

Consolidated financial statements of

Uniserve Communications Corporation

Three months ended August 31, 2009

(Unaudited)

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

The accompanying unaudited interim Consolidated Financial Statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

"Michael Schmidt"

Michael Schmidt, President and CEO

October 26, 2009

Uniserve Communications Corporation

Consolidated statements of operations, comprehensive loss and deficit

	Three months ended August 31,	
	2009	2008
	(Unaudited)	(Unaudited)
	\$	\$
		As restated *
Revenues	3,986,059	5,138,741
Cost of sales	2,033,800	2,717,195
Gross margin	1,952,260	2,421,546
Expenses		
Operations and service delivery costs	1,511,508	2,276,868
Amortization of property and equipment (Note 4)	121,968	160,181
Amortization of intangible assets (Note 5)	110,000	138,681
Amortization of deferred finance costs (Note 5)	1,734	-
Sales and marketing	47,450	108,013
Stock-based compensation (Note 9(d))	2,621	2,937
	1,795,282	2,686,680
Operating income (loss)	156,978	(265,134)
Other (expense) income		
Interest and bank charges	(295,282)	(380,202)
Foreign exchange gain (loss)	4,453	(696,376)
Accretion to face value of preferred shares (Note 8)	(79,798)	(79,798)
	(370,627)	(1,156,376)
Loss before income taxes from continuing operations	(213,649)	(1,421,510)
Income tax recovery (expense)		
Future	(24,409)	67,200
	(24,409)	67,200
Net loss and comprehensive loss for the period		
from continuing operations	(238,058)	(1,354,310)
Results from discontinued operations (Note 3)	-	(605,727)
Net loss and comprehensive loss for the period	(238,058)	(1,960,037)
Deficit, beginning of period	(19,506,785)	(19,415,040)
Deficit, end of period	(19,744,843)	(21,375,077)
Basic earnings per share		
Basic loss per share from continuing operations	(0.01)	(0.06)
Basic loss per share	(0.01)	(0.08)
Weighted average number of common shares outstanding - basic and diluted	24,630,865	24,546,082

* See Note 2(b)(i)

Uniserve Communications Corporation

Consolidated balance sheets

	August 31, 2009 (Unaudited)	May 31, 2009 (Audited)
	\$	\$
Assets		
Current assets		
Cash	19,654	196,651
Accounts receivable	699,385	764,118
Inventory	207,701	204,337
Prepaid expenses	37,113	33,902
Amounts held in escrow (Notes 3, 12)	2,737,500	2,729,250
Future income tax asset	-	16,474
	3,701,353	3,944,732
Future income tax asset	237,077	237,877
Property and equipment (Note 4)	1,521,959	1,594,854
Intangible and other assets (Note 5)	1,723,679	1,621,792
Goodwill (Note 6)	4,312,884	4,312,884
	11,496,952	11,712,139
Liabilities and shareholders' deficit		
Current liabilities		
Bank indebtedness (Note 7)	105,062	122,345
Accounts payable and accrued liabilities	6,914,615	6,978,954
Accrued dividends payable (Note 8)	571,333	485,633
Deferred revenue	906,499	996,628
Obligations under capital leases	31,290	37,611
Future income tax liability	-	6,634
	8,528,799	8,627,805
Obligations under capital leases	44,131	18,442
Future income tax liability	13,769	-
Convertible preferred shares (Notes 8, 9(e))	3,325,239	3,245,441
	11,911,938	11,891,688
Shareholders' deficit		
Share capital (Note 9(a))	14,315,028	14,315,028
Other equity instruments (Note 9(e))	3,613,559	3,642,059
Contributed surplus (Note 9(a))	1,401,270	1,370,149
Deficit	(19,744,843)	(19,506,785)
	(414,987)	(179,549)
	11,496,952	11,712,139

Contingent liability and subsequent event (Note 12)

Approved by the Directors

"Michael Schmidt"
Director

"Maurice Lees"
Director

Uniserve Communications Corporation

Consolidated statements of cash flows

	Three months ended August 31,	
	2009	2008
	(Unaudited)	(Unaudited)
	\$	\$
		As restated *
Operating activities		
Net loss for the period	(238,058)	(1,960,037)
Results of discontinued operations	-	(605,727)
Net loss for the period from continuing operations	(238,058)	(1,354,310)
Items not involving cash		
Amortization of property and equipment	121,968	160,181
Amortization of intangible assets	110,000	138,681
Amortization of deferred finance costs	1,734	-
Accretion of face value of preferred shares	79,798	79,798
Stock-based compensation	2,621	2,937
Unrealized gain on foreign exchange	(8,374)	(69,319)
Future income taxes	24,409	(67,200)
Changes in non-cash operating working capital (Note 11)	8,882	1,159,754
Net cash provided by continuing operating activities	102,980	50,522
Net cash provided by discontinued operating activities	-	774,717
Net cash provided by operating activities	102,980	825,239
Investing activities		
New product development	(213,621)	(252,367)
Purchase of property and equipment	(49,073)	(46,381)
Net cash used in continuing investing activities	(262,694)	(298,748)
Net cash used in discontinued investing activities	-	(154,092)
Net cash used in investing activities	(262,694)	(452,840)
Financing activities		
Revolving line of credit	-	(70,000)
Repayment of short-term debt	(17,283)	(18,851)
Repayments to related parties	-	(5,075)
Net cash used in continuing financing activities	(17,283)	(93,926)
Net cash provided by discontinued financing activities	-	85,729
Net cash used in financing activities	(17,283)	(8,197)
Increase (decrease) in cash and cash equivalents	(176,997)	364,202
Cash, beginning of year	196,651	201,118
Cash, end of year	19,654	565,320
Cash related to:		
Continuing operations	19,654	216,619
Discontinued operations	-	348,701
	19,654	565,320

