Consolidated Financial Statements of

# Sangoma Technologies Corporation

June 30, 2012

# Sangoma Technologies Corporation

June 30, 2012

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# Independent Auditor's Report

To the Shareholders of Sangoma Technologies Corporation

We have audited the accompanying consolidated financial statements of Sangoma Technologies Corporation, which comprise the consolidated statements of financial position as at June 30, 2012, June 30, 2011 and July 1, 2010 and the consolidated statements of comprehensive income (loss), consolidated statements of changes in equity and consolidated statements of cash flows for the years ended June 30, 2012 and June 30, 2011, and a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Sangoma Technologies Corporation as at June 30, 2012, June 30, 2011 and July 1, 2010, and its financial performance and its cash flows for the years ended June 30, 2012 and June 30, 2011 in accordance with International Financial Reporting Standards.

Deloitte & Touche LLP

Chartered Accountants
Licensed Public Accountants
October 10, 2012
Toronto, Canada

# Sangoma Technologies Corporation

## Consolidated Statements of Financial Position
## as at June 30, 2012, June 30, 2011 and July 1, 2010

(In Canadian dollars)

| | **June 30, 2012** | June 30, 2011 (Note 18) | July 1, 2010 (Note 18) |
|---|---|---|---|
| | **$** | $ | $ |
| **Assets** | | | |
| Current assets | | | |
| Cash and cash equivalents (Note 9) | **5,016,825** | 8,784,322 | 7,744,596 |
| Trade receivables (Note 10) | **4,495,018** | 2,232,704 | 1,972,758 |
| Inventories (Note 5) | **3,040,837** | 1,461,212 | 1,648,852 |
| Investment tax credits receivable | **469,108** | 577,444 | 192,877 |
| Income taxes receivable | **-** | 836,210 | 595,882 |
| Sales tax receivables | **217,424** | 50,465 | 21,414 |
| Investment in Vegastream Private Networks Limited (Note 17) | **10,665** | - | - |
| Other current assets | **375,533** | 28,061 | 118,318 |
| | **13,625,410** | 13,970,418 | 12,294,697 |
| Non-current assets | | | |
| Property, plant and equipment (Note 6) | **378,560** | 354,467 | 309,331 |
| Development costs (Note 8) | **2,247,213** | 1,983,665 | 2,158,221 |
| Intangible assets (Note 7) | **2,636,123** | 2,173,962 | 3,926,047 |
| Goodwill (Note 4(i)) | **3,543,912** | 2,984,721 | 6,834,721 |
| | **22,431,218** | 21,467,233 | 25,523,017 |
| **Liabilities** | | | |
| Current liabilities | | | |
| Accounts payable and accrued liabilities | **2,101,598** | 1,516,054 | 1,263,759 |
| Income tax payable | **2,220** | - | - |
| Current portion of term loan (Note 10) | **34,072** | 34,072 | 34,072 |
| Short-term obligation to issue shares | **-** | - | 959,847 |
| Deferred revenue | **102,962** | 60,864 | 76,688 |
| | **2,240,852** | 1,610,990 | 2,334,366 |
| Non-current liabilities | | | |
| Term loan (Note 10) | **17,035** | 51,107 | 85,179 |
| Deferred income tax liabilities (Note 12) | **265,534** | 531,066 | 1,071,637 |
| | **2,523,421** | 2,193,163 | 3,491,182 |
| **Shareholders' equity** | | | |
| Share capital (Note 11) | **15,712,274** | 15,866,455 | 15,158,762 |
| Contributed Surplus (Note 11) | **1,277,393** | 904,468 | 611,030 |
| Retained earnings (Note 18) | **2,918,130** | 2,503,147 | 6,262,043 |
| | **19,907,797** | 19,274,070 | 22,031,835 |
| | **22,431,218** | 21,467,233 | 25,523,017 |

Approved by the Board

(signed) Jonathan Matthews Director

(signed) Yves Laliberte Director

# Sangoma Technologies Corporation

## Consolidated Statements of Comprehensive Income (Loss)

## years ended June 30, 2012 and 2011

(In Canadian dollars)

| | 2012 | 2011 (Note 18) |
|---|---|---|
| | **$** | $ |
| Revenue (Note 14) | **13,762,871** | 11,861,514 |
| Cost of sales | **4,294,815** | 3,022,458 |
| Gross profit | **9,468,056** | 8,839,056 |
| Expenses | | |
| Sales and marketing | **2,642,352** | 1,835,294 |
| Research and development | **2,797,505** | 2,095,042 |
| General and administration | **3,386,584** | 2,988,817 |
| Foreign currency exchange (gain) loss | **(412,913)** | 693,042 |
| | **8,413,528** | 7,612,195 |
| Income before the undernoted | **1,054,528** | 1,226,861 |
| Investment income | | |
| Interest income (Note 9) | **(18,047)** | (26,374) |
| Interest expense | **-** | - |
| Net interest income | **(18,047)** | (26,374) |
| Accelerated amortization of patents (Note 7) | **-** | 1,349,489 |
| Impairment of goodwill (Note 4(i)) | **-** | 3,850,000 |
| Business acquisition costs (Note 17) | **251,490** | - |
| Income (loss) before income taxes | **821,085** | (3,946,254) |
| Provision for (recovery of) income taxes | | |
| Current (Note 12) | **284,224** | 277,913 |
| Deferred (Note 12) | **121,878** | (465,271) |
| **Net income (loss) and total comprehensive income (loss)** | **414,983** | (3,758,896) |
| **Earnings (loss) per share** | | |
| Basic (Note 11 (iii)) | **$ 0.014** | $ (0.125) |
| Diluted (Note 11 (iii)) | **$ 0.014** | $ (0.124) |
| **Weighted average number of shares outstanding (Note 11 (iii))** | | |
| Basic | **29,618,366** | 30,088,138 |
| Diluted | **29,751,876** | 30,261,338 |

# Sangoma Technologies Corporation

Consolidated Statements of Changes in Equity
years ended June 30, 2012 and 2011
(In Canadian dollars)

| | Number of shares | Share capital | Contribued surplus | Retained earnings | Total equity |
|---|---|---|---|---|---|
| | | $ | $ | $ | $ |
| **Balance, July 1, 2010 (Notes 11(i) and 18)** | 29,564,723 | 15,158,762 | 611,030 | 6,262,043 | 22,031,835 |
| Net loss and total comprehensive loss | - | - | - | (3,758,896) | (3,758,896) |
| Issuance of common shares | 778,086 | 959,847 | - | - | 959,847 |
| Share-based payment (Note 11(ii)) | - | - | 293,438 | - | 293,438 |
| Normal course issuer bid redemption (Note 11(i)) | (505,000) | (252,154) | - | - | (252,154) |
| Balance, June 30, 2011 (Note 11(ii) and 18) | 29,837,809 | 15,866,455 | 904,468 | 2,503,147 | 19,274,070 |
| Net income and total comprehensive income | - | - | - | 414,983 | 414,983 |
| Issuance of common shares | - | - | - | - | - |
| Share-based payment (Note 11(ii)) | - | - | 372,925 | - | 372,925 |
| Normal course issuer bid redemption (Note 11(i)) | (299,000) | (154,181) | - | - | (154,181) |
| **Balance, June 30, 2012** | **29,538,809** | **15,712,274** | **1,277,393** | **2,918,130** | **19,907,797** |

# Sangoma Technologies Corporation

## Consolidated Statements of Cash Flows
## years ended June 30, 2012 and 2011

(In Canadian dollars)

| | **2012** | 2011 |
|---|---|---|
| | **$** | $ |
| **Operating activities** | | |
| Net income (loss) | **414,983** | (3,758,896) |
| Adjustments for | | |
| Impairment loss on goodwill | **-** | 3,850,000 |
| Depreciation of property, plant and equipment (Note 6) | **78,455** | 77,404 |
| Amortization of intangible assets (Note 7) | **442,839** | 1,811,710 |
| Amortization of capitalized development costs (Note 8) | **1,590,171** | 1,341,650 |
| Income tax expense (recovery) | **406,102** | (187,358) |
| Share-based payment (Note 11(ii)) | **372,924** | 293,438 |
| Changes in item of working capital | | |
| Trade receivables | **(2,262,314)** | (259,946) |
| Inventories (Note 5) | **(1,554,490)** | 187,640 |
| Other current assets | **(347,472)** | 90,257 |
| Sales tax receivables | **(166,959)** | (29,051) |
| Accounts payable and accrued liabilities | **585,544** | 252,295 |
| Deferred revenue | **42,098** | (15,824) |
| Income tax received | **780,324** | 773,709 |
| Income tax paid | **-** | (628,563) |
| Investment tax credits received | **342,427** | - |
| | **724,632** | 3,798,465 |
| **Investing activities** | | |
| Purchase of property, plant and equipment (Note 6) | **(86,786)** | (122,540) |
| Purchase of intangible assets (Note 7) | **-** | (59,625) |
| Development costs (Note 8) | **(2,701,336)** | (2,290,348) |
| Business combination (Note 17) | **(1,515,754)** | - |
| | **(4,303,876)** | (2,472,513) |
| **Financing activities** | | |
| Repayment of term loan | **(34,072)** | (34,072) |
| Normal course issuer bid redemption | **(154,181)** | (252,154) |
| | **(188,253)** | (286,226) |
| (Decrease) increase in cash and cash equivalents | **(3,767,497)** | 1,039,726 |
| Cash and cash equivalents, beginning of year | **8,784,322** | 7,744,596 |
| **Cash and cash equivalents, end of year** | **5,016,825** | 8,784,322 |

## 1. General information

Founded in 1984, Sangoma Technologies Corporation ("Sangoma" or the "Company") is publicly traded on the TSX Venture Exchange (TSX VENTURE: STC). The Company was incorporated in Canada, its legal name is Sangoma Technologies Corp. and its operating subsidiary is Sangoma Technologies Inc.

