

Consolidated financial statements of

**Uniserve Communications
Corporation**

May 31, 2009

Uniserve Communications Corporation

May 31, 2009

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Auditors' report

To the Shareholders of
Uniserve Communications Corporation

We have audited the consolidated balance sheets of Uniserve Communications Corporation as at May 31, 2009 and 2008 and the consolidated statements of operations, comprehensive loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at May 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants
September 25, 2009

Uniserve Communications Corporation

Consolidated statement of operations, comprehensive loss and deficit

Year ended May 31, 2009

	2009	2008
	\$	\$
		As restated *
Revenues	18,637,624	23,188,579
Cost of sales	9,594,476	11,273,394
Gross margin	9,043,148	11,915,185
Expenses		
Operations and service delivery costs	8,962,754	12,050,126
Amortization of property and equipment (Note 5)	834,015	796,734
Amortization of intangible assets (Note 6)	554,725	905,098
Sales and marketing	270,470	690,142
Stock-based compensation (Note 12(d))	3,969	-
	10,625,933	14,442,100
Operating loss	(1,582,785)	(2,526,915)
Other (expense) income		
Interest and bank charges	(1,381,965)	(1,347,789)
Foreign exchange (loss)/gain	(1,289,519)	891,605
Write-down of goodwill and intangible assets (Notes 6, 7)	(411,146)	(1,017,572)
Write-down of capital assets (Note 5)	(41,318)	-
Loss on settlement of long-term debt (Note 10)	-	(149,057)
Accretion to face value of preferred shares (Note 11)	(237,212)	(306,787)
	(3,361,160)	(1,929,600)
Loss before income taxes from continuing operations	(4,943,945)	(4,456,515)
Income tax recovery (expense) (Note 16)		
Current	369,358	(362,985)
Future	64,341	409,494
	433,699	46,509
Net loss and comprehensive loss for the year		
from continuing operations	(4,510,246)	(4,410,006)
Results from discontinued operations (Note 4)	4,418,501	(1,893,203)
Net loss and comprehensive loss for the year	(91,745)	(6,303,209)
Deficit, beginning of year	(19,415,040)	(13,111,831)
Deficit, end of year	(19,506,785)	(19,415,040)
Basic earnings per share		
Basic loss per share from continuing operations	(0.183)	(0.191)
Basic loss per share	(0.004)	(0.273)
Weighted average number of common shares outstanding		
- basic and diluted	24,609,495	23,076,663

* See Note 2(t)(v)

Uniserve Communications Corporation

Consolidated balance sheet

As at May 31, 2009

	2009	2008
	\$	\$
		As restated *
Assets		
Current assets		
Cash	196,651	102,222
Accounts receivable	764,118	1,040,509
Inventory	204,337	274,202
Prepaid expenses	33,902	96,776
Amounts held in escrow (Notes 4, 19)	2,729,250	-
Future income tax asset (Note 16)	16,474	-
Current assets of discontinued operations (Note 4)	-	2,589,967
	3,944,732	4,103,676
Future income tax asset (Note 16)	237,877	225,661
Property and equipment (Note 5)	1,594,854	2,152,137
Intangible and other assets (Note 6)	1,621,792	2,045,987
Goodwill (Note 7)	4,312,884	4,622,081
Non-current assets of discontinued operations (Note 4)	-	14,273,230
	11,712,139	27,422,772
Liabilities and shareholders' deficit		
Current liabilities		
Bank indebtedness (Note 9)	122,345	1,608,035
Accounts payable and accrued liabilities	7,464,587	6,186,698
Due to vendors of businesses acquired	-	168,637
Income taxes payable	-	369,358
Deferred revenue	996,628	1,339,757
Obligations under capital leases (Note 13)	37,611	-
Due to related parties (Note 8)	-	1,893,458
Current portion of future income tax liability (Note 16)	6,634	33,950
Current liabilities of discontinued operations (Note 4)	-	2,318,040
	8,627,805	13,917,933
Obligations under capital leases (Note 13)	18,442	-
Long-term debt (Note 10)	-	8,306,000
Future income tax liability (Note 16)	-	8,335
Convertible preferred shares (Note 11, 12(e))	3,245,441	3,008,229
Non-current liabilities of discontinued operations (Note 4)	-	2,274,048
	11,891,688	27,514,545
Shareholders' deficit		
Share capital (Note 12(a))	14,315,028	14,247,905
Other equity instruments (Note 12(e))	3,642,059	3,792,559
Contributed surplus (Note 12(a))	1,370,149	1,282,803
Deficit	(19,506,785)	(19,415,040)
	(179,549)	(91,773)
	11,712,139	27,422,772

Nature of operations and going concern (Note 1)

Commitments (Note 13)

Contingent liability (Note 19)

* See Note 2(t)(v)

Approved by the Directors

"William Spratt"
Director

"Maurice Lees"
Director

Uniserve Communications Corporation

Consolidated statement of cash flows

Year ended May 31, 2009

	2009	2008
	\$	\$
		As restated *
Operating activities		
Net loss for the year	(91,745)	(6,303,209)
Results of discontinued operations	4,418,501	(1,893,203)
Net loss for the year from continuing operations	(4,510,246)	(4,410,006)
Items not involving cash		
Amortization of property and equipment	834,015	796,734
Amortization of intangible assets	554,725	905,098
Purchase price re-allocation of intangible assets	-	140,000
Purchase price re-allocation of goodwill	-	(140,000)
Purchase price re-allocation of future income taxes	-	42,000
Write-down of goodwill and intangible assets	411,146	1,017,572
Write-down of property and equipment	41,318	-
Accretion of face value of preferred shares	237,212	306,787
Stock-based compensation	3,969	-
Unrealized loss on foreign exchange	60,859	72
Future income taxes	(64,341)	(409,494)
Loss on settlement of long-term debt	-	149,057
Changes in non-cash operating working capital (Note 18)	983,630	1,809,832
Net cash (used in) provided by continuing operating activities	(1,447,713)	207,652
Net cash used in discontinued operating activities	(542,887)	(1,387,621)
Net cash used in operating activities	(1,990,600)	(1,179,969)
Investing activities		
New product development	(867,658)	-
Purchase of property and equipment	(253,330)	(228,554)
Business disposition, net of cash	16,675,976	-
Due to vendors of businesses acquired	-	(500,381)
Net cash (used in) provided by continuing investing activities	15,554,988	(728,935)
Net cash used in discontinued investing activities	(259,707)	(3,663,449)
Net cash (used in) provided by investing activities	15,295,281	(4,392,384)
Financing activities		
Revolving line of credit	(1,410,000)	1,500,000
Repayment of short-term debt	(75,690)	(158,343)
Repayments to related parties	(1,893,458)	(320,487)
Repayment of long-term debt	(9,930,000)	-
Deferred finance costs incurred	-	(38,431)
Repayment of promissory notes	-	(3,000,000)
Advances from related parties	-	400,000
Net proceeds on issuance of preferred shares	-	1,120,000
Net proceeds on issuance of common shares	-	527,277
Net proceeds from common shares to be issued	-	70,000
Net cash (used in) provided by continuing financing activities	(13,309,148)	100,016
Net cash used in discontinued financing activities	-	(37,816)
Net cash (used in) provided by financing activities	(13,309,148)	62,200
Decrease in cash and cash equivalents	(4,467)	(5,510,153)
Cash, beginning of year	201,118	5,711,271
Cash, end of year	196,651	201,118
Cash related to:		
Continuing operations	196,651	102,222
Discontinued operations	-	98,896
	196,651	201,118

