

LETTER TO THE Shareholders

With the hard work of our staff, whose numbers are growing in anticipation of the installs expected in the fourth quarter and the completion of deliverables for the current customers, we have made progress on all fronts in Q2, despite the continuing struggle with regulatory bodies to achieve our business goals. Supplemental Type Certificates (STCs) are now in place for contracted sales in jurisdictions that we do business and are very close to obtaining (European Airline Safety Authority) STC approval in Europe for the Airbus A319, 320, and 321. Once that is received, we expect to have several new contracts with European carriers. We have also filed our Boeing 737 and 757 packages and Bombardier DHC-8 package for approval in Europe and will continue with each new STC to gain European approval. A government airworthiness delegation from China visited our offices from July 30 to August 9th to get Chinese VSTC approvals in place for the Airbus, 757, and 767. Once these are approved, we will no doubt be adding to our growing list of approved contracts in China. The following chart shows our penetration by aircraft types:

Airlines	Contracted Units	Installed Units	Total Installs to Dec 31 from Customer Plans	Total Installs to Jun 2008 from Customer Plans
16	637	63	142	186

Aircraft Type	Contracted Units	Installed Units	2007 Planned Installs	2008 Planned Installs	Global Fleet	% Signed
Boeing 737	513	29	79	99	5783	8.87%
Boeing 757	19	2	7	17	987	1.93%
Boeing 767	7	0	1	6	886	0.79%
Airbus 330	7	0	0	0	686	1.02%
Airbus 320	30	5	13	16	4750	0.63%
CRJ	2	2	2	2	1430	0.14%
DHC -8	50	23	33	37	626	7.99%
DHC-7	3	2	3	3	52	5.77%
Fokker	6	0	4	6	220	2.73%

Once we receive the EASA STC for the Airbus 319, 320 and 321, we fully expect the number of signed aircraft for this family to approach the levels we are at with the 737's. There are a number of airlines in our sales pipeline who are not willing to commit until STC approvals are made and we expect to have the EASA STCs finalized before the end of the third quarter for the Airbus 320 family and the balance of the STCs to be in place by the end of this year.

As anyone who has followed the AMS story knows, the procurement of STCs is a long and arduous task and getting customers to commit prior to the receipt of the relevant STC is a challenge. Now that we have the relevant STCs for our currently contracted customers, we fully expect to see the installations with our customers increase. As the chart above shows, implementations planned by our customers exceed the forecasts we are using in our presentations to the market. We have 80 remaining installs forecasted this year with 130 total AFIRS units installed. Our customers' estimates indicate that we will end the year at 142 but we are trying to be conservative as all of our projections seem to have a way of creeping out on us. As has been discussed in previous presentations and reports, our recurring revenue break even will occur at roughly 170 installs and we plan to achieve that in the first half of 2008. We do anticipate being cash flow breakeven with installation revenues at the end of Q3 2007.

LETTER TO THE Shareholders

During July of this year, we made an offer to a new VP Sales and Marketing and are pleased to announce that Pat Sandall has accepted a position as our VP Sales and Marketing. Pat brings more than 22 years of senior sales and marketing experience to the management team which will further allow us to handle anticipated growth. We look for great things in rolling our solution out to the marketplace this fall under Pat's seasoned guidance. Gino Ferronato, our COO continues to implement processes and programs in the business to help streamline our implementation and reduce the time from installation to revenue. Gino will also be taking on the day-to-day responsibility of expanding our service offering through end user driven tools to enhance our customers' capabilities.

We are very happy with the progress we have made so far this year. The private placement which was closed this quarter puts us in very solid financial condition to meet corporate objectives for the foreseeable future. We want to thank our investors for their patience, the staff for their loyalty and hard work, and our customers for their continued support and enthusiasm for our services.