Sangoma is a leading provider of hardware and software components that enable or enhance Internet Protocol Communications Systems for both telecom and datacom applications. Enterprises, small to medium sized businesses ("SMBs") and telecom operators in over 150 countries rely on Sangoma's technology as part of their mission critical infrastructures. The product line includes data and telecom boards for media and signal processing, as well as gateway appliances and software.

The Company is domiciled in Ontario, Canada. The address of the Company's registered office and its principal place of business is 100 Renfrew Dr., Suite 100, Markham, Ontario, L3R 9R6.

## 2. Statement of compliance

The Company  adopted International Financial Reporting Standards ("IFRS") effective July 1, 2011. Prior to the adoption of IFRS, the Company prepared its interim and annual financial statements in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). These consolidated financial statements have been prepared in accordance with IFRS.

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and in preparing the opening IFRS balance sheet at July 1, 2010 for the purpose of the transition to IFRS, as required by IFRS 1 – First-Time Adoption of International Financial Reporting Standards ("IFRS 1"). An explanation of how the transition to IFRS affected the reported financial position, financial performance and cash flows of the Company is provided in Note 18. This note includes reconciliations of equity and total comprehensive loss for comparative periods and of equity at the date of transition reported under Canadian GAAP to those reported for those periods and at the date of transition under IFRS.

## 3. Significant accounting policies

*(i) Basis of measurement*

The consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of certain financial assets and financial liabilities to fair value.

*(ii) Basis of preparation*

The Company has elected to present the net income (loss) and comprehensive income (loss) in a single financial statement titled Consolidated Statements of Comprehensive Income (Loss).

The significant accounting policies adopted in the preparation of the audited consolidated financial statements are set out below.

*(iii) Basis of consolidation*

The audited consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary Sangoma Technologies Inc.

Subsidiaries are entities controlled by the Company. Control is defined as the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Subsidiaries are included in the consolidated financial statements from the date control is obtained until the date control ceases. All intercompany balances, transactions, income and expenses have been eliminated on consolidation.

**3. Significant accounting policies (continued)**

*(iv) Inventories*

Parts and finished goods are stated at the lower of cost and net realizable value. Inventory cost includes all expenses directly attributable to the manufacturing process, which include the cost of materials and labor, as well as suitable portions of related production overheads, based on normal operating capacity. Costs of ordinary interchangeable items are assigned using first in, first out formula. Net realizable value is the estimated selling price in the ordinary course of business less any applicable selling expenses.

*(v) Revenue*

Revenue comprises revenue from the sale of goods and the rendering of services. Revenue is measured at the fair value of the consideration received or receivable for the gross inflow of economic benefits during the period, arising in the ordinary course of the Company's activities. Revenue is recognized when it is probable that the economic benefits will flow to the Company.

*Sale of goods (hardware or software)*

For sales of hardware, the recognition criteria are generally met at the time the product is shipped to the customer. Depending on the delivery conditions, title and risk have passed to the customer at that point and acceptance of the product, when contractually required, has been obtained, either via formal acceptance by the customer or lapse of rejection period.

Revenue that consists of license fees relating to software licenses that do not require significant modification or customization of software or where services are not essential to the functionality of the software are recognized when a contract with a customer has been executed, delivery and acceptance of the software have occurred, the license fee is fixed and determinable, and collection of the related receivable is deemed probable by management.

*Rendering of services*

Services comprise after-sales service and maintenance and consulting. The Company provides long term support to its customers and the amount of the selling price associated with the servicing agreement is deferred and recognized as revenue over the period during which the service is performed. This deferred revenue is included in current liabilities. Revenues relating to engineering services are recognized as the services are rendered. Cash received in advance of revenue being recognized is classified as deferred revenue.

The Company also enters into transactions that represent multiple-element arrangements, which may include any combination of equipment and service. These multiple element arrangements are assessed to determine whether they can be sold separately in order to determine whether they can be treated as more than one unit of accounting or element for the purpose of revenue recognition. When there are multiple elements or units of accounting in an arrangement, the arrangement consideration is allocated to the separate units of accounting or elements on a relative fair value basis. If elements cannot be sold separately, revenue recognition is deferred until all elements have been delivered. The revenue recognition policy described above is then applied to each unit of accounting.

*(vi) Cost of sales*

Cost of product sales includes the cost of finished goods inventory and costs related to shipping and handling. Cost of service sales includes direct labour and additional direct and indirect expenses.

**3. Significant accounting policies (continued)**

*(vii) Foreign currency*

The Company's presentation currency is the Canadian Dollar ("C$"). The functional currency of the Company and its subsidiary is the Canadian Dollar.

In preparing the consolidated financial statements, transactions in currencies other than the Company's functional currency are recognized at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are re-translated at the rates prevailing at that date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not re-translated.

Exchange differences are recognized in profit or loss in the period in which they arise.

*(viii) Interest income*

Interest income from financial assets is recognized when it is probable that the economic benefits will flow to the Company and the amount of income can be measured reliably. Interest income is accrued on the basis of time that has passed, by reference to the principal outstanding and at the effective interest rate applicable.

*(ix) Share-based payments*

The Company grants stock options to certain employees. Stock options vest over and expire after various periods of time, with the majority of options vesting 25% after one year and the balance equally over the remaining four years. The fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. Details regarding the determination of the fair value of equity-settled share-based payment transactions are set out in Note 11 (ii).

Share-based compensation expense is recognized over the tranche's vesting period based on the number of awards expected to vest. The number of awards expected to vest is reviewed at least annually, with any impact being recognized immediately.

*(x) Income taxes and deferred taxes*

The income tax provision comprises current and deferred tax. Income tax is recognized in the Statement of Comprehensive Income (Loss) except to the extent that it relates to items recognized directly in equity, in which case the income tax is also recognized directly in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted, or substantively enacted, at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the Statement of Financial Position date and are expected to apply when the asset is realized or liability is settled. Deferred income tax assets are recognized for deductible temporary differences, unused tax losses and other income tax deductions to the extent that it is probable the Company will have taxable income against which those deductible temporary differences, unused tax losses and other income tax deductions can be utilized. The extent to which deductible temporary differences, unused tax losses and other income tax deductions are expected to be realized is reassessed at the end of each reporting period.

**3. Significant accounting policies (continued)**

*(x) Income taxes and deferred taxes*

In a business combination, temporary differences arise as a result of differences in the fair values of identifiable assets and liabilities acquired and their respective tax bases. Deferred income tax assets and liabilities are recognized for the tax effects of these differences. Deferred income tax assets and liabilities are not recognized for temporary differences arising from goodwill or from the initial recognition of assets and liabilities acquired in a transaction other than a business combination which do not affect either accounting or taxable income or loss.

*(xi) Property, plant and equipment*

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the company and the cost can be measured reliably. The carrying amount of a replaced asset is derecognized when replaced. Repairs and maintenance costs are charged to the Statement of Comprehensive Income (Loss) during the period in which they are incurred.

Depreciation is calculated on a straight-line basis over 5 years for all classes except for depreciation for leasehold improvement which is calculated on a straight-line basis over the shorter of the lease term or useful life. Residual values, method of depreciation and useful lives of the assets are reviewed annually and adjusted, if required.

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of other gains and losses in the Statement Comprehensive of Income (Loss).

*(xii) Intangible assets*

Intangible assets with finite lives that are acquired separately are measured on initial recognition at cost, which comprises its purchase price plus any directly attributable costs of preparing the asset for its intended use. Following initial recognition, such intangible assets are carried at cost less any accumulated amortization on a straight-line basis over 10 years for copyright to software, straight-line basis over 10 years for purchased technology, 20 years for patent rights and 3 years for websites. Amortization expense is included in the Statement of Comprehensive Income (Loss) in General and Administration Expense.

The estimated useful life and amortization method are reviewed annually, with the effect of any change in estimate being accounted for on a prospective basis.

*(xiii) Research and development expenditures*

The Company qualifies for certain investment tax credits related to its research and development activities. Research costs are expensed as incurred and are reduced by related investment tax credits, which are recognized when it is probable that they will be realized.

Costs that are directly attributable to the development phase of new products are recognized as intangible assets and amortized over three years provided they meet the following recognition requirements:

**3. Significant accounting policies (continued)**

*(xiii) Research and development expenditures (continued)*

- Completion of the intangible asset is technically feasible so that it will be available for use or sale
- The Company intends to complete the intangible asset and use or sell it
- The Company has the ability to use or sell the intangible asset
- The intangible asset will generate probable future economic benefits. Among other things, this requires that there is a market for the output from the intangible asset or for the intangible asset itself, or, if it is to be used internally, the asset will be used in generating such benefits
- There are adequate technical, financial and other resources to complete the development and to use or sell the intangible asset
- The expenditure attributable to the intangible asset during its development can be measured reliably.

Development costs not meeting these criteria for capitalization are expensed as incurred.

Directly attributable costs include employee costs incurred on software development along with an appropriate portion of relevant overheads and borrowing costs (if any). Internally generated software development recognized as intangible assets are subject to the same subsequent measurement method as externally acquired software licenses. The assets are subject to impairment testing as described below in Note 3(xv) below.

Any gain or loss arising on the disposal of an intangible asset is determined as the difference between the proceeds and the carrying amount of the asset, and is recognized in profit or loss within ‘other income’ or ‘other expenses’.

*(xiv) Goodwill*

Goodwill represents the excess of the acquisition cost in a business combination over the fair value of the Company’s share of the identifiable net assets acquired. Goodwill is carried at cost less accumulated impairment losses. Refer to Note 3 (xv) for a description of impairment procedures.

*(xv) Impairment testing of goodwill, other intangible assets and property, plant and equipment*

For purposes of assessing impairment under IFRS, assets are grouped at the lowest levels for which there are largely independent cash inflows (cash-generating units). Sangoma has only one cash generating unit.