Supplemental cash flow information (Note 18)

* See Note 2(t)(v)

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

1. Nature of operations and going concern

Uniserve Communications Corporation ("the Company") was incorporated on January 19, 1988 under the Company Act of British Columbia. The Company's principal business activity is the provision of Internet access and related communications services primarily in British Columbia, Alberta, Ontario and Quebec which represents a single operating segment.

Our consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business. As at May 31, 2009, the Company has a working capital deficiency of \$4,683,073 (2008 - deficiency of \$9,814,257). For the year ended May 31, 2009, the Company had a negative cash flow from continuing operations, and incurred significant net losses due to interest expense, foreign exchange, amortization of customer lists and other intangible assets, accretion to face value of subordinated debt and preferred shares, and write-down of product development costs.

Liquidity risk is the risk that we will not be able to meet our financial obligations as they become due. Accordingly, the Company's ability to continue as a going concern, which means that it can realize its assets and discharge its liabilities in the normal course of business, is dependent in part upon the Company's ability to continue to generate sufficient cash flow from operations and to obtain additional equity or debt financing in the near term to continue to meet its obligations as they come due.

During the year conditions in the credit markets deteriorated substantially. These credit market conditions had a serious impact on the economy, which has contributed to a significant decline in the demand for and selling price of the products we sell. As a result of these conditions our share price has declined substantially. Current weak global economic conditions make access to the credit and capital markets difficult for us, which may compromise our ability to obtain suitable financing.

The Company may not generate sufficient funds from operations to meet all of its financial obligations and may need to generate funds from other sources to do so. To address our near term liquidity requirements, we have agreements with our key suppliers to provide us with additional time to generate cash and/or access appropriate sources of financing. There can be no assurance that these suppliers will continue to extend credit beyond their normal terms.

We have also taken a number of other steps to assist us in meeting our financial obligations, including deferring the payment of dividends on our Convertible Preferred Shares, Series A, reducing capital and discretionary spending, and significantly reducing the size of our workforce and selling Parasun. We are also pursuing other potential asset sales. There can be no assurance that we will be able to complete further sufficient asset sales on a timely basis.

Our ability to meet our financial obligations depends on a number of factors, some of which are beyond our control. These include general global economic, credit and capital market conditions, and the demand for and selling price of our products. There is no assurance that the expected cash flows from operations in combination with asset sales and other steps being taken will allow us to meet our obligations as they become due.

Our existing financial obligations will constrain our capital spending and that may have an adverse effect on our operations. Our debt levels will also limit our ability to expand our operations or make other investments that would enhance our competitiveness.

Accordingly, there is some risk that the steps described above will not be successful in allowing us to meet our obligations, which may require us to sell core assets or raise debt or equity capital, which management believes would enable us to satisfy our obligations as they fall due. However, these actions may have a material adverse effect on our business and on the market prices of our equity securities.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies

(a) *Basis of presentation*

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include the accounts of the Company and its wholly owned subsidiaries. Results from operations of Parasun are excluded from the date of disposition. All significant inter-company transactions and balances have been eliminated.

(b) *Use of estimates*

The preparation of the Company's consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the amount of revenues and expenses recognized during the reporting period. The most significant application of estimates is in the assessment of the underlying value of accounts receivable, the estimated useful lives and undiscounted net future cash flows attributed to equipment and software, intangible assets and goodwill for purposes of the purchase price allocation related to acquisitions and determining impairment, assumptions used in the determination of stock-based compensation, estimated future cash flows to support the going concern assumption, future income taxes and contingencies and commitments. Actual results could differ from those estimates and these differences could have a material impact on the consolidated financial statements.

(c) *Cash*

Cash represents cash on deposit less cheques issued in excess of funds on deposit.

(d) *Inventory*

Inventory consists of modems and pre-paid wireless phone cards for resale and various computer equipment. Inventory is valued at the lower of cost, on a first-in first-out basis, and net realizable value.

(e) *Property and equipment*

Property and equipment are recorded at cost less accumulated amortization. Amortization is provided on a declining-balance basis at the following annual rates designed to amortize the assets over their estimated useful lives, except leasehold improvements, where amortization is provided on a straight-line basis:

<u>Asset</u>	<u>Rate</u>
Online equipment	15%
Office equipment and signs	20%
Computer equipment	30%
Systems software	30%
Leasehold improvements	
- shorter of term of lease and estimated useful life	

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

(f) *Financing costs*

Costs directly identifiable with the raising of capital are charged against the related capital stock. Costs incurred to obtain debt financing are deferred and amortized by a charge to interest expense over the term of the related debt using the effective interest rate method.

(g) *Customer lists and intellectual property*

Acquired customer lists and intellectual property are amortized on a straight-line basis over periods ranging from three to eight years.

(h) *Research and development expenditures*

Research costs related to original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding are expensed as incurred.

Development costs are related to the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use. Development costs having a future benefit are recognized if and only if it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity and the cost of the asset can be measured reliably.

An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, the Company can demonstrate all of the following:

- (a) the technical feasibility of completing the intangible asset so that it will be available for use or sale.
- (b) its intention to complete the intangible asset and use or sell it.
- (c) its ability to use or sell the intangible asset.
- (d) how the intangible asset will generate probable future economic benefits. Among other things, the Company can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.
- (e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.
- (f) its ability to measure reliably the expenditure attributable to the intangible asset during its development.

The Company assesses the probability of expected future economic benefits using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset. Development costs representing intangible assets are initially measured at cost.