Supplemental cash flow information (Note 11)

* See Note 2(b)(i)

Uniserve Communications Corporation

Notes to consolidated financial statements

August 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 August 31, 2009, the Company has a working capital deficiency of \$4,827,446 (May 31, 2009 - deficiency of \$4,683,073). For the period ended August 31, 2009 the Company had positive cash flow from operations but incurred net losses due to interest expense, foreign exchange, amortization of customer lists and other intangible assets and accretion to face value of preferred shares.

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.

2. Basis of Presentation and Accounting Policies:

(a) Basis of presentation:

The unaudited interim Consolidated Financial Statements include the accounts of Uniserve Communications Corp., and its subsidiaries (collectively the "Company"). The notes presented in these unaudited interim Consolidated Financial Statements include only significant events and transactions occurring since the Company's last fiscal year end and are not fully inclusive of all matters required to be disclosed in the Company's annual audited consolidated financial statements. As a result, these unaudited interim Consolidated Financial Statements should be read in conjunction with the Company's consolidated financial statements for the year ended May 31, 2009.

(b) Accounting Policies:

The unaudited interim Consolidated Financial Statements follow the same accounting policies and method of application as the most recent annual consolidated financial statements.

(i) *Adoption of new accounting policies*

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.

Uniserve Communications Corporation

Notes to consolidated financial statements

August 31, 2009 and 2008

3. 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\$2,737,500 as at August 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 12.

Subsequent to the balance sheet date, US\$1,000,000 was released from escrow. In addition, the escrow period for the remaining balance US\$1,500,000 was extended to March 31, 2010, see note 12.

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. Amounts due to related parties totaling \$1,893,458 and the revolving line of credit balance of \$1,500,000 were also repaid.

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>

Uniserve Communications Corporation

Notes to consolidated financial statements

August 31, 2009 and 2008

3. Discontinued operations (continued)

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

	Aug 31, 2009	Aug 31, 2008
	\$	\$
Revenues	-	2,575,071
Gross margin	-	1,921,638
Expenses	-	2,059,522
Operating loss	-	(137,884)
Other expense	-	(377,843)
Loss before income taxes	-	(515,727)
Income tax expense	-	(90,000)
Net loss and comprehensive loss for the period	-	(605,727)

4. Property and equipment

	August 31, 2009			
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$	\$	\$
Equipment	8,836,706	7,599,962	-	1,236,744
Software	766,422	502,282	-	264,140
Leasehold improvements	342,478	321,403	-	21,075
	9,945,606	8,423,647	-	1,521,959

	May 31, 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

The cost of property under capital leases, equipment and software aggregated \$75,421 as at August 31, 2009 (May 31, 2009 - \$56,053). Amortization charged to continuing operations, which includes amortization associated with property under capital leases, was \$121,968 and \$160,181 for the periods ended August 31, 2009 and 2008, respectively.

Uniserve Communications Corporation

Notes to consolidated financial statements

August 31, 2009 and 2008

5. Intangible and other assets

	Aug 31, 2009			
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$		\$
Customer lists	15,971,161	15,347,828	-	623,333
Deferred finance costs	424,139	405,072	-	19,067
Product development costs	1,081,279	-	-	1,081,279
	17,476,579	15,752,900	-	1,723,679

	May 31, 2009			
	Cost	Accumulated amortization	Write-down	Net book value
	\$	\$		\$
Customer lists	15,971,161	15,135,879	101,949	733,333
Deferred finance costs	424,139	403,338	-	20,801
Product development costs	867,658	-	-	867,658
	17,262,958	15,539,217	101,949	1,621,792

During the period ended August 31, 2009 product development costs of \$213,621 related to Kinzin, a social networking site being developed by the Company, were capitalized. The total capitalized product development costs relating to Kinzin as of August 31, 2009 were \$1,081,279 (May 31, 2009 - \$867,658).