The cash-generating unit to which goodwill has been allocated and intangible assets not yet available for use is tested for impairment at least annually. All other individual assets or cash-generating units are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognized for the amount by which the asset’s or cash-generating unit’s carrying amount exceeds its recoverable amount, which is the higher of fair value less costs to sell and value-in-use. To determine the value-in-use, management estimates expected future cash flows from each cash-generating unit and determines a suitable pre-tax discount rate in order to calculate the present value of those cash flows. The data used for impairment testing procedures are directly linked to the Company’s latest approved budget, adjusted as necessary to exclude the effects of future reorganizations and asset enhancements.

**3. Significant accounting policies (continued)**

*(xv) Impairment testing of goodwill, other intangible assets and property, plant and equipment (continued)*

Discount factors are determined individually for each cash-generating unit and reflect their respective risk profiles as assessed by management.

Impairment losses for cash-generating units reduce first the carrying amount of any goodwill allocated to that cash-generating unit. Any remaining impairment loss is charged pro rata to the other assets in the cash- generating unit. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognized may no longer exist. An impairment charge is reversed if the assets' recoverable amount exceeds its carrying amount only to the extent of the new carrying amount doesn't exceed the carrying value of the asset had it not originally been impaired.

*(xvi) Financial instruments*

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the Statement of Financial Position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

*(i) Financial assets and liabilities at fair value through profit or loss*

A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

Financial instruments are recognized initially and subsequently at fair value. Transaction costs are expensed in the Statement of Comprehensive Income (Loss). Gains and losses arising from changes in fair value are presented in the Statement of Comprehensive Income (Loss) within other gains and losses in the period in which they arise. Financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond twelve months of the Statement of Financial Position date, which are classified as non-current.

*(ii) Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables are comprised of trade receivables, investment tax credit receivable, sales tax receivables and cash and cash equivalents, and are included in current assets due to their short-term nature. Loans and receivables are initially recognized at the amount expected to be received less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.

**3. Significant accounting policies (continued)**

*(xvi) Financial instruments (continued)*

*(iii) Financial liabilities at amortized cost*

Financial liabilities at amortized cost include accounts payable and accrued liabilities and term loan. Trade payables are initially recognized at the amount required to be paid less, when material, a discount to reduce the payables to fair value. Subsequently, trade payables are measured at amortized cost using the effective interest method. Term loan are recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

The Company has classified its financial instruments as follows:

| Asset/liability | Classification | Measurement |
|---|---|---|
| Cash and cash equivalents | Loans and receivables | Amortized cost |
| Investment tax credits receivable | Loans and receivables | Amortized cost |
| Sales tax receivables | Loans and receivables | Amortized cost |
| Trade receivables | Loans and receivables | Amortized cost |
| Accounts payable and accrued liabilities | Other liabilities | Amortized cost |
| Term loan | Other liabilities | Amortized cost |

*(xvii) Impairment of financial assets*

At each reporting date, the Company assesses whether there is objective evidence that a financial asset is impaired. If such evidence exists, the Company recognizes an impairment loss, as follows:

*(i) Financial assets carried at amortized cost*

The loss is the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

*(xviii) Provisions*

Provisions represent liabilities to the Company for which the amount or timing is uncertain. Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are not recognized for future operating losses. Where material, provisions are measured at the present value of the expected expenditures to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

*(xix) Earnings per share*

Basic earnings per share is computed by dividing the net earnings (loss) available to common shareholders by the weighted average number of shares outstanding during the reporting period. Diluted earnings per share is computed similar to basic earnings per share except that the

**3. Significant accounting policies (continued)**

(xix) Earnings per share (continued)

weighted average number of shares outstanding are increased to include additional shares for the assumed exercise of stock options, if dilutive. The average number of shares is calculated by assuming that outstanding conversions were exercised and that the proceeds from such exercises were used to acquire common shares at the average market price during the reporting period.

*(xx) Business combination*

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method. The cost of the business combination is measured as the aggregate of the fair values (at the date of acquisition) of the asset acquired, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree. Acquisition costs are recognized in the Statement of Comprehensive Income (Loss) as incurred unless they relate to the issuance of debt or equity securities.

*(xxi) Investment tax credits*

Investment tax credits (“ITCs”) are recognized where there is reasonable assurance that the ITCs will be received and all attached conditions will be complied with. When the ITCs relates to an expense item, it is recognized as income over the period necessary to match the ITCs on a systematic basis to the costs that it is intended to compensate. Where the ITCs relates to an asset, it reduces the carrying amount of the asset. The ITCs is then recognized as income over the useful life of a depreciable asset by way of a reduced depreciation charge. The Company is actively engaged in scientific research and development (“R&D”) and, accordingly, has previously filed for ITC refunds under both the Canadian federal and Ontario provincial Scientific Research and Experimental Development (“SR&ED”) tax incentive programs. The ITCs recorded in the accounts are based on management's interpretation of the Income Tax Act of Canada, provisions which govern the eligibility of R&D costs. The claims are subject to review by the Canada Revenue Agency and the Minister of Revenue for Ontario before the refunds can be released. To the extent that collection is reasonably assured, ITCs are recorded as a reduction to the underlying expense or asset to which the ITCs is attributable.

*(xxii) Standards, amendments and interpretations to existing standards that are not yet effective and have not been adopted early by the Company*

At the date of authorization of these consolidated financial statements, certain new standards, amendments and interpretations to existing standards have been issued but are not yet effective, and have not been adopted early by the Company.

The Company has adopted all relevant pronouncements in the Company’s accounting policy for the first period beginning after the effective date of the pronouncement. Information on new standards, amendments and interpretations that are expected to be relevant to the Company’s financial statements is provided below. Certain other new standards and interpretations have been issued but are not expected to have a material impact on the Company’s financial statements.

**3. Significant accounting policies (continued)**

*(xx) Standards, amendments and interpretations to existing standards that are not yet effective and have not been adopted early by the Company (continued)*

*Amendments to IAS 1 Presentation of Financial Statements (effective from July 1, 2012)*

Amendments to IAS 1 retain the option to present profit or loss and other comprehensive income either in one continuous statement or in two separate but consecutive statements. Items of other comprehensive income are required to be grouped into those that will and will not be subsequently reclassified to profit or loss. Tax on items of other comprehensive income is required to be allocated on the same basis. The measurement and recognition of items of profit or loss and other comprehensive income are not affected by the amendments. The Company's preliminary assessment indicates that this amendment will not have a material impact on its financial statements.

*IFRS 9 Financial Instruments (effective from January 1, 2015)*

The IASB aims to replace IAS 39 Financial Instruments: Recognition and Measurement in its entirety. The replacement standard (IFRS 9) is being issued in phases. To date, the chapters dealing with recognition, classification, measurement and de-recognition of financial assets and liabilities have been issued. Further chapters dealing with impairment methodology and hedge accounting are still being developed.

The Company has yet to assess the impact that this amendment is likely to have on its financial statements. However, the Company does not expect to implement the amendments until all chapters of IFRS 9 have been published and the Company can comprehensively assess the impact of all changes.

*IFRS 10 Consolidated Financial Statements (effective from January 1, 2013)*

IFRS 10 contains a single consolidation model that identifies control as the basis for consolidation for all types of entities. IFRS 10 provides a definition of control that comprises the following three elements:

- power over an investee;
- exposure, or rights, to variable returns from an investee; and
- ability to use power to affect the reporting entity's returns.

The standard sets out requirements for situations when control is difficult to assess, including cases involving potential voting rights, agency relationships, control of specified assets (silos) and circumstances in which voting rights are not the dominant factor in determining control. The standard also contains accounting requirements and consolidation procedures, which are carried over unchanged from IAS 27, *Consolidated and Separate Financial Statements* ("IAS 27").

The Company has yet to assess the impact that this amendment is likely to have on its financial statements.

*IFRS 11 Joint Arrangements (effective from January 1, 2013)*

IFRS 11 replaces IAS 31, *Interests in Joint Ventures* ("IAS 31"). It requires that all jointly controlled entities be accounted for using the equity method of accounting. IAS 31 allows for a policy choice to account for jointly controlled entities using either proportionate consolidation, or the equity method of accounting.

The Company has yet to assess the impact that this amendment is likely to have on its financial statements.

**3. Significant accounting policies (continued)**

*(xx) Standards, amendments and interpretations to existing standards that are not yet effective and have not been adopted early by the Company (continued)*

*IFRS 12 Disclosure of Interests in Other Entities (effective from January 1, 2013)*

IFRS 12 requires a reporting entity to disclose information that helps users to assess the nature and financial effects of the reporting entity's relationship with other entities. The standard establishes disclosure objectives that require an entity to disclose information that helps users:

- understand the judgments and assumptions made by a reporting entity when deciding how to classify its involvement with another entity;
- understand the interest that non-controlling interests have in consolidated entities; and
- assess the nature of the risks associated with interests in other entities.

*IFRS 13, Fair Value Measurement (effective from January 1, 2013)*

IFRS 13 defines fair value in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The Company has yet to assess the impact that this amendment is likely to have on its financial statements.

*IAS 19, Employee Benefits (effective from January 1, 2013)*

The primary amendment to IAS 19 is the elimination of the corridor approach, with a requirement that all changes to the defined benefit obligation and planned assets to be recognized when they occur. Retrospective application is required with certain exceptions. The Company does not have any defined benefit plan hence it does not expect this change to have any impact on its financial statements.