The Company reviews the amortization method and estimate of the useful life of an intangible asset at least annually.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

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

An intangible asset that is not subject to amortization should be tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test consists of a comparison of the fair value of the intangible asset with its carrying amount. When the carrying amount of the intangible asset exceeds its fair value, an impairment loss is recognized in an amount equal to the excess.

As at May 31, 2009, the Company had \$867,000 in development costs capitalized as a definite life intangible asset (2008 - \$nil).

(i) *Impairment of long-lived assets and intangible assets*

Long-lived assets, including property and equipment, and intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of an asset exceeds the fair value of the asset.

(j) *Goodwill*

Goodwill represents the excess cost over the value assigned to the net assets acquired in business combinations and is not amortized. The recorded amount of goodwill is tested for impairment annually by comparing the carrying value of the reporting unit to which the goodwill relates to the fair value of that reporting unit. Fair value is determined using discounted estimated future cash flows. If the carrying value of the reporting unit exceeds its fair value, goodwill is written down to its fair value.

(k) *Future income taxes*

The Company uses the asset and liability method of accounting for future income taxes. Under this method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the substantive enactment date. Future income tax assets are evaluated and if realization is not considered to be "more likely than not", a valuation allowance is provided.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

(l) Revenue recognition

Revenue derived from monthly internet access subscribers and internet access set-up charges is recognized on a monthly basis as services are provided. The Company bills its internet access subscribers in advance for direct access to the internet, but defers recognition of these revenues and recognizes them on a straight-line basis over the access period. Revenue from the sale of retail products, which to date have not been significant, is recognized when title passes upon product delivery. Revenue from consulting services is recognized when the services are performed. In software arrangements that include rights to multiple software products and/or services, the Company uses the residual method, under which revenues are allocated to the undelivered elements based on vendor specific objective evidence of fair value of the undelivered elements and that residual amount of revenues are allocated to the delivered elements. For those contracts that consist solely of licenses and maintenance, the Company recognizes net license revenues based upon the residual method after all licensed software product has been delivered. The Company recognizes maintenance revenues over the term of the maintenance contract. The maintenance rates for both license agreements with and without stated renewal rates are based upon the Company's price list.

The Company maintains relationships with telecommunication partners (including cable companies) in which it provides services to customers using the "last mile" element of the telecommunication providers' networks. The term "last mile" generally refers to the element of telecommunication networks that is directly connected to homes and businesses.

Generally, when the Company is the primary obligor in the transaction with the subscriber, has latitude in establishing prices, is the party determining the service specifications or has several but not all of these indicators, the Company records the revenue at the amount billed to the subscriber. If the Company is not the primary obligor and/or the telecommunications partner has latitude in establishing prices, the Company records revenue associated with the related subscribers on a net basis, netting the cost of revenue associated with the service against the gross amount billed to the customer and recording the net amount as revenue.

(m) Stock-based compensation

The Company accounts for all stock-based payments, including stock options granted, using the fair value based method. Under the fair value based method, stock-based compensation is measured at fair value of the instrument on the grant date and recognized over the vesting period as a charge to earnings with a corresponding increase in contributed surplus. Any consideration paid by the option holders to purchase shares is credited to share capital and the related stock-based compensation recognized is reclassified from contributed surplus to share capital.

(n) Investment tax credits and government grants

Investment tax credits and government grants related to current operating expenses are recorded as a reduction to these expenses in the period in which a reasonable estimate of the amount can be made, the Company elects to claim the amount, and collectibility is reasonably assured. Investment tax credits and government grants related to the acquisition of capital assets are deducted from the costs of the related capital assets, with any amortization calculated on the net amount.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

(o) *Earnings (loss) per share*

The Company calculates basic net earnings (loss) per share by dividing net earnings (loss) available to common shareholders for the period by the weighted average number of outstanding common shares. Diluted earnings (loss) per share is calculated using the treasury stock method, which takes into account the dilutive effects of outstanding stock options and warrants, if dilutive. A stock option or warrant is dilutive only when the average market price of common shares during the period exceeds the exercise price of the stock option or warrant. Convertible instruments are included in diluted earnings per share using the if-converted method which assumes that all convertible instruments are converted into common shares. As the effect of all share purchase warrants, options, and convertible securities is anti-dilutive, diluted net earnings (loss) per share is not different from basic net earnings (loss) per share for all periods presented.

(p) *Financial instruments*

Financial instruments are classified into one of the following five categories: held-for-trading (assets or liabilities), loans and receivables, held-to-maturity investments, available-for-sale investments, and other financial liabilities. Transaction costs are included in the initial carrying amount of financial instruments except for held-for-trading items in which case they are expensed as incurred. All financial instruments are initially measured at fair value. Measurement in subsequent periods depends on the classification of the financial instrument.

Held-for-trading (assets or liabilities)

This category is comprised of certain investments in equity and debt instruments, stand-alone derivatives, other than those designated as hedging items, and embedded derivatives requiring separation. They are carried in the balance sheet at fair value with changes in fair value recognized in the statements of operations.

Loans and receivables

These assets are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. They arise principally through the provision of goods and services to customers (accounts receivable), but also incorporate other types of contractual monetary assets. They are initially recognized at fair value and subsequently carried at amortized cost, using the effective interest method, less any provision for impairment.

Held-to-maturity investments

These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company's management has the positive intention and ability to hold to maturity and comprises certain investments in debt securities. These assets are initially recognized at fair value and subsequently carried at amortized cost, using the effective interest method, less any provision for impairment.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

(p) *Financial instruments (continued)*

Available-for-sale investments

Non-derivative financial assets not included in the above categories are classified as available-for-sale and comprise certain investments in equity instruments, including the Company's investments in private companies. When the financial instruments have a quoted market price in an active market, they are carried at fair value with changes in fair value recognized as a separate component of other comprehensive income. When they do not have a quoted market price in an active market, they are carried at cost. Where a decline in the fair value is determined to be other than temporary, the amount of the loss is removed from accumulated other comprehensive income and recognized in the statements of operations.

Other financial liabilities

Other financial liabilities includes all financial liabilities other than those classified as held-for-trading and comprise trade payables, other short-term monetary liabilities, and the debt element of convertible debt. These liabilities are initially recognized at fair value and subsequently carried at amortized cost using the effective interest method.

The Corporation's financial assets and liabilities are classified and measured as follows:

<i>Asset/Liability</i>	<i>Category</i>	<i>Measurement</i>
Cash	Held-for-trading	Fair value
Accounts receivable	Loans and receivables	Amortized cost
Amounts held in escrow	Loans and receivables	Amortized cost
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Bank indebtedness and notes payable	Other liabilities	Amortized cost
Obligations under capital leases	Other liabilities	Amortized cost
Long term debt	Other liabilities	Amortized cost

(q) *Leases*

Leases are classified as either capital or operating leases. A lease that transfers substantially all the benefits and risks incidental to the ownership of property is classified as a capital lease. All other leases are accounted for as operating leases wherein rental payments are expensed as incurred. At the inception of a capital lease, an asset and an obligation are recorded at an amount equal to the lesser of the present value of the future minimum lease payments or the property's fair value at the beginning of such lease.

