distribution rights

Distribution rights relate to the distribution of films. Costs include the cost of film acquisition rights and the costs incidental to such rights. The amounts paid for distribution rights are accounted for as distribution rights under "Distribution rights". Distribution rights are recognized in the cost of sales using the depreciation based on use method.

Research and development expenses and research and development tax credits

Research and development expenses are expensed as they are incurred. However, the development costs are deferred when they respect the capitalization criteria under Canadian generally accepted accounting principles.

Research and development tax credits are applied against research and development expenses during the year in which the costs are incurred, provided that the Company is reasonably certain that the credits will be received. The research and development tax credits must be examined and approved by the tax authorities and it is possible that the amounts granted will differ from the amounts recorded.

Income taxes

The Company uses the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined according to the differences between the carrying amounts and tax bases of assets and liabilities. They are measured by applying enacted or substantively enacted tax rates and laws at the date of the financial statements for the years in which the temporary differences are expected to reverse. The Company recognizes future income tax assets only when it is more likely than not that some or all of the future income tax assets will be realized.

Sensio Technologies Inc.
Notes to Financial Statements
May 31, 2011 and 2010

3 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreign currency translation

Monetary assets and liabilities denominated in foreign currency are translated at the exchange rate in effect at the balance sheet date, whereas other assets and liabilities are translated at the exchange rate in effect at the transaction date. Revenue and expenses in foreign currency are translated at the average rate in effect during the year, with the exception of revenue and expenses relating to non-monetary assets and liabilities, which are translated at the historical rate. Gains and losses on financial assets and liabilities are included in the earnings for the year.

Share issue expenses

Share issue expenses are applied against shareholders' equity.

Earnings per share

Basic earnings per common share are calculated based on the weighted average number of shares outstanding during the year. Diluted earnings per share are calculated giving effect to the potential dilution that could occur if securities or other contracts to issue common shares were exercised. The treasury stock method is used to determine the dilutive effect of stock options and warrants. This method assumes that the proceeds from the exercise of in-the-money stock options are used to redeem common shares at the average market price during the period.

Stock option plan

The Company grants stock options, described in Note 17, to the eligible directors, officers, employees and consultants of the Company pursuant to its stock option plan. The stock-based compensation plan is recognized using the fair value method. The compensation cost is measured according to the fair value of the options using the stock price and other measurement assumptions and is recognized as follows:

The compensation cost of options granted to directors, officers and employees is measured on the grant date and recognized over the vesting period.

The compensation cost of options issued to consultants is recognized over the vesting period and measured according to the fair value of the options on each balance sheet date until the earlier of the consultant's option vesting date or the date on which the other party has completed the performance of its obligations by providing the services. Options which vest immediately are measured at the fair value on the grant date.

The compensation cost is expensed in the statement of earnings or capitalized according to the nature of the services received and credited to contributed surplus. The consideration paid on the exercise of the options and the fair value of the options exercised credited to contributed surplus are added to capital stock.

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

4 - INFORMATION INCLUDED IN EARNINGS

	<u>2011</u>	<u>2010</u>
	\$	\$
Research and development expenses		
Expenses	1,199,663	614,341
Research and development tax credits applied against research and development expenses	<u>(228,472)</u>	<u>(98,222)</u>
	<u>971,191</u>	<u>516,119</u>
Financial expenses		
Interest on long-term debt		5,112
Implicit interest relating to the balance of the purchases price of rights to use a technology		<u>9,899</u>
Total interest on long-term debt	-	15,011
Exchange loss	39,474	11,745
Other financial expenses	<u>6,216</u>	<u>4,063</u>
	<u>45,690</u>	<u>30,819</u>
Amortization of property, plant and equipment	211,166	177,777
Amortization of intangible assets	244,663	141,271

The Company earned 54% of its sales from one customer in 2011, a distributor residing in Canada that distributes the Company's products worldwide (93% in 2010).