Yours truly,



Bill Tempany
CEO



Darryl Jacobs
Founder and President

Management Discussion and Analysis

This MD&A contains forward-looking statements. Forward-looking statements are based on current expectations that involve a number of risks and uncertainties that could cause actual events or results to differ materially from those reflected in the MD&A. Forward-looking statements are based on the estimates and opinions of AMS' management at the time the statements were made. AMS assumes no obligation to update forward looking statements, should circumstances or management's estimates change.

This MD&A is dated August 13, 2007.

Overview

AeroMechanical Services Ltd. is a designer, developer, and service provider of innovative solutions to the global aerospace business. The Company's solutions are designed to improve the productivity and profitability of our customers.

The major products of the Company are Automated Flight Information Reporting System (AFIRS), UpTime, and Underfloor Stowage Unit. These products are marketed globally by a team of individuals: five based in Calgary, one in Ontario, one in Florida, and one in Switzerland. One of the Calgary staff is currently spending 85% of his time in China dealing with opportunities there. AMS has sales coverage in many countries around the world.

Financing Activities

On June 1st, 2007 two non-brokered private placements were completed with shares being sold to a group of high net worth individuals and qualified buyers led by Northern Rivers Capital Management's Northern Rivers Innovation Fund. The placements were as follows: 4,912,500 common shares of the Company at a price of \$0.40 per share for gross proceeds of \$1,965,000 and 1,606,967 common shares of the Company at a price of \$0.60 per share for gross proceeds of \$964,180. The cost of the issue was \$121,963.

The private placements were approved by the TSX Venture Exchange on August 1st, 2007.

During the second quarter employees, directors, and consultants exercised stock options totaling 52,000 common shares at a weighted average exercise price of \$0.35 for gross proceeds of \$29,063.

Warrants were exercised during the second quarter totaling 504,600 common shares at a weighted average exercise price of \$0.45 for gross proceeds of \$226,840.

Results of Operations – Six Months Ended June 30, 2007

During the six months ending June 30, 2007 the Company:

Revenue

As shown in the following tables the AFIRS and UpTime Rental Revenue and Unearned Revenue are showing the results forecasted. AMS' long term investment in marketing and relationship building has given the Company a strong pipeline of prospective clients around the world. The ongoing revenue streams from our existing client base will continue to expand throughout this and future years.

AMS has adopted a conservative revenue recognition policy, where by, network access fees are capitalized as unearned revenue and revenue is recognized over the term of the initial contracts. This has the effect of normalizing the revenue through the life of the contract, which in the early stages will show less booked revenue than cash received.

The effect in the quarter is that we received \$591,534 in cash revenues with \$473,122 reported as revenue and \$118,412 being included in unearned revenue.

Recognized revenue increased \$174,270 in the second quarter compared to the second quarter of last year. AFIRS and UpTime revenues increased by \$50,974 over the second quarter of 2006. Sales revenue is up by \$123,296 as the result of the further finalization of the licensing agreement with Vibro-Meter SA, a division of Meggitt Aerospace. AMS now has the AFIRS box with the most recent upgraded technology products that is tested, certified, and ready to install on aircraft. Revenues are expected to grow at a significantly higher rate than our costs because the Company has the infrastructure, sales people, and support organization in place to support revenue growth.

Recognition of the AFIRS and UpTime product superiority and innovation has allowed us to be key note speakers at several leading industry events. This shows that AMS' products are being recognized as leading edge in this industry.

Management Discussion and Analysis

Cost of Sales and Gross Margins

Percentage Cost of Sales in the second quarter of 2007 is 78% of Sales compared to 63% in 2006. This increase is due to increased installations and the resulting increase in the cost of sales of non-routable parts and travel expenses of our engineers on initial installations of aircraft. As part of our service we assist new clients with engineering support on their initial installations. This cost is covered in our access fee. Non-routable parts are parts involved in the installation process that are non-reusable (such as cables) and do not form part of the rental asset. They would remain on the aircraft if the AFIRS unit was extracted. The travel and support costs form part of the non-routable parts and are expensed in the period. The effect is an increase in cost of sales. As we move forward with more clients and the corresponding recurring revenue streams, we will see the cost of sales decline and our margins increase.