(r) *Debt instruments*

Where the Company issues debt instruments with detachable warrants or conversion options in connection with the debt instrument, the estimated fair market value of the warrants and conversion feature are credited to shareholders' equity. The reduced liability component of the debt is accreted to face value by a charge to interest expense.

Prior to fiscal 2009, the Company had historically reclassified amounts from other equity to deficit on the expiry of warrants. During 2009, the Company changed its accounting policy for warrants where on expiry; the related amount on expiry would now be reclassified from other equity to contributed surplus. This change in policy results in a restatement from deficit to contributed surplus of \$66,500, for the year ended May 31, 2008 with no impact on the Company's financial position, cash flows or results of operations.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

(s) *Comprehensive loss*

Comprehensive loss includes all changes in equity except those resulting from investments by owners and distribution to shareholders. Other comprehensive income is defined by revenue, expenses, gains and losses that are recognized in comprehensive loss, but excluded from net loss.

(t) *Adoption of new accounting policies*

(i) *Capital - disclosures:*

On June 1, 2008, the Company adopted the requirements of the CICA Handbook Section 1535, Capital Disclosures, which establishes standards for disclosing information about an entity's capital and how it is managed. This standard requires disclosure of: an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital, and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance.

(ii) *Financial instruments - disclosures:*

Effective June 1, 2008, the Company adopted the requirements of the CICA Handbook Section 3862, Financial Instruments - Disclosures and Section 3863, Financial Instruments - Presentation, which supersedes Sections 3861, Financial Instruments - Presentations and Disclosures. Section 3862 places an increased emphasis on disclosures about the risks associated with both recognized and unrecognized financial instruments and how these risks are managed. Section 3862 requires disclosures, by class of financial instrument that enables users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. In addition, disclosure is required of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable.

(iii) *Financial instruments - presentation:*

Effective June 1, 2008, the Company adopted the requirements of the CICA Handbook Section 3863, Financial Instruments - Presentation, which replaces Section 3861, Financial Instruments - Disclosure and Presentation. The existing requirements on presentation of financial instruments have been carried forward unchanged to Section 3863, Financial Instruments - Presentation.

(iv) *General Standards of Financial Statements - presentation:*

Effective July 1, 2008, the Company adopted the additional requirements of the CICA Handbook Section 1400, "General Standards of Financial Statements". The additional requirements require management to make an assessment of the Company's ability to continue as a going concern, and to disclose any material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

2. Significant accounting policies (continued)

(t) *Adoption of new accounting policies (continued)*

(v) *Goodwill and Intangible Assets:*

In February 2008, the CICA issued Handbook Section 3064 ("CICA 3064"), "Goodwill and Intangible Assets". CICA 3064 replaces Section 3062 "Goodwill and Intangible Assets", and Section 3450, "Research and Development Costs". It establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. The new Section also provides guidance for the treatment of preproduction and start-up costs and requires that these costs be expensed as incurred. This new standard is effective for the Company's interim and annual consolidated financial statements commencing June 1, 2008 and are to be adopted on a retrospective basis. The impact of adopting this accounting standard, on a retrospective basis, is an increase of \$1,100,893 in the net loss for fiscal 2008 and a decrease of \$1,059,964 in shareholders' equity at May 31, 2007, and a decrease in intangible and other assets of \$2,160,857 as at May 31, 2008. This change resulted in the net loss and comprehensive loss per share being \$0.04 and \$0.05 lower for fiscal 2008 and 2007 respectively.

3. Recent accounting pronouncements

(i) *Financial Statement Concepts:*

In February 2007, the CICA issued Handbook Section 1000, "Financial Statement Concepts". This Section will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt this new standard for its fiscal year beginning June 1, 2009. Section 1000 on financial statements concepts removes references to recognition of assets and liabilities solely on the basis of matching of net income items and clarifies timing of expense recognition and the creation of an asset. The Corporation is currently evaluating the impact of the adoption of this new Section on the financial statements.

(ii) *International Financial Reporting Standards ("IFRS"):*

In February 2008, the Canadian Accounting Standards Board ("AcSB") of the CICA affirmed its intention to replace Canadian GAAP with IFRS. The changeover date from Canadian GAAP to IFRS is for annual and interim financial statements relating to fiscal years beginning on or after January 1, 2011. Accordingly, the new standard will apply to the Company effective for the year commencing June 1, 2011. While the Company has started to assess the adoption of IFRS for 2011, the impact to the balance sheet and ongoing results of operations resulting from the transition to IFRS cannot be reasonably estimated at this time.

4. Discontinued operations

On October 7, 2008, the Company completed the sale of its wholly owned subsidiary, Parasun to IBBS, for cash consideration of US\$20,000,000 in exchange for all of the issued and outstanding shares of Parasun. Of the purchase price, US\$2,500,000 (CDN\$2,729,250 as at May 31, 2009) is to be held in escrow for a period of 1 year to satisfy any indemnification claims for any deficiencies in the representations and warranties and for any taxes owing up to the date of sale, see note 19.

In conjunction with the sale, the subordinated debt of US\$10,000,000 including an early payment fee of US\$400,000 plus the accrued interest was repaid, see note 11. Amounts due to related parties totaling \$1,893,458 and the revolving line of credit balance of \$1,500,000 were also repaid, see notes 8 & 9.

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May 31, 2009 and 2008

4. Discontinued operations (continued)

The following is a summary of the consideration received and the book value of the assets and liabilities of Parasun. The sale resulted in a gain on disposition of \$7,373,356 before income taxes. The Company has sufficient tax losses available to fully offset this gain; therefore no income tax expense has been recorded for the sale transaction.