5 - INCOME TAXES

The Company's effective income tax rate differs from the combined federal and provincial income tax rate in Canada. This difference arises from the following items:

	<u>2011</u>	<u>2010</u>
	\$	\$
Loss before income taxes	<u>(4,512,934)</u>	<u>(3,174,454)</u>
Income taxes at the combined federal and provincial income tax rate in Canada of 29.28% (30.48% as at May 31, 2010)	(1,321,387)	(967,574)
Increase resulting from the following:		
Difference between the tax rate used for future income taxes and the statutory tax rate	97,612	95,619
Non-deductible items and other	69,917	82,446
Unrecorded future income tax assets	1,153,858	730,937
Expiration of non-capital losses		<u>58,572</u>
	<u>-</u>	<u>-</u>

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

5 - INCOME TAXES (Continued)

The future income tax assets resulting from unused operating losses and deductions are not recorded in the financial statements. These unused losses and deductions, which are available to reduce income taxes in future years, aggregate \$15,206,215 for federal purposes and \$16,211,661 for provincial purposes and are detailed as follows:

	<u>Federal</u>	<u>Provincial</u>
	\$	\$
Amount of the tax loss carryforwards and deductions expiring within the following years:		
2014	372,713	350,086
2015	317,160	296,485
2026	417,040	393,932
2027	1,961,700	1,940,446
2028	1,678,069	1,709,636
2029	1,966,096	1,970,133
2030	2,900,662	2,903,488
2031	4,023,460	4,025,439
	<u>13,636,900</u>	<u>13,589,645</u>
Research and development expenses that may be carried forward indefinitely	<u>1,569,315</u>	<u>2,622,016</u>
	<u>15,206,215</u>	<u>16,211,661</u>

The Company has a research and development tax credit of approximately \$500,428 which will reduce the future federal tax payable, and expires until 2031.

The tax impact of the temporary differences resulting in unrecognized future income tax assets is detailed as follows:

	<u>2011</u>	<u>2010</u>
	\$	\$
Long-term future income tax assets		
Patents, rights to use a technology and goodwill	23,295	33,198
Lease inducement	19,702	13,030
Deferred share issue and financing expenses	169,770	243,885
Research and development expenses that may be deferred	547,417	414,870
Non-capital losses that may be deferred	3,662,703	2,604,078
	<u>4,422,887</u>	<u>3,309,061</u>
Long-term future income tax liabilities		
Property, plant and equipment	(45,996)	(19,450)
	<u>4,376,891</u>	<u>3,289,611</u>

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

6 - NET LOSS PER SHARE

Stock options that entitle holders to purchase 1,423,995 common shares were outstanding and as at May 31, 2011 (2,307,510 options and 298,333 warrants as at May 31, 2010) but were not into consideration when calculating the diluted loss per share, since the Company incurred losses and the inclusion of stock options in the calculation would have an anti-dilutive effect.

7 - INFORMATION INCLUDED IN CASH FLOWS

Changes in working capital items and the security deposit are detailed as follows:

	<u>2011</u>	<u>2010</u>
	\$	\$
Accounts receivable	(4,579)	(179,577)
Inventories	23,564	(49,298)
Prepaid expenses	17,737	21,909
Accounts payable and accrued liabilities	316,788	(104,588)
Security deposit		(4,718)
	<u>353,510</u>	<u>(316,272)</u>

Cash flows related to interest from operating activities are detailed as follows:

	<u>2011</u>	<u>2010</u>
	\$	\$
Interest paid	-	5,112

8 - ASSET ACQUISITION

On December 1, 2010, the Company acquired certain assets and assumed certain liabilities of Algolith Inc. in return for \$586,000 in cash.

The following table presents the estimated fair value of the net assets acquired at the acquisition date.

	<u>2011</u>
	\$
Assets acquired	
Inventories	59,768
Property, plant and equipment	49,029
Patents	252,000
Goodwill, deductible for tax purposes	316,905
Total of assets acquired	<u>677,702</u>
Liabilities assumed	
Accounts payable and accrued liabilities	67,702
Long-term debt	24,000
Total of assumed liabilities	<u>91,702</u>
Net assets acquired	<u>586,000</u>

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

8 - ASSET ACQUISITION (Continued)

The intangible assets are composed of patents. Goodwill consists of know-how in the R&D field.