*IAS 12, Income Taxes (effective from January 1, 2012)*

Amendments to IAS 12 provide an exception to the general principles in IAS 12 that the measurement of deferred tax assets and deferred tax liabilities should reflect the tax consequences that would follow from the manner in which the entity expects to recover the carrying amount of an asset. The Company has yet to assess the impact that this amendment is likely to have on its financial statements

*IAS 27, Separate Financial Statements (effective from January 1, 2013)*

Amendments to IAS 27 intend to enhance the relevance, reliability, and comparability of the information that a parent entity provides under its control. The standard specifies the circumstances in which an entity must consolidate the financial statements of another entity, the accounting for changes in the level of ownership interest in a subsidiary, the accounting for the loss of control of a subsidiary, and the information that an entity must disclose to enable users of the financial statements to evaluate the nature of the relationship between the entity and its subsidiaries. There is no impact to the Company's consolidated financial statements.

*IAS 28, Investments in Associates and Joint Ventures (effective from January 1, 2013)*

Amendments to IAS 28 prescribe the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. The Company has yet to assess the impact that this amendment is likely to have on its financial statements.

**3. Significant accounting policies (continued)**

*(xx) Standards, amendments and interpretations to existing standards that are not yet effective and have not been adopted early by the Company (continued)*

*Amendments to IAS 32, Financial Instruments: Presentation (effective from January 1, 2014)*

The IASB published amendments to IAS 32 Financial Instruments: Presentation to clarify the application of the offsetting requirements. The Company has yet to assess the impact that this amendment is likely to have on its financial statements.

*IFRS 7, Financial Instruments: Disclosures (effective from January 1, 2013)*

The IASB published new disclosures requirements jointly with the Financial Accounting Standards Board ("FASB") that enable users of the financial statements to better compare financial statements prepared in accordance with IFRS and US GAAP. The Company has yet to assess the impact that this amendment is likely to have on its financial statements.

**4. Significant accounting judgments, estimates and uncertainties**

The preparation of consolidated financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and notes to the consolidated financial statements. These estimates are based on management's best knowledge of current events and actions the Company may undertake in the future. Actual results could differ from those estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to the accounting estimates are recognized in the period in which the estimates are revised. Significant areas requiring the Company to make estimates include goodwill impairment testing and recoverability of assets, business combinations, income taxes, estimated useful life of long-lived assets, internally generated development costs, the fair value of share-based payments, allowance for doubtful accounts and inventory obsolescence. These estimates and judgments are further discussed below:

*(i) Goodwill impairment testing and recoverability of assets*

In accordance with IFRS 1, the Company performed a test for impairment of goodwill at June 30, 2012, June 30, 2011 and July 1, 2010 with the details surrounding these impairment tests discussed below. The goodwill recorded in the consolidated financial statements relates to one CGU. The Company's assumptions used in testing goodwill for impairment are affected by current market conditions, which may affect expected revenue and costs. The Company also has significant competition in markets in which it operates, which may impact its revenues and operating costs. The recoverable amount of the CGU was estimated based on an assessment of fair value less costs to sell using a discounted cash flow approach. The approach uses cash flow projections based upon a financial forecast approved by management, covering a five year period. Cash flows for the years thereafter are extrapolated using the estimated terminal growth rates listed below. The risk premiums expected by market participants related to uncertainties about the industry and assumptions relating to future cash flows may differ or change quickly, depending on economic conditions and other events. Accordingly, it is reasonably possible that future changes in assumptions may negatively impact future assessments of the recoverable amount for the CGU's and the Company would be required to recognize an impairment loss. The Company recognized an impairment of $3,850,000 to goodwill for the year ended June 30, 2011 and as at June 30, 2012, the Company's estimate of the recoverable amount for the CGU exceeded its restated carrying value.

The following are the key assumptions on which management based its determinations of the recoverable amount of goodwill:

(in Canadian dollars)

## 4. Significant accounting judgments, estimates and uncertainties (continued)

*(i) Goodwill impairment testing and recoverability of assets (continued)*

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| Allocated to goodwill | **3,543,912** | 2,984,721 | 6,834,721 |
| Gross margin | **69%** | 75% | 75% |
| Terminal growth rate | **2%** | 2% | 2% |
| After-tax discount rate | **19%** | 21% | 21% |

Whenever property, plant and equipment and other intangible assets are tested for impairment, the determination of the assets' recoverable amounts involves the use of estimates by management and can have a material impact on the respective values and, ultimately, the amount of any impairment.

*(ii) Business combinations*

In a business combination, all identifiable assets, liabilities and contingent liabilities acquired are recorded at their fair values. One of the most significant estimates relates to the determination of the fair value of these assets and liabilities. For any intangible asset identified, depending on the type of intangible asset and the complexity of determining its fair value, an independent valuation expert or management may develop the fair value, using appropriate valuation techniques, which are generally based on a forecast of the total expected future net cash flows. The evaluations are linked closely to the assumptions made by management regarding the future performance of the assets concerned and any changes in the discount rate applied. In August 2011, Sangoma purchased the assets of VegaStream for $1,515,754 and recorded Goodwill of $559,191 (see Note 17). The acquisition has been accounted for using the acquisition method.

*(iii) Income taxes*

The Company operates and earns income in Canada and the United Kingdom and is subject to changing income tax laws within these countries. Significant judgments are necessary in determining worldwide income tax liabilities.

At each consolidated Statement of Financial Position date, the Company assesses whether the realization of future income tax benefits is sufficiently probable to recognize deferred income tax assets. This assessment requires the exercise of judgment on the part of management with respect to, among other things, benefits that could be realized from available income tax strategies and future taxable income, as well as other positive and negative factors. The recorded amount of total deferred income tax assets could be reduced if estimates of projected future taxable income and benefits from available income tax strategies are lowered, or if changes in current income tax regulations are enacted that impose restrictions on the timing or extent of the Company's ability to utilize future income tax benefits.

The Company's effective income tax rate can vary significantly quarter-to-quarter for various reasons, including the mix and volume of business in lower income tax jurisdictions and in jurisdictions for which no deferred income tax assets have been recognized because management believed it was not probable that future taxable profit would be available against which income tax losses and deductible temporary differences could be utilized. The Company's effective income tax rate can also vary due to the impact of foreign exchange fluctuations.

**4. Significant accounting judgments, estimates and uncertainties (continued)**

*(iv) Estimated useful lives of long-lived assets*

Management reviews useful lives of depreciable assets at each reporting date. Management assesses that the useful lives represent the expected utility in terms of duration of the assets to the Company. Actual utility, however, may vary due to technical obsolescence, particularly relating to software and Information Technology equipment.

*(v) Internally generated development costs*

Management monitors the progress of internal research and development projects and uses judgment to distinguish research from the development phase. Expenditures during the research phase are expensed as incurred. Development costs are recognized as an intangible asset when the Company can demonstrate certain criteria listed in Note 3 (xiii). Otherwise, they are expensed as incurred.

*(vi) Share-based payments*

The fair value of all share-based payments granted are determined using the Black-Scholes option pricing model which incorporates assumptions regarding risk-free interest rates, dividend yield, expected volatility, estimated forfeitures, and the expected life of the options. The Company has a significant number of options outstanding and expects to continue to make grants. Therefore the estimates and assumptions related to stock options are critical to the Company's financial position

*(vii) Allowance for doubtful accounts*

The Company is exposed to credit risk associated with its trade receivables. This risk is minimized substantially by having the trade receivable insured by Export Development Canada ("EDC"). Management reviews the trade receivables at each reporting date and assesses and makes an allowance for doubtful accounts when the expected recovery could be less than the actual trade receivable.

*(viii) Inventory obsolescence*

Inventory consists of parts and finished goods recorded at the lower of cost and net realizable value. Inventory represents a significant portion of the asset base of the Company and its value is reviewed at each reporting period. Inventories are written down to net realizable value when the cost of inventories is estimated to be unrecoverable due to obsolescence, damage or slow moving.

*(ix) Functional currency*

The functional currency of the Company has been assessed by management based on consideration of the currency and economic factors that mainly influence operating costs, financing and related transactions. Changes to these factors may have an impact on the judgment applied in the future determination of the Company's functional currency.

*(x) Tax credits recoverable*

Tax credits are recorded based on management's estimate that all conditions attached to its receipt have been met. The Company has significant tax credits recoverable and expects to continue to apply for future tax credits as their research and development activities remain applicable. Therefore the estimates related to these tax credits are critical to the Company's financial position.

(in Canadian dollars)

**5. Inventories**

Inventories recognized in the Statement of Financial Position can be analyzed as follows:

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| Finished goods | **1,972,926** | 1,025,217 | 842,071 |
| Parts | **1,125,760** | 493,844 | 806,781 |
| | **3,098,686** | 1,519,061 | 1,648,852 |
| Provision for obsolescense | **(57,849)** | (57,849) | - |
| Net inventory carrying value | **3,040,837** | 1,461,212 | 1,648,852 |

During the year ended June 30, 2012, there were no additional provisions made against inventory and a total of $3,974,033 of inventories were included in cost of goods sold compared to $2,736,959 for the year ended June 30, 2011.