	May 31, 2009 USD	May 31, 2009 CDN
	\$	\$
Consideration received		
Cash	17,500,000	19,533,500
Amounts held in escrow	2,500,000	2,790,500
Management contract termination fee	500,000	558,100
Purchase price adjustment	(350,000)	(390,670)
Working capital deficiency	(254,434)	(284,000)
Transaction costs		(997,756)
		<u>21,209,674</u>
Assets		
Cash		505,547
Non-cash current assets		2,777,262
Equipment		1,132,755
Other assets		46,780
Intellectual property		3,027,688
Customer list		4,238,763
Goodwill		5,597,810
		<u>17,326,605</u>
Liabilities		
Accounts payable and accrued liabilities		1,488,957
Deferred revenue		99,820
Due to former shareholders		440,652
Future tax liability		1,460,858
		<u>3,490,287</u>
Net book value		<u>13,836,318</u>
Gain on disposition		<u>7,373,356</u>

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4. Discontinued operations (continued)

For the years ended May 31, 2009 and 2008, the financial results associated with the discontinued operations of Parasun were as follows:

	2009	2008
	\$	\$
Revenues	3,485,106	10,381,894
Gross margin	2,474,913	7,798,371
Expenses	3,330,222	8,288,385
Operating loss	(855,309)	(490,014)
Other expense	(2,646,667)	(2,122,507)
Gain on disposition	7,373,356	-
Profit (loss) before income taxes	3,871,380	(2,612,521)
Income tax recovery	547,121	719,318
Net profit (loss) and comprehensive profit (loss) for the period	4,418,501	(1,893,203)

	2009	2008
	\$	\$
Current assets	-	2,589,967
Non-current assets	-	14,273,230
Current liabilities	-	2,318,040
Non-current liabilities	-	2,274,048

5. Property and equipment

	2009			
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$	\$	\$
Equipment	8,778,090	7,457,150	41,318	1,279,622
Software	775,965	482,917	-	293,048
Leasehold improvements	342,478	320,294	-	22,184
	9,896,533	8,260,361	41,318	1,594,854

	2008			
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$	\$	\$
Equipment	8,617,712	6,863,752	-	1,753,960
Software	628,097	391,015	-	237,082
Leasehold improvements	341,041	179,946	-	161,095
	9,586,850	7,434,713	-	2,152,137

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5. Property and equipment (continued)

The cost of property under capital leases, equipment and software aggregated \$56,053 as at May 31, 2009 (2008 - \$nil). Amortization charged to continuing operations, which includes amortization associated with property under capital leases, was \$834,015 and \$796,734 for the years ended May 31, 2009 and 2008, respectively.

6. Intangible and other assets

				2009
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$	\$	\$
Customer lists	15,971,161	15,135,879	101,949	733,333
Intellectual property	520,000	520,000	-	-
Deferred finance costs	424,139	403,338	-	20,801
Product development costs	867,658	-	-	867,658
	17,782,958	16,059,217	101,949	1,621,792

				2008
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$	\$	\$
Customer lists	15,971,161	14,185,287	395,866	1,390,008
Intellectual property	520,000	52,000	468,000	-
Deferred finance costs	1,258,705	602,726	-	655,979
	17,749,866	14,840,013	863,866	2,045,987

During the year ended May 31, 2009 product development costs of \$867,658 related to Kinzin, a social networking site being developed by the Company, were capitalized.

During the year ended May 31, 2009 UPS's customer lists were written-down by \$101,949 to nil.

During the year ended May 31, 2008 customer lists and intellectual property were written-down by \$395,866 and \$468,000 respectively to reflect impairment in the carrying values of the intangible assets of KBT.

Uniserve Communications Corporation

Notes to consolidated financial statements

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7. Goodwill

	Discontinued Operations	Continuing Operations
	\$	\$
Balance, May 31, 2006	-	4,312,884
Acquisition of Parasun	5,112,244	-
Acquisition of KBT	-	364,903
Balance, May 31, 2007	5,112,244	4,677,787
Purchase price reallocation - Parasun	485,566	-
Purchase price reallocation - KBT	-	98,000
Write-down - KBT	-	(153,706)
Balance, May 31, 2008	5,597,810	4,622,081
Disposition of Parasun	(5,597,810)	-
Write-down - KBT	-	(309,197)
Balance, May 31, 2009	-	4,312,884

In the current year, there was an additional written-down of \$309,197 in the carrying value of KBT's goodwill.

8. Related party transactions

	2009	2008
	\$	\$
\$1,000,000 loan payable to a director and shareholder of the Company, payable on demand, bearing interest at 15% per annum payable monthly, secured by a general security agreement granting first charge subject to permitted encumbrances over all assets of the Company (notes 8(a), 8(b), 8(c))	-	912,055
\$650,000 loan payable to a director and shareholder of the Company, payable on demand, bearing interest at 18% per annum payable monthly, secured by a general security agreement granting first charge subject to permitted encumbrances over all assets of the Company (note 8(b))	-	581,403
\$400,000 loan payable to a company controlled by a director and shareholder of the Company, payable on demand, bearing interest at 18% per annum payable monthly, secured by a general security agreement granting first charge subject to permitted encumbrances over all assets of the Company (note 8(b))	-	400,000
	-	1,893,458

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Notes to consolidated financial statements

May 31, 2009 and 2008

8. Related party transactions (continued)

- (a) The Company was charged \$100,000 in loan extension fees in the year ended May 31, 2008. These fees were outstanding as at May 31, 2008 and were included in accounts payable and accrued liabilities.
- (b) As at May 31, 2008 accumulated interest in arrears of \$141,603, \$113,520, and \$18,345 was included in accounts payable and accrued liabilities for the \$1,000,000, \$650,000 and \$400,000 loans respectively.

On October 7, 2008, the \$1,000,000, the \$650,000 and the \$400,000 loans plus accrued interest amounts of \$190,493, \$151,141, \$43,938 respectively, were paid in conjunction with the sale of Parasun to IBBS, see note 4.

- (c) During the year ended May 31, 2007, the Company incurred costs associated with issuing 350,000 share purchase warrants to a director and shareholder for the extension of the expiry date of the \$1,000,000 loan. Each warrant entitled the holder to purchase one common share at an exercise price of \$0.40; the fair value of these warrants was \$66,500. These warrants expired on March 9, 2008, and the previously recorded warrant value was charged to contributed surplus.
- (d) One of the Company's subsidiaries entered into a lease agreement, commencing June 1, 2008 with a private company controlled by a director and shareholder, see note 13(b).

Related party transactions are in the normal course of operations and are recorded at amounts established and agreed between the related parties.

9. Bank indebtedness and notes payable

	2009	2008
	\$	\$
Revolving credit facility bearing interest at prime plus 2%, secured by a general security agreement constituting a first ranking security interest in all assets of the Company	-	1,410,000
Bank demand loan bearing interest at prime plus 3% repayable in monthly blended payments of \$6,250; secured by a general security agreement over assets of KBT	122,345	198,035
	122,345	1,608,035

On October 7, 2008, the revolving credit facility was repaid in conjunction with the sale of the Company's wholly owned subsidiary, Parasun, see note 4.