9 - ACCOUNTS RECEIVABLE

	2011	2010
	\$	\$
Trade accounts (a)	129,505	319,489
Research and development tax credits receivable	146,688	79,938
Sales taxes receivable	159,082	35,413
Interest on the term deposit receivable	619	1,475
Other	5,000	
	<u>440,894</u>	<u>436,315</u>

(a) Percentages of 11%, 26% and 33% are receivable from three customers as at May 31, 2011 (97% receivable from one customer as at May 31, 2010).

10 - INVENTORIES

The amount of inventories recognized as an expense totals \$8,711 (\$140,419 in 2010) and corresponds to the cost of sales presented in the statement of earnings. This amount does not include any amount resulting from the write-down of inventories. No reversal of a previous write-down was recognized as a reduction of the amount of inventories recognized as an expense during the year (nil in 2010).

11 - PROPERTY, PLANT AND EQUIPMENT

	2011		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Computer equipment	258,177	164,111	94,066
Office furniture	78,979	40,971	38,008
Machinery and equipment	788,288	522,734	265,554
Leasehold improvements	445,757	204,004	241,753
	<u>1,571,201</u>	<u>931,820</u>	<u>639,381</u>
	2010		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Computer equipment	158,171	139,606	18,565
Office furniture	43,105	30,167	12,938
Machinery and equipment	609,220	399,504	209,716
Leasehold improvements	302,691	151,377	151,314
	<u>1,113,187</u>	<u>720,654</u>	<u>392,533</u>

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

11 - PROPERTY, PLANT AND EQUIPMENT (Continued)

Real estate acquisitions totalling \$31,738 are included in the Company's accounts payable and accrued liabilities as at May 31, 2010 (none as at May 31, 2011).

12 - INTANGIBLE ASSETS

	2011		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Patents	865,139	276,277	588,862
Rights to use a technology (a)	481,712	481,712	
Web site	93,476	15,579	77,897
Software	21,127	15,981	5,146
	<u>1,461,454</u>	<u>789,549</u>	<u>671,905</u>
	2010		
	Cost	Accumulated amortization	Net
	\$	\$	\$
Patents	374,856	174,069	200,787
Rights to use a technology (a)	481,712	356,636	125,076
Software	17,287	14,181	3,106
	<u>873,855</u>	<u>544,886</u>	<u>328,969</u>

(a) During the year ended May 31, 2007, the Company acquired the rights to use a technology, until 2011, to convert 2D images into 3D images in real time for a cash consideration of \$140,600 and a balance of purchase price payable of an amount of \$341,112 (which corresponds to US\$375,000 discounted at a rate of 7.75%).

Under the agreement to acquire the rights to use the technology, the Company is committed to pay royalties on annual sales until 2011, which are established on the basis of gross annual sales realized. The royalty rate was established by taking into consideration the relative value of the technology acquired compared to the technology developed by the Company.

Intangible assets acquisitions totalling \$210,410 (\$23,041 in 2010) are included in the Company's accounts payable and accrued liabilities as at May 31, 2011.

13 - SECURITY DEPOSIT

The security deposit includes a deposit applicable against the last month of rent of the lease expiring in June 2015.

Sensio Technologies Inc.
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14 - LONG-TERM DEBT

	<u>2011</u>	<u>2010</u>
	\$	\$
Balance of purchase price of rights to use a technology, denominated in U.S. dollars (US\$125,000 in 2010), without interest, discounted at the rate of 7.75%.	—	129,600

15 - LEASE INDUCEMENTS

This amount corresponds to inducements granted by the lessor to the Company that were collected during the fiscal years ended May 31, 2010 and 2007 for the completion of leasehold improvements. These advantages are amortized on a straight-line basis over the lease terms of five and seven years respectively.