6. Goodwill

	Discontinued Operations	Continuing Operations
	\$	\$
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 and August 31, 2009	-	4,312,884

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Notes to consolidated financial statements

August 31, 2009 and 2008

7. Bank indebtedness

	Aug 31, 2009	May 31, 2009
	\$	\$
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	105,062	122,345
	105,062	122,345

8. Convertible preferred shares

	Aug 31, 2009	May 31, 2009
	\$	\$
Series A Convertible Preferred Shares, \$4,285,000 (May 31, 2009 - \$4,285,000) redeemable at the option of the holder on or after May 24, 2014, 8% cumulative dividends, net of unamortized discount of \$959,761 (May 31, 2009 - \$1,039,559 (Note 9(a)(ii)))	3,325,239	3,245,441
	3,325,239	3,245,441

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 9(a)(ii) and 9(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 August 31, 2009 the dividends on the Series A Convertible Preferred Shares are in arrears in the amount of \$571,333 (May 31, 2009 - \$485,633).

Uniserve Communications Corporation

Notes to consolidated financial statements

August 31, 2009 and 2008

9. 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 August 31, 2009, 428,500 (May 31, 2009 - 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, 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
Stock-based compensation expense	-	-	2,621
Expiry of warrants	-	-	28,500
Balance, August 31, 2009	24,630,865	14,315,028	1,401,270

(i) On July 9, 2008, the Company issued an additional 200,000 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 \$70,000. Warrants are exercisable until July 9, 2010 at an exercise price of \$0.45. On issue the amount allocated to share capital was \$67,123 and \$2,877 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%.

(ii) As the Company may be required to redeem the preferred shares for cash, they have been classified as long-term liabilities, see Note 8, with the par value of the conversion right included in other equity instruments, see Note 9(e). On issue the amount allocated to long-term liabilities was \$2,701,441 and \$1,583,559 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.

(b) *Escrow*

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

Uniserve Communications Corporation

Notes to consolidated financial statements

August 31, 2009 and 2008

9. Share capital (continued)

(c) Share purchase warrants

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

Issue date	Expiry date	Number of warrants	Exercise price \$
May 24, 2007	May 24, 2012	3,500,000	0.70
April 24, 2008	April 24, 2010	753,251	0.45
July 9, 2008	July 9, 2010	100,000	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, 2009 and the period ending August 31, 2009, no stock options were granted. For the period ended August 31, 2009, the Company recognized stock-based compensation related to stock options of \$2,621 (August 31, 2008 - \$2,937).

Stock option activity is summarized as follows:

	Options outstanding		
	Shares available for grant	Number of optioned common shares	Weighted average exercise price \$
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			
August 31, 2009	<u>1,425,587</u>	<u>1,037,500</u>	<u>0.50</u>

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Notes to consolidated financial statements

August 31, 2009 and 2008

9. Share capital (continued)

(d) *Share purchase options (continued)*

The following table summarizes information about stock options outstanding and exercisable as at August 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	2.19	975,833	2.19

(e) *Other equity instruments*

	Aug 31, 2009	May 31, 2009
	\$	\$
Conversion rights on Series A preferred shares (Note 9(a)(ii))	1,583,559	1,583,559
Warrants (i)	2,030,000	2,030,000
Warrants (ii)	-	28,500
	3,613,559	3,642,059

- (i) During the year ended May 31, 2007 as part of the US\$10,000,000 subordinated debt financing arrangements, 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 ended May 31, 2009 the subordinated debt was repaid in conjunction with the sale of Parasun, see note 3.
- (ii) 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. During the period these warrants expired and the previously record warrant value was charged to contributed surplus.

10. Related party transactions

- (a) On October 7, 2008, the \$1,000,000, the \$650,000 and the \$400,000 loans payable to a director and shareholder of the Company, 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 3.
- (b) 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.

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

Uniserve Communications Corporation

Notes to consolidated financial statements

August 31, 2009 and 2008

11. Statements of cash flows

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

	Aug 31, 2009	Aug 31, 2008
	\$	\$
Accounts receivable	64,778	49,222
Inventory	(3,364)	2,898
Prepaid expenses	(3,211)	17,367
Accounts payable and accrued liabilities	(44,971)	1,234,005
Accrued dividends payable	85,700	85,700
Deferred revenue	(90,129)	(88,512)
Income taxes payable	-	(145,777)
Effect of foreign exchange rate changes on cash	79	4,851
	8,882	1,159,754

(ii) Supplemental information:

	Aug 31, 2009	Aug 31, 2008
	\$	\$
Interest paid	2,692	22,929
Non-cash financing and investing transactions		
Obligations under capital leases	75,421	-
Expiration of warrants	28,500	-

12. Contingent liability and subsequent event

As a result of the sale of Parasun there is a total of US\$2,500,000 (CDN\$2,737,500 as at August 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 3. As at August 31, 2009 the Company has estimated the contingent liability to be US\$350,000 (CDN\$390,760 as at August 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.

Subsequent to the balance sheet date, US\$1,000,000 was released from escrow. During the quarter the escrow period for the remaining balance US\$1,500,000 was extended to March 31, 2010.