Second quarter 2007 Gross Margin was 22% compared to first quarter of 2007 of 77% and second quarter 2006 of 37%.

Net Loss, General Administrative and Marketing Expenses

The net loss in the quarter ending June 30, 2007 was \$1,978,629 (2006—\$965,349) which is an increased loss of \$1,013,280 over the same period in 2006. This increase is primarily due to stock based compensation increase of \$481,351, increased salaries and benefits of \$445,519 and increased marketing expenses of \$152,681.

Included in General Administrative Expenses are increased marketing costs. Marketing expenses increased by \$152,681 to \$252,625 over the second quarter in 2006. These figures do not include salaries, and are indicative of the increased activity in the marketing and sales area of our company. We expect that expenses in marketing will remain the same or increase into the future as the Company's focus is on generating new customers. Our plans are to continue to attend shows globally that focus on market places where we want our products to penetrate. The costs of the shows are relatively high because of the specific nature of these shows and the far away localities in which they always seem to be held. Our product is a very niche product; therefore attendance at these shows is mandatory as traditional advertising does not yield significant results.

Stock based compensation in the second quarter of 2007 was \$481,351 versus no expense in the corresponding period of 2006. This was the result of a timing difference in the granting of options in 2007 to the second quarter versus the first quarter in 2006. Stocked based compensation continues to be an effective non-cash method to attract the senior experienced employees that AMS requires to drive the Company forward. In addition, the economy in the Calgary area continues to be strong and in order to maintain our current staff, options for tenured individuals were granted to reward them for continued loyalties to AMS and its customers.

AMS' Rent Expense decreased by \$21,025 in second quarter 2007 over 2006, primarily due to an operating expense credit received from the landlord during the quarter. Interest and bank charges were \$4,603 during the second quarter of 2007 versus \$27,342 during the same period of 2006. The decrease was due to the improved cash position of the company over the same quarter in 2006 and the resulting decrease in interest paid on outstanding payables balances.

Salaries continue to be the main cost of doing business for AMS. We are hiring good qualified personnel on an ongoing basis as our customer base grows and in preparation for further growth of the company as a result of our strategic business alliances that are opening many opportunities for a rapid growth in sales. As a result, salaries and benefits increased from \$526,625 in the second quarter of 2006 to \$972,144 in the second quarter of 2007.

All other expenses are tracking as planned.

Research and Development

Research and development costs are being expensed as incurred. The second quarter development costs for 2007 were \$28,646 as compared to \$117,579 in 2006 a decrease of \$88,933 which is a result of decreased direct research and development activity in the quarter versus the previous year and increased emphasis on product delivery. However, the Company continues its ongoing design, testing, and certification of AFIRS, as well as the design and testing of UpTime, to add aircraft types to its approved installation list. We do not anticipate this trend to continue. There are also minor expenses being incurred in the preliminary phases of AeroQ.

Foreign Exchange

All international sales of the Company's products and services are denominated in U.S. dollars. Accordingly, the Company is susceptible to foreign exchange fluctuations. In the second quarter of 2007, nearly 83% of the Company's gross sales were made outside of Canada. The strength of the Canadian dollar and the fact that a majority of the Company's accounts receivable are denominated in United States dollars resulted in foreign exchange losses increasing from \$8,446 in the second quarter of 2006 to \$34,543 for the same period in 2007.

Liquidity and Capital Resources

At June 30, 2007 the Company had working capital of \$3,806,586 compared to a working capital deficit of \$247,144 in the same period in 2006. The increase in the working capital is attributed primarily to: increased cash of \$3,336,836 from to the share offerings in Q3 2006 and Q2 2007, increased sales which led to increased receivables of \$133,909, an increase in inventory of \$112,566, an increase in prepaid expenses of \$41,321, a decrease in accounts payable of \$574,924, and an increase in unearned revenue of \$39,268.