16 - CAPITAL STOCK AND WARRANTS

Capital stock

Authorized

Unlimited number of common shares, voting and participating

Issued and fully paid

The following table presents the changes in the Company's capital stock during the periods:

	<u>Number</u>	<u>Amount</u>
		\$
Balance as at May 31, 2009	40,063,709	8,080,961
Warrants exercised	7,495,585	3,843,267
Reversal of contributed surplus following the exercise of warrants		999,658
Options exercised	181,655	87,178
Reversal of contributed surplus following the exercise of stock options		53,718
Bought deal private placement	3,852,500	10,016,500
Share issue expenses from bought deal private placement (net of a net future income tax asset of \$241,142 that had been entirely written-down)		(896,437)
Issue of 231,150 underwriters' warrants as part of the bought deal		(596,111)
Balance as at May 31, 2010	<u>51,593,449</u>	<u>21,588,734</u>
Warrants exercised	298,333	119,333
Reversal of contributed surplus following the exercise of warrants		41,614
Options exercised	593,515	285,058
Reversal of contributed surplus following the exercise of stock options		230,781
Balance as at May 31, 2011	<u><u>52,485,297</u></u>	<u><u>22,265,520</u></u>

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

16 - CAPITAL STOCK AND WARRANTS (Continued)

Year ended May 31, 2010

During the fiscal year ended May 31, 2010, the Company issued 7,495,585 common shares following the exercise of 7,495,585 warrants. In exchange for this share issue, the Company received \$3,843,267. An amount of \$999,658 was credited under the Company's capital stock and debited under contributed surplus.

During the fiscal year ended May 31, 2010, the Company issued 181,655 common shares following the exercise of 181,655 options. In exchange for this share issue, the Company received \$87,178. An amount of \$53,718 was credited under the Company's capital stock and debited under contributed surplus.

On December 14, 2009, the Company completed its bought deal private placement. Pursuant to the offering, 3,852,500 common shares of the Company were issued at a price of \$2.60 per common share for an aggregate gross proceed of \$10,016,500. An amount of \$896,437 was debited under the Company's capital stock as private placement issue expenses. In connection with the bought deal private placement, the Company awarded 231,150 options to underwriters entitling them to subscribe to 231,150 common shares at a price of \$2.60 per share. These options could be exercised until December 14, 2011. The fair value of the warrants, valued at \$596,111, was debited under the Company's capital stock and credited under contributed surplus.

Year ended May 31, 2011

During the fiscal year ended May 31, 2011, the Company issued 298,333 common shares following the exercise of 298,333 warrants. In exchange for this share issue, the Company received \$119,333. An amount of \$41,614 was credited under the Company's capital stock and debited under contributed surplus.

During the fiscal year ended May 31, 2011, the Company issued 593,515 common shares following the exercise of 593,515 options. In exchange for this share issue, the Company received \$285,058. An amount of \$230,781 was credited under the Company's capital stock and debited under contributed surplus.

Warrants

Warrants outstanding entitle holders to subscribe to an equal number of common shares and are described as follows:

	2011		2010	
	Number of warrants	Average exercise price	Number of warrants	Average exercise price
		\$		\$
Balance, beginning of year	298,333	0.40	11,772,668	0.54
Expired			(3,978,750)	0.60
Issued				
Exercised	(298,333)	0.40	(7,495,585)	0.51
Balance, end of year	—	—	298,333	0.40

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

17 - STOCK OPTION PLAN

The Company offers a stock option plan to its employees, directors, officers or consultants under which they are entitled to purchase common shares. The conditions for exercising options are determined by the members of the Board, however, this plan is governed by the regulations of the TSX Venture Exchange Inc. The exercise price is equal to the closing value of the stock market on the day preceding their grant. Under this plan, the maximum number of common shares reserved for issue shall not exceed 4,040,500 issued shares, and the options issued to any beneficiary cannot exceed 10% of the outstanding common shares at their grant date. The maximum number of common shares reserved for options excludes 229,995 stock options (229,995 in 2010) that are not due issued on December 14, 2009 pursuant to the bought deal private placement. The 229,995 stock options that are not due as at May 31, 2011 have a term of two years following their grant until December 2011. issue includes 86,015 stock options issued on March 6, 2006 as part of the initial public offering. These 86,015 stock options are exercised on May 31, 2011.