**6. Property, plant and equipment**

*Cost*

| | Office furniture and computer equipment | Software and books | Stockroom and production equipment | Tradeshow equipment | Leasehold improvement | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Balance, July 1, 2010 | 529,393 | 158,614 | 95,348 | 41,631 | - | 824,986 |
| Additions | 30,740 | 3,350 | 3,800 | - | 84,650 | 122,540 |
| Disposals | - | - | - | - | - | - |
| Balance, June 30, 2011 | 560,133 | 161,964 | 99,148 | 41,631 | 84,650 | 947,526 |
| Additions | 59,452 | 20,220 | - | - | 7,114 | 86,786 |
| Business combination (Note 17) | 15,763 | - | - | - | - | 15,763 |
| Disposals | - | - | - | - | - | - |
| **Balance, June 30, 2012** | **635,348** | **182,184** | **99,148** | **41,631** | **91,764** | **1,050,075** |

(in Canadian dollars)

## 6. Property, plant and equipment (continued)

*Accumulated depreciation and impairment*

| | Office furniture and computer equipment | Software and books | Stockroom and production equipment | Tradeshow equipment | Leasehold improvement | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Balance, July 1, 2010 | 366,499 | 93,372 | 42,800 | 12,984 | - | 515,655 |
| Elimination on disposal of assets | - | - | - | - | - | - |
| Depreciation expense | 42,577 | 9,167 | 7,662 | 3,882 | 14,116 | 77,404 |
| Balance, June 30, 2011 | 409,076 | 102,539 | 50,462 | 16,866 | 14,116 | 593,059 |
| Elimination on disposal of assets | - | - | - | - | - | - |
| Depreciation expense | 37,704 | 14,103 | 8,544 | 4,328 | 13,776 | 78,455 |
| **Balance, June 30, 2012** | **446,780** | **116,642** | **59,006** | **21,194** | **27,892** | **671,514** |

Carrying amount

| | Office furniture and computer equipment | Software and books | Stockroom and production equipment | Tradeshow equipment | Leasehold improvement | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Balance, July 1, 2010 | 162,894 | 65,242 | 52,548 | 28,647 | - | 309,331 |
| Balance, June 30, 2011 | 151,057 | 59,425 | 48,686 | 24,765 | 70,534 | 354,467 |
| **Balance, June 30, 2012** | **188,567** | **65,542** | **40,142** | **20,437** | **63,872** | **378,560** |

Depreciation expense is included in general and administration expense in the Statement of Comprehensive Income (Loss).

## 7. Intangible assets

*Cost*

| | Copyright to software | Patent rights | Purchased technology | Website | Trademarks | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Balance, July 1, 2010 | 2,948,461 | 1,587,633 | - | 382,203 | 54,869 | 4,973,166 |
| Additions | - | - | - | 59,625 | - | 59,625 |
| Disposals | - | - | - | - | - | - |
| Balance, June 30, 2011 | 2,948,461 | 1,587,633 | - | 441,828 | 54,869 | 5,032,791 |
| Additions | - | - | - | - | - | - |
| Business combination (Note 17) | - | - | 905,000 | - | - | 905,000 |
| Disposals | - | - | - | - | - | - |
| **Balance, June 30, 2012** | **2,948,461** | **1,587,633** | **905,000** | **441,828** | **54,869** | **5,937,791** |

(in Canadian dollars)

### 7. Intangible assets (continued)

*Accumulated amortization and impairment*

| | Copyright to software | Patent rights | Purchased technology | Website | Trademarks | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Balance, July 1, 2010 | 569,866 | 178,590 | - | 243,794 | 54,869 | 1,047,119 |
| Elimination on disposal of assets | - | - | - | - | - | - |
| Amortization expense | 314,673 | 1,409,043 | - | 87,994 | - | 1,811,710 |
| Balance, June 30, 2011 | 884,539 | 1,587,633 | - | 331,788 | 54,869 | 2,858,829 |
| Elimination on disposal of assets | - | - | - | - | - | - |
| Amortization expense | 294,846 | - | 60,000 | 87,993 | - | 442,839 |
| **Balance, June 30, 2012** | **1,179,385** | **1,587,633** | **60,000** | **419,781** | **54,869** | **3,301,668** |

Carrying amount

| | Copyright to software | Patent rights | Purchased technology | Website | Trademarks | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Balance, July 1, 2010 | 2,378,595 | 1,409,043 | - | 138,409 | - | 3,926,047 |
| Balance, June 30, 2011 | 2,063,922 | - | - | 110,040 | - | 2,173,962 |
| **Balance, June 30, 2012** | **1,769,076** | **-** | **845,000** | **22,047** | **-** | **2,636,123** |

Amortization expense is included in general and administration expense in the Statement of Comprehensive Income (Loss).

(in Canadian dollars)

## 8. Development costs

| | $ |
|---|---|
| **Development costs** | |
| Balance at July 1, 2010 | 6,825,492 |
| Additions | 2,290,348 |
| Investment tax credits | (1,112,000) |
| Balance at June 30, 2011 | 8,003,840 |
| Additions | 2,701,336 |
| Investment tax credits | (847,617) |
| **Balance at June 30, 2012** | **9,857,559** |
| | |
| **Accumulated amortization** | |
| Balance at July 1, 2010 | (4,667,271) |
| Amortization | (1,341,650) |
| Balance at June 30, 2011 | (6,020,175) |
| Amortization | (1,590,171) |
| **Balance at June 30, 2012** | **(7,610,346)** |

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| Net capitalized development costs | **2,247,213** | 1,983,665 | 2,158,221 |

Each period the new spending is added net of Investment Tax Credits accrued. In addition to the above amortization, the Company has recognized $1,207,334 of research expenditure as an expense during the year ending June 30, 2012 (June 30, 2011 - $753,392).

## 9. Financial instruments

The Company categorizes each of its fair value measurements in accordance with a fair value hierarchy. The fair value hierarchy establishes three levels to classify the inputs to valuation techniques used to measure fair value. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets, inputs other than quoted prices that are observable for the asset or liability (for example, interest rate and yield curves observable at commonly quoted intervals, forward pricing curves used to value currency and commodity contracts and volatility measurements used to value option contracts), or inputs that are derived principally from or corroborated by observable market data or other means. Level 3 inputs are unobservable (supported by little or no market activity).

The fair value hierarchy gives the highest priority to Level 1 inputs and the lowest priority to Level 3 inputs.

The fair values of the cash and cash equivalents, trade receivables, sales tax receivables, investment tax credits receivable, accounts payable and accrued liabilities and term loan approximate their carrying values due to the relatively short-term maturity of these financial instruments.

(in Canadian dollars)

## 9. Financial instruments (continued)

Cash and cash equivalent is comprised of

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| Cash at bank and on hand | **510,736** | 4,236,993 | 4,394,246 |
| Short-term investments | **4,506,089** | 4,547,329 | 3,350,350 |
| Total cash and cash equivalents | **5,016,825** | 8,784,322 | 7,744,596 |

Cash includes demand deposits with financial institutions and cash equivalents consist of short-term, highly liquid investments purchased with original maturities of three months or less.

The Company's interest income on short-term investment carried at amortized cost is presented on the Statement of Comprehensive Income (Loss) in the Investment income line.

Total interest income and expense and total fee income and expense for financial assets or financial liabilities that are not at fair value through profit or loss can be summarized as follows:

| | **June 30, 2012** | June 30, 2011 |
|---|---|---|
| | **$** | $ |
| Interest income on short-term investments | **(18,047)** | (26,374) |
| Interest expense arising from short-term investments | **-** | - |
| | **(18,047)** | (26,374) |

## 10. Financial instruments risks

The Company thoroughly examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of those risks. These risks may include credit risk, liquidity risk, foreign currency risk, interest rate risk and market risk.

*Credit risk*

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its obligations. The Company has an insurance policy with Export Development Canada ("EDC") for its trade receivables to manage this risk and minimize any exposure. The Company's maximum exposure to credit risk for its trade receivables, is summarized as follows:

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| Trade receivables aging | | | |
| 0-30 days | **3,647,341** | 2,032,367 | 1,644,782 |
| 31-90 days | **471,938** | 213,929 | 186,910 |
| Greater than 90 days | **394,172** | 27,721 | 141,066 |
| | **4,513,451** | 2,274,017 | 1,972,758 |
| Provision for doubtful accounts | **(18,433)** | (41,313) | - |
| Net trade receivable | **4,495,018** | 2,232,704 | 1,972,758 |

## 10. Financial instruments risks (continued)

*Credit risk (continued)*

The movement in the allowance for doubtful accounts can be reconciled as follows:

| | **June 30, 2012** | June 30, 2011 |
|---|---|---|
| | **$** | $ |
| Provision for doubtful accounts | | |
| Allowance for doubtful accounts beginning balance | **(41,313)** | - |
| Allowance used/ (recorded) during the year | **22,880** | (41,313) |
| Allowance for doubtful accounts ending balance | **(18,433)** | (41,313) |

All of the Company's cash and cash equivalents and short-term investments are held with a major Canadian financial institution and thus the exposure to credit risk is considered insignificant. The short-term investments are cashable in whole or in part, generally with interest, at any time to maturity. Management actively monitors the Company's exposure to credit risk under its financial instruments, including with respect to trade receivables.

*Liquidity risk*

Liquidity risk is the risk that the Company will not be able to meet its obligations associated with financial liabilities. The Company has a planning and budgeting process in place by which it anticipates and determines the funds required to support its normal operating requirements. The Company coordinates this planning and budgeting process with its financing activities through its capital management process.

The Company holds sufficient cash and equivalents and working capital, maintained through stringent cash flow management, to ensure sufficient liquidity is maintained. Maturity analysis of debt can be summarized as follows:

| | Fiscal year | | | |
|---|---|---|---|---|
| | 2013 | 2014 | 2015 | Total |
| | $ | $ | $ | $ |
| Accounts payable and accrued liabilities | 2,101,599 | - | - | 2,101,599 |
| Term loan maturity | 34,072 | 17,035 | - | 51,107 |

*Foreign currency risk*

A large portion of the Company's transactions occur in a foreign currency (mainly in US dollars) and, therefore, the Company is exposed to foreign currency risk at the Statement of Financial Position date through its U.S. denominated accounts receivable, accounts payable and cash. As at June 30, 2012 a 10% depreciation or appreciation of the U.S. dollar against the Canadian dollar would have resulted in an approximate $400,000 decrease or increase, respectively, in total comprehensive income. The Company did not employ any currency hedging programs during the current period but did reduce its U.S. dollar exposure since the reporting date see Note 19. On an ongoing basis the Company's top line revenues are also impacted by the swings in the US dollar.

(in Canadian dollars)

**10. Financial instruments risks (continued)**

*Interest rate risk*

The Company has no significant exposure at June 30, 2012, June 30, 2011 and July 1, 2010 to interest rate risk through its financial instruments as the term loan is non-interest bearing and the short-term investments are at fixed rates of interest that do not fluctuate during the remaining term.