Management Discussion and Analysis

The Company's ability to continue is dependent upon attaining sustainable profitable operations and obtaining additional financing in order to fund its working capital requirements and on-going operations. The Company's ability to attain profitable operations and positive cash flow in the future is dependent upon its ability to acquire new customer contracts, the success of management's continued cost controls, and general economic conditions.

The Company currently has no bank debt and has an operating line of \$250,000 which bears an interest rate of Canadian chartered bank prime plus 1.0%, and is secured by assignment of cash collateral and a general security agreement.

Summary of Quarterly Results

	Q2-05	Q3-05	Q4-05	Q1-06	Q2-06	Q3-06	Q4-06	Q1-07	Q2-07
Revenue	\$115,582	\$107,271	\$132,669	\$218,328	\$298,852	\$258,813	\$318,473	\$837,218	\$473,122
Loss	687,659	600,000	1,127,856	1,166,402	965,349	1,175,113	1,231,842	809,265	1,978,629
Loss/Share	\$ 0.04	\$ 0.03	\$ 0.05	\$ 0.04	\$ 0.03	\$ 0.03	\$ 0.02	\$ 0.01	\$ 0.03

Contractual Obligations

The Company has entered into various leases for its operating premises and equipment. Future minimum annual payments under these operating leases are as follows:

	Premises	Equipment	Total
2007	\$ 95,517	\$ 9,567	\$ 105,084
2008	\$ 191,033	\$ 17,043	\$ 208,076
2009	\$ 44,801	\$ 7,081	\$ 51,882
	\$ 331,351	\$ 33,691	\$ 365,042

In addition, the Company has repayment obligations related to two Government of Canada loan programs. Under the Industrial Research Assistance Program (IRAP), the Company has received \$336,722, which is to be repaid as a percentage of gross revenues, over a five to ten year period commencing in October 2006. Under the Technology Partnerships Canada (TPC) program, the Company has received \$104,523 to be repaid over a ten year period commencing in April 2006.

Looking Forward

The Company has been developing a sales networking system around the world to leverage its marketing and delivery capabilities. In January Meggitt Aerospace, a world leader and supplier of aerospace sensor and monitoring equipment, finalized a licensing agreement with AMS to jointly market our product and services. Meggitt has equipment installed on nearly every jet aircraft in the world with its engine sensor, monitoring systems, and other products. Since the initial signing of an agreement in June 2006, Meggitt has opened doors into the OEM market. AMS is currently completing an RFP (Request for Proposal) for a major manufacturer to be included on their new jets. This is a significant move forward in the marketing timelines.

Various strategic relationships leverage our marketing capability worldwide, as these leading organizations have completed their due diligence on AMS' product and service capabilities. The inclusion of AMS in a strategic relationship with Meggitt provides AMS a higher standard of credibility with all customers around the world. We are seeing the results through increased activity in airlines contacting our sales group and invitations for AMS to visit and speak with the major OEMs around the world.

In conjunction with our sales efforts during the second quarter, the company has increased its focus and resources on customer installations and deliverables. This will enable AMS to fully maximize the revenue per installed AFIRS and reduce the time from initial installation on an aircraft to maximum billing. In addition, these efforts will enhance the ability to grow the revenue base of existing installations through additional service offerings. As part of our efforts in both sales and installation we have bolstered the sales group by recruiting a VP Sales and Marketing with extensive experience in solution sales.

Management Discussion and Analysis

Changes in Accounting Policy

Effective January 1, 2007, the Company adopted the new recommendation of the Canadian Institute of Chartered Accountants (CICA) under CICA Handbook Section 1530 Comprehensive Income, Section 3251 Equity, Section 3855 Financial Instruments – Recognition and Measurement, and Section 3861 Financial Instruments – Disclosure and Presentation. These new Handbook sections, which apply to fiscal years beginning on or after January 1, 2007, provide requirements for the recognition and measurement of financial instruments. Section 1530 establishes standards for reporting and presenting comprehensive income, which is defined as the change in equity from transaction and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income but are excluded from net income calculated in accordance with Canadian Generally Accepted Accounting Principles (GAAP).