The repayment of the \$3,000,000 promissory note on July 23, 2007 resulted in a loss of \$149,057 which was charged to the statement of operations in the year ended May 31, 2008.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

10. Long-term debt

	2009	2008
	\$	\$
Subordinated debt, US\$10,000,000 bearing interest at 12% per annum, maturing November 24, 2012, net of unamortized discount of \$1,765,882 (2008 - \$1,624,00) (note 12(e)(ii)), interest-only payments to May 2009, with the loan repayable thereafter at US\$62,500 per month with the balance at maturity	-	8,306,000
	-	8,306,000

Commencing December 2007, the Company agreed to pay US\$50,000 per month for a six month period as part of a temporary relaxation of the financial covenants with the holder of the subordinated debt. As of June 1, 2008 the interest rate on the subordinated debt increased to 18% as the Company was not able to meet the financial covenants of the subordinated debt. On October 7, 2008, the subordinated debt was repaid in conjunction with the sale of the Company's wholly owned subsidiary, Parasun, see note 4. The repayment of the subordinated debt resulted in a loss of \$1,482,118 which has been charged to discontinued operations on the statement of operations.

11. Convertible preferred shares

	2009	2008
	\$	\$
Series A Convertible Preferred Shares, \$4,285,000 redeemable at the option of the holder on or after May 24, 2014, 8% cumulative dividends, net of unamortized discount of \$1,039,559 (2008 - \$1,276,772) (Note 12(a)(iii))	3,245,441	3,008,229
	3,245,441	3,008,229

The Convertible Preferred Shares, Series A are convertible to common shares at \$0.75 in year one, \$0.80 in year two, \$0.90 in year three, \$1.05 in year four and \$1.25 in year five and carry a cumulative dividend rate of 8%. The Company can, at its option, force conversion, if, at any time during the term, the common shares of the Company trade at 200% of the conversion price then in effect for a period of 30 days. The preferred shares are redeemable at the option of the holder on or after the fifth anniversary of the date of issue. As the Company may be required to redeem the preferred shares for cash, they have been classified as long-term debt with the value of the conversion right included in other equity instruments.

On issue the amount allocated to long-term liability was \$2,701,441 and \$1,583,559 was allocated to the conversion right, see Notes 12(a)(iii) and 12(e). The carrying value of the amount allocated to long-term liability is being accreted to the face value of the preferred shares over a five year period.

As at May 31, 2009 the dividends on the Series A Convertible Preferred Shares are in arrears in the amount of \$485,633 (May 31, 2008 - \$142,833) and are included in accounts payable and accrued liabilities.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

12. Share capital

(a) *Authorized and issued and contributed surplus*

The authorized share capital of the Company consists of an unlimited number of common shares and an unlimited number of Convertible Preferred Shares. As at May 31, 2009, 428,500 (2008 – 428,500) Preferred Shares, Series A are outstanding.

Common no par value shares outstanding are as follows:

	Number of shares	Share Capital Amount	Contributed Surplus
		\$	\$
Balance, May 31, 2007	22,924,367	13,742,296	1,124,635
Private placement (i)	1,506,498	505,609	21,668
Private placement (i)	-	-	70,000
Expiry of warrants	-	-	66,500
Balance, May 31, 2008	24,430,865	14,247,905	1,282,803
Private placement (i)	200,000	67,123	(67,123)
Expiry of warrants	-	-	150,500
Stock-based compensation expense	-	-	3,969
Balance, May 31, 2009	24,630,865	14,315,028	1,370,149

- (i) On April 24, 2008, the Company issued 1,506,498 units via a private placement. Each unit consisted of one common share at \$0.35 and one half share purchase warrant for total proceeds of \$527,277. Warrants are exercisable until April 24, 2010 at an exercise price of \$0.45. On issue the amount allocated to share capital was \$505,609 and \$21,668 was allocated to the warrant. The value assigned to the warrants of \$0.0288 per share was determined using the Black Scholes option pricing formula with the following assumptions: risk free interest rate – 3.25%; annual dividends – nil; expected life – 23 months; expected stock price volatility – 40%.

As at May 31, 2008, the Company had received \$70,000 for an additional 200,000 units which were issued in June 2008. On issue the amount allocated to share capital was \$67,123 and \$2,877 was allocated to the warrant.

- (ii) On March 24, 2007, the Company issued 830,000 units via a private placement. Each unit consisted of one common share at \$0.50 and one half share purchase warrant. The warrants were exercisable until October 18, 2008 at an exercise price of \$0.75 and expired during the year. The value assigned to the warrants of \$0.34 per share was determined using the Black Scholes option pricing formula with the following assumptions: risk free interest rate – 3.25%; annual dividends – nil; expected life 19 months; expected stock volatility – 120%.
- (iii) As the Company may be required to redeem the preferred shares for cash, they have been classified as long-term liabilities, see Note 11, with the par value of the conversion right included in other equity instruments, see Note 12(e). On issue the amount allocated to long-term liabilities was \$3,008,229 and \$1,276,772 was allocated to the conversion right. The carrying value of the amount allocated to long-term liabilities is being accreted to the face value of the preferred shares over a five year period.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

12. Share capital (continued)

(b) *Escrow*

As at May 31, 2009, 192,624 (2008 - 192,624) shares are held in trust and are subject to arbitration proceedings.

(c) *Share purchase warrants*

The following share purchase warrants were outstanding as of May 31, 2009:

<u>Issue date</u>	<u>Expiry date</u>	<u>Number of warrants</u>	<u>Exercise price</u>
			\$
May 24, 2007	May 24, 2012	3,500,000	0.70
April 24, 2008	April 24, 2010	853,251	0.45
		<u>4,353,251</u>	

(d) *Share purchase options*

Pursuant to the policies of the TSX Venture Exchange, the Company may grant incentive stock options to its officers, directors and employees. TSX Venture Exchange policies permit the Company's directors to grant incentive stock options of the purchase of shares of the Company to persons in consideration for services. Stock options must be non-transferable and the aggregate number of shares that may be reserved for issuance pursuant to stock options may not exceed 10% of the issued shares of the Company at the time of granting and may not exceed 5% to any individual. The exercise price of stock options and vesting period is determined by the Board of Directors of the Company at the time of grant and may not be less than the average closing price of the Company's shares on the ten trading days immediately preceding the day on which the option is granted and publicly announced. Options have a maximum term of five years and terminate 30 days following the termination of the optionee's employment, except in the case of retirement, death, or disability, in which case they terminate one year after the event.