During the year ended May 31, 2011, the Company awarded 250,000 stock options to its employees and non-employees (182,000 in 2010). Moreover, the Company awarded 231,150 stock options to underwriters during the year ended May 31, 2010. The fair value of these options at the grant date was \$0.97 (\$2.35 and \$2.57 respectively in 2010) and was determined using the Black-Scholes option pricing model and the following weighted average assumptions:

	<u>2011</u>	<u>2010</u>	<u>2010</u>
	Employees and non-employees	Brokers compensation	Employees and non-employees
Rate of return of dividends	None	None	None
Expected volatility	100%	109%	108%
Risk-free interest rate	2.66%	3.05%	3.2%
Expected term of options	5 years	2 years	5 years

For the year ended May 31, 2011, the Company recognized an expense of \$203,140 (\$96,329 in 2010), for the purposes of the stock option plan and a professional fees expense of \$198,306 (\$113,559 in 2010) for options issued to a consultant, and credited these amounts under contributed surplus.

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

17 - STOCK OPTION PLAN (Continued)

The change in the Company's stock options is detailed as follows:

	Number of options	2011 Weighted average exercise price \$
Outstanding as at May 31, 2010	2,307,510	0.85
Expired during the year	(540,000)	3.12
Awarded during the year	250,000	1.27
Exercised during the year	<u>(593,515)</u>	0.48
Outstanding as at May 31, 2011 (a)	<u>1,423,995</u>	1.21
Exercisable at end of year	<u>922,662</u>	1.06

(a) As at May 31, 2011, 229,995 stock options granted to the brokers are excluded from the Company stock option plan (316,010 as at May 31, in 2010). These options are exercisable at \$2.60 per share and expire on December 14, 2011.

	Number of options	2010 Weighted average exercise price \$
Outstanding as at May 31, 2009	2,281,015	0.44
Expired during the year	(205,000)	0.42
Awarded during the year	413,150	2.74
Exercised during the year	<u>(181,655)</u>	0.48
Outstanding as at May 31, 2010	<u>2,307,510</u>	0.85
Exercisable at end of year	<u>1,922,177</u>	0.74

Sensio Technologies Inc.
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17 - STOCK OPTION PLAN (Continued)

The following table summarizes the information relating to the options outstanding as at May 31:

			2011	
Options outstanding			Options exercisable	
Number of options	Weighted average remaining term (years)	Weighted average exercise price \$	Number of options	Weighted average exercise price \$
100,000	1.17	0.60	100,000	0.60
40,000	1.32	0.55	40,000	0.55
30,000	1.55	0.43	30,000	0.43
90,000	1.68	0.30	90,000	0.30
207,000	2.19	0.17	207,000	0.17
45,000	2.91	0.44	45,000	0.44
255,000	2.96	0.41	103,334	0.41
37,000	3.51	3.12	12,333	3.12
100,000	3.60	3.18		
20,000	3.93	2.19	20,000	2.19
20,000	3.95	2.05	20,000	2.05
100,000	4.06	1.63		
20,000	4.12	0.97		
10,000	4.31	1.54	10,000	1.54
15,000	4.60	1.44	15,000	1.44
35,000	4.66	1.21		
70,000	4.92	0.81		
<u>229,995</u>	0.54	2.60	<u>229,995</u>	2.60
<u>1,423,995</u>	2.48	1.21	<u>922,662</u>	1.06

Sensio Technologies Inc.
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17 - STOCK OPTION PLAN (Continued)