*Market risk*

The Company is exposed to market risk with respect to its short-term investments. The fair value of these financial instruments will fluctuate due to changes in market prices.

**11. Shareholders' equity**

*i. Share capital and contributed surplus*

Issued and outstanding common shares consist of the following:

| | **June 30, 2012** | June 30, 2011 |
|---|---|---|
| | **#** | # |
| Shares issued and fully paid | | |
| Beginning balance | **29,837,809** | 29,564,723 |
| Share issue | **-** | 778,086 |
| Normal course bid redemption | **(299,000)** | (505,000) |
| | **29,538,809** | 29,837,809 |
| Opening balance number of stock options outstanding | **4,603,910** | 1,368,950 |
| Shares authorized for share-based payments (granted) | **-** | 3,451,060 |
| Share-based payments options expired | **(365,500)** | (216,100) |
| Number of stock options outstanding | **4,238,410** | 4,603,910 |
| Total shares and options outstanding | **33,777,219** | 34,441,719 |

| | | |
|---|---|---|
| For each class of share capital | | |
| The number of shares authorized | Unlimited | Unlimited |
| The number of shares issued and fully paid | **29,538,809** | 29,837,809 |
| The number of shares issued but not fully paid | **-** | - |
| Par value per share, or that the shares have no par value | **-** | - |

On July 1, 2010, there were 29,564,723 common shares issued and outstanding.

Effective December 10, 2010, the Company received approval from the TSX Venture Exchange to purchase its own common shares up to a maximum of 5% of the issued and outstanding common shares being 1,491,890 of the 29,538,809 shares outstanding. During 2012, under the course of a normal course issuer bid that expires December 18, 2012, the Company repurchased and cancelled 299,000 shares (2011- 505,000) at a total cost of $154,181 (2011- $252,154), an average of $0.52 per share (2011- $0.50). There are no differences between the share capital and the cost of redemption that needs to be added to the contributed surplus.

## 11. Shareholders' equity (continued)

*ii. Stock options*

The Company has a stock option plan (the plan) for directors, officers, employees and consultants of the Company. The number of common shares that may be set aside for issue under the plan (and under all other management stock option and employee stock option plans) is limited to 5,542,160 common shares of the Company, provided that the board of directors has the right, from time to time, to increase such number subject to the approval of the shareholders of the Company and provided that the Company complies with the provisions of policies, rules and regulations of applicable securities legislation.

The maximum number of common shares that may be reserved for issuance to any one person under the plan is 5% of the common shares outstanding at the time of grant (calculated on a non-diluted basis) less the number of common shares reserved for issuance to such person under any stock option to purchase common shares granted as a compensation or incentive mechanism.

Any common shares subject to a stock option, which for any reason is cancelled or terminated prior to exercise, will be available for a subsequent grant under the plan, subject to applicable regulatory requirements.

The stock option price of any common shares cannot be less than the closing price or the minimum price as determined by applicable regulatory authorities of the relevant class or series of shares, on the day immediately preceding the day on which the stock option is granted. Stock options granted under the plan may be exercised during a period not exceeding five years from the date of grant, subject to earlier termination on the termination of the optionee's employment, on the optionee's ceasing to be an employee, officer or director of the Company or any of its subsidiaries, as applicable, or on the optionee's retiring, becoming permanently disabled or dying, subject to certain grace periods to allow the optionee or his or her personal representative time to exercise such stock options. The stock options are non-transferable.

The plan contains provisions for adjustment in the number of common shares issuable thereunder in the event of the subdivision, consolidation, reclassification or change of the common shares, a merger or other relevant changes in the Company's capitalization. The board of directors may, from time to time, amend or revise the terms of the plan or may terminate the plan at any time.

(in Canadian dollars)

## 11. Shareholders' equity (continued)

*ii. Stock options (continued)*

The following table shows the movement in the stock option plan:

| Measurement date | Number of options | Weighted average exercise price |
|---|---|---|
| | | $ |
| Balance, July 1, 2010 | 1,368,950 | 0.86 |
| Granted | 3,451,060 | 0.48 |
| Exercised | - | - |
| Expired | (216,100) | 0.93 |
| Cancelled | - | - |
| Forfeited | - | - |
| Balance, June 30, 2011 | 4,603,910 | 0.58 |
| Granted | - | - |
| Exercised | - | - |
| Expired | (365,500) | 0.69 |
| Cancelled | - | - |
| Forfeited | - | - |
| Balance, June 30, 2012 | 4,238,410 | 0.57 |

The Company uses the fair value method to account for all stock-based awards granted to employees, officers and directors. The estimated fair value of stock options granted is determined using the Black-Scholes option pricing model and is recorded as a charge to income over the vesting period of the stock options, with a corresponding increase to contributed surplus. Stock options are granted at a price equal to or above the fair value of the common shares on the day immediately preceding the date of the grant. The consideration received on the exercise of stock options is added to stated capital at the time of exercise (see Consolidated Statement of Changes in Equity).

The fair value of the stock options granted has been estimated on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

| | **June 30, 2012** | June 30, 2011 |
|---|---|---|
| Weighted average share price | **-** | $0.58 |
| Exercise price | **-** | $0.48 |
| Expected volatility | **-** | 77.24% |
| Expected option life | **-** | 4.55 |
| Expected dividend yield | **-** | - |
| Risk-free interest rate | **-** | 1.96% |

The expected volatility used in the Black-Scholes option pricing model is based on the historical volatility of the Company's shares.

The following table summarizes information about the stock options outstanding and exercisable at the end of each period:

(in Canadian dollars)

## 11. Shareholders' equity (continued)

*ii. Stock options (continued)*

| | **June 30, 2012** | | June 30, 2011 | | July 1, 2010 | |
|---|---|---|---|---|---|---|
| Exercise price | **Number of stock options outstanding and exercisable** | **Weighted average remaining contractual life** | Number of stock options outstanding and exercisable | Weighted average remaining contractual life | Number of stock options outstanding and exercisable | Weighted average remaining contractual life |
| $0.26 - $0.50 | **1,993,498** | **3.39** | 1,993,498 | 4.39 | - | - |
| $0.51 - $0.75 | **1,816,562** | **3.25** | 2,162,062 | 3.66 | 803,100 | 2.86 |
| $1.01 - $1.25 | **428,350** | **0.35** | 448,350 | 1.34 | 565,850 | 2.49 |
| Total | **4,238,410** | **3.02** | 4,603,910 | 3.75 | 1,368,950 | 2.71 |

Total expense recognized for share based payments was $372,925 (June 30, 2011 - $293,438).

*iii. Earnings per share and dividends*

Both the basic and diluted earnings per share have been calculated using the net income attributable to the shareholders of the Company as the numerator.

The weighted average number of outstanding shares used for basic earnings per share amounted to 29,618,366 shares (June 30, 2011 - 30,088,138).

The weighted average number of shares for the purposes of diluted earnings per share can be reconciled to the weighted average number of ordinary shares used in the calculation of basic earnings per share as follows:

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| Number of shares | | | |
| Weighted average number of shares used in basic earnings per share | **29,618,366** | 30,088,138 | 29,458,193 |
| Shares deemed to be issued in respect of share-based payments | **133,510** | 173,200 | 778,086 |
| Weighted average number of shares used in diluted earnings per share | **29,751,876** | 30,261,338 | 30,236,279 |

As of June 30, 2012, 1,993,498 options (2011- 1,244,412) were in-the-money hence it was included in the weighted average number of shares for the purposes of diluted earnings per share calculation above. As a result, 2,244,912 options (2011- 3,359,498) are excluded from the weighted average number of shares calculation above.

## 12. Income tax

The Company has deducted available SR&ED for federal and provincial purposes and has utilized SR&ED investment tax credits, as required, to reduce federal income taxes payable. These consolidated financial statements take into account an income tax benefit resulting from investment tax credits available to the Company to reduce its income for federal income tax purposes in future years as follows:

(in Canadian dollars)

## 12. Income tax (continued)

| Year of investment | Year of expiration | Carry-forward credits |
|---|---|---|
| | | $ |
| 2011 | 2031 | 132,875 |
| 2012 | 2032 | 645,000 |
| | | 777,875 |

The income tax benefit of eligible SR&ED costs incurred in prior years but not utilized have been taken into account in these consolidated financial statements.

| | Federal | Provincial |
|---|---|---|
| | $ | $ |
| SR&ED expenditures carried forward | 1,169,797 | 1,162,137 |

The following reconciles the effective tax rate to the statutory rate on a percentage basis:

| | **June 30, 2012** | June 30, 2011 |
|---|---|---|
| | **%** | % |
| Statutory tax rate (recovery) | **27.9** | (29.2) |
| Tax effect on non-deductible expenses | **13.9** | 2.1 |
| Non-deductible goodwill write-off | **-** | 29.2 |
| Non-deductible cumulative eligible capital ("CEC") | **8.0** | - |
| Tax rate (recovery) on others | **(0.2)** | (6.8) |
| Effective income tax rate (recovery) | **49.6** | (4.7) |

The tax effects of temporary differences and credits carryforwards that give rise to the deferred income tax assets and liabilities are summarized below:

| | **June 30, 2012** | June 30, 2011 | July 1, 2011 |
|---|---|---|---|
| | **$** | $ | $ |
| Property, plant and equipment | **77,237** | (52,678) | (62,980) |
| Non-deductible reserves | **4,922** | 13,180 | - |
| Deferred development costs | **(617,984)** | (513,592) | (632,222) |
| Intangible assets including goodwill | **(697,287)** | (559,116) | (1,056,751) |
| SR&ED investment tax credits | **513,649** | 113,281 | 129,173 |
| Deferred revenue | **27,491** | 16,829 | 22,355 |
| Non-capial lossess | **105,944** | - | 152,927 |
| Unutilized SR&ED expenditure pools | **320,494** | 451,030 | 375,861 |
| Deferred income tax liabilities | **(265,534)** | (531,066) | (1,071,637) |

(in Canadian dollars)

## 13. Related parties

The Company's related parties include its subsidiary and key management personnel and their close family members. Unless otherwise stated, none of the transactions incorporate special terms and conditions and no guarantees were given or received. Outstanding balances payable are usually settled in cash and relate to director fees.