Under Section 3855, all financial instruments are classified into one of five categories: held-for trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets, or other financial liabilities. All financial instruments are measured in balance sheet either at fair value except for loans and receivables, held-to-maturity investments, and other financial liabilities, which are measured at amortized cost. Subsequent measurement and changes in fair value will depend on their initial classification, as follows: held-for-trading financial assets are measured at fair value, and changes in fair value are recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the instrument is derecognized or impaired.

The adoption of these new standards had no impact on the Company's accounts and deficit position as at January 1, 2007. As a result of the adoption of these new standards, the Company has classified its cash and cash equivalents as held-for-trading. Accounts receivable are classified as loans and receivables. Accounts payable and certain accrued liabilities and notes payable are classified as other liabilities, all of which are measured at amortized cost.

Internal Control over Financial Reporting and Disclosure Control

The Company's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP.

Please see page 28 of the Company's Annual Report for the fiscal year ended December 31, 2006 for a discussion of internal controls over financial reporting and disclosure controls. We reported that management had identified three areas of disclosable weakness in internal controls related to financial reporting system, segregation of duties, controls over information systems, and steps that would be taken to remediate each of these weaknesses during the current year.

During the quarter ended March 31, 2007, the Company did not make any changes to its internal control over financial reporting that would have materially affected, or would likely materially affect, such controls. We will take steps to address the weaknesses identified during the remainder of fiscal 2007 where feasible and cost effective.

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CONSOLIDATED BALANCE SHEET
(UNAUDITED)

	June 30 2007	December 31 2006
	(Unaudited)	(Audited)
ASSETS		
CURRENT		
Cash and cash equivalents	\$ 3,129,965	\$ 2,688,389
Restricted cash	284,500	284,500
Accounts receivable	460,155	291,603
Prepaid expenses	95,583	233,040
Inventory	505,011	428,886
	<u>4,475,214</u>	<u>3,926,418</u>
CAPITAL ASSETS – Note 2	231,025	224,644
RENTAL ASSETS – Note 3	978,347	768,696
INTANGIBLE ASSET – Note 4	34,992	34,992
	<u>\$ 5,719,578</u>	<u>\$ 4,954,750</u>
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	\$ 403,752	\$ 497,531
Current Portion unearned revenue - Note 5	145,568	101,774
Current portion of deferred lease inducement – Note 6	13,687	13,687
Current portion of loans payable – Note 7	86,561	120,742
Current portion of obligation under capital lease – Note 9	19,060	16,105
	<u>668,628</u>	<u>749,839</u>
UNEARNED REVENUE – Note 5	379,170	292,920
DEFERRED LEASE INDUCEMENT – Note 6	9,125	15,968
LOANS PAYABLE- Note 7	354,684	351,959
OBLIGATION UNDER CAPITAL LEASE – Note 9	19,865	27,028
WARRANTY	10,919	12,016
	<u>1,442,391</u>	<u>1,449,730</u>
SHAREHOLDERS' EQUITY		
SHARE CAPITAL – Note 10	20,124,402	17,052,282
CONTRIBUTED SURPLUS – Note 10	1,867,264	1,379,323
DEFICIT	(17,714,479)	(14,926,585)
	<u>4,277,187</u>	<u>3,505,020</u>
	<u>\$ 5,719,578</u>	<u>\$ 4,954,750</u>

Financial Statements

CONSOLIDATED STATEMENTS OF LOSS AND DEFICIT
(UNAUDITED)