			2010	
			Options exercisable	
Options outstanding				
Number of options	Weighted average remaining term (years)	Weighted average exercise price \$	Number of options	Weighted average exercise price \$
86,015	0.76	0.50	86,015	0.50
945,000	1.00	0.50	945,000	0.50
100,000	2.17	0.60	100,000	0.60
40,000	2.32	0.55	40,000	0.55
50,000	2.55	0.43	50,000	0.43
92,500	2.68	0.30	92,500	0.30
227,000	3.19	0.17	227,000	0.17
100,000	3.91	0.44	100,000	0.44
255,000	3.96	0.41	51,667	0.41
42,000	4.51	3.12		
100,000	4.60	3.18		
20,000	4.93	2.19		
20,000	4.95	2.05		
<u>229,995</u>	1.54	2.60	<u>229,995</u>	2.60
<u>2,307,510</u>	2.02	0.85	<u>1,922,177</u>	0.74

18 - CONTRIBUTED SURPLUS

Changes in the Company's contributed surplus are detailed as follows:

	2011	2010
	\$	\$
Balance, beginning of year	2,008,399	2,255,776
Options exercised (Note 17)	(230,781)	(53,718)
Options issued to underwriter as part of bought deal private placement on December 14, 2009 (Note 17)		596,111
Stock-based compensation and stock options issued to a consultant (Note 17)	401,446	209,888
Warrants exercised (Note 16)	<u>(41,614)</u>	<u>(999,658)</u>
Balance, end of year	<u>2,137,450</u>	<u>2,008,399</u>

19 - SEGMENTED INFORMATION

The Company has examined its activities and determined that it operates in the single reportable segment. This single reportable segment is 3D video systems expertise for consumer and commercial markets. The Company's revenues are derived from the following areas:

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19 - SEGMENTED INFORMATION (Continued)

	<u>2011</u>	<u>2010</u>
	\$	\$
Revenue by location		
North America	981,333	674,291
South America	3,918	
Europe	67,414	8,232
Africa	78,904	
Middle-East	1,280	
Asia	69,512	
Oceania	50,906	10,845
	<u>1,253,267</u>	<u>693,368</u>

Revenue is attributed to countries based on the location of the customer or distributor.

Property, plant and equipment, intangible assets, goodwill and distribution rights are attributed entirely in Canada.

20 - CAPITAL MANAGEMENT POLICIES AND PROCEDURES

The Company's definition of capital includes shareholders' equity and long-term debt.

The Company's capital includes the following:

	<u>2011</u>	<u>2010</u>
	\$	\$
Shareholders' equity	7,562,727	11,269,824
Long-term debt		129,600
	<u>7,562,727</u>	<u>11,399,424</u>

The Company manages its capital structure and brings about adjustments related to changes in the economic environment and the underlying risks of its assets. To preserve or modify its capital structure and to carry on developing and marketing its technology, and fulfil its various financial obligations, the Company may issue additional shares or negotiate new loans.

To maximize its technology development and marketing efforts, the Company pays no dividends. Furthermore, the Company is not subject to externally imposed capital requirements.

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Notes to Financial Statements
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21 - FINANCIAL INSTRUMENTS

The book value and fair value of the financial instruments are as follows:

	2011		2010	
	Book value	Fair value	Book value	Fair value
	\$	\$	\$	\$
Held-for-trading financial assets				
Cash	69,225	69,225	–	–
Available-for-sale financial assets				
Term deposit	6,026,507	6,026,507	10,600,895	10,600,895
Interest on the term deposit receivable	619	619	1,475	1,475
Loans and receivables				
Accounts receivable	129,505	129,505	319,489	319,489
Other receivables	5,000	5,000	–	–
Other financial liabilities				
Bank overdraft	–	–	31,247	31,247
Accounts payable and accrued liabilities	1,024,106	1,024,106	452,247	452,247
Long-term debt	–	–	129,600	129,600

Fair value

The following methods and assumptions were used to determine the estimated fair value of each class of financial instruments:

– Short-term financial instruments:

The fair value of the term deposit, accounts receivable and accounts payable and accrued liabilities approximates the carrying amount given that they will mature shortly;

– Fair value hierarchy:

Amendments to Section 3862, "Financial Instruments – Disclosures", establish a fair value hierarchy which requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company primarily applies the market approach for recurring fair value measurements. The Section describes three levels of inputs that may be used to measure fair value:

- Level 1: includes quoted prices (unadjusted) in active markets for identical assets or liabilities;

- Level 2: includes other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e. derived from prices); and

Sensio Technologies Inc.