The Company had the following balances with related parties:

| | **June 30, 2012** | | June 30, 2011 | | July 1, 2010 | |
|---|---|---|---|---|---|---|
| | **Key management personnel** | **Other related parties** | Key management personnel | Other related parties | Key management personnel | Other related parties |
| | **$** | **$** | $ | $ | $ | $ |
| The total of the transactions | | | | | | |
| Expense | **-** | **55,142** | - | 16,950 | N/A | N/A |
| The amount of outstanding balances | | | | | | |
| Receivable | **-** | **-** | - | - | - | - |
| Payable | **-** | **5,000** | - | 2,000 | - | - |

*Compensation of key management personnel*

Key management personnel are those individuals having authority and responsibility for planning, directing and controlling the activities of the Company, including members of the Company's Board of Directors. The Company considers key management to be the members of the Board of Directors and three officers.

The remuneration of directors and other members of key management personnel during fiscal year ended June 30, 2012 were as follows:

| | **2012** | 2011 |
|---|---|---|
| | **$** | $ |
| Short-term benefits | **1,325,564** | 1,201,570 |
| Long-term benefits | **30,000** | 30,000 |
| Shared-based payment transactions | **323,077** | 252,640 |
| Total compensation | **1,678,641** | 1,484,210 |

## 14. Segment disclosures

The Company operates in one industry segment; development, manufacturing, distribution and support of voice and data connectivity components for software-based communication applications. The majority of the Company's assets are located in Canada. The Company sells into three major geographic centers: the United States, Canada and other foreign countries. The Company has determined that it has a single reportable segment as the Company's decision makers review information on a consolidated basis.

Revenues for each group of similar products and services can be summarized for year ending:

## 14. Segment disclosures (continued)

| | **2012** | 2011 |
|---|---|---|
| | **$** | $ |
| Products | **13,491,648** | 11,622,088 |
| Services | **271,223** | 239,426 |
| Total revenues | **13,762,871** | 11,861,514 |

The sales, in Canadian dollars, in each of these geographic locations for year ending:

| | **2012** | 2011 |
|---|---|---|
| | **$** | $ |
| USA | **5,174,760** | 4,889,106 |
| Canada | **1,186,851** | 1,233,390 |
| All other countries | **7,401,260** | 5,739,018 |
| Total revenues | **13,762,871** | 11,861,514 |

## 15. Capital management

The Company's objectives in managing capital are to safeguard the Company's assets, to ensure sufficient liquidity to sustain the future development of the business via advancement of its significant research and development efforts, to conservatively manage financial risk and to maximize investor, creditor and market confidence. The Company considers its capital structure to include its shareholders' equity. Working capital is optimized via stringent cash flow policies surrounding disbursement, foreign currency exchange and investment decision-making.

There were no changes in the Company's approach to capital management during the year and the Company is not subject to any capital requirements imposed by external parties.

The Company manages the following capital:

| | **June 30, 2012** | June 30, 2011 | July 1, 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| Share capital | **15,712,274** | 15,866,455 | 15,158,762 |
| Contributed surplus | **1,277,393** | 904,468 | 611,030 |
| Retained earnings | **2,918,130** | 2,503,147 | 6,262,043 |
| Total | **19,907,797** | 19,274,070 | 22,031,835 |

## 16. Commitments

The future minimum lease payments for office space as at June 30, 2012 are as follows:

| | $ |
|---|---|
| Not later than one year | 403,657 |
| Later than one year and not later than five years | 608,703 |
| | 1,012,360 |

(in Canadian dollars)

### 17. Business combination

On August 22, 2011 Sangoma Technologies Inc. acquired certain assets of the VegaStream Group of Companies, a United Kingdom ("UK") based developer of voice over Internet Protocol ("VoIP") Gateway appliances for a total cash consideration of $1,515,754. The transaction was undertaken in two components, the purchase of customer contracts from VegaStream Distribution Limited ("VDL") and the purchase of product design, licenses, prototypes, inventory, test equipment, certain supplier relationship and employment obligations from the administrator acting for VegaStream Group Limited ("VGL"). In addition Sangoma acquired a 5% shareholding in VegaStream Private Networks Limited an Indian company based in Bangalore, which is majority owned by an independent party, and which sells the Vega line of products in India and surrounding countries. On December 1, 2011 Sangoma launched the Vega product line as part of the Sangoma portfolio of products.

The two asset transactions described above are to be accounted for as a single business combination.

| | $ |
|---|---|
| Consideration for the acquisition | |
| Purchase of assets from VDL | 224,231 |
| Purchase of assets from the administrator for VGL | 1,291,523 |
| Total consideration | 1,515,754 |

| | $ |
|---|---|
| Purchase price allocation | |
| Investment in VegaStream Private Networks Limited | 10,665 |
| Inventory | 25,135 |
| Equipment | 15,763 |
| Intangible assets (purchased technology) (Note 7) | 905,000 |
| Goodwill | 559,191 |
| | 1,515,754 |

Since August 22, 2011 all revenues and costs have been incorporated into Sangoma's Financial Statements. Sangoma has established a branch office in the UK for employing staff in the UK. Transaction fees of $251,490 have been expensed in the period.

### 18. Transition to IFRS

The Company's audited consolidated financial statements for the year ended June 30, 2012 are the first annual financial statements that are prepared in accordance with IFRS, and these consolidated financial statements were prepared as described in Note 2, including the application of IFRS 1. IFRS 1 requires an entity to adopt IFRS in its first annual financial statements prepared under IFRS by making an explicit and unreserved statement in those financial statements of compliance with IFRS.

IFRS 1 also requires that comparative financial information be provided. As a result, the first date at which the Company has applied IFRS was July 1, 2010 (the "Transition Date"). IFRS 1 requires first-time adopters to retrospectively apply all effective IFRS standards as of the reporting date, which, for the Company, is June 30, 2012. However, it also provides for certain optional exemptions and certain mandatory exceptions for first time IFRS adopters.

*Initial elections upon adoption*

Set forth below are the IFRS 1 applicable exemptions and exceptions applied in the Company's conversion from Canadian GAAP to IFRS.

(in Canadian dollars)

**18. Transition to IFRS (continued)**

*(i) IFRS exemption options*

1. Share-based payments - IFRS 2 *Share-based Payments*, encourages application of its provisions to equity instruments granted on or before November 7, 2002, but permits the application only to equity instruments granted after November 7, 2002 that had not vested by the Transition Date. The Company elected to avail itself of the exemption provided under IFRS 1 and applied IFRS 2 only to equity instruments granted after November 7, 2002 that had not vested by its Transition Date.
2. The Company has elected to use facts and circumstances existing at the date of transition to determine whether an arrangement contains a lease.
3. Financial assets and liabilities that had been de-recognized before July 1, 2010 under previous GAAP have not been recognized under IFRS.
4. The Company has not elected to designate previously recognized financial instruments at available-for- sale or at fair-value-through-profit-or-loss;
5. The Company has elected to take an election to apply a transitional provision available for borrowing costs and therefore IAS 23 Borrowing Costs will be applied from July 1, 2010.
6. The Company has elected to take an election not to restate the accounting of past business combinations and therefore IFRS 3 Business Combinations will be applied from July 1, 2010;
7. The Company has elected not to select fair value as deemed cost for property, plant and equipment or intangible assets and therefore IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* will be applied with retroactive application;

*(ii) IFRS mandatory exceptions*

1. Estimates - Hindsight is not used to create or revise estimates. The estimates previously made by the Company under Canadian GAAP were not revised for application of IFRS.

*Reconciliations of Canadian GAAP to IFRS*

IFRS 1 requires an entity to reconcile equity, total comprehensive income (loss) and cash flows for prior periods. The changes made to the consolidated Statement of Financial Position and consolidated Statement of Comprehensive Income (Loss) have resulted in reclassifications of various amounts on the consolidated Statements of Cash Flow, however, as there have been no changes to the net cash flows, no reconciliations have been presented.

*Reconciliation of shareholders' equity*

| | Share capital | Contributed surplus | Retained earnings | Total equity |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| As reported under GAAP, July 1, 2010 | 15,158,762 | 554,043 | 6,319,030 | 22,031,835 |
| IFRS 2- share-based payments amortization | - | 56,987 | (56,987) | - |
| As reported under IFRS, July 1, 2010 | 15,158,762 | 611,030 | 6,262,043 | 22,031,835 |

(in Canadian dollars)

**18. Transition to IFRS (continued)**

*Reconciliations of Canadian GAAP to IFRS (continued)*

*Reconciliation of shareholders' equity (continued)*

| | Share capital | Contributed surplus | Retained earnings | Total equity |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| As reported under GAAP, June 30,2011 | 15,866,455 | 754,852 | 2,652,763 | 19,274,070 |
| IFRS 2- share-based payments amortization | - | 149,616 | (149,616) | - |
| As reported under IFRS, June 30, 2011 | 15,866,455 | 904,468 | 2,503,147 | 19,274,070 |

*Reconciliation of total comprehensive income (loss)*

| | Year ended June 30, 2011 |
|---|---|
| | $ |
| As reported under Canadian GAAP | (3,666,267) |
| IFRS 2- share-based payments amortization | (92,629) |
| Comprehensive loss as reported under IFRS | (3,758,896) |

*Changes in accounting policies*

In addition to the exemptions and exceptions discussed above, the following narratives explain the significant differences between the previous historical Canadian GAAP accounting policies and the current IFRS policies applied by the Company.