	For the six months ended June 30, 2007	For the six months ended June 30, 2006	For the three months ended June 30, 2007	For the three months ended June 30, 2006
REVENUE				
Rental revenue	\$ 363,056	\$ 234,205	\$ 191,278	\$ 140,304
Sales revenue	947,985	282,975	281,844	158,548
	1,311,041	517,180	473,122	298,852
COST OF SALES	557,029	368,636	368,452	188,837
GROSS MARGIN	754,012	148,544	104,670	110,015
EXPENSES				
Salaries and benefits	1,885,248	945,230	972,144	526,625
Marketing	444,101	235,216	252,192	99,511
Stock based compensation	498,835	405,602	481,351	-
Research and development	78,454	108,734	28,646	117,579
Office	166,224	176,192	92,578	87,553
Professional fees	100,235	70,193	61,483	70,103
Rent	84,493	93,840	29,073	50,098
Computer services	71,004	55,400	35,657	31,721
Consulting fees	75,985	95,044	42,089	35,211
Insurance	35,225	26,384	16,300	13,177
Depreciation	38,673	15,996	25,761	7,998
Interest and bank charges	10,563	34,252	4,603	27,342
Foreign exchange currency loss	35,898	9,183	34,543	8,446
Stock exchange fees	16,968	9,069	6,879	-
	3,541,906	2,280,295	2,083,299	1,075,364
NET LOSS FOR THE PERIOD	\$ (2,787,894)	\$ (2,131,751)	\$ (1,978,629)	\$ (965,349)
DEFICIT – Beginning of the year	\$ (14,926,585)	\$ (10,386,879)	\$ (15,735,850)	\$ 7,070,757
NET LOSS	(2,787,894)	(2,131,751)	(1,978,629)	(965,349)
DEFICIT- END OF THE PERIOD	\$ (17,714,479)	\$ (12,518,630)	\$ (17,714,479)	\$ (8,036,106)
NET LOSS PER SHARE – Basic and Diluted – Note 10	\$ (0.05)	\$ (0.06)	\$ (0.03)	\$ (0.03)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES	59,638,461	32,262,161	59,638,461	32,262,161

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CONSOLIDATED STATEMENT OF CASH FLOWS
(UNAUDITED)

	For the six months ended June 30, 2007	For the six months ended June 30, 2006	For the three months ended June 30, 2007	For the three months ended June 30, 2006
OPERATING ACTIVITIES				
Net loss	\$ (2,787,894)	\$ (2,131,751)	\$ (1,978,629)	\$ (965,349)
Add items not affecting cash				
Depreciation	38,673	23,496	25,761	19,098
Amortization	40,045		21,984	
Stock based compensation	498,835	406,602	481,352	
Warranty expense	(1,098)	4,500	(2,994)	2,700
Non-cash expenses	12,623	1,590,456	9,000	(24,006)
	(2,198,816)	(107,697)	(1,443,526)	(967,617)
Net change in non-cash working capital balances	(77,797)	(566,012)	(73,568)	597,687
	(2,276,613)	(673,709)	(1,517,094)	(369,930)
FINANCING ACTIVITIES				
Issuance of common shares	3,174,189	2,370,769	3,174,189	149,340
Repayment of capital lease	(7,831)	-	(4,091)	-
Repayment of convertible debenture		(400,000)		-
Short term loan repayment		(990,000)		-
Share issue costs	(121,962)	(253,752)	(121,962)	-
IRAP and TCP loan repayment	(31,456)	(10,216)	(28,413)	(5,250)
	3,012,940	716,801	3,019,723	144,090
INVESTING ACTIVITIES				
Capital assets	(45,054)	(49,472)	(7,755)	-
Rental assets	(249,697)	-	(27,744)	(47,240)
	(294,751)	(49,472)	(35,499)	(47,240)
CHANGE IN CASH AND CASH EQUIVALENTS	441,576	(6,380)	1,467,130	(273,080)
CASH AND CASH EQUIVALENTS - Beginning of the period	2,688,389	84,009	1,662,835	350,709
CASH AND CASH EQUIVALENTS - End of the period	\$ 3,129,965	\$ 77,629	\$ 3,129,965	\$ 77,629