During the year ended May 31, 2007, 2,275,000 stock options were granted. These options were granted at an exercise price of \$0.50 or \$0.65 and expire five years from the date of grant. The vesting periods ranged from vesting immediately to vesting over a 3 year period. The weighted average fair value of the options granted during the year ended May 31, 2007 was \$0.34. Stock-based compensation was measured using the Black Scholes option pricing formula with the following weighted average assumptions: risk free interest rate 3.97%, annual dividend rate nil; expected stock-price volatility 120%; expected life of options 5 years.

During the years ended May 31, 2008 and 2009, no stock options were granted. For the year ended May 31, 2009, the Company recognized stock-based compensation related to stock options of \$3,969 (2008 - \$nil).

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Notes to consolidated financial statements

May 31, 2009 and 2008

12. Share capital (continued)

(d) Share purchase options (continued)

Stock option activity is summarized as follows:

	Shares available for grant	Options outstanding	
		Number of optioned common shares	Weighted average exercise price
			\$
Balance, May 31, 2007	17,437	2,275,000	0.51
Options forfeited	482,500	(482,500)	0.50
Additional shares available for grant	150,650	-	-
Balance, May 31, 2008	650,587	1,792,500	0.51
Options forfeited	755,000	(755,000)	0.53
Additional shares available for grant	20,000	-	-
Balance, May 31, 2009	1,425,587	1,037,500	0.50

The following table summarizes information about stock options outstanding and exercisable as at May 31, 2009:

Exercise price	Options outstanding		Options exercisable	
	Number of common shares issuable	Remaining contractual life (years)	Number of common shares issuable	Remaining contractual life (years)
\$0.50	1,037,500	2.44	975,833	2.44

(e) Other equity instruments

	2009	2008
	\$	\$
Conversion rights on Series A preferred shares (Notes 11, 12(a)(iii))	1,583,559	1,583,559
Warrants (i)	-	150,500
Warrants (ii)	2,030,000	2,030,000
Warrants (iii)	28,500	28,500
	3,642,059	3,792,559

- (i) On May 24, 2007, as part of the \$3,000,000 promissory note payable, the Company issued 350,000 warrants. On issue, the Company allocated \$150,500 of the proceeds received to the warrants issued based on their fair value with the remaining amounts allocated to the promissory note payable. These warrants expired on May 24, 2009, and the previously record warrant value was charged to contributed surplus.

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Notes to consolidated financial statements

May 31, 2009 and 2008

12. Share capital (continued)

(e) *Other equity instruments (continued)*

- (ii) During the year ended May 31, 2007 as part of the US\$10,000,000 subordinated debt financing arrangements described in Note 10, the Company issued a total of 3,500,000 warrants. On issue, the Company allocated \$2,030,000 of the proceeds received to the warrants issued based on their fair value with the remaining amounts allocated to the subordinated debt. During the year the subordinated debt was repaid in conjunction with the sale of Parasun, see note 4.
- (iii) During the year ended May 31, 2007, in consideration for the issue of certain interim financing, the Company issued warrants with a fair value of \$28,500.

13. Commitments

- (a) The Company has obligations under long-term contracts with suppliers of communication services relating to the internet services businesses. The contracts have minimum monthly base charges and pre-determined penalties of terminated costs. Minimum payments under these contracts are as follows:

	\$
2010	32,100
	<u>32,100</u>

- (b) The Company leases office space and equipment under non-cancelable operating leases expiring in various years through 2017 and also leases computer hardware and software under non-cancelable capital leases. Minimum commitments under non-cancelable leases as at May 31, 2009 are as follows:

	Capital leases	Operating leases
	\$	\$
2010	42,184	321,800
2011	11,051	180,556
2012	10,839	137,500
2013	-	160,417
<u>2014 and beyond</u>	<u>-</u>	<u>501,042</u>
Total minimum lease payments	64,074	<u>1,301,315</u>
<u>Less: amount representing interest</u>	<u>8,021</u>	
Present value of future lease payments	56,053	
<u>Less: current portion</u>	<u>37,611</u>	
<u>Long-term portion of capital lease obligation</u>	<u>18,442</u>	

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Notes to consolidated financial statements

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14. Capital disclosures

The Company defines its capital as follows:

- (i) Shareholders' deficit;
- (ii) Convertible preferred shares.

The amounts included in the Company's capital are as follows:

	2009	2008
	\$	\$
Shareholders' deficit	(179,549)	(91,773)
Convertible preferred shares	3,245,441	3,008,229
	3,065,892	2,916,456

The Company's financial strategy is designed and formulated to maintain a flexible capital structure to allow the Company the ability to respond to changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust its capital structure, the Company may issue additional debt or issue debt to replace existing debt with similar or different characteristics. The Company's financing and refinancing decisions are made on a specific transaction basis and depend on such things as the Company's needs, and market and economic conditions at the time of the transaction. There were no changes in the Company's approach to capital management during the period.

15. Financial instruments

The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies, as disclosed below. However, considerable judgment can be required to develop certain of these estimates. Accordingly, these estimated values are not necessarily indicative of the amounts the Company could realize in a current market exchange. The estimated fair value amounts can be materially affected by the use of different assumptions or methodologies.

The methods and assumptions used to estimate the fair value of each class of financial instruments are discussed below. Fair value is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value is determined by reference to quoted bid or ask prices, as appropriate, in the most advantageous active market for that instrument to which the Company has immediate access. When bid and ask prices are unavailable, the Company uses the closing price of the most recent transaction of that instrument. In the absence of an active market, the Company would determine fair value based on internal or external valuation models, such as option-pricing models, and discounted cash flow analysis, using observable market-based inputs.

Uniserve Communications Corporation

Notes to consolidated financial statements

May 31, 2009 and 2008

15. Financial Instruments (continued)

(i) Credit risk

Financial instruments that potentially subject the Company to a significant concentration of credit risk consist primarily of cash and accounts receivable. The Company limits its exposure to credit loss by placing its cash with high credit quality financial institutions. Concentration of credit risk, with respect to accounts receivable is considered to be limited due to the credit quality of the customers comprising the Company's customer base. The Company performs ongoing credit evaluations of its customers' financial condition to determine the need for an allowance for doubtful accounts. The Company has not experienced significant credit losses to date. The maximum amount of credit risk exposure is limited to the carrying amounts of these balances in the consolidated financial statements.

As at May 31, 2009, a balance from one customer (2008 - one) made up 22.1% (2008 - 18.2%) of total accounts receivable.