1. *IFRS 2 - share-based payment*

IFRS 2 is effective for the Company as of July 1, 2010 and is applicable to stock options that are unvested at that date. The transition rules in IFRS 1 and IFRS 2 as applied by the Company result in the following:

- Stock option grants prior to November 7, 2002 are not required to be restated under IFRS 2;
- Stock option grants subsequent to November 7, 2002 are only required to be restated under IFRS 2 if they have not vested as at July 1, 2010; and,
- From July 1, 2010 onwards, all stock options payments are treated under IFRS 2.

Recognition of expense

Canadian GAAP - For grants of share-based awards with graded vesting, the total fair value of the award is recognized on a straight-line basis over the period necessary to vest the award.

## 18. Transition to IFRS (continued)

*Changes in accounting policies (continued)*

1. *IFRS 2 - share-based payment (continued)*

IFRS - Each tranche in an award with graded vesting is considered a separate grant with a different vesting date and fair value. Each grant is accounted for on that basis.

As a result of this difference, the Company recognized an increase in share-based payment expense of $56,987 through opening retained earnings. Implementation also resulted in an increase of $92,629 to share-based payment expense for the twelve months ended at June 30, 2011.

Estimated life/ Forfeitures

Canadian GAAP - Life of the option for the purposes of fair value measurement is the option's contractual life. Forfeitures of awards are recognized as they occur.

IFRS - At the time of recognition IFRS requires the Company to estimate, to its best ability, the number of options that will eventually vest and measure the transaction at this best available estimate. IFRS also requires this best available estimate to be revised when subsequent information indicates a new estimate. On the vesting date, the estimate should be revised to be equal to what is ultimately vested.

The Company has completed an analysis of historical information and has determined at the date of transition - July 1, 2010 the forfeiture rate is 0.46% and is considered immaterial, no adjustments were recognized. *IAS 36 - impairment*

IAS 36 uses a one-step approach for testing and measuring asset impairments, with carrying values being compared to the higher of value in use and fair value less costs to sell. Value in use is defined as being equal to the present value of future cash flows expected to be derived from the asset. In the absence of an active market, fair value less costs to sell may be determined using discounted cash flows. IAS 36 allows reversal of previously recognized impairment losses (other than goodwill) where circumstances change such that impairment loss recognized in prior periods may no longer exist or may have decreased.

Canadian GAAP uses undiscounted future cash flows to compare against the asset's carrying value to determine if impairment exists. Canadian GAAP prohibits reversal of previously recognized impairment losses.

The Company's assets are subject to the one-step approach under IFRS for testing and measuring asset impairments, which may result in some impairments being recognized or reversed under IFRS that would not have been required or permitted under Canadian GAAP.

The Company performed an impairment test and has determined that no impairment is present.

(in Canadian dollars)

## 18. Transition to IFRS (continued)

Reconciliation of consolidated Statement of Comprehensive Income (Loss) as previously reported under Canadian GAAP to IFRS:

| | | | | Year ended June 30, 2011 |
|---|---|---|---|---|
| | Footnote | Canadian GAAP | Effect of transition to IFRS | IFRS |
| | | $ | $ | $ |
| Sales | | 11,861,514 | - | 11,861,514 |
| Cost of sales | | 3,022,458 | - | 3,022,458 |
| Gross profit | | 8,839,056 | - | 8,839,056 |
| Expenses | | | | |
| Sales and marketing (S&M) | (1) | 2,111,037 | (275,743) | 1,835,294 |
| Research and development (R&D) | (2) | 1,352,060 | 742,982 | 2,095,042 |
| General and administration (G&A) | (3) | 2,622,992 | 365,825 | 2,988,817 |
| Foreign currency exchange loss/(gain) | | 693,042 | - | 693,042 |
| Depreciation of property, plant and equipment | (4) | 165,398 | (165,398) | - |
| Amortization of intangible assets | (4) | 374,228 | (374,228) | - |
| Share-based compensation | (4) | 200,809 | (200,809) | - |
| Total expenses | (5) | 7,519,566 | 92,629 | 7,612,195 |
| Operating Income | (5) | 1,319,490 | (92,629) | 1,226,861 |
| Investment income | | (26,374) | - | (26,374) |
| Accelerated amortization of patents | | 1,349,489 | - | 1,349,489 |
| Impairment of goodwill | | 3,850,000 | - | 3,850,000 |
| (Loss) income before provision for income taxes | (5) | (3,853,625) | (92,629) | (3,946,254) |
| Provision for (recovery of) income taxes | | | | |
| Current | | 277,913 | - | 277,913 |
| Future | | (465,271) | - | (465,271) |
| | | (187,358) | - | (187,358) |
| Net loss and total comprehensive loss | (5) | (3,666,267) | (92,629) | (3,758,896) |

The Company has elected to categorize expenses by function rather than type of expense and thus some expenses have been captured by function.

(1) Some of Canadian GAAP S&M line items now are categorized in G&A

(2) The engineering costs expensed each year are now shown in R&D in addition to the development cost amortization.

(3) G&A has been reduced by engineering costs but now includes amortization of intangible assets and share-based payment expense.

(4) Amortization and share-based payments are charged to G&A

(5) The net change to Net Income is solely the change in the rate at which IFRS amortizes the value of stock option expense versus Canadian GAAP.

(in Canadian dollars)

### 18. Transition to IFRS (continued)

Reconciliation of consolidated Statement of Financial Position as previously reported under Canadian GAAP to IFRS:

| | | | | June 30, 2011 | | | July 1, 2010 |
|---|---|---|---|---|---|---|---|
| | Footnote | Canadian GAAP | Adjustment | IFRS | Canadian GAAP | Adjustment | IFRS |
| | | $ | $ | $ | $ | $ | $ |
| Assets | | | | | | | |
| Current assets | | | | | | | |
| Cash and cash equivalents | | 8,784,322 | - | 8,784,322 | 7,744,596 | - | 7,744,596 |
| Trade receivable | | 2,232,704 | - | 2,232,704 | 1,972,758 | - | 1,972,758 |
| Inventories | | 1,461,212 | - | 1,461,212 | 1,648,852 | - | 1,648,852 |
| Investment tax credits receivable | | 577,444 | - | 577,444 | 192,877 | - | 192,877 |
| Income taxes receivable | | 836,210 | - | 836,210 | 595,882 | - | 595,882 |
| Sales tax receivables | (2) | - | 50,465 | 50,465 | - | 21,414 | 21,414 |
| Other current assets | | 28,061 | - | 28,061 | 118,318 | - | 118,318 |
| | | 13,919,953 | 50,465 | 13,970,418 | 12,273,283 | 21,414 | 12,294,697 |
| Non-current assets | | | | | | | |
| Property, plant and equipment | (1) | 464,507 | (110,040) | 354,467 | 447,740 | (138,409) | 309,331 |
| Development costs | (1) | 1,983,665 | - | 1,983,665 | 2,158,221 | - | 2,158,221 |
| Intangible assets | | 2,063,922 | 110,040 | 2,173,962 | 3,787,638 | 138,409 | 3,926,047 |
| Goodwill | | 2,984,721 | - | 2,984,721 | 6,834,721 | - | 6,834,721 |
| | | 21,416,768 | 50,465 | 21,467,233 | 25,501,603 | 21,414 | 25,523,017 |
| Liabilities | | | | | | | |
| Current liabilities | | | | | | | |
| Accounts payable and accrued liabilities | (2) | 1,465,589 | 50,465 | 1,516,054 | 1,242,345 | 21,414 | 1,263,759 |
| Current portion of term loan | | 34,072 | - | 34,072 | 34,072 | - | 34,072 |
| Short-term obligation to issue shares | | - | - | - | 959,847 | - | 959,847 |
| Deferred revenue | | 60,864 | - | 60,864 | 76,688 | - | 76,688 |
| | | 1,560,525 | 50,465 | 1,610,990 | 2,312,952 | 21,414 | 2,334,366 |
| Non-current liabilities | | | | | | | |
| Term loan | | 51,107 | - | 51,107 | 85,179 | - | 85,179 |
| Deferred income tax liabilities | | 531,066 | - | 531,066 | 1,071,637 | - | 1,071,637 |
| | | 2,142,698 | 50,465 | 2,193,163 | 3,469,768 | 21,414 | 3,491,182 |
| Shareholders' equity | | | | | | | |
| Share capital | | 15,866,455 | - | 15,866,455 | 15,158,762 | - | 15,158,762 |
| Contributed surplus | (3) | 754,852 | 149,616 | 904,468 | 554,043 | 56,987 | 611,030 |
| Retained earnings | (3) | 2,652,763 | (149,616) | 2,503,147 | 6,319,030 | (56,987) | 6,262,043 |
| | | 19,274,070 | - | 19,274,070 | 22,031,835 | - | 22,031,835 |
| | | 21,416,768 | 50,465 | 21,467,233 | 25,501,603 | 21,414 | 25,523,017 |

**18. Transition to IFRS (continued)**

Reconciliation of consolidated Statement of Financial Position as previously reported under Canadian GAAP to IFRS (continued):

(1) The carrying value of $138,409 and $110,040 for website cost on July 1, 2010 and June 30, 2011, respectively, have been reclassified from property, plant and equipment to intangible assets to correct for a classification error under Canadian GAAP and IFRS.

(2) Sales tax receivable of $21,414 and $50,465 on July 1, 2010 and June 30, 2011, respectively, have been reclassified from accounts payable and accrued liability to sales tax receivables as a correction of classification error under Canadian GAAP and IFRS.

(3) The changes in contributed surplus and retained earnings are related to the IFRS 2 adjustment on transition to IFRS as explained in Note 18.

**19. Post-reporting date events**

No adjusting or significant non-adjusting events have occurred between the reporting date and the date of authorization.

**20. Authorization of financial statements**

The consolidated financial statements for the period ended June 30, 2012 (including comparatives) were, as per recommendation of the audit committee, approved by the board of directors on October 10, 2012.