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED JUNE 30, 2007 (UNAUDITED)

NOTE 1 SIGNIFICANT ACCOUNTING POLICIES

These unaudited interim Consolidated Financial Statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP) on a basis consistent with those followed in the most recent audited annual financial statements for the year ended December 31, 2006 except as noted below. These unaudited interim Consolidated Financial Statements do not include all note disclosures required by GAAP for annual consolidated financial statements. Accordingly, these statements should be read in conjunction with the Company's annual audited financial statements for the year ended December 31, 2006.

Effective January 1, 2007, the Company adopted the new recommendation of the Canadian Institute of Chartered Accountants (CICA) under CICA Handbook Section 1530 Comprehensive Income, Section 3251 Equity, Section 3855 Financial Instruments – Recognition and Measurement, and Section 3861 Financial Instruments – Disclosure and Presentation. These new Handbook sections, which apply to fiscal years beginning on or after January 1, 2007, provide requirements for the recognition and measurement of financial instruments. Section 1530 establishes standards for reporting and presenting comprehensive income, which is defined as the change in equity from transaction and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income but are excluded from net income calculated in accordance with Canadian Generally Accepted Accounting Principles.

Under Section 3855, all financial instruments are classified into one of five categories: held-for trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets, or other financial liabilities. All financial instruments are measured in balance sheet either at fair value except for loans and receivables, held-to-maturity investments, and other financial liabilities, which are measured at amortized cost. Subsequent measurement and changes in fair value will depend on their initial classification, as follows: held-for-trading financial assets are measured at fair value and changes in fair value are recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the instrument is derecognized or impaired.

The adoption of these new standards had no impact on the Company's accounts and deficit position as at January 1, 2007. As a result of the adoption of those new standards, the Company has classified its cash and cash equivalents as held-for-trading. Accounts receivable are classified as loans and receivables. Accounts payable and certain accrued liabilities and notes payable are classified as other liabilities, all of which are measured at amortized cost.

Carry value and fair value of financial assets and liabilities are summarized as follows:

	<u>Carrying Value</u>	<u>Fair Value</u>
Held for trading	\$ 414,465	\$ 3,414,465
Loans and receivables	460,155	460,155
Held-to-maturity	-	-
Available-for-sale	-	-
Other liabilities	883,922	883,922

NOTE 2 CAPITAL ASSETS

	Cost	Accumulated Amortization	June 30 2007	Dec 31 2006
Computers	\$ 286,381	\$ 170,387	\$ 115,994	\$ 102,936
Equipment	128,459	48,221	80,238	73,363
Leasehold Improvements	77,689	42,896	34,793	48,345
	<u>\$ 492,529</u>	<u>\$ 261,504</u>	<u>\$ 231,025</u>	<u>\$ 224,644</u>

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NOTE 3 RENTAL ASSETS

	Cost	Accumulated Amortization	June 30 2007	Dec 31 2006
Asset available for Lease	\$ 557,036	\$ -	\$ 557,036	\$ 457,633
Leased assets	545,953	124,642	421,311	311,063
	<u>\$ 1,102,989</u>	<u>\$ 124,642</u>	<u>\$ 978,347</u>	<u>\$ 768,696</u>

NOTE 4 INTANGIBLE ASSETS

	June 30 2007	Dec 31 2006
Licensing Agreement – indefinite life	<u>\$ 34,992</u>	<u>\$ 34,992</u>

NOTE 5 UNEARNED REVENUE

Balance December 31, 2006	385,574
Installation access fees	83,731
Earned revenues	<u>(28,294)</u>
Balance March 31, 2007	441,011
Installation access fees	123,100
Earned revenues	<u>(39,373)</u>
Balance June 30, 2007	524,738
Less current portion	<u>145,568</u>
	<u>\$ 379,170</u>