Notes to Financial Statements

May 31, 2011 and 2010

21 - FINANCIAL INSTRUMENTS (Continued)

- Level 3: includes inputs for the asset or liability that are not based on observable market data (unobservable inputs).

As at May 31, 2011 and 2010, the short-term deposit and accrued interest are recognized at fair value. And classified as Level 2. No transfers occurred between those levels for the fiscal year ended May 31, 2011.

Financial risks

Exchange risk

The Company is exposed to exchange risk due to cash, accounts receivable and trade and other accounts receivable and accounts payable and accrued liabilities denominated in U.S. dollars. As at May 31, 2011, the assets in U.S. dollars represent cash and trade and other accounts receivable totalling US\$379,143 (US\$395,619; US\$335,548 as at May 31, 2010 (US\$321,560)); the liabilities in U.S. dollars total US\$76,966 (US\$79,445; US\$167,539 as at May 31, 2010 (US\$161,357)).

The Company does not enter into any agreements to hedge its exchange risk exposure.

Interest rate risk

The term deposit bears interest at a fixed rate and the Company is, therefore, exposed to the risk of changes in fair value resulting from interest rate fluctuations.

The Company's other financial assets and liabilities do not comprise any interest rate risk since they do not bear interest.

The Company does not use derivative financial instruments to reduce its interest rate risk exposure.

Credit risk

Generally, the carrying amount on the balance sheet of the Company's financial assets exposed to credit risk, net of any applicable provisions for losses, represents the maximum amount exposed to credit risk.

The Company's credit risk is mainly attributable to its trade accounts receivable. The Company does not require a guarantee from its customers. The Company's policy is to have each customer undergo a credit check. Moreover, trade account receivable balances are managed and analyzed on an ongoing basis and, accordingly, the Company's exposure to doubtful accounts is minimized.

Sensio Technologies Inc.
Notes to Financial Statements
 May 31, 2011 and 2010

21 - FINANCIAL INSTRUMENTS (Continued)

The ageing of trade accounts receivable is as follows:

	2011	
	\$	%
Current accounts	82,661	64
Over 30 days	9,029	7
Over 60 days	37,815	29
	<u>129,505</u>	<u>100</u>
	2010	
	\$	%
Current accounts	258,354	81
Over 30 days	12,008	4
Over 60 days	49,127	15
	<u>319,489</u>	<u>100</u>

Cash and the term deposit are held in a recognized financial institution.

Liquidity risk

Liquidity risk management serves to maintain a sufficient amount of cash and term deposits and to ensure that the Company has financing sources such as bank loans for a sufficient authorized amount.

During the past year, the Company financed its expenditure commitments and working capital requirements primarily through its long-term deposit. Management maintains a sufficient amount of cash and cash equivalents to fulfil the Company's commitments. Management establishes monthly budget and cash flows to ensure that the Company has the necessary funds to fulfil its obligations.

The financial liabilities due at term, are made up of accounts payable and expenses payable totalling \$959,526.

Market risk

The Company sells its products mainly to enterprises in the video sector. Despite the fact that this sector represents its most important client, the Company also develops products for other markets.

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22 - COMMITMENT

The Company has entered into a long-term lease agreement expiring in June 2015, which calls for lease payments of \$400,643 for the rental of premises. Minimum lease payments for the next five years are \$97,524 in 2012, \$99,232 in 2013, \$98,130 in 2014 and \$97,529 in 2015, and \$8,228 in 2016. The lease contains a renewal option for an additional five-year term, which the Company may exercise by giving notice no later than December 31, 2014.

In addition, by virtue of three contracts with suppliers, the Company has agreed to pay \$918,793 in advances for distribution rights. The payment terms of these advances is as follows:

- 25% upon signing of the contracts;
- 25% within 30 days of receipt of the master tapes of the films;
- 50% within 60 days of beginning the distribution of the films.