The following table sets forth details of the aged receivables as well as the related allowance for the doubtful accounts:

	2009	2008
	\$	\$
Current	475,664	525,302
30-60 days past billing date	123,682	226,957
61-90 days past billing date	56,457	119,935
Greater than 90 days past billing date	381,370	571,019
Total accounts receivable	1,037,173	1,443,213
Less: allowance for doubtful accounts	(273,055)	(402,704)
	764,118	1,040,509

Allowance for doubtful accounts

Changes in the allowance for doubtful accounts are as follows:

	2009	2008
	\$	\$
Balance, beginning of year	402,704	219,015
Provision for doubtful accounts	233,849	536,894
Bad debts written off, net of recoveries, and other	(363,498)	(353,205)
Balance, end of year	273,055	402,704

The provision for doubtful accounts has been included in operating expenses in the consolidated statements of operations, comprehensive loss and deficit, and is net of any recoveries that were provided for in a prior period.

(ii) Interest rate risk

The Company does not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates as the interest rates that we pay are fixed.

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Notes to consolidated financial statements

May 31, 2009 and 2008

15. Financial instruments (continued)

(iii) Currency risk

The Company has customers and suppliers that transact in currencies other than the Canadian dollar which gives rise to a risk that earnings and cash flows may be adversely affected by fluctuations in foreign currency exchange rates. The U.S. Dollar is the only other foreign currency to which the Company has exposure. The Company currently does not use financial instruments to hedge these risks.

The Company holds balances in foreign currencies that give rise to exposure to foreign exchange risk. Sensitivity to a +/- 10% movement in US currency versus the Canadian dollar would affect the Company's loss and other comprehensive loss by \$234,000.

Balances denominated in foreign currencies that are considered financial instruments are as follows:

As of May 31, 2009	CDN Total	US
FX rates used to translate to CDN		1.0917
	\$	\$
Financial assets		
Cash	196,651	16,352
Accounts receivable	764,118	1,527
Amounts held in escrow	2,729,250	2,729,250
	3,690,019	2,747,129
Financial liabilities		
Accounts payable and accrued liabilities	7,464,587	409,530
	7,464,587	409,530

(iv) Liquidity risk exposure

Liquidity risk arises from our general and capital funding needs. Further discussion on liquidity risk is included in Note 1.

(v) Fair values

The carrying amounts of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, bank indebtedness and notes payable approximate their fair values because of the short-term to maturity of these instruments. The carrying amount of the bank loan approximate its fair value as the debt bears interest at rates which approximates market rates.

The Company has determined that the fair value of the Convertible Preferred Shares, Series A is less than the carrying value given the current market conditions. The carrying value and fair value for the Convertible Preferred Shares are as follows:

As at May 31, 2009	Carrying value	Fair Value
Convertible preferred shares (Note 11)	3,245,441	2,759,808

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May 31, 2009 and 2008

16. Income taxes

Income tax recovery (expense) differs from the amount that would be computed by applying the combined Canadian Federal and provincial statutory income tax rates of 30.0% (2008 – 31.5%) to income before income taxes. The reasons for the differences are as follows:

	2009	2008
	\$	\$
Computed tax recovery (expense)	1,483,184	1,403,802
Tax effect of:		
Tax losses not previously recognized	3,782,354	-
Change in tax rates	(188,015)	(759,927)
Change in valuation allowance	(3,694,991)	(242,898)
Expired non-capital losses	(723,163)	-
Non-deductible items and other	(225,670)	(354,468)
	(1,049,485)	(1,357,293)
	433,699	46,509

The tax effects of temporary differences that give rise to significant portions of the future tax assets and future tax liabilities at May 31, 2009 are presented below:

	2009	2008
	\$	\$
Future tax assets		
Loss carry forwards	3,726,763	1,195,362
Difference between book and tax value of software and equipment	203,359	514,339
Difference between book value and tax value of intangible assets and other assets	797,026	1,052,083
Investment tax credits	1,437,290	-
	6,164,438	2,761,784
Valuation allowance	(5,693,420)	(1,998,429)
	471,018	763,355
Future tax liability		
Difference between book value and tax value of intangible and other assets	(223,301)	(579,979)
Investment tax credits	-	-
	(223,301)	(579,979)
Net future asset	247,717	183,376

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16. Income taxes (continued)

The net future tax asset is presented on the balance sheet as follows:

	2009	2008
	\$	\$
Current future tax asset	16,474	-
Long-term future tax asset	237,877	225,661
Current future tax liability	(6,634)	(33,950)
Long-term future tax liability	-	(8,335)
	247,717	183,376

In determining the valuation allowance, management considers whether it is more likely than not that some portion of all of the future tax assets will not be realized. The ultimate realization of future tax assets is dependent on the generation of future income during the periods in which those temporary differences become deductible. As at May 31, 2009, the Company has non-capital loss carry forwards in Canada aggregating approximately \$14,875,667 available to reduce taxable income otherwise calculated in future years. These losses will expire as follows:

	\$
2010	2,182,975
2014	2,265,731
2015	3,591,885
2026	858,424
2027	843,273
2028	3,547,277
2029	1,586,102
	14,875,667

17. Business segment information

The Company carries on business in Internet access and related communications services industry and all sales are made in this segment. Substantially all of the Company's revenues from continuing operations were generated in Canada and substantially all of the Company's revenues from discontinued operations were generated in the United States. Substantially all of the long-lived assets including property and equipment and intangible assets are located in Canada.

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18. Statements of cash flows

(i) Changes in non-cash balance related to operations are as follows:

	2009	2008
	\$	\$
Accounts receivable	276,391	257,920
Inventory	69,865	81,203
Prepaid expenses	62,874	(31,071)
Accounts payable and accrued liabilities	1,277,889	2,009,193
Deferred revenue	(343,129)	(385,503)
Income taxes payable	(369,358)	(102,013)
Effect of foreign exchange rate changes on cash	9,098	(19,897)
	983,630	1,809,832

(ii) Supplemental information:

	2009	2008
	\$	\$
Interest paid	525,128	380,252
Non-cash financing and investing transactions		
Obligations under capital leases	56,053	-
Expiration of warrants	150,500	66,500

19. Contingent liability

As a result of the sale of Parasun there is a total of US\$2,500,000 (CDN\$2,729,250 as at May 31, 2009) to be held in escrow for a period of 1 year to satisfy any indemnification claims for any deficiencies in the representations and warranties and for any taxes owing up to the date of sale, see note 4. As at May 31, 2009 the Company has estimated the contingent liability to be US\$350,000 (CDN\$390,760 as at May 31, 2009) and has recorded this amount in the statement of operations. In the event that the amounts held in escrow are not sufficient to cover all claims, the Company would be potentially liable for amounts in excess of the funds held in escrow.