NOTE 6 DEFERRED LEASEHOLD INDUCEMENTS

Balance December 31, 2006	\$ 29,655
Amortization	<u>(3,421)</u>
Balance March 31, 2007	26,234
Amortization	<u>(3,422)</u>
Balance June 30, 2007	22,812
Less current portion	<u>(13,687)</u>
	<u>\$ 9,125</u>

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NOTE 7 LOANS PAYABLE

	June 30 2007	Dec 31 2006
The industrial Research Assistance Program "IRAP" loan is non-interest bearing and is repaid annually, based on 1.11% of gross revenues, commencing October 2006. The current portion is calculated based on the actual gross revenues in the previous quarter plus the Company's revenue projections for the next nine months.	\$ 336,722	\$ 49,066
The Technology Partnerships Canada "TCP" loan is non-interest bearing. The loan is repayable annually, based on 15% of the initial contribution when the Company has achieved more than 10% growth in gross revenues above the previous year's gross revenue and the gross revenue for the year is greater than the base amount. The base amount is defined as the Company's gross revenue in fiscal 2004, which was at \$556,127.	104,523	123,635
	441,245	472,701
	(86,561)	(120,742)
<u>Less: Current portion</u>	<u>\$ 354,684</u>	<u>\$ 351,959</u>

NOTE 8 BANK LOAN

Operating demand loan is available to the Company up to a maximum of \$250,000. The operating demand loan is payable on demand, bears at Canadian chartered bank prime plus 1.0% and is secured by an assignment of cash collateral in the amount of \$284,500 and a general security agreement including a first security interest in all personal property. The amount of the cash collateral has been disclosed as restricted cash. As at June 30, 2007 the facility has not been drawn.

NOTE 9 OBLIGATION UNDER CAPITAL LEASE

The Company is party to various capital leases for computer hardware and software that expire in 2009. Future minimum lease payments under the capital leases are as follows:

2007	\$ 12,356
2008	23,310
2009	10,186
2010	451
	<u>46,303</u>
Less: imputed interest	(7,378)
Less: current portion	<u>(19,060)</u>
	<u>\$ 19,865</u>

Financial **Statements****NOTE 10 SHARE CAPITAL**

Authorized:
 Unlimited number of:
 Common shares
 Class A, B and C preferred shares, issuable in series

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges, restrictions, and conditions attached to the shares of each series.

ISSUED:**a) Common shares**

	<u>Number of Shares</u>	<u>Value</u>
Balance December 31, 2006	58,488,823	17,052,282
Issued for cash	6,519,467	2,929,180
Exercise of employee options	52,000	29,063
Exercise of warrants	504,600	226,840
Share subscription receivable		(121,963)
Share issue costs		9,000
Balance June 30, 2007	<u>\$ 65,564,890</u>	<u>\$ 20,124,402</u>

b) Stock Option Plan

	<u>Number of Shares</u>	<u>Weighted Average Exercise Price</u>
Outstanding December 31, 2006	2,426,995	\$ 0.420
Options granted	939,000	0.662
Options exercised	(52,000)	0.349
Outstanding June 30, 2007	<u>3,313,995</u>	<u>\$ 0.426</u>

c) Contributed Surplus

Balance December 31, 2007	\$ 1,379,322
Share based compensation	498,835
Employee share options exercised	(10,893)
Balance June 30, 2007	<u>\$ 1,867,264</u>

d) Warrants

	<u>Number of Warrants</u>	<u>Weighted Average Exercised Price</u>
Balance December 31, 2006	17,136,016	\$ 0.51
Warrants granted		
Warrants expired	(593,750)	(0.50)
Warrants exercised	(504,600)	(0.45)
Outstanding June 30, 2007	<u>16,037,666</u>	<u>\$ 0.51</u>

The calculation of basic loss per share is based on the weighted-average number of common shares outstanding during the six months ending June 30, 2007 of 59,638,461 (2006 – 32,262,161).